Report

Review of the Western Australian Railways (Access) Code 2000 - Summary of Issues Raised by Interested Parties in Relation to the Railways (Access) Act 1998

23 September 2005

Economic Regulation Authority
WESTERN AUSTRALIA

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REVIEW OF THE WESTERN AUSTRALIAN RAILWAYS (ACCESS) CODE 2000 - SUMMARY OF ISSUES RAISED BY INTERESTED PARTIES IN RELATION TO THE RAILWAYS (ACCESS) ACT 1998

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1 INTRODUCTION

1.1 Scope of the Recent Code Review

The Western Australian Rail Access Regime ("the Regime") came into effect on 1 September 2001. The Regime is comprises the Railways (Access) Act 1998 ("the Act"), and the Railways (Access) Code 2000 ("the Code"). The main objective of the Act, stated in section 2A, is to establish a rail access regime that encourages the efficient use of and investment in railway facilities within a contestable market. The Regime was established to provide a legislative option for access seekers, and not to force all access seekers under the umbrella of an access code.

Under Part 2 section 12, of the Act, the Authority is to undertake a review of the Code on the third anniversary of its commencement; and every five years thereafter. Section 12(2) of the Act stipulates 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 (CPA) in respect of railways to which the code applies".

Although the scope of the Authority's review is limited to the Code, in order to ascertain a complete picture of the effects of the current provisions of the Code, the review asked for comments on a variety of matters under the Regime including the Code and the Act. Although outside the scope of this review, the Authority has needed to give consideration to Act matters in order to maintain consistency with the Code. Whilst the Authority has received and considered issues relating to the Act, the Authority has no role under the Terms of Reference to recommend Act changes.

The purpose of this separate report is to bring to the attention of the Western Australian (WA) Government matters raised in submissions by interested parties related to the Act. As noted above, these matters fall outside the scope of the review of the Code and, consequently, are not dealt with in the Final Report. However, the Authority notes that these matters may have relevance to the efficient operation of the Regime and should, therefore, be forwarded to the WA Government for its consideration. The Authority acknowledges that any changes to the Act are a WA Government policy decision.

It should be noted that as the matters discussed in this separate report fall outside the terms of reference for the Code Review, the Authority has not given consideration to these issues or formed a view in relation to such matters.

1.2 Issues raised in relation to the Act

Submissions to this review made comments on five issues which are covered by the Act, as follows:

1) The definition of Rail Infrastructure in the Act;
2) Enforcement mechanisms to support the right to negotiate access;
3) Greenfields Lines;
4) Segregation Arrangements; and
5) Consistency with National Regime;

Section 2 of this Report summarises the comments from interested parties regarding these five issues.

2 KEY ISSUES RAISED IN SUBMISSION RELATING TO THE RAILWAYS (ACCESS) ACT

This section of the report summarises the views of interested parties as they related to five key sections of the Act.

2.1 The definition of Rail Infrastructure in the Act

The definition of what is covered by the Regime is found in section 3(1) of the Act which defines "Rail Infrastructure" as:

"the facilities necessary for the operation of a railway including –

a) Railway track, associated truck structures, over or under track structures, supports (including supports for equipment or items associated with the use of a railway);
b) Tunnels and bridges;
c) Stations and platforms;
d) Train control systems, signalling systems and communication systems;
e) Electric traction infrastructure;
f) Buildings and workshops; and
g) Associated plant machinery and equipment,

But not including –

h) Sidings or spur lines that are excluded by subsection (3) or (4) from being railway infrastructure associated with the railway concerned;
i) Rolling stock, rolling stock maintenance facilities, office buildings, housing, freight centres, or terminal yards and depots."

Under this definition, access to yards, sidings and terminals is not included because it has been deemed they do not exhibit nationally significant infrastructure characteristics and use by multiple parties may not be practical. This means that under the current arrangements, access seekers who need access to these facilities need to negotiate additional contracts outside their access agreement with the railway owner or railway operator. The definition of railway infrastructure does, however, include 'stations and platforms' which could arguably be excluded due to the reasoning applied to terminals and sidings.

The Trade Practices Act allows interested parties to seek declaration of these facilities, if it can be shown that they are not economically or practicably duplicable. The Australian Rail Track Corporation (ARTC) stated in their response to the Issues Paper that "*the access regime should cover infrastructure that would reasonably be required by an access seeker in order to utilise the network where it is considered that the duplication of that infrastructure is uneconomic."*[1]

ARTC would like to see an amendment so that approval for access is assumed unless the Minister formally rejects declaration, as opposed to the current practice whereby rejection to access is assumed.

This viewpoint reflected the general consensus of the majority of users, that the Act should cover all necessary infrastructure required to deliver a declared service, which could possibly include sidings and terminals. In their submission, Queensland Rail (QR) suggested that there is a merit in adopting an approach similar to the one in Queensland which assesses each rail terminal and associated facility on a case by case basis to determine whether it should be subject to third party access.

[1] ARTC, Submission to the 'Issues Paper: Review of WA Railways Access Code, April 2005, p 8.

