

Pacific National Submission to the Review of the Western Australian Rail Access Regime Issues Paper

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1. Introduction

Pacific National welcomes the opportunity to make a submission to the Western Australian Government's review (the Review) of the Western Australian rail access regime as established by the Railways (Access) Act 1998 (the Act) and the Railways (Access) Code 2000 (the Code).

Pacific National is a major freight rail operator in Australia and has a strong interest in improving the regulatory and access regimes which currently apply to Australian rail infrastructure. Pacific National operates the following trains on the Arc Infrastructure standard gauge rail network between Perth, Kalgoorlie and Esperance:

- interstate intermodal container trains;
- intrastate fuel trains; and
- intrastate mineral trains (where these operations are on behalf of a third party access holder. As the access and commercial interfaces for these operations are between Arc Infrastructure and a third party access holder this submission makes no comment on issues relating to these operations).

Given the scope of these Pacific National operations, the comments in this submission apply only to the Arc Infrastructure rail network in the south west of Western Australia.

This submission is public.

2. Pacific National Position on the Western Australian Rail Access Regime

Pacific National understands that the intention of the Review is to identify improvements to the rail access regime in order to encourage the efficient utilisation of rail infrastructure, efficient investment in rail infrastructure, facilitate a contestable market for rail operations and improve outcomes for access seekers and operators. Pacific National believes that addressing the issues identified in this submission will improve both the Western Australian rail access regime and the efficiency of the Western Australian freight rail industry.

Pacific National has made submissions to previous reviews of the Western Australian Rail access regime. The position in these submissions be broadly summarised as:

- Strong support for nationally consistent approaches to access; and
- Concerns regarding the natural monopoly position and the information advantages of rail infrastructure and the potential for this to create imbalances in pricing negotiations.

As outlined in the Review's Issues Paper (page 2) the recommendations of the ERA 2011 and 2015 reviews of the Code are yet to be addressed. Pacific National believes that the recommendations arising from these Reviews should be implemented. In particular Pacific National very strongly supports recommendation 1 of the ERA's 2015 Review that the interstate route be regulated consistent with the ARTC access undertaking.

Pacific National notes that the objectives of the Western Australian rail access regime as outlined in the Issues Paper (page 2) include the prevention of the misuse of market power and regulatory certainty, which Pacific National believes includes pricing certainty. These issues need to be addressed within the current review of the regime.

3. Western Australian Rail Access Regime – Areas for Improvement

The Western Australian rail access regime was previously certified as being effective but this certification has now lapsed. Pacific National understands the State Government intends to consider applying for re-certification once improvements to the regime have been made. Pacific National believes that the issues outlined in this submission need to be addressed prior to any application for certification.

The Code currently does not seek to prescribe indicative tariffs or regulator approved access agreement, but rather it seeks to facilitate a negotiation process. Pacific National believes that the Code needs to provide more prescriptive regulation, particularly on the Kalgoorlie - Perth rail line.

a. Consistency across Rail Access Regimes

One of Pacific National's main concerns with rail access in Australia is the number of rail access regimes and the misalignment between the various state and Commonwealth access regimes¹. These multiple access regimes with multiple regulators add costs and complexity to interstate rail access for little (if any) benefit. The Arc Infrastructure standard gauge rail line between Kalgoorlie and Perth is part of an interstate freight supply chain allowing the transport of goods between Western Australia and the eastern states. Pacific National believes that on interstate supply chain rail infrastructure,² a nationally consistent approach to rail access is required.

¹ Pacific National operates its above rail operations under five state-based access regimes and the National Access Regime.

² Pacific National recognises that regulation should be flexible enough to accommodate different business structures and operations, therefore on physically separate railways (such as the Pilbara) or railways that deal primarily with intrastate supply chains (such as most grain railways) then state access regimes may be appropriate.

The Issues Paper (page 33) recognises that consistency across access regimes is important for interstate freight routes. Pacific National strongly supports this position.

The 2015 ERA Code Review recommended that:

The Government consider options to bring interstate services offered by Brookfield Rail [i.e. Arc Infrastructure] on the interstate route under regulations consistent with the ARTC undertaking, in line with the 2006 Competition and Infrastructure Reform Agreement.

Pacific National understands that the ERA envisaged Arc Infrastructure would submit an access undertaking to the Australian Competition and Consumer Commission (ACCC) for regulation of the interstate services under the national access regime, and that this could be achieved by amending the Code to remove its application to interstate services. This would allow a consistent access framework to be applied to interstate services.

Pacific National strongly supports this proposal but recognises that the proposal creates potential inconsistencies, notably that intrastate services operating on the Kalgoorlie-Perth line would continue to be subject to the Western Australian rail access regime. This has the potential to create inconsistencies as a single rail line would be subject to two different access regimes.

To address this potential inconsistency all standard gauge services on the standard gauge Kalgoorlie-Perth line could be regulated under a nationally consistent access regime, with the remaining narrow gauge network and Pilbara networks subject to the Western Australian rail access regime.

Pacific National recognises that requiring Arc Infrastructure to offer an undertaking to the ACCC would not necessarily lead to consistent access regulation for interstate services as Arc Infrastructure and ARTC may each submit undertakings which, while they meet the relevant regulatory criteria, are not consistent with each other. However, an approach where the Arc Infrastructure undertaking has to include as a minimum indicative tariffs for a reference services and a regulator approved access agreement (i.e. the Arc Infrastructure undertaking has to contain similar elements to the ARTC undertaking) then this would in itself be a major step forward in addressing issues of regulatory uncertainty.

