

Submission to the ACCC

**ARTC 2010 Draft Hunter Valley
Access Undertaking**

October 2010

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1 EXECUTIVE SUMMARY

Asciano welcomes the opportunity to make a submission to the Australian Competition and Consumer Commission (ACCC) on the Australian Rail Track Corporation (ARTC) proposed 2010 Hunter Valley Access Undertaking (HVAU), which was submitted by ARTC to the ACCC in September 2010.

In recent months Asciano has commenced discussions with coal miners and the ARTC within the framework of the new contracting structure. Asciano's early experience raises concerns about how these structures will operate, and in particular the need for improved transitional provisions and the need to reconsider the nature of obligations placed on the operator by the Access Holder Agreement, when the operator is not a party to this agreement.

Asciano also has a major concern with the development of the efficient train configuration as outlined in section 4.16 of the draft HVAU. Asciano believes that the lack of an obligation to consult with operators and the long time frame allowed for determining the efficient train configuration both need to be revised if the process is to result in a workable and timely solution.

This submission also raises:

- new concerns with Indicative Access Holder Agreement and Operator Sub Agreement; and
- re-states major concerns Asciano has raised previously in the HVAU consultation process. The previous concerns which are raised include:
 - the fact that pricing structures create incentives for Asciano to operate sub-optimal train sizes , which reduce system capacity; and
 - problems with the network management principles, which arise as the system is attempting to operate both timetabled non-coal services and sequenced coal services.

Asciano believes that these major concerns previously raised have not been adequately addressed.

This submission is public.

2 NEW ISSUES ARISING FROM CONTRACTING STRUCTURES

Since the ACCC HVAU Draft Decision in March 2010 Asciano has commenced discussions and negotiations with both coal miners and ARTC as to how the new contracting structures, which utilise an Access Holder Agreement (AHA) and Operator Sub Agreement (OSA), will operate in practice. These discussions have raised and reinforced several issues as outlined below.

2.1 Relationship between the Operator and the Access Holder Agreement

The OSA is, appropriately, required to be endorsed by the access holder. Via this mechanism the access holder can ensure the OSA meets the access holder's requirements and any obligations the access holder has under the OSA can be fully understood and acted upon.

Asciano's concern is that the operator does not have a corresponding right to view the AHA and this is problematic as the OSA effectively requires the operator to comply with the terms and conditions of the AHA thus placing obligations or other requirements on the operator which are not adequately reflected in the OSA. For example Recitals D and E of the OSA state:

Recital D: ARTC agrees to grant the Operator rights to use and provide Services to the Access Holder on the Network upon the terms and conditions set out in this agreement and the Access Holder Agreement

Recital E: The Operator will exercise its right to use and provide Services on the Network in accordance with this agreement and the Access Holder's access rights under the Access Holder Agreement.

More examples where the AHA places obligations on the Operator can be found throughout the OSA. For example:

OSA 3.1 a) ii)... the Operator may, during the Term, for the purpose of transporting coal, operate a Service on a Train Path or a Path Usage, upon the terms and conditions set out in this agreement, subject to ... the terms of access granted to the Access Holder under the Access Holder Agreement

OSA 3.1 c) The Operator agrees at all times during the Term not to access or attempt to access the Network on behalf of the Access Holder in any way other than is authorised by this agreement and the Access Holder Agreement, or as authorised under a separate valid and binding agreement

The examples above are not exhaustive.

Thus the operator is providing services under the terms of the AHA, but the operator is not necessarily permitted to view the AHA. Asciano believes that if triangular contracting is to be workable in the long term the operator must have a right to view the AHA as agreed between the ARTC and the access holder prior to it being able to execute and agree the OSA. Asciano recognises that an indicative AHA is publicly available, but as the operator is required to act in accordance with the AHA agreed by ARTC and the access holder, and indeed will be in breach of its own OSA if it breaches the AHA, Asciano believes that it is only reasonable and appropriate that the operator have a right to view this document so that the operator can fully understand the requirements of the AHA and thus all of the obligations the operator has under the OSA can be fully understood and acted upon. In addition, the operator should be made aware of any amendments to any AHA that it holds the applicable OSA so it can understand any implications the amendments may have on its obligations.

2.2 Transitional Issues

Asciano appreciates that the ARTC has provided an extensive guide relating to the transition of regulatory arrangements in Appendix 5 of the Explanatory Guide released in September 2010. However, Asciano continues to believe that a similar explanation is needed of issues relating to practical operation in general, and contractual arrangements and contractual transition in particular.

