Review of the *Railways (Access) Code 2000*

Draft Report

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Economic Regulation Authority
WESTERN AUSTRALIA

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Contents

OVERVIEW

1. The Authority is required to undertake a review of the Code on the third anniversary of its commencement and every five years thereafter. The Code commenced on 1 September 2001.

2. The purpose of this review of the Code is to assess the suitability of the provisions of the Code to give effect to the Competition Principles Agreement (CPA) in respect of railways to which the Code applies.

3. The CPA provides a framework to allow third parties to access nationally significant infrastructure facilities that exhibit natural monopoly characteristics and cannot be duplicated economically.

4. Some submissions to this review have sought to address the wider effectiveness of the Code, including in terms of meeting the objectives of the WA railways access regime itself, which is to encourage the efficient use and investment in railway facilities by establishing a contestable market for rail operations.

5. With respect to the effectiveness of the Code in facilitating third party access, the Authority notes the following:

    - To date there have been no access agreements struck under the Code.
    - There have been a number of agreements made outside the Code despite the regulatory option being available.
    - Most regulatory regimes for access are a safety net whereby agreements outside of the regulatory scheme are not unusual and in some cases may be preferable as they allow suitable terms and conditions to be agreed without restrictions.
    - There have recently been two proposals made pursuant to the Code and both are incomplete in terms of the negotiations. The arbitration provisions have been employed in the case of one application and it is yet to be determined whether the parties will conclude the regulatory process.
    - Submissions to this review provide some evidence that access seekers have been challenged in employing the Code processes.

6. The Authority does not consider the absence of Code access agreements, per se, as evidence of a Code failure given the nature of the regime is light handed and intended to be available to parties who are otherwise unable to negotiate access. Therefore, the Authority considers it is too early to objectively assess the effectiveness of the Code, particularly given the proposals currently under negotiation remain unresolved. Nevertheless, it is evident that the Code processes have presented some challenges.

7. On 20 February 2015, the Authority published an Issues Paper. Submissions were invited on matters raised in the Issues Paper or on any other issue.

8. Eleven submissions were received in response to the Authority's Issues Paper. These initial submissions have been published on the Authority's website.

9. On 7 May 2015, the Authority invited further submissions specifically on prescriptiveness of the regime and the valuation method prescribed in the Code. Ten

submissions were received in response to this invitation and these have been published on the Authority's website.

10. The Authority has considered the issues raised in submissions under a number of headings. The Authority has made nine recommendations under these headings.

Objects of the Railways Access Regime

11. The CPA requires that an access regime has an objects clause that promotes the economically efficient use of, operation and investment in significant infrastructure thereby promoting effective competition in upstream or downstream markets.

12. The Code does not have an objects clause, and the objects clause in the Act applies, which is:

> The main object of this Act is to establish a rail access regime that encourages the efficient use of, and investment in, railway facilities by facilitating a contestable market for rail operations.

13. The Authority has received two submissions that considered the current object of the regime to be sufficient. One other submission commented that the object was deficient as it did not explicitly refer to upstream or downstream markets.

14. The National Competition Council, when it last considered the suitability of the WA rail access regime as an effective regime, reported that the objects clause in the WA Act was sufficient to meet the requirement that the regime includes an appropriate objects clause.

15. The Authority considers that the regime includes an adequate object clause and has not made any recommendation for amendment in relation to this issue.

Scope of Railway Regulation

16. The Act and the Code apply to below-rail facilities. Railway infrastructure is defined in section 3 of both the Act and the Code to include: railway track, tunnels and bridges, control systems, associated plant and equipment; and specifically excluding: rolling stock, freight centres, terminal yards and depots.

17. The Authority has received one submission that commented on the scope of railway regulation. That submission commented that the regulations should encompass the entire supply chain, including loading and unloading facilities at mines and at ports.

18. This issue has been revisited a number of times in consideration of the railway owner's regulatory instruments, and has also been the subject of regulatory decisions made in respect of railways to which the WA Code does not apply. The Act is particular about the definition of 'railway infrastructure' that applies to the regime, and non-railway infrastructure is specifically excluded.

19. The Authority is aware of an Australian Competition Tribunal ruling that "end effects", and in particular port operations, should not be ignored in assessing capacity for the purposes of rail access. The Authority has included provisions in regulatory instruments for some railway owners, where appropriate, to take account of shipping timetabling requirements and 'committed capacity'.

20. The Authority has not made any recommendations for amendments in relation to this issue.

Prescriptiveness of the Regime

21. The WA rail access regime is 'light-handed', which means that it does not establish a 'reference' tariff in relation to an access proposal, but instead establishes boundaries for negotiations on price. The regime allows for negotiations between the railway owner and proponent on the terms and conditions for access, and for arbitration where the terms and conditions cannot be agreed.

22. Generally, it would be expected that rail access would be less regulated than electricity or gas access due to the competition to rail from other transport services. This competition should provide for a greater degree of countervailing market power in rail access negotiations than in electricity or gas access negotiations.

23. The Code provides guidelines for negotiation of prices between total and incremental costs boundaries determined by the regulator. The guidelines require that prices are consistent between operators and reflect the standard of the infrastructure concerned as well as the operations proposed to be carried out by the proponent.

24. The Authority has received a number of submissions that commented on the prescriptiveness of the regime.

25. Some submissions indicated that a more prescriptive approach was preferred and, in particular, that the Code should require reference tariffs to be set by the regulator. In contrast, submissions from railway owners expressed a preference for continuation of the more light-handed approach.

26. The Authority agrees with comments in some submissions that a change to a more prescriptive approach would require substantial parts of the Code to be re-written and that the periodic determination of reference tariffs would require a method that calculates the actual depreciated value of assets for particular routes over time. The introduction of reference tariffs would lessen the role of negotiation.

27. The Authority accepts the comments in some submissions that the negotiate-arbitrate approach is appropriate where the condition of the track is not at replacement standard or where capital investments to the infrastructure cannot be justified by either the railway owner or the access seeker. This is because the negotiate-arbitrate approach allows the parties to establish an agreed price on the basis of the condition of the track, and the economic value the proponent expects to obtain from use of the track in that condition.

28. The Authority agrees with the views of some stakeholders that, under certain circumstances, a more prescriptive approach with reference tariffs being set by the regulator would be preferred over a light handed negotiate-arbitrate approach. These circumstances are:

    - Where there is a significant number of access proposals in relation to a particular service type (that is, homogenous freight tasks). In this situation, there is less need for negotiation to meet the circumstances of a particular access seeker, and fewer reference tariffs would need to be established.

    - Where the track condition is close to replacement condition. This is because it is likely that prices would be negotiated close to the ceiling, and the potential for regulatory error in setting a reference tariff would be lessened.

- Where there is less incentive for the infrastructure provider to negotiate for access to its rail network. For example, this could be due to its vertical integration into competing downstream markets.

29. These circumstances do not prevail across all WA railway networks, but elements are apparent on some routes. On this basis, the Authority considers that:

- The negotiate-arbitrate approach is suited to those parts of the WA freight network where the track condition may not be at replacement standard, or where there is a wide variety of service types.
- A more prescriptive approach may be appropriate on the interstate freight route where freight tasks are more homogenous and the track condition is consistently good, and where price outcomes are more likely to be negotiated closer to the ceiling.
- In respect of the TPI railway, that the homogeneity of freight task, standard of track and also the above-rail operation of the railway owner will result in prices being negotiated at, or close to, the ceiling, thereby diminishing the usefulness of the negotiate-arbitrate framework in the context of that railway.

30. The Authority notes comments in submissions relating to the Competition and Infrastructure Reform Agreement (CIRA), signed by all Australian Governments in 2006, which requires significant interstate routes to be open for regulation by the Australian Competition and Consumer Commission (ACCC) on the basis of the Australian Rail Track Corporation Ltd. (ARTC) access undertaking. The Authority has noted that the CIRA appears to be drafted to apply unconditionally to the interstate routes and to apply to other (intra-state) routes on an agreed basis, subject to cost benefit assessment.

31. The Authority considers that implementation of the CIRA in respect of the interstate freight route (from Kalgoorlie to Kwinana) may provide benefits by reducing the resources required by parties to arrive at a negotiated outcome in respect of access to that route, while at the same time preserving the usefulness of the negotiate arbitrate approach as it currently applies to the remainder of the network. By removing the interstate route from Schedule 1 of the Code, a more prescriptive regime may be applied to that route, making it more consistent with the remainder of the interstate route owned by the ARTC and without requiring the WA Code to be substantially revised to accommodate a more prescriptive approach across the whole network.

Recommendation 1

That the Government implement the 2006 Competition and Infrastructure Reform Agreement (CIRA) in respect of the interstate route west from Kalgoorlie, and the TPI railway.

Merits Review

32. The WA rail access regime does not currently include provisions for a merits review process. The Authority has received submissions that indicate that a merits review process would be beneficial.

33. The Authority has previously recommended that a formal process for merits review would not provide reassurances either to railway owners or access seekers in the

context of a light handed regulatory regime, where the role of the regulator in establishing an efficient price is limited and that role is undertaken by the parties in negotiation or by the arbitrator.

34. The Authority considers that, if the regime were more prescriptive, and if the role of the regulator was to determine the efficient price, then a merits review process may be warranted.

35. One submission argued that, to the contrary, the regulator's exercise of discretion is greater in a less prescriptive regime.

36. The Authority has not agreed with that assertion, as the regulator does not determine precise tariffs in a less prescriptive regime, but only broad parameters for negotiation. The Authority considers that the arbitrator effectively assumes the role of merits review in a less prescriptive regime.

37. The Authority considers that recourse to judicial review of an Authority determination by the WA Supreme Court is appropriate in a light-handed regime.

38. The Authority has not made any recommendations for amendments in relation to this issue.

Enforcement of Railway Owners' obligations

39. The Act and the Code provide for the application of penalties for non-compliance by the railway owner with some parts of the Code. The regulator is responsible for monitoring and enforcing compliance by railway owners with the Act and the Code. Access seekers are able to seek injunctive relief in respect of disputes between themselves and a railway owner in respect of a railway owner's obligations under the Code.

40. The Authority has received two submissions, from access seekers, that have called for a greater role for the Authority to enforce the Code.

41. The Authority considers that access seekers are as well-placed as the regulator to prosecute any failure on the part of railway owners to meet their obligations under the Code. The Code gives access seekers their own right to injunctive relief, which enables the regulator to remain impartial in inter-party disputes. The Authority considers that its own power of injunctive relief is a last resort, when the railway owner may be in default of its obligations in some respect and when there is no access proposal in the course of resolution.

42. The Authority has not made any recommendations for amendments in relation to this issue.

Segregation Arrangements

43. The regime requires railway owners to "segregate", which means that they have to separate the part of their business that provides rail infrastructure from the other parts of their business that compete with businesses that may also want to use their infrastructure. Specifically, railway owners must segregate their "access-related" functions from their other functions.

44. This requirement is described in the Act (sections 28-34). The Act requires that railway owners segregate their functions in order to protect access seekers' confidential information, to avoid conflicts of interest when a related party to the

railway owner has its own above-rail operations to ensure that other operators are treated fairly and to ensure that accounts and records are provided separately for their access and non-access functions.

45. The Authority received submissions indicating that the requirements for segregation go beyond the requirements of the CPA; the scope of the segregation arrangements should be expanded to include fairness in train path allocation; and the segregation arrangements are not adequately enforced.

46. The Authority notes that railway owners are required under the Act to segregate their access-related functions from their non-access related functions. "Access-related functions" is defined in the Act to mean "the functions involved in arranging the provision of access to railway infrastructure under the Code". "Non-access functions" therefore encompasses all other functions, including arranging the provision of access to infrastructure outside of the Code. On this basis, an expansion of the scope of segregation is not required in order to ensure fairness in allocation of train paths between operations under the Code and outside of the Code. The Authority has also noted that fairness in train path allocation is required by Part 5 of the Code.

47. The Authority notes that, although some other railway access regimes do not have stand-alone segregation or ring-fencing arrangements, equivalent provisions are included in railway owners' Access Undertakings regulated by the ACCC.

48. The Authority has not made any recommendations for amendments in relation to this issue.

Prohibitions on hindering or preventing access

49. Under the Act, a railway owner cannot hinder or prevent either access to which a person is entitled, or the making of an access agreement. A person who has access is likewise prohibited from hindering access by another person.

50. The term 'Access agreement' is defined in the Act and the Code and refers to an agreement under the Code for access to railway infrastructure.

51. The Authority has received a submission that the Code should expand on the prohibition of hindrance, due to the scope for railway owners to cause unnecessary delays. In particular, the submission suggested that 'hindering or preventing access' should include (a) "repeated failure to comply with obligations to provide information" and (b) "any conduct that has the effect of repeatedly and unnecessarily delaying an access proposal".

52. The Authority considers that "repeated failure to comply with obligations to provide information" or '"any conduct that has the effect of repeatedly and unnecessarily delaying an access proposal" is clearly conduct that hinders the making of an agreement and that the provisions of the Act would not be improved by the addition of these words.

53. The Authority has not made any recommendations for amendments in relation to this issue.

Section 8(4) and 8(5) – when can an extension and expansion be proposed?

54. The Code provides at section 8(4) for an access proposal to specify an extension or expansion and at section 8(5) for an extension or expansion to be specified in the

course of negotiations on the ground that it would be necessary to accommodate the proposed rail operations if it was not specified in the initial proposal.

55. The validity of an access proposal has been challenged in the Courts on the basis that an expansion was not specified as part of the proposal.

56. The Authority has received a number of submissions addressing this issue. Some submissions commented that an extension or expansion should be able to be proposed at any time after the making of a proposal and that an access proposal should not be invalidated on the basis that the proponent has not identified any investment required to accommodate its proposal. One submission noted that in other jurisdictions the railway owner is responsible for identifying any required investment and for advising the proponent accordingly.

57. A number of submissions have suggested that, to the extent that section 8 may be ambiguous, it should be clarified.

58. The Authority is of the view that the failure to specify an extension or expansion in an access proposal cannot invalidate an access proposal, and that the Code does not require amendment to clarify section 8(5) which clearly states that:

> The fact that an extension or expansion is not specified in a proposal as mentioned in subsection 4 does not prevent the proposal of such an extension or expansion being made in the course of negotiations under Part 3 on the grounds that such an extension or expansion would be necessary to accommodate the proposed rail operations.

59. The Authority has not made any recommendations for amendments in relation to this issue.

Section 10 – when is section 10 relevant?

60. Section 10 of the Code requires the railway owner to seek approval from the regulator to enter into negotiations on a proposal, under circumstances where providing the proposed access may preclude any further access to the existing infrastructure.

61. Section 10 is relevant when it is possible to provide adequate 'capacity' to accommodate the proposed access, but not possible to provide any further capacity.

62. The Authority has received a number of submissions addressing this issue. Most of these submissions have suggested that the wording of section 10 should be clarified, especially in the context of economic expansions.

63. Some submissions have suggested that there should be guidelines that stipulate the factors that the regulator must consider in making a decision under section 10, and that the implications of the regulator disallowing negotiations on the proposed access should be laid out.

64. Submissions from railway owners have highlighted that section 10 serves to ensure the allocation of scarce capacity to its highest value use. One railway owner submitted that the fact that an extension or expansion may accommodate a proposal does not necessarily result in the expanded capacity becoming an unlimited resource, and that the regulator should be able to assess whether or not the proposed access is allocating limited capacity to its highest value use.

65. Another railway owner has commented that other jurisdictions do not address this issue and rely on the commercial objectives of the infrastructure provider to ensure capacity is allocated to its highest value use.

66. The Authority has previously issued a section 10 decision (in 2013) that approved the commencement of negotiations in relation to an access proposal on the basis that there was no evidence that the route in question could not be expanded and that future access would not be precluded by the proposed operations.

67. The Authority notes that section 10 existed in the Code prior to amendments made in 2003, which introduced provisions for extensions and expansions.

68. The Office of the Rail Access Regulator issued a section 10 decision in 2002 that approved the commencement of negotiations in relation to an access proposal, despite there being no provisions for extensions and expansion in the Code at that time, on the basis that it was not in the public interest to do so unless it was technically not feasible to augment the capacity of the route.

69. The Authority considers that reference to section 10 is not appropriate where a route may be expanded. The Authority agrees that the commercial objectives of the infrastructure provider should be relied on to ensure that capacity is allocated to its highest value use, and recommends that Section 10 be removed from the Code.

Recommendation 2

Section 10 should be removed from the Code.

Sections 14 & 15 – Can a railway owner challenge the validity of a proposal prior to receiving the required information from the proponent?

70. Sections 14 and 15 of the Code require a proponent to show that it has management capability to undertake operations on the proposed route and to show that its proposed operations are within the capacity of the route or expanded route. A railway owner is required to inform the proponent of its requirements under these sections when it responds to an access proposal.

71. Sections 14 and 15 are “threshold issues’ relating to the obligations of a railway owner to negotiate. That is, these sections provide for matters of financial capability and route capacity to be addressed after a proposal has been made (as described in Part 2 of the Code) but before negotiations commence (described in Part 3).

72. The Authority received a number of submissions on this matter. Most submissions supported the view that the railway owner should not be able to challenge the validity of a proposal before it has received the information it requires under sections 14 and 15.

73. One submission indicated that the definition of ‘necessary financial resources’ and ‘capacity’ should be clarified in sections 14 and 15, and suggested - in relation to financial capacity - that the threshold for any such objective test should be low, as a high threshold would unfairly discriminate against access seekers that are in the process of establishing project viability. The same submission also suggested the assessment of capacity for the capacity test in section 15 should be prescriptively defined and subject to third party audit.

74. Another submission commented that the proponent should be liable for all expenses associated with expansion studies and that, in order for the proponent to provide an assessment that any proposed expansion is viable - the railway owner should be obliged to provide all necessary information to the proponent to undertake that assessment.

75. A railway owner submitted that sections 14 and 15 should be clarified to make it clear that they function as threshold issues for negotiation only, and not to confirm the validity of an access proposal. That railway owner also submitted that the validity of an access proposal should be able to be challenged at any time but only according to whether or not the proponent has met the information requirements of section 8.

76. Two other railway owners have submitted that the proponent should be required to establish financial capacity at the date of making the proposal and that a time limit should be prescribed for the satisfaction of a railway owner's section 14 and 15 requirements.

77. The Authority considers that it is clear that sections 14 and 15 are threshold issues for negotiation only. The Authority considers that the validity of a proposal is established when the proponent meets the requirements of section 8, and that meeting the railway owner's requirements under section 14 and 15 is not a criterion for making a valid proposal. The Authority notes that the railway owner is not able to indicate its requirements under sections 14 and 15 until it responds to a proposal.

78. The Authority agrees that the Code should require the railway owner to provide any information that is necessary for the proponent to undertake a capacity assessment and that the proponent should cover any costs incurred by the railway owner in doing so.

79. The Authority considers that timeframes should be established in the Code to indicate when the information required by railway owner should be provided by the proponent. This would assist the railway owner by ensuring that its requirements are met in a reasonable timeframe and reinforce the status of sections 14 and 15 as threshold requirements for negotiations, and not a requirement that establishes the validity of a proposal. The Authority considers that 30 business days is an appropriate timeframe and seeks further comment on this recommendation.

Recommendation 3

Sections 14 and 15 of the Code should be clarified to indicate a timeframe for the provision of the information required by the railway owner by those sections.

The Code at section 15 should require the railway owner to provide any required information necessary for the proponent to undertake a capacity assessment, and that the proponent must cover any reasonable costs incurred by the railway owner in providing this.

Section 16 – What does the term "unfairly discriminate" mean?

80. The Code requires a railway owner to make all reasonable endeavours to avoid unnecessary delays and to meet the requirements of a proponent whose proposal complies with the Code.

