



Review of the NSW Rail Access Undertaking
Independent Pricing and Regulatory Tribunal (IPART)
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Review of the NSW Rail Access Undertaking

Dear IPART,

Thank you for the opportunity to comment on the Independent Pricing and Regulatory Tribunal's (IPART) **Draft Report (October 2022) Review of the NSW Rail Access Undertaking** (the Draft Report).

Aurizon supports the application of economic regulation where there is a clear economic problem that needs a regulatory solution and there are demonstrated economic public benefits that outweigh the costs. Our support depends on the regulation being well-designed, targeted and consistently applied.

Third-party access to significant infrastructure facilities such as rail networks is intended to:

1. Encourage efficient use of, and operation and investment in, rail infrastructure; and
2. Promote competition in upstream and downstream markets.

The form of regulation depends on the risk of misuse of market power, whether intentionally, or because of out-dated and unchallenged practices developed with different objectives in mind.

The NSW Rail Access Undertaking (NSW RAU) reflects the time in which it was created. It's scope and application to network components that vary in terms of traffic task and markets served, means that it has a 'one size fits all' approach. It is too high level to negate bargaining power imbalances and facilitate effective commercial negotiations for access. The framework requires an increased level of prescription by way of principles and oversight.

Aurizon supports IPART's recognition of the concerns of rail operators and development of a workable solution that:

- Retains the negotiate-arbitrate model across all NSW rail infrastructure
- Addresses bargaining power imbalances by including broad, clear, and comprehensive 'principles' for access providers to meet in developing their own undertaking/s for their different networks,

- Empowers IPART to play a more active role as regulator, including being responsible for approving undertakings, and
- Removes the threat of regulatory uncertainty as a bargaining position for ARTC in relation to the Hunter Valley Coal Network (HVCN).

IPART's proposal will address the need for flexibility across rail networks with different characteristics and access providers with varying opportunities and incentives to misuse market power. It bolsters the regulatory framework by:

- improving information disclosure requirements
- incentivising timely negotiations
- enhancing dispute resolution processes, and
- ensuring obligations are enforceable

Aurizon agrees that:

1. individual access providers are best placed to develop and offer an undertaking that is compliant with the amended rail access framework under the *Transport Administration Act 1988 (NSW)* (TAA) as well as tailored to their network, and
2. IPART is best placed to determine whether those undertakings successfully address the economic problems specific to their network components and satisfy the criteria set out in the TAA.

For several years Aurizon has experienced a similar approach working successfully in Queensland under the provisions of Part 5 of the *Queensland Competition Authority Act 1997* (QCA Act). Aurizon Network provides access to the Central Queensland Coal Network in accordance with its access undertaking¹, while the terms and conditions under which Queensland Rail provides access to its rail infrastructure, including the Metropolitan network that primarily services commuter passenger services, is set out in its own access undertaking².

Both undertakings are voluntarily submitted and approved by the Queensland Competition Authority (QCA) under a clearly defined process and in accordance with defined principles in the QCA Act. To the extent the different networks and markets covered by the two undertakings require varying regulatory intervention, the relevant controls set out in the undertakings reflect this.

As IPART has recognised, and proposed for the NSW rail access framework, under the QCA Act, the regulator has the power to ultimately draft an undertaking for an access provider should they fail to provide one or meet the legislative requirements of an undertaking. This ensures access providers are incentivised to develop their own undertaking in a timely manner and respond to IPART's (in NSW) feedback on whether an undertaking satisfies the requirements in the TAA.

The recommendations proposed by IPART are enthusiastically supported by Aurizon and considered to be largely consistent with the 5 guiding principles set out by IPART in its Issues Paper³.

Aurizon also acknowledges that the Draft Report references the significance of network fragmentation, not just in NSW, but nationally. For traffic like coal and freight, that may operate over multiple networks (regulated under multiple access regimes) the lack of

¹ currently – Aurizon Network's 2017 Access Undertaking (UT5)

² currently -Queensland Rail's 2020 Access Undertaking (AU2)

³ IPART, *Review of the NSW Rail Access Undertaking Issues Paper*, November 2021, p 2

harmonisation of operating rules, standards, processes, and regulations, impact efficient and competitive supply chain services.

The issue of interoperability was also considered by the Australian Competition and Consumer Commission (ACCC) as part of its review of the regulatory framework to apply to Australian Rail Track Corporation's (ARTC's) Interstate Network⁴. There was some industry hope that these important issues would be considered in more depth by the regulators during these reviews, even if these matters are broader in nature than the rail undertakings and also need to be addressed by governments. Although analysis hasn't been forthcoming, Aurizon considers the goal of harmonising rail access regulation across Australia should remain a guiding principle for regime design and decision-making.

Aurizon recognises the balance to be struck between supporting individual undertakings for separate NSW rail networks while pursuing greater alignment between all applicable rail access regimes in terms of the form of regulation, regime design and compliance and enforcement requirements. Improved interfacing between networks can be facilitated by regulation.

For example, engagement and cooperation between adjacent rail networks can be mandated to ensure seamless through running of services and/or minimal interruption to services. This is one strategy proposed by IPART, and Aurizon is appreciative that IPART has recommended such consultation occur when network maintenance plans are being developed. A similar obligation, to engage and cooperate, could also minimise unforeseen impacts arising from:

- changes to path allocations, including when scheduling possessions, and
- changes to operational performance requirements.

