

# **Pacific National Submission to the ACCC in Relation to the ARTC's Proposed Variation to the 2011 HVAU**

February 2018

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# 1. Introduction

Pacific National welcomes the opportunity to make this submission to the Australian Competition and Consumer Commission's (ACCC) January 2018 Consultation Paper relating to the Australian Rail Track Corporation's (ARTC) proposed variation to the 2011 Hunter Valley Access Undertaking (HVAU).

Pacific National is a major operator of coal trains in the Hunter Valley coal rail network. Pacific National does not currently hold coal haulage rail access rights<sup>1</sup> or pay coal haulage access charges in the Hunter Valley coal rail network, however Pacific National recognises that rail access regulation and rail access pricing provide strong incentives to access holders (and hence to operators) as to how train operations should be managed on the Hunter Valley network. Thus Pacific National has a strong interest in ensuring effective access regulation and access pricing in order to ensure efficient train operations in the Hunter Valley network. In particular Pacific National strongly supports access regulation and pricing which encourages more efficient consumption of capacity in the Hunter Valley coal rail network, which in turn allows more coal to be moved through the network.

Pacific National has made previous submissions to the ACCC<sup>2</sup> in relation to the access pricing structures that apply in the Hunter Valley coal rail network. These submissions have consistently supported access pricing structures which support larger and more efficient trains. This submission continues to support this Pacific National position and generally supports the 2011 HVAU variations proposed by ARTC, although Pacific National has some concerns regarding details of the proposed variations.

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<sup>1</sup> Pacific National holds access rights through the Hunter Valley rail system for non-coal trains and access rights for ancillary train services (for example wagon movements) which serve the coal industry but which do not haul coal.

<sup>2</sup> Note that when the submissions listed below were prepared Pacific National was part of the Asciano group. The submissions include

- Asciano, November 2011, Submission to the ARTC: 2011 Hunter Valley Access Undertaking – Response to the Initial Indicative Service Proposal
- Asciano, January 2012, Submission to the ACCC in relation to the ACCC Consultation Paper on the ARTC Hunter Valley Access Undertaking Variation
- Asciano, May 2012, Submission to the ACCC in relation to the ACCC Position Paper on the ARTC Hunter Valley Access Undertaking Variation
- Asciano, August 2012, Asciano Submission to ACCC Further Consultation on the ARTC Proposal to Defer Implementation of Initial Indicative Access Charges
- Asciano, September 2012, Asciano Submission to ACCC Consultation on the ARTC Revised Application to vary the Hunter Valley Access Undertaking
- Asciano, March 2014, Submission to the ACCC: Response to ACCC Consultation Paper Regarding the Proposed Final Indicative Service Variation to the ARTC Hunter Valley Access Undertaking
- Asciano, September 2014, Submission to the ACCC: Response to the ACCC Position Paper Regarding the Final Indicative Service Variation to the ARTC Hunter Valley Access Undertaking
- Asciano, March 2016, Submission to the ACCC 206 ARTC Hunter Valley Coal Network Access Undertaking

Pacific National notes that the Consultation Paper contains thirty three explicit questions. Pacific National's responses to some of these questions are in Attachment 1 to this submission.

This submission is public.

## 2. ARTC's Proposed Variation to the 2011 HVAU

Pacific National understands that ARTC's proposed variation to the 2011 HVAU has been submitted to meet the ACCC's requirement in the June 2017 variation to the HVAU that ARTC submit variations which incorporate path based pricing and apply certain incremental cost methodologies including:

- requiring that Pricing Zone 3 users contribute incremental costs for Pricing Zone 1;
- requiring that certain cost categories be allocated on the basis of certain cost allocators; and
- the application of a dual ceiling limit (where this is a mechanism to provide a level of certainty on the contribution of Pricing Zone 3 access holders to the costs of pricing Zone 1).

Following the ACCC's requirements (as outlined above) ARTC has submitted proposed variations to the 2011 HVAU to amend the rail access pricing structure to operate as follows:

- Take or Pay Price Component 1 – based on contracted train kilometres (currently based on contracted GTKs);
- Take or Pay Price Component 2 – based on incremental capital costs in Pricing Zone 1 (currently incremental capital costs in Pricing Zone 1 are a non-Take or Pay price component); and
- Non-Take or Pay Price Component – based on actual GTKs (currently based on actual GTKs).

Pacific National understands that the proposed 2011 HVAU pricing structure will apply to all train configurations and will not explicitly differentiate between configurations.

Pacific National believes that the ARTC's proposed variations generally meet the requirements of the ACCC.

### 3. Pacific National's Position on the ARTC's Proposed Variation to the 2011 HVAU

Currently rail access pricing is based on an indicative-service access pricing structure where both take-or-pay and non-take-or-pay access charges are based on GTKs for a defined indicative-service (where various indicative-service train configurations each have their own pricing structure based on GTK). This approach does not encourage larger trains to the extent that the proposed price variations will encourage larger trains and so the current pricing approach does not result in the most efficient utilisation of the Hunter Valley coal rail network.

Under the proposed variations to the 2011 HVAU the ARTC is now moving towards a path based pricing model (where train configurations are not relevant and a component of access pricing is based on train kilometres rather than GTKs). This approach can act to incentivise larger trains as the dollar per kilometre pricing unit is essentially fixed and so if this fixed charge can be spread over a larger tonnage of coal then the access holder has a financial incentive to move to a higher payload train (as the access cost per tonne will decrease). Thus the proposed variation of the HVAU access pricing approach provides stronger incentives for efficient utilisation of capacity than the current access pricing approach.