In the near future the Hunter Valley may have trains operating on both the current contracting model and the OSA – AHA contracting model. It is envisaged that the same operator will have trains operating under both models, and it is conceivable that trains operating under both models may potentially serve a single mine for a period of time.

Asciano is concerned that the HVAU's lack of transitional arrangements between these two models creates significant potential for uncertainty. In particular, Asciano is concerned whether, if paths to serve a mine are not permitted to an operator under one model, whether the operator can then use paths it is entitled to under the other model to serve the mine.

Similarly Asciano is concerned as to whether paths under either model are intended to receive preference in the event of any conflict.

Asciano believes that further transitional arrangements are required to reduce uncertainty and the potential for delays and misalignment, particularly in relation to contracting arrangements. Ideally these transitional provisions should be part of the HVAU document package and in any event, in advance of the execution of an AHA and OSA for any parties.

3 NEW ISSUES ARISING FROM THE AMENDED HVAU, IAHA AND OSA

While Asciano generally welcomes the improvements made in the HVAU it has concerns about some of the new or amended wording including those sections outlined below.

3.1 Issues with Amended HVAU

Efficient Train Configuration

Section 4.16 of the HVAU contains a substantially expanded section on the "Determination of the Indicative Service (Efficient Train Configuration)" which outlines that within four years of the commencement date the ARTC will submit to the ACCC the characteristics of the indicative service, developed in consultation with the HVCCC, which ARTC considers will optimise utilisation of the coal chain capacity. This analysis will be based on "certain system assumptions". The ARTC will seek ACCC approval to amend the HVAU to reflect this efficient train configuration. The HVAU 4.16 indicates that the ARTC are only obliged to consult with the HVCCC in determining the characteristics of the efficient service.

Asciano has three main concerns with the above approach:

- (a) The time frame of four years: This time frame is unacceptable. Much of the data is already held by HVCCC and / or the operators and, similarly, much

of the modelling is already undertaken by the HVCCC and / or the operators. A maximum time frame of 6 months would be more appropriate time frame in which to undertake this modelling and seek ACCC approval. Asciano understands that current HVCCC congestion modelling highlights the significant impact of congestion throughout the coal chain. This congestion is increasing as:

- additional trains are being operated within the coal chain; and
- not all trains within the coal chain are operating at the maximum length enabled by the fixed infrastructure.

Current congestion requires that efficient train configuration issues be resolved in the very near future, not within a four year time frame.

- (b) The nature of the system assumptions used. The system assumptions used to underpin the analysis should be subject to testing by operators and other interested parties.
- (c) The lack of an obligation to consult with operators: As the operators operate the trains, and consequently have more detailed knowledge of train (as opposed to track) operations and issues, the ARTC should be obliged to consult with the operators prior to finalising its position on the efficient train configuration. Similarly, in considering the ARTC proposal the ACCC should seek input from train operators regarding the ARTC proposal. Depending on the final decision on efficient train configuration, the decision may have substantial consequences for operator investments and operators should be provided with an opportunity to comment on the proposal.

Asciano seeks that the final HVAU includes a maximum time frame of 6 months and an obligation to consult train operators on system assumptions and other matters before the efficient train configuration is finalised.

General Issue of Future Reviews Required by the HVAU

As outlined above the HVAU contains a new section which outlines a process for determining the efficient train configuration within the next four years. The outcomes of this process may result in the HVAU being amended. Similarly, the HVAU contains a new section 5.9 “Review of Cancellation Policy and Operation” which outlines a process for reviewing cancellation policy within 12 months. The outcomes of this review may result in the HVAU being amended.

Asciano is concerned that the HVAU contemplates areas where work remains to be completed by the ARTC beyond the current HVAU review. Asciano considers that the Final Decision on the HVAU should address all issues in order to make the best decision possible. Asciano has concerns that by deferring resolution of these matters, and potentially making decisions on these matters in isolation, the single and integrated nature of decision making in relation to the 2010 HVAU has the potential to be diluted. Asciano has a preference that in future reviews of the HVAU that decision-making in relation to specific undertaking components not be deferred or otherwise separated.

KPIs

The HVAU contains new sections, 8.1 relating to “Network KPIs” and 8.2 relating to “Negotiation of KPIs for each Access Agreement”. There is also a new schedule which identifies the Network KPIs and reporting scope and responsibility. ARTC will report on its website against the KPIs in Schedule D.

Asciano notes that the recently approved QR Network Access Undertaking (which also relates to a rail asset which transports coal for export) also includes numerous KPIs, which are reported on quarterly basis. Asciano believes that there is merit in aligning some of these Network KPI definitions over time to allow performance and cost efficiency comparisons and benchmarking.

