

# REVIEW OF SOUTH AUSTRALIAN RAIL ACCESS REGIME INFORMATION KIT DISCUSSION PAPER

**December 2009**



## **REQUEST FOR SUBMISSIONS**

The Essential Services Commission of SA (the Commission) invites written submissions from interested parties in relation to the issues raised in this paper. Written comments should be provided by 29 January 2010. It is highly desirable for an electronic copy of the submission to accompany any written submission.

It is Commission policy to make all submissions publicly available via its website ([www.escosa.sa.gov.au](http://www.escosa.sa.gov.au)), except where a submission either wholly or partly contains confidential or commercially sensitive information provided on a confidential basis and appropriate prior notice has been given.

The Commission may also exercise its discretion not to exhibit any submission based on their length or content (for example containing material that is defamatory, offensive or in breach of any law).

Responses to this paper should be directed to:

### **Review of South Australian Rail Access Regime Information Kit: Discussion Paper**

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### ***Public Information about ESCOSA's activities***

Information about the role and activities of the Commission, including copies of latest reports and submissions, can be found on the ESCOSA website at [www.escosa.sa.gov.au](http://www.escosa.sa.gov.au).

## TABLE OF CONTENTS

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Request for Submissions	2
Public Information about ESCOSA's activities	2
Glossary of Terms	iii
<b>1 Summary</b>	<b>1</b>
<b>2 Background</b>	<b>3</b>
2.1 Part 4 of the ROA Act	3
2.1.1 Pricing Principles (Part 4, Division 1)	3
2.1.2 Information about Access (Part 4, Division 2)	4
2.2 2005 Review	5
2.2.1 Whether to establish pricing principles	5
2.2.2 Role of Information Brochure	6
2.2.3 Reference tariffs	6
2.3 The Approach	7
<b>3 Section 27 Guidelines</b>	<b>9</b>
3.1 Legislative requirements	9
3.2 Key Issues	9
3.2.1 Floor price	9
3.2.2 Ceiling price	10
3.3 Proposed Amendments	13
<b>4 Section 28 Guidelines</b>	<b>14</b>
4.1 Legislative framework	14
4.2 Key Issues	14
4.2.1 Unbundling of Access Prices	15
4.2.2 Section 28(3) requirements	15
4.2.3 Likely (or Indicative) Access Prices	16
4.2.4 Other (non-price) terms and conditions	16
4.3 Proposed Amendments	17
<b>5 Section 29 Guidelines</b>	<b>18</b>
5.1 Legislative framework	18



5.2	Key Issues	18
5.2.1	Likely (or Indicative) Access Prices	19
5.2.2	Scope of (non-price) terms and conditions	20
5.3	Proposed Amendments	22
6	Consultation Process	23

## GLOSSARY OF TERMS

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2005 Review	The review of the then Information Kit conducted by the Commission during 2005
2009 Inquiry	The current inquiry into the Access Regime being conducted by the Commission
Access Provider	A party providing, or able to provide, railway infrastructure (or 'below rail') services – referred to as "an operator" under the ROA Act
Access Regime	The Access Regime in Parts 3 to 8 of the ROA Act
Access Seeker	An above-rail operator seeking access to railway infrastructure
ARTC	The Australian Rail Track Corporation Ltd
AustralAsia Railway	The railway running from Tarcoola in South Australia to Darwin in the Northern Territory, the access regime for which is also regulated by the Commission
The Commission	The Essential Services Commission of South Australia
ESC Act	<i>Essential Services Commission Act 2002</i>
GWA	Genesee and Wyoming Australia Pty Ltd
Information Brochure	A document containing information relevant to access that an access provider is obliged to prepare and provide in accordance with section 28 of the ROA Act
Information Kit	The Commission's primary publication concerning the Access Regime
ROA Act	<i>Railways (Operations and Access) Act 1997</i>

# 1 SUMMARY

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The Essential Services Commission of South Australia (the Commission) has finalised its Inquiry<sup>1</sup> into the Access Regime that applies to the major intrastate railways in South Australia.

During the course of the Inquiry, the Commission has identified several aspects of the South Australian Rail Access Regime: Information Kit (Information Kit)<sup>2</sup> that could be better clarified and/or improved. The Commission therefore proposed in its Draft Inquiry Report<sup>3</sup> to carry out a separate but concurrent review of its Information Kit, and invited stakeholders to provide comment as part of the Draft Inquiry Report's public consultation process.

While submissions to the Draft Inquiry Report were supportive for a separate review of the Information Kit to be carried out, the Commission did not receive any specific comments from stakeholders on the type of changes that should be made to the Information Kit. Nevertheless, the Commission commenced the Information Kit review process based on aspects already identified for further improvement and/or clarification in its Draft Inquiry Report.

On the basis, the Commission stresses that the draft revision decisions made in relation to the Information Kit in this Discussion Paper will reflect the context of the existing Access Regime only. This review does not anticipate the South Australian Government's response to the recommendations put forward by the Commission in its Final Inquiry Report. This review therefore takes the ROA Act and the legislative scheme therein, as it is, and not as it might be.