81. Section 16 of the Code specifies that a railway owner should not be unfair in relation to allocation of train paths, management of train control and operating standards. This means that it is permissible for a railway owner to discriminate against a proponent, but not "unfairly". A definition of "unfair" is not provided in the Code.

82. The Authority received a number of submissions addressing this issue. All submissions suggested that section 16 should be clarified. Most submissions indicated that the onus should be on the aggrieved party to show a reasonable foundation for a claim of unfair discrimination. These submissions suggested that a list of 'unfair discriminations' would not reduce the flexibility of the Code, but that a list of 'fair discriminations' would.

83. A railway owner submitted that section 16 should be amended to provide a non-exclusive list of examples of 'unfair discrimination', that the railway owner should not engage in. This submission did not agree with the Authority's recommendation in the second review of the Code that a non-exclusive list of examples of 'fair discrimination' should be added to section 16.

84. In contrast, two other railway owners have submitted that the Code should provide a list of examples of permissible 'fair discrimination'. Reference was made in these submissions to regulation 23 of the (now repealed) Gas Transmission Regulations 1994 (WA), and to CPA section 6(e)(9), which provide a list of considerations that should be taken into account when deciding on terms and conditions for access. A railway owner submitted that, in order to give effect to the CPA, this list should provide the basis for a list of 'permissible discrimination' by a railway owner under the Code.

85. The Authority agrees with submissions that suggest that a list of examples of 'fair discrimination' would not improve the flexibility of the Code. However, the Authority does not consider that inclusion of a list of examples of 'unfair discrimination' is required, as the remedy for unfair discrimination by a railway owner can be pursued by the access seeker through legal means. In any situation, the particular circumstances would need to be examined in order to determine whether there is a case to be made for unfair discrimination. The Authority does not consider that further prescriptiveness in the interpretation of 'fairness' or 'unfairness' is consistent with a light-handed approach to regulation.

86. The Authority has noted suggestions from one potential access seeker that there should be two key tests to demonstrate that unfair discrimination has occurred, which are: (a) it has a material adverse effect on an access seeker; and (b) it has a substantial impact on competition in the relevant market.

87. The Authority seeks any comment from stakeholders on whether the Code should further define unfair discrimination or provide a list of examples of unfair discrimination.

Part 3 – Should Part 3 prescribe a time limit for the conclusion of arbitration?

88. There are no time limits prescribed in Part 3 of the Code for the conclusion of arbitration proceedings. The Authority received a number of submissions addressing this issue.

89. Submissions from railway owners commented that it is not appropriate for arbitrary time limits to apply to the arbitration process, as this could restrict the capacity and

freedom of an arbitrator to properly consider the claims and evidence on all matters that could be presented.

90. All other submissions indicated that time limits should be prescribed for arbitration. Some of these submissions expressed the view that it would not be appropriate to impose a 'blanket' timeframe in the Code as the issues in each arbitration would vary in nature and complexity. It was submitted that a timeframe should be determined at the start of each arbitration to reflect the individual circumstances of the dispute along with provision to vary this timeframe with the agreement of both parties.

91. Consistent with the view that a timeframe should be established for each arbitration according to the circumstances of each dispute, the Authority notes that there is currently provision in in section 28 of the Code for a preliminary conference to be held as a first step in arbitration. The purpose of this preliminary conference is to establish timeframes for the conduct of the arbitration and the arbitrator's determination.

92. The Authority does not consider that further clarification in this section is required.

Section 50 – should a railway owner be able to declare any information confidential?

93. Section 50 of the Code says that the regulator is not authorised to disclose information that is confidential without the consent of those to whom the protection of confidentiality belongs. The Code does not provide a definition of "confidential". The Act provides a definition of "confidential information", which applies to railway owners' obligations in segregation and therefore relates only to protection of proponents' confidential information.

94. There have been some differing views on the meaning of section 50 as it relates to the disclosure of confidential information which may be disclosed by a railway owner to the regulator when providing costs for routes subject to an access proposal.

95. The cost information required to be provided by the railway owner to both the proponent and the regulator is limited to the calculated costs determined for each route subject to a proposal. The provision of any more detailed or additional information underpinning those calculations is provided at the railway owner's discretion.

96. The Authority received a number of submissions addressing this issue. Submissions from potential access seekers argued that primacy should be given to the transparency of regulatory processes, or a 'presumption of disclosure'. In particular, access seekers indicated that confidentiality should only be allowed if publication of that information would be commercially damaging to the railway owner in its role as an infrastructure provider charging efficient prices.

97. One submission suggested that all determinations that affect the interests of an access seeker (whether made by the regulator or the railway owner) should be provided to the access seeker in unredacted form, with limited confidentiality provisions where appropriate.

98. Another submission suggested the clauses of the CPA that relate to transparent and efficient regulatory processes are not satisfied when railway owners are able to keep information confidential. This submission cited the South Australian Rail Access Regime and the National Gas Law as examples of jurisdictions where regulators may disclose information to the detriment of the provider of the information, if the regulator

considers that the public interest in disclosing that information outweighs the detriment. This submission also commented that cost determinations are not confidential information as they are hypothetical calculations of costs for a replacement railway.

99. Railway owners submitted that there are no provisions of the CPA which say that the regulator should disseminate information, or that any weight should be given to the interests of third parties not directly involved with providing or seeking access. Railway owners submitted that they should be able to require the confidentiality of documents and information that are provided to the regulator.

100. The Authority published a decision in August 2011 that stated it would not publish the railway owner's or its own determinations of costs relevant to a proposal unless the proposal proceeded to an agreement.

101. However, in the course of finalising its most recent two cost determinations, the Authority has subsequently established a process that meets the requirements of the access seeker for adequate transparency as well as the railway owner's requirements to protect its confidential information.

102. This process has resulted in the access seeker being provided with an unredacted copy of the Authority's determination, including the costing information provided by the railway owner, on a confidential basis, and the Authority publishing a redacted version of the determination, which obscures the railway owner's confidential information.

103. The Authority has not made any recommendations for amendments in relation to this issue.

Clause 2 Schedule 4 – is there a better means of estimating capital costs than the GRV method?

104. The approach of the WA rail access regime is "light-handed", which means that the regulator sets a range within which parties negotiate a price. This report has concluded that the light handed approach to regulation is appropriate for the WA rail networks currently covered by the Code, with the exception of the interstate route on the freight network and the TPI railway.

105. The negotiating range is the range of costs between "incremental costs", being usually only operating costs associated with the proposed operations, and "total costs" which is all costs including capital costs and operating costs associated with all operations on the route.

106. Parties can negotiate a price for a route that incorporates a capital component that varies depending on the number of operators on the route and the condition of the asset.

107. For the purposes of establishing the capital component of total costs, the Code currently requires that a "Gross Replacement Value" method (GRV) be used, which is the cost to replace the asset with a new asset. The GRV does not necessarily relate to the asset's current condition.

108. All other railway access regimes in Australia establish the capital component of total costs based on an asset value that is rolled forward over time, established in the first instance on a 'Depreciated Optimised Replacement Cost' (DORC) basis. This has

been referred to in this report as the 'DORC approach' to valuation. This approach aims to determine a precise capital value for the asset incorporating depreciation of, and additions to, the asset stock. The capital component of costs under a DORC approach therefore reflects condition of the asset as closely as possible.

109. The DORC approach of other railway access regimes is generally not associated with a light-handed "negotiate-arbitrate" regulatory regime but rather with a more prescriptive "reference tariff" scheme where there is less scope for negotiation.

110. The issue of whether the DORC approach should replace the GRV method in the WA regime has been the subject of previous Code Reviews. In this review, the Authority has received a number of submissions addressing this issue.

111. Potential access seekers all submitted that a DORC approach is preferred to the GRV method. The reasons given for this include consistency with other Australian rail regimes; capital values being set to reflect the condition of the asset; and the avoidance of potential windfall gains to the railway owner associated with capital costs rising over time.

112. Railway owners submitted that the GRV method was preferred, generally on the basis that it is simpler and less costly to administer and enables more flexible negotiations. These submissions commented that the implementation of a DORC approach would require a substantial revision to the Code.

113. One railway owner and one potential access seeker have submitted that railway owners should be able to choose the valuation method that applies to their railway.

114. The Authority considers that it is not practical for the Code to accommodate both the GRV method and DORC approach. There are different information requirements associated with administering these two schemes as well as different levels of prescriptiveness associated with the two approaches.

115. The Authority does not consider that the DORC approach to establishing capital costs is broadly compatible with a light handed negotiate-arbitrate approach. This is because one of the principal grounds for negotiating a price is the condition of the asset. If the condition of the asset is reflected in the capital component of total costs, then the scope for negotiation below the "ceiling" price is limited.

116. An argument common to a number of submissions was that the GRV is "flawed" as it results in a misalignment of the assumed standard of the infrastructure with its actual standard. However, the Authority notes that the Code clearly lists the actual condition of the track as a determinant of price in negotiation, and the replacement specification of the track as a determinant of the upper cost bound for negotiation. The standard of the asset used by the regulator to determine capital costs can be significantly different to the standard of the asset assumed in negotiations on price.

117. The Authority does not agree with assertions that the use of a GRV method provides the potential for windfall gains to the railway owner. These assertions appear to assume that the agreed escalation of prices in an access agreement is necessarily related to subsequent cost determinations; however, this is not the case. Price terms (including escalation) in access agreements are negotiated between the parties and may conceivably involve no escalation of prices at all. Subsequent cost determinations provided by the regulator may relate to separate access proposals from other operators and would not impact on the price terms of an earlier access agreement unless the parties aligned their contract to subsequent determinations.

118. The Authority notes that a number of submissions commented that the GRV approach is problematic where the technical life of an asset exceeds its economic life, and that the GRV approach is unable to adequately compensate for development risks in greenfields projects. The Authority does not consider that either the GRV or DORC scheme presents more or less problems in these respects.

119. The Authority has not made any recommendations for amendments in relation to this issue.

Clause 10 Schedule 4 – is the prescribed 30 day time limit for the making of the regulator's determination sufficient?

120. The time limit prescribed in the Code for the regulator to approve or make a cost determination is 30 days. This time limit may be extended with the proponent's agreement. The Authority received two submissions addressing this issue, both from railway owners.

121. These submissions argued that this timeframe should be increased. One of the submissions suggested that the approval of the railway owner should be sought, in addition to that of the access seeker, for any extension of time sought by the regulator.

122. The Authority considers that the provisions in clause 11 of Schedule 4 provides adequate scope for an extension of the 30 day time limit stipulated in clause 10 of Schedule 4.

123. While the Authority considers that it is appropriate for the regulator to seek the railway owner's views on whether an extension of time to make a determination is reasonable, it does not consider that a requirement to seek the approval of both the proponent and the railway owner would be a practical approach to achieving an extension of time if it were required. The Authority considers that it is the proponent's interests that are primarily affected when considering whether delaying an access determination is appropriate.

124. The Authority has not been prevented from meeting its obligations under the Code, utilising the existing provisions for time frames. The Authority has not made any recommendations for amendments in relation to this issue.

125. The Authority notes that the term "days" is not defined in the Code. By default, therefore, the term "days" must be taken to mean calendar days. The use of calendar days to define timeframes has resulted in inconsistencies and uncertainties in relation to timeframes, especially where these timeframes straddle extended public holidays such as Easter or Christmas.

126. The Authority supports the proposition that "days" in the Act and the Code should be defined to mean "business days" for consistency with other regimes, and to alleviate irregular time constraints caused by public holidays at particular times of the year.

Recommendation 4

The term "days" in the Act and the Code should be defined to mean "business days".

Part 1 [section 4A] – Parties have the option to negotiate agreements outside this Code.

127. The Code indicates that, if parties choose to negotiate an agreement for access outside the Code, nothing in the Code applies to the negotiation or any resulting agreement. This means, for example, that the Over-payment rules do not apply to any arrangements made outside the Code. The Authority received a number of submissions that commented on this issue.

128. One potential access seeker submitted that parties negotiating outside the Code should be allowed to bring that negotiation to arbitration under the Code, and that the regulator should include all agreements made, both under the Code and outside the Code, on its 'register of agreements'.

129. Another potential access seeker submitted that it is not appropriate that the Over-payment rules are not enforceable when there is no total cost determination in place. This submission commented that, because Over-payment refunds are not made to out-of-Code operators, there is an incentive for railway owners to keep operators outside the regime.

130. A railway owner submitted that it is not appropriate that Over-payment rules apply in the absence of agreements under the Code. This submission referred to clause 6(4)(a) of the CPA, which states that if an agreement is able to be made without reference to the Code, then the provisions of the Code should not apply.

131. The Authority does not consider it necessary for the regulator to maintain information on out-of-Code agreements in order to properly audit over-payment accounts. Railway owners are required to keep separate accounts and records and the regulator may require copies of these records at any time. Further, arrangements are currently in place with all railway owners for over-payment accounts to be independently audited when required, with terms of reference provided by the Authority.

132. Further, if there are no access agreements in place under the Code for a route, then there is no basis on which to establish or audit the ceiling price test (over-payment account) and there are no returns to be made to any above-rail operators regardless of the revenue earned by the railway owner. The Authority does not consider it appropriate that out-of-Code revenues for a route should be monitored by the regulator in respect of Code provisions where there are no Code agreements in place for a route.

133. The Authority has not made any recommendations for amendments in relation to this issue.

Part 2A & 2 [sections 6, 7, 7A-E] – Required and Preliminary Information

134. The Code requires that certain information provided by railway owners is required to be kept up to date and in a format available to be provided to any person who requests it. This is referred to as 'required information'. The Code also requires that

certain other information must be provided by a railway owner to any person interested in making an access proposal. This is known as 'preliminary information'.

135. The Authority received a number of submissions that commented on required and preliminary information, including one from a railway owner. All submissions commented that required information should be available free of charge from the railway owner's website.

136. A number of submissions made suggestions for improvements to the definition of specific items for required information such as train movements and the specification of capacity. The railway owner supported a consultative review to improve the usefulness of information routinely available to access seekers. It was also submitted that required information should be updated every six months, rather than every two years.

137. The Authority agrees that required information should be updated more frequently than every two years, and that modern information systems would allow this improvement at low cost. The Authority agrees that updates on a six monthly basis are appropriate.

138. A potential access seeker submitted that preliminary information should include detailed pricing information on a route-by-route basis. The railway owner referred to this comment and responded that it is the regulator's role to independently review costs and prices, and not appropriate for an access seeker to 'audit' those costs.

139. The railway owner submitted that, when an access seeker requests preliminary information, it should be required to provide information about its proposed operations in sufficient detail to enable the railway owner to tailor its response appropriately.

140. The Authority agrees with the railway owner's suggestion that a consultative process be undertaken to re-examine the appropriateness of inclusions in preliminary information, and invites further comment on appropriate inclusions. The Authority agrees that the Schedule would be improved by a clear definition of the term "available capacity". The requirement for "gross tonnage" at item 4(l) of Schedule 2 has not enabled a straight forward assessment of freight tasks in Gross Tonne Kilometre terms (the standard definition) in recent Authority determinations.

141. The Authority re-iterates its recommendation from the second review that this information should be freely available on the railway owner's website.

Recommendation 5

The prescribed time limit set out in section 7C(2)(b) for the amendment or replacement of Required Information (information described in section 7A) be reduced from two years to six months**.**

Recommendation 6

That Schedule 2 Preliminary Information be amended to clarify the meaning of "available capacity" and specify the information which must be provided under item 4(o) of that schedule.

Part 2 [section 8] – Proposals for Access

142. The Authority received two submissions, both from railway owners, addressing the information obligations of an access seeker when lodging an access proposal.

143. It was submitted that the information which must be included by a proponent in an access proposal should be expanded to assist railway owners in assessing costs, expansion requirements and negotiable terms. A list of suggested additional information was submitted.

144. The Authority agrees that the suggested additional information may assist the railway owner in providing an indicative price to an access seeker. The usefulness of the indicative price provided by the railway owner would be determined by the level of detail provided by the access seeker with its proposal. The access seeker may provide any level of detail it considers appropriate in the context of the minimum requirements laid out in the Code.

145. According to the circumstances, some of the additional information that has been suggested may only be determined in the course of negotiations. The Authority considers that the parties could only arrive at the level of detail suggested through the process of negotiating a price. In this way, the price would be determined in consideration of the suggested additional details.

146. The Authority is interested to hear further views in respect of this suggestion.

Part 3 [Division 3] Arbitration of disputes – other matters

147. The Code makes provisions for the arbitration of disputes. The regulator is required to establish a panel of arbitrators on the recommendation of the WA Institute of Arbitrators and Mediators Australia. The *Commercial Arbitration Act 2012* applies to an arbitration under the Code.

148. The Code describes the circumstances in which an entity is taken to be in dispute with a railway owner. An entity may refer a dispute to arbitration by notifying the regulator. The entity is not required by the Code to advise the railway owner that it has done so. The regulator must appoint an arbitrator, or arbitrators, from the panel of arbitrators. A railway owner may not declare itself to be in dispute with an entity.

149. A preliminary conference must be held to establish arbitration timeframes.

150. The arbitrator may refer any question relating to the arbitration to the regulator, and give whatever weight he or she sees fit to any opinion, advice or comments provided by the regulator.

151. The determination of the arbitrator is binding on the railway owner. The other party is not required to give effect to a determination if within 14 days of the determination it elects not to do so.

152. The Authority received three submissions that addressed issues related to arbitration.

153. One submission suggested that Part 3 of the Code should include a list of circumstances under which an access seeker could declare itself in dispute with a railway owner.

154. The Authority considers that Part 3 provides an adequate list of circumstances that must exist for the proponent to be considered in dispute with the railway owner and does not need to be expanded.

155. The other two submissions were received from a railway owner and a potential access seeker that were previously involved in the arbitration of a dispute between them. Both submissions expressed the view that (1) only technical matters should be brought before an arbitrator, and not statutory (legal) matters; and (2) that the parties should be involved in the appointment of an arbitrator.

156. The Authority agrees with submissions that contend that matters which can be referred to arbitration should be technical matters only and not statutory (legal) matters, for which the courts offer adequate recourse in the event of a dispute.

157. The railway owner also submitted that the entity in dispute with the railway owner should be required to advise the railway owner (and not just the regulator) that it considers itself in dispute; that the arbitration process should involve a preliminary mediation step; and that the pool of arbitrators available for selection should not be confined to WA arbitrators but extend to arbitrators with expertise nationally.

158. The Authority does not consider that the Code should be amended to require the entity in dispute with the railway owner to also provide notice to the railway owner, in addition to the regulator. The regulator is not prevented from notifying the railway owner, when it is notified by the entity in dispute.

159. The Authority does not consider that additional mediation should be stipulated in the Code. Recent experience has indicated that parties are able to undertake contract mediation services in order to assist negotiations if both parties agree this is warranted.

160. The Authority considers that the Code does not prevent the regulator from consulting with parties in the selection of an arbitrator from the panel.

161. The railway owner also submitted that the arbitrator's determination should be binding on both parties (not just the railway owner) and that this would accord with the objective of the CPA that arbitration should not be used as a substitute for negotiation, and that decisions of an arbitrator should bind the parties (subject to appeal rights).

162. The Authority does not consider that arbitration should be binding on both parties. This is because an arbitrated outcome may not be commercially feasible for an access seeker, in which case the access seeker would be disadvantaged, if it were required to pay the arbitrated price. The Authority considers that arbitrators have the power to dismiss vexatious disputes or disputes which seek to usurp proper negotiations.

163. The railway owner indicated that the decision of the arbitrator should be confidential, as each dispute is aimed to resolve specific disagreements under specific circumstances and should remain subject to the confidentiality provisions of the

Commercial Arbitration Act 2012. The potential access seeker submitted that the decisions of the arbitrator should be public so that other access seekers do not waste resources on similar disputes and to ensure consistency between decisions.

