ROY HILL INFRASTRUCTURE PTY LTD

FURTHER SUBMISSION TO ECONOMIC REGULATION AUTHORITY

2015 REVIEW OF RAILWAYS (ACCESS) CODE 2000

1 INTRODUCTION

This submission is made by Roy Hill Infrastructure Pty Ltd (**Roy Hill**) in response to the invitation by the Economic Regulation Authority (**Authority**) dated 7 May 2015 for written submissions on "...issues associated with the prescriptiveness of the regime and the valuation method prescribed in clause 2(4) of Schedule 4 to the Code…" (Notice issued by the Authority dated 7 May 2015).

2 SUMMARY

In summary, this submission by Roy Hill recommends the following:

(a) In relation to the "prescriptiveness of the regime", the Western Australian access regulation framework created by the Railways (Access) Act 1998 (WA) (**Act**) and the Railways (Access) Code 2000 (WA) (**Code**) (together the **WA Access Regime**) are not consistent with the Competition Principles Agreement of 11 April 1995 as amended 13 April 2007 (**CPA**). The prescriptiveness of the WA Access Regime should be reduced. The WA Access Regime requires that negotiations are conducted within a number of significant limiting parameters and therefore the parties are not free to negotiate the terms and conditions of access as required by the CPA and which would allow an arm's length negotiation process.

(b) In relation to "… the valuation method prescribed by clause 2(4) of Schedule 4 to the Code…" (namely the Gross Replacement Value(**GRV**) of the railway infrastructure), the GRV should be retained in the first instance. However, as the GRV methodology is inadequate in relation to greenfields developments in that it does not account for risk assumed by the owner or the developer of the railway, the GRV of any new railway which becomes subject to the Code should include a loading above the actual cost of the infrastructure to accommodate the initial risks assumed by the infrastructure owner.

3 PRESCRIPTIVENESS OF REGIME

3.1 The underlying principles of the CPA are set out in paragraphs 6(4)(a)-(c), (e) and (f) of the CPA. The fundamental elements of the CPA are that:

(a) the terms and conditions of third party access should be negotiated between the owner of the infrastructure and the third party access seeker;
(b) there should be an enforceable right to negotiate;
(c) if the infrastructure owner and the third party access seeker cannot reach agreement, the parties should be required to appoint and fund an independent body to resolve the dispute; and
(d) the dispute resolution body must take into account certain prescribed matters in resolving the dispute, including those set out in CPA paragraph 6(4)(i) of the CPA.

3.2 This submission explains in some detail how the WA Access Regime does not allow parties to freely negotiate the terms and conditions of access as required by Part 111A and the CPA. The restrictions which are imposed on parties to freely negotiate the terms of an access regime should be eliminated.

3.3 Section 17 of the Code provides that in negotiating an access agreement the railway owner and the access seeker must:

(a) ensure that provision is made in detail for the matters specified in Schedule 3 of the Code;
(b) give effect to the provisions of schedule 4 of the Code; and
(c) include in the agreement all matters agreed between them apart from provisions implied by law or incorporated in the agreement by reference.

Schedule 3 sets out a list of 23 issues or matters which must be addressed in an access agreement. Schedule 4 sets out certain parameters regarding the calculation of the price payable by the operator to the railway owner.

3.4 Further, section 6 of the Code requires that a railway owner prepare and make available for purchase a standard access agreement. Section 7 of the Code requires that the railway owner make available to the access seeker within 14 days of any request detailed information regarding:

(a) an initial indication of:
    (i) the available capacity of the route;
    (ii) the price that the access seeker might pay for the access;
    (iii) the terms, conditions and obligations that the railway owner would want to be included in any access agreement;
(b) for each relevant route, particulars of:
    (i) the gross tonnes carried on the section for each of the three complete financial years of the railway owner preceding the day on which the request is received;
    (ii) the curve and gradient systems;
(c) the working timetables for the route; and
(d) the origin and destination of the train paths proposed by the railway owner for the route.

3.5 A railway owner is also required to have approved by the ERA the Part 5 Instruments. The Part 5 Instruments deal with detailed matters concerning the regulation and operation of the railway, being the train management guidelines (section 43 of the Code), the statements of train path policy (section 44 of the Code), the costing principles (section 46 of the Code) and the overpayment rules (section 47 of the Code).

3.6 Section 40(2) of the Code also prescribes that the Part 5 instruments are binding on a railway owner.

3.7 In contrast, section 4A(1)(c) of the Code provides that a Part 5 Instrument is not to be taken into account in determining the rights, powers, duties and remedies of parties to negotiations carried on or an agreement made otherwise than under the Code. It is clear that section 4A is inconsistent with section 40(2) of the Code – if the Part 5 Instruments are binding on a railway owner, how can they not be taken into account in determining the rights, powers and duties of the railway owner as required by section 4A of the Code?

