Australian
Competition &
Consumer
Commission

Draft Decision

Australian Rail Track Corporation

Application to Vary Access Undertaking – Interstate Network

December 2008

CONTENTS

Glossary

ACCC	Australian Competition and Consumer Commission
ARTC	Australian Rail Track Corporation
IAA	Indicative Access Agreement
Network	The interstate rail network managed by ARTC
SCT	Specialised Container Transport Logistics
Service provider or provider	In relation to a service, means the entity that is the owner or operator of the facility that is used (is to be used) to provide the service.
The Tribunal	The Australian Competition Tribunal
The Act	*Trade Practices Act 1974 (Cth)*
WACC	Weighted Average Cost of Capital

Executive Summary

Draft Decision

The Australian Competition and Consumer Commission's (ACCC) draft decision is to not consent to Australian Rail Track Corporation's (ARTC) application to vary the 2008 Interstate Rail Access Undertaking (the Undertaking) submitted on 9 October 2008 on the basis of, and for the reasons outlined, in this Draft Decision.

ARTC's 2008 Interstate Rail Access Undertaking

On 30 July 2008, the ACCC released its Final Decision to accept ARTC's Undertaking. The Undertaking came into operation on 20 August 2008 and will remain operative until 2018 (unless withdrawn earlier).

The Undertaking covers the terms and conditions that ARTC applies in negotiating access for all traffic on the Interstate Rail Network (the Network). The Network covers the mainline standard gauge track linking Kalgoorlie in Western Australia, Adelaide, Wolseley and Crystal Brook in South Australia, Melbourne and Wodonga in Victoria and Broken Hill, Cootamundra, Albury, Macarthur, Moss Vale, Unanderra, Newcastle (to the Queensland border) and Parkes in New South Wales (NSW).

Schedule D of the Undertaking is an Indicative Access Agreement (IAA) which forms an essential part of the Undertaking. The IAA is a *Track Access Agreement* that is used as the basis for the terms and conditions on which the ARTC agrees to grant a rail operator access to the Network.

Application to vary the Interstate Rail Access Undertaking

On 9 October 2008, ARTC applied to the ACCC for consent to vary the Undertaking under Part IIIA of the *Trade Practices Act* 1974 (the Act). The variation application relates to the indemnity and loss regime in clause 15 of the IAA of the Undertaking so that the liability of either party to third parties for loss or damage is limited in certain circumstances.

Under subs. 44ZZA(7) of Part IIIA of the Act, a service provider may vary an undertaking at any time, but only with the consent of the ACCC. The ACCC may consent to the variation if it thinks it appropriate to do so having regard to the specified statutory criteria.

The ACCC has considered ARTC's variation application and assessed whether, overall, it would be appropriate to consent to the variation after having had regard to the criteria in s. 44ZZA of the Act. In making that assessment the ACCC has drawn on:

- ARTC's Undertaking including the IAA;
- ARTC's variation application (which includes its supporting submission); and
- submissions from interested parties on the variation application.

Applying for a variation of the Undertaking – Threshold issues

Prior to making a request to the ACCC to vary the Undertaking, ARTC must meet certain pre-conditions which are set out in the Undertaking.

Change of circumstances

Under clause 2.4(a) of the Undertaking, before ARTC can seek to vary the Undertaking, it must be of the opinion that there has been a change of circumstances such that the Undertaking is no longer commercially viable for the ARTC or it has become inconsistent with the objectives prescribed at clause 1.2 of the Undertaking.

Given the low threshold for meeting this pre-condition, the ACCC is of the view that ARTC has met this requirement of the Undertaking, but in doing so, various concerns about the nature of the change in circumstances are raised.

Consultation

Further, under clause 2.4(d) of the Undertaking, ARTC may only request a variation of the Undertaking following consultation with rail operators over the proposed variation. On the basis of submissions, it is the ACCC's preliminary view that ARTC has not met the requirement to consult with rail operators prior to making its request for variation.

ACCC Draft Decision

The ACCC does not consent to ARTC's proposed variation to the Undertaking because it does not consider the variation to be appropriate for the reasons set out in this Draft Decision.

In summary, the ACCC is of the view that the proposed variation to the liability and indemnity clause (clause 15) in the IAA is not justified as currently drafted because the proposed indemnity clause would prevent a rail operator (or indeed ARTC) from being indemnified for loss arising out of a contract between a rail operator and a third party (or ARTC and a third party) in circumstances where ARTC (or the operator) has breached the IAA and caused an Incident which has resulted in loss to that third party. As such, after assessing the proposed variation against the statutory criteria, the ACCC is of the preliminary view that it is not appropriate to consent to the proposed variation.

The following discussion summarises the key elements of the submissions received in support of and in response to the application, considers the threshold issues that ARTC must satisfy in order to seek a variation, and sets out the ACCC's assessment and draft decision on the variation request with particular regard to the statutory criteria required to be applied by the ACCC in making its draft determination.

Legislative Process – Variation Application, Submission and Assessment Process

This chapter sets out the legislative process applicable to Part IIIA access undertaking variation applications.

On 9 October 2008, the ARTC lodged an application to vary the Undertaking with the ACCC for assessment under subs. 44ZZA(7) of Part IIIA of the Act. ARTC seeks to vary clause 15 of the IAA in order to limit the circumstances in which one party is obliged to indemnify the other for losses incurred to the former party.

Background to clause 15

As part of the consultation process relating to the Undertaking, the ACCC sought comment from interested parties on the appropriateness of the *Indemnities / Loss or Damage* provisions of the IAA in the then proposed undertaking. No relevant comments were received in response to the ACCC's request. As a consequence, clause 15 was approved by the ACCC in the form initially presented to it by ARTC as part of its then proposed undertaking.

Application process

Subsection 44ZZA(7) provides that a provider may vary an undertaking at any time, but only with the consent of the ACCC. The Act does not detail the process that the ACCC must undertake in assessing a variation request, however, subs. 44ZZA(7) further provides that the ACCC may consent to the variation of the undertaking if it thinks it appropriate to do so having regard to the matters in subsection (3) (see Part B for a discussion of these matters).

The ACCC is of the view that the legislative provisions that apply to an original application for an undertaking under subs. 44ZZA(1) also apply in relation to a variation application. Accordingly, in deciding whether or not to consent to a variation request, the ACCC has adopted the same process to that which it applies when a service provider lodges an original application for an undertaking under Part IIIA.

Public consultation

Section 44ZZBD provides that the ACCC may undertake a public consultation process to assist it to assess an access undertaking (or variation of an undertaking) if it considers it appropriate to do so. The ACCC considered it appropriate to do so given the potential implications of the variation. Hence, on 31 October 2008, the ACCC released an Issues Paper inviting public comment on ARTC's variation application together with a media release announcing the variation request.

The Issues Paper together with the ARTC application was sent directly to a number of parties that the ACCC identified as likely to be interested in the application as well as posting these documents on the ACCC website. Submissions from interested parties were required by the close of business on 21 November 2008.

Submissions and assessment

In response to the request for submissions, the ACCC received three submissions. All submissions as well as ARTC's variation application are available on the ACCC's web site at **www.accc.gov.au**.

A list of the parties making submissions in response to the variation application is set out in **Appendix A**.

In assessing the application to vary the Undertaking, the ACCC had regard to the submissions received from ARTC and interested parties. Part B of this Draft Decision discusses in detail the statutory criteria that the ACCC must have regard to in considering the submissions and in deciding whether or not to consent to the variation.

Timing for decision

Under s. 44ZZBC, the ACCC is required to use its best endeavours to make a final decision on the (variation) application within six months of receiving a (variation) application, that is, by 9 April 2009. The ACCC is releasing this Draft Decision for comment before making its final decision on the application.

Operation of a variation

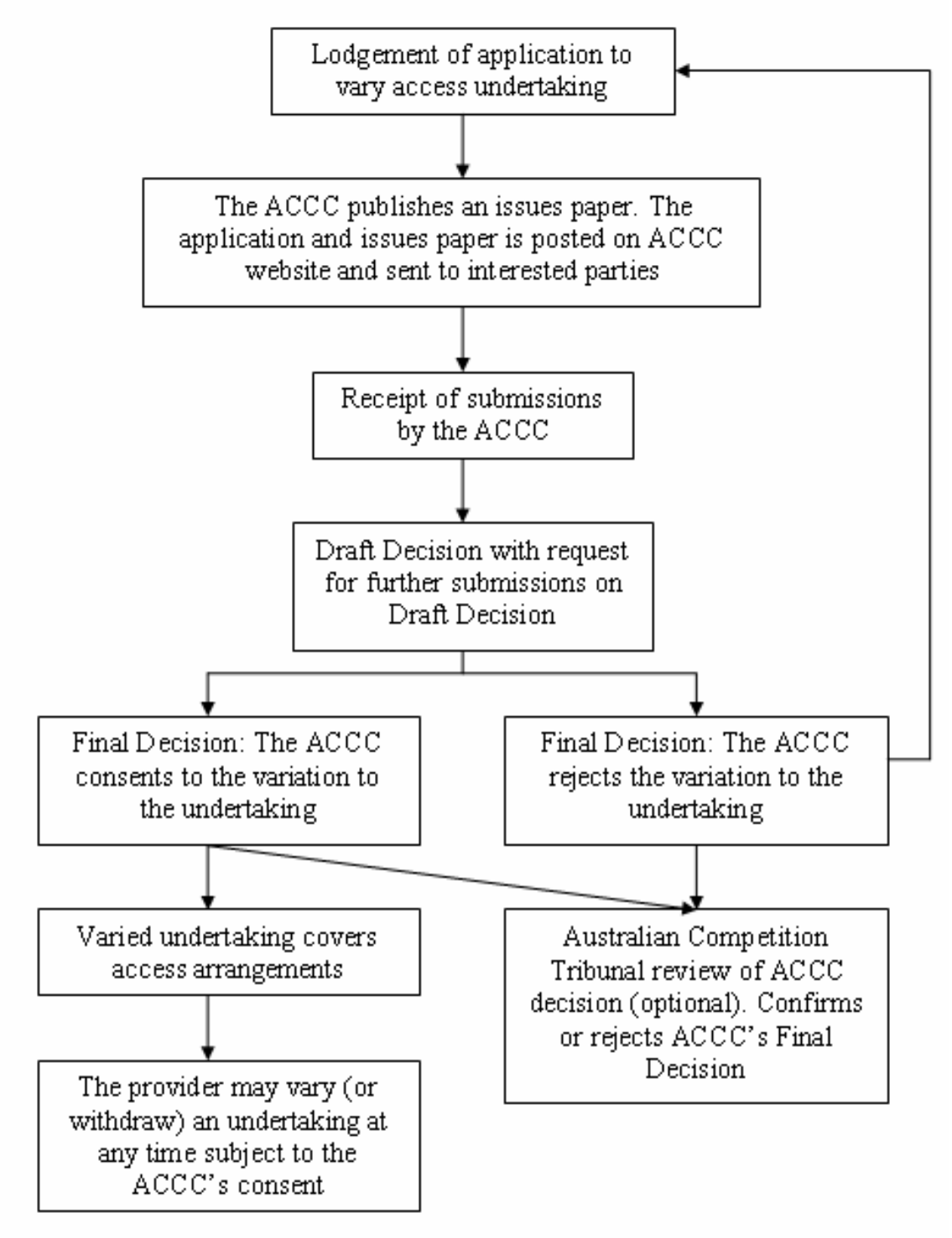
If the ACCC consents to a variation, the varied form of the undertaking becomes applicable for the purposes of providing access to the Network. The varied form of the undertaking would take effect 21 days from the day the ACCC publishes its final decision to consent to the variation [subs. 44ZZBA(1)].

Tribunal review

Section 44ZZBF provides that a person whose interests are affected by an (variation) access undertaking decision may apply in writing to the Tribunal for review of the decision. A person must apply for review within 21 days after the ACCC publishes its decision.

The following figure (Figure 1) summarises the general procedure for the ACCC's assessment of the proposed variation to the Undertaking.

Figure 1: Variation to Access Undertakings - Assessment Process



Indicative Timetable

Process	Timing
Publication of Draft Decision and invite further submissions	December 2008
Submissions on Draft Decision	21 January 2009
Assessment of submissions and preparation of Final Decision	February 2009
ACCC Final Decision	March 2009

Submissions on the Draft Decision

Stakeholders are invited to make a submission on the ACCC's Draft Decision. These submissions will be taken into account in forming the ACCC's Final Decision.

Details of the ACCC's mailing and electronic mail addresses for lodging submissions are detailed below. Submissions should be forwarded by 5:00pm (AEDST) **21 January 2009** to:

Mailing Address

David Salisbury
A/g General Manager – Transport
Regulatory Affairs Division
ACCC
GPO Box 520
MELBOURNE VIC 3001

(03) 9290-1919

Electronic versions should be emailed to: **transport@accc.gov.au**

Confidentiality and use of information

All submissions will be made available to any person or organisation on request unless the submission or part thereof is claimed as confidential and the ACCC accepts such claim of confidentiality. The sections of submissions that are considered confidential should be clearly identified and reasons given supporting the claim. The ACCC will consider each claim of confidentiality on a case by case basis. If the ACCC refuses a request for confidentiality, the submitting party will be given the opportunity to withdraw the information. The ACCC will then assess the variation application in the absence of that information.

Information sharing provisions in the Act allow the ACCC in certain circumstances to disclose protected information it receives with other government agencies.[1]

1 Section 155AAA, Trade Practices Act 1974

For further information about the collection, use and disclosure of information provided to the ACCC, please refer to the ACCC publication *"Australian Competition and Consumer Commission / Australian Energy Regulator Information Policy – the collection, use and disclosure of information"*, available on the ACCC website.

Further inquiries:

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Part A Industry Background

Introduction

This section provides a brief overview of the ARTC and its operations as well as a description of the main users of its Network. For a detailed discussion of the industry background, please refer to the *"ACCC Draft Decision on the Interstate Rail Network – April 2008"* which includes such matters as the various components of the Network, ARTC regulatory history and the rail market.

Background

The ARTC was created after the Commonwealth and State Governments agreed in 1997 to the formation of a 'one stop' shop for all rail operators seeking access to the national interstate rail network.

ARTC is responsible for the access management of over 10,000 kilometres of standard gauge track in South Australia, Victoria, New South Wales and Western Australia. Access management incorporates the planning, scheduling and transit of trains through the network and associated commercial arrangements with train operators.

