



OVERPAYMENT RULES

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1. INTRODUCTION

Section 47(1) of the Railways (Access) Code 2000 (“the Code”) requires each Railway Owner to prepare and submit to the ERA a statement of rules (“the 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.

The Ceiling Price Test is defined under Schedule 4 Clause 8 of the Code, and refers to a Ceiling Price Test that must be met for each Operator in isolation (sub-clause 1 and 2) as well as a combinatorial Ceiling Price Test (which is the Ceiling Price Test referred to in sub-clause 3). Clause 8 states that the Total Revenue earned on a particular route must not exceed the Total Costs attributable to that route.

In the event that over-payment occurs, these overpayments are deemed to be allowable within the Code provided the following applies:

1. The Railway Owner can show that over-payment could not be reasonably avoided;
1. Over-payment must be at all times within a percentage limit;
2. All over-payments must be cleared (reimbursed to Operators) within each successive 3 year period; and
3. The method of reimbursing Operators must follow rules set out in the over-payment rules.

This document outlines the Overpayment Rules that will apply to West Net Rail (WNR). These Over-payment Rules provide a mechanism to:

- Calculate the amount by which Total Revenue earned on a particular route exceeds the Total Costs attributable to the route section and infrastructure; and
- Reimburse Operators who are provided with access under the Code to that route section in the event of an over-payment.

2. BASIS OF THE OVER-PAYMENT RULES

2.1 Definition Of Route And A Route Section

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.

The following division of the freight network has been proposed by WNR and approved by the ERA. These route sections were selected on the basis of

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differences in track characteristics and traffic densities, and may be redefined over time, subject to approval by the ERA.

Forrestfield to Kalgoorlie (eight route sections)

Forrestfield – Midland

Midland - Millendon Junction

Millendon Junction - Toodyay West

Toodyay West - Avon Yard

Avon Yard - West Merredin

West Merredin - Koolyanobbing

Koolyanobbing - West Kalgoorlie

West Kalgoorlie - Kalgoorlie

Kalgoorlie to Esperance (four route sections)

West Kalgoorlie - Hampton

Hampton - Kambalda

Kambalda - Salmon Gums

Salmon Gums - Esperance

Kalgoorlie to Leonora (two route sections)

Kalgoorlie - Malcolm

Malcolm - Leonora

Kwinana to Bunbury Inner Harbour (eight route sections)

Kwinana - Mundijong Junction

Mundijong Junction - Pinjarra

Pinjarra - Alumina Junction

Alumina Junction - Pinjarra South

Pinjarra - Wagerup

Wagerup - Brunswick Junction

Brunswick Junction - Picton Junction

Picton Junction - Bunbury Inner Harbour

The term “route” referred to in this document has the meaning ascribed in Clause 8 Schedule 4 of 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

Each route section has one regulatory Ceiling that will apply to all Operators when negotiating access prices, and will be the basis of determining whether Total Revenue earned on a particular route section has exceeded the Total Costs.

These Total Costs will be calculated by WNR 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 of the Code.

2.3 What constitutes revenue in the Ceiling Price Test under Clause 8 of Schedule 4 in the Code

In assessing the extent of over-payments under Section 47 and Clause 8(a), Schedule 4 of the Code, all access and non-access income received by WNR 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 network.

Total Revenue is the sum of Access Revenue and Non-Access Revenue.

Access Revenue is deemed to be all income received by WNR for the provision of track access to the network, to Operators

Non-access revenue may include private and government contributions in accordance with the ERA’s approved set of Costing Principles to apply to WestNet Rail.

Access Revenue from Operators with Access Agreements negotiated outside the Regime (“non- Regime operators”) will also be included in evaluating WNR’s compliance with the Floor Price Test and Ceiling Price Test of the Code. Furthermore, in assessing the extent of over-payment under Section 47 of the Code, Access Revenue from non-Regime operators are included in the Ceiling Price Test. However, since the Code does not provide non-Regime operators a legal entitlement to any refund for any over-payment, such over-payments will be returned to WNR unless otherwise specified in an Access Agreement with an Operator.

2.4 Breaches of the Ceiling Price Test

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

WNR will assess revenues earned on particular route sections on a periodic basis to determine whether there is likely to be a breach of the Ceiling Price Test. Where it is possible to forecast potential over-payments, WNR will seek to negotiate new access prices with affected Operators to ensure that Total Revenue remain within the Ceiling.

