



WHAT

This document sets out IPART's Final Decision on RailCorp's compliance with the New South Wales Rail Access Undertaking (the undertaking) for its Hunter Valley Coal Network (HVCN) in 2015-16, 2016-17 and 2017-18. Our final decisions are that:

- ▼ RailCorp's asset valuation roll-forward for the HVCN meets the undertaking requirements
- ▼ RailCorp's HVCN access revenue was below the ceiling in 2015-16 and 2016-17 but above the ceiling in 2017-18.

This is not the first compliance review where we have found that revenue for the HVCN has exceeded the ceiling amount. We share the concerns of stakeholders that the NSW regime has not been effective in dealing with this.

We have made several recommendations aimed at improving the regime including recommending that the NSW Government asks IPART to review the undertaking and note that there is broad stakeholder support for such a review.



WHERE

The rail infrastructure covered by this decision is the five sectors of the HVCN between Newstan Junction and Woodville Junction.



WHO

NSW Government-owned RailCorp is the operator of the relevant HVCN rail infrastructure. It sells rail access to

operators of coal and non-coal freight trains.



WHEN

This compliance assessment relates to the financial years 2015-16, 2016-17 and 2017-18.



WHY

As a rail infrastructure owner, RailCorp is required to submit annual compliance statements. These statements enable IPART to determine whether RailCorp has complied with the asset valuation roll forward and ceiling test requirements of the undertaking.



HOW

IPART reviews RailCorp's submitted asset valuation roll-forward, ceiling test and unders and overs account by testing the logic of RailCorp's calculations and the reasonableness of the cost inputs. In doing this we have regard to the arguments put forward by RailCorp, benchmarking data and our previous regulatory decisions. We also considered stakeholder feedback on our draft decision.



WHAT NEXT

RailCorp's annual compliance submission for the 2018-19 year is due by 31 October 2019.

1 Overview of decisions and recommendations

Decisions:

1. RailCorp has complied with the asset valuation roll forward principles in the NSW Rail Access Undertaking for 2015-16, 2016-17 and 2017-18
2. RailCorp has complied with the ceiling test in the NSW Rail Access Undertaking in 2015-16 and 2016-17, as its access revenue was below the full economic cost of providing access.
3. RailCorp has not complied with the ceiling test in 2017-18, as its access revenue for two groups of access seekers exceeded the full economic cost of providing access.

Recommendations:

1. RailCorp updates its unders and overs account balances using the under and over recoveries calculated by IPART, set out in Table 3.10. For the combined access seeker group, this results in a closing balance at 30 June 2018 of \$7,956,472 (over recovery).
2. In future compliance submissions, RailCorp provides additional analysis of its unders and overs account in support of its proposed starting values for the coal only access seeker group and the general freight access seeker group.
3. The NSW Government asks IPART to undertake a review of the NSW Rail Access Undertaking.
4. In future compliance submissions, RailCorp publishes access revenue, annual under/over-recoveries and the unders and overs account balance on a per gross tonne kilometre, per train kilometre and a per net tonnes shipped basis. This should be done separately for each group of access seekers – coal, general freight and the combined group.
5. RailCorp revises its unders and overs account policy. We will assist RailCorp to develop a policy that meets the needs of stakeholders and will consult with a wide range of stakeholders as part of the approval process.

2 Assessment of compliance with the asset valuation roll forward principles

The NSW Rail Access Undertaking (the undertaking) requires RailCorp to submit documentation demonstrating its compliance with the asset valuation roll forward principles. These principles are set out in clause 3 of schedule 3 of the undertaking and provide that the regulatory asset base (RAB) in any given year is equal to the RAB in the prior year plus the CPI increase on that prior RAB, plus capital expenditure in the given year, less depreciation and any asset disposals in the given year. Depreciation is to be calculated on a straight line basis using the estimate of the remaining mine life set by IPART.¹

¹ IPART, *NSW Rail Access Undertaking - Review of the rate of return and remaining mine life From 1 July 2014, Final Report and Decision*, 15 July 2014.

Table 2.1 sets out RailCorp’s proposed roll forward calculation for combined coal and general freight. We consider that RailCorp’s roll forward calculation is reasonable and consistent with the requirements of the undertaking.