ARTC owns tracks in the interstate network in South Australia and leases tracks in Victoria. In September 2004, ARTC also entered a 60-year lease over the interstate NSW rail tracks and the NSW Hunter Valley coal network. The Undertaking covers terms and conditions of access to standard gauge tracks along the interstate network, including the track leased in NSW. However, the Undertaking does not cover access to tracks in the Hunter Valley coal network. ARTC is expected to lodge a separate access undertaking for the Hunter Valley coal network with the ACCC in the future.

There are eight major operators currently using the ARTC owned or leased Network namely— Asicano;[2] Australian Southern Railroad; CityRail; CountryLink; Freight Link; Great Southern Railway; Queensland Rail; and Specialised Container Transport Logistics.

Major Operators on the ARTC Network

The following above rail operators are the largest users of tracks in the Network:

- Asciano (the consolidated holding company of Pacific National (PN)) – the dominant operator on most segments of the Network, providing general and bulk freight services;

- Specialised Container Transport Logistics (SCT) – mainly services the general non-container freight market along the East-West route, although it has commenced services from Melbourne to Sydney (Parkes);

[2] Asciano was listed on the ASX in 2007. The company combines Pacific National rail operations with the Patrick's ports and stevedoring businesses.

- Queensland Rail (QR) – the dominant vertically integrated operator in Queensland. Also operates along the eastern seaboard with general freight services on the Brisbane-Sydney and Sydney-Melbourne corridors, commenced intermodal services from Melbourne to Perth in November 2007, and provides coal freight services in the Hunter Valley;

- FreightLink – provides above rail services on the Tarcoola-Darwin line;

- CityRail and CountryLink – mainly provides passenger services in NSW; and

- Great Southern Railway (GSR) – provides long distance passenger services between Sydney and Perth (The Indian Pacific), Melbourne and Adelaide (The Overland), and Adelaide and Darwin (The Ghan).

Part B Legislative Framework and Principles

Introduction

This Part provides an overview of the legislative provisions relevant to the ACCC's assessment of ARTC's variation application as well as a discussion of the statutory criteria that the ACCC must apply in deciding whether or not to consent to an (variation) undertaking.

B.1. Access Undertakings and Part IIIA of the Act

Part IIIA was introduced in 1995 as part of the competition policy reforms adopted by the Council of Australian Governments (COAG). The purpose of Part IIIA is to promote the efficient provision and use of a limited class of infrastructure facilities by establishing a statutory basis for users to gain access to the services provided by those facilities.

One mechanism under Part IIIA for dealing with access issues is for the owner or operator to offer an undertaking to the ACCC stipulating the terms and conditions upon which it is willing to provide access to third parties.

Access undertakings have the advantage that they 'provide a means by which the owner or operator of a facility can obtain certainty about access arrangements, before a third party seeks access.'[3] Once accepted, the services covered by the undertaking cannot be declared. Undertakings thus avoid the possibility of time consuming and expensive processes about whether to declare a service and then establishing the terms and conditions of access through arbitration. Further, an undertaking is enforceable through the courts.

Once an access undertaking is in operation, a service provider may withdraw or vary the undertaking at any time, but only with the consent of the ACCC. The ACCC may consent to a variation of the access undertaking if it thinks it appropriate to do so having regard to the matters in subs. 44ZZA(3).

B.2. Legislative Considerations Under Part IIIA

This section provides a brief discussion of the ACCC's understanding and approach to the criteria. While not all of these provisions will be relevant and applicable to the ACCC's analysis of the proposed variation, each criterion has been considered as part of the ACCC's assessment of the variation application in this Draft Decision.

B.2.1. Objects Clauses

Section 44AA of the Act provides that the objects of Part IIIA are to:

> (a) promote the economically efficient operation of, use of and investment in the infrastructure by which services are provided, thereby promoting effective competition in upstream and downstream markets; and

3 Second Reading Speech accompanying the Competition Policy Reform Bill 1995.

(b) provide a framework and guiding principles to encourage a consistent approach to access regulation in each industry.

Object (a)

When assessing an application to vary an undertaking the ACCC should take into account the object of promoting economic efficiency in the operation of, use of and investment in the infrastructure by which services are provided. In the ACCC's view, this requires the consideration of the different types of economic efficiency:

- Technical or productive efficiency, which is achieved where individual firms produce the goods and services that they offer to consumers at *least* cost;

- Allocative efficiency, which is achieved if the resources used to produce a set of goods or services are allocated to their highest valued uses (i.e. those that provide the greatest benefit relative to costs); and

- Dynamic efficiency, which reflects the need for industries to make timely changes to technology and products in response to changes in consumer tastes and in productive opportunities.

These three types of economic efficiency are, in general, complementary, and are all promoted by effective competition. Determination of terms and conditions for access to the services provided by the infrastructure can, however, sometimes involve balancing the consideration of the different benefits of the three types of economic efficiency. How this balancing is achieved will typically depend on the physical and cost characteristics of the infrastructure and the demand for the services, such as whether capacity is scarce.

The ACCC's understanding of Object (a) is that, in terms of promoting the efficient operation of, use of and investment in access infrastructure, and hence promoting effective competition in upstream and downstream markets, any pricing framework should generally satisfy two high-level criteria. First, it should encourage the efficient use of the existing access infrastructure by access users. For example, by appropriately reflecting the costs associated with providing the declared service. Second, the pricing framework should reveal and signal opportunities for investment or other improvements to access provision.

Object (b)

Object (b) encourages consistency in the approach to access regulation, while also recognising that the most efficient access pricing framework for a particular access service should be determined on the basis of relevant characteristics of the industry in which that service is provided.

The ACCC's understanding of Object (b) is consistent with that adopted in the *Revised Explanatory Memorandum to the Trade Practices Amendment (National Access Regime) Bill 2006.* As stated in the explanatory memorandum, while this objective seeks to promote a consistent approach to access regulation in each industry, it is also important to recognise that industry-specific access regimes accepted under Part IIIA may be divergent due to different market characteristics. In particular, it is the ACCC's view that the intention of Object (b) is to provide a consistent 'overarching framework'

for access regimes and not to place binding restrictions on how access pricing frameworks are applied – for example, by state and territory regimes – which should properly be determined on the basis of the characteristics of the access facility in that jurisdiction.

B.2.2. The Pricing Principles specified in s. 44ZZCA

Section 44ZZCA of the Act provides that the pricing principles for Part IIIA are:

> (a) that regulated access prices should:
>
> > (i) be set so as to generate expected revenue for a regulated service or services that is at least sufficient to meet the efficient costs of providing access to the regulated service or services; and
> >
> > (ii) include a return on investment commensurate with the regulatory and commercial risks involved; and
>
> (b) that the access price structures should:
>
> > (i) allow multi-part pricing and price discrimination when it aids efficiency; and
> >
> > (ii) not allow a vertically integrated access provider to set terms and conditions that discriminate in favour of its downstream operations, except to the extent that the cost of providing access to other operators is higher; and
>
> (c) that access pricing regimes should provide incentives to reduce costs or otherwise improve productivity.

Pricing Principle (a)

(i) Expected revenue at least sufficient to meet efficient costs of providing access

The ACCC's understanding of pricing principle (a) is that it is intended to set a 'revenue floor' for the revenue raised by the provider from access charges, being the 'efficient costs of providing access to the regulated service.'

Section 44ZZCA does not prescribe a particular methodology (such as long-run marginal cost or incremental cost) for determining the efficient costs. The appropriate methodology will depend on the circumstances of each case.

(ii) Regulatory risk

The revised *Explanatory Memorandum to the Trade Practices Amendment (National Access Regime) Bill 2006* notes that the reference to regulatory risk 'is intended to refer to the perception that the exercise of regulatory discretion will be undertaken in a heavy-handed, arbitrary or uneven fashion.' The memorandum goes on to state:

> While such perceptions may deter investment in any dysfunctional market subject to regulation, regulatory risk takes on greater importance for infrastructure investors, due to the length of time and expense required for service providers to respond to changes in a market, perceptions that regulatory decisions tend to be biased in favour of service users rather than service providers/investors, the scale of investment in infrastructure and the sunk nature of assets. Pricing Principle (a)(ii) requires regulators specifically to factor in regulatory and commercial risks in setting access prices. This may assist to address perceptions that regulatory bias favours service users.

In the past, the ACCC has taken a cautious approach to setting regulatory parameters and continues to develop transparent and predictable processes, which help to deal with many of the perceived problems commonly associated with regulatory risk. The ACCC considers, however, that, in general, dealing with any actual or perceived regulatory risk simply by systematically increasing the allowed rate of return on investment is not an appropriate methodology. To systematically increase the allowed rate of return on investment would result in the redistribution of the proceeds of investment from consumers to shareholders, thereby obviating one of the purposes of regulation in the first place. It might also distort investment if the risk mark-up was greater than the actual risk for the project.

(iii) Commercial risk

When assessing an application to vary an undertaking it is generally necessary to consider the appropriate rate of return on capital. The rate of return on capital is a market-determined rate required by investors to provide capital to the company. The appropriate rate of return on capital may depend on the level of commercial risk of the project.

One method of determining the appropriate rate of return on capital is to estimate the WACC. In determining the WACC, cost of debt financing is separated from the cost of equity financing, as the two options carry different levels of commercial risk. The WACC is then calculated by taking the average of these two weighted by the proportion of each type of financing used in the project.

The cost of debt financing is often derived by directly measuring the current effective interest rate on the various debts held by the firm. Alternatively, it can be derived by a benchmark return on bonds with similar credit rating to the firm. Cost of equity financing is derived by starting with the risk-free rate of investment, and adding a premium based on the commercial risk of the investment, determined on a case-by-case basis.

While there are a number of methods for determining the appropriate return on equity, a common method is the use of the capital asset pricing model. Under such a model, a premium reflecting the riskiness of a project is added to the risk-free rate. The premium is calculated using the market-determined risk premium coupled with the riskiness of the project relative to the riskiness of the market as a whole.

Pricing Principle (b)

(i) Multi-part pricing and price discrimination

Sub-paragraph 44ZZCA(b)(i) states that access price structures should allow multi-part pricing when it aids efficiency. Access pricing arrangements that incorporate multi-part prices can, in principle, allow for many of the efficiency advantages associated with setting marginal or per-unit prices equal to short-run marginal cost, while at the same time promote efficient investment by allowing an access provider to recover a relevant share of fixed costs through fixed charges or higher infra-marginal pricing. The simplest multi-part pricing arrangement is a two-part tariff that involves an up-front charge which contributes to the recovery of fixed costs, as well as a per unit, or usage charge, which reflects the short-run marginal cost of providing the service.

(ii) Vertical integration

Sub-paragraph 44ZZCA(b)(ii) states that access price structures should not allow a vertically integrated access provider to set terms and conditions that discriminate in favour of its own downstream operations, except to the extent that the costs of providing access to other operators is higher. This section aims to ensure that access pricing allows suppliers of goods and services that are dependent upon access to the declared service to be able to compete on their relative merits.

Pricing Principle (c)

Subsection 44ZZCA(c) states that access pricing regimes should provide incentives to reduce costs or otherwise improve productivity.

In principle, there are numerous ways in which an access pricing regime for a specific service may be designed. In practice, however, pricing regimes are often variants of either cost-of-service/rate-of-return regulation or price-cap regulation. Depending on how they are implemented, both of these forms of regulation, and variations based on them, have the potential to provide incentives to reduce costs and improve performance. The general point is that the incentives to reduce costs and improve performance under any access pricing regime depends on how closely linked an access provider's general level of prices are to the access provider's actual costs associated with providing those services.

The appropriateness of a particular pricing regime will depend on the characteristics of the facility under examination and how it is implemented in practice. Generally, this will involve considering the different types of potential efficiency gains, as well as facility-specific factors such as the importance of service quality, the potential for efficiency gains and the relative risk allocation between access providers and access users.

B.2.3. Legitimate Business Interests of the Provider

When having regard to the legitimate business interests of the access provider, the ACCC considers whether particular terms and conditions in the proposed undertaking are sufficient and necessary to maintain those interests.

The following issues may be relevant to identifying the legitimate business interests of the service provider:

- ongoing viability of services covered by the undertaking and the impact of consenting to the variation;
- the costs of extensions to the facility incurred by the service provider — such extensions may be required to facilitate access where capacity constraints exist;
- protection of plant and equipment — in some circumstances it may be appropriate for the service provider to specify the terms and conditions of use of infrastructure facilities to limit damage or for safety reasons; and
- ability of the service provider to meet obligations imposed by government.

B.2.4. Public Interest, Including the Public Interest in Having Competition in Markets (whether or not in Australia)

In having regard to the public interest, the ACCC explores the extent to which the proposed variation to an undertaking improves the welfare of other parties and the broader community. It considers a broad range of public interest issues, but has particular regard for economic efficiency considerations, reflected in the specific references to the public interest of having competition in markets, which is a clear reference to the Act's objective of promoting competitive markets.

While no list of public interest considerations can be exhaustive, clause 1(3) of the *Competition Principles Agreement* (11 April 1995) provides an example of such considerations:

- government legislation and policies relating to ecologically sustainable development;
- social welfare and equity considerations, including community service obligations;
- government legislation and policies relating to matters such as occupational health and safety, industrial relations and access and equity;
- economic and regional development, including employment and investment growth;
- the interests of consumers generally or as a class of consumers;
- the competitiveness of Australian businesses; and
- the efficient allocation of resources.

Interests of Consumers

The way a variation of an undertaking impacts on end-users, not just the users of the infrastructure service, can be an important public interest consideration. This can include the interests of end-users in obtaining:

- lower prices than would otherwise be the case;
- increased quality of service; and
- increased diversity and scope in product offerings including access to innovations in a quicker timeframe than would otherwise be the case.

The Tribunal noted that, over the long-term, the apparent tension between the interests of the service provider and end-users may be resolved. For example, very low prices may be in the short-term interests of end-users. However, over the long-term, sustainably low prices are more likely to enhance their interests. Similarly, in *Re Michael; Ex parte Epic Energy (WA) Nominees Pty Ltd (2002)* ATPR 41-886 (*Michael*), Parker J discussed the public interest in the maintenance and encouragement

of future investment in significant infrastructure, by protecting past investment decisions.

B.2.5. Interests of Persons Who Might Want Access to the Service

Persons who might want access to the service will, in general, use that service as an input to supply services to end-users. That is, they are likely to be upstream producers (such as electricity generators) or downstream service providers (such as electricity and gas retailers and rail freight operators). The interests of final consumers (end-users) will, in general, be considered in the context of the public interest.