In addition, as a rule, access seekers and holders should not incur performance liabilities operating on one network because of the performance of the adjoining network provider. Adjacent network managers have the capacity to agree between themselves on how risk will be allocated at the interface. Rail operators do not. It is reasonable that access providers of adjacent networks:

- consider the impact of decisions relating to rolling stock and network standards (including matters such as signalling and communication systems) on operators who travel over several networks,
- recognise that delays to a service caused by one network provider should not result in the service being penalised by an adjoining network provider, and
- undertake to review requests from operators for modifications to improve efficiency and/or productivity in the context of cross-network paths where this is relevant, and to engage with the operator on possible solutions involving all stakeholders, rather than leaving an operator to engage one-on-one with each network provider.

These types of measures are especially important where there is the potential for privatisation of infrastructure. As the experience with the Port of Newcastle has shown recently, the risk of monopoly power being exercised is likely to increase when assets are privatised. As part of a supply chain, one privatised infrastructure operator, could create significant barriers to entry and growth in below rail markets. They will be incentivised to stifle productivity and innovation by rail operators if this advantages their ability to extract a greater share of available rents.

⁴ <https://www.accc.gov.au/regulated-infrastructure/rail/interstate-rail-network-access-undertaking/the-regulatory-framework-for-artcs-interstate-network/guidance-paper>

Our comments below are structured in the same sequence as IPART's Draft Report and recommendations. We haven't commented on every recommendation but hope that our feedback is useful to IPART going forward.

Form of Regulation

For the reasons given above, Aurizon welcomes the recommendations concerning the form of regulation. The proposed amendments to the TAA introduce clearer and more comprehensive criteria for approving an undertaking and setting out what an undertaking must address.

One suggested addition for an undertaking is a provision for an approved undertaking to be varied, both voluntarily and at the regulator's direction⁵.

The changes recommended to enhance IPART's powers of engagement and compliance will improve the regime's suitability across all the rail networks it covers. Bringing this aspect of the NSW RAU in line with Part IIIA of the *Competition and Consumer Act 2010 (Cth)* (CCA) enables IPART's pragmatic recommendation to allow the NSW rail access framework to remain uncertified under the CCA, so that ARTC may continue to voluntarily submit Interstate and Hunter Valley access undertakings with the ACCC. In the Hunter Valley, the recommended approach will retain the negotiated 'coal-network specific' elements of the Hunter Valley Access Undertaking (HVAU) while ensuring that the NSW RAU offers a genuine safety net for users of the network.

In relation to the 'form of regulation' assessment to be undertaken for the different parts of the NSW rail network, Aurizon notes the suggested test on page 17 of the Draft Report, relating to an access provider's ability to exercise market power:

The rail owner's market power depends partly on the competitive constraint of alternative transport modes. In areas where road competes with rail, the rail owner has limited ability to exercise market power.

As Aurizon pointed out in its response to IPART's Issues Paper⁶, an access provider's ability to exercise market power isn't solely determined by the competitive constraint of alternative transport modes. This statement doesn't adequately address the problem that demand for below rail services is a derived demand for rail freight services which are contestable with road. As below rail does not compete directly with road then it may still have market power where the above rail market is workably competitive. IPART's Draft Report recognises this later in the discussion on the 'hold-up problem'.

The exercise of market power can occur intentionally (to capture industry rents) or consequentially due to information asymmetry and a lack of transparency and accountability. Consequently, Aurizon considers the criteria that should be applied in assessing the ability and incentive for an access provider to exercise market power needs to have regard to:

- where prices are set at or close to the ceiling limit, the potential for the access provider to increase prices above the economic costs of providing the service,

⁵ *Queensland Competition Authority Act 1997 (Qld) Pt 5 Div 7* includes provisions to this effect

⁶ https://www.ipart.nsw.gov.au/sites/default/files/cm9_documents/Online-Submission-Aurizon-D.-Steele-13-Jan-2022-132117120.PDF pages 3-6

- where prices are set below the ceiling, the potential for the access provider to increase prices to expropriate a greater share of available rents, and
- whether the access provider's actions could adversely impact competition in a dependent market.

These types of measures are especially important where there is the potential for privatisation of infrastructure. As the experience with the Port of Newcastle has shown recently, the risk of monopoly power being exercised is likely to increase when assets are privatised. As part of a supply chain, one privatised infrastructure operator, could create significant barriers to entry and growth in freight rail markets.

The Inland Rail completion and eventual inclusion in the ARTC Interstate Access Undertaking provides one example of where this wider test of ability to exercise market power will be critical. ARTC, or another network provider, could seek to maximise returns on the investment and squeeze the returns of freight operators. The ACCC's Guidance paper on ARTC's Interstate network access undertaking 2023⁷, recognised that government ownership's broader policy objectives may have moderated ARTC's pricing and profit maximisation. The receipt of government funding for Inland Rail, on social, environmental, or economic grounds, means that passing through the full costs of the infrastructure in access charges would not only run counter to the government objectives, but possibly leave the asset stranded. However, a private network owner will be incentivised to recover as much as possible from its investment without the constraining moderation of government policy.

IPART has recognised the importance of effectively constraining market power held by access providers by virtue of a lack of transparency around key information relevant to commercial access negotiation. Aurizon supports the comprehensive information disclosure obligations and other measures recommended by IPART. Consistent with the benefits of customer-centric regulation, Aurizon would welcome the inclusion in IPART's binding guidelines of its expectations for how the access provider should constructively engage stakeholders and how IPART will consider the quality of that engagement in assessing a submitted undertaking.

