PRODUCTIVITY COMMISSION INQUIRY

LEGISLATION REVIEW OF CLAUSE 6 OF THE COMPETITION PRINCIPLES AGREEMENT AND PART IIIA OF THE TRADE PRACTICES ACT 1974

AUSTRALIAN RAIL TRACK CORPORATION SUBMISSION

The Issues Paper prepared by the Productivity Commission in relation to its inquiry into a legislation review of Clause 6 of the Competition Principles Agreement (CPA) and Part IIIA of the Trade Practices Act (TPA) 1974 was issued in October 2000. The inquiry gives effect to a commitment made, as part of the NCP, by the Commonwealth and States and Territories to review the national access arrangements after five years of operation. The paper covers such issues as current access arrangements, including the Part IIIA national access regime and industry specific regimes, the use of and rationale for the national regime, means of improving the regime, access, and the implication for any changes on Clause 6, industry specific regimes and other regulation. The Commission has sought comment on these issues.

It is understood that the Commision will be coordinating its processes to ensure that relevant information is shared between this inquiry and a concurrent inquiry into telecommunications services addressing the industry specific access regime for those services. It is also recognised that there are overlaps between this inquiry and the inquiry into the Prices Surveillance Act (PSA) for which the Commission has recently released an interim report.

The Australian Rail Track Corporation (ARTC) is a Limited Corporation established under Corporations Law in February 1998 and commenced operations in July of that year. Commonwealth ownership of ARTC is held jointly by the Department of Finance and Administration and the Department of Transport and Regional Development. ARTC was created after the Commonwealth and State Governments agreed, through an Inter-Government Agreement (IGA) in 1997, to the formation of a 'one stop' shop for all operators seeking access to the national interstate rail network. This was seen as a means of furthering the IGA objectives of expanding the rail industry through improved efficiency and competitiveness, increasing the rail share of the interstate freight market and encouraging investment to improve rail infrastructure. ARTC is not permitted to conduct above rail activities.

ARTC currently has responsibility for the management of 4430 route kilometres of standard gauge interstate track, mainly in South Australia, Victoria and Western Australia. A wholesale access agreement, which allows ARTC to provide a one-stop shop for current and potential train operators seeking access to the national interstate standard gauge rail network in Western Australia has recenue been negotiated with Westrail. Negotiations are progressing between ARTC, Rail Access Corporation

(NSW) and Queensland Rail for ARTC to obtain similar wholesale access agreements with these organizations. Under the IGA, ARTC is required to submit an undertaking dealing with access to the interstate rail network to the ACCC. A draft discussion form of this undertaking has been recently provided to the ACCC and ARTC's customers for comment.

The national interstate rail network has significant spare and available capacity and ARTC, in order to achieve it's objectives, must seek substantial growth in the interstate rail freight market and increase utilisation of it's asset in order to provide sufficient long term returns and attract investment.

The interstate freight market is highly competitive where rail has, over the past decades, struggled to maintain market share against its main rivals road and sea. In order to be competitive with road, in particular, rail pricing must in most cases be below that of road in order to compensate for a perceived deficiency with respect to road in non-price choice factors such as flexibility, reliability and transit time.

It is generally recognised that the long distance road transport industry is not paying, through taxes and charges, for the full cost of it's shared usage of the infrastructure. As a result, rail would be unable to compete with road if it were required to pay the full cost of maintaining its infrastructure in the long term. In order to achieve it's objectives, ARTC must take additional long term market risk by pricing at a level which, using any asset valuation which seeks to ensure long term preservation and improvement of the asset (eg DORC, DAC), would not provide a return. At this level, rail is able to provide a competitive price/service package to the industry. Rewards, in the longer term, would come through market growth.

There are currently a number of state based access regimes which operate on various parts of the interstate rail network. The NSW Rail Access regime was certified as effective by the NCC in late 1999 for a period of 12 months, with a view to it being reviewed at that time to assess consistency with the national regime for those parts of the NSW infrastructure considered part of the national network. The rail industry structure in NSW is vertically separated.