In *Michael* Parker J noted (at [135]) that this criterion is counterpoised to the 'legitimate business interests' criterion of the service provider although there is scope for the 'respective interests to find mutual accommodation.'[4] As discussed above in relation to the interests of consumers, assessed over the long-term, there is likely to be less conflict between the interests of the access provider and access seeker, particularly where the access provider is not integrated into the downstream market. For example, it is in the access seeker's long-term interest that prices and returns are sufficient to provide the incentives needed to induce the access provider to invest in and adequately maintain services.

In assessing terms and conditions included in a proposed undertaking against the interests of access seekers, a range of issues may arise including:

- Does the undertaking appropriately provide for the services which access seekers are likely to require?

- Are access terms and conditions reasonable? In general, it will be in the interests of access seekers that prices reflect the efficient provision of the service (subject to commercial viability) and do not incorporate pricing designed to generate significant monopoly profits.

- Does the undertaking incorporate non-price barriers to access?

- Does the undertaking include incentives for the access provider to improve efficiency over time?

- To the extent that pricing is based on asset valuation, how appropriate is the approach to valuing assets given the circumstances of the undertaking?

- Does the pricing provide incentives for efficient investment by the access provider? In general, it will be in the interests of access seekers that pricing reflects efficient investment choices, and not reflect the choice of inappropriate technology, construction of facilities much larger than could be justified by existing or prospective usage or earlier than necessary replacement of plant and equipment.

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[4] In the context of s.2.24(f) of the *National Third Party Access Code for Natural Gas Pipeline Systems*.

- Are the processes for negotiating and setting prices clear and transparent?

- Is sufficient information available to access seekers to engage in meaningful negotiation with the prospect of outcomes reflecting the objects of Part IIIA?

- Are the ongoing operational arrangements such that access seekers are reasonably informed about the service?

- Does the undertaking need to include service standards? Will the service standards meet reasonable user needs? Has the access provider demonstrated a commitment to ongoing maintenance of the service? Is there transparency in service quality (for example availability of measures of service reliability to interested parties on request and/or processes for regular independent service audits)?

Access seekers may also want to ensure that their use of the infrastructure service is not unnecessarily limited by restrictive standards.

B.3. Existence of Another Effective Access Regime and Other Relevant Considerations

In some instances, a service may already be covered by an existing access regime. Access regimes may take the form of:

- State regimes;

- Commonwealth regimes; or

- private regimes such as industry based access codes.

The ACCC is required to reject an undertaking lodged by an infrastructure provider if the Commonwealth Minister has already decided that the infrastructure is subject to an effective state or territory access regime under s.44N (subs. 44ZZA(3AA)).

In this instance, the ARTC leased rail network assets in NSW are subject to the 2004 NSW Rail Access Undertaking, but this regime has not been certified as effective by the Commonwealth Minister. There is also no rail industry access code that applies to the Network so that subpara. 44ZZA(3)(da) is not relevant to the assessment of this Undertaking or variation application.

Finally, as noted above, the ACCC must also have regard to any other matters it thinks are relevant to its assessment of the variation to the Undertaking (para. 44ZZA(3)(e)). This gives the ACCC the flexibility to consider circumstances specific to a particular service. This could include, for example, the capacity to enforce the undertaking, or other matters such as the extent to which the undertaking is consistent with other regulation, or the extent to which the undertaking protects existing contracts. Any such considerations must not be irrelevant to the ACCC's consideration of the proposed Undertaking.

Part C Assessment of ARTC's Variation Application

The following Part sets out the structure of the ACCC's assessment of the variation application:

- C.1. Applying for variation of the Undertaking – Threshold Issues; and
- C.2. Proposed variation to clause 15 of the Indicative Access Agreement.

C.1. Varying the Undertaking – Threshold Issues

Introduction

The ACCC has a statutory obligation to assess and make a decision on the variation application. However, the operation of the Undertaking is such that it sets out some conditions precedent to ARTC seeking a variation to the Undertaking. If these conditions are in the ACCC's opinion not satisfied, there may be a threshold issue as to whether ARTC is entitled to seek the approval of the ACCC to vary the Undertaking.

Clause 2.4 of the Undertaking sets out the circumstances in which the ARTC can seek ACCC approval for variation of the Undertaking. In its application, the ARTC identified clauses 2.4(a) and 2.4(d) of the Undertaking as the relevant 'threshold' criteria that must be satisfied before an application for variation can be made.

Clause 2.4(a) - Change of circumstances

Under clause 2.4(a) of the Undertaking, before the ARTC can apply to the ACCC to vary the Undertaking, it must be of the opinion that there has been a change of circumstances such that the Undertaking is no longer commercially viable for the ARTC or it has become inconsistent with the objectives prescribed at clause 1.2 of the Undertaking.

Specifically, clause 2.4(a) provides as follows:

> "If, during the Term, ARTC is of the opinion that circumstances have changed such that this Undertaking is no longer commercially viable for ARTC or becomes inconsistent with the objectives prescribed at clause 1.2, ARTC may seek the approval of the ACCC to vary this Undertaking."

The Objectives in clause 1.2 of the Undertaking are similar to the statutory criteria required to be applied by the ACCC in assessing a variation to an undertaking. In summary, they are:

- to provide a framework to manage negotiations with applicants for access to the Network;

- establish a workable, open and non-discriminatory process for processing access applications;

- use transparent and detailed methodologies and principles for determining access revenue limits, terms and conditions;

- reach an appropriate balance between the legitimate business interest of ARTC, the interest of the public, and the interests of applicants wanting access to the Network.

In making this request for variation, ARTC submitted that it considers that its circumstances have changed sufficiently to warrant the application.

ARTC's submission as to changed circumstances

Clause 15 of the current IAA allocates liability between ARTC and an operator for loss or damage arising out of an Incident on ARTC's Network.

According to ARTC, the proposed variation:

> "… remove[s] contractual liability to third parties from the clause 15 liability allocation regime" [5]
>
> and is necessary because the clause:
>
> "was drafted on the assumption that operators do not accept liability to third party claims."[6]

In its variation application, ARTC stated that it was recently provided:

> "with extracts from agreements between an operator and consignors which suggest the operator accepts the risk of loss in respect of all goods it carries, regardless of the cause of the loss".[7]

According to ARTC, this was the first evidence it had received of the existence of these provisions, and that it became aware of the practice after the ACCC accepted the Undertaking.[8] In ARTC's view, these types of provisions:

- expose ARTC to substantial liabilities that it is not able to mitigate which results in ARTC assuming risk under the IAA in a manner that is not commercially viable;[9] and

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[5] ARTC *Application by ARTC to vary the ARTC Interstate Access Undertaking* (ARTC submission), 9 October 2008, p. 1.
[6] Ibid., p. 1.
[7] Ibid., pp. 3-4.
[8] Ibid., pp. 3-4.
[9] Ibid., pp. 4-5.

- results in a mismatch between ARTC's rate of return on its investment under the Undertaking and the level of commercial risk it is exposed to – resulting in an inconsistency with the objectives in Clause 1.2 of the IAA.[10]

As a result, ARTC contends that there has been a change of circumstances that permits ARTC to seek to vary the Undertaking pursuant to clause 2.4(a).

Views of Interested Parties

Interested parties that made submissions have expressed concerns about whether ARTC can reasonably hold the opinion that there has been a change of circumstances such that the Undertaking is no longer commercially viable for ARTC or that the Undertaking has become inconsistent with the prescribed objectives.

Interested parties submitted that ARTC's opinion is not reasonable for the following reasons:

The timing as to when ARTC became aware of the change in circumstances

SCT argues that not only should a 'reasonably-aware ARTC' have had knowledge of the industry practice that ARTC claims it has only recently learned,[11] but that SCT has evidence that ARTC was informed by SCT of the existence of an operator's contractual terms regarding the acceptance by freight forwarders of third party liability prior to the ACCC accepting the Undertaking. As such, ARTC cannot have formed the opinion that circumstances have changed (on this ground) since the Undertaking was accepted.

In its submission, SCT provides examples and offers to provide documentary evidence to support SCT's assertion that it had,

> "formally advised the ARTC of SCT's position prior to approval of the Undertaking by the ACCC and in some instances prior even to the ARTC submitting the Undertaking to the ACCC".[12]

SCT contends that the practice of carriers accepting responsibility for goods in their possession is probably hundreds of years old. Further, the Board of ARTC includes members who claim to have experience in the transport industry and senior personnel who have general freight experience and as such it is inconceivable that these persons were not aware of the industry practice whereby freight forwarders cover the risk of certain client's goods in their possession. As such, SCT argues that it is unreasonable for ARTC to claim that they were not aware of such general industry practices until after the ACCC approved the Undertaking.[13]

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[10] Ibid., p. 5.
[11] Specialised Container Transport, *SCT submission re Application for variation of ARTC Interstate Access Undertaking*, 20 November 2008 (SCT submission), p. 4.
[12] Ibid., pp. 5-6.
[13] Ibid p.5.

The extent of the practice within the industry cannot make the Undertaking commercially unviable or inconsistent with the prescribed objectives

Asciano note that ARTC does not say whether the practice applies to one particular customer contract or a number of rail operator customer contracts. As such, the extent of the problem is unclear. Accordingly, Asciano argue that there is little evidence of the extent to which operators are passing on liability to ARTC other than ARTC's assertions regarding a single operator and its concerns about a possible spread of the practice throughout the industry.[14]

In Asciano's view, this practice ('no-fault' liability) is not likely to be widespread amongst larger operators, and as a result, the practice is unlikely to substantially impact ARTC's operations. Asciano confirm that none of the Asciano group of companies has entered into such an arrangement with its customers ('no-fault' liability) and it suggests that it would be surprising if the practice complained of was followed by any of the larger operators. Asciano therefore doubts that the problem impacts a substantial proportion of traffic on the Network. Asciano argues that this makes the claim that the current Undertaking is, as a result of the change in circumstances, commercially unviable or inconsistent with the objectives in clause 1.2 of the Undertaking, unconvincing.[15]

In addition, SCT have noted that

> "… whether the ARTC is liable directly to a third party (as would be the case with clients of freight forwarders other than SCT) or whether it accepts liability to SCT, the cost to ARTC is the same. Previously it recognised that it was exposed directly to third party claims through common law; now it believes it is exposed to claims (for the same damage) through contractual arrangements. Ultimately, there is little difference to its exposure at present; in both the old and "new" understandings it remains responsible for the cost of the product damage if it is at fault; in both the old and "new" understandings it is not responsible for any cost if it is not at fault."[16]

As a result, SCT conclude that without some further quantification as to what ARTC sees as the economic effect of the change in ARTC's perception, the application for variation should fail to meet this threshold criteria.[17]

SCT also notes that ARTC has not identified an inconsistency in the objectives in clause 1.2 of the Undertaking, and as such, this provision cannot be used as a trigger for the application for variation.[18]

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[14] Asciano Limited, *Application for variation of ARTC Interstate Access Undertaking – Clause 15*, 21 November 2008 (Asciano submission), pp. 2-3.
[15] Ibid, pp. 2-3.
[16] SCT submission, p. 6.
[17] Ibid., p. 6.
[18] Ibid., p. 7.

ACCC Assessment of Changed Circumstances

A low threshold

The ACCC notes that the wording of clause 2.4(a) imposes a low threshold on when ARTC may seek the approval of the ACCC to vary the Undertaking.

Provided ARTC, *during the term* of the Undertaking, is of the *opinion* that circumstances have changed such that the Undertaking is no longer commercially viable for ARTC or the Undertaking has become inconsistent with the objectives prescribed at clause 1.2, then it is able to seek the approval of the ACCC.

As such, there does not appear to be a requirement in the wording of clause 2.4(a) of the Undertaking that ARTC's opinion be formed at a particular time. As a result, it may be irrelevant that the ARTC was aware of the existence of the "no-fault" liability clauses prior to the acceptance of the Undertaking by the ACCC. The opinion may have been formed at a later date despite that knowledge. However, a reasonable person might ordinarily expect the opinion to be formed at the time ARTC became aware of the relevant contract terms.

Further, there does not appear to be a requirement in the wording of clause 2.4(a) that the opinion be a reasonably held belief, provided that ARTC are of that opinion. Accordingly, although there may be no convincing evidence about the widespread use of the third party liability provisions in the industry or a quantification of its effects on which to base an opinion of a change of circumstances, that does not prevent this pre-condition being met.

An additional issue raised by interested parties, on which there appears to be a lack of clarity, is what exactly ARTC should have been aware of as the industry practice in contracts prior to the approval of the Undertaking.

ARTC submits that:

> "… following discussions with an operator, ARTC was provided [with agreements] which suggest that the operator accepts risk of loss in respect of all goods it carries regardless of the cause of loss. The actions of an operator in accepting liability, in the absence of negligence or breach of statutory duty …"[19]

Whereas, SCT submit:

> "The practice of carriers accepting responsibility for goods in their possession is probably hundreds of years old." … "It is inconceivable that these persons were not aware of the not-uncommon industry practice whereby freight forwarders do and have always covered the risk of some client's good whilst in their

[19] ARTC submission, p. 3

possession. As such, it is unreasonable for ARTC to claim that they were not aware of such general industry practices …"[20]

ARTC would appear to be arguing that they were not aware of operators accepting "no–fault" liability whereas SCT appear to be arguing about ARTC awareness of carriers accepting responsibility for goods in their possession and not specifically about the form of that responsibility – i.e. 'no-fault' liability. This is relevant to the issue of whether it can reasonably be argued that ARTC should have been aware of 'the practice' prior to acceptance of the Undertaking.

As noted above, regardless of what 'the practice' is, ARTC's application indicates that it was of the opinion, as at 9 October 2008 (during the term of the Undertaking), that the use of "no-fault" liability clauses constitute a change in circumstances such that, in its opinion, the Undertaking is no longer commercially viable for ARTC and is inconsistent with the objectives in clause 1.2 of the Undertaking.

However, even though ARTC may have held this opinion, it is not clear to the ACCC how ARTC's exposure to liability under clause 15 can be increased by an Operator entering into a "no-fault" contract with a third party. This is explained below.

Clause 15, contractual liability and ARTC's exposure

The ACCC notes that the indemnity provisions in clause 15 of the IAA will only be triggered when a party to the IAA (e.g. ARTC) has caused, or has contributed to, an Incident that results in "loss or damage" (as defined) to another party (e.g. an Operator) in breach of the IAA.

The current definition of "loss or damage" includes "any liability to or claim made by a third party".

According to ARTC's variation application, ARTC recently became aware that Operators were providing "no-fault" liability contracts to their customers, and it was this discovery that provided the impetus for the application, in that ARTC is of the view that such contractual arrangements increase their risk of exposure.

