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Mr Matthew Schroder  
General Manager  
Fuel, Transport and Prices Oversight Branch  
Australian Competition and Consumer Commission  
GPO Box 520  
Melbourne Vic 3001

(By email: [transport@acc.gov.au](mailto:transport@acc.gov.au))

Dear Mr Schroder

**Final indicative Services Variation (ACCC Position Paper) - ARTC's Hunter Valley Rail Network Access Undertaking**

Idemitsu Australia Resources Pty Ltd (**Idemitsu**) welcomes the opportunity to provide the following submission in regard to the Position Paper issued 1 August 2014 by the Australian Competition and Consumer Commission (**ACCC**) in relation to Australian Rail Track Corporation's (**ARTC**) proposed variation to the Hunter Valley Rail Network Access Undertaking (**HVAU**).

Idemitsu is an active coal producer with mines located in both the Hunter Valley (Pricing Zone 1 – **PZ1**) and the Gunnedah Basin (Pricing Zone 3 – **PZ3**). Idemitsu is uniquely positioned to comment on this matter as it is the only producer in the Hunter Valley Coal Chain which currently has operating mines in both PZ1 and PZ3.

Idemitsu notes that the Position Paper expresses the ACCC's preliminary views on the application made by ARTC to vary the HVAU with respect to the Indicative Services and associated Access Charges (the **Variation**). Idemitsu has been an active participant in all consultations conducted by both the ACCC and ARTC with respect to the development of the Indicative Services.

As a PZ3 producer, Idemitsu's primary concern is the appropriateness, application and transparency of the differentiation factors and their weightings. Idemitsu, in its previous submissions has strongly advocated improved transparency around ARTC's pricing process, to improve the understanding of all stakeholders and promote efficient decision making with respect to rail and mine infrastructure. Idemitsu commends the ACCC for providing the detailed outline of ARTC's pricing methodology for the Indicative Service contained in Appendix A of the Position Paper.

Idemitsu notes the ACCC currently has three active consultations underway; 2013 Annual Compliance Assessment, Revenue Allocation and the Indicative Services. Although these have been treated separately they are all strongly linked. Some of the issues being raised by stakeholders go to the underpinning foundations of the HVAU. To make changes to these foundations mid-term of the HVAU is inappropriate, and, to the extent that material changes are proposed, it is inappropriate to consider amending an aspect of the HVAU in isolation, without revisiting related matters which form part of the 'package' of the HVAU. For example, Idemitsu may well have different views on the appropriateness of gtkm as a billing unit, in the event that revenue allocation practices are changed.

Should you have any queries regarding this submission or would like to discuss this matter further please do not hesitate to contact Mr Craig Forster (Ph +61 7-3222 5623)

Yours sincerely

A handwritten signature in black ink, appearing to read 'Lee Gordon', with a stylized, cursive script.

Lee Gordon  
General Manager Marketing & Logistics  
Idemitsu Australia Resources Pty Ltd

## Idemitsu Submission

# ARTC Hunter Valley Rail Access Undertaking – Final Indicative Service Variation

### 1. Introduction

Idemitsu is an active coal producer located in both the Hunter Valley (Pricing Zone 1 – **PZ1**) and the Gunnedah Basin (Pricing Zone 3 – **PZ3**) utilising the Hunter Valley Rail Network (**Network**) to haul coal from its load points to the port of Newcastle. Idemitsu is uniquely positioned to comment on this matter as it is the only producer in the Hunter Valley Coal Chain which currently has operating mines in both PZ1 and PZ3.

Idemitsu understands the Indicative Services are intended to indicate to Access Holders the train configurations for coal haulage that contribute to achieving the optimum utilisation of Coal Chain Capacity in the Network. In addition, the associated Access Charges are intended to provide pricing signals and incentives for the adoption of more efficient train configurations.

After industry consultation and Hunter Valley Coal Chain Coordinator (**HVCCC**) modelling, the ARTC has proposed a Variation in accordance with section 4.18 of the HVAU which is intended to take effect as of 1 January 2015, however the ACCC has advised it has not yet formed a view on the appropriateness of the Variation and provides its preliminary views in the Position Paper<sup>1</sup>.

The HVAU prescribes a multi-stage approach to the development of the Indicative Service and the Variation proposed by ARTC is the conclusion of this process. This approach is in recognition of the complexity of determining the optimal train configuration.