A certification application by the WA Government before the NCC for the WA Rail Access Regime has recently been withdrawn. This regime has a term of five years and included applicability to the interstate standard gauge network in that state. The NCC had considered the regime as satisfying the principles of Clause 6 of the CPA in all areas except for one left unresolved, being the uncertainty as to the interface between the WA regime and the national regime. The relevant legislation has been passed by parliament (but not yet proclaimed) and the Access Code has been gazetted. The freight arm of the WA Government Railways (Westrail) has recently been privatized as a vertically integrated entity, with the sale conditions requiring the new owner to organizationally separate its monopoly and contestable activities. The regime has been designed around the activities of a vertically integrated service provider.

An access undertaking submitted by Queensland Rail (QR) to the Queensland Competition Authority (QCA) is yet to be approved. It is understood that the QCA has concerns about QR's approach to separating its monopoly and contestable activities and its effect on competition on rail in that state. The undertaking is currently not applicable to that part of the standard gauge interstate network in Queensland. QR is to remain as a vertically integrated service provider.

The Tarcoola – Alice Springs section of the interstate network is soon to be leased at a peppercorn rental to the operator of the Alice Springs – Darwin network. This part of the network is covered by the AustralAsia Railway Access Regime certified as effective in early 2000. Certification is until 31 December 2030. The operator of the Tarcoola – Darwin network will be vertically integrated.

The Issues Paper has raised a number of issues (as questions) under broad headings. This submission will detail ARTC's consideration and comment with respect to some of these questions below.

Rationale for a national access regime

Are the circumstances in which a facility would seek to deny access widespread?

Should vertically integrated bottleneck facilities be treated differently than non-integrated facilities? Is the real concern underpinning access regimes denial of access, or the price and conditions of access?

ARTC draws some fundamental distinctions between third party and open access regimes.

A "third party" access regime, as applies where a vertically integrated track owner competes with third parties for above rail activity, is designed to regulate the activities of an organization which has a commercial imperative to minimize third party access to the infrastructure and reduce competition for its contestable activities ('closed shop'). The organization can give effect to this imperative in a range of ways both conspicuous and inconspicuous. The focus with respect to an access regime in this case is generally on ease of access, ring-fencing, information flows, anti-competitive conduct and dispute resolution. The access regime is generally designed to reduce the risk to third parties by restricting some of the more obvious behaviours associated with anti-competitive activities. Such activities include cross-subsidisation of above and below rail activities, hindering access to the network (at the negotiation stage or during operations) and internal flow of market information.

It is extremely difficult for a regulator to monitor and/or appropriately remedy the more inconspicuous behaviours which could occur, and for which the owner has a commercial incentive to carry out. Such behaviours may include the use of creative accounting techniques to disguise cross subsidization of activities, information 'leaks', day-to-day resolution of operational conflicts and strategic investment (or lack thereof) in contestable parts of the network. Such behaviours are difficult to detect, and only surface via a market outcome after the commercial damage, which can be significant, has been done. Penalties are often minor compared to the extent of damage that could be experienced by the third party.

The type of market resulting from a third party regime is usually thin and closed. Access is individually negotiated, lacks transparency and pricing more often reflects the users ability to pay.

Such an arrangement is generally only suitable where the synergy benefits of vertical integration are necessary for the owner to compete effectively intermodally, and outweigh any benefit of having competition on rail. The Productivity Commission in its final report "Progress in Rail Reform" (August 1999) proposed that urban passenger and low volume branchline networks are more suited to this type of arrangement.

An "open" access regime applies where the track owner has a commercial imperative to maximize value through the encouragement of above rail activity to increase asset utilization. Access revenue is the sole revenue source. Above rail competition is seen as a catalyst for market growth. An open access regime generally focuses moreso on ensuring the owner does not extract monopoly rents from the asset, providing incentives to the owner to improve productivity, invest efficiently in the network, maintain or improve asset performance, and on appropriate risk sharing arrangements. Often, intermodal competition limits the ability of the owner to over-price. Disincentives for anticompetitive behaviours as described above need not be as strong, if at all relevant.