3.8 If a dispute arises between a railway owner and an access seeker, the access seeker may refer the dispute to arbitration. The appointed arbitrator is required to, in determining the dispute, to "… give effect to… the Act and the Code and matters determined by the Regulator…" (section 29(1) of the Code). It is only in those particular situations identified in sections 25(2)(a) and (c) of the Code that the arbitrator is to apply the provisions of paragraphs 6(4)(i), (j) and (l) of the CPA. These situations are limited to the refusal to negotiate and the failure to agree an access agreement: they do not extend for example to a disagreement about a matter determined by the Regulator. There is no guidance in section 29 as to whether the Act, the Code and the matters determined by the Regulator prevail over clauses 6(4)(i), (j) and (l) of the CPA in the event of any inconsistency.

3.9 Therefore, in relation to disputes to be determined by an arbitrator which do not fall within the circumstances in section 25(2)(a) and(c) of the Act, the arbitrator is not required to have regard to the principles of paragraphs 6(4)(i), (j) and (l) of the CPA. The arbitrator will nevertheless be required to give effect to the Act and the Code, which cause the regime created by the Act and the Code to be overly prescriptive.

3.10 The WA Access Regime is prescriptive and requires the railway owner and access seeker to negotiate within certain parameters and to address certain predetermined issues in those negotiations. These predetermined issues are not ancillary or side issues. They are significant fundamental access issues, and are inconsistent with the fundamental requirements of the CPA. Roy Hill submits that the WA Access Regime is too prescriptive on matters which are critical to a railway owner. Matters which should be left to the parties to negotiate and which should be left to the independent dispute resolution body to resolve if

the parties cannot agree, are prescribed by the WA Access Regime or are dependent upon the Part 5 Instruments and other determinations by the ERA.

3.11 It follows from this conclusion by Roy Hill that the WA Access Regime is currently too prescriptive that:

(a) Roy Hill agrees with the conclusion by Ernst &Young in their paper dated April 2015 (attached to the submission by The Pilbara Infrastructure Pty Ltd dated 2 April 2015) rejecting the adoption of a prescribed benchmark tariff as it would limit terms available for negotiation;
(b) Roy Hill agrees with the conclusion by Brookfield Rail at paragraph 1.2.17 of the Brookfield Rail submission that "… BR is not of the view that a change to a more prescriptive regime would improve the ability of the Code to give effect to the objectives of the CPA"; and
(c) Roy Hill supports the comments by Aurizon in its submission dated 2 April 2015 supporting the Code as a high level, principles based governing document, and commenting that Aurizon "… would not support any material increase in the level of prescription and detail in the Code itself' (at para 4.3 of the Aurizon submission).

4 VALUATION METHOD

4.1 In Roy Hill's submission of 23 March 2015, Roy Hill concluded that "….*consideration should be given to accommodating either GRV or DORC approaches to be adopted by infrastructure owners."*

4.2 Roy Hill has accepted the Authority's invitation to provide further input and commentary on other submissions made to the Authority. In summary Roy Hill has concluded as follows:

(a) Roy Hill supports the conclusions by Brookfield Rail:

(i) that in order for there to be any change to an alternative valuation method, it must be conclusively demonstrated that the GRV valuation method fails to calculate efficient costs, and further that it must be demonstrated that the change from GRV to an alternative method would result in benefits that exceed the costs of the change (at paragraph 1.1.10 of the Brookfield submission);
(ii) The ERA has not provided any evidence of the unsuitability of the GRV methodology as it relates to the giving effect to the objectives of the CPA, nor has the ERA provided commentary regarding how a valuation method other than GRV would function, although such a change would have substantial and wide ranging ramifications on the application of the Code (at paragraph 1.1.2 of the Brookfield submission);

(b) Roy Hill supports the commentary and the conclusions by Aurizon:

(i) That "… there are also issues with the application of the Gross Replacement Value (GRV) methodology to greenfields infrastructure. This includes its potential failure to account for risks incurred by the developer during the development and construction phase, which could be completely ignored in a GRV process" (at page 13 of the Aurizon submission); and

(ii) recognising that the different approaches (namely the GRV, the Depreciated Optimised Replacement Cost (DORC) and the Optimised Replacement Cost (ORC) methodologies) have their strengths and weaknesses railway owners should be able to propose the methodology which best suites the circumstances of their particular network (at page 24 of the Aurizon submission);

(iii) that the Regulator should be able to approve the particular methodology selected by the railway owner, and once approved, neither the Regulator nor the railway owner should be subsequently able later to apply a different approach (at page 24 of the Aurizon submission).

Roy Hill Infrastructure Pty Ltd

17 June 2015