164. The Authority agrees that information and outcomes of arbitration should remain confidential, as confidential information belonging to both the railway owner and the access seeker might otherwise be disclosed. Further, the Authority considers that it would not be appropriate to publish arbitration outcomes if that outcome is not subsequently reflected in an agreement.

165. The Authority has not made any recommendations in relation to this issue.

Part 5 – Certain approval functions of the regulator

166. Part 5 of the Code describes certain regulatory instruments that the regulator must approve and the processes for approving them. These are the Train Path Policy, Train Management Guidelines, Costing Principles and Over-payment rules (sometimes referred to as "Part 5 Instruments"). A number of submissions commented on these instruments and the required processes for their approval.

167. A potential access seeker and a railway owner each submitted that they did not support standardised Part 5 instruments although the railway owner commented that a new railway should be allowed to adopt the form of instruments from an existing railway.

168. Another submission supported a consistent consultation regime on all Part 5 instruments. Currently, public consultation is required in relation to Train Path Policy and Train Management Guidelines but not in relation to Costing Principles or Over-payment rules. This submission also suggested that access seekers, as they do not participate in the approval of Part 5 instruments except through these consultation processes, should be able to negotiate variations from Part 5 instruments where appropriate. This submission noted that the railway owner is limited in its capacity to "accommodate the requirements of access seekers" if all access seekers are subject to the same operating procedures.

169. The Authority agrees that a one-size-fits-all approach to Part 5 instruments is not appropriate, and is not contemplated by the Code. The Authority requested comment on the efficacy of new railway owners adopting existing railway owners' Part 5 instruments as a temporary measure only, and prior to approval of alternative instruments by the Authority.

170. The Authority considers that access agreements generally would include provisions reflecting the railway owner's Train Path Policy and Train Management Guidelines but not the provisions of Costing Principles and Over-payment rules. The views of stakeholders are therefore taken into account in relation to the approval of those instruments that govern the terms of pathing and capacity management in an access agreement. On this basis, the Authority considers that consultation is appropriately provided for in the Code.

171. The Authority has not made any recommendations for amendments in relation to this Part of the Code.

Section 48 – Railway Owner must supply certain information if requested

172. The Code requires a railway owner to provide the costing information that is provided to a proponent to any other person who requests it. The Authority received one submission that commented on this issue.

173. The submission commented that railway owners should not be required to provide costing information on request to persons who cannot demonstrate that they do conduct, or have a genuine intention to conduct, business that requires access to the portion of the network to which the information relates.

174. The Authority considers that the existing confidentiality provisions provide adequate protection to a railway owner in respect of confidential information provided to the proponent. Railway owners have demonstrated an understanding of this protection by limiting the level of detail provided to proponents, such that confidential information is not able to be made public as a result of this section.

175. The Authority has not made any recommendations for amendments in relation to this issue.

Clause 7A Schedule 4 – Apportionment of costs of extension or expansion

176. The Code requires that the costs of extensions and expansions are shared between all entities that will use the expanded route, based on their usage and the economic benefit that they are expected to derive from this use. The Authority received one submission from a railway owner that commented on this issue.

177. This submission commented that the Code was not clear on how costs of extensions or expansions should be shared. The railway owner commented that the Code does not indicate (a) how the allocation of economic benefits should translate into a specific tariff apportionment; or (b) whether costs referred to total, incremental, operating or capital costs.

178. The Authority considers the form of words used in that clause anticipates the application of standard commercial principles and that further prescription in clause 7A of Schedule 4 is not warranted. The Authority considers that if a railway owner wishes to establish a template for the application of these principles then it may propose a method of allocating costs in accordance with clause 7A, by providing details of that method in its costing principles.

179. The Authority has not made any recommendations for amendments in relation to this issue.

Invitation to make submissions

Interested parties are invited to make submissions on this draft report by **4:00 pm (WST) Friday, 23 October 2015** via:

Email address: publicsubmissions@erawa.com.au

Postal address: PO Box 8469, PERTH BC WA 6849

Office address: Level 4, Albert Facey House, 469 Wellington Street, Perth WA 6000

Fax: 61 8 6557 7999

CONFIDENTIALITY

In general, all submissions from interested parties will be treated as being in the public domain and placed on the Authority's website. Where an interested party wishes to make a submission in confidence, it should clearly indicate the parts of the submission for which confidentiality is claimed, and specify in reasonable detail the basis for the claim.

The publication of a submission on the Authority's website shall not be taken as indicating that the Authority has knowledge either actual or constructive of the contents of a particular submission and, in particular, whether the submission in whole or part contains information of a confidential nature and no duty of confidence will arise for the Authority.

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INTRODUCTION

180. The Economic Regulation Authority (**Authority**) has prepared this Draft Report to assist interested parties in making further submissions on the Authority's review of the *Railways (Access) Code 2000* (**Code**).

181. The review is being undertaken pursuant to the provisions of section 12 of the *Railways (Access) Act 1998* (**Act**).

182. The Authority published an Issues Paper in February 2015 and invited submissions on matters raised in that Issues Paper and any other relevant matters. In May 2015, further submissions were invited on specific matters and matters raised in the initial submissions. All relevant comments provided in submissions have been considered in the making of this draft report.

183. A Final Report will be provided to the Treasurer following consideration of further submissions received in response to this draft report.

Background

184. The main object of the Act is to establish a rail access regime that encourages the efficient use of and investment in railway facilities by facilitating a contestable market for rail operations.

185. Part 2 of the Act provides for the establishment of the Code as subsidiary legislation. The Code contains provisions as set out under the requirements of Part 2 of the Act, including the process for the negotiation of access agreements between the railway owner and the entity seeking access, the arbitration of disputes during the course of such negotiations and the regulator's role in this process.

186. The Authority is the regulator responsible for administering the Regime.

187. The Authority is required to undertake a review of the Code on the third anniversary of its commencement and every five years thereafter.[1] The Code commenced on 1 September 2001.

188. In October 2004, the Authority commenced its first review of the Code. The Final Report of this review was provided to the Treasurer on 23 September 2005 and, following the Treasurer's approval, it was published by the Authority on 5 December 2005.

189. Following consideration by the Government and a further round of public consultation by the Treasurer in accordance with section 10 of the Act, the Treasurer gazetted amendments to the Code on 23 June 2009.

190. In October 2009, the Authority commenced its second review of the Code. A Final Report of the review was provided to the Treasurer on 20 December 2011 and following the Treasurer's approval, the Authority published the Final Report on 7 February 2012.

[1] Section 12, Part 2 of the Act.

191. No further consultation on the recommendations of the Final Report of December 2011 has been undertaken by the Government.

Legislative Requirements

192. As noted above, the Authority is required to undertake a review of the Code on the third anniversary of its commencement and every five years thereafter.[2]

193. The Authority is required to prepare a report on the review and give it to the responsible Minister (the Treasurer) for consideration.[3] The Act does not require that any action be taken by the Government in response to the Authority's Review.

194. Copies of the Act and the Code are available on the Authority's website (www.era.wa.gov.au).

Scope of the Review

195. Part 2 of the Act sets out provisions relating to the establishment of a Code.

196. Section 4(1) of the Act states that "The Minister is to establish a Code in accordance with this Act to give effect to the Competition Principles Agreement in respect of railways to which the Code applies".

197. The primary purpose of this review of the Code is to assess the suitability of the provisions of the Code to give effect to the CPA in respect of railways to which the Code applies.[4]

198. Under the Act, a requirement of a review of the Code is to seek public comment on the effectiveness of the regime.

199. The CPA is defined in the Act as "the Competition Principles Agreement made on 11 April 1995 by the Commonwealth, the States and the Territories as in force for the time being".

200. The CPA is part of the National Competition Policy (NCP), which was formulated and signed by all Australian Governments.[5] The NCP is underpinned by three separate inter-governmental agreements:

(a) The CPA

(b) The Conduct Code Agreement

(c) The Agreement to implement the NCP and related reforms.

[2] Section 12(1) of the Act.

[3] Section 12(6) of the Act.

[4] Section 12(2) of the Act.

[5] Further information on the CPA, third party access and state based access regimes is available from the National Competition Council at http://ncc.gov.au/articleZone.asp?articleZoneID=64

201. The CPA provides a framework to allow third parties to access nationally significant infrastructure facilities that exhibit natural monopoly characteristics and cannot be duplicated economically.[6]

202. The definition under the Act means that the relevant version of the CPA made on 11 April 1995, for the purpose of the Code review, is the most recent version of the Agreement. The Authority understands that the CPA, as amended at 13 April 2007, is the most recent version.[7]

203. As noted previously, the Act requires the Authority's review of the Code to assess the suitability of the provisions of the Code to give effect to the CPA in respect of railways to which the Code applies. Therefore, under the scope of this review, the Authority can only give consideration to proposed amendments to the Code that are not inconsistent with the CPA (as amended to 13 April 2007) or with relevant provisions of the Act, including those set out under Part 2 of the Act ("Establishment of Code").

204. The sections of Part 2 of the Act that are relevant include section 4(2)(d) relating to the regulator's supervisory role, section 5 "Criteria to be considered in applying Code to particular routes", and sections 11 and 11A, which relate to consultation on amendment or replacement of the Code.

205. The Code refers to five regulatory instruments (Segregation Arrangements, Costing Principles, Train Path Policy, Train Management Guidelines, and Over-payment rules) that may provide a greater level of detail to enable implementation of specific principles contained in the Code. These instruments are able to be amended on the direction or with the agreement of the regulator.

206. Consequently, these instruments will be reviewed and where necessary refined in a separate process with key stakeholders. Comments on issues relating to regulatory instruments made during this process may inform any subsequent reviews of those instruments.

207. Nonetheless, the focus of this review is on the potential for refinements to the Code to improve the Code's ability to give effect to the CPA.

Objectives of third party access

208. The broad objective of third party access under the CPA is to encourage the efficient use of nationally significant network assets to promote competition in related markets.

209. The provisions of the CPA most relevant to this review are those provisions contained in Clause 6 under the heading "Access to Services Provided by Means of Significant Infrastructure Facilities".[8] Clauses 6(c), 6(e) and 6(f) are of particular relevance to this review.

210. Clause 6(c) of the CPA requires that, for an access regime to conform to the principles set out in Clause 6, it should apply to significant facilities that would not be

[6] This framework is outlined at clause 6(4) of the CPA.

[7] The amended Competition Policy Agreement document is available at http://ncp.ncc.gov.au/docs/Competition%20Principles%20Agreement,%2011%20April%201995%20as%20amended%202007.pdf

[8] See COAG Competition Principles Agreement, at: http://ncp.ncc.gov.au/docs/Competition%20Principles%20Agreement,%2011%20April%201995%20as%20amended%202007.pdf

economic to duplicate; that are necessary to permit effective competition in upstream or downstream markets; and for which safe access may be economically provided.

211. Clause 6(e) of the CPA requires that an access regime should, among other things, provide for a negotiate/arbitrate approach to access that incorporates a right to negotiate access and dispute resolution provisions. Clause 6(e) requires that the owners of facilities promote access and do not hinder access and that accounting separation applies to those elements of a business that are covered by the regime.

212. Clause 6(f) requires that an access regime incorporates the following principles:

- An object clause that promotes the economically efficient use of, operation and investment in significant infrastructure thereby promoting effective competition in upstream or downstream markets.
- Access prices that meet the efficient costs of providing access, allow multi-part pricing and price discrimination, do not allow a vertically integrated operator to discriminate in favour of its downstream operations, and provide incentives to reduce costs.

SUBMISSIONS RECEIVED

213. On 20 February 2015, the Authority published an Issues Paper and invited submissions in response to the Issues Paper. Submissions were invited on matters raised in the Issues Paper or on any other issue.

214. Eleven submissions were received in response to the Authority's Issues Paper. These were received from:

- Asciano
- Association of Mining and Exploration Companies (AMEC)
- Aurizon
- Brockman Mining Australia (Brockman)
- Brookfield Rail (BR)
- Cooperative Bulk Handling (CBH)
- Department of Transport (DOT)
- Professor Michael Dillooly
- Roy Hill Infrastructure (Roy Hill)
- The Pilbara Infrastructure (TPI)
- Western Australian Farmers Federation (WAFF)

215. These initial submissions were published on the Authority's website on 20 April 2015.

216. On 7 May 2015, the Authority invited further submissions on the issues of prescriptiveness of the regime and the valuation method prescribed in the Code. In particular, the Authority called for responses to comments that were made in the first round of submissions on these specific issues.

217. Ten submissions were received in response to the invitation for further submissions. These were received from:

- Asciano
- Aurizon
- Brookfield Rail (BR)
- Michael Carmody
- Bill Cowan

- Department of Transport (DOT)
- Roy Hill Infrastructure (Roy Hill)
- The Pilbara Infrastructure (TPI)
- Lindsay Tuckwell
- Wheatbelt Railway Retention Alliance (WRRA)

218. These further submissions were published on the Authority's website on 10 July 2015.

219. Relevant matters raised in submissions are detailed in the following sections of this report:

> GENERAL MATTERS – matters that do not relate to any specific provision of the Code, but to the regime overall, including provisions of the Act.
>
> MATTERS RAISED IN THE ISSUES PAPER – matters relating to specific provisions of the Code, as raised in the Issues Paper.
>
> FURTHER SECTION-SPECIFIC MATTERS - matters relating to specific provisions of the Code, which were not raised in the Issues Paper.

220. Comments in submissions that the Authority has been unable to consider in the context of this review are referred to in an Appendix to this document, from paragraph 553.

GENERAL MATTERS

221. This section refers to general comments made in submissions that are not identifiable as pertaining to a particular section of the Code, and may relate generally to the administration, enforcement or objectives of the Code.

222. Comments in submissions that refer to provisions of the Act are included in this section. The Authority sought further comments on the prescriptiveness of the WA regime, and these comments are also summarised in this section. The Authority considers all issues identified in this section to be relevant to the review.

Object of Railways Access Regime

Submissions

223. Aurizon submitted that this review needs to be focussed on achieving the object of the Act, which is to promote effective competition in the above-rail market (initial submission page 3).

224. Aurizon commented that the focus of the WA rail access regime should be limited to its original legislative intent of promoting competition in the rail haulage market (further submission page 2), and that the WA rail access regime is unlikely to be the appropriate instrument to achieve the objective of efficient multi-user supply chains. Aurizon commented that an expansion of the scope of the regime to address upstream and downstream markets would require a more detailed consideration and review of the objectives of the regime.

225. BR submitted that the object of the WA Railways Access Regime is focussed on the promotion of efficiency, and that this overall objective directly reflects the equivalent objective of access to third party infrastructure as established in the CPA (attachment to further submission page 5). BR submitted that there are different elements to efficiency, and that care must be taken not to promote one aspect of efficiency at the expense of another, for example promoting transactional efficiency at the expense of allocative efficiency.

226. CBH submitted that the object of the Act does not recognise upstream or downstream markets that rely on the rail network (initial submission page 57). CBH submitted that CPA clause 6(5)(a) requires an effective regime to have an objects clause that clearly states that the purpose of access regulation is to promote economic efficiency in the operation, use of and investment in significant infrastructure, thereby promoting competition in upstream or downstream markets. CBH submitted that this reflects the underlying goal of access regulation under the CPA. CBH submitted that the object of the Act is relevant to this review of the Code to the extent that it informs the application and interpretation of the Code and whether the CPA objectives have been achieved.

227. CBH submitted that the NCC made note of this deficiency in its final recommendation on the certification of the WA Rail Access Regime.

228. CBH submitted that the regime should acknowledge in its objects, the broader range of markets to which the regime is directed. CBH submitted that the regime is currently not promoting competition in the WA grain market. CBH submitted that the Act should acknowledge the grains market in its objects, either directly, or indirectly as a downstream market.

Authority considerations

229. The Authority considers that to the extent that the object of the Act reflects the requirements in the CPA, and as the Code is legislation subsidiary to the Act, then it is appropriate to address the object of the Act as part of this review.

230. In relation to Aurizon's submission that this review needs to be focussed on achieving the object of the Act, the Authority considers that the requirements of the Review are outlined in section 12(2) of the Act and this section expressly requires that:

> the purpose of the review is to assess the suitability of the provisions of the Code to give effect to the Competition Principles Agreement in respect of railways to which the Code applies.

231. In relation to CBH's assertion that the NCC has made note of a 'deficiency' in relation to the object clause in the Act, the Authority notes that the NCC considers the object clause in the Act is "sufficient to address the certification requirement that the regime include an appropriate objects clause".[9]

232. The Authority agrees with CBH's submission that the regime should acknowledge related markets. However, the Authority does not consider that the grains market should be specifically identified, in this respect, or any other related market.

[9] NCC Final Recommendation of the certification of the WA Rail Access Regime dated 13 December 2010, paragraph 9.16.

233. The Authority considers that the market for rail operations (the 'above-rail' market) is a downstream market, and is appropriately acknowledged in the Act.

Scope of Railway Regulation

Submissions

234. Roy Hill submitted that all decisions of the ERA and any arbitrator should take into account the whole supply chain (initial submission page 3). Roy Hill referred to an Australian Competition Tribunal finding that end effects, in particular operations at the port and mine terminal facilities, cannot be ignored in assessing rail capacity for purposes of third party access. Roy Hill submitted that statements made by the Authority in relation to the finalisation of Part 5 instruments for TPI indicated that these end effects would not be taken into account.

Authority considerations

235. The Authority notes, in relation to the Roy Hill submission, that the Authority has allowed for recognition of the operation of TPI's port and mine facilities at terminal ends of its railway by allowing "available capacity" to be defined as "capacity that is not committed capacity" and for a distinction to be made between train paths as either "cyclic traffics" or "timetabled traffics".

236. These classifications of train paths allow for a number of cycles of train paths associated with loading requirements for each ship, and give priority to loaded trains.[10]

237. The object of the regime includes "to facilitate a contestable market for rail operations". The Authority considers that supply chain considerations relate to railway operations (above-rail) and activities that interface with railway operations. 'Railway infrastructure' defined in the Code, and subject to the regulations in the Code, is restricted to facilities necessary for the provision of below-rail services. Owners of below-rail facilities, or segregated below-rail parts of vertically integrated businesses do not for the purpose of the Code have "supply-chain" considerations.

Prescriptiveness of the Regime

Submissions

238. Asciano submitted that a move towards a more prescriptive regulatory approach (such as a reference tariff scheme) would likely result in more access seekers seeking access under the Code (initial submission page 7). Asciano submitted that cost certainty and transparency are not provided for under the current 'negotiate-arbitrate' floor and ceiling price approach. Asciano submitted that ideally the Code

[10] This recognition of above rail priorities is best explained in the Authority's Draft Determination on TPI's Train Path Policy (March 2009) pp. 13-18 https://www.erawa.com.au/cproot/7440/2/20090327%20The%20Pilbara%20Infrastructure%20Pty%20Ltd%20-%20Draft%20Determination%20on%20the%20Proposed%20(Revised)%20Train%20Path%20Policy.pdf The Authority notes that the view expressed by Hancock Prospecting Pty Ltd in relation to consideration of supply chain priorities for TPI's train path policy does not align with the view expressed by Roy Hill Infrastructure for this current review

should provide for ERA-approved access agreements and ERA approved access tariffs for reference services.

239. Asciano submitted that if a negotiate-arbitrate approach must be used then, as a minimum, the Code should require access providers to provide sufficient cost information to facilitate more balanced access negotiations and more efficient access pricing.

240. Aurizon submitted that it supports the light-handed approach of the WA regime and that it is closer than any other Australian rail regime to encouraging commercial negotiation (initial submission page 6). Aurizon submitted that a more prescriptive approach would reduce the flexibility of both parties in negotiation (initial submission page 20). Aurizon submitted that a reference tariff would be difficult to implement given the range of commodities transported and service types for which reference tariffs would need to be defined.