This Discussion Paper explores the role that the Information Kit plays in the Access Regime and includes some preliminary Commission positions that may assist further discussion, and to expedite the development of the Information Kit. It discusses how the existing Information Kit might be structured so that:

- ▲ it is more comparable with the Commission's AustralAsia railway guidelines<sup>4</sup> and the Australian Rail Track Corporation (ARTC) Access Undertakings<sup>5</sup>; and

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<sup>1</sup> The Inquiry was to focus on the extent to which the existing Access Regime, which is set out in the *Railways (Operations and Access) Act 1997* (ROA Act), is consistent with certain principles under the Council of Australian Government's Competition and Infrastructure Reform Agreement (CIRA). It also considered whether or not the Access Regime would otherwise be generally improved.

<sup>2</sup> A copy of the Commission's South Australian Rail Access Regime: Information Kit is available at: <http://www.escosa.sa.gov.au/sa-rail-overview/codes-guidelines-rules.aspx>.

<sup>3</sup> A copy of the Commission's Draft Inquiry Report is available at: <http://www.escosa.sa.gov.au/projects/42/2009-south-australian-rail-access-regime-inquiry.aspx#stage-list=2>.

<sup>4</sup> Guidelines in relation to the Tarcoola-Darwin railway are available at: <http://www.escosa.sa.gov.au/sa-rail-overview/codes-guidelines-rules.aspx>.

<sup>5</sup> Information in relation to ARTC's Access Undertakings is available at: <http://www.accc.gov.au/content/index.phtml/itemId/789738>.



- ▲ information provided as part of the Information Brochure and throughout the commercial negotiation is sufficiently detailed enough to give initial guidance to an access seeker to formulate the starting point for an eventual access proposal anywhere on the covered network.

## 2 BACKGROUND

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Third-party access to major intrastate railway lines in South Australia is subject to the Access Regime set out in the ROA Act. The terms and conditions of rail access are detailed in an Information Brochure prepared and issued by an access provider in accordance to requirements of the Information Kit. This is the Commission's principal regulatory publication in relation to the Access Regime, and contains what the Commission might otherwise publish separately as guidelines.

Besides some general descriptive material, the current Information Kit comprises:

- ▲ chapter 3 – which sets out the pricing principles developed by the Commission;
- ▲ chapter 4 – which sets out the information required in an access provider's Information Brochure;
- ▲ chapter 5 – which sets out the reporting requirements on access providers; and
- ▲ chapter 6 – which discusses compliance systems and reporting.

As chapters 3 and 4 of the Information Kit reflect the requirements of Part 4 of the ROA Act, any revisions or extensions must therefore take into account these legislative requirements, which are discussed in further detail below.

### 2.1 *Part 4 of the ROA Act*

#### 2.1.1 Pricing Principles (Part 4, Division 1)

Section 27 of the ROA Act provides as follows:

*Pricing principles*

*(1) The regulator may establish principles (the pricing principles) for fixing a floor and ceiling price for the provision of railway services generally or railway services of a particular class.*

*(2) The floor price should reflect the lowest price at which the operator [access provider] could provide the relevant services without incurring a loss and the ceiling price should reflect the highest price that could fairly be asked by an operator for provision of the relevant services.*

*(3) The pricing principles do not prevent an operator from entering into an access contract on terms that do not reflect the principles.*

*(4) However, if in an arbitration the arbitrated price for services cannot be less than the floor price and cannot exceed the ceiling price.*

A decision by the Commission to establish pricing principles means that they become, in practice, an additional matter for an arbitrator to take into account.<sup>6</sup>

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<sup>6</sup> Section 38 of the ROA Act sets out the principles that an arbitrator must take into account in an arbitration. These principles include the pricing principles (section 38(1)(g)).



However, the pricing principles are not intended to bind behaviour to the extent that they might in other access regimes. Section 27(3) of the ROA Act permits the parties to an access contract to agree to terms outside the bounds set by any applicable floor and ceiling prices. This is consistent with the negotiate-arbitrate framework underpinning the Access Regime.

## 2.1.2 Information about Access (Part 4, Division 2)

Division 2 of Part 4 (sections 28-30) of the ROA Act establishes minimum rights and obligations to facilitate the exchange of preliminary information about access. The division deals with information requests and exchanges that typically arise prior to a specific access application being lodged, and includes a requirement for an Information Brochure.

Section 28 of the ROA Act provides as follows:

### *Information brochure*

*(1) An operator [access provider] must, on the written application of an industry participant, provide an information brochure containing –*

- (a) if the operator carries on the business of providing passenger or freight services – a statement of the terms and conditions on which the operator provides the services; and*
- (b) the terms and conditions on which the operator is prepared to make the operator's railway infrastructure available for use by others; and*
- (c) other information required by the regulator.*

*(2) The information brochure must be provided within 30 days (or a longer period allowed by the regulator) after the operator receives the application.*

*(3) The information brochure must refer to any relevant pricing principles and show how the terms and conditions relate to, or compare with, relevant pricing principles.*

*(4) The form of the information brochure must comply with requirements imposed by the regulator.*

*(5) The operator must, within 14 days after providing an industry participant with the information brochure, give a copy to the regulator.*

*(6) If the operator fails to comply with this section in any respect, the operator is guilty of an offence.*

*Maximum penalty: \$20 000.*

Section 29 of the ROA Act provides as follows:

### *Operator's obligation to provide information about access*

*(1) An operator [access provider] must, on the application of a person with a proper interest in making an access proposal to the operator, provide the applicant with information reasonably requested by the applicant about –*

- (a) the extent to which the operator's railway infrastructure is currently being utilised; and*

*(b) the extent to which it would be necessary, and technically and economically feasible, to add to or extend the operator's railway infrastructure so that it could meet requirements stated in the application; and*

*(c) whether the operator would be prepared to provide a service of a specified description and –*

*(i) if so, the general terms and conditions (including an indication of the likely price) on which the operator would be prepared to provide the service; and*

*(ii) if not, the reasons why the service cannot be provided.*

*(2) The operator may make a reasonable charge (to be determined on a basis decided or approved by the regulator) for providing information under this section.*

*(3) If the operator makes a charge for providing information under this section, the operator must give the regulator written notice of the amount of the charge and the nature of the information provided.*

Section 30 of the ROA Act provides as follows:

*Information to be provided on non-discriminatory basis*

*An operator [access provider] must provide information to persons interested in making access proposals to the operator on a non-discriminatory basis.*

## **2.2 2005 Review**

The Commission previously reviewed the Information Kit during 2005. Its final decision was published in October 2005 (2005 Review)<sup>7</sup> along with a revised Information Kit.

The revisions arising out of the 2005 Review reflected developments at the time in the administration and design of rail access regimes and conditions at the time in the Australian rail sector.

The 2005 Review is important as it contains previous relevant decisions made by Commission. It included:

### **2.2.1 Whether to establish pricing principles**

During the 2005 Review, the Commission considered the option of not establishing pricing principles under section 27 of the ROA Act. The basis for this was the notion that pricing principles would provide little practical effect in an arbitration, noting the low likelihood of a reasonable arbitrator ever setting a price lower or higher than a reasonably set floor or ceiling.

Nevertheless, the Commission ultimately concluded that the establishing of pricing principles for the purpose of the Access Regime could assist with pricing transparency early in the access process. The Commission also noted the importance placed on pricing principles in the Productivity Commission's review of

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<sup>7</sup> A copy of the Commission's 2005 Review is available at: <http://archive.escosa.sa.gov.au/site/page.cfm?u=179&c=1454>.

the National Access Regime, and resulting decisions by the Australian Government to include provision for pricing principles in that regime.

The 2005 Review therefore saw the Commission decide to establish pricing principles under section 27(1) of the ROA Act for the purpose of the Access Regime.

## 2.2.2 Role of Information Brochure

In the 2005 Review, the Commission acknowledged that its Guidelines in relation to the Information Brochure must take account of the role of the Information Brochure in this Access Regime and the content obligations that the ROA Act already provides.

*"An Information Brochure in this Access Regime appears at the very first stage of an access seeker's enquiries. This means that it is only reasonable to expect the Information Brochure to provide high level, generic or indicative information, as it could not be possible for the access provider to anticipate the specifics of most access requests. Nevertheless, the timing of the Information Brochure means that it should provide sufficient detail for an access seeker to formulate the starting point for an eventual access proposal anywhere on the covered network."*

The Commission also noted that the requirement to provide terms and conditions in section 28 of the ROA Act can be read broadly as covering all aspects of access (that is, a full railway service quality description including pricing information). However, as it might also be read more narrowly, the Commission decided in the 2005 Review to continue the previous Information Kit practice of providing for additional comprehensive information – thereby achieving the effect of a broader interpretation.

## 2.2.3 Reference tariffs

The Information Kit in place prior to the 2005 Review (mainly reflecting decisions of the Commission's predecessor) included a requirement for reference tariffs. The 2005 Review concluded that such a requirement was "problematic". While recognising the potential value of reference tariffs in an access regime, the Commission acknowledged that the ROA Act made no clear provision for the Commission to require reference tariffs as they are usually understood in other regimes – that is, a tariff at which a defined reference service is available and having a binding effect such that an access provider cannot otherwise refuse to offer the defined service at the published price.

In the 2005 Review, the Commission therefore decided to remove from the Information Kit:

*"...the current, ineffective, regulator imposed requirement for reference tariffs and instead focus on compliance with those 'equivalent' obligations already in the ROA Act."*

Noting that sections 28(1)(b) and 28(3) of the ROA Act require a complying Information Brochure to contain some pricing information that has some of the character of reference tariffs, the Commission decided to add the following requirements to those already in the Information Kit in place of the reference tariffs requirement. The Commission therefore retained the existing ancillary pricing information requirements, with the addition of the following:

- “ • An operator [access provider] must provide indicative floor and ceiling prices for all significant railway services – being services it provides that are, or are highly likely to be, subject to access interest (e.g. major network tasks) – that it can offer and which are subject to the Access Regime.*
- The Commission may identify railway services to be significant railway services.*
- The indicative floor and ceiling prices provided must be accompanied by statements explaining how the floor and ceiling prices relate to the pricing principles, including disclosing any rate of return used.*
- Any prices or price information provided by an operator are to be expressed in terms ordinarily and reasonably used in the rail industry for the railway service in question.”*

## 2.3 The Approach

The Commission's review of the Information Kit is being undertaken against the background of relevant experience with application of the associated guidelines, any relevant experience regarding operations on the railway, and developments in regulatory practice.