Alcoa argued that Australian Western Railroad (AWR) has a competitive advantage in bidding for the above rail operations due to the fact that existing facilities are not available to new entrants and there is only limited availability of land suitable for these activities.[2] Alcoa further commented that "*given disputes in other jurisdictions, and the competitive advantage afforded to the incumbent above rail operator, the Authority should consider including additional facilities under the control of the railway owner in future amendments to the Act. "*[3]

The Authority understands that the railway infrastructure inclusions and exclusions as listed in the Act were influenced by a series of National Competition Council (NCC) decisions in 1997 in relation to five applications by Specialised Container Transport (SCT) for declaration of rail and freight support services provided by Westrail. The first application covered the Kalgoorlie to Perth railway line (Eastern Goldfields Railway- EGR). The other application covered rail freight support services such as arriving/departing services, marshalling/shunting services and access and fuelling services. The NCC recommended that the EGR be declared but not the rail freight support services. The NCC found that the latter services were economic to duplicate.[4] The NCC findings were influential in the WA Government's decision as to what could be assessed under the current Regime.

2.2 Enforcement mechanisms to support the right to negotiate access

To be an effective access regime, there must be enforcement mechanisms that apply if a party fails to comply with particular obligations. The current enforcement provisions (Division 2, section 21 and 22 of the Act) include fines initiated by the Regulator and then enforced by a Supreme Court ruling. Additionally, the Authority can also apply to the Supreme Court to grant an injunction if it is satisfied that the railway owner has engaged or is proposing to engage in conduct that amounts to a breach of the Code. These measures impose financial penalties to deter non-compliance with the regime, and are supported by the railway owner. The Australian Railroad Group (ARG) have stated that they support "*enforcement being based on the power of the regulator to issue direction supported by appropriate civil penalties."*[5]

There could be some grounds to introduce the ability for access seekers to be awarded damages if it can demonstrate a loss or damage from breach of an access agreement with the railway owner. The concept is supported by Worsley, who maintain that $100,000 is an insufficient disincentive, and losses incurred from the railway owner should be recoverable as damages by the party that suffers damage. Worsley propose that any penalties should reflect the full economic value of the loss suffered by the party. However, fines are generally set at a level broadly commensurate with the significance of the offence, and it would be impractical to fine based on an individual economic loss. This approach is arguably more suitable for civil compensation claims.

2.3 Greenfields Lines

A Greenfield investment typically refers to the construction of a new rail line which is not connected to an existing network. A greenfield extension is generally viewed as a new line connected to an existing network.

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[2] Alcoa, Submission to the 'Issues Paper: Review of WA Railways Access Code, March 2005, p 3.
[3] Ibid, p 5.
[4] NCC Submission to the Productivity Commission Inquiry, Progress In Rail Reform, November 1999, p 7.
[5] ARG submission, 'Options for Reform of the Victorian Rail Access Regime', August 2004, p 4.

Greenfields investments and expansions of the railway infrastructure need to generate a considerable level of demand if operations are to be profitable, and to compensate for the high level of risk. Thus, the regulation of greenfields projects needs to deal appropriately with ex-ante risks facing the investor, otherwise incentives to invest may be lower. Consequently, access arrangements should not deter investment, however, it must also promote access and competition in related markets.[6]

Greenfield expansions are covered by section 3(2) of the Act, which states that if any new railways are constructed which connect to the railway, the Minister may declare the new railway to be part of the railway network. Any new lines also need to pass the test for inclusion which is covered in section 5(3) of the Act, whereby the proposed route needs to satisfy the following criteria:

a) *Whether access to the route will promote competition in a least one market, other than the market for railway services;*
b) *Whether it would be uneconomical for anyone to establish another railway on the route;*
c) *Whether the route is of significance having regard to :*
    a. *Its length;*
    b. *Its importance to trade or commerce; or*
    c. *Its importance to the economy*
d) *Whether access to the route can be provided without undue risk to human health or safety*
e) *Whether there is not already effective access to the route; and*
f) *Whether access or increased access to the route would not be contrary to public interest.*

Any new and extended route needs to pass this test for inclusion in order to be added to Schedule 1 of the Code which lists all the routes to which the Code applies. If railway infrastructure, covered by the Code, is extended or expanded, (e.g. a new passing loop or a rail line duplication), the Code will also apply to that route or infrastructure.

Currently under the Code, the Authority has no formal involvement in regulating new rail lines until they are operational and formally added to Schedule 1 of the Code. Under this process the railway developer could be subject to a lengthy waiting period between line commissioning and Ministerial approval for formal inclusion of the rail line in Schedule 1 of the Code. Therefore, proponents of new rail lines are uncertain if a potential rail line will be covered by the Regime and this can impact on the bankability of the proposal.

This process is yet to be tested, as no expansions or extensions of the network have been included into the Code. Proponents building new rail lines are likely to seek to contract a base load of volume prior to construction in order to reduce the high level of risk associated with investment in long-lived assets.

This uncertainty related to the regulation of new rail lines is viewed by some interested parties as a disincentive to invest in the network. Therefore, there is a desire to be able to obtain a view at the proposal stage on whether coverage is likely as well as reforms to minimise this waiting period prior to inclusion into the Regime by speeding up the testing process.