Asciano recognises that Network KPI comparisons may be problematic, and should be used with caution, as:

- definitions and data collection processes may not be comparable, and
- the two networks are not necessarily directly comparable in all aspects.

Consequently, Network KPI comparisons should only be used when adjusting the KPIs to take account of the differences between networks, where appropriate.

Asciano seeks that ARTC and ACCC consider alignment of Network KPIs with other coal networks over the longer term. Asciano notes that KPI comparisons are used in other regulated infrastructure industries.

Clause 8.2 allows KPIs to be negotiated in individual access agreements. Asciano recognises that there is an issue in balancing the comparability of performance

indicators across the infrastructure, and allowing flexibility in allowing parties to determine performance measures relevant to their individual situation. Asciano believes that there should be a core set of performance measures which are consistent across infrastructure which can be supplemented by additional KPI measures agreed by the parties, allowing matters which are important to the parties to be measured, and thus improved upon.

3.2 Issues with Amended IAHA

Agency and Liability

Clause 4.6 c) of the IAHA includes an expanded “Limited Agency” which states that the access holder does not incur liability for incidents caused by acts or omissions of the operator as a result of the operation of the AHA. Asciano believes that this wording is inappropriate in an AHA to which the operator is not a party. Asciano believes that this clause may have the effect of encouraging the parties to the AHA to assign fault to the operator, even in the event where the causes are more complex.

Originally this clause corresponded to the “Limited Agency” clause in the OSA, which provides that the access holder does not incur liability for incidents caused by acts or omissions of the operator as a result of the operation of the limited agency clause. The amendments proposed in the IAHA broaden the scope and original intent of this clause considerably by taking it beyond the operation of the “Limited Agency” clause and expanding its operation to the whole agreement. As noted above, Asciano does not consider that this is appropriate. In fact, Asciano questions the need for this carve-out of liability in the “Limited Agency” clauses in either the IAHA or OSA at all.

Asciano believes that this clause should be removed.

New and Varied Access Undertakings and AHAs

Clause 19.1 of the IAHA requires that:

- changes to mandatory provisions in a new or amended access undertaking will be uplifted to the AHA, and
- changes to non-mandatory provisions in a new or amended access undertaking will be subject to negotiation with a view to modifying the AHA to amend the agreements

Asciano is concerned that in these instances clauses which may directly impact on operators are being uplifted into the AHA, while the operators have no explicit right to comment on these clauses. Asciano seeks that:

- where any material changes are to be made to an AHA, which may reasonably be expected to impact on operators, the operators are consulted prior to the changes being made; and
- that the relevant operator is notified of all changes to the AHA so that the operator is aware of all of its obligations under the OSA (which as discussed above effectively incorporates the terms and conditions of the AHA).

3.3 Issues with Amended OSA

Indemnities and Liabilities

Asciano has continually expressed concerns about the difficulty and complexity of the “Indemnities and Liabilities” clause included in the OSA. The amendments proposed in the Amended OSA only serve to increase the complexity of the clause. The amendments also create uncertainty, which arises from this increased complexity but also because it is not clear what the amendments are seeking to achieve. This is particularly the case with the amendments to the definition of third party liability and the consequential loss clause as those amendments do not appear to be necessary based on the other clauses and definitions included in the OSA. This uncertainty potentially gives rise to expensive and unnecessary litigation for the purpose of determining the intention of the clauses. In Asciano’s view, it would be more desirable and cost effective for these clauses to be clarified and simplified now.

On that basis, Asciano believes that the amendments should not be accepted and indeed a full review of the liability and indemnity regime under the OSA should be undertaken with a view to simplifying the clauses.

New and Varied Access Undertakings and AHAs

An amended “New and Varied Access Undertaking” which clarifies that any changes in the standard OSA which are accepted by the ACCC as part of a revised AU will be automatically incorporated into OSAs unless the clauses are specifically negotiated. In the event of a dispute the dispute is resolved via the OSA dispute resolution clauses.

Asciano has a practical concern that in the event the amendment in question is an amendment to the dispute resolution clause then this process may become unworkable. It may be more practical that in the event of a dispute the dispute be resolved by either ACCC arbitration pursuant to the undertaking or the dispute resolution clause in the OSA, as agreed by the parties. If there is no agreement ACCC arbitration should be the default dispute resolution mechanism.