In addition to ensuring consistency with the objects of the ROA Act, the review is to be carried out guided by the following criteria:

- ▲ **clarity and general acceptance** – the Information Kit is to be clearly stipulated and capable of being understood by both access providers and access seekers;
- ▲ **supportive of commercial negotiations** – the Information Kit must facilitate – not deter – meaningful commercial access negotiation, and reflect general accepted business practice;
- ▲ **competitive neutrality** – the Information kit should contribute towards promoting competitive neutrality;
- ▲ **consistency with interfacing networks** – the Information Kit is aimed to achieve consistency with ARTC's Access Undertaking and the AustralAsia railway access regime to the maximum extent possible and appropriate.

On the latter point, while the Commission recognises that there may be benefits to greater consistency between access regimes applying to interfacing railway networks, it believes that it needs to be balanced against the specific context in which regulation is being applied and, more importantly, should only be pursued if there will be a net gain.



For the purpose of this review, stakeholders are invited to comment on the extent to which there are net benefits from the Commission's proposed changes to the Information Kit that seek to achieve greater consistency between the Access Regime and the regimes applying to interfacing railway networks.

### 3 SECTION 27 GUIDELINES

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The Commission considered the detailed construction of the floor and ceiling prices in the 2005 Review. This chapter considers possible revisions or extensions to the Commission's floor and ceiling pricing principles (or guidelines) set out under the Information Kit.

#### 3.1 *Legislative requirements*

Section 27 of the ROA Act in part provides as follows:

##### *Pricing principles*

*(1) The regulator may establish principles (the **pricing principles**) for fixing a floor and ceiling price for the provision of railway services generally or railway services of a particular class.*

*(2) The floor price should reflect the lowest price at which the operator [access provider] could provide the relevant services without incurring a loss and the ceiling price should reflect the highest price that could fairly be asked by an operator for provision of the relevant services.*

While the decision by the Commission to establish pricing principles means that they become, in practice, an additional matter for an arbitrator to take into account (under (section 38(1)(g) of the ROA Act), establishing pricing principles also has the effect of providing some additional guiding information in the early stages of an access negotiation. Accordingly, the Information Brochure provided by the access provider must therefore refer to any relevant pricing principles established by the Commission and demonstrate how the terms and conditions it contains relate to, or compare with, the pricing principles.

#### 3.2 *Key Issues*

##### 3.2.1 Floor price

The Commission's floor price guidelines are provided in part 3.1 of chapter 3 of the Information Kit.

These floor price guidelines in some minor detailed respects fall short of the pricing principles/guidelines applicable to the AustralAsia railway and evident in ARTC's latest Access Undertaking.

Both regulatory arrangements require that the access price payable must not be less than the avoidable below-rail cost of providing the railway infrastructure service, on the premise that the access provider should not be required to provide a service where it is unable to recover the cost of providing that service.

Under clause 4.4(b) of the ARTC Undertaking:

*...incremental costs means the costs that could have been avoided if a Segment was removed from the Network including Segment Specific Costs and Non-Segment Specific Costs relating to the following activities:*

- (i) track and signalling and communication maintenance;*
  - (ii) maintenance contract support, administration and management and project management;*
  - (iii) train control and communication;*
  - (iv) train planning and operations administration; and*
  - (v) system management and administration;*
- but excluding Depreciation and return on assets relating to Segment Specific Assets and Non-segment Specific Assets, such return being determined by applying a real Rate of Return to the value of these assets.*

The AustralAsia railway guidelines:

- ▲ restrict the labour and materials costs that could be avoided to maintenance costs expensed (including any variable (e.g. usage related) major planned maintenance);
- ▲ restrict the administrative costs that could be avoided to those train control and operations administration costs and business management-related costs that vary with the usage of the access seeker;
- ▲ restrict that the capital costs that could be avoided to the cost of replacing the required railway infrastructure assets brought forward by the operation of the service, and the costs incurred by providing specific infrastructure enhancements for the traffic in question;
- ▲ provide some general guidance on the meaning of a return on investment being commensurate with “the regulatory and commercial risks involved”; and
- ▲ require all additional costs associated with meeting increased track standards required by a particular traffic (e.g., passenger traffic) to be attributable to that traffic and thereby form part of the floor price for that traffic.

### 3.2.2 Ceiling price

The Commission’s ceiling price guidelines are provided in part 3.2 of chapter 3 of the Information Kit.

These ceiling price guidelines in some detailed respects fall short of the pricing principles/guidelines applicable to the AustralAsia railway and evident in ARTC’s latest Access Undertaking.

Notably, under clause 4.4 of the ARTC Undertaking:

- (c) Where applicable, the Ceiling Limit means revenue sufficient to cover the Economic Cost of that Segment or group of Segments.*
- (d) In calculating the Economic Cost for the purposes of the Ceiling Limit, the Network and Associated Facilities will be:*
  - (i) valued initially using the depreciated optimised replacement cost method of valuing assets (“Initial Regulatory Asset Base (Initial RAB)”);*

(ii) revalued annually by roll forward according to the following methodology:

$$RAB_{t \text{ start}} = RAB_{t-1 \text{ end}} =$$

$$(1 + CPI_{t-1}) * RAB_{t-1 \text{ start}} + Net \text{ Capex}_{t-1} - Depreciation_{t-1}$$

where

$RAB_{t-1 \text{ start}}$  is the RAB at the start of the relevant year (t) (which, for the first year following the Commencement Date, would be the Initial RAB).