It is Idemitsu's view the Indicative Service will continue to evolve over time as capital investment is undertaken, innovations occur and new technologies are developed for above and below rail.

Idemitsu has expressed its views with respect to the development of the Indicative Services in numerous consultations, submissions and engagements with both the ACCC and ARTC. As previously outlined in its submissions, Idemitsu has concerns with respect to 82 wagon trains originating in PZ3 (Indicative Service 1) and travelling through PZ1 (as Indicative Service 2) with significant price differentiation being applied despite this service being the most efficient train configuration that can be operated from PZ3. Despite considerable investment by PZ3 Access Holders and the support of above and below service providers, PZ3 Access Holders are limited through rail infrastructure on the train configurations that can operate in PZ3 in the "near term" (next 5 years).

Traditionally, PZ3 Access Holders face numerous challenges with respect to rail infrastructure limitations which limit competitiveness and growth and lead to significantly higher rail transport costs than coal producers in PZ1 and PZ2. These include:

- longer haul distances;
- rail infrastructure restrictions (i.e. single track, axle load, banking requirements, aged infrastructure etc.); and
- limitation on rolling stock configurations (i.e. physically unable to use the proposed Final Indicative Service in PZ1).

Idemitsu notes a number of additional information requests were made by the ACCC to ARTC, in particular their financial modelling of Access Charges. It is Idemitsu's understanding that these additional information requests have enabled the ACCC to provide a detailed outline in Appendix A of the Position Paper; ARTC's pricing methodology for the Indicative Service. This has provided all Access Holders with a better understanding of the ARTC pricing methodology.

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<sup>1</sup> ACCC Position Paper, 1 August 2014, p8.

This submission provides Idemitsu's responses to the Position Paper and addresses the specific questions raised by the ACCC.

## 2. Process for determining the Indicative Service characteristics

The ACCC has acknowledged the ARTC consultation with industry stakeholders and the HVCCC "...were less adequate than others..."<sup>2</sup>, however the ACCC is of the view the ARTC consultation has complied with the requirements set out in the HVAU. Idemitsu supports any future consultation by ARTC with all stakeholders being conducted in a transparent and collaborative manner.

## 3. Proposed Indicative Service characteristics

The Indicative Service characteristics proposed by ARTC are based upon modelling conducted by the HVCCC. The HVCCC modelling considered three scenarios covering a variety of different axle loads and train lengths. The Indicative Services proposed per pricing zone are:

- (a) Indicative Service 1 (PZ1) – 96 wagon 30TAL
- (b) Indicative Service 2 (PZ1) – 82 wagon 30TAL
- (c) Indicative Service 1 (PZ2) – 96 wagon 30TAL
- (d) Indicative Service 1 (PZ3) – 82 wagon 30TAL

Some of the key underlying assumptions of the HVCCC modelling included:

- (a) the model ignored congestion;
- (b) any variation to axle load and length could fit on the infrastructure;
- (c) the model has been set up using the likely *near term* infrastructure; and
- (d) restricted shipping queue with an average of 20 vessels.

In conjunction with the above assumptions, the ARTC adopted Scenario 3 – the Gunnedah Basin network will move to the same axle load and train length configurations as the central and western Hunter Valley. ARTC acknowledged a number of limitations with respect to the HVCCC modelling in particular the cost to the coal chain in adopting test train configurations.

It is Idemitsu's view the assumption of the Gunnedah Basin producers moving to the 96 wagon 30TAL configuration in the *near term* is unrealistic and cost prohibitive given the requirements to develop infrastructure to accommodate longer trains. These requirements include a cost effective solution to the Liverpool Range, all network loops in PZ3 would need to be extended an additional 200-300 metres and potential upgrades to existing load points (all of which are longer term investments). On this basis Idemitsu questions the efficiency of such investment and the capability of the model to assist in efficient infrastructure decisions. Rather than incurring significant capital expenditure in PZ3 it may be more efficient to develop infrastructure in PZ1. The consideration of efficient costs aligns with the objects of Part IIIA of the Competition and Consumer Act 2010 (section 44A).

To the extent that the FIS is intended to provide a price signal to PZ3 users (to move to 96 wagon trains), the price signal is most likely inappropriate, as, if it was effective, it would incentivise investment in PZ3 infrastructure which is likely to be imprudent (or at least, has not been modelled to establish its prudence). As a pricing signal, Idemitsu considers that the higher Access Charges applied to 82 wagon trains will be:

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<sup>2</sup> ACCC Position Paper, 1 August 2014, p21.