241. Aurizon also submitted that the current light-handed regime could be improved by expanding the information requirements in clause 9(1), including full disclosure of the costs of providing access. Aurizon submitted that the regime could also be improved by the regulator publishing non-binding guidelines, which would be preferable to moving to a more prescriptive approach.

242. In its further submission, Aurizon provided clarification that, in its view, the ERA should avoid unnecessary prescription and detail that can limit the ability of participants to flexibly respond to the needs of the market (page 1). Aurizon commented that negotiations between monopoly owners of components of supply chains should involve the exercise of countervailing market power and the role of regulation should be limited (further submission page 2).

243. On the matter of its proposal for non-binding pricing guidelines, Aurizon commented (further submission page 3) that the allocation of common, or sunk, costs above incremental costs requires consideration of a broad range of factors, including:

- Next Best Alternative. It is reasonable that prices should not exceed the price of a substitute service.
- Incentives for efficiency and barriers to entry. Prices should not discourage innovation and productivity and not lock the industry into continued utilization of sunk legacy assets and declining productivity.
- Hierarchy of Replacement Costs. Prices should reflect the economic cost of entry.
- Congestion and Opportunity Costs. An efficient below rail price should reflect the lower of (a) the incremental cost of alleviating constraints and (b) the highest contributing access charge if expansion is not feasible.
- Past prices and changes in circumstances. On the basis that any previous negotiated price was efficient, this would be an appropriate reference price for access.
- Promoting efficiency in rail haulage. If an operator was able to propose a reduced number of paths to achieve the same haulage task, a service provider might seek to increase access charges to capture the value of efficiency gains made by the operator. An arbitrated price should provide incentives to reduce costs and improve productivity.

- Competitiveness of the supply chain. Efficient below rail prices should be representative of relative proportions of costs and risks within the supply chain.

244. Brockman indicated that it did not have a definitive view on whether a reference tariff approach should be adopted in place of the current floor and ceiling approach (initial submission page 13). Brockman submitted that a reference tariff approach is widely used in other Australian regimes and has a number of advantages, including (a) decreased time and cost in negotiations (b) increased transparency and certainty, and (c) better replicates the outcomes of competitive markets. Brockman submitted that it favoured the development of regulator-approved standard access agreements (initial submission page 9).

245. BR submitted that there is a strong emphasis on flexibility and negotiation in clauses 6(4)(a)-(f) of the CPA (initial submission page 6). BR submitted that a more prescriptive approach would diminish the railway owner's ability to take into account the 'requirements of the persons seeking access', and that the presence of a reference tariff is not conducive to providing access 'on the basis of terms and conditions agreed between the owner of the facility and the person seeking access'.

246. BR submitted that the 2006 Competition and Infrastructure Reform Agreement (CIRA) between Australian governments included a commitment to implement a consistent national system of rail regulation (initial submission page 7). BR submitted that the ACCC commenced an investigation on the matter, and that it became apparent that the proposal was not appropriate given the diversity of rail networks in Australia.[11]

247. BR submitted that the adoption of a reference tariff approach would require substantial revision of much of the Code. BR submitted that the segregation arrangements in the WA regime are already more prescriptive than in other regimes and that many of the features of the ARTC and Aurizon access undertakings are already present in the Part 5 instruments required by the WA Code (initial submission page 8).

248. Further to the above comments, BR submitted that comments made in other submissions implied that a lack of regulatory oversight in the price-setting process is ineffective in giving effect to the objectives of the CPA (further submission page 17). BR submitted that, to the contrary, regulator involvement in the price setting process would diminish the efficiency of the negotiation process, and that experience in other regulatory regimes shows that this is a time consuming, complex and costly process.

249. BR submitted that a process of setting reference tariffs effectively 'outsources' the work of arriving at an appropriate price to the regulator. BR submitted that compared to well-resourced interested parties negotiating to arrive at a mutually acceptable price, it is not effective to rely on a third party with limited resources and no stake in the outcome to undertake this role.

250. BR also submitted that the range of tasks and operating parameters on BR's network, means that a large number of 'reference tariffs' would need to be developed by the regulator in order to provide the 'price guidance' suggested in some submissions (further submission page 18). BR also commented that the development of reference tariffs changes the time when the assessment of an appropriate price is made, such that the regulator must establish prices outside the context of a specific negotiation,

[11] BR did not cite a reference in relation to the ACCC investigation

where the regulator would be even further from the commercial objectives and imperatives of the parties to the negotiation.

251. In its further submission, BR referred to comments in other submissions that the Code should address information asymmetries and imbalanced negotiations (further submission page 21). BR submitted that the Code already protects access seekers from this. BR submitted that if parties fail to agree in negotiations, then an arbitrated outcome will provide a conclusive outcome, and that the railway owner loses any advantage it may have during negotiations.

252. BR commented that other submissions claim that the railway owner has a negotiating advantage because it has much greater information about its own network than an access seeker has (further submission page 22). BR submitted that the access seeker retains knowledge of its own costs of operations as well as the economic value extracted from the use of the infrastructure, and that this bestows significant negotiation advantage on the access seeker.

253. BR commented that both parties in an access negotiation have price boundaries that limit their negotiation positions, and that the railway owner's costs boundaries are known by the access seeker in advance. BR submitted that the access seeker is not disadvantaged in negotiations without recourse to the railway owner's information simply because the railway owner knows its own business.

254. BR submitted that the Productivity Commission has indicated a preference for negotiated outcomes over prescribed regulatory outcomes (attachment to further submission page 8). BR cited reasons for this preference, including that negotiated outcomes:

- lower compliance and regulator's costs;
- reduce scope for regulatory error, and regulatory risk; and
- promote innovation and discourage gaming.

255. BR also referred to the views of the Hilmer Report, the previous Productivity Commission Chairman Gary Banks and the Export and Infrastructure Taskforce that support this position (attachment to further submission page 9).

256. BR submitted that a more prescriptive regime was investigated at the time the WA regime was implemented, and that this approach was rejected for a number of reasons consistent with those outlined above (attachment to further submission page 10).

257. BR submitted that the benefits of regulated tariffs will outweigh the costs only under certain circumstances, including where (attachment to further submission page 16):

- there is a significant number of access proposals in relation to a particular service type (that is, homogenous freight tasks). In this situation, there is less need for negotiation to meet the circumstances of a particular access seeker, and fewer reference tariffs would need to be established,
- the track condition is close to replacement condition. This is because it is likely that prices would be negotiated close to the ceiling, and the potential for regulatory error in setting a reference tariff would be lessened,
- there is less incentive for the infrastructure provider to negotiate for access to its rail network. For example, this could be due to its vertical integration into competing downstream markets.

BR stated that these circumstances do not apply to its network (attachment to further submission page 17).

258. CBH submitted that the approach in the Code to negotiating a price between the floor and ceiling does not give effect to the objects and the pricing principles of the CPA (initial submission page 20). CBH submitted that clause 6(5)(b) of the CPA aims to ensure that the access price promotes the efficient use of the railway to promote efficient competition in dependent markets, and given that the prices are determined by negotiation, it is critical that the Code also give effect to clauses 6(4)(a)-(c) of the CPA, which emphasise transparency and effective resolution of disputes. CBH submitted that these attributes are generally facilitated by procedures that are independent, transparent, consultative and that provide certainty to an access seeker.

259. CBH submitted that, in its experience, there is a lack of up-front certainty regarding pricing, and the pricing guidelines outlined in clause 13 of Schedule 4 of the Code provide only overarching obligations as to what the prices should reflect. CBH submitted that, in its experience, there is limited regulatory oversight of the price-setting process, and that this is limited to the role afforded the regulator under section 21 to provide an opinion on a price, which is not binding and for the information of the access seeker only. CBH submitted that clause 6(5)(a) requires that the regime ensures that access providers do not misuse market power, and that the lack of regulatory oversight under the Code is not suitable to address the imbalance in market power when dealing with a monopoly service provider.

260. CBH submitted that, in contrast, other access regimes involve a more transparent method of determining access price, based on the setting of reference prices (initial submission page 21). CBH provided examples where this occurs, which include the ARTC interstate Access Undertaking, the *Victorian Rail Management Act 1996*, and the *Queensland Competition Authority Act 1997.* CBH submitted that there is merit in considering a similar reference tariff approach under the WA Code.

261. CBH also submitted that since the ERA ceased regular clause 9 determinations, the reduction in cost information has placed access seekers at a distinct disadvantage. CBH submitted that a lack of recent costings is the reason that the BR/CBH determination took over six months to make. CBH submitted that there would be value in considering a reference tariff rather than upper and lower price boundaries.

262. Department of Transport (DOT) submitted that it supported a move towards reference tariffs, on the basis that the current approach results in a large range between the floor and ceiling price, which provides little assistance in facilitating an arbitration process (initial submission page 2). DOT submitted that, on the other hand, a reference tariff leaves little room for negotiation and assumes sufficient accuracy in the price, which may be unreasonable given the uncertainty of valuation (initial submission page 3).

263. Roy Hill submitted that the level of the prescriptiveness of the WA regime should be reduced (further submission page 1). Roy Hill submitted that the WA regime does not allow parties to negotiate access on commercial terms without reference to the Code (further submission page 2).

264. Roy Hill submitted that Section 4A(1)(c) of the Code is inconsistent with Section 40(2) of the Code (further submission page 3). In support of this comment, Roy Hill outlined Section 40(2) as prescribing that Part 5 instruments are binding on a railway owner,

and Section 4A(1)(c) as providing that nothing in the Code applies to negotiations outside the Code.

265. Roy Hill submitted that in the event of arbitration, the arbitrator is unable to make a ruling on the merits of a cost determination by the regulator, and that therefore the WA regime is overly prescriptive.

266. Roy Hill submitted (further submission page 4) that it:

- agrees with TPI that the adoption of reference tariffs would limit terms available for negotiation (see paragraph 267 below);
- agrees with BR that additional prescription would not improve the ability of the Code to give effect to the CPA (see paragraph 245 above); and
- endorses Aurizon's position that increases in prescription and detail are not supported as the Code is appropriate as a high level principles-based document.

267. TPI submitted that it does not support regulator-approved access agreements or reference tariffs, as these would restrict the terms available for negotiation (attachment to submission page 25, further submission page 3).

268. TPI submitted that rail access proponents are companies with professional advisors and advocates who contribute to negotiations, and that there is not an imbalance in negotiating power between railway owners and proponents (further submission page 3). TPI submitted that railway owners have far more onerous statutory obligations and responsibilities than proponents, which acts to constrain the railway owner's power in negotiation.

269. TPI submitted that increasing the prescriptiveness of the regime would increase compliance costs for both the ERA and railway owners, and would require the design of a framework to limit regulatory discretion and to ensure rigorous review and correction of regulatory error (further submission page 4). TPI commented that the associated costs would outweigh any perceived benefits relating to economic efficiency.

Authority considerations

270. The Authority has considered Asciano's submission that the current light-handed negotiate-arbitrate approach could be improved by ensuring the availability of more detailed cost information, which would result in more balanced negotiations. The Authority has also considered BR's counter arguments that, in the absence of a corresponding disclosure of proponents' supply-chain costs, further disclosure of railway owners' costs would result in less balanced negotiations.

271. The Authority considers that the appropriate level of disclosure of railway owners' costs is related to the level of prescription, and that as the level of prescription increases, so does a requirement for transparency of railway owners' costs. That is, that a requirement to disclose railway owners' cost information should increase as the scope for determining an outcome by balanced negotiation decreases.

272. The Authority has considered Aurizon's submission that non-binding guidelines should be introduced. The Authority considers the pricing guidelines provided by clause 13 of Schedule 4 to the Code provides a sufficient framework for efficient pricing. The Code also, at section 7(1)(b) requires the railway owner to provide an indicative price for access when an access seeker initially proposes access.

273. The Authority does not agree in principle with all of the guidelines proposed by Aurizon. In particular, competition with alternative services should be enabled, not mandated, by the Code and references to previous prices and supply chain cost components are not considered appropriate guidelines.

274. The Authority notes Aurizon's submission that operators' efficiency gains should not be open to appropriation by the railway owner via the pricing process. The Authority considers that consideration of efficiency gains made by operators is able to be appropriately considered in the negotiation of an agreement between the parties.

275. In relation to non-price guidelines, the Authority notes that the provisions of railway owners' Part 5 instruments reflect the sorts of conditions written into access arrangements in more prescriptive regimes, thereby providing an over-arching 'guideline'. In this respect, provisions protecting operators' efficiency gains may be made in a railway owner's Train Path Policies in response to any specific concerns expressed to the regulator by operators.

276. The Authority acknowledges BR's submission that the Productivity Commission has indicated a preference for negotiated outcomes over prescribed regulatory outcomes, and that the negotiate-arbitrate approach to regulation is the best means of giving effect the to the CPA principles 6(4)(a)-(f).

277. The Authority agrees that well-resourced parties may be better placed to determine a set of mutually beneficial outcomes than a regulator who does not have a commercial stake in the outcome.[12]

278. The Authority accepts that a negotiate-arbitrate approach trades off some 'transactional' efficiency in the interests of maximising 'negotiation' efficiency.

279. The Authority agrees with BR that the negotiate-arbitrate approach is less likely to result in outcomes approaching the 'ceiling' price, especially where above- and below-rail operations are not integrated and track condition may be variable. The Authority considers these conditions exist especially on the non-interstate routes of the freight network where freight tasks are less homogenous, and where the condition of the rail track on some routes gives more scope for negotiation between parties.

280. In relation to BR's contention that the ACCC has investigated the appropriateness of a consistent form of rail regulation across all Australian networks (paragraph 246 above), the Authority has noted that, as part of the 2006 CIRA, the WA Government agreed only that a consistent system of regulation, based on the ARTC model, should apply to nationally significant rail corridors.[13]

281. In this respect, the CIRA agreement referred specifically to the interstate rail corridor between Kalgoorlie and Perth and not to the entire WA network.[14] The CIRA agreement was to be implemented for other (intra state) corridors only on an agreed

[12] In this respect, the Authority notes that Parliament discussed the distinction between requiring tariffs to be prescribed by the regulator, and allowing prices to be negotiated between the parties, as options prior to the establishment of the Code. Hansard for 18 November 1998 recording the Second reading of the *Government Railways (Access) Bill 1998*, reports Mr Paul Omodei as saying that "the issue of posted tariffs as they are otherwise known was considered by a working group of the Western Australian Rail Advisory Council comprising government and industry representatives. There was general agreement that the industry does not want posted tariffs" (p. 3687).

[13] This was noted in the Issues Paper at paragraph 74 https://www.erawa.com.au/cproot/13352/2/Review%20of%20the%20Railways%20(Access)%20Code%202000%20-%20Issues%20Paper.pdf ,

[14] Competition Infrastructure Reform Agreement (CIRA) February 2006 paragraph 3.1.

basis depending on an assessment of costs and benefits. The implementation of the agreement in respect of the interstate route does not appear to have been made contingent on any cost benefit criterion.

282. The Authority considers that, due to the homogeneity of freight services on the interstate portion of the WA network that the Minister may give further consideration to implementing the CIRA agreement, at least as far as it applies to the rail corridor between Kalgoorlie and Perth.

283. The Authority is aware of TPI's view that the WA Rail Regime should not apply to its railway.[15] The Authority considers that consideration should also be given to implementing the 2006 CIRA agreement in respect of the TPI railway, due to homogeneity of traffic and consistent high level of track standard. The Authority considers this practical, as TPI is a vertically integrated service provider, and as prices are, therefore, more likely to be negotiated closer to the 'ceiling price'.

284. In respect of the above, the Authority has noted comments in Aurizon's submission (see paragraphs 404-406 of this report) that the GRV valuation method is better suited to 'brownfield' railways where the economic life of the railway is likely to be greater than the railway's technical life, and that the practical commercial difference between alternative valuation methods is diminished where the primary purpose of the railway is to service its own operations.

285. From a WA government perspective, implementation of the CIRA agreement may simply require removing the affected routes from Schedule 1 of the Code, thereby potentially opening them up to declaration or to the provision of an access undertaking equivalent to the ARTC access undertaking. The ACCC administers the ARTC access undertaking.

286. The Authority agrees with BR's submission that transforming the Western Australian Rail Access Regime into a more prescriptive regulatory approach would require the Code to be substantially revised, and involve considerable cost and regulatory disruption.

287. In relation to CBH's submission referring to the merits of regular 'clause 9' determinations, the Authority notes that these determinations have not been related to specific access proposals.

288. The Authority has ceased making these regular determinations, as they are considered to be no longer consistent with the requirements of clause 9, which provides for determinations to be made by the regulator if it is considered "likely that a proposal will be made in respect of a route".

289. The Authority does not agree that a lack of recent costings is the reason that the BR/CBH determination took over six months to make. The Authority notes that the number of route sections subject to CBH's recent proposal were far greater than the number of route sections for which previous 'clause 9' determinations were provided. The Authority notes that there were other significant factors impacting on the progress of CBH's access proposal.

290. The Authority does not agree with Roy Hill's submission that the WA regime does not allow parties to negotiate access without reference to the Code. In particular, Section 4A is titled "Parties have option to negotiate outside this Code".

[15] See paragraphs 563 to 566

291. The Authority does not agree with Roy Hill's comment that Section 4A(1)(c) of the Code is inconsistent with Section 40(2) of the Code. Section 40(2) prescribes that Part 5 instruments are binding on a railway owner. That is, a railway owner must observe its regulatory instruments in relation to negotiations inside the Code. Section 4A(1)(c) provides that nothing in the Code applies to negotiations outside the Code.

292. The Authority does not agree with Roy Hill's submission that the absence of a process for merits review indicates that the regime is overly prescriptive. The Authority considers that the lack of prescription in the regime diminishes the requirement for a merits review process.

Merits Review

Submissions

293. BR submitted that merits review of the regulator's decisions should be stipulated (initial submission page 15). BR submitted that it is not enough to argue, as the ERA did in its second review of the Code, that the regulator's decisions "only establish frameworks", as frameworks must also be correctly and fairly determined. BR submitted that as the Part 5 instruments that impact on the railway owner's day to day operations are determined by the regulator, it is reasonable that the railway owner has recourse to merits review if it believes the regulator's discretion was unreasonable.

294. CBH submitted that it may be appropriate for merits review to apply to arbitrators decisions (such as on pricing and service standards), especially where there is limited regulatory intervention, but significant consequences (initial submission page 38). CBH cited a list of issues suggested by the NCC that would inform a decision on whether the need for merits review is appropriate. These issues are:

- The likely complexity and extent of regulatory intervention.
- The potential impact of regulation on property rights and values.
- The risk of gaming of processes by participants.
- The need to balance potential delays to access rights against the need to protect the rights of affected parties.

295. Roy Hill submitted "that the Code must be amended to deprive the ERA of the ability to seek to protect its erroneous decisions on the basis that the decisions are only subject to a very limited narrow form of review" (initial submission page 2).

296. TPI submitted that the importance of merits reviews is heightened where the regulator has a high degree of discretion, and that discretion is higher in less prescriptive regimes (initial submission page 31). TPI submitted that there is a strong case that merits review should apply to decisions made by the ERA under the Code.

Authority considerations

297. The Authority has previously recommended that a formal process for merits review would not provide reassurances to railway owners or access seekers in the context of a light handed regulatory regime, where the role of the regulator in establishing an efficient price is limited, and that role is undertaken by the parties in negotiation or by the arbitrator.

298. The Authority considers that, if the regime were more prescriptive, and if the role of the regulator was to determine the efficient price, then merits review processes may be warranted.

299. The Authority has noted TPI's submission to the effect that the importance of a merits review is heightened in less prescriptive regimes. The Authority does not agree with that assertion. The Authority does not agree with Roy Hill's view that the absence of a merits review process has resulted in the Authority seeking to "protect its erroneous decisions".

300. The Authority has referred to a recent judicial review of an Authority determination by the WA Supreme Court. The Authority considers that this is the appropriate recourse to review by parties in a light-handed regime.