Under this arrangement, the market for access generally contains more participants and is open in nature. Pricing is often transparent and more equitable, and risks are appropriately shared. The market tends also to be more value driven and is conducive to such elements as secondary trading and auctioning.

Such an arrangement is appropriate where intramodal competition would drive intermodal competitiveness through reducing costs and improved service, further resulting in community benefits. This is currently the case with respect to the interstate network and this type of industry structure and regime is viewed as appropriate in the report referred to earlier. Where intermodal competition is slight or not existent, as occurs on the Hunter Valley and Queensland coal networks, ARTC considers that a vertically separated, open access arrangement would be appropriate in all but a very limited number of circumstances, where separation would severely impede the 'production process' of the owner. The potential for the collection of monopoly rents would require a more 'heavy handed' regime in this area.

What is the evidence that access regulation reduces prices and/or improves the range and quality of services available to end users?

How do the costs of access regulation compare with the costs of not facilitating access for third parties?

Does the relativity between benefits and costs vary across infrastructure segments?

There is little doubt that the introduction of above rail competition in the rail freight industry in Australia generally, and to the interstate rail freight industry in particular, has resulted in major benefits to end users both in terms of reduced prices and service quality. It also appears that the extent of the benefit is, to some extent, proportional to the extent of intramodal competition, or at least the threat of competition. The benefits are likely to be higher where there is less intermodal competition.

On the east-west interstate rail corridor, it is generally recognized that freight transport costs have fallen around 30-40% since the introduction of on rail competition on this corridor. Access cost yields to train operators have fallen as a result of the operation of more efficient above rail asset configurations brought about by changes to the infrastructure. In addition, selective investment in the network and above rail assets during this time, together with competitive forces has significantly improved service timeliness and reliability on this corridor. The result of this is that rail's market share of the total land freight market to WA has increased from around 60-65% to 70-75% since 1995. The community has reaped significant benefits in terms of lower transport costs, more efficient service provision, plus the external benefits associated with reducing the incidence of heavy haul road transport.

It is probably fair to say that the vertical separation of a large part of the east-west interstate rail corridor, together with the presence of a highly efficient intermodal competitor, were largely responsible for the advent of this competition rather than access regulation per se. From the outset, ARTC, and its predecessor, sought to encourage growth in the relevant interstate freight markets by encouraging third party access and competition, and by pricing access in such a way so as to improve rail's competitive position in the market as well as encourage more productive use of both below and above rail assets.

It could be argued that, in this sort of business environment, the benefits of access regulation are smaller and may not outweigh the cost of such regulation. As stated in the Issues Paper, access regulation may have more of a role to play in relation to the inter-operability of networks as well as to service quality. On the other hand, the presence of a vertically integrated infrastructure owner and/or lack of intermodal competition would alter this argument.

What are the regulatory alternatives to access regimes? In the longer term are the differences between access regulation and more explicit price control (eg prices surveillance) likely to be significant?

Where a third party access regime exists (vertically integrated provider), it is likely that access regulation, in addition to any price control, would continue to be necessary, notwithstanding earlier comments as to the effectiveness of such a regime in curbing anti-competitive behaviours.

Should access regulation be in the form of a national regime, industry specific arrangements or a combination of both.

ARTC sees a place for both a national regime and industry specific arrangements. Where an industry specific arrangement exists, however, an entity should have the choice as to whether it applies the provisions of that arrangement, without reference to the ACCC, or submit an alternative undertaking to the ACCC, to meet the specific business circumstances in which that entity operates.

As an example, the gas industry has a code which has been primarily designed around the provision of access to existing pipelines with significant current cashflows and are operating at a higher level of utilization. The focus of the code appears to be on providing third parties with rights of access to pipelines, an enforceable means to establish those rights, and inhibiting serious monopolistic behaviours, whilst protecting the interests of pipeline service providers. It is ARTC's view that the code would not promote vigorous competition in the natural gas market and may serve, to some extent, as a barrier to entry into the market, and investment. Aspects of the code which bring about this view are the setting of reference tariffs to recover full cost of service provision, including a return, depreciation and non-capital costs. The code also appears to leave scope for a degree of price discrimination between users.