- unnecessary, as ARTC, above rail haulage operators and PZ3 coal producers have been investing to ensure efficient use of infrastructure consistently since the establishment of PZ3 mines, without the need for an incentive through Access Charges; and
- ineffective, as the feasibility of any decision to move to longer trains in PZ3 will be driven primarily by capacity considerations, below rail investment costs and above rail cost impacts, rather than by the potential to reduce the Access Charges in PZ1.

Idemitsu notes that the FIS has been developed based on modelling which has significant limitations, including:

- (a) not reliably modelling outputs greater than the current contracted capacity of 208 Mtpa;
- (b) not reliably modelling the effects of Advanced Train Management Systems allowing increased capacity; and
- (c) assuming the system operates with only one train type configuration, so that the modelling does not provide an accurate representation of the interaction of multiple train configurations and how system throughput might vary accordingly<sup>3</sup> (this is inevitable given the age of some rolling stock and the commercial arrangements with above rail haulage providers).

The adoption of the modelling results from Scenario 3 have been used by ARTC in determining the Indicative Services, however the ACCC acknowledges that the differences in the modelling results between Scenario 2 and Scenario 3 do not appear to be material<sup>4</sup>. Furthermore, the ACCC notes Scenario 3 assumptions appear to be inconsistent with the general assumptions of likely *near term* infrastructure investment. It is Idemitsu's view the application and results of Scenario 2 are more appropriate for the purposes of determining the Indicative Services and ultimately the calculation of Coal Chain Capacity as a differentiation factor.

In summary, Idemitsu considers the train characteristics of the proposed Indicative Services do reflect the most efficient train configurations that can operate on the Network given current infrastructure constraints in the near term, but disagrees with the magnitude of (and purpose of) the price differentiation of Indicative Service 2 in PZ1.

#### 4. Proposed Access Charges for the Indicative Services

Idemitsu acknowledges ARTC's view that as long as there is appropriate price differentiation to encourage efficient utilisation of the Network the pricing unit is immaterial, however it is the magnitude of this differentiation in PZ1 for services originating in PZ3 which is of concern for Idemitsu.

The ACCC has expressed its preliminary view that ARTC's proposed structure of Access Charges between the Non-TOP and TOP components as outlined in Box 5.1 of the Position Paper is appropriate.

#### ***Do stakeholders have any comment on the train configurations and assumptions used by ARTC in its calculation of the differentiation factors relating to variable maintenance in the Non-TOP component of the charges?***

Idemitsu considers the approach taken by ARTC in its calculation of the differentiation factors for the Non-TOP component (variable maintenance) of the Access Charges to be reasonable. However, despite the information provided by ARTC to the ACCC in Appendix A (Table 11) it still remains unclear to Idemitsu why there is a differentiation factor of greater than one. Table 11 provides the relevant data used to calculate the variable maintenance differentiation from ARTC's confidential pricing model. There appears to be unexplained differences between the characteristics of

<sup>3</sup> Aurizon submission, 21 March

<sup>4</sup> ACCC Position Paper, 1 August 2014, p29.

Indicative Service 1 and Indicative Service 2 in PZ1, i.e. wagon tare, average axle load (loaded) and average axle load (empty). Idemitsu would have expected the characteristics to be the same for the *near term* as most above rail haulage providers are seeking to standardise their rollingstock for operational and cost efficiency and the only differential should be train length. Furthermore, it is Idemitsu's understanding that most of the wagons are interchangeable between Indicative Service 1 and Indicative Service 2.

***Do stakeholders have any comments on the train configuration and assumptions used by ARTC in its calculation of the differentiation factors relating to fixed maintenance in the TOP component of the charges?***

Idemitsu considers the approach taken by ARTC in its calculation of the fixed maintenance as a differentiation factor for the TOP of the Access Charges to be reasonable based upon the additional information provided in Appendix A of the Position Paper. The slight issue is the difference in wagon tare in Table 12 of Appendix A between Indicative Service 1 and Indicative Service 2 in PZ1.

