

S T R A T E G I E S

26 April 2001

Margaret Arblaster
General Manager – Transport
Regulatory Affairs Division
ACCC
GPO Box 520J
Melbourne VIC 3001

Dear Ms Arblaster

Re:- ARTC Access Undertaking

PTM Strategies is a small consulting firm, providing consulting services to the rail industry.

There are two principals – Peter Mason and Laurel Black. Both have been involved in rail access from the very first application of the Competition Principles Agreement and open access in Australia. In fact, both negotiated the first rail access contract signed under the regime. Both have maintained a continuing active interest in promoting rail open access since that time.

The purpose of this letter is to respond to the ACCC's request for comments on the ARTC Access Undertaking.

Our submission is that the ARTC undertaking should not be accepted with the use of DORC as the asset base on which ceiling prices are determined. The asset base should be the actual investment, depreciated over the life of each asset).

We have not undertaken a detailed and comprehensive review of the undertaking. However, we do wish to draw the Commission's attention to that one single aspect. This aspect has wider ramification than just the ARTC Undertaking. By addressing this issue now, the Commission achieves a secondary benefit of guiding the overall development of open access in Australia.

The Competition Principles Agreement provides for access considerations to include consideration of "the provider's investment in the facility". This requirement (with exactly the same wording) is carried through into the issues that the Commission must take into account in making a determination for access to a declared service - s44X.

There is no specific similar obligation on the Commission in assessing whether to accept an undertaking or not. However, there is a general provision allowing the Commission to include "any other matters that the Commission thinks are relevant" – s44ZZA(3)(c)(c).

S T R A T E G I E S

It would seem inconsistent if the Commission were not to consider that the Competition Principles Agreement requirements were appropriate in determining the price for access by the undertaking route. It would seem inconsistent if the Commission were to consider that the owner's investment in the facility was not relevant in determining fair access prices in an undertaking. It would also seem inconsistent if the Commission were to take the quantum of the owner's investment into account in settling in a dispute but that a different approach (a hypothetical valuation) would be allowed for an owner to set different maximum access charges through the undertaking route.

Accordingly, "the owner's investment in the facility" is one of the issues that the Commission needs to consider in assessing the ARTC undertaking.

The undertaking proposes to use the Depreciated Optimised Replacement Cost (DORC) in determining the asset base on which a return should be allowed.

The principal point in our submission is that the use of DORC is not consistent with and is not "the provider's investment in the facility".

The asset base on which a return should be based should be the **actual** owner's investment in the facility. Such actual investment needs to be depreciated over the life of the asset and that depreciation allowed as an expense.

There are many ways of valuing an asset. DORC is only one. But all are a valuation as at today. They are not the cost of the asset. They are not the investment in the asset.

Accordingly, the maximum price allowed to be charged by the ARTC in its undertaking should be based on the **actual** investment made by the ARTC (and its predecessors?)

Although not strictly applicable to the ARTC undertaking, the problems and "unfairness" from the use of DORC (or the similar present-day valuation methodologies) can best be seen from the present state of "privatisations" of rail tracks.

In general, the purchase price (or its equivalent in leasing terms) has been around \$10,000 to \$20,000 per km of track. The replacement value is generally of the order of \$1.0 to \$1.5 million per km of track. It is generally reasonable to consider that the track is half-way through its life.

Thus the asset base on a DORC basis would be some \$500,000 to \$750,000 per km of track. This, in turn, would imply an allowable return in excess of \$50,000 pa per km of track. ie well in excess of the total price paid for the track.

The end result is that the use of DORC effectively prevents open access and prevents competition.

S T R A T E G I E S

In the case of the ARTC, the use of DORC in the undertaking, allows for maximum prices that provide an excessive returns on the actual investment in the track. It also provides a mechanism for a possible future owner of the track (if the ARTC were to be privatised) to block competition. It could be argued that the present ARTC would have no interest in blocking access as it has no above-rail operations that compete with its customers. This may be so today but it may not be so tomorrow.

The ARTC has not undertaken that it will never have any association with above-rail activities; it has not undertaken that its Constitution will not be amended in the future to allow for above-rail activities; and the Government has flagged in the past that sale of the ARTC in the future is a possibility.

For the Commission to address this issue now would do two things.

It would specifically assess the issue as it applies to the ARTC undertaking.

It would flag to the industry at large, how the Commission would assess the words "the provider's investment in the facility".

The latter, in particular, would be of strong guidance to the industry in the present application of open access, where Part IIIA of the Trade Practices Act provides the umbrella under which access is negotiated, there being no state regimes presently in operation, which have been determined by the National Competition Council as "effective".

For your consideration.

Peter Mason
Managing Director