Over-payment Rules

Draft

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1. Introduction

(a) Section 47(1) of the Railways (Access) Code 2000 (**Code**) requires each Railway Owner to prepare and submit to the ERA a statement of the rules (**Over-payment Rules**) that are to apply where breaches of the Ceiling Price Test occur on the part of that Railway Owner that could not reasonably be avoided.

(b) The expression "**Ceiling Price Test**" is used in clause 8 of Schedule 4 to the Code. There are two separate tests: a Ceiling Price Test that must be met for each Operator in isolation (clauses 8(1) and (2) of Schedule 4) as well as a combined Ceiling Price Test (which is the Ceiling Price Test referred to in clause 8(3) of Schedule 4).

(c) Clause 8 of Schedule 4 states that the "**Total Revenue**" earned on a particular Route must not exceed the "**Total Costs**" attributable to that Route.

(d) If an Over-payment occurs, the Over-payment is deemed to be allowable within the Code provided the following applies:

- (i) the Railway Owner can show that the Over-payment could not be reasonably avoided;
- (ii) the Over-payment is at all times within a percentage limit;
- (iii) all Over-payments are reimbursed to Operators within each successive three year period; and
- (iv) the method of reimbursing Operators follows the rules set out in these Over-payment Rules.

(e) This document outlines the Over-payment Rules that will apply to RHI. These Over-payment Rules set out a mechanism to:

- (i) calculate the amount by which Total Revenue earned on a particular Route Section exceeds the Total Costs attributable to the Route Section; and
- (ii) reimburse Operators who are provided with access under the Code to that Route Section in the event of an Over-payment.

2. Basis of Over-payment Rules

2.1. Definitions of Route and Route Section

(a) The Route Section is the basic unit to which the Over-payment Rules apply. A "**Route Section**" is a section of a Route on the railway network that has been divided for management and costing purposes.

(b) The term "**Route"** referred to in this document has the meaning ascribed in clause 8 of Schedule 4 to the Code. A negotiated route (in an Access Agreement) could equate to a Route Section (or part thereof) or be a combination of several Route Sections.

2.2. One regulatory Ceiling

(a) Each Route Section has one regulatory Ceiling that will apply to all Operators when negotiating access prices and will be the basis for determining whether Total Revenue earned on a particular Route Section has exceeded the Total Costs incurred on that Route Section.

(b) Total Costs will be calculated by RHI using methods set out in the Costing Principles, and submitted for approval by the ERA as required by clauses 9 and 10 of Schedule 4 to the Code.

2.3. What constitutes revenue in the Ceiling Price Test under clause 8 of schedule 4 to the Code?

(a) In assessing the extent of over-payments under section 47 and clause 8(1) of schedule 4 to the Code, all Regime Revenue and Non-Regime Revenue received by RHI for a Route Section, or part of a Route Section, and associated Railway Infrastructure will be included to calculate the Total Revenue attributable to that Route Section of the RHI Railway.

(b) Total Revenue is the sum of Regime Revenue and Non-Regime Revenue. Regime Revenue is all income received by RHI for the provision of access to the RHI Railway to Operators. Non-Regime Revenue may include private and government contributions in accordance with the ERA's approved set of Costing Principles to apply to RHI.

(c) Revenue from Non Regime Operators will also be included in evaluating RHI's compliance with the Floor Price Test and Ceiling Price Test. Furthermore, in assessing the extent of the Over-payment under section 47 of the Code, Non Regime Revenue from Non Regime Operators is included in the Ceiling Price Test. However, since the Code does not provide Non Regime Operators a legal entitlement to any refund of any Over-payment, such Over-payments will be retained by RHI unless otherwise specified in an access agreement with the Non Regime Operator.

2.4. Breaches of the Ceiling Price Test

(a) Section 47(1) of the Code states that the Over-payment Rules are to apply where breaches occur on the part of the Railway Owner that could not reasonably be avoided.