Where a new 'greenfields' pipeline is built which would commence operation with only a small proportion of capacity being utilized and where the operator is taking significant market risk, a different type of undertaking, designed to promote gas-on-gas and pipeline-on-pipeline competition, to develop the market, to competitively price transportation services and to stimulate growth. Such an undertaking may require a different approach to pricing of access and the facilitation of access provision, such as a more transparent and non-discriminatory 'open' approach. In this case, the operator should be free to submit an undertaking to the ACCC, designed to suit these specific requirements.

As it stands under the national code, if the pipeline meets most of the criteria for declaration (excluding the tests for national significance and existence of an applicable effective access regime), as assessed by the NCC, then the NCC must recommend to the relevant Minister that the pipeline be covered under the code.

Improving the current national access regime

Should the national access regime contain a clearer statement of objectives?

Could other parts of the TPA or prices control/surveillance provide a more effective remedy where access is generally provided, but at monopoly prices? If so, should access regulation focus solely on vertically integrated infrastructure providers?

Should Part IIIA apply only to natural monopoly facilities? If so how should natural monopoly be defined? Should the focus be on natural monopoly technology (eg rail infrastructure) in the broad, or more narrowly on situations where a natural monopolist has the scope to obtain significant monopoly rents?

In order to assist with the facilitation of a more consistent approach by regulators to regulation of access to rail and other infrastructure, ARTC would support a statement of the objectives of the national access regime. Such objectives would clarify the definitions and criteria associated with the various paths to gaining access and provide greater certainty to access providers and seekers.

It was stated in the issues paper that s152AB of the TPA (specifically relating to the telecommunications access regime) provides that 'The object of this Part is to promote the long-term interests of end users of carriage services or of services provided by means of carriage services'. This provision logically infers some protection of the interests of a number of parties including the service provider, direct users of carriage services, and the public.

The Report by the Independent Committee of Enquiry (Aug 1993) and titled 'National Competition Policy' (otherwise known as the Hilmer Report) cited three main factors creating the imperative for developing a national competition policy. These factors included:

- An increasing acknowledgement that Australia is for all practical purposes a single integrated market, where the economic significance of State and Territory boundaries is diminishing rapidly as advances in transport.
- Trade policy reforms have markedly increased the competitiveness of the internationally traded sector where many goods and services provided by public utilities, professions and some areas of agriculture are sheltered from international and indeed domestic competition.
- Domestic pro-competitive reforms implemented to date (1993) have all been progressed on a sector-by-sector basis, without the benefit of a broader policy framework or process.

In the seven years since this report, there have been significant developments in competition reform with only some degree of success, when considered in the national context.

The report further states that borne out of the above considerations, Governments agreed on the need to develop a national competition policy which would give effect to the principles set out below:

- No participant in the market should be able to engage in anti-competitive conduct against the public interest;
- As far as possible, universal and uniformly applied rules of market conduct should apply to all market participants regardless of the form of business ownership;
- Conduct with anti-competitive potential said to be in the public interest should be assessed by an appropriate transparent assessment process, with provision for review, to demonstrate the nature and incidence of the public costs and benefits claimed;
- Any changes in the coverage or nature of competition policy should be consistent with, and support, the general thrust of reforms:
    - To develop an open, integrated domestic market for goods and services by removing unnecessary barriers to trade and competition;
    - In recognition of the increasingly national operation of markets, to reduce complexity and administrative duplication.

The above principles, where the emphasis appears to be protecting the public benefit and recognition of the increasingly national nature of the Australian economy, would, where applied to the more specific provision of access for 'nationally significant' infrastructure, form the basis for the objectives of the national access regimes.

Given the business environment in which ARTC operates, where any ability to extract monopoly rents from the market is removed by the presence of strong intermodal competition, ARTC would agree that the focus of Part IIIA should be more narrow as described above.

A vertically separated provider with a commercial imperative to stimulate use of the asset operating in a price constrained market could, to a large extent, operate without legislation. This commercial imperative would also provide stimulus for the provider to operate and invest efficiently and meet service quality standards.