Enforcement of Railways Owners obligations

Submissions

301. Brockman submitted that enforcement of the Code can be improved, and that the obligation of the Authority to monitor and enforce the Code should go beyond the regulator's statutory functions (initial submission page 7). Brockman submitted that clarification is required to ensure that the Authority's existing responsibilities to monitor and enforce the Code are broad and actioned. Brockman submitted that it continues to endure the consequences (in terms of cost and significant delay to access) of the Authority's unwillingness to monitor and enforce the Code.

302. CBH submitted that a tighter enforcement regime is required so that parties do not have to resort to court proceedings or arbitration to enforce Part 2 and 3 obligations (initial submission page 51). CBH submitted that the Code should include an enforcement regime, and that the ERA should have greater powers, as common in other regimes,[16] to enforce the regime on behalf of access seekers.

Authority considerations

303. The Authority considers that access seekers are as well-placed as the regulator to prosecute any failure on the part of railway owners to meet their obligations under the Code. The Code explicitly gives access seekers their own rights to access injunctive relief, which enables the regulator to remain impartial in inter-party disputes.

304. The Authority considers that its own power of injunctive relief is a last resort where the railway owner may be in default of its obligations in some respect and where there is no extant access proposal in the course of resolution.

[16] CBH cited (on page 53 of its initial submission) the South Australian Rail Access Regime, the Rail Management Act 1996 (Vic) and the National Gas Law as regimes which allow for the regulator to enforce penalty provisions on behalf of the access seeker.

Segregation Arrangements

Submissions

305. Aurizon submitted that the scope of the above-rail market needs to be appropriately defined to recognise the range of factors that participants compete on, which is not just the provision of above-rail services, but also (for example) the design and construction of rolling stock (initial submission page 17).

306. Brockman submitted that the Code should expand on Division 3 of the Act (segregation) to include fairness in the allocation of train paths, that ring fencing is not effective or enforced, and that enforcement is required (initial submission page 11).

307. Roy Hill submitted that the existing segregation arrangements go well beyond the requirements of the CPA for separate accounting arrangements and that this results in the railway owner incurring unnecessary costs and inefficiencies (initial submission page 4).

Authority considerations

308. The Authority notes, in relation to the Aurizon submission, that railway owners are required to segregate their access functions from their non-access functions. "Access-related functions" is defined at section 24 of the Act to mean "the functions involved in arranging the provision of access to railway infrastructure under the Code". "Non-access functions" therefore includes all other functions, including arranging the provision of access to infrastructure outside of the Code.

309. In relation to Brockman's submission, the Authority notes that the requirements of the Act in relation to segregation includes an obligation to not unfairly discriminate between access seekers or users (section 33), and that the Code requires (at Section 16(2)) that railway owners must not unfairly discriminate between operators in the allocation of train paths.

310. In relation to enforcement, the Authority has also noted the powers conferred by the Code on access seekers to seek legal injunction for non-compliance by railway owners.

311. In relation to Roy Hill's assertion, that the requirements for segregation arrangements in the WA Rail Access Regime go beyond the requirements of the CPA, the Authority notes that equivalent provisions are included in the ARTC and Aurizon Access Arrangements, as part of their Access Undertakings. In the same way, stand-alone Train Path and Capacity Management policies are not a feature of those regimes, but are included as components of the Access Undertakings approved by those regulators.

Prohibitions on hindering or preventing access

Submissions

312. Brockman submitted that the Code should expand on the prohibition of hindrance, as outlined in section 34A of the Act, due to the scope for railway owners to cause unnecessary delays (initial submission page 6). Brockman submitted that the Code

should clarify conduct that would constitute 'hindering or preventing access' for purposes of 34A of the Act, which would include (a) repeated failure to comply with obligations to provide information and (b) any conduct which has the effect of repeatedly and unnecessarily delaying an access proposal.

Authority considerations

313. In relation to Brockman's submission, the Authority considers that "repeated failure to comply with obligations to provide information" and "any conduct which has the effect of repeatedly and unnecessarily delaying an access proposal" are clearly conducts that hinder the making of an agreement, and that the provisions of section 34A of the Act would not be improved by the addition of these words.

MATTERS RAISED IN THE ISSUES PAPER

314. Comments were sought by the Authority in response to issues outlined in the Issues Paper, which related to particular sections of the Code. Relevant comments from interested parties are summarised under headings that refer to these sections.

315. Further comments received from interested parties that do not correspond to these headings, or which are more general in nature, are summarised in the sections headed "General matters" and "Further section-specific matters".

Section 8(4) and 8(5) - when can an extension and expansion be proposed?

Submissions

316. Asciano submitted that an extension or expansion should be able to be proposed at any time after the making of a proposal (initial submission page 8). Asciano submitted that the extent of any requirement for an extension or expansion may not be clear at the time of the proposal, and the determination of any requirement may require exchanges of information subsequent to the proposal.

317. Aurizon submitted that an access proposal should not be invalidated on the basis that the proponent has not identified any investment required to accommodate its proposal, or that the railway owner does not agree with the proponent's proposed investment (initial submission page 18). Aurizon noted that in other jurisdictions, the railway owner is responsible for identifying any required investment, and for advising the proponent accordingly.

318. Brockman submitted that section 8 of the Code be amended to clarify that a proponent may amend an access proposal to include extensions and expansions, including in circumstances where an arbitrator determines that there is no capacity on the current configuration (initial submission page 9). Brockman submitted that the Code should contain a general provision allowing amendments to be made to any aspect of a proposal after it has been made.

319. Brookfield Rail submitted that, to the extent that section 8 may be ambiguous, it should be clarified (initial submission page 16). In this regard, Brookfield Rail noted that sections 14 and 15 exist to assess the financial, managerial and operational capability of the proponent, and that these functions exist as a threshold for

negotiations. Brookfield Rail also submitted that, as section 8(5) allows an extension/expansion to be proposed in the course of negotiations, that section 8(5) should be amended to allow the railway owner to re-enliven sections 14 and 15 (and, in turn, sections 18 and 19) in the event that an extension/expansion is proposed in the course of negotiations, so that the railway owner can again require the proponent to demonstrate capability under sections 14 and 15.

320. CBH submitted that the meaning of section 8(4) and 8(5) should be clarified such that there is certainty that a proponent can propose an extension or expansion at any time after making a proposal (initial submission page 30).

321. TPI submitted that sections 10, 13, 14 and 15 of the Code do not (a) prevent an access seeker from proposing an extension or expansion during the course of negotiations, or (b) compel a railway owner to negotiate until the criteria provided by sections 14 and 15 have been met (attachment to submission page 24). Therefore, if both parties wish to enter into negotiations, sections 8(5) and 10 of the Code allows for them to commence those negotiations prior to an extension or expansion being proposed. TPI submitted that this provides an appropriate allocation of rights and responsibilities.

Authority considerations

322. As noted in its decision required by section 10 of the Code in relation to Brockman Iron's proposal to access TPI's railway (page 5), the Authority is of the view that the failure to specify an extension or expansion in an access proposal cannot invalidate an access proposal.

323. The Authority does not consider that a railway owner's requirements under section 14 and 15 would need to be re-enlivened unless the proponent has sought to satisfy those requirements prior to proposing an extension or expansion. The Authority considers the likelihood of this to be minimal. Further, the Authority considers that the railway owner is able to stipulate in its section 14 and 15 requirements that the proponent's satisfaction of those requirements would need to be re-examined if an extension is proposed subsequent to the proponent meeting those requirements.

324. In relation to Brockman's submission that the Code should explicitly allow for a proposal to be amended at any time, the Authority considers that an amendment of a proposal to incorporate an extension is not required, as the Code contemplates the proposal for access to existing infrastructure as separate from any expansion proposal, as the Code requires costs to be determined in respect of existing infrastructure.

325. The Authority is of the view that the Code does not require amendment to clarify section 8(5), which clearly states that:

> The fact that an extension or expansion is not specified in a proposal as mentioned in subsection 4 does not prevent the proposal of such an extension or expansion being made in the course of negotiations under Part 3 on the grounds that such an extension or expansion would be necessary to accommodate the proposed rail operations.

Section 10 - when is section 10 relevant?

Submissions

326. Asciano submitted that the intent of this section should be clarified, as network expansion is a normal option to address capacity constraints (initial submission page 8).

327. Aurizon submitted that the intent and meaning of section 10 should be clarified, including the implications of the regulator not approving the proposed access (initial submission page 15). Aurizon suggested that section 10 could be revised to make it clear that the section could not be invoked if it were economically efficient to expand the network.

328. Aurizon submitted that guidelines should be made that stipulate the factors that the regulator must consider in making a decision under section 10, and clarify the term "other entities" (being other operators who might be excluded if access is agreed), as it is currently not clear whether these entities even need to exist, or be likely to emerge in the future.

329. Brockman submitted that the intention and meaning of section 10 should be clarified (initial submission page 10).

330. BR submitted that section 10 appears to be aimed at ensuring that scarce capacity is not contracted without potential access seekers having an opportunity to gain access, and therefore is aimed at ensuring the allocation of scarce capacity to its highest value use (initial submission page 17).

331. BR noted that other jurisdictions do not address this issue, and rely on the commercial objectives of the infrastructure provider to ensure capacity is allocated to its highest value use. BR also noted that section 10 was written into the Code prior to the 2009 amendments, which introduced provisions for extensions and expansions, and that section 10 does not contemplate the implications of the regulator not approving the proposed access.

332. BR submitted that section 10 should be removed from the Code, as the objectives of the section can be achieved without the involvement of the regulator.

333. TPI submitted that the wording of section 10 does not place any onus on the railway owner to seek approval from the regulator to negotiate, only to advise the regulator of its opinion if it considers that an access proposal may in effect preclude other entities from access to that infrastructure (attachment to submission page 23).

334. TPI submitted that the fact that an extension or expansion may accommodate a proposal does not necessarily result in the expanded capacity becoming an unlimited resource, and that the regulator should be able to assess whether or not the proposed access is allocating limited capacity to its highest value use.

335. TPI submitted that the meaning and intent of section 10 should be clarified so to prevent any forced negotiation that may result in an inefficient allocation of network capacity.

Authority considerations

336. The Authority has considered TPI's submission that section 10 does not require the railway owner to seek approval from the regulator to negotiate, but has noted that section 10 requires that negotiations on the proposal must not be entered into without the approval of the regulator, if the railway owner considers that other entities may be precluded from access.

337. The Authority has considered BR's submission that provision for the Regulator to take a position on the relative value merits of a proposal is not included in other jurisdictions, and that section 10 was written into the Code prior to introduction of provisions for extensions and expansions in 2009.

338. The Authority considers that section 10 should be removed from the Code, as the objectives of the section can be achieved without the involvement of the regulator.

Sections 14 & 15 – Can a railway owner challenge the validity of a proposal prior to receiving the required information from the proponent?

Submissions

339. Asciano submitted that a railway owner should not be able to challenge the validity of a proposal before it has received any information it has required to be provided under sections 14 and 15 (initial submission page 8). Asciano submitted that if a railway owner seeks information then it should wait for the information and then consider it before challenging the validity of a proposal.

340. Aurizon submitted further that, in order to meet the objectives of the CPA, expansion investment must be the most efficient solution (initial submission page 19). Aurizon noted that the Code makes no reference to the efficiency of investment solutions, and suggested that the Code might be amended to require the railway owner to demonstrate that extension and expansion solutions offered in order to meet proponents' requirements are the most efficient solution available.

341. Aurizon submitted that the proponent should be liable for all expenses associated with expansion studies and that, in order for the proponent to meet the requirements of section 15(2) – which entitles the railway owner to require that the proponent provide an assessment that any proposed expansion is viable - the railway owner should be obliged to provide all necessary information to the proponent to undertake that assessment (initial submission page 19).

342. Aurizon submitted a general view - relating to this issue - that the negotiation process is time consuming and in favour of the railway owner, with a number of triggers for dispute by the railway owner, which could also serve to stall the process (initial submission page 26). Aurizon submitted that a dispute should only be able to be triggered once all of the information has been provided by the access seeker.

343. Brockman submitted that the definition of 'necessary financial resources' and 'capacity' should be clarified in sections 14 and 15 (initial submission page 10). In relation to financial capacity, Brockman submitted that the threshold for any such objective test should be low, as an access seeker is not liable to commit financially until (and only if) arbitration occurs. Brockman submitted that a high threshold would

curb the effectiveness of the Code by unfairly discriminating against access seekers that are in the process of establishing project viability.

344. Brockman submitted that the capacity test in section 15 should be clarified such that the assessment of capacity, based on the information provided by a railway owner under sections 6 and 7, should be prescriptively defined and subject to third party audit (initial submission page 11).

345. BR submitted that sections 14 and 15 should be clarified to make it clear that they function as threshold issues for negotiation only, and not to the validity of an access proposal (initial submission page 18). BR submitted that a railway owner should be able to challenge the validity of an access proposal at any time according to whether or not the proponent has met the information requirements of section 8.

346. Roy Hill submitted that section 8 should be amended such that an access seeker cannot make a valid proposal until the requirements of section 14 are met (initial submission page 5). Roy Hill noted that existing access undertakings under Part IIIA provisions allow for the railway owner to require an access seeker to establish appropriate prudential requirements at any time before or during negotiations.

347. TPI submitted that sections 14 and 15 are, and should be treated as, issues that the proponent should be required to address at the date of making the proposal, or shortly thereafter (initial submission page 3). TPI further submitted that sections 14 and 15 should prescribe a time limit for the satisfaction of the railway owner's section 14 and 15 requirements. TPI noted that delays (of 12 months or more) in the meeting of these requirements creates uncertainty for the railway owner and is not consistent with the economic objectives of the Code or the CPA (initial submission page 4). TPI referred to unmanageable access seeker credit risk that might compromise the owner's legitimate business interests and the interests of all persons using the facility (attachment to initial submission page 22).

Authority considerations

348. The Authority considers the validity of a proposal is established by the proponent meeting the requirements of section 8. The Authority notes that the railway owner is not required to indicate its requirements under sections 14 and 15 until after it has received a valid proposal.

349. The Authority therefore considers the Code is clear that sections 14 and 15 act as threshold issues for negotiation only, and do not stand as grounds for claiming that an access proposal is invalid.

350. The Authority considers that, in addition to the capacity information required to be provided to the access seeker at section 7, the Code should require the railway owner to provide any required information necessary for the proponent to undertake a capacity assessment, and that the proponent must cover any costs incurred by the railway owner in doing so.

351. The Authority also considers that criteria could be established in the Code for the satisfaction of the railway owner's requirements in these sections, including prescribing the assessment of capacity in a way consistent with a railway owner's obligation to provide capacity information in sections 6 and 7.

352. The Authority agrees with TPI that timeframes should be established in the Code for the satisfaction of the railway owner's requirements in these sections.

Section 16 – What does the term "unfairly discriminate" mean?

Submissions

353. Asciano submitted that the term 'unfairly discriminate' should be clarified (page 8). Asciano notes that CPA clause 6(f) allows some discrimination between access seekers if their circumstances are not similar or if economic efficiency is aided by price discrimination (initial submission page 9).

354. Aurizon submitted that the duty to not unfairly discriminate should apply to all parts of the Code and not just Part 3 (Negotiations) (initial submission page 15). Aurizon submitted that the duty to not unfairly discriminate should apply to Part 5 Instruments and should apply regardless of whether the arrangement is inside or outside the Code.

355. Aurizon submitted that 'unfair discrimination' should be defined (initial submission page 16). Aurizon submitted that there should be a defined basis for unfair discrimination such that the onus is on the aggrieved party to show a reasonable foundation for a claim of unfair discrimination. Aurizon proposed that there be two key tests to demonstrate that unfair discrimination has occurred, which are: (a) it has a material adverse effect on an access seeker; and (b) it has a substantial impact on competition in the relevant market.

356. Aurizon further submitted that the regulator should have access to all commercial arrangements to ensure that discrimination is not occurring.

357. Brockman submitted that clear guidance should be provided as to what the objective meaning of 'unfair discrimination' is (initial submission page 11). Brockman also submitted that the section 7 provisions allowing an access seeker to request information on capacity should be read together with section 16(2).

358. BR submitted that section 16 should be amended to provide a non-exclusive list of 'unfair discrimination' that the railway owner should not engage in (initial submission page 19). BR does not agree with recommendation 7 of the second review which suggested that a non-exclusive list of examples of 'fair discrimination' be added to section 16.

359. BR submitted that the inclusion of examples of 'unfair discrimination' would improve the ability of the Code to give effect to sections 6(4)(e) and 6(4)(f) of the CPA, and that inclusion of a list of 'fair discrimination' would reduce the flexibility of the Code and its ability to give effect to section 6(4)(e) of the CPA.

360. Roy Hill submitted that the Code should provide for the types of instances and reasons that would give rise to permissible differential treatment (initial submission page 5). Roy Hill referred to the definition of "discriminate" in regulation 23 of the *Gas Transmission Regulations 1994* (WA) (now repealed) for an approach to the issue of permissible discrimination.

361. TPI noted that the CPA section 6(e)(9) provides a list of considerations that a dispute resolution body should take into account when deciding on terms and conditions for access (attachment to initial submission page 19). TPI submitted that, in order to give effect to the CPA, this list should provide the basis for a list of 'permissible discrimination' by a railway owner under the Code.

362. TPI submitted that reasonable discrimination should be construed in light of the commercial risks that the infrastructure owner incurred in the development of the infrastructure, and would include the ability to discriminate between access seekers according to (initial submission page 20):

- their contribution to the railway owner's capital costs and risks;
- their contribution to the railway owner's operations and maintenance costs and risks;
- credit risk;
- the amount and quality of security offered to the railway owner;
- any loss of expansion option value resulting from proposed access;
- any supply chain disruption risk; and
- the extent of any cross subsidy between existing users and new users

363. TPI also referred to the suggested list of 'permissible discrimination' provided by Oakajee Port and Rail in their 2010 submission to the second review of the Code, as being appropriate considerations.

Authority considerations

364. In relation to the Aurizon submission that the duty to not unfairly discriminate should apply to Part 5 Instruments, the Authority notes that section 16(2) currently refers specifically to the allocation of train paths, the management of train control, and operating standards. On this basis, the Authority considers that section 16 applies already to those corresponding elements of Part 5 instruments.

365. The Authority does not consider that it is appropriate for the provision of section 16 to apply to commercial agreements outside the Code, or for the regulator to have access to such agreements as a matter of course, as argued by Aurizon. The regulator is able to request this information from a railway owner at any time under the provisions of section 21 of the Act.

366. The Authority has reconsidered its recommendation from the second review of the Code that a list of examples of fair discriminations should be included in the Code. The Authority agrees with submissions that suggest that a list of examples of 'permissible discrimination' would not improve the flexibility of the Code. The Authority does not consider that inclusion of a list of examples of 'unfair discrimination' is required, as the remedy for unfair discrimination by a railway owner is able to be pursued by the access seeker through legal means. The Authority does not consider that further prescriptiveness in the interpretation of 'fairness' or 'unfairness' is consistent with a light-handed approach to regulation.

367. The Authority has noted suggestions from Aurizon that there should be two key tests to demonstrate that unfair discrimination has occurred, which are: (a) it has a material adverse effect on an access seeker; and (b) it has a substantial impact on competition in the relevant market.

Part 3 – should Part 3 prescribe a time limit for the conclusion of arbitration?

Submissions

368. Asciano submitted that an indeterminate timeframe for arbitration may provide an incentive for one party to delay (initial submission page 9). Asciano submitted that a time limit should be prescribed for arbitration; however, that this limit should be able to be varied if both parties agree to an extension of time.

369. Aurizon submitted that there would be benefit in putting timeframes on arbitration to provide parties with certainty (initial submission page 27). Aurizon does not consider it appropriate to impose a 'blanket' timeframe in the Code as each arbitration will vary in the nature and complexity of issues. Aurizon submitted that timeframes should be determined at the start of each arbitration to reflect the circumstances of each dispute.