(b) RHI will assess Total Revenues earned on particular Route Sections on a periodic basis to determine whether or not there is likely to be a breach of the Ceiling Price Test. Where it is possible to forecast potential Over-payments, RHI will seek to negotiate new access prices with affected Operators to ensure that Revenue remains within the Ceiling.

(c) If breaches of the Ceiling Price Test occur as a result of variations in traffic volume or revenues that are deemed to be temporary or unpredictable in nature, and if RHI has Access Agreements with Operators under the Code, then RHI will advise the ERA of such circumstances and will follow the procedure set out in these rules to deal with such Over-payments.

2.5. Over-payments and Under-recoveries

(a) For the purposes of these rules, the expression "**Over-payment**" means the amount of Total Revenue received by RHI for a Route Section that exceeds the Total Costs attributed to the Route Section for a one-year period.

(b) Conversely, the expression "**Under-recovery"** refers to a situation where the Total Revenues to the Railway Owner on a Route Section for a one-year period are less than the Total Costs attributed to that Route Section.

(c) The ERA has determined that net Over-payments will be assessed over a successive three-year period, during which Over-payments in a particular year may be balanced out by Under-recoveries in a subsequent year or preceding year within the three-year period. Net Over-payments in a three-year period will be paid back to Operators in accordance with these rules.

(d) Conversely, where an Under-recovery occurs the Operator is not required to pay RHI compensation for such Under-recovery. However, where a net Under-recovery occurs in a particular 3 year period, there are circumstances under which RHI will be allowed to carry-over this net Under-recovery as an accounting balance into the subsequent three-year period, which may be used to offset Over-payments in that subsequent three-year period. The circumstances where this will be allowed to occur are set out in example 4 in section 4 of these rules.

(e) Example 4 refers to a situation where, as a result of having to reimburse Operators during the three-year period because the Over-payment is greater than 10 per cent of the Ceiling (refer to the Over-payment Rule 5 in section 3), there are insufficient funds in the interest bearing account for RHI to recoup an Under-recovery that has occurred during the same three-year period. In this instance, RHI will put a case to the ERA to carry the Under-recovery credits over to the next three years up to the amount RHI has been required to refund to Operators as a result of exceeding the 10 per cent limit. If allowed, the carry forward will only apply for that one additional successive three-year period.

2.6. Allocation of Access Revenue

(a) Under section 9(1)(c)(i) of the Code, RHI is only required to provide one Floor Price and one Ceiling Price for a proposed access to a Route (i.e. from origin to destination) even though the access proposal could traverse multiple Route Sections.

(b) Since price is determined on a Route or multiple Route basis, and Total Costs are determined on a Route Section basis, it is necessary to distribute Total Revenue earned over one of more Routes to individual Route Sections. The distribution of such Total Revenue will be done according to the following rules:

  (i) Total Revenue derived from a Route can only be allocated to the Route Sections on that Route; and

  (ii) RHI will allocate Total Revenue to cover the costs attributed to the applicable Route Sections in the following order:

    (A) incremental costs against all applicable Route Sections;

    (B) up to the Ceiling on all applicable branch or feeder (dedicated) Route Sections; and

    (C) up to the Ceiling on all applicable shared Route Sections.

(c) The justification for the ordering of the allocation process is based on the following economic principles:

  (i) first, to avoid cross subsidisation between Route Sections, Total Revenue allocated to each Route Section must at least cover the incremental cost; and

  (ii) second, recovery of capital costs on branch or feeder lines ranks ahead of shared lines on the basis that there is no other traffic on these lines to fund the dedicated infrastructure and unless those costs are covered the line may close.

(d) If RHI and the Operators have reached agreement to a different Total Revenue allocation arrangement in an Access Agreement that arrangement will prevail.

2.7. Allocation of Non-Regime Revenue

(a) Non-Regime Revenue (private or government contributions) will only be allocated to the Route Section for which the contribution was received.