QR have stated that there is an information asymmetry between the rail developer and potential users. They suggest that the "*rail developer should have the capacity to gain an understanding of the status of its proposed rail infrastructure and the*

[6] NCC, "*Australian Railway Access Regime, Final Determination",* February 2000, p.1.

nature of the regulation that would be applied to it, before the proposed rail infrastructure is developed."[7] QR also recommended that changes be made to the Act (and Code) to identify the nature of the Service to be covered, in addition to the infrastructure required to deliver it.

Some submissions suggested that the confidence of railway developers could potentially be improved if it was possible to obtain a preliminary view from the Authority on whether the proposed line would be covered, and the likely ceiling and floor costs.

2.4 Segregation Arrangements

The segregation arrangements in a regime are integral to the negotiation process, as they aim to ensure confidentiality of negotiations and fairness. The crucial importance of segregation sees the duty to separate (or ring fence) the access related (below rail) functions from the other functions outlined in Part 4 Division 3 (section 28 to 34) of the Act. The duty to segregate under section 28 of the Act requires the development of the Segregation Arrangement instrument which details the specific separation control procedures which need to be approved by the Authority.

Consequently, reference to the Segregation Arrangements in the Code is limited to section 42, which refers to the approval process of the arrangements. There were no submissions suggesting changes to section 42 of the Code. However, a number of other views on segregation were expressed.

In earlier reviews which established the Segregation Arrangements, the Authority considered the merit of requiring separate buildings for WestNet Rail (WNR) and AWR. This requirement was not imposed due to a view that it would not preclude the illegal exchange of confidential information and it also created extra costs whilst reducing communication effectiveness in relation to permissible exchanges (e.g. maintenance and operating strategy).

The Authority is proposing to strengthen the segregation arrangements by providing the Regulator with the ability to audit consistency between prices provided to associated entities and access seekers. This should strengthen customer confidence in the segregation arrangements.

The statutory segregation requirements are contained in Part 4 Division 3 of the Act. The duty to segregate under section 28 of the Act requires the development of the Segregation Arrangement instrument which details the specific separation control procedures which need to be approved by the Authority. Submissions on issues relating to the Segregation Arrangement instrument are summarised in Section 5.3 of the Final Report.

A number of submissions indicated concern about the effectiveness of the Regime in maintaining these segregation arrangements with some suggesting more structural separation is required. For instance, "*AWB feels that the Code needs to be revised to end vertical integration in the Western Australian rail infrastructure, or to reinforce the virtual separation of the entities, which it feels has not been achieved with any degree of success."*[8] Some submissions also suggested that as vertically integrated railway owners have greater incentive to frustrate access by competitors, it is critical that the Regime provides adequate safeguards against the railway owner favouring its associated entities.

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[7] QR submission to the '*Issues Paper; Review of the WA Railways Code',* April 2005, p.9.

[8] AWB, Submission to the 'Issues Paper: Review of WA Railways Access Code, April 2005, p 3.

Pacific National (PN) expressed the view that it considered that the segregation arrangements are adequate.[9]

Overall, the use of a vertically integrated structure was a WA Government policy decision, which is reinforced by clauses within the Act and the sale agreement with ARG.

2.5 Consistency with National Regime

Clause 6(4)(p) of the CPA states that there should be consistency of access arrangements, where more than one set of arrangements applies to a service. An effective access regime should be able to facilitate cohesion with other regimes to ensure smooth running over the interstate jurisdictions. This should enable the access seeker to coordinate usage of the rail infrastructure between states.

The ARTC has negotiated a wholesale agreement with the WA Government that gives the ARTC exclusive rights with respect to new agreements on the interstate part of the network. As yet, no operations are being conducted in this part of the network pursuant to an access agreement developed under the wholesale agreement.[10]

Under section 27(1) of the Code, if there is an issue which is relevant to arbitration under another access regime, then arbitration is to take place both under the Code and the other relevant regime.

Despite these arrangements to enable some consistency between jurisdictions, the practical effectiveness is yet to be tested. Currently, the ARTC Undertaking appears to be the most likely regulatory framework to emerge as a National Rail Access Regime.

ARTC stated in their submission to the Issues Paper that the Regime has a number of different treatments that can cause some uncertainty in access for the operator of an interstate service, (e.g. provision for capacity transfer, resolution of capacity demand conflicts, openness in pricing and treatment of costs in floor/ceiling limits). The preference of incumbent interstate operators (SCT and PN) is to deal directly with the party controlling maintenance and operations on the network, rather than indirectly through the ARTC suggests the one-stop-shop concept has less merit to operators than a direct communication line with the actual network owner and controller. Overall, "*ARTC does not consider the arrangement as being particularly effective, however it does provide a base for an effective ceiling on access pricing and terms for interstate operators within WNR.*"[11]

[9] PN, Submission to the 'Issues Paper: Review of WA Railways Access Code, April 2005, p 3.
[10] ARTC, Submission to the 'Issues Paper: Review of WA Railways Access Code, April 2005, p 3.
[11] Ibid p 5.