Under the current approach the access pricing and access contracting of a freight train from Melbourne to Perth is regulated via an indicative tariff and a regulator approved access agreement from Melbourne to Kalgoorlie and there is then no access pricing regulation or access contracting regulation apply from Kalgoorlie to Perth. This raises concerns as to the potential for Arc

Infrastructure to set access pricing to capture economic surplus created by the price regulation on other sections of the rail infrastructure.

b. Natural Monopoly Infrastructure, Information Imbalances and Access Pricing

Railways in Western Australia, particularly railways serving interstate supply chains and bulk product markets in regional areas, have the inherent characteristics of natural monopoly infrastructure. In Pacific National's experience of negotiating for rail access in Western Australia this natural monopoly position can be used to seek substantial access price increases. Thus a regulated price determination process is essential to balancing the position of the rail infrastructure provider with the interests of the access seeker. .

The current Western Australian rail access regime (Code (Schedule 4 clauses 7 and 8)) requires the establishment of a floor price (effectively a price based on incremental cost) and a ceiling price (effectively a price based on stand alone cost), and the access seeker and access provider then negotiate the final access price between these two price limits. The floor and ceiling approach provides for a very wide range of possible prices within which access prices may be negotiated. There are no indicative tariffs approved by the regulator.

Pacific National strongly believes that this floor and ceiling pricing approach is inadequate as it requires the use of a "negotiate and arbitrate" access approach between two distant price benchmarks. This "negotiate and arbitrate" access approach is also problematic as it requires access seekers to negotiate with a natural monopoly rail infrastructure provider. Under the "negotiate and arbitrate" approach these negotiations are likely to favour the rail infrastructure provider due to its relative bargaining power and access to information.

In particular under the current model there is a lack of independently tested cost information available to access seekers, which places access seekers at a further disadvantage in negotiating efficient access prices, as only the access provider has detailed knowledge of their costs. It is impossible for an access seeker to assess the reasonableness of a proposed access charge given the asymmetry of information between a railway owner and access seeker in the absence of an indicative price. (If the "negotiate and arbitrate" access model continues to be applied then rail access negotiations and outcomes need to be improved by requiring rail infrastructure providers to supply a level of cost information which facilitates balanced price negotiations).

In the context of the WA rail access regime, these imbalances may be best addressed by developing:

- indicative tariffs for defined reference services. Pacific National believes that the regulator should have the power to approve tariffs for defined reference services, with these being

the default tariffs for these reference services, (but the access seeker and access provider should be able to negotiate away from these tariffs if there is mutual agreement). In addition it should be recognised that these tariffs are to be used as a reference point for negotiations for non-reference services;

- a regulator approved standard access agreement. Currently under the Code (clause 6) the access provider's standard access agreement (as determined by the access provider) has to be provided to the access seeker. Pacific National believes that the access provider's standard access agreement should be approved by the regulator for the defined reference services, with these agreements being the default access agreements. This ensures that the regulator approved indicative tariffs are consistent with the regulator approved access agreements. (The access seeker and access provider should be able to negotiate away from these agreements if there is mutual agreement);
- amended regulations which require the provision of sufficient information to allow a more balanced negotiation. In particular there should be regular and more detailed reporting of costs, service quality and asset quality for specific supply chain corridors. (These reports should be capable of being audited); and
- amended regulations which allow for any access negotiation undertaken outside the Code that is in dispute to be brought within the Code, with the parties able to progress straight to arbitration under the Code.

Given the natural monopoly rail infrastructure provider can provide a service with no alternatives Pacific National believes that the benefits of developing and applying an indicative tariff (with supporting cost information) and a regulator approved access agreement, would outweigh any costs associated with the development and regulatory implementation of this tariff.

c. Extensions and Expansions

The Western Australian rail access regime has a lack of detail regarding the extension and expansion process and how these infrastructure improvements are priced (particularly pricing for expansions or extensions that may ultimately be used by more than one user). The current lack of detail in the Code around the extension and expansion process creates an imbalance in negotiating power. Pacific National believes that a more detailed process would provide greater certainty about the costs of an expansion or extension.

One particular issue of concern (as identified by the Issues Paper (page 11)) identifies that an access seeker (not the railway infrastructure operator) has to identify if an extensions or expansion is needed. Pacific National believes that it is more efficient to place the responsibility on the railway infrastructure operator to assess whether an access proposal can be accommodated on the

network. This is the approach taken in other Australian rail access regimes. Pacific National would support changes that would require the railway infrastructure operator rather than access seeker to determine the extensions or expansions required and otherwise determine if capacity exists on the railway.

d. Asset Valuation Approaches

Pacific National notes that in Western Australia for the purposes of regulation rail assets are valued on a Gross Replacement Value (GRV) basis rather than a Depreciated Optimised Replacement Cost (DORC) basis. Pacific National notes that for the purposes of regulation other Australian rail access and pricing regimes typically use the DORC asset valuation basis. Consequently in the interests of a consistent national approach to regulation Pacific National believes that a shift to the DORC valuation basis should be considered. The move to more consistent pricing approaches is particularly relevant if indicative pricing is to be adopted for the interstate network. Pacific National notes that in the 2015 ERA review it was recommended that the Established Asset Base (EAB) approach which is similar to the DORC approach replace GRV.

More broadly in considering asset valuation approaches Pacific National notes that the Competition Principles Agreement requires that access prices should be set to include a return on investment. Pacific National believes that this could be interpreted as a return on actual investment.

4. Conclusion

Overall Pacific National strongly supports:

- nationally consistent approaches to rail access; and
- the implementation of regulated access prices, regulated access agreements and improved information provision.

As outlined in the Review's Issues Paper (page 2) the recommendations of the ERA's 2011 and 2015 reviews of the Code are yet to be implemented. Pacific National supports these recommendations. In particular Pacific National very strongly supports recommendation 1 of the ERA's 2015 Review that the interstate route be regulated consistent with the ARTC access undertaking.