However, it appears that the current definition of "loss or damage" already encompasses any loss that a third party suffers as a result of an Incident that was caused or contributed to by ARTC in breach of the IAA, regardless of the contractual liability the other party has in place.

How does the "no-fault" liability contract between an Operator and a third party increase ARTC's exposure under clause 15 of the IAA?

Under clause 15, the general principle is that the party (e.g. ARTC) that caused or contributed to the Incident will be responsible for indemnifying the other party (the Operator) for "loss or damage" to the extent that the "loss or damage" was caused or contributed to by the (ARTC's) breach of the IAA.

[20] SCT submission p. 5.

Therefore, unless ARTC has breached the IAA and that breach caused damage to the Operator or the third party, ARTC cannot be required to indemnify an Operator for the losses suffered by either itself or a third party under the terms of clause 15.

However if ARTC has breached the IAA and that breach caused loss to the third party, ARTC must indemnify an Operator for the losses suffered by the third party, to the extent that the losses were caused by ARTC's breach of the IAA, regardless of whether or not an Operator has agreed to provide a contractual indemnity to the third party.

It is not clear to the ACCC how, under clause 15, a contract between an Operator and a third party can result in ARTC being held responsible for the loss or damage of that third party where ARTC did not cause or contribute to that loss or damage. If this is the case, it is not clear to the ACCC what the change in circumstances is.

The following figures (Figure 2 and Figure 3) demonstrate the ACCC's understanding of ARTC's exposure to liability under clause 15 of the IAA in circumstances with and without an Operator providing a contractual indemnity to a third party.

Figure 2

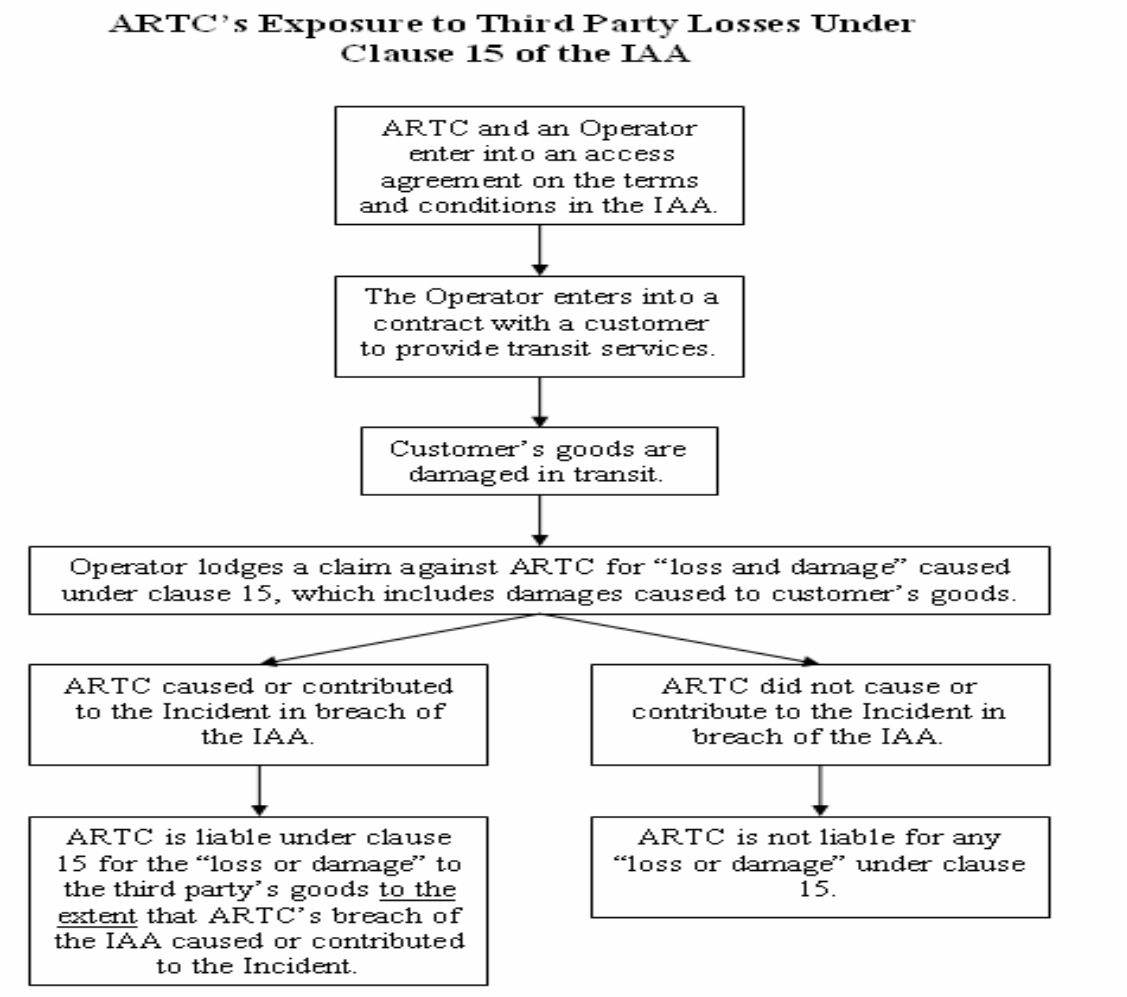
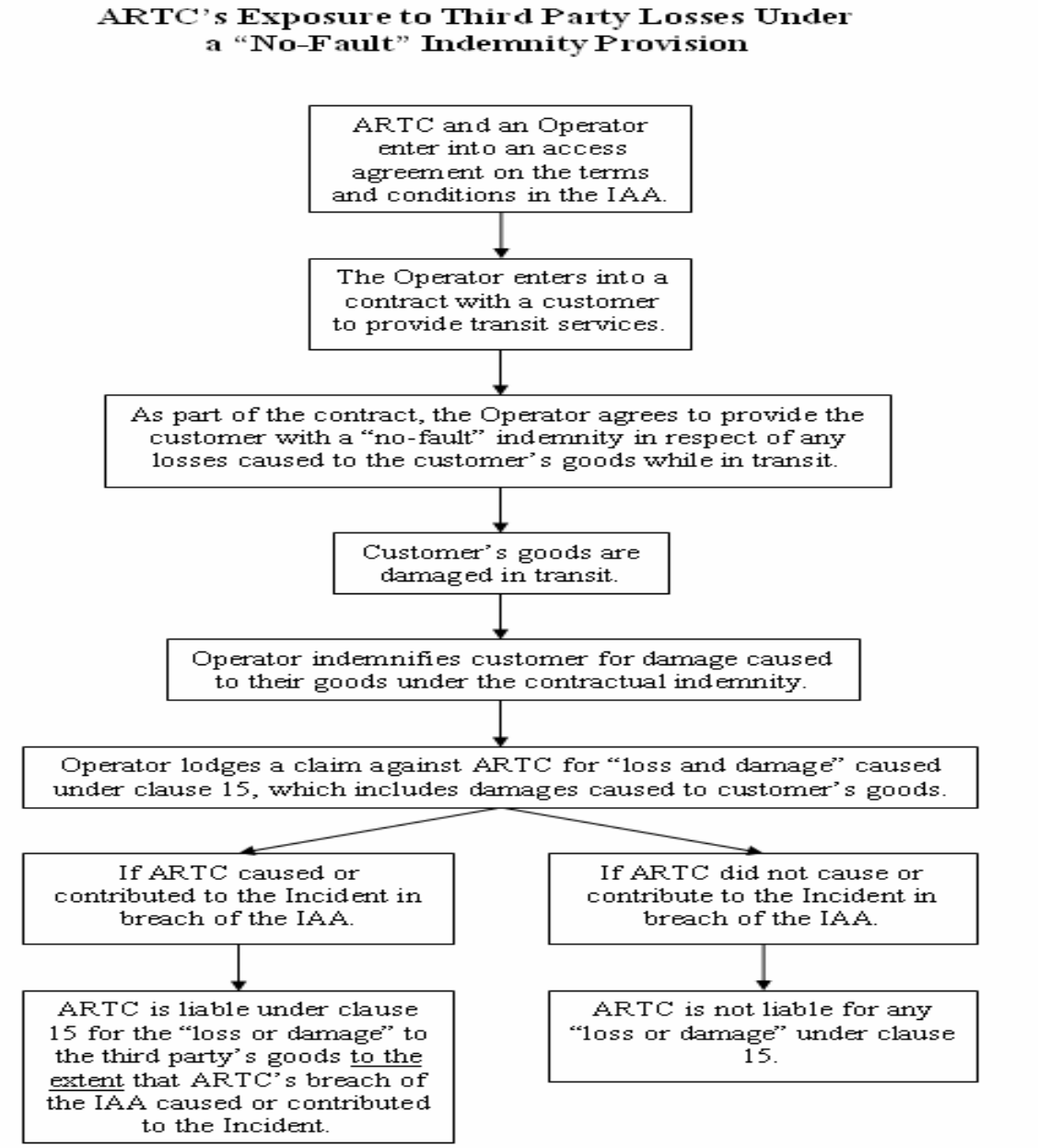


Figure 3



However, it is difficult for the ACCC to contest what ARTC's opinion was. Given the low threshold for meeting the pre-condition, the ACCC is of the view that ARTC has met this requirement.

Clause 2.4(d) - Consultation

ARTC may only request a variation of the Undertaking following consultation with operators about the proposed variation.

Specifically, clause 2.4(d) of the Undertaking provides that,

> "Prior to seeking the approval of the ACCC under clause 2.4(a), ARTC will first consult with Operators regarding the proposed variation."

ARTC submission

ARTC notes in its variation application that ARTC advised by letters dated 3 October 2008 that:

> "… all operators currently seeking contracts under the Access Undertaking that ARTC is amending clause 15 of the IAA".[21]

ARTC also submits that when the application for variation was submitted on 9 October 2008, it was:

> "… still in the process of negotiations with operators in relation to the new contracts, including clause 15".[22]

Views of Interested Parties

Interested parties who discussed the "consultation" issue expressed concerns about the process that was adopted by ARTC in advising operators about the proposed variation.

Interested parties note that although (some) operators received two letters regarding the proposed variation, this constituted nothing more than ARTC informing them of its intention to make certain changes. It was also noted by interested parties that they were not given an opportunity to respond to these letters prior to the variation application being made.

For example, Asciano note that it is:

> " … a train operator and major access customer of ARTC, [and] has not been consulted about the proposed variation prior to the ACCC consultation process".[23]

SCT note that:

> "ARTC has not consulted with SCT … ", and " … the only correspondence or communication we have received from the ARTC regarding this matter is a letter advising, after the event, that the variation had been submitted to the ACCC".[24]

In describing the process that was undertaken by ARTC, Asciano state that:

> "ARTC advised Asciano of the proposed variation by letter dated 3 October 2008 but subsequently advised Asciano that the letter was sent in error … and should be disregarded. ARTC did not provide Asciano with any further correspondence about the proposed variation prior to ARTC's letter to the ACCC of 9 October 2008".[25]

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[21] ARTC application p. 6.
[22] Ibid. p. 6.
[23] Asciano submission p. 4.
[24] SCT submission p. 7.
[25] Asciano submission p. 4.

In addition, Asciano further note that in the letters that it did receive from ARTC in relation to the application for variation, ARTC did not indicate "an intention to consider comments".[26]

ACCC Assessment of Consultation

While there is no definition of 'consult' in the Undertaking, the ACCC notes that the plain dictionary meaning of the term is:

> To seek counsel from; ask advice of; to have regard for (a person's interest, convenience etc.) in making plans. To consider or deliberate; take counsel; confer.[27]

Accordingly, in having a requirement to consult in the Undertaking as a precondition to seeking a variation, the ACCC would expect ARTC to have engaged with the operators in an attempt to at least receive the views of the operators on the proposal *prior* to seeking the variation.

In light of this, although it appears that up to two separate letters were sent to a number of operators (however, without further information from ARTC, it is unclear whether this process involved all relevant operators), it is questionable whether ARTC consulted with the operators prior to seeking the approval from the ACCC and therefore whether ARTC are entitled, under the terms of the Undertaking, to seek the approval of the ACCC to vary the Undertaking.

The ACCC's view regarding consultation tends to be supported by the divergent views of operators on the likely effect and consequences of the proposed variation, as currently drafted.

Therefore, it is the ACCC's preliminary view that ARTC has not met the requirement to consult with operators prior to making its request for variation.

However, given the submissions received from interested parties and the concerns raised about the affect of the drafting of the proposed liability provision in the IAA, the ACCC has nevertheless proceeded with an assessment of the proposed variation.

Part C.2. - ARTC Proposed Variation – Indemnities / Loss or Damage Arising from an Incident

Introduction

Schedule D of the Undertaking is an Indicative Access Agreement (IAA) which forms an essential part of the Undertaking. The IAA is a *Track Access Agreement* that is used as the basis for the terms and conditions on which the ARTC agrees to grant a rail operator access to the Network.

The IAA sets out the terms and conditions that must be offered to an access seeker for the provision of Indicative Services.[28] Clause 15 of the IAA establishes a regime to

[26] Ibid p. 4.
[27] Macquarie Online Dictionary

define and allocate liability between the ARTC and the rail operator for loss or damage arising out of an incident on the rail network.

Clause 15

Clause 15 and related provisions, as they appear in the IAA, are set out in their entirety below.

15. Indemnities/Loss Or Damage Arising From An Incident

15.1 General

(a) The purpose of this clause 15 is to establish a regime in which the liability of ARTC and the Operator to each other for loss or damage arising out of an Incident is clearly defined, and is determined only by reference to this clause 15.

(b) ARTC and the Operator release each other from all Claims for loss or damage resulting from an Incident, including where the Incident is caused or contributed to by the negligence of one or both parties, except Claims that each party to this Agreement may make against the other pursuant to this clause 15.

(c) The provisions of this clause should be interpreted to give effect to the intention that where ARTC and/or the Operator are in breach of this Agreement, and any such breach is the cause or a contributing factor to loss or damage arising from an Incident;

(i) any party in breach should bear responsibility for such loss or damage to the extent of such cause or contribution, and;

(ii) where the acts or omissions of a party other than ARTC or the Operator (as defined in this clause) has caused or contributed to such loss or damage, neither ARTC or the Operator will be responsible to the other for loss or damage to the extent that the loss or damage is caused by or contributed to by the acts or omissions of that other party.