If breaches of the Ceiling Price Test occur as a result of variations in traffic volume or revenue that are deemed to be temporary or unpredictable in nature, then WNR will advise the ERA of such circumstances and will follow the procedure set out in these over-payment rules to deal with such over-payments.

2.5 Over-payments and under-recoveries

Over-payment is defined as the amount of Total Revenue received by WNR for a route section that exceeds the Total Costs attributed to the route section for a one-year period.

Conversely, “under-recovery” refers to a situation where the Total Revenue to the Railway Owner on a route section for a one year period are less than the Total Costs attributed to that route section.

The ERA has determined that net over-payments will be assessed over a successive three year period, during which overpayments in a particular year may be balanced out by under-recoveries in a subsequent year. Net over-payment in a three year period will be paid back to Operators according to these Over-payment Rules.

Conversely, where under-recovery occurs the Operator is not required to pay WNR compensation for such under-recovery. However, where a net under-recovery occurs in a particular 3 year period, there are circumstances under which WNR will be allowed to carry-over this net under-recovery as an “accounting balance” into the subsequent 3 year period, which may be used to offset overpayments 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 Over-Payment Rules.

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

2.6 Allocation of Access Revenue

Under Section 9(1)(c)(i) of the Code, WNR is only required to provide one Floor and one Ceiling price for a proposed access to a route (ie. from origin to destination) even though the access proposal could transverse over multiple route sections as defined in the Code.

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 Access Revenue earned over a particular route(s) to individual route sections. The distribution of such Access Revenue will be done according to the following rules:

1. Access Revenue derived from a route can only be allocated to the route sections on that route.
2. WNR will allocate Access 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.

The justification for the ordering of the allocation process is based on economic principles. First, to avoid cross subsidisation between route sections, Access Revenue allocated to each route section must at least cover the Incremental Cost. 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.

Where WNR and the Operators have reached agreement to a different Access Revenue allocation arrangement in an Access Agreement that arrangement would prevail.

2.7 Allocation of Non-Access revenue

The allocation of Non-Access revenue, private or government contributions will only be allocated to the route section for which the contribution was received for. The allocation principles for Access Revenue do not apply to Non-Access Revenue.

2.8 Allocation of an over-payment

The following process will apply in the allocation of an over-payment on a route section:

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1. If an Operator can be identified as being responsible for triggering the over-payment, then the overpayment will be allocated back to all Operators on the entire route of that Operator.
2. If more than one Operator can be identified as being responsible for triggering the over-payment, then the over-payment will be allocated back to all Operators on all of the routes of those Operators.
3. If it is not possible to single out the Operators responsible, then an assumption will be made that the over-payments are the result of all Operators' payments on that route section. In such cases the over-payment will be allocated back to all Operators on all of the routes of those operators that share that route section.

The repayment will be apportioned based on the total annual Access Revenue received above the Floor for access by each Operator on the route as a proportion of the Total Access Revenue above the Floor for the route section. 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.

3. THE OVERPAYMENT RULES

1. The Over-payment Rules commenced on 1 July 2003.
2. The Over-payment Rules apply where breaches of the ceiling could not reasonably be avoided.
3. WNR is to calculate over-payments in respect of each route section for a financial year.
4. In these overpayment rules, financial year is the year beginning on 1 July and ending on 30 June.
5. Where an over-payment is greater than the 10 percent amount allowable for breaches of the Ceiling for that route section for the financial year, WNR must reimburse the Operators on that route section for the amount of the over-payment calculated according to the pro-rata formula in paragraph 6 by 30 September of the following financial year.
6. Payments to Operators (who have negotiated their Access Agreement inside the Code) will be apportioned, based on the total annual Access Revenue above the Floor by each Operator on the route. The following formula is to apply:

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$$\frac{\text{An Operators}^{(d)} \text{ annual Access Revenue above the Floor}}{\text{Total annual Access Revenue}^{(a)} \text{ above the Floor}} \times \text{Amount of net over-payment}$$

Notes:

- (a) Includes Regime and non-Regime operators.
- (b) Only Operators who have negotiated inside the Code are eligible for a share of the net over-payment