Would it be sensible to define a list of industries to which the national regime applies, or does changing technology make this an inappropriate approach?

Given the changing nature of industries and markets, it would be inappropriate to have such a list. It may be possible to miss industries/markets to which the national regime should apply. In some cases, the mere threat of Part IIIA application to an industry, may limit some monopolistic behaviours without direct intervention.

Is the list of activities currently excluded from Part IIIA appropriate? Does the exclusion of 'production processes' create particular problems? For example, could it encourage firms to vertically integrate to avoid declaration under the regime?

The current definition of service, and in particular the treatment of production processes in the definition, has resulted in some problems where the NCC's interpretation of the intent of the definition has failed a legal test (Hamersley Iron Pty Ltd v The NCC & Ors). This legal interpretation seems to encourage vertical integration and other business structures designed to avoid declaration. If exclusion of production processes from Part IIIA is desirable, then the definition needs to be more specific.

Criteria for declaration

Should there be more guidance in Part IIIA itself with respect to declaration criteria?

What is meant by national significance? In seeking to delineate the national and State-based regimes, could the national significance criterion leave important intrastate facilities outside the purview of any regime?

Provided that there is a certification or similar mechanism in place for State-based regimes to minimize the potential for regulatory duplication, is a national significance test necessary?

The test for national significance should include a number of criteria as assets can have an impact nationally in a variety of ways. Such a test should be suitably flexible. It could be expected however that any decision on national significance would in the end be more of a matter of judgement in specific circumstances. Some suggested criteria (not exhaustive) might be:

- Does the service provided by the facility have a bearing on the national economy? This may be a test of the significance of the impact of the service on, say, national GDP.

- Does the service have any impact on activity outside of the state in which the related facility is located? That is, does the service have any impact on interstate or international trade?

ARTC is also concerned about the public interest test being stated in the negative. It has often been argued that the introduction of competition in industries servicing both suburban and regional Australia would see a reduction in services to regional areas. Pre-competition, regional services would have been cross-subsidised by higher (monopoly) profits extracted from suburban users. Competition would limit these profits and the ability of the service provider to cross-subsidise. The negative public interest

test places this issue at the foot of the NCC/ACCC to be dealt with under the competitive reform framework.

Cross-subsidisation should be exposed as such and un-commercial activities, if cessation is considered to be to the detriment of the public interest, should be funded separately and outside of the competitive framework. Relief from the competitive framework under the negative public interest test merely enables the service provider to continue to mask cross-subsidisation.

The negative interest test could thus be considered unnecessary, where negative impacts on the public interest, if deemed intolerable by the community, such as that described above, should be handled outside the competitive framework.

Certifications/Undertakings

How well are the certification and undertaking mechanisms working? What improvements could be made to them? What are the pros and cons of combining the two?

ARTC is of the view that the current process which enables State Governments alone to seek to establish an access regime via the certification path through the NCC, whilst any other private entity must submit an arrangement to the ACCC, is both unnecessary and unbalanced. It also results in a proliferation of inconsistent regimes designed to protect the owner of the asset and associated revenue streams to varying extents, in combination with the industry structure (integrate, separate) provided for.

Certifications/Undertaking

All entities, whether they be public or private should submit an access regime to the ACCC. The ACCC would then assess whether the service satisfies the national significance test, and depending on the outcome, determine whether the regime should be administered by itself, a national regulator or a state based regulator. The process and criteria for assessment of regimes would be consistent. Only the administration of the regime would vary.

Declaration

Similarly, all parties seeking declaration of a service provided by a facility should seek that declaration from the ACCC. Once again, the ACCC would assess the national significance of the service. Where the service was nationally significant, the recommendation would be made to the Commonwealth Minister.

With regard to eligibility to lodge an undertaking, under s44ZZA of the TPA, an undertaking may be lodged by 'a person who is, or expects to be, the provider of a service'. In s44B, provider is defined as follows:

"'Provider', in relation to a service, means the entity that is the owner or operator of the facility that is used (or is to be used) to provide the service."