15.2 Definitions

In this clause 15:

(a) **'Claim Period'** means each and every twelve month period during the Term of this Agreement, such that the first Claim Period commences on the Commencement Date and expires at midnight on the day before the first anniversary of the Commencement Date, the second Claim Period commences on the first anniversary of the Commencement Date and expires at midnight on the day before the second anniversary of the Commencement Date, and so on;

(b) **'loss or damage'** includes loss or damage to property belonging to a party to this Agreement, any liability to or claim made by a third party, and the costs of recovery of any property damaged or affected by the relevant Incident and legal expenses on a full indemnity basis;

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[28] 'Indicative Services' are services with the following characteristics – maximum axle load of 21 tonnes; maximum speed of 110 km/h; and length not exceeding certain specifications depending on where on the network the train is travelling (refer to clause 1.1 of IAA).

(c) '**Prohibited Claim**' means, subject to clause 15.5(b), a Claim arising from an Incident where the total value of the loss or damage suffered by a party to this Agreement is less than $50,000.00;

(d) A reference to ARTC or the Operator includes a reference to any servant, agent, employee, contractor, supplier to, or volunteer of or associated with, or a related entity (as defined in the Corporations Act 2001) of ARTC or the Operator;

(e) A reference to a "breach" includes a breach arising from the acts or omissions of a servant, agent, employee, contractor, supplier to, or volunteer of or associated with or a related entity (as defined in the Corporations Act 2001) of, ARTC or the Operator.

15.3 Indemnity

Where ARTC and/or the Operator suffer loss or damage as a result of an Incident, and:

(a) if:

(i) there is a breach of this Agreement by ARTC or the Operator; and

(ii) the breach is the sole cause of the Incident,

then the party in breach will:

(iii) be responsible for its own loss or damage arising from the Incident; and

(iv) completely and effectually indemnify the other party in respect of loss or damage suffered by the other party as a result of the Incident;

(b) if:

(i) there is a breach or are breaches of this Agreement by ARTC or the Operator;

(ii) there is no breach of this Agreement by the other party; and

(iii) the breach or breaches contributed to the Incident but was or were not the sole cause of the Incident:

then,

(iv) the party in breach is to be responsible for its own loss or damage arising from the Incident;

(v) the party in breach is to indemnify the other party (that is, the party not in breach) in respect of the loss or damage suffered by the other party as a result of the Incident to the extent that the breach or breaches contributed to the Incident;

(vi) the other party (that is, the party not in breach) is to be responsible for its own loss or damage arising from the Incident to the extent that the breach or breaches did not contribute to the Incident;

(c) if:

(i) there has been a breach of the Agreement by ARTC and the Operator; and

(ii) breaches by both parties contribute to the Incident,

then each of ARTC and the Operator will:

(iii) indemnify the other party in respect of the loss or damage suffered by the other party as a result of the Incident to the extent that the breach or breaches of that party contributed to the Incident;

(iv) be responsible for their own loss or damage arising from the Incident to the extent that the loss or damage was not contributed to by the breach or breaches of the other party;

(d) if there has been a breach or breaches of the Agreement by both ARTC and the Operator, but the breach or breaches of one of them has not or have not caused or contributed to the Incident, then (whether or not there is any other person or party who has caused or contributed to the Incident) the party whose breach has caused or contributed to the Incident will bear their own loss and damage and indemnify the other party in respect of the loss or damage suffered by that other party as a result of that Incident to the extent that the breach or breaches contributed to the Incident.

15.4 No Claim for Consequential Loss

Notwithstanding:

(a) how an Incident is caused;

(b) that ARTC and/or the Operator is in breach of any duty of care or in breach of this Agreement;

(c) any other rights that ARTC and/or the Operator may have under this Agreement;

(d) that ARTC and/or the Operator may be liable to the other for other loss or damage other than Consequential Loss,

ARTC and the Operator will not make a Claim against the other, and hereby release the other from any Claim, in respect of any Consequential Loss they suffer arising out of any Incident. For the avoidance of doubt, it is agreed that Consequential Loss does not include any liability of ARTC or the Operator to a third party.

15.5 Prohibited Claim

(a) Subject to sub-paragraph (b) hereof, ARTC and the Operator agree that they will not make a Claim against the other if the Claim is a Prohibited Claim.

(b) Where, in any Claim Period, the total value of all Prohibited Claims exceeds $250,000.00, then no further Claims arising from Incidents that occur during that Claim Period will be Prohibited Claims.

15.6 No Other Limitations

Nothing in this clause 15 is intended to remove, limit, restrict, or otherwise prejudice the right of ARTC or the Operator to recover loss or damage or a contribution from a third party.

15.7 Obligation to Mitigate/ Betterment

(a) Each party to this Agreement will take reasonable steps to mitigate that party's losses, damages, liabilities, costs and expenses, and a party's entitlement to recover losses, damages, liabilities, costs and expenses will be determined on the basis that the party should have observed the obligation to mitigate.

(b) Where a party restores or repairs a damaged asset and that repair or restoration results in improved functionality of an asset, such improved functionality will not be regarded as a betterment and no reduction or adjustment of the costs of repair or restoration will be made on that account.

15.8 Obligation to Pay

(a) In this sub-clause, a party liable to indemnify the other is called the "Responsible Party" and a party who is entitled to be indemnified is called an "Indemnified Party".

(b) An Indemnified Party will, as soon as practicable after an incident, give written notice to the Responsible Party of any claim to indemnity including:

(i) the date of the incident;

(ii) brief details of the loss or damage suffered or which might be suffered; and

(iii) a brief description of the grounds upon which indemnity is claimed.

(c) An Indemnified Party may deliver notices requesting reimbursement of costs or expenses incurred, or payment of other loss and damage, on an ongoing basis, as and when such costs and expenses are incurred or such other loss and damage is identified and quantified.

(d) The Responsible Party will

(i) reimburse the indemnified party all costs or expenses incurred by the Indemnified Party in repairing or reinstating plant, equipment or other assets, and

(ii) pay any other loss or damage which is the subject of the indemnity,

within fourteen days (14) of being requested in writing by the Indemnified Party to do so.

(e) Where a Responsible Party has not complied with sub-clause (d) above, the Responsible Party will also be liable to pay interest to the Indemnified Party from the time that such monies should have been paid as requested, until that amount or any outstanding balance is paid in full. The interest rate will be determined in the same manner as the interest rate is determined under clause 4.8 hereof.

(f) The making of any progress or part payment by a Responsible Party to the Indemnified Party will not relieve the Responsible Party of its obligation to indemnify the Indemnified Party for all loss or damage arising out of the same incident to the full extent to which it is liable to do so under this clause 15,

unless the Indemnified Party has given the Responsible Party a release in writing to that effect.

(g) The making of any payment by a party under this clause 15.8 may be made without prejudice to any rights of that party to contest its liability to indemnify.

15.9 Defence of Claims

(a) The parties will render to each other all reasonable assistance in the defence of any Claim made against the other party by a third party arising out of any Incident.

(b) To the extent that a party ('Responsible Party') is obliged to fully indemnify the other party ('Indemnified Party') against a Claim by a third party against the Indemnified Party, the Responsible Party;

(i) may, subject only to the terms of any applicable insurance which the Indemnified Party may have, at its own expense, defend and settle any action or proceedings in the name of the Indemnified Party and execute such documents in the action or proceedings as the Responsible Party sees fit.

(ii) will indemnify the Indemnified Party in respect of all costs, expenses and losses that the Indemnified Party may incur or have incurred on account of the action or proceedings.

Clause 1.1 - IAA – Definitions

"Claim" means all claims, legal actions and demands (including the costs and expenses of defending or settling any action, proceeding, claim or demand)

"Incident" means a breakdown, accident or emergency on the Network which involves the Operator and which causes or may reasonably be expected to pose a danger of causing any one or more of the following:

(a) material damage to or interference with the Network or any associated Facilities managed by ARTC;

(b) material damage to property;

(c) material personal injury to any person;

(d) an Environmental Condition;

(e) a Category A incident or a Category B incident as defined in the Standards;

(f) an incident which requires notification under the relevant Rail Safety Act to the Administering Authority (as defined in such Act); or

(g) an incident requiring notification under the Dangerous Goods Code.

ARTC submission as to how clause 15 operates

ARTC submits that:

> "Clause 15 allocates liability between ARTC and an operator for loss or damage arising out of an incident on ARTC's rail network. Clause 15 was drafted on the assumption that operators do not accept liability to third party claims."[29]
>
> "Under the IAA liability regime, ARTC and the operator are liable to each other for their own direct loss or damage as well as the liability of either ARTC or the operator to a third party."[30]

ARTC submits that the essential aspects of the liability regime are as follows:

> **"Incidents not involving breach of the IAA**
>
> Clause 15(1)(b) releases both parties from claims against each other resulting from an Incident, including where this Incident was caused or contributed to by the negligence of a party, unless otherwise agreed
>
> **Incident involving a breach of the IAA**
>
> Clause 15.3 provides that a breach of the IAA by one party could render that party liable to indemnify the other. For ARTC, the principal obligation in the IAA, that, if breached, could render ARTC liable to the operator is clause 6.1 under which ARTC agrees to maintain the Network in a condition fit for use by the operator to provide rail transport services.
>
> For an operator, there are several obligations which, if breached, would render the operator liable to ARTC, including
>
> - clause 5.4 to maintain rolling stock in a condition which is fit for use at all times
> - clause 5.5(e) to minimize obstruction of the network
> - clause 5.5(g) not to materially change, alter, repair, deface or otherwise affect any part of the network
> - clause 5.5(h) not to materially damage the network.
>
> A breach of the IAA by ARTC or the operator could expose the party of breach to liability to the other party. As noted above, for the purposes of determining liability arising out of Incidents, negligence was not a relevant concept because 15.1(b) makes it clear that liability for negligence is released."[31]

According to ARTC, the rationale for drafting clause 15 in this manner was that:

> " … it was assumed that any third party that suffered loss or damage would have to prove negligence or a breach of statutory duty against either ARTC or the operator before ARTC or the operator would have any liability directly to that third party.

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[29] ARTC submission p. 1
[30] Ibid p. 2.
[31] Ibid pp 2 - 3

> If there was no breach of the IAA (in the case of the operator, if the train was in a fit and proper conditions) then it was unlikely that a third party could establish liability against the operator and hence there would be no claim by that third party, in turn, that could be passed on to ARTC under the clause 15.
>
> … If an operator enters into contractual arrangement with its customers that causes the operator to be liable to its customer irrespective of negligence or breach of statutory duty by the operator, there is the potential for that liability to be passed on to ARTC in circumstances where such liability was never contemplated."[32]

ACCC Assessment of how Clause 15 Currently Operates

There are some key terms in clause 15 that should be set out in order to fully understand the scope and intent of the clause. In summary:

> **"Incident"** means a breakdown, accident or emergency on the Network which causes or may reasonably be expected to pose a danger of causing damage to the network or damage to a person or property (amongst other things).
>
> **"Loss or damage"** includes loss or damage to property belonging to an operator or ARTC, any liability to or claim made by a third party and the costs of recovery of any property damaged and legal expenses on a full indemnity basis.

Particularly pertinent is the definition of 'Loss or damage' which notably includes any liability to or claim made by a third party.

General

15.1(a)

This explains the purpose of clause 15. That is, to establish a regime in which the liability of the parties to each other for loss or damage arising out of an Incident is clearly defined and is determined by clause 15 alone.

15.1(b)

The wording of clause 15.1(b) is largely explained by clause 15.1(a) in which the intention is that the regime for liability between the parties be determined only by reference to clause 15 of the IAA.

The clause itself provides that ARTC and the Operator agree not to bring a claim against the other party for loss or damage resulting from an Incident, *including* where an Incident was caused by the negligence of one party, *except claims a party may make using clause 15*.

The effect of this clause is that claims for loss or damage against the other party are permitted, including claims that arise due to negligence of a party, provided the claim

[32] ARTC submission pp. 2 – 3.

falls within the operation of clause 15. Claims for loss or damage using mechanisms other than clause 15 cannot be brought against the other party.

15.1(c)

This clause enunciates the principles and intent underlying clause 15 in that where ARTC or the Operator breach the IAA and the breach is the cause or contributing factor of the loss or damage arising from an Incident, then:

- the party in breach should be responsible for the loss to the extent the breach contributes to the loss; and

- where the acts or omissions of a third party has caused or contributed to the loss, neither ARTC or the operator are responsible to the other for the loss to the extent that the loss was caused by the third party.

Indemnity

Generally speaking, these clauses define the circumstances and manner in which one party will be responsible to the other where there has been a breach of the IAA and the other party not in breach suffers loss as a result of the actions of the first party.

15.3(a)

Where one party suffers loss as a result of an Incident and there is a breach of the IAA by the other party, and the breach is the sole cause of the Incident, then the party in breach is responsible for its own loss and the loss of the other party incurred as a result of the Incident.

15.3(b)

Where a party suffers loss as a result of an Incident and there is a breach of the IAA by that party, but there is no breach by the other party, and the breach contributes to, but was not the sole cause of the Incident, then, the party in breach:

- is responsible for its own loss;

- is responsible for the loss suffered by the other party to the extent that the breach contributed to the Incident; and

- the party not in breach is responsible for its own loss to the extent that the breach did not contribute to the Incident.

15.3(c)

If there has been a breach of the IAA by both parties and the breaches contributed to the Incident, then a party will:

- indemnify the other party for its loss to the extent that the breach of a particular party contributed to the Incident;

- be responsible for their own loss arising from the Incident to the extent that the breach did not contribute to the Incident; and

- if there has been a breach of the Agreement by both parties, but the breach of one of the parties did not contribute to the Incident, then the party whose breach caused or contributed to the Incident is responsible for its own loss and that party must indemnify the other party for the loss suffered by the other party as a result of the Incident to the extent the breach contributed to the Incident.

15.3(d)

If there has been a breach of the IAA by both parties, but the breach by one of the parties has not caused or contributed to the Incident, then the party whose breach caused or contributed to the Incident is responsible for its own loss and indemnifies the other party for the loss suffered by the other party as a result of the Incident to the extent that the breach contributed to the Incident.

The operation of the indemnity provisions in clause 15.3 only refer to loss or damage arising out of an Incident that is the result of the breach of the IAA. The operation is not limited by how that breach arose – for instance whether it was the result of a wilful act or negligence of a party.

ACCC observations in respect of ARTC submission

ARTC assumption

ARTC submit that:

> "Clause 15 was drafted on the assumption that operators do not accept liability to third party claims."[33]

ARTC's application does not appear consistent with clause 15 being drafted on this assumption given that the definition of 'loss or damage' specifically includes any liability to or claim made by a third party. This suggests that third party claims were specifically contemplated when the clause was drafted albeit not necessarily 'no-fault' claims.