$RAB_{t-1 \text{ end}}$  is the RAB at the end of the preceding year (t-1) as applicable.

$RAB_{t-1 \text{ start}}$  is the RAB at the start of the preceding year (t-1) as applicable.

$CPI_{t-1}$  is the inflation rate for the preceding year (t-1), determined by reference to the All Groups Consumer Price Index Statistics published for the March quarter of that year.

$Net \text{ Capex}_{t-1}$  is the net additions to the RAB in year t-1 (that is out-turn Capital Expenditure by ARTC less any disposals during period t-1) on a Prudent basis.

$Depreciation_{t-1}$  is the Depreciation applicable to the RAB in year t-1.

For the purpose of this clause, the optimised replacement cost means the cost of replacement by commercially efficient application of best known currently available technology based on existing capacity and performance characteristics of the asset.

(e) For the purpose of this Part 4, any increase to Capital Expenditure would be limited to that which may result from:

(i) the addition of a capital or renewals project by ARTC needed to meet market demand for capacity and performance of the Network, or needed to extend the economic life of the Network;

(ii) an increase in the scope of works identified in the applicable ARTC Corridor Strategy current as at the Commencement Date or as varied from time to time;

(iii) the addition of a capital or renewals project by ARTC resulting from what is considered to represent an efficient means to achieve that demand or extend that economic life;

(iv) a change in what is consistent with existing standard and configuration of adjacent and/or existing infrastructure with similar utilisation and market requirements, or its modern engineering equivalent;

(v) whether expenditure is incurred efficiently in implementing the capital or renewals project, in the context of prevailing access and operating requirements, and input costs;

(vi) adjustments in relation to the timing of commencement and/or commissioning of projects;  
or

(vii) the removal or addition of a capital or renewals project by ARTC that is supported by the industry.

For the purpose of this clause, ARTC will obtain the approval of the ACCC, having regard to the factors in this clause, for any increase to Capital Expenditure exceeding 20% of Capital Expenditure on the Network in any single year.



*(f) For the purposes of this Part 4, Economic Cost of a Segment means:*

- (i) Segment Specific Costs;*
- (ii) Depreciation of Segment Specific Assets;*
- (iii) a return on Segment Specific Assets, being determined by applying a real Rate of Return to the value of Segment Specific Assets;*
- (iv) an allocation of Non-Segment Specific Costs;*
- (v) an allocation of Depreciation of Non-Segment Specific Assets;*
- (vi) an allocation of return of Non-Segment Specific Assets, being determined by applying a real Rate of Return to the value of Non-Segment Specific Assets; and*
- (vii) the costs described in clause 4.4(f)(i) to (vi) as applicable to Additional Capacity.*

*(g) For the purposes of clause 4.4(f), Non-Segment Specific Costs and Depreciation of, and return on, Non-Segment Specific Assets will be allocated to Segments in accordance with the following principles:*

- (i) where possible, costs will be directly attributed to a Segment;*
- (ii) where possible, Non-Segment Specific Costs and Non-Segment Specific Assets will be identified with a corridor, corridors or identified as system-wide;*
- (iii) Non-Segment Specific Costs and Depreciation of, and return on, Non-Segment Specific Assets identified with a corridor or corridors, or identified as system-wide, will be allocated to those parts of Segments in that corridor or corridors, or, where identified as system wide, to Segments owned, leased or licensed by ARTC respectively, in proportion to:*

*(A) gtkm with respect to Non-Segment Specific Costs and Depreciation of, and return on, Non-Segment Specific Assets associated with track maintenance; and*

*(B) Train kilometres with respect to Non-Segment Specific Costs and Depreciation of, and return on, Non-Segment Specific Assets not associated with track maintenance.*

*All costs will comprise ARTC's reasonably anticipated costs over a reasonable future timeframe.*

*(h) The Rate of Return for the purposes of this Part will be equivalent to ARTC's weighted average cost of capital ("WACC") as accepted by the ACCC after consideration of all risks with the commercial environment in which ARTC operates on the Network, the elements of which will comprise:*

- (i) a capital asset pricing model ("CAPM") method of determining the cost of equity;*
- (ii) a debt to equity ratio which would be considered prudent for ARTC's business in relation to the Network by reputable lenders; and*
- (iii) an appropriate adjustment (beta) factor to the equity risk margin appropriate for investment in railway infrastructure forming part of the Network.*

### **3.3 *Proposed Amendments***

In order to provide firmer guidance in the early stages of an access negotiation, the Commission proposes that:

- ▲ the Information Kit's floor and ceiling pricing principles be extended to incorporate relevant and appropriate features of the AustralAsia railway guidelines and the ARTC Undertaking; and
- ▲ a financial model similar to that included in the ATRC Undertaking be incorporated into the ceiling pricing principles.

## 4 SECTION 28 GUIDELINES

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This chapter considers possible revisions or extensions to the Commission's requirements in relation to an access provider's Information Brochure.