(b) Where a capital contribution is made whether it be private or government, the value of the contribution to be used in the Ceiling Price Test is to be expressed as an annualised amount taking into account the Total Cost, expected life and Weighted Average Cost of Capital determined by the ERA. Where capital is spent over multiple Route Sections, the actual expenditure will be allocated appropriately into each Route Section based on the actual expenditure on each individual Route Section at the time it was incurred. The allocation principles for Regime Revenue do not apply to Non-Regime Revenue.

3. Allocation of an Over-payment

The following process will apply in the allocation of an Over-payment on a Route Section:

(a) Where an Over-payment on a Route Section results from the Ceiling Price Test, all Operators who have negotiated their Access Agreement inside the Code who have contributed to the Total Revenue on that Route Section will be entitled to a share of the Over-payment;

(b) The proportion of Over-payment due to each Operator will be determined by each Operator’s annual contribution to Regime Revenue and Non Regime Revenue above the floor accumulated on a Route Section divided by the aggregate of all Operators’ Regime Revenue and the Non Regime Revenue above the floor recorded on the Route Section over the preceding 12-month period from July to June. An Operator paying only the incremental cost on the Route will not be considered for any refund as this would compromise the Floor Price Test in the Code.

4. The Over-payment Rules

(a) These Over-payment Rules will commence on 1 January 2017.

(b) These Over-payment Rules apply where breaches of the Ceiling could not reasonably be avoided.

(c) RHI is to calculate Over-payments in respect of each Route Section for a financial year.

(d) In these Over-payment Rules, a financial year is the year beginning on 1 July and ending on 30 June.

(e) Where an Over-payment is greater than the 10 per cent amount allowable for breaches of the Ceiling for that Route Section for the financial year, RHI must reimburse the Operators on that Route Section for the amount of the Over-payment calculated according to the pro-rata formula in rule (f) by 30 September of the following financial year.

(f) Payments to Operators (who have negotiated their Access Agreement inside the Code) will be apportioned based on the total annual Regime Revenue above the Floor Price by each Operator on the Route. The following formula is to apply:

$$\frac{\text{An Operator's annual Regime Revenue above the Floor Price paid plus annual Non Regime Revenue received by the Railway Owner for the Route Section}}{\text{Total annual Regime Revenue above the Floor plus total annual Non Regime Revenue for the Route Section}} \times \text{Amount of net Over-payment plus interest accrued for the Route Section}$$

Notes:

(i) Includes Regime and Non-Regime Operators.

(ii) Only Operators who have negotiated inside the Code are eligible for a share of the net Over-payment as prescribed in the Code.

(iii) Each Non Regime Operator is entitled to a share of the net Over-payment provided that its access agreement contains a provision which entitles that Non Regime Operator to any Over-payment. Accordingly, their share will be calculated using the formula in its access agreement.

(g) RHI is to establish in its accounting records an account to be known as the “Over-payment Account”.

(h) The Over-payment Account is to be credited with all Over-payments that are equal to or less than the 10 per cent amount allowable for breaches of the Ceiling Price level for the financial year.

(i) Any Over-payment for the previous financial year shall be calculated by 31 July of each year and credited to the Over-payment Account. The Over-payment will be treated as if were credited to the Over-payment Account on 1 July of each year.

(j) RHI will also credit to the Over-payment Account any interest actually paid on the amount standing to the credit of the Over-payment Account and calculated daily on the balance from time to time standing to the credit of the Over-payment Account.

(k) Interest paid and calculated in accordance with paragraph (j) of these notes will be distributed to Operators on the same basis as other amounts are distributed to Operators.

(l) At the end of each three-year period the amount standing to the credit of the Over-payment Account (due to Operators, refer to section 4) must be distributed by RHI to Operators (who have negotiated inside the Code) for the amount of the Over-payment calculated according to the pro-rata formula in rule (f) by 30 September.