ARTC interpretation of clause 15.1(b)

The ACCC does not agree with ARTC as to the effect of clause 15.1(b). ARTC characterize 15.1(b) as a clause relevant to Incidents not involving breaches of the IAA and as releasing each other from claims resulting from an Incident, including claims caused by the negligence of the other party.

The ACCC's view of clause 15.1(b) is that claims against the other party, including claims for negligence arising out of an Incident, are limited to claims made under clause 15 (which involve claims for breach of the IAA). A party is only precluded from making a claim against the other party to the extent that the claim is brought outside of clause 15.

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[33] ARTC submission p. 1.

Clause 15.3 which sets out the indemnity regime appears to permit claims based on negligence (as does 15.1(b)) – provided there is an Incident which causes loss or damage and the Incident is attributable in some way to a breach of the IAA.

ARTC proposed variation to clause 15

ARTC is proposing to vary two aspects of the IAA by way of changes to clauses 15.1 and 15.2 as follows:

- Clause 15.1(b) – delete the words 'for loss or damage':

> **15.1 General**
>
> …
>
> (b) ARTC and the Operator release each other from all Claims ~~for loss or damage~~ resulting from an Incident, including where the Incident is caused or contributed to by the negligence of one or both parties, except Claims that each party to this Agreement may make against the other pursuant to this clause 15.
>
> …

- Clause 15.2(b) – amend the definition of 'loss or damage' as follows:

> **15.2 Definitions**
>
> …
>
> (b) 'loss or damage' includes:
>
> (i) loss or damage to property belonging to a party to this Agreement;
>
> (ii) any liability to ~~or claim made by~~ a third party, arising from the negligence or breach of statutory duty of ARTC or the Operator to such third party (as the case may be) but excluding any liability of ARTC or the Operator to a third party arising under an Agreement with that party (whether by way of indemnity or otherwise) or arising from a breach of an agreement with that third party;
>
> (iii) the costs of recovery of any property damaged or affected by the relevant Incident,
>
> (iv) and legal expenses on a full indemnity basis;
>
> …

ARTC submission as to the proposed variation

ARTC submits that:

> "These amendments to the IAA … have the effect of excluding from the definition of loss or damage any liability that either ARTC or the operators may have to a third party which arises:

- solely under an agreement, whether by way of indemnity or otherwise, to accept a liability; or

- from a breach of an agreement with that third party.

The proposed change addresses the disparity that has now arisen between the commercial returns and the level of risk to which ARTC is potentially exposed. It does so without materially impacting on operators. Operators are still free to accept no fault liability to Consignors but cannot, and should not, be able to pass on that liability to ARTC.

Importantly, this change does not exclude any rights of a third party to claim directly against ARTC in the event of loss or damage of its goods. ARTC will remain liable to third parties in the event that a third party can establish a legitimate claim based on the principles of general law, such as negligence or breach of statutory duty.

The change is limited to contractual liability. If either ARTC or an operator are liable to a third party for negligence or breach of a statutory duty arising from an Incident and the other party has contributed to that Incident, then that liability is still potentially subject to allocation between ARTC and the operator in accordance with clause 15."[34]

Who is potentially affected by this change?

The IAA is a track access agreement that is struck between ARTC and a rail operator. A rail operator is the entity that provides above rail haulage services. That is, it provides the service of physically transporting, via train, goods between points A and B using the ARTC Interstate rail network.

Accordingly, the only parties potentially directly affected by the proposed variation are rail operators given that the IAA and the proposed changes go directly to the contractual relationship between the rail operator and ARTC.

However, the proposed changes would indirectly affect the contractual relationship that rail operators have with third parties. As such, each rail operator that contracts with a third party in whatever capacity is theoretically relevant. Rail operators contract with third parties (typically freight forwarders) for the services they provide.

Freight forwarders are a relevant industry player in the goods supply chain by rail. Freight forwarders are entities that are engaged by customers / owners of goods to arrange delivery of the customer's goods. Freight forwarders contract directly with customers for the delivery of goods and assume whatever liability for loss or damage to the goods as is agreed between the customer and freight forwarder. Freight forwarders engage rail operators to transport the goods. They therefore contract directly with both rail operators and customers for the carriage of goods. Freight forwarders, however, do not generally contract directly with ARTC – only rail operators. Accordingly, freight forwarders are not, by and large, directly affected by the proposed changes.

The ACCC notes that there is at least one party in the industry in a slightly different position to either a stand alone rail operator or freight forwarder. That party is SCT

[34] ARTC application p. 5.

who is an integrated freight forwarder / rail operator and who contracts with both the owner of the goods and ARTC for use of the Network.

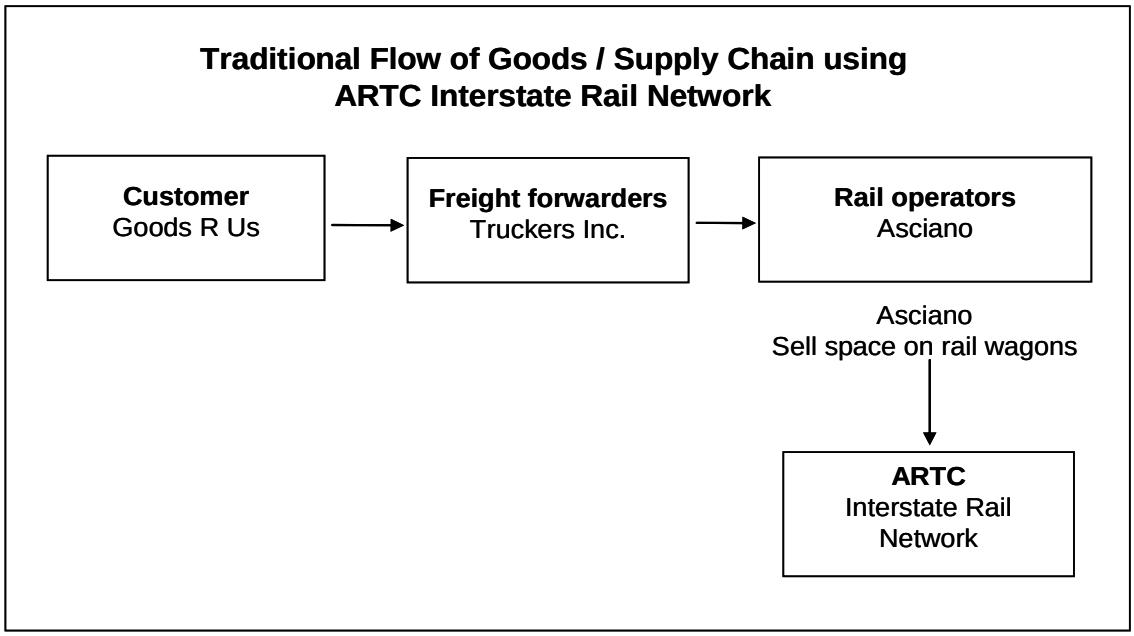
SCT, in its submission, notes that it believes that it is the only freight forwarder to contract directly with the ARTC and that it does cover some, but not all, of its clients against damage to their goods whilst in SCT's care (and in so doing protects itself with Marine Insurance). As such, SCT believes that the proposed variation discriminates against it.[35]

In terms of stand alone rail operators, Asciano, the dominant rail operator using the Network, has confirmed in its submission that it is market practice for operators to enter into contracts with their customers that include an indemnity for losses that would otherwise be claimable under statute or general law. It further confirms, however, that its group of companies do not enter into such arrangements ("no-fault" liability) with customers and would be surprised if the practice was followed by other larger operators. It notes that the operator/customer contracts (SCT's situation) that ARTC is concerned about, is not industry standard.[36]

The ACCC concludes that due to the nature of the proposed changes, any rail operator that enters into a contract with a third party and in which the operator assumes some liability or faces some potential claim by a third party is potentially affected by the proposed variation. The proposed changes appear to particularly affect SCT because they contract with some customers on a 'no-fault' liability basis whereas Asciano suggest that its group do not and other larger operators probably do not.

The following figures (Figure 4 and Figure 5) are a depiction of the typical supply chain arrangements involving ARTC.

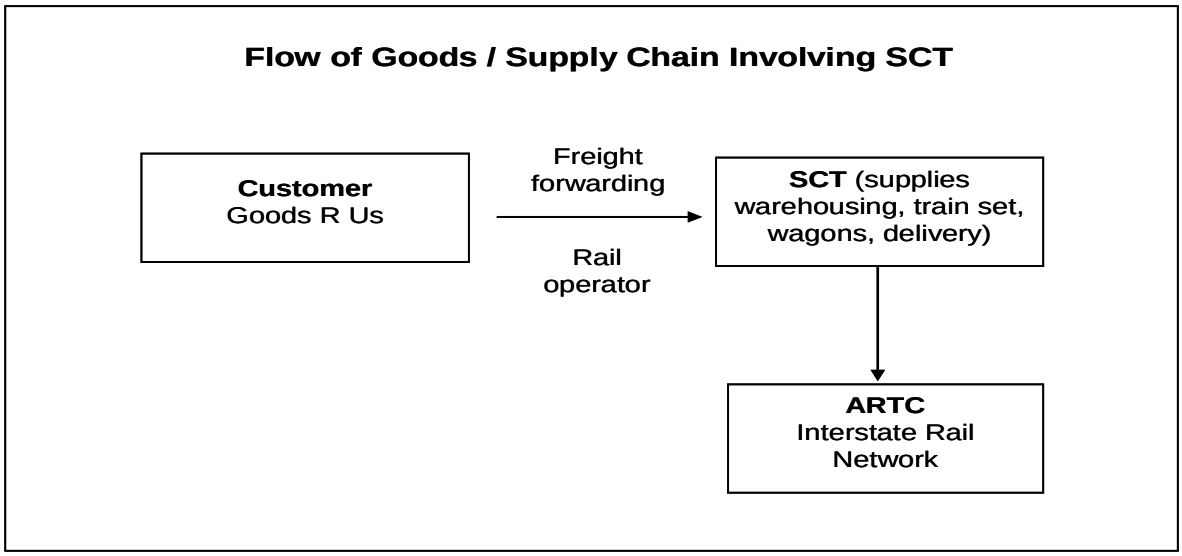
Figure 4



[35] SCT submission p. 4.
[36] Asciano submission p. 2.

1. Customer requires goods to be transported from point A to point B.
2. Customer contacts freight forwarder who collects the goods and transports them to rail operator warehouse at point A depot.
3. Freight forwarder contracts with rail operator for container space on train to transport the goods.
4. Rail operator transports the good using trains which operate using the ARTC Interstate Rail Network pursuant to contract with ARTC.

Figure 5



1. Customer requires goods to be transported from point A to point B.
2. Customer contracts with SCT who collect the goods and transport them to its warehouse at point A depot.
3. At point A depot, SCT pack the goods onto its rail wagons using its own train set and wagons and transports the goods using trains which operate using ARTC Network pursuant to contract SCT has with ARTC.
4. At point B depot, SCT unpack and transport goods for distribution.

Note: In this operation, SCT act a both freight forwarder (in that it collects the goods from customer / owner and delivers them to packing onto train) and rail operator (in that it operates the train set that transports the goods to its point B depot)

Interested party submissions on the proposed variation

Asciano

Asciano is a rail operator who contracts directly with ARTC for use of the Interstate rail network in order to run its trains and transport goods for customers (owner of goods and/or freight forwarders).

The ACCC notes that Asciano does not support the variation in its current form.

Asciano submits that it accepts the principle underlying the proposed variation that where a party is unable to manage risk of exposure to a third party, it is not appropriate to accept liability for the risk. However, it further submits that the proposed variation as drafted does not accurately give effect to this principle.

The main point of contention for Asciano is that the effect of the proposed variation is that the variation as drafted excludes all third party losses arising via a contract between Party A and a third party. Party A cannot recover loss from Party B where the loss arises via a contract between Party A and a third party, notwithstanding that Party B may have caused or contributed to an Incident and is responsible for the loss. That is, where a rail operator has agreed to indemnify a customer for a loss that would ordinarily be claimable under general law or statute, which Asciano submits is the standard industry practice.

Asciano submits that if the proposed variation was accepted, losses arising from such indemnities under the contract would not be recoverable from ARTC even though ARTC has breached its statutory or general law obligations. Contrary to ARTC's intention, the proposed variation as drafted would exclude all third party losses arising from a contract between Party B and a third party, including those that are appropriate for Party A to be responsible for due to Party A having caused or contributed to an incident.

Asciano submit that the affect of the proposed variation if consented to would be to alter the risk profile of the rail operator's existing customer contracts which would then bring about a substantial change in standard industry practice. This industry wide impact would be far greater than the purported change in circumstance that ARTC seeks to address.[37]

SCT

As noted above, SCT is an integrated freight forwarder / rail operator. Consequently, it contracts directly with the customer/owner of goods for carriage and delivery of those goods and with ARTC for use of the Network (see Figure 5 above for further discussion of this arrangement).

The ACCC notes that SCT opposes the variation because SCT are of the view that ARTC's variation is an invalid application, is an unreasonable variation and it discriminates against SCT.

Firstly, SCT submits that one of the ARTC articulated policies underpinning the Undertaking is that a party in breach of the IAA which results in an Incident fully indemnifies the other party. SCT submits that the proposed variation now moves away from and contradicts this principle as articulated to industry. SCT point to an industry information session given by ARTC in Adelaide on 26 February 2007 in which one of the principles put forward by ARTC was that where a party breaches the IAA and the

[37] Asciano submission pp. 4 – 5.

breach causes an Incident, then the party responsible for the breach covers its own loss and fully indemnifies the other party.[38]

SCT submits that the import of the proposed change is to allow ARTC to deny having to reimburse SCT for any payment that SCT might have to make to a customer for goods damaged in an accident even where ARTC is at fault under the contracted arrangement. SCT considers this contrary to past practice in the rail industry and practice in other transport industries.

SCT notes that it does cover some, but not all, of its clients against damage to their goods which are in SCT's care and it does so through Marine Insurance. However, it is submitted that the effect of the variation is to prevent SCT (or its insurance company standing in SCT's shoes) from claiming against ARTC where ARTC is at fault. SCT state that its insurance brokers have indicated that it is probable that SCT would be denied Marine Insurance because of this potential outcome.