Here, the provider is defined as the owner or operator of the facility rather than the operator of the service. This has potential to give rise to anomalies where the owner or operator of the facility may not necessarily be the operator who provides the relevant service. This was noted by the Full Court of the Federal Court in Rail Access Corporation v NSW Minerals Council limited (1998).

Potentially the provider of the service may not be able to submit an undertaking, whereas the owner or operator of the facility must submit the undertaking but is not the provider of the service. This issue is of particular relevance to ARTC with regards to the submission of an undertaking for those parts of the interstate network not owned or leased by ARTC (as required by the IGA), but for which access to interstate services will be managed by ARTC in accordance with the wholesale agreement between ARTC and the owner.

Is there a rationale for having different criteria for the three access routes accommodated by Part IIIA?

The process described above obviates the need for an access route via certification.

In any event, there should be consistency with regards to the criteria for the three paths to gaining access.

Role of Ministers

What are the pros and cons of Ministerial involvement in Part IIIA processes?

Under the current arrangements, recommendations with respect to declaration of state provided services go to the relevant State Minister, otherwise the recommendation goes to the Commonwealth Minister. Certification recommendations go to the Commonwealth Minister, and the undertaking process has no Ministerial involvement.

Under arrangements proposed by ARTC, all declaration recommendations would go to the Commonwealth Minister, reinforcing the nationally significant nature of the service. It is understood that the facility involved may be state owned or operated, but it seems inconsistent that a State Minister has the right to open a facility up to competition or not where the facility provides a nationally significant service. The current result of this

inconsistency is that there are very few declared facilities. The process of State Ministerial approval, where the Minister is not required to make decisions public (except to the parties involved), and where no decision within 60 days represents a rejection (without the requirement to publish reasons, makes a rejection an easier decision for the State Minister who is likely to have some interest in the protection of the facility owner/operator.

Regulatory Bodies

Why is there a need for both the NCC and ACCC to be involved in the administration of Part IIIA?

The process as described above does not envisage the involvement of the NCC. The ACCC would absorb all roles currently carried out by the NCC.

Pricing issues

Should Part IIIA include some explicit pricing principles?

ARTC would not support the inclusion of explicit pricing principles as flexibility is needed at the undertaking level to develop a pricing approach which best meets the needs of the relevant industry. Forcing a service provider to operate within an explicit pricing framework may restrict entrepreneurialism. As technology and commercial practices alter over time, the industry may require an approach not envisaged in Part IIIA.

How can pricing regimes best deter the entry of firms that are unable to deliver services in related markets as efficiently as the facility owner?

What constitutes anti-competitive discriminatory pricing? How should regulators differentiate between efficiency enhancing discrimination and anti-competitive behaviour?

The need for a regulator to differentiate such behaviours will largely be governed by the motives of the relevant service provider. In a third party access environment, the threat of anti-competitive behaviour is far greater. In an open access environment any price discrimination is more likely to be driven by a need to maximize efficiency and promote growth, with the provider having little incentive to act anti-competitively.

With regard to how a regulator could differentiate between such behaviours, ARTC proposes that, in an open access environment, the onus of proof should be on the party

asserting anti-competitive conduct by the service provider. In a third party access environment, the onus should be on the service provider to prove that the behaviour was not anti-competitive.

Should access prices be based on the existing configuration of facilities, or should they try to anticipate technological developments and the like?

Maximum access prices for a service should be based on the configuration of facility that users of the service would choose, should they duplicate the monopoly facility in an efficient manner themselves. In duplicating the facility, the users would utilize currently available and most efficient materials and labour supply, and would seek to provide sufficient capacity to meet at least medium term demands, with respect to usage, characteristics of service provision and quality.

In a competitive environment, access pricing to users of the service should be no more than the price the user can afford to charge in the users competitive market place less the users efficient short run costs, if not restricted by the first maximum price test above. The user could not commercially sustain a position in that market otherwise.

Alternatively, access pricing should not be less than the incremental costs to the provider of providing the service. Where pricing is less than the price charged by the user in the users competitive market place, less the users efficient long run costs, there is potential, through competition, for pricing in the users marketplace to fall. The extent to which this may occur, resulting in end user benefits, depends on the level of competition in that market place.