370. Brockman submitted that dispute timeframes under the Code do not effectively encourage efficient progression of access proposals (initial submission page 5). Brockman submitted that structured timeframes for each phase of the dispute process would limit unnecessary recourse to the courts, and delays.

371. BR submitted that it is not appropriate for arbitrary time limits to apply to the arbitration process (initial submission page 20). BR submitted that the arbitrator should be free to hear the claims and defences of the parties and review all evidence, and that any limitation on the freedom of the arbitrator to conduct an arbitration would diminish the ability of the arbitrator to discharge his responsibilities under section 6(4)(i) of the CPA.

372. CBH submitted that a time limit should be placed on the conclusion of arbitration (initial submission page 35). CBH submitted that a time limit on arbitration would ensure that costs are minimised and that negotiations may be commenced more efficiently, consistent with the negotiate-arbitrate principles under the CPA.

373. CBH noted that in South Australia, an award must be made within 6 months from the date a dispute was referred to arbitration and that in Victoria, dispute resolution is subject to a 45 day time limit (initial submission page 36).

374. DOT submitted that the Code should provide a timeframe for the resolution of disputes, in order to ensure that negotiations proceed without due delay (initial submission page 3).

375. TPI submitted that time limits on arbitration are inappropriate if they result in matters not being fully considered before a final decision is made (attachment to initial submission page 26). TPI submitted that if timelines are to be provided, then decision points may be required to allow for timely resolution of issues, with break points in the event that certain issues need to be considered in further detail.

Authority considerations

376. The Authority notes that there is currently provision in the Code at section 28 for a preliminary conference to be held as a first step in arbitration, the purpose of which is to establish timeframes for the conduct of the arbitration and the making of the arbitrator's determination.

377. The Authority considers that this is consistent with the view that a timeframe should be established for each arbitration according to the circumstances of each dispute. The Authority does not consider that a blanket timeframe for conclusion of arbitration should be included in the Code.

378. The Authority does not consider that further clarification in this part of the Code is required.

Section 50 – should a railway owner be able to declare any information confidential?

Submissions

379. Asciano submitted that making costing information confidential makes it impossible for interested parties to make informed comment on those costs, and so makes consultation problematic (initial submission page 9). Asciano submitted that monopoly infrastructure owners should not be able to prevent these costs being made public, as making costs public should not damage a natural monopoly, and that primacy should be given to transparency of regulatory processes.[17]

380. Asciano submitted that section 50(3) should only allow for confidentiality if publication of that information would be commercially damaging to the railway owner in its role as an infrastructure provider charging efficient prices. Asciano submitted that other related activities of the railway owner, and the railway owner's ability to receive supernormal profits are not relevant to this consideration.

381. Aurizon submitted that the sharing of information should be encouraged as it reduces information asymmetries (initial submission page 26). Aurizon submitted that confidentiality claims should be limited to legitimate circumstances and that greater weight should be given to information that is not marked confidential.

382. Brockman submitted that all determinations that affect the interests of an access seeker (whether made by the regulator or the railway owner) should be provided to the access seeker in unredacted form, with limited confidentiality provisions where appropriate (initial submission page 11).

383. BR submitted that there are no provisions of the CPA which describe that the regulator should disseminate information, or that any weight should be given to the interests of third parties not directly involved with providing or seeking access, except the benefits accruing to the public in having competitive markets (initial submission page 21).

384. BR submitted that changing the Code to provide the Regulator with discretionary power over the confidentiality of information provided by the railway owner under any section of the Code will not improve the ability of the Code to give effect to the objectives of the CPA, as the CPA contains no such objective.

[17] This argument is distinct from arguments put forward separate to this review by some stakeholders who argue that disclosure of railway owners' cost information may and should assist in negotiating out-of-Code agreements with railway owners. This argument was put in a submission to the Economics and Industry Standing Committee report on The Management of Western Australia's Freight Rail Network. The Authority does not agree with this view, as (1) the Code requires at s4A that nothing in the Code applies to agreements made outside the Code and (2) some railway routes face strong competition from road transport and the railway owners' costs are commercially sensitive in this respect.

385. BR submitted that where confidential information provided by the railway owner contains confidential information regarding the access seeker, any change to the Code that diminishes the application of confidentiality would put at risk the objective of section 23 of the Act.

386. CBH submitted that a number of Code requirements, including consultation, carry a 'presumption of disclosure' and cannot be met if information is made confidential (initial submission page 53). CBH submitted that (a) the railway owner should not be permitted to claim confidentiality over information it is required to provide under the Code, and (b) the ERA should be compelled to publish regulatory decisions made under the Code, including costs determinations, in full and without confidentiality restrictions.

387. CBH submitted that clauses 6(4) (a) to (c) of the CPA, which relate to transparent and efficient regulatory processes, are not satisfied when railway owners are able to keep information confidential.

388. CBH submitted that cost determinations are not confidential information belonging to railway owners, as they are hypothetical calculations of costs for a replacement railway (initial submission page 54).

389. CBH cited the South Australian Rail Access Regime and the National Gas Law as examples of jurisdictions where regulators may disclose information to the detriment of the provider of the information, if the regulator considers that the public interest in disclosing the information outweighs the detriment (initial submission page 56).

390. DOT submitted that the confidentiality of railway owners information should be assessed on a case-by-case basis and should be informed by provisions of commercial contracts (state agreements) and leases between the railway owner and the Government (initial submission page 3).

391. Roy Hill submitted that railway owners should be permitted to require that the Authority retain the confidentiality of documents and information provided to the Authority in accordance with the Code (initial submission page 1).

392. TPI submitted that it is important that the access regime protect confidential and commercially sensitive information (initial submission page 27). TPI cited a recent High Court decision upholding the protection of private property rights of infrastructure owners in the context of regulation intended to serve the public interest. TPI submitted that the ERA should bear this in mind, as proprietary knowledge is a form of private property.

Authority considerations

393. In relation to BR's submission that any diminution of confidentiality would put at risk the objective of section 23 of the Act, the Authority notes that section 23 of the Act relates specifically to the provisions of section 31 of the Act (Segregation Arrangements) and so is not relevant to the disclosure of railway owners' information by the Regulator.

394. The Authority published a decision in August 2011 which outlined its decision not to publish determinations of railway owner's costs relevant to a proposal unless the proposal proceeds to an agreement.[18]

395. That decision also outlined the Authority's intention to require at least one (the first) cost determination for each railway to be published on the Authority's website, including a costing model, to provide guidance and a 'starting point' for future access seekers. Since that time, railway owners have not allowed the Authority to publish costing models provided in support of their determinations of costs.

396. The Authority notes that the information provided by railway owners in support of their cost determinations has generally been in excess of that required to be provided by the Code.

397. The Authority has established a process in the course of finalising its recent two cost determinations, which meets the requirements of the access seeker for adequate transparency, and also the railway owner's requirements to protect their confidential information. This process has allowed the access seeker to be provided with an unredacted copy of the regulator's determination, and for a redacted version of the determination to be published on the Authority's website.

Clause 2 Schedule 4 – is there a better means of estimating capital costs than the GRV method?

Submissions

398. Asciano submitted that consistency of the WA rail access regime with other Australian rail access regimes is generally desirable and supports using DORC as an upper bound on asset valuation (initial submission page 10).

399. Aurizon submitted that the Modern Equivalent Asset GRV approach can cause a misalignment between the assumed standard of infrastructure and its actual standard (initial submission page 23). Aurizon submitted that this therefore has the potential to allow inefficient pricing. Aurizon submitted that this may be a recognized problem with SW grain lines, but provides a risk on any network as assets age.

400. Aurizon submitted that with changes in technology, it is highly likely that there will be differences between installed technology and the modern equivalent, giving rise to windfall gains or losses, even if assets are in Modern Equivalent Asset (MEA) condition. Aurizon submitted that this is a problem especially for long-lived assets.

401. Aurizon also submitted that the application of the GRV method is problematic where the technical life of an asset exceeds its economic life. Aurizon submitted that GRV is not well-suited to greenfields railway developments (page 23). Aurizon referred to an inability of the GRV method to adequately compensate for development risks in greenfields projects (initial submission page 16).

402. Aurizon submitted that owners of new railways should have the choice of GRV or DORC as valuation scheme (initial submission page 24). Aurizon submitted that, for

[18] https://www.erawa.com.au/cproot/9819/2/20110825%20Final%20Decision%20-%20Review%20of%20the%20Requirements%20for%20Railway%20Owners%20to%20Submit%20Floor%20and%20Ceiling%20Costs.pdf paragraph 131.

established networks, a change in method could compromise their business interests.

403. Aurizon submitted that consideration should be given to the limitations of the GRV approach to established networks, although that should not give rise to a change in the level of prescriptiveness of the rail access regime. In particular, Aurizon does not support a change from negotiated/arbitrated outcomes, to a more prescriptive reference tariff approach.

404. In its further submission, Aurizon clarified that the use of GRV is reasonably sound in its initial application to a brownfield railway, where the demand for the service would be expected to extend beyond the physical life of the asset, and the ceiling price would better reflect the conditions applying in competitive markets with threat of entry and changes in technology. Aurizon re-iterated that nonetheless asset values should be adjusted to reflect the level of service provided (further submission page 6).

405. In its further submission, Aurizon expanded on its views in relation to the suitability of the GRV method to greenfield export infrastructure (outlined in paragraph 401 above). Aurizon submitted that:

- The GRV back-loads asset recovery, which distorts accounting depreciation and the attractiveness for financing.
- Economic life assumptions are subject to Regulatory risk.
- Market risks associated with changes in rail construction costs, which is inconsistent with the normal approach to high fixed-cost infrastructure investment.
- GRV valuations do not reflect development risks.

406. Aurizon qualified the above concerns with recognition that where rail infrastructure has been built for the primary purpose of supporting its own operations, the incentives to invest may not be so adversely affected, and regulatory error may not have a material bearing on financial outcomes. Further, if access occurs substantially after the construction date, then the variance between GRV and DORC is diminished (further submission page 7).

407. Aurizon commented that the GRV approach avoids the complexity and subjectivity of assessing the depreciated component of DORC (further submission page 7). For instance, in the absence of robust information on installation dates and historical capital expenditures, considered judgements are required to establish opening asset values and depreciated life of older assets.

408. Aurizon elaborated on its initial submission comment that the interests of parties impacted by any change in valuation scheme should be considered, especially in respect of the absence of a regulatory compact on optimization risks associated with the freight network lease. Specifically, that the assets were acquired on the basis that demand risks are assumed by the service provider, rather than being fully transferred to remaining users via higher access prices, in order to maintain capital maintenance (further submission page 7).

409. Aurizon took issue with the assertion made in the report attached to the CBH submission (Frontier Economics), that the GRV method allows returns that are not consistent with risks faced because railway networks face predictable increases in replacement costs (further submission page 8). Aurizon submitted that this is not

correct, and that replacement costs are liable to increase or decrease, and to the extent that future changes are predictable, these are reflected in any purchase price of assets. Aurizon further added that CPA principles do not preclude windfall gains - or losses - associated with application of the GRV method, and that the GRV method exposes the owner to a misalignment between the value of its assets and the costs of renewals because major periodic maintenance costs are excluded.

410. In respect of the above, as it relates to the leased freight network, Aurizon provided its view that the most relevant valuation would be that which reflects the expectations of the owner when it acquired the rights to provide the service, and that the transaction price may not be an appropriate benchmark as it will reflect the value of any future costs expected to be incurred as part of the transaction. Aurizon noted that any reference to a business valuation determination in 2000 should reflect that the below-rail assets have been subject to subsequent transactions (further submission page 9).

411. In relation to the report attached to the CBH submission Aurizon submitted also that the issue of whether prices lead to inefficient duplication of the service is of little relevance to regulatory objectives, and that the principle objective is to ensure efficient investment in the regulated facility.

412. Brockman submitted that a DORC valuation method should be adopted, and would align the WA regime with other regimes in Australia (initial submission page 13). Brockman submitted that a DORC regime would provide for more stability in prices over time.

413. Brockman also submitted that DORC approach is not inconsistent with a cost boundary negotiate-arbitrate approach and does not support the development of reference tariffs. Brockman noted some advantages of reference tariffs (initial submission page 14) being (a) decreased time and cost in negotiating (b) increased transparency and certainty, and (c) replicates outcomes of competitive markets and so aligns with CPA.

414. BR submitted that in order to justify any change in the valuation method, it must be established that the change will enhance the effectiveness of the Code in meeting the objectives of the CPA (initial submission page 3). BR submitted that the ERA has not provided any evidence of the unsuitability of the GRV method as it relates to giving effect to the objectives of the CPA.

415. BR submitted that the WA regime philosophy is one of light-handedness and encourages negotiation, giving effect to the CPA, and that a change in valuation method would impose a more costly administrative burden and would require wide-ranging and costly changes to the Code.

416. BR submitted that utilisation of a different valuation method would have no impact on the interface issues of concern to the National Competition Council (NCC), and that the section of the NCC report which addressed interface issues (section 6) did not consider the issue of valuation technique (initial submission page 4), and that harmonisation of valuation methods is not necessary to ensure that upstream and downstream markets are exposed to efficient costs.

417. BR noted that for older assets, a DORC approach could substantially reduce the ceiling price on some of BR's routes, and as such would substantially reduce the business value determinations made by shareholders at the time of the sale of the Westrail business in 2000. BR re-iterated this assertion in its further submission, and

added that the GRV was also a fundamental pricing tenet for Brookfield's subsequent purchase of the lease over the network (further submission page 2).

418. BR submitted that the GRV is not complex and is transparent (further submission page 3). BR submitted that the GRV scheme is easy to understand as simply the current cost of replacing the railway, and that any interested party can assess the market price for railway infrastructure by obtaining its own quotes (further submission page 4). BR commented that the GRV method does not require an assessment of the condition and remaining life of existing infrastructure, which BR advised might be difficult to do under certain circumstances.

419. BR submitted that the ease by which the GRV method can be used in this way is a valuable attribute not shared by other methods. BR submitted that a further benefit of the GRV method is that the Modern Equivalent Asset (MEA) basis for the GRV reflects current industry standards that are easily verifiable by the regulator (further submission page 7).

420. BR submitted that the GRV method also ensures that effective competition in upstream and downstream markets (as required to be promoted by the CPA) is promoted by the use of GRV, as participants in those markets are exposed to the full contemporary cost landscape in which they are engaged (further submission page 8). In this respect, BR also provided some comment on subsidies provided to road transport and capital investments made by Governments in roads (further submission page 9).

421. BR countered comments made in other submissions to the effect that windfall gains or losses may accrue to the railway owner by virtue of the updating of valuations (further submission page 10). BR submitted that the only way a railway owner would benefit from a re-determination of costs would be if it recovered the ceiling costs on each route each year. BR commented that this was an unlikely outcome, as negotiations establishing the proportion of each participant's sunk costs that will be recovered, and that the railway owner will seek to offset any revenue losses by negotiating cost savings in other areas, such as capacity availability or service standards.

422. BR countered comments in other submissions that if there is a tendency for replacement costs to increase over time, that this facilitates income transfers from the railway owner to the operator (further submission page 11). BR submitted that replacement costs do not necessarily increase in real terms over time.

423. BR submitted that 'build or buy' signals, referred to in some submissions as not relevant due to the natural monopoly characteristics of railways, are in fact relevant (further submission page 12). BR commented that infrastructure only exhibits natural monopoly characteristics where it can service all the demands put upon it, and that if capacity becomes scarce, then duplication becomes feasible, as evidenced in the Pilbara.

424. BR submitted that the risk of inefficient duplication of infrastructure is low under the GRV-MEA system (further submission page 13). BR submitted that this is because an accurate contemporary price for infrastructure access is presented and that negotiation/arbitration ensures that an access seeker will pay the appropriate price for its use of the infrastructure provided. These comments were provided in the context of replacing very old grain rail infrastructure that might not be considered economic to duplicate today in its original form, on existing routes.

425. BR countered comments in other submissions that changing asset valuations are incompatible with negotiated outcomes due to uncertainty about future asset values (further submission page 14). BR submitted that this is not correct as the Code does not prevent the railway owner and access seeker negotiating whatever pricing arrangements suit their needs, including "locked-in prices", and that in this respect there is no difference between negotiated outcomes under the Code or outside the Code.

426. BR submitted that the ability to lock in pricing combined with the ceiling price test provides that any cost volatility will work in the access seeker's favour – that is, they will pay only the negotiated price or – if the railway owner breaches the ceiling price test – less than the negotiated amount. BR submitted that, in this way, the Code gives effect to s.6(5)(b) of the CPA, because the railway owner is entitled to recover only efficient costs, while both parties are able to negotiate arrangements that provide certainty, mitigate risk, promote efficiency and incentivise productivity.

427. BR referred to comments made in other submissions to the effect that GRV should be adjusted to reflect actual investments made by railway owners (further submission page 15). BR submitted that the railway owner may find itself in a position where it accepts a price substantially lower than the cost of providing access, in effect "mining" the existing infrastructure to an extent that it is not able to be maintained in perpetuity. BR submitted this provides for an efficient outcome, as price reflects the absence of sufficient investment to keep the infrastructure operable, allowing the access seeker to benefit from the existing infrastructure without needing to invest to secure the future of that infrastructure.

428. BR submitted that, in the event that unusual circumstances conspire to make this the most efficient outcome, and if the consequences of this are well understood, then the fact that the Code does not prevent this from happening is a strength of the regime that gives effect to the "efficient use" object of section 6(5)(a) of the CPA.

429. BR submitted that a consideration of the status of the infrastructure in determining prices is contemplated in the Code, by virtue of the pricing guidelines in Schedule 4 clause 13, which say that prices should reflect the standard of the infrastructure and the operations proposed by the proponent. BR submitted that this means that in negotiation (or arbitration) the parties will come to agreement on the appropriate service being exchanged for the appropriate price.

430. BR provided examples showing where negotiated outcomes have enabled significant investment in parts of its network, by establishing a commitment by users to pay the efficient cost for use of the network (further submission page 16). BR submitted that, without that commitment by the access seeker, any investment in the network by the railway owner may be considered inefficient and 'gold plating' the network.

431. BR submitted that the analytical purpose to which asset valuation is put determines the most appropriate form of asset valuation (attachment to further submission page 23). BR submitted that if the asset value is being used to assess whether access charges lay between the economic concepts of incremental and stand-alone cost, then the simple, forward looking GRV approach has a strong advantage over DORC. If the asset valuation is being used to prescribe prices, and the purpose is to ensure that the regulated asset achieves recovery of efficient investment, then a DORC methodology has an advantage in that it provides greater flexibility in the establishment of capital charges.

432. CBH quoted the NCC view on the potential to replace GRV (attachment to submission page 20):

> The WA Rail Access Regime is also the only regime to adopt GRV and consistency in national regulation would be promoted with a review, and potentially replacement of the GRV methodology.

433. CBH submitted that the GRV method, as applied in the Code, allows the railway owner to earn returns on assets that are not consistent with risks faced or investments actually made (attachment to submission page 21). CBH submitted that the implementation of the GRV allows for updates of valuations, a new set of (higher) annuities, and the accrual of windfall gains to the railway owner. CBH submitted that no access seeker would reach a long-term access agreement that allowed for ongoing revaluation of the asset base upon which prices would be based (attachment to submission page 28).

434. CBH submitted that the 'build or buy' signals associated with GRV valuations, do not promote efficient prices for natural monopoly providers, as 'building' is by definition an inefficient solution in the presence of an incumbent natural monopoly (attachment to initial submission page 23).

435. CBH submitted that asset revaluation anomalies are widely recognised by regulators in Australia (attachment to submission page 26), and cited as examples (a) the ARTC Hunter Valley undertaking, which currently uses a fixed asset base, with capital expenditure rolled in at cost, (b) in telecommunications, the ACCC, which was a long-time proponent of GRV, moving to a fixed RAB in 2011, and (c) amendments to electricity and gas laws through to 2007 having had the effect of eliminating asset revaluations.