Asciano also has a concern with this clause in that it permits agreed contracts to be varied by a regulatory instrument agreed after the fact of the contract and which has the potential to have a substantial impact on the commercial viability of the agreed contract. As such Asciano has concerns that this process may create substantial contracting and commercial problems when the undertaking is amended, as contemplated in HVAU 4.16 and 5.9. For this reason Asciano strongly believes that the Final Decision on the HVAU should address all issues in order to make the best decision possible.

More broadly, Asciano is concerned that AHAs and OSAs are likely to be agreed prior to the ACCC's Final Decision and these AHAs and OSAs will then be subject to changes arising from the Final Decision. Rather than be subject to this short term contracting uncertainty Asciano believes that it would be preferable that no long term AHAs or OSAs be agreed prior to the finalisation of the HVAU. Asciano recognises that it may be possible to agree short term AHAs and OSAs that would apply until the time of the Final Decision but these agreements would then be re-negotiated as new agreements once the HVAU was finalised.

4 ISSUES PREVIOUSLY RAISED BY ASCIANO WHICH CONTINUE TO BE OF CONCERN

In its consultation paper the ACCC notes that if a respondent believes that issues raised in the respondents' previous submissions are still outstanding then these should be identified. Asciano has raised numerous issues in previous submissions which Asciano believe still require resolution. This section identifies major items which Asciano has raised in previous submissions and which Asciano believes remain outstanding.

4.1 Pricing Structures

In its submission of March 2010 Asciano has expressed concern around the ARTC's pricing proposal which does not distinguish between short and long trains, in effect

incentivising inefficient above rail operation. The ARTC continues to put forward a coal access pricing structure that consists of:

- A variable component based on gross tonnes per kilometre (GTK) which is intended to recover variable costs in line with GTK usage via a variable GTK charge; and
- A take or pay component for the access rights which is intended to recover fixed costs relating to assets existing at the commencement date and assets built or acquired after the commencement date. These costs are recovered via a charge calculated on expected monthly GTK usage.

Within the proposed price structure there is no fixed component linked to a flagfall charge. Asciano continues to believe that one of the ARTC's main cost drivers is the number of train journeys and that this cost driver should be reflected in the pricing regime. Asciano does not believe that GTK is the major driver of fixed costs, and consequently basing fixed cost charging structures on GTK is an inefficient approach to cost recovery. This charging structure results in larger coal trains being charged a greater amount for the same train path, and as Asciano indicated in its March 2010 submission Asciano is being encouraged to respond to these pricing signals by operating shorter trains, thus reducing system capacity.

Asciano cannot see any economic justification for current pricing structures discriminating against larger coal trains as opposed to smaller coal trains. The proposed pricing structures mean that it is possible for the same coal train path to be subject to a different pricing outcome, with no economic basis for this price differential.

Asciano recognises that the ARTC is proposing a process to determine the efficient train (as commented on in section 3.1 of this submission), however until this process is finalised the proposed ARTC pricing structure will continue to unnecessarily create inefficient outcomes and provide incentives for operators, such as Asciano, to operate inefficient trains.

Asciano recognises that by using this pricing structure the ARTC is seeking to avoid price shocks, however as costs structures and price structures are misaligned such shocks will inevitably occur. Asciano believes that it would be more constructive to

actively engage in a plan for transitioning these price structures rather than delay the inevitable price shock.

Asciano believes the price structure must be reconsidered as it is currently providing perverse incentives for operators to operate inefficient trains. A move towards cost reflective rail pricing structures which include a flagfall component will send improved price signals to operators.

Asciano believes that the ARTC pricing structure should be rejected by the ACCC as it does not meet the criteria test set out in section 44ZZA(3) of the TPA. The pricing structure, as currently proposed, does not accurately reflect cost structures. This can be addressed by requiring the fixed price component to have a train path or flagfall charge.

4.2 Network Management Principles and Early and Late Services

General Concerns with the Network Management Principles

As previously outlined by Asciano the Network Management Principles are constrained in their ability to manage the Hunter Valley coal network. The Network Management Principles are not designed for the sequencing requirements of coal trains delivering in sequence from coal mines to ports. Rather, the Network Management Principles are based on facilitating the efficient operation of a main line interstate network transport where on time running takes precedence over sequencing. Asciano is aware that the proposed Network Management Principles are contained in ARTC's lease of the Hunter Valley network from the NSW Government and that this lease does not make provision for the Network Management Principles to be altered.