As with any regulatory change, the impact of the changes recommended by IPART will take some time to be apparent. While we recognise the benefits of regulatory certainty in having a longer term for a Schedule 6AA undertaking, we consider it preferable that the initial term is 5 years, with 10-year reviews thereafter. This will allow an evaluation of the efficacy of the reforms and an increased level of confidence in the terms of the undertaking prior to long term regulatory certainty.

Accountabilities under the NSW RAU

Aurizon welcomes the recognition of stakeholder frustration about protracted commercial negotiation, the lack of clear accountability in governance arrangements, and the resulting fragmented provision of access.

We do not have an 'in principle' objection to a framework that centralises the ownership and management of all transport assets. Aurizon considers that significant efficiency gains could be made by managing and planning road, rail, and port infrastructure as one transport system

⁷ <https://www.accc.gov.au/regulated-infrastructure/rail/interstate-rail-network-access-undertaking/the-regulatory-framework-for-artcs-interstate-network/guidance-paper>

that aligns to the needs of people and places. This would drive more informed decision-making leading to higher quality, faster and cheaper infrastructure investment.

Our primary concern is the customer service interface should facilitate access, regardless of the asset governance and management structure. This requires clear responsibility and accountability on the part of access providers. The party giving the undertaking must assume full legal responsibility for obligations to access seekers under the undertaking, and the party negotiating and signing the access agreement must assume full legal responsibility for obligations under the agreement.

Good commercial customer service models reflect this approach absent any regulatory intervention. ARTC manages to coordinate all aspects of access from one central point of contact for access seekers.

Our experience with the NSW RAU in respect of the TAHE network is unfortunately not this efficient or transparent, and we believe this has led to an inability to address the concerns of rail freight operators, as demonstrated by the following example. In the box below is an extract of the key themes and issues raised by freight operators in Freight Rail Operator Forums with ST and TfNSW; the first on 29 June 2017, and the second on 23 February 2022.

In brief the key themes from the day were:

- Data – The ability to share it, and use it meaningfully.
- Infrastructure – the need to bring infrastructure along to support more trains, more services for freight and passengers, and to give greater certainty for business.
- Network Presentation – managing the live run environment of trains that present outside the 5 minute window and how Sydney Trains will deliver on their commitments to ensuring freight services will still have appropriate access to the network.
- Network Communications – improving and formalising communication between Sydney Trains, ARTC and John Holland CRN to better manage trains through the networks.
- Performance – how do we measure performance, what measures are good for operators, and how do we reward operators for doing the right thing?

Additional themes identified at the workshop include:

- Possessions, possession management and special events
- ASA – resourcing to assist rail operators with issues related to rolling stock, schedules, TOC waivers and the TOC manual
- Future freight growth and capacity planning – separation of freight and passenger
- Use of ad hoc paths

List of key themes raised at the Freight Rail Operators Forum held 23 February 2022

- possession planning – no meaningful consultation with operators or customers
- late path approvals and poor coordination between adjoining networks
- priority of service to passenger over freight in the ST ROC beyond the scope of the Op Protocols
- collapse of rail freight consultative forums designed to facilitate supply chain coordination – Port Botany Rail Operators Group and Rail Freight Industry Group
- data and performance management initiatives
- infrastructure investment

There is significant overlap in topics across the 5-year period including: possession management, the ineffectiveness of the ASA (now AMB), data and performance management, treatment of freight vs passenger in the live run environment, and investment in infrastructure for freight. The lack of progress doesn't necessarily reflect a lack of intent, but the intractability of these key issues is facilitated by:

1. Multiple NSW rail networks that lack coordinated oversight.
2. Multiple NSW government agencies involved in providing access to TAHE networks. This creates complexity for operators to navigate and opportunity for 'buck passing' between different agencies to the disadvantage of operators (and in the long run, the NSW economy).
3. Legislative obligations not aligning with contractual responsibilities held by government agencies (TAHE is the only party to the NSW RAU and access agreement, but doesn't allocate capacity, carry out maintenance or conduct negotiations. It does, however, reserve the right to determine prices, and this can slow down negotiations).
4. TAHE isn't an accredited Rail Infrastructure Manager (RIM) but both Sydney Trains (ST) and TfNSW are. Currently, TfNSW has responsibility for determining the Standard Working Timetable (SWTT) in the sense of developing a new SWTT and modifying an existing SWTT. ST provides input into this process by advising on the capacity required for passenger services, Special Events and track possessions, and proposing amendments to optimise use and reliability of the TAHE network. ST is responsible for scheduling the Daily Train Plan and providing Train Control services. ST is also a vertically integrated passenger services provider, competing for capacity/train paths with other operators.

Consequently, Aurizon believes that the complexity of the access management framework for the TAHE rail networks requires fundamental overhaul.

A recent example of the unwieldiness of the existing arrangements is the TfNSW proposal to alter the process for developing the SWTT for the Metropolitan Rail Network (MRN).

Schedule 1 Part 2 section 5 TAA provides that TfNSW has responsibility for determining the SWTT in the MRN. Aurizon was advised in October 2022 that a new service model for the SWTT was being proposed, involving an outcome based SWTT Design Specification by TfNSW, development of SWTT options by ST, and determination of the final SWTT by TfNSW. This change requires amendment of a key operational document under MRN access agreements: the Operational Protocols⁸.

Leaving aside the issues of competitive neutrality in the allocation of capacity, and ST's conflicting role as a vertically integrated commuter passenger service provider, the timing of this proposal directly conflicts with earlier undertakings given by TAHE and TfNSW.