Table 2.1 RailCorp’s proposed Asset Valuation Roll Forward combined coal and general freight Access Seekers (\$)

RAB Component	2015-16	2016-17	2017-18
Opening RAB	15,086,489	14,856,597	14,564,098
Opening RAB x CPI	290,332	225,100	294,292
Add CAPEX	0	0	0
Add Additions	0	0	0
Less Depreciation	-520,224	-520,318	-520,325
Less Disposals	0	0	0
Closing RAB	14,856,597	14,564,098	14,338,286

Source: RailCorp compliance submission, April 2019, Table 5, p 12.

Decision

- 1 RailCorp has complied with the asset valuation roll forward principles in the NSW Rail Access Undertaking in 2015-16, 2016-17 and 2017-18.

3 Assessment of compliance with the ceiling test

The undertaking also requires RailCorp to demonstrate that it has complied with the ceiling test set out in the undertaking, which provides that the revenue for any access seeker, or group of access seekers, must not exceed the cost of providing access. The cost is to be estimated as the full economic costs on a standalone basis. The ceiling test is set out in clause 1 of Schedule 3 of the undertaking.

RailCorp’s compliance submission states that under its own estimates of access revenue and full economic costs:

- ▼ The ceiling test is not met for the combined group of access seekers in 2017-18
- ▼ The ceiling test is not met for the coal group in 2015-16, 2016-17 & 2017-18
- ▼ The ceiling test is met for the general freight access seekers in all years.

We consider that RailCorp has calculated the ceiling test for the appropriate groups of access seekers but we do not accept the proposed values of all the components of RailCorp’s full economic cost.

Our decision in relation to RailCorp’s compliance with the ceiling test is that:

- ▼ The ceiling test is met for the combined group of access seekers and the coal only group in 2015-16 and 2016-17
- ▼ The ceiling test is not met for the combined group of access seekers in 2017-18

- ▼ The ceiling test is not met for the coal group in 2017-18
- ▼ The ceiling test is met for the general freight access seekers in all years.

More information on our assessment is set out below.

Relevant access seekers or groups of access seekers

RailCorp submitted ceiling tests conducted on three different bases:

1. Combined coal and general freight access seekers
2. Coal access seekers
3. General freight access seekers.

In our view the three groups proposed by RailCorp are appropriate and as a result, we have focused our compliance assessment on the three ceiling tests submitted.

The sectors required on a standalone basis are the same for all three groups of access seekers (that is, they all use the same assets). This means that the full economic cost is similar for each group, differing only to the extent that direct costs (variable maintenance costs) differ.

IPART assessment of RailCorp's proposed full economic costs

RailCorp's proposed Full Economic Cost for each group of access seekers is the sum of the following cost components:

- ▼ Maintenance costs
- ▼ Corporate & system overheads
- ▼ Network control costs
- ▼ Depreciation
- ▼ Return on assets.

Overall, RailCorp's proposed costs are more reasonable than those proposed in the past. However, in calculating the ceiling tests for the individual access seeker groups, RailCorp has allocated its overall costs to each of the coal and general freight groups rather than estimate a standalone cost for these groups of access seekers, as required by the undertaking. As a result, some of our recommendations for these groups result in a higher cost than estimated by RailCorp.

Maintenance costs

RailCorp's proposed maintenance costs are set out in Table 3.1. These estimates are based on a benchmarking exercise undertaken by consultants SNC Lavalin using publicly available data.²

² SNC Lavalin, TfNSW Rail access review, 26 March 2019.

Table 3.1 RailCorp proposed maintenance costs – by access seeker group (\$ nominal)

	Combined access seeker group	Coal access seekers	General freight access seekers
2015-16	4,606,131	1,814,205	2,791,926
2016-17	5,026,441	2,005,067	3,021,374
2017-18	5,749,204	2,713,192	3,036,012

Source: RailCorp, *Hunter Valley Coal Network submission on compliance with the pricing principles in the NSW rail access undertaking 2015-16 to 2017-18*, April 2019, pp 15-17.