***Do stakeholders have any comment on the assumptions used by ARTC in its calculation of the differentiation factors relating to Network Capacity in the TOP component of the charges?***

ARTC has proposed that the consumption of Network Capacity is driven by the average speed of a train and by its maximum length. Idemitsu notes that:

- PZ3 Access Holders have a train length imposed upon them due to infrastructure limitations and
- PZ3 Access Holders have the capability of operating at higher speeds throughout the Network, but are restricted by the slower 96 wagon trains operating in PZ1.

However, ARTC has identified there appears little basis for differentiation on train lengths having regard to infrastructure constraints up until the expiry of the HVAU and all train configurations not exceeding crossing loops. In relation to speed, ARTC acknowledge differentiation is difficult due to the limitations of modelling to accurately estimate<sup>5</sup>, despite the elevated speed capability of the 82 wagon trains (in PZ1).

As a result of the proposed approach by ARTC train length and speed are not considered differentiation factors with respect to Network Capacity, Idemitsu considers it reasonable to assume all train configurations regardless of size consume a single path. Subsequently, ARTC apply a conversion factor to convert from a price per path to a price per gross tonne kilometre (gtkm) which again appears reasonable.

***Do stakeholders have any comment on the methodology used by ARTC in its calculation of the differentiation factors relating to Coal Chain Capacity in the TOP component of the charges?***

***Do stakeholders have any comment on the use of the HVCCC modelling in the calculation of the differentiation factor relating to Coal Chain Capacity for the TOP component of the charges?***

ARTC has proposed that the most appropriate basis for comparing and differentiating Coal Chain Capacity is tonnes delivered to the terminals and that tonnes carried on the Indicative Service would consume the least Coal chain Capacity. ARTC also note Coal Chain is measured as whole of Coal Chain and therefore there is little justification in differentiation between pricing zones.

Idemitsu has a number of concerns with this differentiation factor and the application by ARTC.

Firstly, the HVCCC modelling uses the underpinning assumption of Scenario 3; Gunnedah Basin Access Holders will move to the same axle load and train length configurations as PZ1 and PZ2. This assumption specifically excludes the renowned PZ3 rail infrastructure limitations and does not

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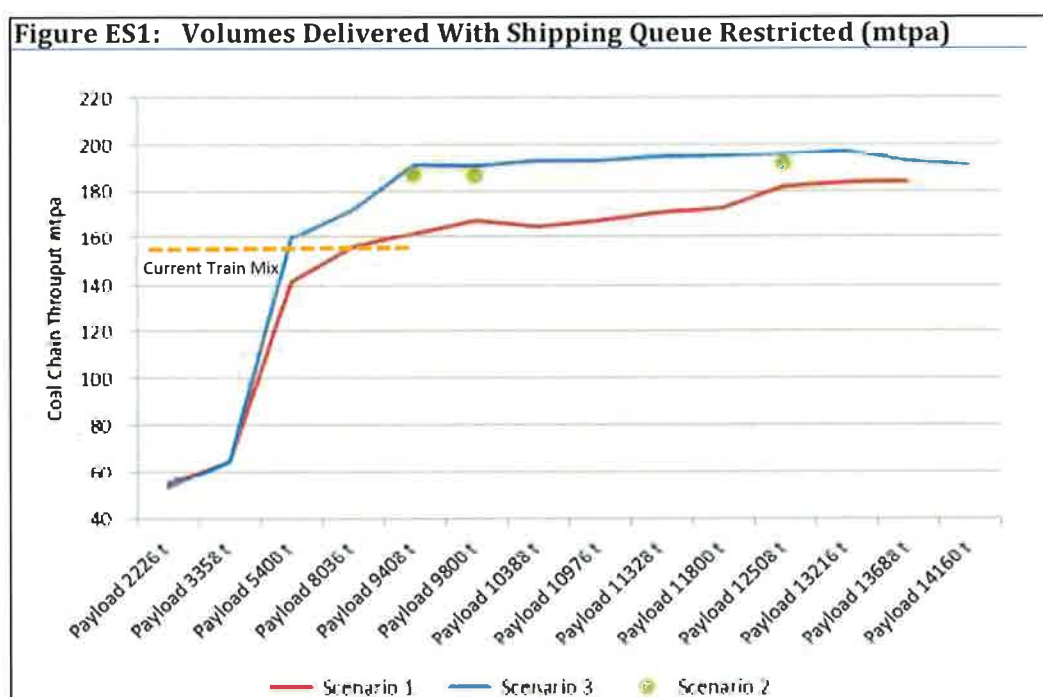
<sup>5</sup> ACCC Position Paper, 1 August 2014, p42.

consider the concept of *near term* as the time basis for much of the Indicative Service discussion and creates an unrealistic and aspirational coal chain capacity of 191.2 Mtpa.