In May 2022 TAHE advised rail operators that it was putting the development of the Standard Track Access Agreement (STAA) on hold *because of changes to the operating model associated with management of the metropolitan rail network and the review of the NSW Rail Access Undertaking by the Independent Pricing and Regulatory Tribunal (IPART)*.

⁸ TAHE Operational Protocols, Version 4.0, s.2

The STAA Development and Implementation Plan, sent to rail operators by TfNSW in June 2022, explained that a 2-year extension to existing access agreements was to be *offered to enable a renewed approach to developing the STAA which will specifically review:*

- *Aligning the terms of the STAA with the TfNSW and TAHE operating model,*
- *Ensuring functional alignment with regulatory and legislative responsibilities, including railway operations, the Standard Working Timetable and Network Control, and*
- *Considering and implementing any changes required following the release of the IPART review of the NSW Rail Access Undertaking, expected to be released at the end of 2022.*

IPART released its Draft Report on 18 October 2022, after the SWTT proposal was communicated.

The SWTT process is a critical part of the provision of access. It is a key element of capacity allocation. The expectation Aurizon held, due to TAHE's pausing of the STAA development, was that IPART's recommendations on the NSW RAU would be considered and implemented. This understanding was reinforced when the extended timing of the IPART review was referred to as a reason for delays in progressing milestones in the STAA Development and Implementation Plan.

Aurizon supports the conclusion that a single point of accountability is necessary under any undertaking, and for the TAHE network the NSW Government should decide who that party is. If any other entity acts on behalf of the accountable body, they must also be bound to comply with the undertaking.

Equally critical, any access agreement entered under an undertaking, must provide an access holder with confidence that the counter party is solely responsible for all matters pertaining to network access. Access holders should not be responsible for resolving issues with any agencies or sub-contractors who the access provider engages to perform activities on its behalf.

Negotiation Framework

IPART's recommendations about the NSW rail access negotiation framework will put greater structure and rigor into the negotiation process.

Aurizon's experience with access regimes across various jurisdictions is that specification of key tasks and timeframes is beneficial, but sometimes ineffective if there is no consequence for a failure to meet those obligations. The proposed 3-month dispute resolution trigger creates an incentive for all parties to a negotiation to stay "on task".

It may also be worthwhile reporting on the number of negotiations that go beyond the 3-month period by mutual agreement of the parties. This data may assist in identifying potential bottlenecks in the process and inform any future decision to change the length of the negotiation period.

The recommendation to permit collective negotiations in the specified circumstances is welcomed. The function performed by the Rail Operators Group (ROG) collectively negotiating (with ACCC authorisation) with TfNSW on the 2018 Standard Track Access Agreement (STAA) has highlighted how difficult it is to get change made to an existing or standard contractual provision.

The STAA process has involved renegotiation of the entire access agreement (excluding pricing and other commercially sensitive matters) and for this reason has been comprehensive. The outcome is seen as critical to a successful rail freight industry and significant resources have been allocated by industry.

As one rail operator involved in this process, it is frustrating that finalisation of the STAA is still years away. However, it would be uncommercial for a single rail operator to have engaged in such an access negotiation. The reality for operators is that they need access to stay in business and they can't afford a lengthy negotiation.

In combination with the dispute resolution recommendations from IPART and the 3-month dispute trigger, the ability to negotiate collectively should increase an access provider's motivation to negotiate a mutually agreeable outcome.

Collective negotiation will also reduce duplication of negotiation costs for access providers.

Aurizon supports the inclusion of an obligation on access seekers to negotiate in good faith and considers that most rail operators will likely see value in this change. It is in everyone's (the access providers, access seekers/holders and IPARTs) interest to avoid unnecessary time and money being spent applying the undertaking in circumstances where access is not applied for in good faith, or negotiation is not proceeding in good faith. Such a provision could be used to cease or exclude a particular access seeker from collective negotiations as well as individual negotiations.

It may also be worth considering the inclusion of a frivolous or vexatious access requests clause in the undertaking, like that in the Western Australian Rail Access Regime (WARAR)⁹. This would allow the access provider to refer a particular access request/seeker to an arbitrator if they believe their request is frivolous or vexatious.

To avoid the potential for an access provider to use a frivolous or vexatious access requests clause to slow down or prevent access, the burden would be on the access provider to prove why the request is frivolous or vexatious. The arbitrator would assess whether the access request is genuine and there is an intention to obtain, and a reasonable likelihood of using, access rights.

Dispute Resolution

As mentioned above, Aurizon supports IPART's recommendations about dispute resolution and believes they will incentivise access providers to reach commercial agreement with access seekers.

Aurizon also endorses the suggestion that collective bargaining be recognised in the dispute resolution mechanism as well as the negotiation framework. Allowing joint or collective arbitration will improve the efficiency of the arbitration process and avoid the prospect of inconsistent arbitration outcomes where the same or similar matters are in dispute.

⁹ Government of Western Australia, *Review of the Western Australian Rail Access Regime Final Decision Paper*, February 2020, p 51-53

Section 44ZNA CCA is an example provision that allows the ACCC to jointly arbitrate 2 or more access disputes where more than one matter is in common in those disputes.

The inclusion of a conciliation option is noted. In our experience it can be difficult finding suitably qualified parties to undertake the role of conciliator, however, there doesn't seem to be any disadvantage in providing a voluntary option for access seekers to go down this path to resolve disputes. There may be value, however, in allowing an access seeker to ask IPART for its view on whether a particular dispute should go to conciliation first.