### 4.1 *Legislative framework*

Section 28 of the ROA Act in part provides as follows:

#### *Information brochure*

28. (1) An operator [access provider] must, on the written application of an industry participant, provide an information brochure containing –

- (a) if the operator carries on the business of providing passenger or freight services – a statement of the terms and conditions on which the operator provides the services; and
- (b) the terms and conditions on which the operator is prepared to make the operator's railway infrastructure available for use by others; and
- (c) other information required by the regulator.

...

(3) The information brochure must refer to any relevant pricing principles and show how the terms and conditions relate to, or compare with, relevant pricing principles.

Section 28 of the ROA Act therefore sets out the requirements of an Information Brochure to be prepared by the access provider. The role of the Information Brochure is to provide access seekers with some initial information about access to the access provider's railway services, including the terms and conditions on which the access provider is prepared to make its railway infrastructure available for use by others. The purpose of these information requirements is to establish minimum rights and obligations to facilitate the exchange of preliminary information about access, and is not intended to dictate how a party must start or conduct its commercial negotiations.

### 4.2 *Key Issues*

Chapter 4 of the Commission's Information Kit sets out the current requirements for the Information Brochure. These include:

- ▲ a description of the access provider's railway infrastructure that the Access Regime covers;
- ▲ proposed terms and conditions of access that would comprise an access contract;
- ▲ floor and ceiling prices for access showing how the proposed terms and conditions of access relate to the pricing principles; and
- ▲ corporate information about the access provider.

In its Draft Inquiry Report, the Commission nominated three existing deficiencies in the Information Kit that it planned to consider addressing, namely:

- ▲ unbundling of access prices;
- ▲ providing more explicit information on the level of service quality that is to be provided at a particular price; and
- ▲ demonstrating how any proposed capital expenditure is linked to service requirements and how it is being incorporated into the access prices (either through capital contributions or tariffs).

While the requirement for access prices to be unbundled is consistent with information to be provided prior to the access provider receiving information regarding specifics of any third-party access to railway infrastructure (e.g. in the Information Brochure), the same is not necessarily the case with regard to the level of service quality or any proposed capital expenditure that may be linked to service requirements. The Commission expressed the view in its Draft Inquiry Report that:

*"...the principal function of these [s.28] standard terms and conditions, including price limits, is to provide a starting point for meaningful commercial negotiations to occur, and is not intended to limit the extent or scope of information being exchanged in a commercial negotiation process. Therefore, it is reasonable to expect the Information Brochure to provide only high level and indicative information, noting that it is not possible for the access provider to address the specifics of an access request in the first instance."*

On this basis, the Commission believes that matters in relation to the level of service quality or any proposed capital expenditure are better dealt with as part of any guidelines developed by the Commission with regard to the obligations under section 29 of the ROA Act on an access provider. This is further discussed in chapter 5.

#### 4.2.1 Unbundling of Access Prices

While there had been concern expressed in submissions to the Inquiry's Issues Paper and Draft Inquiry Report that access offers were provided in a bundled form, encompassing both above and below rail services, the Commission was ultimately satisfied that bundled access prices were not generally the case. Nevertheless, for the avoidance of doubt, the Commission can see merit in requiring access prices to be unbundled such that associated below-rail access prices are separately identified as a matter of course.

The Commission stresses that that prices provided to access seekers must be provided in a manner that would provide for a clear differentiation in above- and below-rail access prices and, more importantly, allow access seekers to determine the reasonableness of the access prices offered.

#### 4.2.2 Section 28(3) requirements

In accordance with section 28(3) of the ROA Act, the Information Brochure must refer to any relevant pricing principles established by the Commission and show how the terms and conditions it contains relate to, or compare with, the pricing principles.

While the Information Brochure already provides certain information (e.g. rate of return on capital used for the purpose of the floor and ceiling price calculations and a repeat of the floor and ceiling price concepts from the Commission's pricing principles), the Commission believes that the Information Kit could be extended to list in more detail the requirements to be met by the access provider in order to comply with this obligation. Indeed, the Commission expressed in its Draft Inquiry Report that:

*"...the Commission considers the current requirement for an access provider to demonstrate how the floor and ceiling prices relate to the pricing principles is somewhat vague and could be clarified. As such, it would be more beneficial to require an access provider to provide more specific information to demonstrate how the proposed access price was developed."*

The nature of this 'more specific information' is suggested by the elaboration to the Commission's floor and ceiling pricing principles proposed in chapter 3.

#### 4.2.3 Likely (or Indicative) Access Prices

Beside indications of the likely floor (incremental cost) and ceiling (economic cost) prices for each of the main segments to which access may be sought, the Commission is of the view that any meaningful pricing information provided by the access seeker – if it is not prepared to nominate likely access prices – should at least also requires some indication of the factors used in determining where the access price might most appropriately fall between the floor and ceiling price.

The Commission believes the provision of such information could assist the access seeker in determining the reasonableness of the access prices offered.

#### 4.2.4 Other (non-price) terms and conditions

Under section 28(1) of the ROA Act, the access provider is obligated to include in its Information Brochure a statement of the terms and conditions on which it provides access to its railway infrastructure. These terms and conditions go beyond just pricing indications. Chapter 4 of the Information Kit currently specifies minimum level of non-price terms and conditions that the access provider is obliged to provide in the Information Brochure. These relates to, among other things, average transit times and ruling grade.