SNC Lavalin used the limited benchmarking data that was publicly available from ARTC’s Hunter Valley export coal system, Aurizon’s Moura coal network and QR’s West Moreton network. It summarised the key cost and usage data for each of these comparators. SNC Lavalin used the benchmarking data to estimate the total maintenance cost (the sum of routine maintenance and major periodic maintenance) as a rate per thousand gross tonne-kilometres (gtk) for each system. They found that this rate varied markedly between systems:

- ▼ ARTC HVCN \$3.09 per thousand gtk
- ▼ Aurizon Moura \$7.41 per thousand gtk
- ▼ QR West Moreton \$13.18 per thousand gtk.³

RailCorp did not use the ARTC HVCN benchmark when proposing its maintenance costs. RailCorp submits that the ARTC should be excluded as a benchmark comparator as it has very large volumes of coal and enormous economies of scale, which distort comparisons with RailCorp’s HVCN, which has very low volumes.

SNC Lavalin considered that an efficient cost for RailCorp’s HVCN as a standalone network would lie somewhere between \$7.41 and \$13.18 per thousand gtk. RailCorp used a cost of \$10 in its compliance submission.

We do not consider that RailCorp’s proposed maintenance costs are reasonable and as a result, we have used our own estimates. Our estimates are lower than RailCorp’s proposed maintenance costs for the combined access seeker group but higher for the other two access seeker groups, as our estimates have a higher proportion of fixed costs than RailCorp’s.

IPART analysis

Overall we consider that RailCorp’s maintenance estimates for 2015-16 to 2017-18 are more reasonable than their proposed costs for 2014-15 and prior years. The use of consultants SNC Lavalin has produced better estimates than RailCorp’s previous modelling approach.

However, we disagree with the following aspects of the proposed maintenance costs:

- ▼ The exclusion of ARTC’s HVCN from the benchmark comparators
- ▼ The estimation of maintenance costs on a per thousand gtk (all variable cost) approach.

³ RailCorp, *Hunter Valley Coal Network submission on compliance with the pricing principles in the NSW rail access undertaking 2015-16 to 2017-18*, April 2019, p 10.

In our view, ARTC’s network costs should not be excluded from the benchmarking analysis. RailCorp’s five sectors form part of the broader HVCN. RailCorp has leased the remainder of the network (32 sectors) to ARTC on a long term basis. We included the ARTC sectors in our previous benchmarking analysis.

While the traffic densities are substantially higher than those on the RailCorp HVCN and the two Queensland comparators, we expect that across all three comparator networks there would be:

- ▼ A similar range for fixed maintenance costs per track km
- ▼ A similar range for variable maintenance costs per gross tonne-kilometre.

We have analysed the SNC-Lavalin data on this basis and found no reason to reject the ARTC data point as an outlier. We consider that obtaining a maintenance cost estimate by dividing total costs by gtk is a less robust approach because it does not adequately account for the differences between the three networks, including differences in traffic density.

Using the benchmark data obtained by SNC Lavalin (for 2017-18), we have analysed the cost drivers based on the total costs, track kilometres and gtk for each of the three comparator rail networks (using regression analysis) and found that:

- ▼ The overall maintenance costs for RailCorp’s HVCN from this analysis are lower than proposed by RailCorp
- ▼ The benchmark fixed cost is \$68,861 per track km and variable cost is \$1.58 per gtk
- ▼ For the network as a whole, approximately 80% of the maintenance costs are fixed compared with RailCorp’s proposal which essentially treats all costs as variable with gtk.

The fixed and variable costs identified by our benchmark analysis are set out in Table 3.2.

Table 3.2 Comparison of fixed and variable maintenance costs (\$ nominal)

	IPART 2014-15	RailCorp 2017-18	IPART 2017-18
Fixed maintenance cost (per km of track)	33,607	0	68,861
Variable cost (per thousand gtk)	3.38	10.00	1.58

Source: IPART 2014-15 compliance statement, RailCorp compliance proposal and IPART analysis of SNC’s benchmark data.

Our approach takes into account all of the available (albeit limited) data. In our view, it better accounts for differences in network characteristics for both fixed and variable costs than RailCorp’s proposed approach of dividing total costs by gtk.