At clause 21(b) of IPART's arbitration practice directions¹⁰, there is reference to the arbitrator publishing the written determination of a dispute, setting out reasons for the decision, as soon as practicable after completing hearing the dispute. It isn't clear whether this 'publication' is just to the parties to the dispute, or broadly to the public.

Aurizon believes that an arbitrator should be required to publish (publicly) an arbitration report and statement of reasons. Information contained in arbitration determinations is likely to be useful to other parties negotiating in the future while not necessarily being commercially sensitive.

Other access regimes and undertakings, such as the ARTC Interstate Access Undertaking and HVAU and in undertakings made under the QCA Act, allow for discretion on whether arbitration determinations are published or kept confidential, either in full or in part. They also deal with regulator discretion to decide whether information submitted to them for an arbitration should be kept confidential.

Under the Queensland regime, the QCA can decide whether to release information, subject to the requirement that information is not released if a party's belief that releasing it would be commercially damaging is justified and releasing the information would not be in the public interest.

A similar discretion applies under the ARTC undertakings and was recommended for inclusion in the WARAR in the recent review of that regime¹¹.

Provided information owners are given adequate opportunity to support confidentiality claims, Aurizon supports IPART having the power to make an informed decision about whether information is commercially sensitive and determine what information will be published.

Information Disclosure

An imbalance in bargaining power is a key impediment to effective negotiated outcomes with monopoly network providers. Without sufficient information to assess the service being offered and the costs of providing that service, access seekers may settle for inefficient prices. In turn this may lead to unfair price differentiation between access seekers and undermine competition in the downstream rail haulage market.

¹⁰ IPART, *Arbitration under Part 4A of the Independent Pricing and Regulatory Tribunal Act 1992 (NSW) Practice Directions*, May 2012

¹¹ Government of Western Australia, *Review of the Western Australian Rail Access Regime Final Decision Paper*, February 2020, p 73

Aurizon supports the IPART recommendations to increase transparency of information provision by access providers regarding relevant costs and service performance standards.

However, in relation to the publication of prices paid by other users of the infrastructure, Aurizon is hesitant to agree with IPART. Aurizon has commented in more detail in the next section on the issue of price differentiation and in what scenarios it should be permitted by the rail access regime. We favour sufficient flexibility in the provision of access, including negotiation of variations to an existing access agreement, to improve the productivity and efficiency of rail operations to lower costs and improve competitiveness.

The price paid by another user for a similar service may legitimately differ based on differences in cost or risk. For example, one access holder's price might differ as it includes the costs of additional infrastructure specific to that access holder.

It is unclear how you could publish that price without also disclosing the specifics of the costs and risks that have been assumed, or at the very least, flagging that there is a quantifiable distinction between the services. Revealing the reason/s for the price variation may uncover commercially sensitive information. Publishing the price without the reason/s raises suspicion but is otherwise unhelpful to an access seeker or operator who wants to ensure they are not discriminated against.

One alternative is provided in the WARAR¹², where an access seeker may seek an opinion from the regulator on whether the price sought by the access provider is negotiations meets the non-discrimination obligations. The combination of proposed and current obligations on the access provider:

- not to price discriminate,
- to provide more comprehensive cost and service information up front, and
- to comply with an enforceable information disclosure guideline,

along with a provision enabling an access seeker to ask IPART's opinion (as per the WARAR) would be preferable to publication of all contracted access prices.

The Draft Report includes the recommendation for the avoidable costs associated with the service sought by the access seeker to be included in the indicative offer. Aurizon recognises an effective access regime needs to appropriately balance the benefits of information provision with the costs of its collection and maintenance. It is unclear from the draft recommendations whether the requirement to provide the avoidable costs is necessary for all indicative offers or only where the indicative offer is not otherwise the subject of a standing offer or there is a published price for the same service.

Aurizon notes that where an offer price is a standing offer or is the published price for the same service then the avoidable costs will have limited value in the negotiation process, particularly where the access provider and ultimately the arbitrator is bound by non-discrimination obligations. Therefore, Aurizon would welcome further clarification in the final report that the requirement to provide details of the avoidable costs is limited to the circumstances where that information is relevant to the negotiation process.

¹² Railways (Access) Code 2000 (WA), s.21

Non-pricing Provisions

Aurizon appreciates IPART's:

- review of the minimum terms and conditions that the NSW RAU currently prescribes for inclusion in an access agreement¹³ and
- recommendations for improving an access provider's accountability.

Capacity

Our comments in the section above titled, Accountabilities under the NSW RAU, detail the concerns Aurizon has about the responsibilities of TfNSW and ST in the MRN, particularly in relation to capacity allocation and management. As IPART has recognised, for the TAHE network, access providers have significant discretion in how they allocate capacity.

This creates significant perception of bias issues in the MRN where ST's top priority is the success of its vertically integrated commuter passenger services. The current Rail Timetable Review proposal has inflamed these concerns by outsourcing additional capacity allocation responsibilities to ST from TfNSW.

Aurizon believes that this scenario is comparable to that which existed in Queensland when the rail access regime¹⁴ was first introduced. At that time, the vertically integrated, State-owned network owner and operator, QR Ltd, proposed that scheduling and train control services would be provided by the same people who provided those services for and on behalf of the integrated passenger and freight operators.

