

Issues Paper

Review of the Requirements for Railway Owners to Submit
Floor and Ceiling Cost Proposals.

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Economic Regulation Authority



WESTERN AUSTRALIA

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Overview

1. The Economic Regulation Authority (Authority) administers the *Railways (Access) Act 1998* (Act) and the *Railways (Access) Code 2000* (Code). The Code is a requirement of the Act and both became effective in 2001.
2. The Authority's role is to oversee, monitor and enforce compliance with the Act and the Code. The rail network and types of infrastructure subject to the Regime are defined in Schedule 1 of the Code.
3. Pursuant to the requirements of Clauses 9 and 10 of Schedule 4 of the Code, a Railway Owner must prepare proposed ceiling (maximum) and floor (minimum) costs applicable to those sections of their network on which an access proposal (as defined in Section 8 of the Code) is likely to be made (Clause 9) or is actually made (Clause 10).
4. The Authority reviews the Railway Owner's proposal and makes its own determination on the floor and ceiling costs to apply to the route sections subject to the likely or actual access proposal.
5. The Code refers to the Railway Owners' proposed floor and ceiling costs as 'initial determinations'. The Authority has adopted the convention of referring to these proposed costs as 'floor and ceiling cost proposals' in order to avoid confusion between the Railway Owner's initial determination and the Authority's determination of floor and ceiling costs.
6. The Authority has previously reviewed the requirements for the Public Transport Authority to submit floor and ceiling cost proposals. In 2009, following public consultation, the Authority decided that it would not undertake future reviews of PTA's floor and ceiling costs, except where required under Clause 9 or Clause 10, Schedule 4 of the Code in response to an actual or expected proposal by an access seeker.
7. Documents relating to that review may be found on the Authority's website, at: http://www.erawa.com.au/3/1114/48/compliance_arrangements_public_transport_authorit.pm
8. The Authority is currently reviewing the requirements for WNR and TPI to submit floor and ceiling cost proposals. Some issues associated with a change in these requirements are outlined in this issues paper. The potential changes subject to this review would not involve any change to the existing rail access legislation.
9. The purpose of this paper is to provide background information on this matter to assist interested parties in making submissions to the Authority. Following the receipt of these submissions, the Authority will make a final decision on the requirements for Railway Owners to submit floor and ceiling cost proposals.
10. Further changes to compliance arrangements for Railway Owners, such as review periods for Part 5 Instruments, are being addressed in the Authority's current *Review of the Railways (Access) Code 2000*. The changes in compliance arrangements contemplated in that Review require amendment to legislation.

The WA Rail Access Regime and legislative obligations on Railway Owners

11. The railway network covered by the Regime is set out in Schedule 1 of the Code and includes 5,000 route kilometres of rail track the in south-west of Western Australia, being the regional freight railway network operated by WestNet Rail (WNR) and the urban passenger network operated by the Public Transport Authority (PTA). The railway operated by The Pilbara Infrastructure (TPI) into Port Hedland is also included in Schedule 1 of the Code.
12. Section 28 of the Act requires that Railway Owners must prepare a Segregation Arrangements document, which outlines how a Railway Owner will 'ring-fence' its below-rail and above-rail operations (where the Railway Owners also operates its own rolling stock on the railway) such that third parties seeking access to the rail network are not unfairly disadvantaged compared with the Railway Owner's above-rail operation. The Segregation Arrangements must provide for the key elements of protection of confidential information, avoidance of conflict of interest, duty of fairness, and maintenance of separate accounts and records.
13. In addition to the requirement to segregate as outlined in Section 28 of the Act, Part 5 of the Code details requirements to prepare four regulatory instruments, referred to collectively as 'Part 5 instruments'. The four Part 5 instruments are the Train Management Guidelines, the Train Path Policy, the Costing Principles and the Over-payment Rules. Railway Owners must prepare documents demonstrating their compliance with the requirements of the Code and submit these to the Authority for approval.
14. This current review does not contemplate any amendment to these legislative requirements.

Current arrangements for submission of floor and ceiling cost proposals by Railway Owners

15. The Code contemplates a determination of floor and ceiling costs being made by the Authority under three clauses, as following:
 - Clause 9 '*Determination of costs by Regulator*' – applies if the Regulator considers it likely that a proposal will be made in respect of a route section;
 - Clause 10 '*Determination of costs where clause 9 does not apply*' – applies if a proposal has been made and clause 9 does not apply; and
 - Clause 12 '*Review and redetermination of costs*' – relates to a situation where the Regulator considers there has been a material change in circumstances and that a revisiting of a previous floor and ceiling cost determination is warranted.
16. Railway Owners are therefore required to submit floor and ceiling cost proposals in response to an actual or likely receipt of an access proposal. The Authority is required to make a determination on those proposed costs under Clauses 9 or 10 of Schedule 4 of the Code, as appropriate.