Notwithstanding, the Commission can see merit in expanding the types of non-price terms and conditions that it would find to be in compliance with the access provider's obligations under section 28(1) of the ROA Act and, also, to ensure greater consistency with the ARTC's Access Undertaking.

The types of non-price terms and conditions that the Commission would find to be in compliance with the obligations are suggested by the (non-price) terms and conditions listed in the ARTC Undertaking to be made available to access applicants to assist with negotiations. It includes:

- ▲ path length availability;
- ▲ available capacity;
- ▲ axle load limitations;
- ▲ maximum allowable speeds;
- ▲ infrastructure characteristics;
- ▲ applicable safeworking requirements; and
- ▲ segment run times.

### **4.3 *Proposed Amendments***

In order to provide firmer guidance in the early stages of an access negotiation, the Commission proposes to revise the Information Kit's requirements with respect to the access provider's Information Brochure be revised with a view to:

- ▲ making explicit the requirement for separation of above- and below-rail components of the indicative prices;
- ▲ requiring the access provider to provide more detail regarding the factors to be used to determine where access prices are likely to fall within the floor-ceiling range;
- ▲ including greater detail regarding the quantitative basis of the indicative floor and ceiling prices provided; and
- ▲ listing the types of non-price terms and conditions of access to be provided by the access provider.

## 5 SECTION 29 GUIDELINES

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In addition to the proposed amendments to Chapter 3 and 4 of the Information Kit, the current review also needs to consider whether or not the Information Kit should provide greater guidance on the information requirements set out in section 29 of the ROA Act.

This final chapter of the Discussion Paper therefore sets out the Commission's views as to nature and detail of information which an Operator ought to provide under s. 29 in order to meet the intention of that section. While the Commission's views on this issue are not binding per se on an Operator, they represent a best practice approach in access regulation by promoting an exchange of information between an Operator and a person applying for access that is intended to facilitate successful negotiation of access.

### 5.1 *Legislative framework*

Section 29 of the ROA Act in part provides as follows:

*Operator's obligation to provide information about access*

*(1) An operator [access provider] must, on the application of a person with a proper interest in making an access proposal to the operator, provide the applicant with information reasonably requested by the applicant about –*

- (a) the extent to which the operator's railway infrastructure is currently being utilised; and*
- (b) the extent to which it would be necessary, and technically and economically feasible, to add to or extend the operator's railway infrastructure so that it could meet requirements stated in the application; and*
- (c) whether the operator would be prepared to provide a service of a specified description and –*
  - (i) if so, the general terms and conditions (including an indication of the likely price) on which the operator would be prepared to provide the service; and*
  - (ii) if not, the reasons why the service cannot be provided.*

### 5.2 *Key Issues*

Sections 28 and 29 of the ROA Act each concerns a distinct and separate phase of the overall access negotiation process. While the former deals with information provided before any access is sought, or even discussed, the latter deals with information exchanges once an access proposition is being discussed, but before any formal access application has been made. Hence, both sections deal with the formative stages of an access negotiation.

Specifically, section 29(1)(c)(i) of the ROA Act obliges the access provider to make available:

*...the general terms and conditions (including an indication of the likely price) on which the operator [access provider] would be prepared to provide the [access] service.*

Based on the Commission's compliance powers under section 9(2) of the ROA Act, access negotiations would therefore be assisted were the Commission to identify – in its Information Kit – the types of information about access that would be compliant with the access provider's obligations under section 29(1)(c)(i) of the ROA Act.

The Commission believes the provision of relevant information forms a critical input into the process of commercial negotiations between an access provider and an access seeker and, ultimately, underpins the effectiveness of the Access Regime's negotiate-arbitrate framework. Indeed, it expressed in its Draft Inquiry Report that:

*"The Commission believes that the requirement on an access provider to negotiate in good faith encompasses the need to provide sufficiently detailed information on the terms of access, including price, to ensure that an access seeker can understand the basis on which the offer was prepared. Transparent and timely information is a key input into successful negotiation."*

On this basis, the Commission can see merit to give more guidance on information requirements in relation to section 29 rather than solely in relation to section 28 of the ROA Act. Furthermore, the Commission is also of the view that its identification of limitations in the Information Kit regarding the level of service quality or any proposed capital expenditure are better dealt with under the obligations on an access provider under section 29 of the ROA Act.

### 5.2.1 Likely (or Indicative) Access Prices

Under section 29(1)(c)(i) of the ROA Act, the onus is on the access provider to specify:

*...the general terms and conditions (including an indication of the likely price) on which [it] would be prepared to provide the service [requested by the access applicant] (emphasis added).*

The Commission is of the view that the Information Kit should include guidance as to the general nature of likely (or indicative) prices that would be compliant with the access provider's obligations under 29(1)(c)(i) of the ROA Act. This could involve guidelines generally based on the reference prices required to be published under the ARTC's Access Undertaking and the AustralAsia railway access regime, without going so far as requiring the publication of any 'reference prices'. Indeed, by their nature, such likely (or indicative) prices would need to be based on assumed or standard loads or characteristics.