Asset Valuation

What are the pros and cons of the various asset valuation methodologies available to access price regulators? What lessons have already emerged?

ARTC accepts that all methodologies suffer from deficiencies and offer advantage to varying extent and in certain circumstances. These deficiencies and advantages have been widely documented. The choice of an appropriate methodology is specific to the circumstances of the industry involved and the characteristics of the service provider and should, above all, address the reasonable business interests of the service provider and the need for future investment in the asset.

ARTC is concerned however with the proliferation of differing interpretations and permutations of the commonly used methodologies available. For example, the DORC approach involves a number of separate considerations each of which can be interpreted in a variety of ways. Often the interpretations made are based on convenience and assumption.

ARTC would propose that available methodologies be more precisely defined for the purposes of the TPA to add greater credibility to the approach and provide greater certainty to both providers and users.

Access holidays

Are access holidays an appropriate option for addressing some of the adverse impacts of mandated access on investment in infrastructure facilities? Is the pricing regime in place for the Tarcoola to Darwin rail link broadly equivalent to an access holiday?

Tarcoola - Alice Springs regime has not been structured to encourage competitors to the operator of the network. High rate of return, cross-subsidy of Alice Springs – Darwin asset with Tarcoola – Alice Springs asset despite lease at peppercorn rent and established revenue base. This, no doubt makes the investment more favourable to private investment, and may well enable the investment to materialise. This is however at a cost to the shareholders associated with the public investment in the project (Tarcoola – Alice Springs) given that the regime is likely to result in lower levels of service, higher pricing and monopoly pricing than might otherwise have been the case. Whether the economic benefit of having the rail link justifies the cost of restricting competition would not appear to have been proven at any time. The project economics should stand alone without this implied direct and indirect cost to the community.

Given that the regime has been certified for thirty years (with a five year review by the relevant minister of the NT/SA governments; a situation not seen as effective by ARTC) this may end up resulting in a very lengthy access holiday.

If it were deemed that the benefit of this rail link justified the cost to the community of such a holiday, ARTC considers that it would have been appropriate to 'call it as it is', and define the holiday specifically rather than structure a regime to encourage such an outcome.

Comparing some of the alternative pricing approaches

How well do the various access pricing methodologies rate with respect to the trade-off between precision and undue complexity? Will the most appropriate methodology depend on the facility or infrastructure sector in question?

The choice of pricing methodology should be flexible and the most appropriate methodology will depend on the business environment in which the service provider operates. Factors which could impact on the choice of methodology include:

- The structure of the industry – whether the service provider is vertically integrated or separated, whether the market is thin or not, the extent of competitive neutrality existing in the market, the extent to which risk should be apportioned.
- The type of service – homogeneous commodity, differentiable services
- The extent of competition in the market place – competition for the service, competition with other services
- The way in which the market places differential value on the service
- Market sophistication - technology
- Internal factors – risk apportionment, revenue adequacy

ARTC's approach to pricing is predicated upon the following factors:

- ARTC operates in a competitive environment where constraints on rail freight and access pricing come from competitive pressure of other modes, particularly road. As such, ARTC is unlikely in any of its markets to be able to price at levels that will recover the full economic costs of its assets. As such, ARTC is taking considerable market risk which it is seeking to mitigate through a pricing policy which encourages market growth.
- ARTC seeks to stimulate customer confidence and market growth in the evolving market in which government owned vertically integrated railways are being replaced by privately owned operators with access to shared infrastructure. As the manager of a significant part of the interstate track infrastructure, ARTC has adopted the concepts of equity and transparency as key elements of its pricing policy. ARTC will not price discriminate on the basis of the identity of the customer, the commodity being transported or the market being served.