7. WNR is to establish in its accounting records an account to be known as the Over-payment Account.
8. The Over-payment Account is to be credited with all over-payments that are equal to or less than the 10 percent amount allowable for breaches of the Ceiling level for the financial year.
9. 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 overpayment will be treated as if were credited to the Over-payment Account on 1 July of each year.
10. WNR will also credit to the Over-payment Account interest calculated daily on the balance from time to time standing to the credit of the Over-payment Account.
11. Interest is to be credited at a rate equal to the 10 year long term bond rate as at 30 June each year but if 30 June falls on a day which is not a business day then the rate published on the first day after that date.
12. At the end of the 3 year period commencing 1 July 2003 and the end of each subsequent 3 year period the amount standing to the credit of the Over-payment Account (due to Operators, refer Section 4) must be distributed by WNR to Operators (who have negotiated inside the Code) for the amount of the over-payment calculated according to the pro-rata formula in paragraph 6 by 30 September.
13. Payments in respect of non-regime Operators will be retained by WNR, subject to the terms of any Access Agreement to the contrary.
14. No payment is to be made from the Over-payment Account without the prior approval of the ERA.
15. The Over-payment Accounts must be audited each year by an independent auditor appointed by WNR at WNR'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 3 year period that the interest credited and payment of amounts from the Over-payment Account is appropriate and consistent with the Over-payment Rules. The auditors report is to be provided to the ERA as soon as it is completed, and is to be confirmed by the ERA.

16. If the audited and confirmed over-payment is different to that calculated by WNR in paragraph 9 or 10, an adjustment is to be made to the Over-payment Account as if it occurred on 31 July.
17. WNR must enter into a legally binding agreement with those Operators with Access Agreements negotiated inside the Code and the person or persons described in part 1 of Schedule 1 to these Over-payment Rules. That agreement should contain the provisions described in Part 2 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 paragraph 12.

4. APPLICATION OF THE OVER-PAYMENT RULES

The examples shown in Table 1 below demonstrate how these 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.

The annual interest rate assumed is 5% compounded, which given the deposit occurs annually would only apply to year one and two deposits. It is also assumed that the Ceiling cost for the route section in the examples below is \$100,000, and over-payments in excess of \$10,000 are reimbursed immediately.

Example 4 refers to the one exception the carrying over of under-recovery credits to the next three-year period may apply. In this example, WestNet incurred a breach of 20 percent above the ceiling in year 1. At the end of year 1, it has to reimburse operators \$10,000 and deposit \$10,000 into the interest bearing account. However, in year 2, WestNet incurred an under-recovery of 15 percent. Assuming that the revenue from access is exactly at the ceiling in year 3, there are now insufficient funds to compensate WestNet 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.

If an Operator has negotiated access outside the Regime then its share of the overpayments would go to WestNet. For instance, if in Example 3 that route section comprised only non-Regime operators then the total accrued principal in the interest bearing account, ie. \$15,000, and interest earned, ie. \$1,275, would go to WestNet.

Table 1. Examples illustrating operation of the trust account

Over Payment Rules

	Example 1	Example 2	Example 3	Example 4
<i>Net annual over or under payment</i>				
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
<i>Total of the 3 year period</i>	\$0	- \$20,000	\$5,000	\$5,000
Reimbursed to operators	\$0	\$0	\$0	\$10,000
<i>Accrued Principal in Trust</i>	\$10,000	\$10,000	\$15,000	\$10,000
<i>Accrued Interest in Trust</i>	\$1,025	\$1,025	\$1,275	\$1,025
<i>Refund to WNR</i>	\$10,000	\$10,000	\$10,000	\$10,000
<i>Refund to operators</i>	\$1,025	\$1,025	\$6,275	\$1,025
<i>Carry forward of credit</i>	\$0	\$0	\$0	\$5,000

5. REVIEW AND CONSULTATION

WestNet will review the Overpayment Rules every third year after the ERA's approval of this document to determine whether any amendments are required.

WestNet's compliance with the Overpayment Rules will be subject to an annual independent external audit. The ERA may select and manage the auditor with costs paid by WestNet. The ERA will approve the scope of the audit and the final audit report will be made available to the ERA and access proponents.