The regulator (QCA) did not allow QR Ltd to implement this model. It had to structurally move the scheduling and train control function into the below rail business, and it had to implement onerous ring-fencing procedures to further ensure no unfair advantage was provided to its related operational businesses. In addition, its access undertaking includes clear rules around allocation of capacity, and management across the various scheduling timeframes and into the day of operation. Reporting metrics were also included in the regime.

Aurizon provides this example to back its support for IPART's recommendations regarding non-price provisions in an undertaking, particularly:

That the access provider allocate capacity according to well-defined steps that meet competitive neutrality and efficiency tests.¹⁵

Aurizon also supports the IPART recommendations regarding consultation in relation to expansions and infrastructure investment. Observing the success of the Hunter Valley Rail Coal Chain Coordinator and the Rail Capacity Group in ARTC's Hunter Valley network, and the Rail Infrastructure Group in Aurizon Network's CQCN, there is value in facilitating the development of industry group to represent the interests of operators and other supply chain participants. Aurizon would welcome the involvement of such a group in consultation into capacity investment and determination of system parameters in the TAHE networks.

Objective standards for rolling stock

Rolling stock standards and approval to operate is one area in which the lack of national harmonisation creates a barrier to entry and investment. However, there are also other issues, that IPART has identified, in some rail networks, that exacerbate the lack of inter-jurisdictional consistency. We believe that these issues are also related to the lack of clear accountability

¹³ IPART, *Review of the NSW Rail Access Undertaking Draft Report*, October 2022, p 75

¹⁴ *The Queensland Competition Authority Act 1997* (Qld), Part 5

¹⁵ IPART, *Review of the NSW Rail Access Undertaking Draft Report*, October 2022, p 77, draft rec 15.a

and responsibility in the governance arrangements for the TAHE network. We discussed these concerns earlier and won't repeat them here.

Aurizon supports IPART's recommended approach to dealing with approvals for rolling stock, on the ground that it will require the access provider to publish its approval process and put timeframes around key steps in the process. Accountability will be improved through the publication requirements.

Service level KPIs

Aurizon recognises that an effective access regime strikes an appropriate balance between transparency and confidence in the access provider's adherence to its obligations and the consequential regulatory burden imposed on the access provider.

Ideally many aspects of a framework for performance measuring, monitoring and information disclosure will involve cost to the access provider that should be minimised by ensuring regulatory obligations align with internal data collection and reporting frameworks. With respect to the TAHE network however, existing data systems do not appear adequate, and Aurizon believes that considerable work still needs to be done to develop necessary systems for collecting and reporting data before key performance indicators are developed and implemented.

Network performance is a particular issue on TAHE's MRN because it is densely trafficked, and passenger traffic has 'reasonable priority' over freight. The NSW Government has strategic policy goals to shift more freight onto rail¹⁶. Given two thirds of all freight in NSW moves through Greater Sydney and one additional 600m freight train could replace 54 trucks through this area¹⁷ there is strong public interest in ensuring correct modal choice to achieve the most efficient transportation outcome.

However, the 2021 report of the NSW Auditor-General into Rail freight and Greater Sydney¹⁸ revealed not only did the transport agencies not have strategies or targets in place to improve the efficiency or capacity of the MRN, but they also did not have sufficient information to know how to use the MRN to maximise freight without compromising passenger rail services because they lacked adequate data. The various agencies did not know what data was being captured, who owned it or how it could be shared to best effect.

A range of recommendations flowing from the Auditor-General's report focused on improving the collection and sharing of data to facilitate better analysis of train movements to support planning and policy decisions, including data about the management of delays to rail freight services. The deadlines set for TAHE and the government agencies to complete these recommendations has already past, and to Aurizon's knowledge, none have been met.

Aurizon acknowledges that TfNSW has commenced the Freight Level of Service (FLOS) project, that it hopes will improve customer experience and performance of rail freight on the MRN. This involves a specified level of service for rail freight that will be:

¹⁶ TfNSW, Future Transport 2056: TfNSW, Freight and Ports Plan 2018-2023

¹⁷ Audit Office of New South Wales, Rail Freight and Greater Sydney, October 2021, <https://www.audit.nsw.gov.au/our-work/reports/rail-freight-and-greater-sydney>

¹⁸ Audit Office of New South Wales, Rail Freight and Greater Sydney, October 2021, <https://www.audit.nsw.gov.au/our-work/reports/rail-freight-and-greater-sydney>

- reflected in the service contract between TfNSW and ST (for the performance of network management on the MRN)¹⁹, and
- reported on through KPIs

TfNSW has advised Aurizon that data collected will assist it in identifying infrastructure requirements and investment priorities to achieve an optimum long-term freight level of service. Aurizon's concern is that until TfNSW knows what the best combination of road and rail freight is, they won't know what levers to pull vis-à-vis network performance. Without any freight specific targets, the default through the MRN will be passenger first, and freight where possible. This doesn't incentivise a service provider such as ST to improve the use of rail freight capacity.

Aurizon believes that an incentive is required to achieve this because the current arrangement does not even recognise that a contracted access entitlement should, *prima facie*, be provided through the scheduling and train control function. The drafting of both the current and proposed Operational Protocols, referred to earlier in the section titled *Accountabilities under the NSW RAU*, describes the obligation of the RIM developing (or modifying) the SWTT (insofar as non-passengers paths are concerned) as "...*attempts to provide for all pre-existing non Sydney Trains or NSW Trains Train Paths within the new or varied SWTT....*"²⁰

Other regimes typically place absolute obligations upon access providers to provide contracted access rights, and then provide a small number of specific circumstances in which this obligation may be excused, for example, to schedule an ad hoc possession. Typically, the access provider must also consult with the access holder whose contracted service entitlement is not being met and provide a period of notice before the modification²¹.