Asciano appreciates that ARTC's Lease from the NSW Government does, to an extent, constrain network traffic priorities. Notwithstanding this Asciano believes there is scope for the provision of more suitable Network Management Principles than is being proposed by ARTC, and which can cater for the unique characteristics of export coal trains operating on the same network as other freight and passenger trains. Asciano recognise that ARTC has supplemented their proposed set of Network Management Principles with an additional set of guidelines to be applied when Coal Trains run out of course, although Asciano is unsure of the nature and status of these guidelines, and would seek that they be clarified in this regulatory process.

In any event, as previously proposed by Asciano, the preferred solution for any conflict in Network Management principles relating to passenger service priorities may be the amendment of the lease.

Asciano believes that it would be beneficial for ARTC, ACCC and operators to meet to discuss the Network Management Principles.

Early and Late Services

Of particular concern to Asciano is the impact of the Network management principles on the OSA and AHA clauses relating to early and late trains.

Clauses 3.6 and 3.8 of the OSA (and clause 3.9 of the IAHA) provide that a train must be ready for departure within 15 minutes of the nominated time.

Asciano believes that this emphasis on 'on time' running is inconsistent with the primary objective of the sequencing approach needed to manage coal trains delivering from mines to ports in sequence, and consequently these clauses should be reconsidered.

Asciano recognises that one of the main drivers of this requirement for 'on time running' is driven by ARTC requirements to meet non-coal train timetabling obligations and the Network Management Principles.

Asciano has raised this issue in discussions with the ARTC and believe that ARTC also recognise this as a potential issue.

At a minimum Asciano believe that the relevant clauses in the AHA and OSA should be amended to require that in the event of the time windows not being met for whatever reason that all parties use their best endeavours to implement a course of action to meet the over-arching goal of achieving delivery of trains from the mines to port in sequence. This amendment is not intended to result in any breach of the Network Management principles or result in early or on-time trains departing at later than their scheduled time.

Asciano believes a revision of the Network Management Principles may provide more scope for these clauses to be more extensively reviewed and amended.

4.3 Other Issues Previously Raised by Asciano Which Continue to be of Concern

Asciano raised numerous other concerns in both its June 2009 submission and March 2010 submission. Asciano's continuing concerns with elements of the ARTC proposal are outlined in this section.

4.3.1 Concerns with the Access Undertaking Previously Raised by Asciano Which Continue to be of Concern

Unreasonably Long Time Period to Provide an Indicative Access Proposal

Asciano is concerned that in the proposed HVAU there remains an unreasonably long time period, being sixty business days, to provide an Indicative Access Proposal. Asciano re-state their concern that, compared to the other major coal network provider in Australia, QR Network, which provides an indicative access proposal in 30 days, the time frame for ARTC to provide an Indicative Access Proposal is unreasonably prolonged.

Domestic User Coal Access Issues

Asciano welcomes the changes made to facilitate the transport of domestic coal, in particular removing certain provisions from the requirement of Tier 1 mandatory access holder agreement provisions in cases where the coal is intended for domestic use.

However as domestic coal access users are less able to trade paths as typically they each have unique destinations this creates issues with meeting take or pay provisions as trading paths is not an available option as there is no trading counterparty. Similarly domestic coal users may have different contracting time frames such that the ten year take or pay contract time frames envisaged for the Access Holder Agreements may not align with the commercial situations and time frames of domestic coal users.

Given the above Asciano is seeking that ARTC continue to be flexible when negotiating contracts to meet the needs of domestic coal users.

4.3.2 Concerns with the OSA and IAHA Previously Raised by Asciano Which Continue to be of Concern

While the issue of early and late services outlined in section 4.2 above is Asciano's major concern with the AHA and OSA, Asciano has numerous other concerns which it has previously raised as outlined below:

- OSA – the definition of solvent. Asciano believes two to three years rather than five years is an appropriate time frame to demonstrate solvency;
- OSA – 5.4 (b) – Asciano believes that the operator obligation to comply with the Code of Practice, should be amended to require that, to the extent practicable, ARTC consult with the Operator prior to amending the Code of Practice
- OSA – 5.4(n) – Asciano believes that this clause which relates to the potential spillage or leakage of freight carried by the Operator on to the Network should be subject to a “best endeavours” clause rather than an absolute obligation;
- OSA – 6.2 – Asciano believes that in the event a speed or weight restriction has a material impact on the operator there should be an obligation on ARTC to remove the restriction as soon as practicable.
- OSA 9.3 (c) - Asciano believes ARTC consultation with the Operator on network possessions should be on the broader long term network possession plan and not just the current possession;

Asciano believes these concerns should be addressed by the ACCC in the current process.