(m) Payments to Non-Regime Operators will be retained by RHI, subject to the terms of any access agreement to the contrary.

(n) No payment is to be made from the Over-payment Account without the prior approval of the ERA.

(o) If there are Operators with Access Agreements under the Regime, then the Over-payment Accounts must be audited each year by an Independent Auditor appointed by RHI at RHI's expense. The audit must be completed by 31 August. The audit will ensure that each of the amounts credited to the Over-payment Account is correct and in respect of the audit for the year which is the end of the three-year period that the interest credited and payment of amounts from the Over-payment Account is appropriate and consistent with these Over-payment Rules. The auditor's report is to be provided to the ERA as soon as it is completed, and is to be confirmed by the ERA.

(p) If the audited and confirmed Over-payment is different to that calculated by RHI in rule (i) or rule (j), an adjustment is to be made to the Over-payment Account as if it occurred on 31 July.

(q) RHI must enter into a legally binding agreement with those Operators with Access Agreements negotiated inside the Code. That agreement should contain the provisions described in part 1 of schedule 1 to these Over-payment Rules. The agreement must remain in force and effect and bind the parties to the agreement so long as any amount remains standing to the credit of the Over-payment Account and has not been distributed in accordance with rule (l).

5. Application of the Over-payment Rules

(a) The examples shown in Table 1 below demonstrate how the Over-payment Rules apply. Years 1, 2 and 3 show Over-payments and Under-recoveries (denoted by a minus sign) for a Route Section. All Operators are also assumed to be in the Regime and have met their Floor Costs.

(b) The annual interest rate assumed is 5% compounded which, given the deposit occurs annually, will only apply to Year 1 and Year 2 deposits. In the examples below, it is also assumed that the Ceiling Cost for the Route Section is $100,000, and Over-payments in excess of $10,000 are reimbursed immediately.

(c) Example 4 refers to the one exception in which the carrying over of Under-recovery credits to the next three- year period may apply. In this example, RHI incurred a breach of 20 per cent above the Ceiling in Year 1. At the end of Year 1, it has to reimburse to Operators $10,000 and deposit $10,000 into the interest bearing account. However, in Year 2, RHI incurred an Under-recovery of 15 per cent. Assuming that the revenue from access is exactly at the Ceiling in Year 3, there are now insufficient funds to compensate RHI in the interest bearing account for the three-year period. In this example, the ERA may approve a carry-over in under-recovery credits of $5,000.

(d) If a Non Regime Operator has negotiated access outside the Regime then its share of the Over-payments would go to RHI. For instance, if in example 3 that Route Section comprised only Non-Regime Operators then the total accrued principal in the interest bearing account (i.e. $15,000), and interest earned (i.e. $1,275), would go to RHI.

Table 1. Examples illustrating operation of the trust account

	Example 1	Example 2	Example 3	Example 4
*Net annual over or **under** payment*				
Year 1	$10,000	$10,000	$10,000	$20,000
Year 2	**- $10,000**	**- $30,000**	$5,000	**-$15,000**
Year 3	$0	$0	**- $10,000**	$0
Total of the three-year period	$0	**- $20,000**	$5,000	$5,000
Reimbursed to Operators	$0	$0	$0	$10,000
Accrued Principal in Trust	$10,000	$10,000	$15,000	$10,000
Accrued Interest in Trust	$1,025	$1,025	$1,275	$1,025
Refund to RHI………..	$10,000	$10,000	$10,000	$10,000
Refund to Operators	$1,025	$1,025	$6,275	$1,025
Carry forward of credit	$0	$0	$0	$5,000

6. Compliance and review

(a) Stakeholders have the ability to express any concern to the ERA which may arise at any time and the ERA will investigate such claims.

(b) The ERA has the power under the Code to amend the Over-payment Rules at any time and Access Seekers and Operators can at any time request the ERA to consider amendments.