6. DEFINITIONS

Access Agreement Means an agreement entered into by an Operator and WestNet Rail governing access for the Operator to run services on the Network.

Access Related Function Means the functions involved in arranging the provision of access to Railway

Over Payment Rules

	Infrastructure under the Code
Access Revenue	Means revenue received by WestNet from Operators for track access, under an Access Agreement.
Act	Means “The Railways (Access) Act 1998”
Ceiling	Means the sum equal to the Total Costs
Ceiling Price Test	Means an Operator (or group of Operators) that is provided with access to a route and associated Railway Infrastructure whom must pay for the access not more than the Total Costs attributable to that route and that 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.
Floor	Means the sum equal to the total Incremental Costs.
Floor Price Test	Means a Operator that is provided access to a route and associated Railway Infrastructure must pay for the access not less than the Incremental Costs resulting from its operations on that route and use of that infrastructure.
Incremental Costs	Means Incremental Costs as defined in Clause 1, Schedule 4 of the Code

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Network	Means the track and infrastructure controlled by WestNet to which access has or can be granted under an Access Agreement.
Non-Access Revenue	Means revenue received by WestNet that may include private and government contributions in accordance with the ERA's approved set of Costing Principles to apply to WestNet Rail.
Operator	Means the Operator or Operators which have access to the WestNet Network under an Access Agreement.
Railway Infrastructure	Has the same meaning assigned to Railway Infrastructure in Section 3 of the Code.
Railway Owner	Means the person having the management and control of the use of the Railway Infrastructure
Economic Regulation Authority (ERA)	means the Western Australian Independent Rail Access Regulator under Section 13 of the Act.
Total Costs	Means the total of all: <ul style="list-style-type: none">• operating costs;• capital costs; and• overheads attributable to the performance of the Railway Owner's access related functions whether by the Railway Owner or

an associate

as defined in Clause 1, Schedule 4 of the Code.

Total Revenue Means Access Revenue and Non-Access Revenue.

WestNet Means WestNet Rail Pty Limited.

SCHEDULE 1

TO BE ATTACHED TO WESTNET'S TRACK ACCESS AGREEMENT AS A SCHEDULE FOR OPERATORS WHO HAVE NEGOTIATED AN ACCESS AGREEMENT INSIDE THE REGIME

PART 1 – ADDITIONAL PARTIES

AUSTRALIAN RAILROAD GROUP PTY LTD (A.C.N. 080 579 308) OF 2-10 Adams Drive Welshpool 6106 in the said State (being hereinafter in this Schedule referred to as the "Guarantor")

PART 2 – PRESCRIBED PROVISIONS

1. Establishment of Over-payments Account

Within seven (7) days of the date of this agreement WestNet must, in accordance with Rule (4) of the Over-payments Rules, establish within its books of account an account to be styled "Over-payments Account" and must maintain at all times during the continuation of this agreement.

2. Operation of Over-payments Account

WestNet 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.

3. Guarantee and Indemnity

In consideration of WestNet and the Operator entering into this agreement:

- (1) The Guarantor guarantees the due and punctual payment by WestNet of the payment to be made by WestNet to the Operator pursuant to the Over-payment Rules.
- (2) The Guarantor agrees that if WestNet shall go into liquidation the following provisions shall apply:

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- (a) the Guarantor will not prove in such liquidation in competition with the Operator to the extent of any amount due and payable to the Operator from the Over-payments Account.
- (b) The Guarantor will forthwith if required by the Operator in writing prove in any such liquidation for all monies owed by the Guarantor to Operators hereunder in such event will not exercise or attempt to exercise any right of set-off against or realise any security taken from WestNet;
- (c) Moneys recovered by the Guarantor from any such liquidation shall be received and held in trust for the Operator to the extent of the unsatisfied liability of the Guarantor hereunder;
- (d) The Guarantor authorises the Operator to prove for all moneys which are payable by WestNet to the Guarantor and to retain and carry to a suspense account and appropriate at the discretion of the Operator any amounts received until the Operator shall with the aid thereof have been paid the whole of the amounts payable to it by WestNet pursuant to the Over-payment Rules; and
- (e) The Guarantor waives in favour of the Operator all rights whatsoever against WestNet so far as necessary to give effect to anything contained in this agreement.