We consider that there is a level of maintenance that is required regardless of volumes transported. Rail infrastructure maintenance involves a number of fixed costs that are not driven by track usage, including:

- ▼ Routine track inspections for safety
- ▼ Repair and cyclical replacement of structures (ie, bridges and culverts)
- ▼ Repair and cyclical replacement of any signalling and communication system assets
- ▼ Sleeper replacement

- ▼ Ballast cleaning and renewal (of which the majority is driven by time but some proportion of this cost is also affected by usage).

Maintenance costs also include the following components, which do vary with the frequency and weight of trains using the track:

- ▼ Rail replacement
- ▼ Resurfacing (ie, rail grinding and correction of alignment by fettling track).

Where traffic levels are relatively low, we expect that the majority of maintenance costs incurred would be fixed and a minor portion would be variable.

As a result, we consider that our analysis of the benchmark data results in maintenance cost estimates that are more in line with the fixed and variable nature of maintenance costs than RailCorp’s estimates. The results of our analysis are also more consistent with the fixed to variable cost ratio we have adopted in previous years, which was based on benchmarking analysis previously undertaken for us by Sapere and Booz. We used a Maintenance Cost Index (MCI) to deflate the 2017-18 unit costs to calculate our maintenance cost estimates for 2015-16 and 2016-17, consistent with the approach we have used in previous years to inflate maintenance costs over time.⁴ Our recommended maintenance costs are set out in Table 3.3.

Table 3.3 IPART maintenance cost estimates – by access seeker group (\$ nominal)

	Combined access seeker group	Coal access seekers	General freight access seekers
2015-16	4,107,547	3,685,933	3,833,581
2016-17	4,251,102	3,786,079	3,942,500
2017-18	4,491,905	4,010,751	4,061,912

Source: IPART analysis

IPART’s decision estimates for the coal only and general freight only access seeker groups are higher than what RailCorp proposed because our analysis suggests that a large proportion of maintenance costs are fixed. On the other hand, RailCorp’s estimates, which are based on a dollar per gtk value, are lower because of the lower access volumes from these two groups. Note that for the coal only access seeker group, using RailCorp’s proposed maintenance costs, RailCorp does not meet the ceiling test for this group in any of the three years whereas under our maintenance cost estimates RailCorp does not meet the test in 2017-18 only.

Network control costs

RailCorp estimated network control costs (Table 3.4) based on a figure of \$2.86 per train kilometre. RailCorp submits that these costs are reasonable given that if the separate network control centre were to be established to operate trains over the RailCorp HVCN it would need to be staffed on a 24/7 basis which would require six network control staff on rotating shifts.

⁴ We estimated the fuel cost sub-index (3.2% of the MCI) using only Sydney terminal gate prices for unleaded petrol (80%) and diesel (20%). In past years we also included Newcastle unleaded petrol prices in this calculation. As Sydney and Newcastle unleaded petrol prices are highly correlated this change makes a negligible difference to the MCI calculated.

Table 3.4 RailCorp proposed network control costs – by access seeker group (\$ nominal)

	Combined access seeker group	Coal access seekers	General freight access seekers
2015-16	513,241	174,066	339,175
2016-17	554,395	191,826	362,568
2017-18	626,903	260,544	366,360

Source: RailCorp, *Hunter Valley Coal Network submission on compliance with the pricing principles in the NSW rail access undertaking 2015-16 to 2017-18*, April 2019, pp 15-17.

We consider that RailCorp’s proposed network control costs for the combined access seeker group are reasonable. However, we consider that for the coal only and general freight only access seeker groups, RailCorp’s proposed network control costs have not been determined on a standalone basis. We have adopted the same estimates for these groups as for the combined group reflecting the fixed nature of these costs.

IPART analysis

RailCorp’s network control costs for the combined group of access seekers 2015-16 to 2017-18 are in line with those we have previously adopted. We consider they are reasonable and recommend adopting these estimates for the ceiling test. We note that RailCorp has built these costs up from a cost per train kilometre, which suggests that these costs depend on usage of the track.

This is not consistent with our previous analysis that these costs are largely fixed costs nor with RailCorp’s comments that there is a minimum cost associated with network control when costs are looked at on a standalone basis. In our view, this means that RailCorp’s cost estimates for the coal only and general freight only access seeker groups are understated. We have adopted the same network control cost for each access seeker group in calculating the ceiling test (Table 3.5).