17. The frequency of the Authority's review of these regulatory instruments is not set out in the legislation. Rather, periodic review of floor and ceiling cost proposals are mandated in the Costing Principles approved for each Railway Owner and in the determinations published by the Authority.
18. The requirement for floor and ceiling costs to be escalated in accordance with annual changes in CPI and the WACC is not a requirement of the legislation. This requirement is mandated in the Railway Owners' approved Costing Principles.
19. WNR first submitted floor and ceiling cost proposals in January 2003, for 23 route sections. These 23 route sections were nominated as those considered likely by the Regulator to be subject to an access proposal under the Code. In 2003, the Regulator was the Office of the Rail Access Regulator (ORAR). The determination of floor and ceiling costs by the Regulator was therefore made under Clause 9 of the Code in that first instance.
20. Each subsequent determination on floor and ceiling costs by the Authority has required that WNR resubmit floor and ceiling cost proposals for these nominated route sections at regular three yearly intervals. The resubmission of floor and ceiling cost proposals is also mandated in WNR's approved Costing Principles (Section 5.1).
21. WNR has subsequently nominated route sections to be added and removed from the list of route sections considered likely to be subject to an access proposal, and most recently (2008) submitted floor and ceiling cost proposals for 53 route sections. WNR and the Authority have liaised closely on the appropriateness of changes to these nominated route sections.
22. In summary, the submission of floor and ceiling cost proposals by WNR was initiated by the Regulator under Clause 9 of the Code, and resubmission has been mandated in each of the Regulator's subsequent determinations and in WNR's Costing Principles, as an 'automatic clause 9' requirement.
23. In contrast, the requirements for TPI to submit (and regularly resubmit) floor and ceiling cost proposals is outlined in TPI's Costing Principles. This was a required amendment outlined in the Authority's draft determination on TPI's Costing Principles.
24. There were four submissions received in response to the Authority's draft determination on TPI's Costing Principles, and no objections were recorded to the inclusion of this amendment. Three of the four submissions argued that the time period allowed between approval of TPI's Costing Principles and the submission of proposed floor and ceiling costs should be three months. A three month time allowance was incorporated by the Authority in its final determination on TPI's Costing Principles.
25. The Authority has suspended its review of TPI's proposed floor and ceiling costs submitted in July 2010 on the basis that the TPI network has been subsequently expanded and there is no basis on which to disaggregate the TPI network for the purposes of separating it into route sections likely to be subject to an access proposal.
26. At present, under the current arrangements, WNR is required to submit revised floor and ceiling cost proposals by October 2011, and TPI is required to submit proposed

floor and ceiling costs for its expanded network in accordance with the provisions of Section 6.1 of its Costing Principles.

Possible changes to the requirements to submit Floor and Ceiling Cost proposals.

27. To date, neither WNR nor TPI have received a proposal for access under the Code and the Authority has not received a firm indication from any potential access seeker that a proposal should be considered likely to be made.
28. The Authority's view is that until an access proposal is received by WNR or TPI, the submission of floor and ceiling cost proposals may be unnecessary and might require duplication of effort in the event that an actual access proposal is received.
29. In the case of WNR, the Authority is considering revising its standing 'Clause 9 expectation' that an access proposal is likely on any of the 53 route sections currently subject to the requirement on WNR to submit floor and ceiling cost proposals. The Authority is prepared to consider revising this expectation on the basis that an access proposal has not been received in the time period which has elapsed since ORAR nominated the initial 23 route sections considered likely to be subject to an access proposal.
30. Concurrently, the Authority is considering suspending the 'Clause 9 requirement' for TPI to submit floor and ceiling cost proposals until such time as a clear indication is received of the precise route sections likely to be subject to a proposal, or until TPI receives an actual access proposal.
31. These changes would require that Railway Owners' Costing Principles be amended to remove the requirement for regular submission of floor and ceiling cost proposals, and for annual adjustment of floor and ceiling costs.
32. This would lessen the compliance burden imposed by the Regime on WNR and TPI.

Issues

33. The objective of the rail access regime is to establish and implement a framework in order to promote efficient, effective, fair and transparent competition on Western Australian railway networks to achieve a net public benefit to the State.
34. To maximise the net benefit of the rail access regime, the regime needs to be managed in a timely and efficient manner. Where costs could be avoided without an associated loss of benefit, the net public benefit would be increased.
35. Broadly, the costs can be categorised as the compliance costs, which are borne by the Railway Owner and the administration costs which are borne by the Authority.
36. The Authority is cognisant that there are some benefits to both Railway Owners and access seekers from continuation of the current arrangements for regular determination of floor and ceiling costs. These benefits include broad information availability to potential access seekers.

37. The Authority is interested to learn the views of stakeholders as they pertain to the relative merits of retaining or altering the current arrangements for submission of floor and ceiling cost proposals by Railway Owners. In particular, the Authority is interested to understand the views of stakeholders on the following questions:

- Do regular floor and ceiling cost reviews potentially require duplication of effort on the part of the Railway Owner if an access proposal is received for a set of route sections for which floor and ceiling costs have not been determined?

At issue here is whether it is efficient to require floor and ceiling costs to be calculated on a route section basis prior to required route sections being identified.

- Would regular reviews of floor and ceiling costs assist the Railway Owner in the event of a proposal being made, by ensuring that route section costs are instantly available?

The Authority is prepared to consider that determined route section floor and ceiling costs may be disaggregated on receipt of an access proposal which requires access to a subset of the routes for which costs have been previously determined.

- Is there an advantage to the Access Seeker in having determined floor and ceiling costs available on the Authority's website, as opposed to discovering those via the proposal process?
- Would the availability of "pre-determined" floor and ceiling costs on the Authority's website minimise the likelihood that a potential access seeker will seek to have the Authority instigate a floor and ceiling cost determination for a combination of route sections (under Clause 9) but rather approach the Railway Owner directly with a proposal, thereby initiating a determination under Clause 10?
- In the absence of pre-determined route section costs, do the provisions of Clauses 9 and 10 of Schedule 4 of the Code allow sufficient time for an adequate review of proposed floor and ceiling costs to be undertaken?

38. The Authority is interested to learn of any stakeholder views on additional issues in relation to the requirements to submit floor and ceiling cost proposals that have not been identified above.