436. CBH submitted that a 'line in the sand' fixed valuation approach be adopted, acknowledged the increased regulatory burden such an approach would entail, and provided some examples of how an 'opening value' asset base might be established (attachment to submission page 29-30).

437. DOT submitted that it supports the ERA in identifying an appropriate asset valuation method, and suggested consideration be given to the suitability of DORC, deprival value and historical value (initial submission page 2).

438. Roy Hill submitted that the DORC valuation method (with straight line depreciation) should be available to all infrastructure owners as it is the common methodology used for regulated infrastructure around Australia (initial submission page 5). Roy Hill submitted that consideration should be given to accommodating either GRV or DORC approaches to be adopted by infrastructure owners (initial submission page 6).

439. Roy Hill submitted that where the lives of time-limited customer projects are known at the outset to be less than the rail asset life, a GRV approach increases the stranded asset risk (initial submission page 6).

440. Roy Hill submitted (further submission page 4) that it agrees with:

- BR's submission that in order for a change in valuation method to be justified, it must be shown that the GRV method fails to calculate efficient costs and that any change would result in benefits exceeding the costs of change (see paragraph 414 above).
- Aurizon's submission that the GRV method may fail to adequately account for development and construction risk (see paragraph 401 above).

- Aurizon's submission that the railway owner should be able to propose the method that best suits the circumstances of their particular network (see paragraph 402 above).

441. TPI submitted that the GRV valuation method is well suited to long-lived assets, which are able to be extended by regular maintenance and periodic renewal expenditure (attachment to submission page 24). TPI submitted that the GRV method better reflects the nature of railway assets than DORC, and is used to value assets similar in nature (water assets, irrigation channels), and leads to more consistent prices over time.

442. TPI noted that GRV and DORC valuations should deliver similar net present values, but do provide differences in cash flow, which in the event that a change is made from one method to the other, will lead to material changes in net present value. TPI also noted that changing method would involve compliance costs for the access provider (initial submission page 25).

443. TPI submitted that it is not obvious that the distinction between DORC and GRV is particularly relevant, or why a change from GRV to DORC would have significant advantages. TPI submitted that if a change were made, an adjustment should also be allowed for to ensure that it is net present value neutral to all parties.

444. In its further submission, TPI commented that GRV is the most appropriate valuation methodology due to the long life and cost structure of assets (initial submission page 1) and that the GRV method provides for more stable prices over time. TPI submitted that GRV enables negotiations to take place using the most current information available, allowing outcomes that are economically efficient.

445. TPI submitted that GRV is more likely than DORC to encourage new investment, given the higher upfront prices potentially incurred by access seekers under DORC (further submission page 2). TPI submitted that the use of GRV best reflects the intent of clause 6(b) of the CPA, as this valuation provides the basis for showing a proponent the costs of constructing its own facility.

446. TPI submitted that changing the valuation approach would require significant amendment to negotiation and arbitration procedures outlined in the Code, and would be prejudicial to the business interests of railway owners currently covered by the Code.

447. TPI submitted that the arguments presented in the report attached to the CBH submission, which indicate a preference for DORC over GRV, are contradicted by the statement at section 3.3.4 of the report that GRV and DORC can produce identical outcomes. Further, TPI submitted that the arguments made in the report attached to the CBH submission are based on an assessment of the BR network only, and do not apply to other railway owners regulated by the Code.

448. WAFF submitted that the floor and ceiling prices set under the Code do not reflect the true value of the network (initial submission page 3). WAFF also submitted that the current ceiling price is determined to be the cost to replicate the current network, but that the true value of the network is the gross replacement value.

Authority considerations

449. The Authority does not agree with a premise of Aurizon's submission; that is, that the MEA standard used to determine capital costs, is also used as the assumed standard

of the infrastructure. This is because clause 13(c)(i) of Schedule 4 of the Code clearly anticipates a standard of infrastructure which may be less than the MEA, and that the standard of infrastructure is a basis for price negotiation.

450. The Authority does not agree with Aurizon's submission that the accommodation of technical lives which are longer than economic lives is problematic within a GRV scheme. Clause 2(4)(c) of Schedule 4 to the Code clearly indicates that the economic life of the railway is to be the time period basis for the capital cost annuity calculation.

451. Railway owners' costing principles have been approved by the Authority that make explicit provision for the economic life of a railway to be shorter than the technical lives of its component assets. The Authority considers that an annuity calculation based on a DORC valuation would refer to similar practical considerations.

452. In respect of comments made by Aurizon and Roy Hill, the Authority considers that adequately recognising development risks is no less problematic within a DORC scheme than within a GRV scheme. The Authority has approved railway owners' costing principles that accommodate an allowance for "asymmetric risk" as a capital cost within the GRV framework.[19]

453. The Authority has noted Aurizon's and Brockman's submissions that a change in valuation methodology from GRV should not give rise to a change in the level of prescriptiveness and, in particular, both stakeholder's preference for negotiated/arbitrated outcomes over a more prescriptive reference tariff approach.

454. The Authority considers that estimating capital costs on a DORC valuation would reduce ceiling prices substantially on some routes, to close to what would otherwise be a regulator-determined reference tariff.[20] Similarly, in respect of Aurizon's submission that asset values should be adjusted to reflect the level of service provided, the Authority considers that this too would have an effect on the negotiation range similar to implementing a DORC approach to valuations.

455. The Authority acknowledges Aurizon's and BR's comments in relation to the impact of a change in regulatory valuation on the leaseholder of the freight network. The Authority is not able to provide any comment that addresses the 'sovereign risk' arguments put forward by these stakeholders.

456. In particular, the Authority is not able to comment on the demand risks being 'sold' to the lease holder, or the more general issue of the business expectations associated with the original transaction. This is because the obligations attached to the lease have been altered since the original sale, particularly in relation to some specific grain routes, and because the vertically integrated business has been separated and on-sold subsequent to the original transaction, as acknowledged by Aurizon in its submission.[21]

[19] Further scope for recognition of costs associated with development risk is evidenced by the Authority's acceptance of "owner's costs" components of on-costs attached to individual asset costs in a recent determination. Owner's costs are those in-house project management costs which cannot be outsourced to an Engineering Project Construction Management service provider, such as administration and insurance costs. Railway owners' costing principles also make provision for equity raising costs, which would be expected to be higher for riskier developments with lower gearing

[20] The Authority does not consider that this, in itself, would be a problematic outcome, but that it highlights the fundamental difference between the 'forward looking' (build-or-buy) approach provided by the GRV method and the 'backwards-looking' (cost-recovery) approach provided for by the DORC method.

[21] These matters were open for review as part of the Economics and Industry Standing Committee report on the Management of Western Australia's Freight Rail Network.

457. Consistent with the Authority's comments in relation to Aurizon's and Brockman's submissions at paragraph 453, the Authority agrees with BR's and TPI's submissions that a change from the GRV scheme would impose a more costly administrative burden and require substantial changes to the Code, by way of enabling a more prescriptive DORC-based capital cost assessment.

458. The Authority acknowledges the comments of BR and TPI to the effect that the GRV method promotes effective competition by exposing access seekers to the full cost of providing the service. The Authority agrees with BR that the GRV method provides relevant "buy or build" signals.

459. The Authority considers that this argument is also relevant in the context of infrastructure that is not at MEA standard. The Authority agrees that the 'mining' of existing infrastructure that is not economic to rebuild, results in an economic price which reflects an efficient outcome if the access seeker also considers the infrastructure is not economic to rebuild or duplicate, and therefore cannot justify committing funds to an expansion.

460. The Authority acknowledges comments made by BR in relation to the "levelness" of the "playing field" between provision of rail and road services and the incidence of direct and indirect subsidies provided to these competing modes of transport. The Authority is not able to consider these comments in the context of this review.

461. The Authority agrees with the comments made by BR (summarised in paragraph 431) that the GRV valuation method provides for a forward looking "buy or build" regime, and that the DORC method provides for a backward-looking "cost recovery" regulatory regime, and that the former is necessarily less prescriptive than the latter.

462. The Authority notes, in relation to CBH's submission that the updating of valuations results in increasing annuities, that each cost determination relates to a singular access proposal (or potential proposal), and that there is no provision in the Code for price terms negotiated in access agreements to be automatically linked to subsequent cost determinations.

463. The Authority considers, in relation to CBH's submission that 'build or buy' signals are irrelevant, that the GRV valuation provides an important 'bypass' cost that would inform negotiations, regardless of the practicality of replicating monopoly infrastructure. The GRV for a route would also in the same way inform negotiations around the re-building of a route to restore it to MEA standard.

464. The Authority notes, in response to a number of comments relating to the wide range between total and incremental costs shown in the recent BR cost determination, that the difference between the total and incremental costs for a single user route is simply the annual replacement capital cost of the route.

465. The Authority has noted CBH's observation that regulators have moved away from GRV to alternative valuation methods in some other jurisdictions (see paragraph 435). CBH did not provide any commentary or assessment of the rationale for these changes or of any improvements which have resulted.

466. The Authority does not agree with Aurizon's and Roy Hill's submissions that railway owners may be given a choice of either DORC or GRV as a valuation basis if both these options would be within the current Code framework. The Authority does not consider that it would be practical to incorporate the two different approaches within one Code, or set of regulations. The Authority agrees with the comments of BR and

TPI that the Code would need to be substantially re-written to accommodate the DORC valuation method.

467. The Authority has noted that the *Railway (Roy Hill Infrastructure PL) Agreement Act 2010* provides Roy Hill with the option of being incorporated into the WA Rail Access Regime, or having a haulage undertaking accepted by the ACCC.

468. The Authority considers that allowing Pilbara railway owners the choice of being subject to the WA Railway Access Regime, or having services declared by the ACCC using an arrangement based on DORC is appropriate.

469. The Authority does not agree with Roy Hill's submission that GRV presents more of a stranding risk than DORC where economic life of the railway is less than the technical life of the railway. The Authority currently allows for the truncation of technical lives to the economic life of mines served by the railway infrastructure for the calculation of annuities based on GRV valuations.

470. The Authority has noted TPI's submission that GRV is the most appropriate valuation methodology for longer life assets and that, in respect of the cost structures of longer lived assets, the GRV method provides for more stable prices over time. The Authority agrees that the GRV method may provide for more stable prices over time where the economic life of the railway exceeds its technical life.

471. The Authority has previously noted TPI's view that the economic life of its railway is limited to less than 20 years.[22] Although the Authority did not agree with that view, the Authority allowed the economic life of the railway to be truncated to 40 years,[23] that is, less than the technical life of some of its component assets. The Authority does not therefore consider that TPI's views in this respect are of particular relevance to its own railway, but apply generally to all railway networks.

472. The Authority notes in relation to the WAFF submission – that the true value of the network is the gross replacement value - that WAFF may have intended to comment on the non-congruence of the replacement cost of the network and its current (depreciated) value. The Authority notes that the cost to replace the current network with a new equivalent is the GRV and that the true value of the current network is less than that amount.

Clause 10 Schedule 4 – is the prescribed 30 day time limit for the making of the Regulator's determination sufficient?

Submissions

473. BR submitted that it supported an increase in a range of timeframes in the Code and a change in definition of days to coincide with business days (initial submission page 13). BR suggested a range of timeframes consistent with the use of business

[22] ERA Cost Determination for the Route subject to Brockman Irons Access Proposal https://www.erawa.com.au/cproot/13744/2/Redacted%20Version%20–%20The%20Pilbara%20Infrastructure%20–%20Redetermination%20of%20Costs%20relevant%20to%20Brockman%20Iron's%20Access%20Proposal.pdf] paragraph 422.

[23] Ibid paragraph 454.

days, and some increased timeframes consistent with the ARTC Interstate Access Undertaking and the Aurizon Network Access Undertaking.

474. BR submitted that the timeframe stipulated in Schedule 4 clause 10(3) should be 60 business days (initial submission page 14) and that this reflects the time required by the ERA in recent determinations. BR submitted that this change would improve the ability of the ERA to afford procedural fairness to the parties.

475. BR clarified comments made in its initial submission to indicate that, if parties correctly adhere to the requirements in the Code, the existing timeframe for negotiations under the Code are comparable to normal commercial processes (further submission page 23).

476. BR submitted that the approval of the railway owner should also be sought, in addition to that of the access seeker, if the regulator wishes to extend the timeline for the making of a determination under clause 11(2) of Schedule 4.

477. TPI submitted that the ERA should be allowed more time to make its costs determination (attachment to initial submission page 26) and that the railway owner should be allowed more than the current seven (7) days prescribed in clauses 9 and 10(2) of schedule 4 to the Code, given the greater complexity of the initial cost assessment.

478. TPI also noted that there are no explicit time limits imposed on the achievement of access seekers' obligations in the Code.

Authority considerations

479. The Authority considers that the current timeframes in the Code are adequate for the purposes described in the Code. The Authority has not been prevented from meeting its obligations under the Code, utilising the existing timing provisions. The Authority is concerned that longer timeframes could result in unnecessary delays in the progress of an access proposal.

480. The Authority supports the proposition that "days" in the Act and the Code should be defined to mean "business days" for consistency with other regimes, and to alleviate irregular time constraints caused by public holidays at particular times of the year.

481. The Authority notes TPI's submission that the initial determination of costs by the railway owner is more complex than the regulator's subsequent assessment of the railway owner's determination. The Authority does not agree with this assertion.

482. The Authority considers that the provisions in clause 11 of Schedule 4 of the Code provides adequate scope for extension of the 30 day time limit stipulated in clause 10 of Schedule 4.

483. The Authority considers that it is reasonable for the Regulator to seek the railway owner's views on whether an extension of the timeline for making of a determination is reasonable. The Authority does not consider that a requirement to seek the approval of both the proponent and the railway owner would be a practical requirement under all circumstances.

FURTHER SECTION-SPECIFIC MATTERS

484. Interested parties provided comment on matters in addition to those raised by the Authority in the issues paper. These comments have been grouped together and summarised under headings corresponding to the relevant parts of the Code.

Part 1 [section 4A] – Parties have the option to negotiate agreements outside this Code

Submissions

485. Aurizon submitted that parties that have been negotiating outside the Code should be allowed to bring that negotiation to arbitration under the Code (initial submission page 4). Aurizon also submitted that the register of access agreements maintained by the regulator be broadened to include all agreements made, both under the Code and outside the Code.

486. BR responded to comments in other submissions that access seekers are unable to assess whether the railway owner has breached the ceiling price test (further submission page 29). BR submitted that it is not the role of access seekers to make this assessment.

487. CBH submitted that the over-payment rules are not enforceable when there is no total cost determination in place (initial submission page 23). CBH submitted that because overpayment returns are not made to out-of-Code operators, this is an incentive for railway owners to keep operators outside the regime. CBH submitted that the operation of the ceiling price test should be clarified to ensure that it operates at all times, and can be enforced at all times.

488. BR submitted that it is not necessary, as suggested in other submissions, that the ceiling price test be monitored in the absence of any agreements under the Code. BR submitted that if, as per 6(4)(a) of the CPA, an agreement is able to be made without reference to the Code, then the provisions of the Code should not apply.

Authority considerations

489. The Authority notes that parties negotiating outside the Code have access to arbitration processes through the *Commercial Arbitration Act 2012*, that is, on the same basis as provided for in the Code.

490. It is not necessary for the Authority to maintain information on out-of-Code agreements in order to properly audit over-payment accounts. Railway owners are required to keep separate accounts and records by section 34 of the Act and the Regulator may require copies of these records at any time. Further, arrangements are currently in pace with all railway owners for audits of over-payments accounts to be undertaken by independent auditors, with terms of reference provided by the ERA.

491. The Authority agrees with CBH's observation that the over-payment rules are not enforceable when there is no total cost determination in place. If there are no access agreements in place under the Code for a route, then there is no basis on which to establish or audit the ceiling price test (overpayment account) and there are no returns to be made to any above-rail operators regardless of the revenue earned by the railway owner.

492. In respect of the wording of clause 8 Schedule 4 (Ceiling price test) the Authority notes that the terms “access” and “operator” are Code-defined terms, and that – for the purposes of the Code - neither of these two terms apply to an entity with a commercial agreement outside the Code.

493. The Authority does not consider it appropriate that out-of-Code revenues for a route should be monitored by the Regulator in respect of Code provisions where there are no Code agreements in place for a route.

Part 2A & 2 [sections 6, 7, 7A-E] – Required and Preliminary Information

Submissions

494. Aurizon submitted that, consistent with most other rail regimes in Australia, it is reasonable to require railway owners to publish all required information on their website (initial submission page 25). Aurizon submitted that transparency is important in relation to standard of infrastructure/service levels, particularly where there are obligations established via lease arrangements.

495. Brockman submitted that all required information should be available free of charge on the railway owner’s website (initial submission page 8). Brockman submitted that the prescribed time set out in section 7(c)(2)(b) for the amendment or replacement of this information should be reduced from two years to six months.

496. Brockman submitted that item 4(m) in Schedule 2 (information to be made available) should be clarified so that it relates to individual train movements, and not aggregate figure for the three year period referred to in section 7D. Brockman submitted that item 4(o) in Schedule 2 (information to be made available) should be clarified by defining available capacity or clarifying what information must be provided in relation to ‘available capacity’.

497. Brockman submitted that railway owners should be required to include reasonably forecast future demand where that information is known. This could include capacity subject to an access proposal or contractual arrangements. Brockman submitted that railway owners should be required to provide all information on which the assessment of available capacity or forecast demand is based (initial submission page 9).

498. Brockman submitted that regulator–approved standard access arrangements should be a part of preliminary information.

499. BR submitted, in response to submissions that detailed pricing information should be provided as preliminary information, that the GRV method allows for a completely independent assessment of costs and that it is not appropriate for an access seeker to audit calculations provided to the regulator by the railway owner (further submission page 5).

500. In respect of the above, BR submitted that it is the role of the regulator to assess the railway owner’s costs and the regulator has the opportunity to re-determine costs if circumstances change (clause 12 Schedule 4) or to determine costs if it expects a proposal to be made (clause 9 Schedule 4). BR commented that this broad and open-ended power of the regulator gives ample opportunity for the access seeker to raise relevant issues for the unbiased assessment of the regulator.

501. BR submitted that this aspect of the Code allows for revision of costs that would not be possible under a Regulated Asset Base (DORC) approach, and particularly not at the regulator's discretion triggered by information provided by the access seeker.

502. BR submitted that it agrees all required information should be available from the railway owner's website (initial submission page 23). BR submitted that, when a section 7 request is made, the proponent should be required to provide more detailed information about its proposed operations. This would assist the railway owner in tailoring its information response appropriately.

503. BR agreed with other submissions that some Schedule 2 information is of limited use or is not clearly defined (further submission page 22). BR commented that it supported a consultative review of this schedule to improve the usefulness of information routinely available to access seekers.

504. CBH submitted that it agrees all required information should be available from the railway owner's website (initial submission page 40). CBH submitted that items 4(l) and 4(m) should be specified in Gross Tonne Kilometres (GTK), which is the standard industry measurement, and that origin points should be specified (page 41).

505. CBH submitted that provision of prices on a route-by-route basis (sections 7 & 9) should be clarified, and that it is not sufficient for a railway owner to give one aggregated price for access. CBH submitted that the ambiguity should be removed that enables a railway owner to not quote prices for routes that are in Schedule 1 to the Code but which the railway owner claims have no capacity.

Authority considerations

506. The Authority does not agree with CBH's assertion that railway owners are currently enabled to not provide information for routes that are in Schedule 1 to the Code but which the railway owner claims have no capacity. The Authority acknowledges that this has occurred, but does not agree that the Code allows it.