Idemitsu considers Scenario 2 is more appropriate in the *near term* for calculating the differentiation factor for Coal Chain Capacity. Scenario 2 assumes Gunnedah Basin Access Holders will move to 30TAL in the *near term*, which is happening currently. This scenario is expected to produce a whole of coal chain capacity of 187.6 Mtpa (based upon information provided by the HVCCC).

The following graph from the ARTC consultation document<sup>6</sup> demonstrates there is only a minimal difference in coal chain throughput between Scenario 2 (green dots) and Scenario 3 (blue line), with *near term* investment, Scenario 2 is clearly the most optimal and efficient scenario in providing coal chain capacity.

Furthermore, this graph emphasises the investment to upgrade from 25TAL to 30 TAL currently being made by PZ3 Access Holders when compared to Scenario 1 (red line) is providing an increase to coal chain capacity for the benefit of all Access Holders.



Secondly, the additional information provided by the ACCC in Appendix A provides an overview of the ARTC methodology when calculating the Coal Chain Capacity differentiation factor:

$$\frac{\text{Coal Chain Capacity}_{\text{Service X}}}{\text{Coal Chain Capacity}_{\text{Indicative Service 1}}} \quad \text{Based on HVCCC modelling } 172 \text{ Mtpa}/191 \text{ Mtpa} = 0.900$$

Idemitsu does not consider this approach appropriate when considering the *near term* capabilities of the Network and the inability of the rail infrastructure to allow PZ3 Access Holders to operate longer, 96 wagon trains. Therefore, Idemitsu propose a more appropriate determination of the Coal Chain Capacity differentiation factor is to change the numerator in the above equation to the Coal Chain Capacity throughput as calculated by the HVCCC under Scenario 2 (first green dot). This would mean the revised Coal Chain Capacity differentiation factor would be:

$$188 \text{ Mtpa}/191 \text{ Mtpa} = 0.9843$$

<sup>6</sup> ARTC, Variation to the HVAU Final Indicative Service (s 4.18(B)), Support Documentation, January 2014, p5.

Thirdly, the ACCC has raised a valid concern with respect to the modelling of Coal Chain Capacity and the consideration given to axle load, train length and payload. These characteristics are also considered in the differentiation factors for Maintenance and Network Capacity thus giving rise to potential “overlaps” between the differentiation factors. The ACCC have suggested these overlaps should be addressed in the appropriateness of the weightings.

***Do stakeholders have any further comment on the weightings applied to the differentiation factors by ARTC in its calculation of the TOP component of charges in light of the additional information presented in this Position Paper?***

The weightings applied to the differentiation factors have been a contentious issue throughout the Indicative Services process, with stakeholders having opposing views and ARTC providing only limited supporting material. In particular, the current equal weighting applied to Network Capacity and Coal Chain Capacity remains contentious.

The argument for a high weighting on Network Capacity rather than Coal Chain Capacity has been predicated on the Network being the most significant limitation in the coal chain, however it is Idemitsu’s view that this may no longer be the case given the number of capacity projects that have been delivered in recent years and their benefits most certainly being realised. Idemitsu considers that Coal Chain Capacity ought to provide a measure which fully reflects all of the impacts of differences in train types. Combining this measure which is based on all elements of the chain with a Network Capacity element must double-count the Network Capacity element. Idemitsu considers that a 50% weighting for the Network Capacity element is too high, and therefore we strongly disagree with any suggestions that it should be increased.

***What further information, if any, do stakeholders consider will provide the appropriate level of transparency regarding the basis upon which ARTC differentiates charges for services other than the Indicative Services?***

Transparency of the pricing methodology and process has been a major concern for Idemitsu since the inception of the HVAU. The information provided in Appendix A has provided Idemitsu with an improved understanding with respect to the differentiation factors and the weightings applied. Idemitsu would request this transparency to continue.

Idemitsu would welcome increased detailed transparency in regards to maintenance, overheads and overall economic costs budgets used by ARTC when establishing annual pricing. Idemitsu acknowledges ARTC discloses aggregate amounts for these items, however greater detail will provide a better understanding for all Access Holders.