SCT also notes that the proposed variation directly affects them as an integrated freight forwarder / rail operator who directly contracts with customers for the transport of goods and with ARTC. Other freight forwarders can contract to cover customer's goods and not have the same problems of insurance nor of having to contract with ARTC.

Other rail operators will continue to contract with ARTC but not have a direct customer relationship that a freight forwarder has. Therefore, SCT argues that this change appears to only affect SCT because of its unique integrated supply chain model. SCT therefore submit that the IAA agreement if changed would discriminate against it.

SCT also note that the ARTC claim that the variation would not prevent SCT's clients from suing the ARTC directly for negligence or loss is "disingenuous and misleading" because a customer would ordinarily look to the party with whom it directly contracts in order to recover loss and not go through the more "tortuous route" of a legal claim against ARTC. Therefore, while technically a party may sue ARTC directly, it is not the most likely course of action.

SCT submits that it is generally accepted that if a person causes loss or damage to another, then that person is responsible to the other for the loss regardless of whether the cost is high or low. This approach is fair to the lay observer and is supported in common law. SCT submits that the proposed variation seeks to walk away from this. Under the proposed variation, ARTC would not be responsible to SCT for any costs incurred by SCT for damage to its customers products even where ARTC was demonstrably and totally at fault.[39]

SCT note that the Undertaking was approved by ACCC in July 2008 as a 10 year undertaking. It submits that contracts in the freight industry last for several years and therefore there needs to be some stable framework for the comfort of SCT and its customers. Without such stability, rail suffers in competition against road and sea and exposes SCT to unacceptable risk. SCT believes that the ACCC should consider

[38] SCT submission p. 7.
[39] Ibid pp. 4 and 8.

whether the original application was adequately thought through and the short duration in which the Undertaking has been in operation.

FreightLink (and Asia Pacific Transport Pty Ltd)

FreightLink is a vertically integrated rail freight business. Asia Pacific Transport is an entity within FreightLink that is responsible for track access.

The ACCC notes that FreightLink (and Asia Pacific Transport) support the proposed variation. FreightLink agrees with ARTC proposed changes and that they believe that the proposed changes as drafted have the intended effect and do not have any possible unintended effects. FreightLink further submit that no other changes are required in order to achieve the desired result and that there are no other related matters that the ACCC needs to take into account.[40]

ACCC Assessment of the Proposed Variation

Clause 15.1(b) – delete the words " … for loss or damage …"

The purpose of clause 15.1(b) is unchanged. Clause 15.1(a) explains that the intention of clause 15.1(b) is that the regime for liability of ARTC and an operator to each other is determined only by reference to clause 15.

Deletion of the words 'for loss or damage' from clause 15.1(b) broadens the coverage of the clause in which each party agrees to release each other from all claims. The changed clause would mean that each party agrees to release each other *from all claims* resulting from an Incident, including where the Incident was caused by the negligence of one of the parties, *except to the extent that the claims are made under clause 15*.

In other words, no claim can be made against the other party if it is brought outside of the operation of clause 15. If it is a claim that arises within the operation of clause 15, however, then there is no release of the other party and the claim is permitted.

This clause sets out the circumstances as to when a party is not able to bring a claim against the other party. The changed clause now makes it clear that *all claims* are released against the other party, *except* claims that can be made under (the revised) clause 15 whereas under the current form of clause, only claims for loss or damage are released (except to the extent that they fall within clause 15). The removal of the words "loss or damage" means that the clause effectively limits any claims except those made pursuant to clause 15.3.[41]

[40] FreightLink submission to ACCC of 17 November 2008.
[41] It is noted that this change appears to remove *all* rights of a party to bring an action except those permitted by clause 15 and therefore may potentially have broader implications for the parties.

Clause 15.2(b) – amend the definition of 'loss or damage' as follows:

The term 'loss or damage' is used frequently throughout clause 15 and is therefore important in terms of the overall operation of the clause. ARTC propose to vary clause 15.2(b) by inserting a substantially changed version of the term into the IAA. This has the effect of materially altering the scope of the indemnity provisions set out in clause 15.3.

The ACCC notes as follows:

- The first limb of the definition is unchanged from the current wording.
- The second limb limits the meaning to any liability to a third party (now excludes a claim by a third party) and then limits the meaning of liability further by specifying that the liability to the third party must arise from the negligence or breach of statutory duty of ARTC or the Operator – but – specifically excludes liability to a third party arising out of an agreement with the third party or breach of that agreement with a third party.
- The third limb is unchanged from the current wording.
- The fourth limb is unchanged from the current wording.

Accordingly, when clause 15 uses the term 'loss or damage' of either the Operator or ARTC in relation to a third party, it includes one party's liability to a third party arising out of the negligence or breach of statutory duty of the Operator or ARTC - but - *specifically excludes circumstances where that liability has arisen due to an agreement (or breach of) with the third party*.

This can be contrasted with the current meaning of 'loss or damage' in which the term includes any liability or claim made by a third party without limiting the circumstances in which that liability might arise.

An example of how the ACCC understands that the varied term 'loss or damage' alters the operation of clause 15 is illustrated below:

Clause 15.3(a) of the IAA currently provides as follows:

> **15.3 Indemnity**
>
> Where ARTC and/or the Operator suffer loss or damage as a result of an Incident, and:
>
> (a) if:
>
> (i) there is a breach of this Agreement by ARTC or the Operator; and
>
> (ii) the breach is the sole cause of the Incident,
>
> then the party in breach will:
>
> (iii) be responsible for its own loss or damage arising from the Incident; and

(iv) completely and effectually indemnify the other party in respect of loss or damage suffered by the other party as a result of the Incident;

Clause 15.3(a) provides a regime whereby if ARTC and/or the Operator suffers loss or damage arising out of an Incident and the Incident is a result of a breach of the IAA by for example, ARTC, then ARTC must meet its own losses and the ARTC must fully cover the Operator for its losses suffered as a result of the Incident.

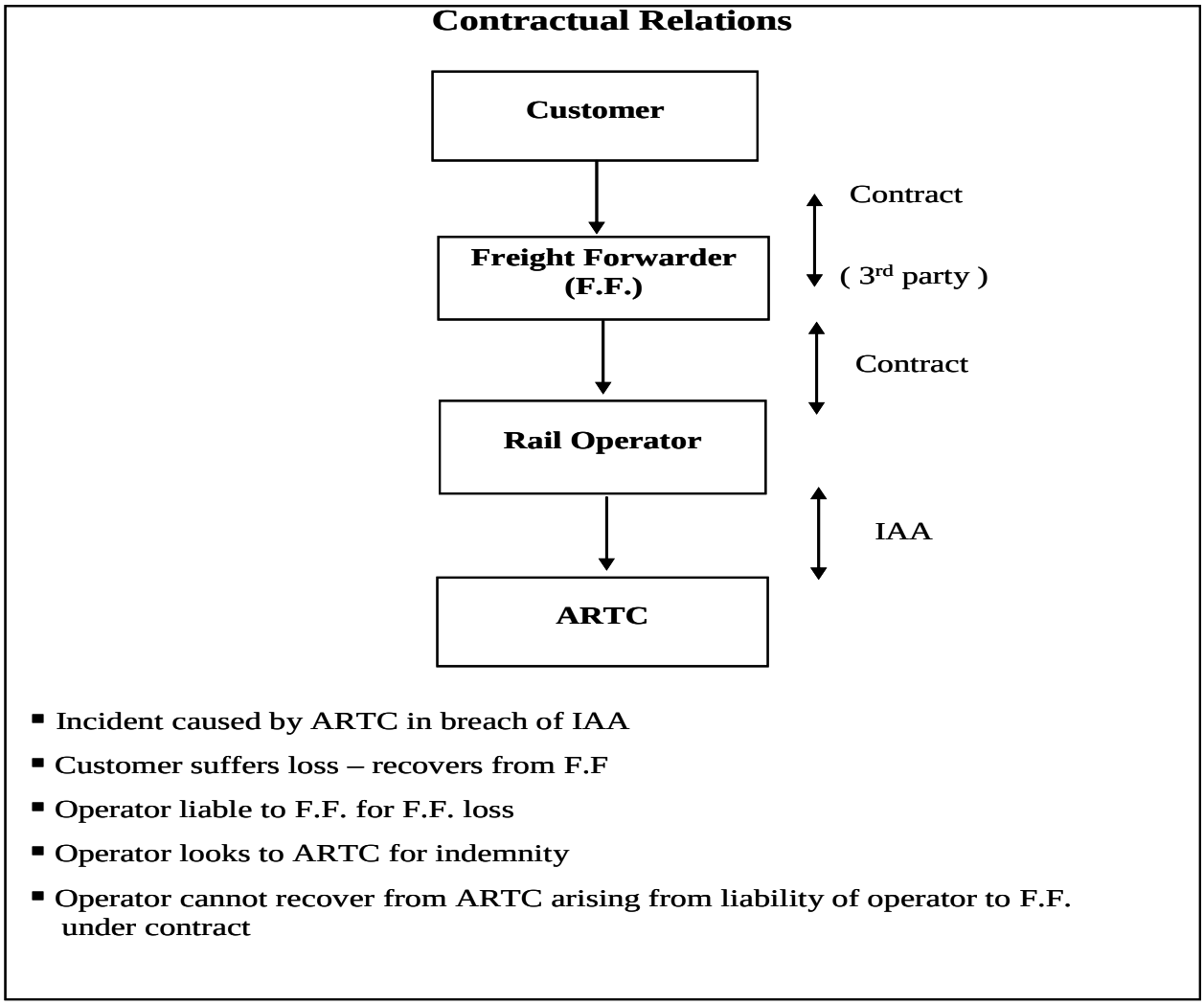
In this example, based on the proposed varied clause 15, the Operator's loss cannot include any liability that the Operator owes to a third party arising out of an agreement the Operator has with the third party. In other words, under clause 15.3(a), that contractual liability to the third party cannot be recovered by the Operator from ARTC.

This would appear to be the outcome even where the Operator suffers loss or damage out of an Incident that was wholly caused or contributed to by ARTC in breach of the IAA. This is because the varied term 'loss or damage' excludes liability an Operator may have pursuant to an agreement with a third party. In other words, if ARTC breach the IAA and as a result an Incident is caused in which a third party suffers damage to its goods and the Operator becomes liable to the third party for the damage to the goods pursuant to the agreement the Operator has with the third party, the Operator cannot recover the loss from ARTC. It is uncertain whether this was the intended effect of the proposed change, but this appears to be the practical effect of the proposal.

However, where the Operator's liability to the third party arises due to the negligence (i.e. general law) or breach of statutory duty by ARTC, then this form of liability qualifies as 'loss or damage' and the Operator may look to ARTC for full indemnity of this amount of loss or damage.

The ACCC's view is that the proposed changes have the effect of narrowing the scope of liability to a third party by excluding forms of liability arising out of an agreement a party has with a third party. This in turn alters what a party may potentially claim from another party under the clause 15 regime. This is illustrated by the following figure (Figure 6):

Figure 6



The regime still permits liability owed to a third party where that liability arises out of negligence or breach of statutory duty, however, contractual liability is specifically excluded from the claimable forms of loss.

The ACCC notes that both SCT and Asciano do not support the proposed variation. Asciano supports the underlying principle that where a party is unable to manage a risk of exposure to a third party, then it is not appropriate for it to accept the risk, but conversely, it notes that the proposed variation as drafted will exclude all third party losses arising from contract, including those that it is appropriate for a party, that has caused, or contributed to, an incident, should be responsible for.

Similarly, as a matter of principle, SCT note that it is generally accepted that if a person causes loss or damage to another, then the first person is responsible to the second person for the cost of the damage regardless of whether the cost is high or low. SCT submit:

> "[the] ARTC would not be responsible to SCT for any costs incurred by SCT for damage to its customers products even where ARTC was demonstrably and totally at fault."[42]

In its submission as to the effect of the proposed variation, ARTC submit that:

> "Operators are still free to accept no fault liability to Consignors but cannot, and should not, be able to pass on that liability to ARTC".[43]

ARTC continues:[44]

> "The proposed change addresses the disparity that has now arisen between the commercial returns and the level of risk to which ARTC is potentially exposed. It does so without materially impacting on operators."

Whether or not it was the intended effect, the ACCC does not consider it appropriate for a party to completely relieve itself of responsibility for another party's liability to a third party, including liability for negligence or breach of statutory duty arising out of contract. It would seem appropriate that where the loss or damage that arose out of an Incident which was the result of the conduct or omission of a party in breach of an agreement with that other party (i.e. the IAA), then the other party who is liable to a third party, should be able to recover that loss from the party at fault – even if that liability arises pursuant to contract.

In considering what should be the underlying principle relevant to the indemnity provisions, it seems to be not so much a question of whether one party should be entitled to pass on liability, but rather the fundamental issue of a party being responsible for the loss it creates.

This is not to detract from the similarly important principle that a party should be able to manage risk of exposure to a third party. However, in keeping with the above principle, it would seem more proper for ARTC to be planning for the risk of having to indemnify a party where it caused an Incident in breach of the IAA rather than planning around how to avoid that risk.

In the ACCC's view, a rail operator is most likely going to be required to accept some risk and therefore liability for handling a customer's goods in order to do business. However, in doing so, it must also recognise that there will be circumstances where it should not expect indemnity from ARTC. The ACCC is of the view that the current form of indemnity clause strikes a reasonable balance in terms of allocation of risk in that the party that causes or contributes to an incident must indemnity the other party not at fault for any losses it may incur.

Accordingly, one level of indemnity that the ACCC is of the view that ARTC (or an Operator) must expect to assume is where it is responsible for the loss suffered by a third party and in turn the loss of a rail operator. This should not be confined merely to

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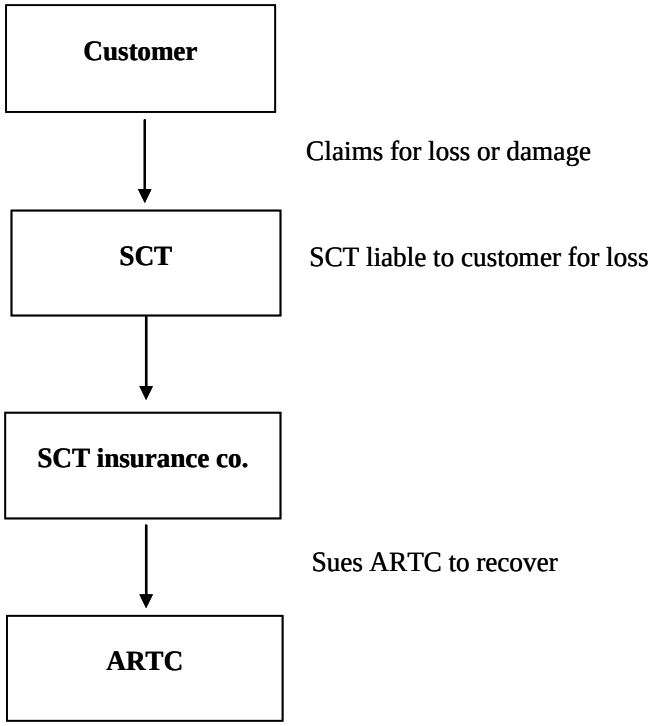
[42] SCT submission p. 8.
[43] ARTC submission p. 5.
[44] Ibid p. 5.

circumstances of negligence or breach of statutory duty. The below figure (Figure 7) illustrates the lines of responsibility for indemnity in the SCT scenario.