(c) The ERA can also commission special audits to monitor RHI's compliance with the Over payment Rules at any time on any issue relating to these Over-payment Rules where it takes the view (acting reasonably) that additional assurance is required.

7. Definitions

In these Over-payment Rules the following terms have the following meanings:

Access Agreement means an agreement in writing under the Code between RHI and an entity for access to the RHI Railway by that entitv.

Access Related Function means the functions involved in arranging the provision of access to Railway Infrastructure under the Code.

Access Seeker means a person seeking access to the RHI Railway.

Act	means the *Railways (Access) Act 1998* (WA).
Capital Costs	means those costs which fall within the meaning of the term "Capital Costs" in section 2 of the Costing Principles.
Ceiling	means an amount equal to Total Costs.
Ceiling Price	has the same meaning as in clause 9(4) of the Code.
Ceiling Price Test	means the test in clause 8 of schedule 4 of the Code to determine the maximum price which may be paid by an Operator for access to a Route and associated railway infrastructure.
Code	means the Railways (Access) Code 2000 established under the Act
Costing Principles	means the principles, rules and practices determined by the ERA in accordance with section 46 of the Code.
Economic Regulation Authority (ERA)	means the Economic Regulation Authority established by the Economic Regulation Authority Act 2003.
Floor	means the sum equal to the total incremental costs.
Floor Price	has the same meaning as in clause 9(4) of the Code.
Floor Price Test	means the test set out in clause 7 of schedule 4 of the Code to determine the minimum price which may be paid by an Operator for access to a Route and associated railway infrastructure.
incremental costs	means incremental costs as defined in clause 1 of schedule 4 to the Code.
Independent Auditor	means an auditor independent of RHI approved by the ERA.
Non-Regime Operator	means an entity to which RHI provides access to the RHI Railway under arrangements outside the Code.
Non-Regime Revenue	means revenue other than Regime Revenue received by RHI that may include private and government
Operating Costs	means the those costs which fall within the meaning of the term "Operating Costs" in section 3 of the Costing Principles.

Operator	means an entity to which RHI provides access to the RHI Railway under an Access Agreement.
Overhead Costs	means those costs which fall within the meaning of the term "Overhead Costs" in section 4 of the Costing Principles.
Over-payment	is defined in section 2.5(a) of these Over-payment Rules.
Railway Infrastructure	has the same meaning as in section 3 of the Code.
Railway Owner	means the person having the management and control of the use of the Railway Infrastructure.
Regime Revenue	means revenue received by RHI from Operators for track access under an Access Agreement.
RHI	means Roy Hill Infrastructure Pty Ltd ABN 60 130 249 633.
RHI Railway	means the Railway and Railway Infrastructure owned and controlled by RHI to which access has or can be
Route	is defined in section 2.1(b) of these
Route Section	is defined in section 2.1(a) of these Overpayment Rules.
Total Costs	means, as defined in clause 1 of schedule 4 to the Code, the total of all: (a) Operating Costs; (b) Capital Costs; and (a) Overhead Costs, attributable to the performance of the Railway Owner's Access Related Functions incurred by either the Railway Owner or an associate.
Total Revenue	means Regime Revenue and Non-Regime Revenue.
Under-recovery	is defined in section 2.5(b) of these Over-payment Rules.

Schedule 1

To be attached to RHI's track Access Agreement as a schedule for Operators who have negotiated an Access Agreement inside the Access Regime.

Part 1 – Prescribed Provisions

1. Establishment of Over-payments Account

Within seven (7) days of the date of this agreement RHI must, in accordance with rule 7 of the Over-payment Rules, establish within its books of account an account to be styled Over-payments Account and must maintain that account at all times during the continuation of this agreement.

2. Operation of Over-payments Account

RHI must at all times operate the Over-payments Account in a manner consistent with the requirements of the Over-payment Rules and must make payments to the Operator in a manner and at the times contemplated by the Over-payment Rules.