Table 3.5 IPART network control costs – by access seeker group (\$ nominal)

	Combined access seeker group	Coal access seekers	General freight access seekers
2015-16	513,241	513,241	513,241
2016-17	554,395	554,395	554,395
2017-18	626,903	626,903	626,903

Source: IPART analysis

Corporate & system overheads

RailCorp’s corporate & system overhead costs were estimated as 13.7% of the sum of maintenance and network control costs. That percentage reflects Sydney Trains current accounting practice. RailCorp’s proposed corporate and system overheads are set out below.

Table 3.6 RailCorp proposed maintenance costs – by access seeker group (\$ nominal)

	Combined access seeker group	Coal access seekers	General freight access seekers
2015-16	701,354	272,393	428,961
2016-17	764,574	300,974	463,600
2017-18	873,527	407,402	466,125

Source: RailCorp, *Hunter Valley Coal Network submission on compliance with the pricing principles in the NSW rail access undertaking 2015-16 to 2017-18*, April 2019, pp 15-17.

We do not consider that RailCorp’s proposed corporate and system overhead costs are reasonable. As a result, we have used our own estimates. As these estimates are a mark-up on maintenance & network control costs, our cost estimates are lower for the combined access seeker group and higher for the coal and general freight groups than RailCorp’s proposal.

IPART analysis

In our previous RailCorp compliance reviews, we used a rate of 9.2% of the sum of maintenance and network control costs to determine an efficient level of corporate & system overheads. This value was derived from industry benchmarking commissioned by IPART.⁵ In our 2014-15 compliance assessment we considered RailCorp’s proposed rate of 10.6% to be above the rate for comparable networks.

In its 2015-16 to 2017-18 compliance proposal, RailCorp has not provided evidence to support the higher 13.7% rate. We consider that RailCorp’s proposed corporate and system overhead costs are not reasonable. We have instead continued to estimate these costs using the rate of 9.2%.

Table 3.7 sets out the corporate and system overhead costs that we have estimated. The difference between the two sets of estimates is the combined effect of the reduction in the rate applied and the different maintenance costs adopted by IPART (see above).

Table 3.7 Comparison of IPART and RailCorp corporate and system overhead costs for the combined access seeker group

	Combined access seeker group	Coal access seekers	General freight access seekers
2015-16	425,113	386,324	399,908
2016-17	442,106	399,324	413,714
2017-18	470,930	426,664	431,371

Source: IPART analysis and RailCorp’s compliance submission

The corporate and system overheads we have adopted are significantly lower than those proposed by RailCorp for the combined access seeker group. However, as these costs are estimated as a percentage of maintenance costs, and we found that maintenance costs are largely fixed, the corporate and system overhead costs allocated to the coal and general freight access seeker groups are higher than the estimates proposed by RailCorp.

⁵ IPART, Final Report, Compliance with the NSW Rail Access Undertaking RailCorp HVCN, 2009/10, p 8.

Depreciation and return on assets

As noted, we are satisfied that RailCorp has correctly rolled forward its RAB. We are satisfied that RailCorp has used the correct depreciation and return on assets for the combined access seeker group. However, RailCorp has estimated the depreciation and return on assets values for the coal only and general freight only access seeker groups by apportioning the values for the combined group based on access volumes (Table 3.8).

Table 3.8 RailCorp proposed depreciation and return on assets – by access seeker group (\$ nominal)

	Combined access seeker group		Coal access seekers		General freight access seekers	
	ROA	Depn	ROA	Depn	ROA	Depn
2015-16	883,321	520,224	388,371	228,728	494,950	291,496
2016-17	867,910	520,318	382,958	230,418	484,953	289,900
2017-18	852,620	520,325	409,502	269,696	443,118	250,629

Source: RailCorp, *Hunter Valley Coal Network submission on compliance with the pricing principles in the NSW rail access undertaking 2015-16 to 2017-18*, April 2019, pp 15-17.

We consider that RailCorp's proposed depreciation and return on assets for the combined access seeker group are reasonable. For the coal and general freight groups we consider that the same value should be used as for the combined access seeker group, which results in higher costs for these groups than proposed by RailCorp.