A related issue to the establishment of network KPIs, is the development of operator KPIs. In practice a network provider has far greater ability to subject an operator to punitive provisions (e.g. suspension or termination) for failure to meet performance metrics, than an operator has for an access provider's failure in relation to network performance. For this reason, the information on which any enforcement is sought to be based must be verifiable and the process followed must be fair and reasonable.

TfNSW has also advised the ROG, as part of the STAA process, that it considers individual performance measures need be agreed with access seekers negotiating an access agreement.

While some access seekers may see value including bespoke performance obligations in their access agreement, Aurizon believes that standard performance metrics should be encouraged to reduce the cost of contract performance monitoring and the overall costs of access. The public disclosure or reporting of standard performance metrics is also supported, as:

- the performance measures of importance to operators are likely to be common across all access seekers,
- this reduces the costs associated with contract negotiations and monitoring, and
- it provides data on system performance that will give operators greater confidence that the access provider is complying with its obligations

¹⁹ known as the Rail Operations Agreement

²⁰ TAHE Operational Protocols, Version 4.0, s.2.3.2

²¹ For eg. see Queensland Rail's 2020 Access Undertaking (AU2), Schedule F cl.2

Aurizon notes that the performance indicator reporting in the ARTC Interstate Access Undertaking represents the minimum benchmark standard for performance reporting.²²

Setting Access Prices

Price differentiation

In relation to an access provider's ability to negotiate (or subsequently change an access price) away from a published or standing offer price, and consequently differentiate between access seekers competing in the same downstream market, Aurizon believes this should be permitted to reasonably reflect differences in the cost or risk to the access provider. This is the approach accepted in the Aurizon Network²³ and Queensland Rail²⁴ access undertakings.

For example, differentiation may be necessary to reflect differences in credit risk which underpins capacity reservation charges where the access seeker has agreed to a higher price as an alternative to provision of financial surety.

It is also important to ensure price differentiation provisions, for structurally separated access providers, are sufficiently flexible to promote innovation and efficiency. A rail operator may be willing to commit to higher performance standards through the more efficient use of assets and/or incur additional above rail costs to meet the higher standard, in the negotiation of a lower access price commensurate with more efficient use of existing capacity.

Aurizon also notes that a structurally separated rail access provider may elect not to price differentiate and rely primarily on standing offers (comprising price and terms). However, they should be permitted to price differentiate where this is consistent with the objects of the regime.

In this regard, in contrast to the broader definition of 'similar' services that applies in the ARTC Interstate Access Undertaking, the Draft Report refers to the 'same' service²⁵. Aurizon considers this is a preferable scope for an access provider to price differentiate where it aids efficiency²⁶.

In addition to differences in cost or risk of providing a service, there may be other reasons why a published rate may not be charged by an access provider. One primary reason would be to encourage modal shift to rail. The economic and environmental benefits of moving a freight task from ship or road to rail are well documented, and alone may justify price differentiation on the grounds of cost or risk. There is also longer term, strategic advantage in being flexible with price and / or conditions to facilitate new entrants to a network, provided this doesn't attenuate the service offering to existing network users.

Where an access provider does price differentiate and offers an alternate price to another access seeker then under the WARAR arrangements proposed in the *Information Disclosure*

²² <https://www.artc.com.au/customers/access/access-interstate/performance-indicators/reporting/>

²³ Aurizon Network's 2017 Access Undertaking (UT5), cl6.2.3(a)

²⁴ Queensland Rail's 2020 Access Undertaking (AU2), cl3.3(c)

²⁵ IPART, *Review of the NSW Rail Access Undertaking Draft Report*, October 2022, p 85

²⁶ Clause 6.5(b)(2) of the Competition Principles Agreement

section above, it would be necessary for them to demonstrate to IPART the basis for that differentiation.

Ceiling and floor tests

The Draft Report recommendations effectively retain a price floor limit (**direct costs** of a single service) and revenue floor limit (incremental costs of all traffics using a particular line segment). Aurizon notes that the former is necessary to ensure there is no cross-subsidy between traffics and the latter ensures there is no subsidy between the access provider and access holders, subject to the consideration of government support for public interest outcomes.

The inclusion of the levelised charge for variable major periodic maintenance costs in the definition of **direct costs** should promote sustainable access prices which seek to minimise or reduce the level of public contribution to the provision of rail services in NSW.

However, with respect to the ceiling test and the definition of **depreciation**, the Draft Report recommends that only obsolescence-related depreciation is captured in the depreciation allowance, ostensibly because major periodic maintenance is captured in the **direct costs** and factoring it into capital expenditure would lead to double counting²⁷.

This suggests that for an investment to be NPV = 0 all assets requiring like for like replacement (including items such as culverts that will require replacement over time but not necessarily through use) would need to be amortised in the direct costs if they are not able to be depreciated in the Regulated Asset Base (RAB) roll-forward.

This could require a material increase in **direct costs** and consequently an increase in the revenue floor. The practical effect of excluding non-obsolescence related depreciation from the RAB roll-forward is that the non-depreciating assets are subject to a DORC based depreciation model and the depreciating assets are subject to a Gross Replacement Value annuity (as they are assumed to be a perpetual asset maintained through major periodic maintenance).