Figure 7

Contractual Relationships in the SCT Supply Chain

Scenario: Rail accident – ARTC fault in network – negligence or breach of statutory duty – goods damaged.



➡ Changed clause will mean that the insurance company will not be able to sue ARTC where ARTC is at fault.

Further, the ACCC is not of the view that the fact a third party would still have the right to recover losses directly from the ARTC is any comfort to the party that has the liability to the third party. A third party is most likely to pursue the simplest and most cost effective means of recovering its losses and this will be against the party with whom it directly contracts and who has provided for this contingency.

In addition, the information presented to the ACCC does not support the ARTC contention that the change could be made without materially impacting on operators. It is uncertain how widespread the issue is but Asciano note that it is market practice for operators to enter into contracts with their customers that includes an indemnity for losses otherwise claimable under statute or general law. Asciano also contend, therefore that the effect of the proposed variation would be to substantially alter the risk profile of rail operators existing contracts and require a substantial change to industry practice.

While most rail operators do not contract directly with the customer/owners of goods, it remains unclear how widespread the issue of assumption of “no-fault” liability is by rail operators, the proposed changes clearly have the potential to materially impact on SCT given its direct contractual relationship with customer /owners.

Further, the information available does not support the contention that the practice (of assuming “no-fault” liability) will become more widespread and be industry practice and therefore it seems difficult for ARTC to assert that this measure is required to offset the level of risk that ARTC is potentially exposed without further evidence supporting such an assertion.

Part D Draft Decision

As noted in Part B, the ACCC may consent to the proposed variation to the undertaking if it thinks it appropriate to do so having regard to the statutory criteria in subs. 44ZZA(3) of the Act. In the Issues Paper, interested parties were invited, in responding to the proposed variation, to address the statutory criteria that the ACCC is required to apply.

The ACCC has considered the proposed variation in the light of the criteria and the parties' submissions and, based on its assessment, has come to the following preliminary conclusions.

1. The objects of Part IIIA

- ***The promotion of the economically efficient operation of, use of and investment in the infrastructure by which services are provided, thereby promoting effective competition in upstream and downstream markets; and***

- ***Provide a framework and guiding principles to encourage a consistent approach to access regulation in each industry.***

The proposed form of clause 15 would shift risk for third party indemnity away from ARTC. This is because clause 15 would no longer require ARTC, for example, to indemnify an operator for losses that the operator incurs in the form of third party liabilities under contract, in circumstances where ARTC has breached the IAA and such breach has caused or contributed to an Incident causing the loss.

The ACCC is of the view that this shifting of allocation of risk lowers incentives for ARTC to use and invest in the rail infrastructure efficiently because of its lower risk to the operators.

As a result, the ACCC is of the preliminary view that the proposed variation is not consistent with the object of promoting the economically efficient operation of the infrastructure and thereby promoting competition in other markets.

2. The pricing principles specified in s. 44ZZCA

ARTC submit that:

> "The rate of return approved by the ACCC under the undertaking did not envisage ARTC taking on the risk exposures arising from the change in circumstances"[45]

Therefore:

[45] ARTC submission p. 5.

> "There is now a mismatch between the ARTC's returns and level of commercial risk which was never intended and which is not necessary for users to obtain fair access to the network'.[46]

In response to this, Asciano note that:

> "The documentation provided by ARTC to the ACCC during consideration of the Undertaking earlier in 2008 showed that ARTC will earn substantially below the allowed rate of return on every line sector covered by the Undertaking. The ACCC acknowledged this in its Final Decision on the Undertaking"
>
> …
>
> "It is, therefore, very difficult to understand an argument based on ARTC's allowed rate of return, a rate that both ARTC and the regulator agreed it would never achieve. ARTC's argument appears to be that, had it been aware of the undesired practice at the time of the approval, then ARTC would have asked for a higher rate of return … [however] … ARTC was never going to earn the rate it was granted, let alone a higher rate.[47]

In their submission, SCT note that the proposed variation:

> "is an improvement in ARTC's commercial position from where it is at present and where it always was, not a restoration of its commercial position".[48]

Pricing principle 44ZZCA(a)(ii) of the Act provides that regulated access prices should:

> "include a return on investment commensurate with the regulatory and commercial risks involved".

It is the ACCC's view that if the proposed variation was accepted as currently drafted, ARTC's exposure to potential liability under the IAA would be significantly reduced. This is because loss arising from indemnities granted by operators to their customers under contract would not be recoverable by operators from ARTC notwithstanding ARTC being at fault for an Incident. In other words, there is a reasonable argument that ARTC's commercial risks would not be commensurate with the allowable return on investment.

The current form of clause 15 is based on the understood level of risk that ARTC was exposed to at the time the Undertaking was approved. The variation, if made, would result in a marked improvement in ARTC's commercial position, however, without any adjustment in the return on investment.

The ACCC does not agree with the proposition that the proposed variation would reflect a return on investment commensurate with the level of commercial risk involved. Accordingly, it is of the preliminary view that the proposed variation to

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[46] Ibid. p. 5.
[47] Asciano submission p. 3.
[48] SCT submission p. 6.

clause 15 of the IAA does raise objections under section 44ZZA(3)(ab) of Part IIIA of the Act.

3. The legitimate business interests of the service provider

As noted above, ARTC submit that:

> "The rate of return approved by the ACCC under the undertaking did not envisage ARTC taking on the risk exposures arising from the change in circumstances"[49]

Therefore:

> "There is now a mismatch between the ARTC's returns and level of commercial risk which was never intended and which is not necessary for users to obtain fair access to the network'.[50]

Asciano note that ARTC has not identified the train operator who has entered into the arrangements that ARTC complain of. Further, it is unknown whether this practice applies to one particular operator or a number of operators.

Asciano confirms that none of the Asciano group of companies has entered into an arrangement complained of by ARTC and it "would be surprising"[51] if this was the practice followed by the larger operators. As such, Asciano submits that it is doubtful whether the issue is widespread and substantial and therefore whether the potential impact on ARTC would be as significant as claimed.

Further, Asciano makes the additional point that the ARTC submission is largely based on the possible spread of this practice throughout the industry:

> "Further, given competition between operators in above rail services it is quite possible that such provisions could become industry standard for large Consignors."[52]

The ACCC is of the view that there little evidence to suggest that "no-fault" liability is, or will become, a widespread industry practice. On the contrary, the submissions received suggest that the practice is probably isolated.

Further, the proposed variation (whether intended or not) will remove all third party liability arising under contract from the indemnity provisions regardless of whether either party has breached the IAA. That is, an operator, for example, could never be indemnified under the IAA for loss it incurred pursuant to a third party contract even if ARTC was in breach of the IAA and had caused an Incident.

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[49] ARTC submission p. 5.
[50] Ibid. p. 5.
[51] Asciano submission p. 2.
[52] ARTC submission p. 4.

The ACCC understands that it is appropriate for a party to be responsible for the loss it causes and therefore to be required to indemnify another party for losses incurred by that party even if the loss arises out of contract or by other means.

As such, the ACCC is of the view that the risk is probably not as significant as suggested by ARTC and the clause as drafted removes responsibility for loss which it might normally be exposed to in normal commercial dealings, consequently the proposed variation goes beyond what is necessary to protect the legitimate commercial interests of ARTC.

The ACCC's preliminary view is that the proposed variation does raise objections under subs. 44ZZA(3)(a) of Part IIIA of the Act.

4. The public interest, including the public interest in having competition in markets (whether or not in Australia)

Asciano note that:

> "It is not in the public interest to have an inappropriate allocation of risk. It is efficient for the party that can control the risk to be liable for the risk. ARTC's proposal results, albeit unintentionally, in an inappropriate allocation of risk namely that ARTC does not bear the risk of an ARTC breach of a general law or statute."[53]

SCT note that:

> "It is generally accepted that if a person causes loss or damage to another, then the first person is responsible to the second for the cost of that damage."
>
> …
>
> "Under the proposed variation, the ARTC would not be responsible to SCT for any cost incurred by SCT for product damage even in situations where the ARTC was demonstrably and totally at fault".[54]

The ACCC is of the view that if the proposed amendments were accepted as currently drafted, an operator could not recover losses from ARTC that arise from contractual indemnities they have offered their customers in situations where the loss was caused by ARTC.

Such an approach would be contrary to considerations of efficiency in that the allocation of risk and responsibility for compensation to a third party would sit entirely with the operator even though ARTC is best placed to manage the maintenance of its Network and therefore the potential for loss of a third party.

Accordingly, the ACCC is of the preliminary view is that the proposed variation does raise objections under subs. 44ZZA(3)(b) of Part IIIA of the Act.

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[53] Asciano submission p. 6.
[54] SCT submission p. 8.

5. The interests of the persons who might want access to the service

ARTC note that as a result of the changed circumstances:

> "There is now a mismatch between the ARTC's returns and level of commercial risk which was never intended and *which is not necessary for users to obtain fair access to the network'*[emphasis added].[55]

Asciano is of the view that:

> "… the drafting of the proposed amendment has consequences over and above those argued by ARTC as necessary so that the risk relationship between ARTC and train operators is altered in favour of ARTC. Whether intended or not, this is contrary to the interests of access seekers and goes beyond the principle ARTC claims it is applying".[56]

In addition, Asciano argues that:

> "ARTC has failed to follow the appropriate requirements under its own Undertaking. This is contrary to the interests of access."[57]

The ACCC is of the view that if the proposed variation was accepted as currently drafted, it is highly unlikely to appropriately meet the commercial needs of operators as they are required to do business with their customers. Interested parties expressed concern that the proposed variation is likely to require a substantial change to standard industry practice regarding the granting of limited indemnities by operators to their customers. As such, the variation would mean important changes to the nature of the relationship that operators currently have with their customers.

If the operators were not able to change the terms on which they contracted with their customers, then the level of risk that operators would be required to adopt in order to do business would be out of proportion to what would be considered a reasonable allocation of risk.

Further, the proposed variation would directly alter and affect the allocation of risk for liability to third parties between rail operators and ARTC in such a way that ARTC would not be required to bear the burden of losses to third parties under contract, even where it may have caused the loss. As noted above, if the variation came into operation, it seems that operators would have to change standard industry practice which would affect their existing and future customer relationships.

Accordingly, the ACCC is of the view that the proposed variation is not in the interests of persons who have or who may want access to the service.

The ACCC is of the preliminary view that the proposed variation to clause 15 of the IAA does raise objections under paragraph 44ZZA(3)(c) of Part IIIA of the Act.

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[55] ARTC application p. 5.
[56] Asciano submission, p. 6.
[57] Ibid. p. 6.

6. ***Whether the undertaking is in accordance with an access code that applies to the service***

The ACCC is of the view that this criterion is not relevant to the current assessment.

7. Whether access to the service is already the subject of an access regime that the Commonwealth Minister has decided is an effective regime under s. 44N; and

The ACCC is of the view that this criterion is not relevant to the current assessment.

8. Any other matters that the ACCC thinks relevant.

There are no other matters that the ACCC thinks relevant to this Draft Decision.

CONCLUSION

The ACCC's Draft Decision is to not consent to the ARTC application to vary the Undertaking as the ACCC does not believe that it is an appropriate variation, having regard to the statutory criteria under subs. 44ZZA(3).

This Draft Decision notes that there are several matters which ARTC may wish to further consider in relation to this variation request.

The ACCC's discussion of the "changed circumstances" in Part C.1 notes how it is unclear to the ACCC, from the submissions received, as to what the "changed circumstances" are which would increase ARTC's exposure to risk of loss or damage bearing in mind the unchanged operation of clause 15 of the IAA. ARTC's variation application would benefit from further explanation and examples of how this is said to occur.

Similarly, the application and subsequent interested party submissions suggest there is some confusion about what was/is understood to be the current industry practice in relation to rail operators contractually accepting liability for loss or damage to their customers.

The ACCC's preliminary view is that the proposed variation is not appropriate because of the effect of the proposed wording of clause 15. The form and effect of the proposed variation raises some fundamental concerns for the ACCC about the appropriate allocation of risk for loss or damage.

The Draft Decision further notes the ACCC's preliminary view that there has been no consultation with rail operators on the variation prior to seeking the ACCC's consent. This is of concern to the ACCC given that the consultation requirement is a binding term of the operative Undertaking.

It is for ARTC to develop the text of the variation that it wishes to implement. Overall, the submissions indicate that there may not be a common understanding about (1) what ARTC seeks to achieve or (2) the effect of the proposed variation. The apparent level of misunderstanding may reflect the lack of a prior consultation process.

ARTC and interested parties have an opportunity to clarify the above matters through the making of submissions in response to this Draft Decision.

The ACCC notes that Part IIIA of the Act does not require ARTC to proceed with this variation request. A variation application may be withdrawn at any time prior to the ACCC making a final decision. Any revised form of words from the ARTC for the ACCC to consider under subs. 44ZZA(7) will, however, constitute a fresh variation application.

The ARTC may wish to consider these matters further in responding to the issues raised by the ACCC, including whether some or all of these issues may be dealt with in consultation with rail operators prior to proceeding with a variation to the Undertaking.

Appendix A

List of Interested Party Submissions

Submissions to the ACCC issues paper – 31 October 2008

- Asciano Limited, *Asciano submission – Application for variation of ARTC Interstate Access Undertaking*, 21 November 2008 (Asciano submission), received 21 November 2008;

- Freight Link Pty Ltd, *Freight Link submission – ARTC Interstate Rail Access Undertaking – Application for Variation*, 17 November 2008 (FreightLink submission), received 21 November 2008;

- SCT Logistics, *SCT submission re Application for variation of ARTC Interstate Access Undertaking*, 20 November 2008 (SCT submission), received 20 November 2008.