IPART analysis

The undertaking is clear that the depreciation and return on capital that should be used for the ceiling test for any group of access seekers is the value that is relevant for the sectors that are used by those access seekers. Both the coal and general freight groups use the entire five sectors of RailCorp's HVCN. As such, the same depreciation and return on capital should be used for all three groups (Table 3.9).

Table 3.9 IPART depreciation and return on assets – by access seeker group (\$ nominal)

	Combined access seeker group		Coal access seekers		General freight access seekers	
	ROA	Depn	ROA	Depn	ROA	Depn
2015-16	883,321	520,224	883,321	520,224	883,321	520,224
2016-17	867,910	520,318	867,910	520,318	867,910	520,318
2017-18	852,620	520,325	852,620	520,325	852,620	520,325

Source: IPART analysis

IPART's calculation of the ceiling test

Using the costs that we consider reasonable, the results of our ceiling test calculations are shown in Table 3.10.

Our assessment of the ceiling test indicates that in 2017-18 RailCorp's access charges do not comply with the requirements of the undertaking for both the combined access seeker group and for the coal access seeker group, as access revenue exceeds the full economic costs of providing access.

Table 3.10 IPART ceiling test

Combined access seeker group	2015-16	2016-17	2017-18
Maintenance costs	4,107,547	4,251,102	4,491,905
Network control costs	513,241	554,395	626,903
Corporate and system overheads	425,113	442,106	470,930
Depreciation	520,224	520,318	520,325
Return on assets	883,321	867,910	852,620
Full economic cost	6,449,446	6,635,831	6,962,684
Access revenue	6,379,502	6,037,864	8,756,261
Over recovery	-69,944	-597,967	1,793,577
Coal only access seeker group	2015-16	2016-17	2017-18
Maintenance costs	3,685,933	3,786,079	4,010,751
Network control costs	513,241	554,395	626,903
Corporate and system overheads	386,324	399,324	426,664
Depreciation	520,224	520,318	520,325
Return on assets	883,321	867,910	852,620
Full economic cost	5,989,043	6,128,026	6,437,263
Access revenue	4,804,654	4,304,336	6,931,163
Over recovery	-1,184,389	-1,823,690	493,900
General freight access seeker group	2015-16	2016-17	2017-18
Maintenance costs	3,833,581	3,942,500	4,061,912
Network control costs	513,241	554,395	626,903
Corporate and system overheads	399,908	413,714	431,371
Depreciation	520,224	520,318	520,325
Return on assets	883,321	867,910	852,620
Full economic cost	6,150,274	6,298,837	6,493,131
Access revenue	1,574,848	1,733,528	1,825,098
Over recovery	-4,575,426	-4,565,309	-4,668,033

Source: IPART calculations and RailCorp's compliance submission

Decisions

- RailCorp has complied with the ceiling test in the NSW Rail Access Undertaking in 2015-16 and 2016-17, as its access revenue was below the full economic cost of providing access.

- 3 RailCorp has not complied with the ceiling test in the NSW Rail Access Undertaking in 2017-18, as its access revenue for two groups of access seekers exceeded the full economic cost of providing access.

4 Operation of RailCorp's unders and overs account

While IPART is not required to assess compliance with the unders and overs account, IPART is to have regard to the operation of the unders and overs account as part of its compliance review.

RailCorp submitted that the Unders and Overs Account balance for the combined access seeker group at 30 June 2018 should be \$4,423,943 overpayment by customers (RailCorp compliance submission table 11, p 18). RailCorp also submitted unders and overs accounts for the other two groups of access seekers. RailCorp's unders and overs account values are shown in Table 4.1 below.

Table 4.1 RailCorp proposed unders and overs account (\$ nominal)

Item	Combined access seeker group	Coal access seekers	General freight access seekers
Balance at 30 June 2015	6,830,805		
2015-16 estimated under-recovery	-844,769	1,926,891	-2,771,660
Balance at 30 June 2016	5,986,036		
2016-17 – estimated under-recovery	-1,695,774	1,193,092	-2,888,866
Balance at 30 June 2017	4,290,262		
2017-18 – estimated over-recovery	133,681	2,870,827	-2,737,146
Balance at 30 June 2018	4,423,943		

Note: Annual under recoveries are negative and annual over-recoveries are shown in red

Source: RailCorp compliance submission, April 2019, Table 11, p 18.