Under the ARTC Undertaking, an "indicative access proposal [offer]" is to set out (among other things):

*...an initial estimate of the Charges for the Access Rights, based on the pricing principles set out in Part 4 [of ARTC's Undertaking]... (clause 3.8(c)(v))*

Also relevant is section 23(2) of the ROA Act which states:



*An operator [access provider] must not unfairly discriminate between industry participants in the terms and conditions on which the operator provides access to railway services.*

The Commission believes that price differentiation – with different prices being charged for the same or similar services – can be consistent with economic efficiency in a number of senses.

For this reason, the Commission's position in the AustralAsia railway context has been that any price differentiation within a 'market' should be based on cost and risk differences alone. On this basis, different prices for different traffics would be justified only where different markets are being served, whether because of product or service quality. The Commission therefore believes that similar guidance could be useful under the Access Regime.

The Commission also accepted in the AustralAsia railway context that access prices should be structured so as not to distort competition in above-rail or end-user markets. In particular, there should be consistent charges for directly competing services (same specified commodity between a specified origin and destination at a similar time). Prices in the same market (limited by commodity, geography etc) should therefore be set so that prices only differ because of identifiable costs or risks, noting that it would not prevent service-related price differences within a market.

This stance is also consistent with the ARTC Undertaking (clause 4.3).

#### *Limits on Charge Differentiations*

*(a) ... in formulating its Charges, ...ARTC will not have regard to:*

*(i) the identity of the Applicant; and*

*(ii) whether or not the Applicant is a Government Authority.*

*(b) ... in formulating its Charges, ARTC will not differentiate between Applicants in circumstances where:*

*(i) the characteristics of the Services are alike; and*

*(ii) the Applicants are operating within the same end market.*

*For the purposes of this clause, ARTC will determine whether the characteristics of two Services are alike having regard to matters including but without limitation location, duration and quality of the Train Path, nature of Train consist, characteristics of the Service, longevity of Access, arrival and departure times of the day and week.*

## **5.2.2 Scope of (non-price) terms and conditions**

Under section 29(1)(c)(i) of the ROA Act, the onus is on the access provider to specify:

*...the general terms and conditions (including an indication of the likely price) on which [it] would be prepared to provide the service [requested by the access applicant] (emphasis added).*

The Commission is of the view that the Information Kit could include guidance as to the minimum nature of the (non-price) terms and conditions that would be compliant with the access provider's obligations under section 29(1)(c)(i) of the ROA Act. This could involve guidelines generally based on similar requirements regarding the (non-price) terms and conditions required to be published under the ARTC Undertaking and the AustralAsia railway access regime.

Such additional guidance in the Information Kit would particularly address concerns expressed by the Commission in its Draft Inquiry Report with existing deficiencies in relation to information with respect to both:

- ▲ the level of service quality that is to be provided at a particular price; and
- ▲ how any proposed capital expenditure is linked to service requirements and how it is being incorporated into the access prices (either through capital contributions or tariffs).

More generally, the general terms and conditions could include (but not limited to):

- ▲ the minimum performance standards to be met by the access provider;
- ▲ any minimum or indicative annual purchase quantity obligations;
- ▲ the length of the period/term of the proposed access arrangement, and the terms laid down for renegotiation of terms and conditions at the end of the access contract;
- ▲ details of any actions or activities by one or other party prohibited under the terms of the proposed access contract;
- ▲ details of any actions or activities required to be undertaken by one or other party under the proposed access contract;
- ▲ the risks to be assigned to each party under the proposed access contract; and
- ▲ all other material non-price terms and conditions.

Notably, under the ARTC Undertaking (clause 3.3(a)), there is also a catch-all provision that ARTC will provide, where requested:

*(x) any other information relating to Capacity or Train operations reasonably required by the Applicant in relation to the Access Application, provided ARTC is given an opportunity to provide to the Applicant an estimate of the reasonable cost of preparing the aspects of such other information which are not ordinarily and freely available to ARTC, and the Applicant agrees to pay such costs.*

*(b) ARTC's obligation under clause 3.3(a) is subject to:*

*(i) ARTC not disclosing any information which would breach a confidentiality obligation binding on it; and*

*(ii) the Applicant agreeing to pay the reasonable costs incurred by ARTC in obtaining information that is not ordinarily and freely available to ARTC.*

### **5.3 Proposed Amendments**

In order to provide firmer guidance during access negotiations (and beyond the Information Brochure), the Commission proposes to extend the Information Kit to include:

- ▲ general guidelines as to the nature of likely (or indicative) prices that would be compliant with the access provider's obligations under section 29(1)(c)(i) of the ROA Act (including in relation to complying price differentiation); and
- ▲ guidance as to the minimum nature of the (non-price) terms and conditions that would be compliant with the access provider's obligations under section 29(1)(c)(i) of the ROA Act.

## **6 CONSULTATION PROCESS**

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This Discussion Paper and the accompanying Draft Revised Information Kit is designed to obtain feedback and comment from stakeholders in relation to the form and content of proposed amendments to the Commission's Information Kit. The Commission has attempted to highlight relevant issues and considerations throughout this paper to assist stakeholders with the preparation of submissions.

The proposed amendments to the Information Kit put forward in this Discussion Paper have been reflected in the accompany Draft Revised Information Kit for stakeholders' comment.

Submissions to the Discussion Paper and the accompanying Draft Revised Information Kit are to be provided by 29 January 2010.

The Commission will review all comments and prepare a Final Revised Information Kit for release in March 2010.