ARTC's approach is pricing is based around the negotiate and arbitrate framework. A seeker of access has some certainty in the pricing of access being underpinned by ARTC's commitment to equity and transparency. ARTC publishes a market negotiated price for access in the most common and competitive intermodal freight transport market, where competing operators run trains with similar operating characteristics, as an indicative price for access. Guidelines for pricing negotiations require prices to reflect:

- Indicative prices
- Cost of additional capacity
- Specific service characteristics including, but not limited to, axle load, speed, train length, time of day and week
- Commercial impacts on ARTC's business including, but not limited to, term of access, growth potential, business foregone in consequence, credit risk
- Logistical impacts on ARTC's business included, but not limited to, impact on other trains, reduced system capacity and flexibility
- Capital or other contributions by the seeker

Prices will not reflect:

- The identity or characteristics of the seeker
- Whether the train is provided by the Government or otherwise
- The commodity carried
- The end market served.

Once negotiated in a particular set of circumstances, prices will become transparent to the market and will serve as a guide to pricing for another seeker wishing to operate in, substantially, the same set of circumstances.

ARTC revenue derived from a particular part of its network will be limited to a floor representing the incremental cost associated with that part of the network and a ceiling representing the full economic cost of that part of the network.

Trading of capacity between users is permitted with ARTC approval. ARTC recognizes that market efficiency would best be served where the price paid for access reflects the true market value of that access and that the access seeker is in the best position to assess that value. ARTC will, therefore, promote the use of an efficient auctioning mechanism to price and sell access.

Are there alternatives to regulated price setting for access? For example would auctioning access to a declared service obviate any need for the regulator to set access prices? In what circumstances would auctioning access be a practical option? Would auctioning reduce the monopoly rents earned by the facility owner, or simply provide for efficient allocation of existing capacity in the facility?

Auctioning of access, in conjunction with a simple and flexible mechanism for secondary trading in access, could provide an efficient means of pricing access. The price paid would represent the value of the access to the user. It would be necessary to have some form of reserve in such a situation to ensure revenue adequacy to the infrastructure owner. In addition, the market for access would need to be competitively neutral.

How effective is clause 6 of the CPA in providing an underpinning for the national access regime and in establishing guiding principles?

By way of example, there would appear to be three means by which the NCC or track owner have endeavoured to facilitate a national approach to access on the national rail network.

- Where the infrastucture is not owned or leased by ARTC, exclude that part of the national network within the state jurisdiction from the state based regime with a view to it being included within the scope of the national regime. This has been done in Queensland. As it stands, the nature of the wholesale agreements either negotiated or being negotiated with the states by ARTC, where ARTC has exclusive right to sell access to interstate services on that part of the interstate network in each state, but does not directly maintain or control day to day usage of the network, places a legal question over whether ARTC is the provider of the service, and therefore can submit an undertaking covering that part of the network, as envisaged by the IGA. In this case it may be necessary for the owner of the infrastucture to submit an undertaking consistent with the national regime despite not being the party whose activities would be most affected by the provisions of an undertaking. This anomaly was eluded to earlier.
- The NCC would retain that part of the national network in the state within the scope of the state regime and seek to achieve consistency between the state regime applying to that part of the network and the national regime via the certification process, under the principles of Clause 6. This is yet to be achieved so far. With respect to the NSW regime, where certification lapses at the end of 2001, the ability of the NCC, and Clause 6, will be tested as the NCC seeks to achieve consistency between the NSW regime and the national regime before extending the certification.
- In WA, the NCC originally sought to exclude interstate train operations from the scope of the state based regime. This action was reversed by the NCC after it made an interpretation of the Hammersley Iron v Robe River ruling which resulted in a legal view of the definition of a 'service'. It was asserted that specific operations on a part of the infrastucture could not be excluded from the regime on the basis that those operations originated or terminated outside of WA. Since then, the NCC has requested the WA Government to submit a separate undertaking with respect to these services (yet another approach). This was rejected by the WA Government. The application for certification has subsequently been withdrawn by the WA Government, with the issue left unresolved.

It can be seen from the above that Clause 6 of the CPA, and possibly parts of Part IIIA, do not provide a clear mechanism by which consistency of access to the national network, where different parts are owned and/or operated by different parties, and are subject to different regimes, can be achieved. As such, access to the interstate network on a consistent basis under a single framework, without a truly national approach to control of the network, will be difficult to achieve in the short to medium term.