For the combined access seeker group, the starting account balance at 30 June 2015 adopted by RailCorp accords with our final decision on RailCorp's HVCN compliance for 2014-15, and therefore we consider it is reasonable. However, as noted in section 3 above, we disagree with RailCorp's estimated under-recoveries in 2015-16 and 2016-17 and its estimated over-recovery in 2017-18. The under and over-recoveries that result from our decisions give a positive account balance (over-recovery) of \$7,956,472 at 30 June 2018. Our derivation of this figure is shown in Table 4.2.

Table 4.2 IPART unders and overs account balances – combined access seeker group

Item	\$
Balance at 30 June 2015	6,830,805
IPART decisions:	
2015-16 under-recovery	-69,944
Balance at 30 June 2016	6,760,861
2016-17 – under-recovery	-597,967
Balance at 30 June 2017	6,162,894
2017-18 – over-recovery	1,793,577
Balance at 30 June 2018 (over recovery)	7,956,472

There is no relevant starting value for an unders and overs account for the coal and general freight groups of access seekers. We consider that any accounts established for these access seeker groups should be adjusted over the three years from 2015-16 to 2017-18 using the amounts included in IPART’s calculation of the ceiling test. We also consider that RailCorp should provide additional analysis with regard to the relevant starting values of these accounts, as it may not be reasonable to start these accounts with a zero balance at 30 June 2015.

Recommendations

- 1 RailCorp updates its unders and overs account balances using the under and over recoveries calculated by IPART, set out in Table 3.10. For the combined access seeker group, this results in a closing balance at 30 June 2018 of \$7,956,472 (over recovery).
- 2 In future compliance submissions, RailCorp provides additional analysis of its unders and overs account in support of its proposed starting values for the coal only access seeker group and the general freight access seeker group.

5 Improving the effectiveness of the current regime

The undertaking was drafted in 1999. At that time, the infrastructure covered by the regime was different and access regimes across the country were in their early stages of development. Twenty years on, there is information to suggest that the regime is in need of review.

In our recent review of the rate of return and remaining mine life, we recommended that the NSW Government ask IPART to review the undertaking. We received a range of complaints about the current regime and broad support for a review. The comments we received came from rail infrastructure owners, rail access seekers, users of rail freight services and other regulators.

One of the areas of dissatisfaction raised is continued over-recovery by RailCorp (as an infrastructure owner), pointing to the lack of an effective compliance regime. The undertaking imposes obligations on rail infrastructure owners regarding how the unders and overs account should be operated (see Box 5.1). However, IPART has no compliance role in relation to these requirements.

We consider that there is a clear need to review and update the undertaking as this is the only way to address the inadequacy of the compliance/enforcement regime, as well the regulatory overlap between the NSW and federal access regimes.⁶ In the interim there are two other measures that would go some way to addressing stakeholder concerns about overcharging:

- ▼ More transparent compliance reporting in relation to over-recoveries
- ▼ A more comprehensive unders and overs account policy.

We received a submission from Pacific National in support of this view stating that “the undertaking is not effective in constraining monopoly behaviour. The over-recovery (and the under reporting of the over-recovery amount) is further evidence of this deficiency.”⁷ In addition, Pacific National considers that the current regime does not adequately reflect the benefits to the community of moving freight from road to rail and that this mode-shift should be one of the aims of reviewing the undertaking.⁸

Recommendation

- 3 The NSW Government asks IPART to undertake a review of the NSW Rail Access Undertaking.

Box 5.1 Unders and overs account requirements

Clause 4 of Schedule 3 of the Undertaking states that:

- a) The Rail Infrastructure Owner will establish an Unders and Overs Account to manage average deviations around the maximum rate of return.
- b) The Rail Infrastructure Owner will keep an account for Access Seekers and groups of Access Seekers who could potentially breach the Ceiling Test.
- c) The Rail Infrastructure Owner will provide an annual reconciliation of each account to the applicable Access Seekers.
- d) The Rail Infrastructure Owner will attempt to return the account balance to zero each year.
- e) The Unders and Overs Account balance should not exceed +/- 5 percent of forecast access revenue.
- f) The Rail Infrastructure Owner will develop and publish a policy for the operation of the Unders and Overs Account in consultation with Access Seekers and submit to IPART for approval.