507. In the recent past, the Authority has provided determinations of costs for routes that the railway owner - on the basis of a claim that a route has no capacity - has declined to determine costs for.

508. The Authority agrees with BR's suggestion that a consultative process be undertaken to re-examine the appropriateness of inclusions in Schedule 2 as Preliminary Information. The Authority agrees with Brockman's view that a definition of "available capacity" should be made clear in Schedule 2, and that the prescribed time for the amendment or replacement of this information should be reduced from two years to six months. The Authority re-iterates its recommendation from the second review that this information should be freely available on the railway owner's website.

Part 2 [section 8] – Proposals for Access

Submissions

509. BR submitted that the information that must be included by a proponent in an access proposal should be expanded to assist railway owners in assessing costs, expansion requirements and negotiable terms and conditions (initial submission page 33). BR submitted that the following additions should be made to the information requirements shown at section 8(3) of the Code:

- 8(3)(a) entry and exit points
  - points on the route that may be used for servicing/stabling
- 8(3)(b) frequency of access and relevant cycles/seasonality
- 8(3)(c) dimensions and operating characteristics of rolling stock
  - configuration of rolling stock and length of train
  - travel speed of trains
  - loading and unloading times at relevant points
  - number of fleets available

510. TPI submitted that section 8 should be clarified to require the proponent to indicate in its proposal specific times (of day and of week) that access is required, and a commencement date (initial submission page 3).

Authority considerations

511. The Authority agrees that the suggested additional information may assist the railway owner in the provision of an indicative price to an access seeker in response to a proposal. The usefulness of the indicative price provided by the railway owner would be determined by the level of detail provided by the access seeker with its proposal. The access seeker may provide any level of detail it considers appropriate in the context of the minimum requirements laid out in the Code.

512. According to the circumstances, some of the additional information suggested may only be determined in the course of negotiations. The Authority considers that the parties could only arrive at the level of detail suggested through a process of negotiating a price. The price would be determined in consideration of the suggested additional details.

Part 3 [Division 3] – Arbitration of disputes – other matters

Submissions

513. Brockman submitted that section 25(2) of the Code should clearly provide an exhaustive list of circumstances in which a matter may be referred to arbitration under the Code (initial submission page 11).

514. BR submitted that matters that can be referred to arbitration should be technical matters only, and not legal or statutory matters (initial submission page 24). BR submitted that, if disputes were triggered by legal matters then it is not clear why arbitration would provide a better outcome than resolution through the courts. BR submitted that as matters in sections 7-9 and Part 2 of the Code are more legal than technical, there is benefit in having disputes related to these sections resolved by court injunction rather than arbitration.

515. BR submitted that section 6(4)(g) of the CPA stipulates that owners and access seekers should be able to appoint an independent body to resolve a dispute (page 10). BR submitted that section 26(2) of the Code should be removed and be replaced with the following provisions to relate to the selection of an arbitrator;

- The parties in dispute to agree on an arbitrator(s) and that this agreement occur within 10 business days of the Regulator being notified that the disputing parties seek to refer the dispute to arbitration.

- That the proponent must notify the Regulator of the appointment of such an arbitrator(s) within 5 business days of the agreement of such an appointment.

- That if no agreement is reached within 10 business days of the Regulator being notified that the disputing parties seek to refer the dispute to arbitration, both parties to the dispute may nominate one arbitrator each, with a third and presiding arbitrator to be appointed by the Regulator.

516. BR submitted that section 26(1) should be amended to require the entity that is in dispute with the railway owner to also provide notice to the railway owner, in addition to the regulator (initial submission page 11).

517. BR submitted that the outcome of arbitration should be binding on both parties (initial submission page 27). BR submitted that without binding arbitration, there is no incentive for access seekers to negotiate access other than on terms and conditions most favourable to them as they can elect not to be bound by an arbitration, and then repeat the process of arbitration to seek a better outcome.

518. BR submitted that making the outcome of arbitration binding on both parties supports the CPA objectives at 6(4)(a) by not enabling arbitration to be used as a substitute for negotiation, at 6(4)(b) by providing a conclusive outcome in relation to using the infrastructure 'facility' and at 6(4)(h), which states that "the decisions of the dispute resolution body should bind the parties, however, rights of appeal under existing legislation should be preserved" (initial submission page 29).

519. BR submitted that all information provided by the parties in mediation should be confidential and the information provided should not be referred to in any subsequent arbitration.

520. BR submitted that the Code should be amended to introduce a mediation step before the parties go to arbitration. BR submitted that this would serve to meet the objectives of 6(4)(a) of the CPA by further encouraging and facilitating negotiation of access on terms and conditions agreed between the parties.

521. BR submitted that any arbitration process should be completed before any other timeframes in the Code are considered to have begun or elapsed (initial submission page 30).

522. BR submitted its view that the WA branch of the Institute of Arbitrators and Mediators Australia (IAMA) is not necessarily the best source of recommendations for a panel of arbitrators (initial submission page 39). BR submitted that the National branch might be a preferable source.

523. BR responded to comments in other submissions that the hurdle for seeking arbitration is too high, and is much lower in other regimes (further submission page 27). BR submitted that not only is recourse to arbitration available at important junctures in the Code process, but also that the access seeker is largely in control of this recourse.

524. BR submitted that it disagrees with submissions that suggest the regulator should act as arbitrator, as the regulator does not necessarily possess the required resources or skillset to do this, and nor should it (further submission page 28). BR submitted

that the parties in negotiation should be involved in the appointment process of an arbitrator, and noted that other submissions supported this approach.

525. BR submitted that it does not agree with suggestions that arbitration decisions should be made public. BR submitted that the purpose of arbitration is to resolve specific disputes relating to specific negotiations, and should remain subject to the confidentiality provisions of the *Commercial Arbitration Act 2012.*

526. CBH submitted that the failure to allow the parties to participate in the appointment of an arbitrator does not provide confidence in the dispute resolution process, and is contrary to clause 6(4)(g) of the CPA which requires that the parties be able to appoint an independent body to resolve a dispute (initial submission page 34).

527. CBH submitted that the parties to a dispute should be able to agree on an arbitrator, or have a right to nominate persons to the panel for the ERA to choose from (initial submission page 35). CBH submitted that it would be reasonable for the ERA to appoint the arbitrator where the parties cannot agree on an appointment.

528. CBH submitted that it does not support the referral of statutory matters (in Part 2 and 3) to arbitration, as it is a costly and unpredictable process (initial submission page 36). CBH submitted that these statutory obligations should be enforced by the ERA by issuing orders, penalties or infringement notices.

529. CBH submitted that dispute proceedings should be able to be initiated at any time (initial submission page 36). CBH submitted that it does not serve a timely transparent and efficient process to have a proponent wait out the entire negotiation period (if necessary) in order to resolve a dispute (initial submission page 37). CBH submitted that the scope of when a dispute can arise should be broadened to allow the access seeker to commence dispute resolution at any time, and that this would facilitate a more streamlined path to a negotiated outcome.

530. CBH submitted that the required confidentiality of arbitration decisions may result in potentially inconsistent outcomes from similar disputes, and wasted resources in revisiting similar disputes (page 39). CBH submitted that arbitration decisions should be made public, subject to appropriate confidentiality restrictions.

Authority considerations

531. The Authority considers that the current list of situations referred to in section 25(2) that must exist for the proponent to be considered in dispute with the railway owner is an adequate list and does not need to be expanded.

532. The Authority agrees with submissions that contend that matters that can be referred to arbitration should be technical matters only and not legal or statutory matters, for which the courts offer adequate recourse in the event of a dispute. The Authority has noted BR and CBH comments supporting this contention.

533. The Authority does not agree with BR's suggested replacement of section 26(2) of the Code. The process currently outlined in section 26(2) allows for the establishment of a panel of independent arbitrators. Selection of arbitrators by the parties will not ensure this. The Authority agrees with BR's submission that the regulator should not act as an arbitrator.

534. The Authority does not consider that arbitration should be binding on both parties. This is because an arbitrated outcome may not be commercially feasible for an

access seeker, in which case the access seeker would be disadvantaged, for example, by being required to pay an arbitrated price. The Authority considers that arbitrators have the power to dismiss vexatious disputes, or disputes that seek to usurp proper negotiations.

535. The Authority considers that the Code does not prevent the regulator from consulting with parties in the selection of an arbitrator from the panel established under section 24 of the Code. The Authority has noted BR and CBH comments supporting the involvement of parties in selection of an arbitrator.

536. The Authority considers that the WA branch of IAMA is the most appropriate local body with which the regulator should consult on the matter of appropriate arbitrators. The WA branch of IAMA has recourse to consult with the national branch or other arbitration/mediation bodies.

537. The Authority does not consider it necessary, as submitted by BR, that section 26(1) be amended to require the entity in dispute with the railway owner to also provide notice to the railway owner, in addition to the Regulator. The Regulator is not prevented from notifying the railway owner, when it is notified by the entity in dispute.

538. The Authority does not consider that additional mediation should be stipulated in the Code. Recent experience has indicated that parties are able to undertake contract mediation services in order to assist negotiations if both parties agree this is warranted.

539. The Authority agrees that information and outcomes of arbitration should remain confidential.

Part 5 – Certain approval functions of Regulator

Submissions

540. Aurizon submitted that it does not support standardised Part 5 instruments, and that these documents would be better addressed in conjunction with Development Approvals (initial submission page 14).

541. BR submitted that it does not agree with a one-size-fits-all approach to initial Part 5 instruments. BR submitted that if a new railway commences, it could adopt the form of instruments from an existing railway (initial submission page 26).

542. CBH submitted that it agrees with a consistent consultation regime on all Part 5 instruments (initial submission page 49). CBH submitted that parties should be able to negotiate variations from standard instruments where appropriate, as access seekers do not participate in the negotiation or approval of Part 5 instruments, except through the public consultation process (initial submission page 50). CBH submitted that the railway owner is limited in its capacity to “accommodate the requirements of access seekers” if all access seekers are subject to the same operating procedures.

543. Roy Hill submitted hat the ERA should accept railway owners’ proposed operating principles (Train Path Policy and Train Management Guidelines) unless these can be shown to be unfair or inefficient (initial submission page 3).

Authority considerations

544. The Authority has considered the efficacy of adopting a standard set of Part 5 instruments as a temporary measure, as a means of enabling the "access date" for new railways to be achieved, and prior to approval of alternative instruments by the Authority.

545. The Authority agrees with Aurizon and BR that a one-size-fits-all approach to Part 5 instruments is not appropriate.

546. In relation to Roy Hill's submission, the Authority currently publishes proposed operating instruments from each railway owner, and is required to accept them, either with or without amendment. If the instruments are judged to be fair and efficient, then they may be accepted unamended.

Section 48 – Railway owner must supply certain information if requested.

Submissions

547. BR submitted that the Code should limit the entities eligible under section 48 to receive copies of section 9(1) material on request, to exclude persons who cannot demonstrate that they do conduct or have a genuine intention to conduct business that requires access to the portion of the network that the information in section 9(1) relates to.

Authority considerations

548. The Authority considers that the existing confidentiality provisions provide adequate protection to the railway owner in respect of confidential information provided to the proponent in accordance with section 9(1)(c). Railway owners have demonstrated an understanding of this protection by limiting the level of detail provided to proponents, such that confidential information is not able to be made public as a result of a section 48 request.

Clause 7A Schedule 4 – Apportionment of costs of extension or expansion.

Submissions

549. TPI submitted that the wording of clause 7A of Schedule 4 is unclear on how costs of extensions or expansions should be shared (attachment to initial submission page 28). TPI submitted that clause 7A requires these costs to be apportioned in accordance with usage of the expanded infrastructure and the economic benefits derived from that use, but it is not clear (a) how the allocation of benefits should translate into a specific tariff apportionment or (b) whether the costs referred to are total costs, incremental costs, operating or capital costs.

Authority considerations

550. The Authority considers that further prescription in clause 7A of Schedule 4 is not warranted and that the form of words used in that clause anticipates the application of standard commercial principles.

551. The Authority considers that if a railway owner wishes to establish a template for the application of these principles, that it may propose a method of allocating costs in accordance with clause 7A, by providing details of that method in its costing principles.

552. The Authority notes the exclusions of clause 7A in relation to agreements that do make provision for a contribution to be made for expansions, and agreements made prior to 2009.

APPENDIX – Issues raised in submissions that are incidental to the review or irrelevant to the review

553. There were matters raised in submissions which are outside the scope of this review. That is, these matters do not relate to the effectiveness of the Code in meeting the objectives of the CPA. Some of these matters are referred to below, where the Authority considers it useful to outline why the Authority considers these matters not relevant to the Review.

554. Other, incidental, comments are also referred to in this section. These comments may relate to updates required to the Code, but not to the objectives of this review.

Initial Submissions

555. The AMEC submission did not comment on the issues identified in the Issues Paper. AMEC commented that the regime did not appear to be serving any practical purpose. AMEC re-iterated its support for the recommendations of the second review.

556. BR and Brockman provided a number of legislation updates, as follows:

- *Rail Safety Act 1998* is now *Rail Safety Act 2010*
- *Rail Safety National Law 2014* is forthcoming
- "Corporations Law" should be *Corporations Act 2011*
- *Trade Practices Act 1974* is now *Competition and Consumer Act 2010*
- IAMA joined with LEADR to become LEADR & IAMA, on 1 January 2015.

557. In respect of the above, the Authority notes that IAMA remains a separate organisation, regardless of its affiliations. The Authority also notes that in addition to the legislation updates identified above, the *Commercial Arbitration Act 1985* is now *Commercial Arbitration Act 2012*.

558. CBH provided comments on timelines and specific factors resulting in delays in the BR/CBH negotiation process. These comments are not referred to in this report.

559. DOT and TPI commented on the calculation of maintenance costs for the purposes of determining costs relevant to the floor and ceiling price tests. The Authority notes that the method of calculation of maintenance costs is not prescribed in Schedule 4 to the Code, and is the subject of railway owners' Costing Principles, which are open to review by railway owners at any time.

560. DOT commented that the current review of the Code should provide clarity and direction to the access negotiations between the lessee and users of the so-called 'Tier 3' routes. DOT commented that the withdrawal of these routes from service is in contravention of clause 6(e) of the CPA, which requires the railway owner to promote, and not hinder, access. The Authority considers that the provisions of the Code must apply equally to, and without distinction between, all routes listed in Schedule 1. The Department of Transport also commented on the effect that disclosure of railway owner information may have on perceptions of sovereign risk associated with government contracts. The Authority considers that this matter is for

consideration in the legal drafting of contracts, and is not a proper consideration in the administration of the law.

561. The Authority does not recognise any distinction, for purposes of administering the regime, between the so-called 'Tier 3' routes and any other route listed in Schedule 1 of the Code, as "Routes to which this Code applies". The categorisation of these routes as 'Tier 3' is a construction of the Strategic Grain Network Committee. The establishment of this class of route may have involved a variation to the commercial lease agreement between WestNet Rail (at the time) and the government, but did not involve a variation to the Act or the Code. Neither 'Tier 3' or 'Tier 3 route' are Code-defined terms.

562. Professor Gillooly provided a correction of fact in relation to the status of the Code as subsidiary legislation.

563. TPI commented on the application of the Code to its railway, the expectation of its 'original sponsors', and the implications for risk. These TPI comments appear to address a question of whether or not it is appropriate for access regulations to apply to the TPI railway at all. The Authority does not consider that matter relevant to this Review. As detailed by the Authority in its Section 10 decision of August 2013, the matter of managing the displacement of alternative investment proposals, costs and delays associated with negotiations, potential disputes and operating allowances are unavoidable elements of any open-access railway, and are considered normal business costs associated with owning an open access railway.

564. The Authority considers that TPI's business interests must be considered in a context where TPI (and its 'original sponsors') knew, at the time it decided to proceed with its investment in the railway infrastructure, that it would be subject to third party access proposals. In particular, in order to obtain the State's assistance with development of multi-use rail and port infrastructure, TPI made commitments to the State Government in the *Railway and Port (The Pilbara Infrastructure Pty Ltd) Agreement Act 2004*, including a commitment to operate the railway under open third party access arrangements and to use all reasonable endeavours to promote access to, and attract above-rail customers for, the railway in accordance with the Act[24] and the Code.

565. TPI commented generally on the issue of duplicability, and asserted that the NCC will adopt the Harper committee definition of 'economic to duplicate' in its 2016 assessment of whether or not the WA Rail Access Regime is effective[25] (attachment to initial submission page 10). The Authority does not consider wider issues to do with application of the regime to types of railways as relevant to this Review.

566. TPI also commented on federal regulation and the diminishing role of the ERA as an access Regulator. TPI asserted that a logical step would be for the Government to transfer all rail access regulation to the national regime. The Authority cannot comment on this assertion. The Authority notes that for as long as the TPI railway remains listed in Schedule 1 to the Code, then the Code will apply to that railway, and that if the NCC does not certify the Code as effective in 2016, then any railway currently listed in Schedule 1 to the Code will be able to be declared under Part IIIA of the *Competition and Consumer Act 2010*.

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[24] See sub-clauses 16(2)(a), (3), (5) and (7) of the TPI State Agreement.

[25] The Harper Committee recommended that the private profitability criterion for "economic to duplicate" be retained, but that the current infrastructure owner be excluded from that test..

567. The issues raised by TPI all lead to the question of whether the Code should apply to the TPI railway. TPI asserted that if the Code is not declared effective, and all infrastructure laid open to declaration, that the TPI railway would not be declared. The Authority is not able to comment on this assertion, but notes again that the question of the appropriateness of applying the Code to particular railways is a quite separate issue from the suitability of the provisions of the Code itself.

568. The Authority notes that the responsible Minister is able to reconsider the application of the Code to the TPI railway[26], such that the railway might be removed from Schedule 1 to the Code, and the commitments made by TPI in its Agreement with the State Government might become no longer binding.

569. WA Farmers commented that the legislation and the lease is not transparent. The Authority considers that the legislation is totally transparent, and that the transparency of the lease between BR and the WA Government is not relevant to the review of the Code.

Further Submissions

570. As with the initial submissions, some matters raised in further submissions were also outside the scope of this review, or relate to commercial matters that the Authority will not comment on. These matters are referred to below.

571. BR provided comments on the cost structures facing CBH for grain transport, in the context of subsidised road transport and capital investments by government.

572. BR referred to CBH's comments on delays in the BR/CBH negotiation process. BR's comments are at page 25 of its further submission and are not referred to in this report.

573. Michael Carmody's submission raised issues of freight cost quantums and road safety, which are considered outside the scope of this review. Mr Carmody also commented that the Depreciated Optimised Replacement Cost (DORC) valuation scheme should replace the current Gross Replacement Value (GRV) scheme for reasons of consistency with other regimes in Australia. Mr Carmody did not substantiate that comment.

574. Bill Cowan's submission raised issues of freight cost quantums and the freight cost component of total costs for farmers. Mr Cowan's submission also touched on the closure of the so-called 'Tier 3' routes and the management of the lease of the freight network. These matters are considered outside the scope of this review.

575. The DOT submission suggested that there may be advantages and disadvantages to various valuation schemes. DOT submitted that it supported the ERA adopting a methodology that meets an industry standard, and that the Code requires clarity on how any interim arrangements are to be dealt with. The Authority has noted these general comments, and also notes that the adoption of alternative valuation methods is not at the ERA's discretion and that the valuation scheme is mandated in Schedule 4 to the Code.

576. Lindsay Tuckwell's submission summarised some elements of the Report of the Economics and Industry Standing Committee Report on the Management of the

[26] Railways (Access) Act 1998 section 5.

Freight network lease, and provided other comments on the background to the lease. These matters are considered outside the scope of this review.

577. The WRRA submission summarised some elements of the Report of the Economics and Industry Standing Committee Report on the Management of the Freight network lease, and provided other comments on the competitiveness of the WA grain industry. These matters are considered outside the scope of this review.