Aurizon recommends that to make the proposed definition of **direct costs** work as intended, with no depreciation for asset renewals to be included in the Regulatory Asset Base, IPART should:

1. confirm what assets are assumed to be included in the definition of **direct costs** (i.e. levelised cost of replacement of assets worn out by use, including sleepers, ballast and rail), and
2. clarify that the reference to replacement of assets in the proposed definition of **depreciation** includes asset renewals not associated with major periodic maintenance.

Protection against hold-up strategies

Aurizon welcomes IPART's recommendation that an access provider must have regard to commercial requirements, such as any increase in the cost of access, in the renewal of an existing access agreement.

²⁷ IPART, *Review of the NSW Rail Access Undertaking Draft Report*, October 2022, p 89

In contrast to many dedicated bulk rail networks, access providers and access seekers under the NSW RAU are not able to commit to long term access prices and terms and conditions and may be subject to economic hold-up when renewing access agreements²⁸. This is a result of a combination of competition, transaction costs, uncertainty, and government transport policy.

It is important that any additional pricing provision dealing with hold-up risk, does not become a default mechanism for increasing access charges at renewal irrespective of other circumstances such as modal competition or market conditions.

For example, an existing service may pay an access charge above its direct costs so that the access provider is recovering more than the full incremental costs from all traffics. At the point of renewal of access, the direct costs of access may have increased by CPI + 1% but due to an increase in competition the total freight rate may have decreased by CPI – 2%. The consequence of increasing access charges by CPI + 1% to reflect the increase in direct costs is a reduction in the rail operator's margins. This is not the intended outcome.

Applying the ceiling test

Depreciation policy

The Draft Report notes that depreciation of the RAB should occur on a straight-line basis over the useful life of the assets. For the HVCN, the useful life of assets is determined with reference to weighted average mine life.

The Draft Report proposes to amend the depreciation requirements so that assets are depreciated over their useful lives rather than mine lives. IPART recognises that global decarbonisation policies may result in resources and reserves potentially exceeding long-term demand as mines cease operation, prior to resource depletion, due to changing economics. Consequently, demand for rail transport services will be a function of the demand for coal rather than the productive capacity of coal mines within the geographical catchment.

Similarly, this long-term demand uncertainty may be subject to change over time. IPART has recognised these issues and proposed²⁹ that:

- asset lives be determined with reference to line sectors rather than a single network point, and
- more frequent reviews of asset lives are carried out.

Aurizon supports the Draft Report's recommendations on the useful lives of assets on the basis it allows for a broader range of economic considerations than permitted under the current NSW RAU and makes the framework more responsive to long-term demand risks. This reduces uncertainty for operators in the current environment.

Rate of return

In line with the flexible approach recommended by IPART to the application of the NSW RAU, Aurizon believes it is appropriate to allow different rates of return to be applied to the different

²⁸ Note: this can arise due to information asymmetry due to the separation of the access provider from the market for rail freight transportation, as well as due to hold-up strategies.

²⁹ IPART, *Review of the NSW Rail Access Undertaking Draft Report*, October 2022, p 98

networks. This is consistent with the concept of determining a WACC reflective of an asset's underlying risk profile. It is also appropriate that the rate of return value be able to be re-assessed within the regulatory period, and not locked in for that period.

Loss capitalisation

Loss capitalisation can facilitate investment in rail infrastructure where the demand for the services provided by that investment is expected to grow over the expected life of that investment. Aurizon notes that under these circumstances, investment risk would conventionally be addressed through a backloaded depreciation profile. However, this would contradict the regime policy that requires depreciation is calculated on a straight-line basis.

The two examples of loss capitalisation allowed by other rail access regimes referred to by IPART are in ARTC's Hunter Valley Access Undertaking and the Queensland Rail Access Undertaking. Under both regimes the loss capitalisation applies to assets that were valued *after* the original investment was made.

In this regard IPART notes:

In practice, there may be limited use of this mechanism, as most investment in the NSW network is driven by government funding, with limited sections funded by access seekers³⁰.

Aurizon agrees there may be merit in the application of loss capitalisation, if the regulatory framework doesn't support backloading of depreciation, and government requires investments to be recovered through access charges from users. Under these circumstances, the access provider should provide details of the loss capitalisation approach, including how the costs are expected to be recovered from users over the useful life of the assets.

Compliance and enforcement

As noted above, publication of service quality information can support lower transaction costs in the negotiation and monitoring of performance under an access agreement.

Asset condition reporting may also be appropriate to enable access seekers assess the quality of service it may reasonably expect to obtain. This would include route maintenance history and asset renewals, track recording information etc.

Aurizon's experience across various rail networks is that the most critical components of effective, performance compliance reporting are a reliable system for collecting data, expertise to interrogate and present meaningful findings in an accessible manner, and willingness to investigate data further where justified. The comments above under the *Service level KPIs* section, detail some of our concerns around the current data collection capability of some access providers. Aurizon encourages IPART to recommend setting clear timeframes for access providers to implement the necessary systems to report compliance with levels of service they contract to provide to access seekers/holders.

³⁰ IPART, *Review of the NSW Rail Access Undertaking Draft Report*, October 2022, p 114

As indicated earlier in this paper, Aurizon endorses IPART's proposed new powers to investigate potential non-compliances, enforce compliance and impose sanctions where necessary.

In conclusion, Aurizon welcomes IPART's thorough review of the NSW RAU. We are available to answer any questions you have about this submission and look forward to receiving your final report in due course.

Kind regards,

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Manager
Commercial Development & Implementation
Coal Customers