⁶ See IPART’s final report, Mine Life and Rate of Return under the NSW Rail Access Regimes, July 2019, ch 4.

⁷ Pacific National submission, 14 August 2019.

⁸ Pacific National submission, 14 August 2019.

Greater transparency in relation to over-recoveries

We understand that it is typical, but not universal, for contracts between rail operators and users of freight rail services to include access charges as a direct pass-through. Users of freight rail services, who ultimately pay the access prices, do not always have a contractual relationship with the rail infrastructure owner. Where a user's contract is in place with the rail operator, the user may need to negotiate directly with the rail infrastructure owner to ensure that any rail access over-payment is rectified. However, in order to do this, the users of freight rail services require additional information in order to estimate what portion of the total over-recovery, if any, relates to them.

We consider that there would be value in rail infrastructure owners publishing additional unit rate data that users of rail freight services have information to assist them in working out how much of an over/under-recovery relates to them. This should be done as part of the annual compliance return for any network where there is an unders and overs account.

We obtained gross tonne kilometres (GTK), train kilometres (km), trips and gross tonnes shipped (GT) from RailCorp. Table 5.1 sets out the difference between the total fees paid and the ceiling price calculated by IPART for each year between 2015-16 and 2017-18 on a per unit basis.

Table 5.1 Annual average fee paid compared with ceiling price per unit (\$ nominal)

	2015-2016	2016-2017	2017-2018
Per thousand GTK			
Coal	-5.81	-8.11	1.64
General Freight	-17.62	-16.15	-16.63
Combined Group	-0.15	-1.18	3.08
Per km			
Coal	-19.46	-27.19	5.42
General Freight	-38.58	-36.01	-36.44
Combined Group	-0.39	-3.08	8.18
Per trip			
Coal	-346.41	-508.84	104.64
General Freight	-639.03	-615.68	-622.49
Combined Group	-6.61	-54.36	146.79
Per GT			
Coal	-0.10	-0.15	0.03
General Freight	-0.33	-0.31	-0.32
Combined Group	0.00	-0.02	0.06

Note: A negative value indicates that fee paid was below the ceiling amount. A positive value indicates that the average fee paid exceeded the ceiling amount.

Source: Information provided by Transport for NSW and IPART analysis

Recommendation

- 4 In future compliance submissions, RailCorp provides access revenue, annual under/over-recoveries and the unders and overs account balance on a per gross tonne kilometre, per train kilometre and a per net tonnes shipped basis. This should be done separately for each group of access seekers – coal, general freight and the combined group.

Updating the unders and overs account policy

RailCorp's compliance submission acknowledges the current over-recovery and states that it is reviewing its pricing framework with these obligations in mind. We support Railcorp's review of its pricing framework and we also recommend that RailCorp updates its unders and overs account policy. We will work with RailCorp to develop an appropriate unders and overs policy that meets the needs of stakeholders.

We approved the current policy over 10 years ago. While the policy was developed in consultation with access seekers (rail operators) at that time, access revenue for RailCorp's five HVCN sectors had not approached the ceiling, so there was no actual over-recovery. A revised policy should outline in sufficient detail how any under or over-recovery would be recovered or refunded or used to offset access prices.

In drafting the policy, RailCorp should consider options for ensuring that any refund or price off-set for an over-recovery is delivered to the party who made the overpayment irrespective of how contracts are structured between rail operators and end users. For example, this may favour reducing the overs balance by offering discounted access prices in the future rather than via lump-sum refunds. We are happy to assist RailCorp to develop an appropriate approach.

The requirement to consult on the proposed unders and overs policy specifies that RailCorp must consult with access seekers. We consider that consultation should involve users of rail freight services who ultimately pay access charges in addition to rail operators. Consultation should include how the over-recovery is allocated amongst access seekers (and/or end users) as well what information will be made available to each party and when.

Recommendation

- 5 RailCorp revises its unders and overs account policy. We will assist RailCorp to develop a policy that meets the needs of stakeholders and will consult with a wide range of stakeholders as part of the approval process.

September 2019