Pacific National strongly supports this ARTC move towards a rail access pricing structure with a component of access pricing based on train kilometres rather than having access pricing solely based on GTKs. The proposed variation of the HVAU access pricing approach is an improvement on the current access pricing approach.

The current indicative-service model has been subject to extensive consultation and analysis since 2011. Pacific National has consistently put forward the position that longer and higher payload trains configured with sufficient power to operate within system assumptions are the most efficient trains for the Hunter Valley coal supply chain. Pacific National continues to strongly hold this view and believes that the Hunter Valley coal supply chain is best served by providing access pricing incentives for longer and higher payload trains. The proposed ARTC access price structure variations now provides improved incentives for the operation of longer and higher payload trains within the services envelope.

With the planned introduction of path based pricing Pacific National is actively investigating both:

- longer trains that will provide additional customer value by reducing the access cost per tonne of coal. The access cost now has a larger fixed component and so increasing the train size spreads the fixed access component over a greater volume of coal; and
- new wagon designs that will provide additional customer value by reducing the access cost per tonne of coal. The access cost now has a larger fixed component and so changing the wagon design to increase wagon capacity spreads the fixed access component over a greater volume of coal.

These projects, which will increase the volumes of coal moving through the Hunter Valley supply chain are being driven by the move towards path based pricing.

Pacific National strongly supports the move towards path based pricing as it provides incentives for the operation of larger and more efficient trains and incentives for innovation in both train design and operation.

Pacific National notes that the services envelope being introduced as part of the proposed HVAU variations may act to limit the incentives for the operation of larger and more efficient trains. Pacific National believes that further incentives for efficiency could be obtained if the services envelope was not limited to a train length but instead the services envelope stated that the length was whatever was operationally approved. This would allow operators to investigate longer trains while recognising that there are operational limits to these trains operating on the network.

## 4. Pacific National's Concerns with Detail with the ARTC's Proposed Variation to the 2011 HVAU

While Pacific National strongly supports the ARTC's proposed variations Pacific National has concerns with several aspects of the ARTC proposal as outlined below.

Restrictions Imposed by Adjoining Networks: Some coal train operations in the Hunter Valley are restricted due to the limitations of adjoining rail networks, including the Sydney Trains network. This means that coal trains which enter the adjoining networks usually have to be smaller than trains using the Hunter valley coal rail network due to the physical limitations of these adjoining networks.

Pacific National recognises that ARTC are aware that the proposed change in the Hunter valley access pricing structure impacts on users who use adjoining networks as well as the Hunter Valley coal network. ARTC argue that the impact has been mitigated by having a portion of the take-or-pay component being levied on a GTK basis. In addition ARTC in section 4.15 of the HVAU sets

out in broad terms factors that will be taken into account when determining the access charges for coal train services outside the train services envelope.

While Pacific National acknowledges this ARTC position, Pacific National believes that until the detailed access pricing is made available the extent of this price mitigation on these users cannot be identified.

Pacific National believes that it is inequitable that users of the Hunter Valley coal network that also use the Sydney Trains network are disadvantaged by the limitations of the Sydney Trains network that are not within the users control. To address this matter Pacific National believes that before approving the proposed variation the ACCC should consider the infrastructure constraints of adjoining networks and consider providing some access price relief when pricing the access rights for trains which use these adjoining networks (on the condition that the trains are efficiently sized for the infrastructure constraints of the adjoining network). If permanent price relief is not possible then Pacific National believes that a pricing glide path over the remaining term of the HVAU should be considered in order to dampen any initial access price differential between current access prices and future access prices.

Pacific National recognises that such an approach will lead to an additional level of complexity but believes that this complexity may be necessary in order to address this matter. Pacific National believes that when the detailed access pricing is made available it will facilitate resolution of this matter as the size and scope of the pricing impact will be known.

Services Envelope: The services envelope is the set of parameters which a train configuration must satisfy. Any trains within these parameters will be charged the proposed access charges. Pacific National has some concerns regarding the services envelope:

- Need for an Access Undertaking Amendment to the Services Envelope May Delay Innovation: Establishing the services envelope for train configurations and train performance may act as a disincentive for train operators to trial and adopt improved and more efficient forms of rolling stock and train configurations. While the envelope can be amended via an HVAU variation this additional administrative process may act to delay or deter the implementation of improved rolling stock.

Pacific National believes that further incentives for innovation could be obtained if the services envelope did not limit certain set parameters (such as train length) but instead the services envelope stated that the parameters are whatever was operationally approved.

This would allow operators to innovate while recognising that there are operational limits to these trains operating on the network.

- Speed Parameters: the services envelope includes speed parameters being maximum speed when empty and maximum speed when full. Pacific National believes that some form of lower limit of maximum speed capability should be included to remove the potential for any grossly inefficient usage of paths. Pacific National recognises that the requirement that a train service must meet the Sectional Run Times is a de facto speed requirement, but the requirement to run at a certain lower limit of maximum speed should be definitive.
- Sectional Run Times: The services envelope includes Sectional Run Times but these times are not contained in the proposed variation but are published on the ARTC website from time to time. Pacific National is concerned that changes to the sectional run times may impact the services envelope yet they will not be subject to the same level of scrutiny as the HVAU. Pacific National believes that if the sectional run times are to be substantially changed there should be consultation with stakeholders on this issue and the ACCC should be informed.

Non-coal Access: Pacific National notes that non-coal trains use the Hunter Valley rail infrastructure and Pacific National seeks that the 2011 HVAU will continue to facilitate these non-coal operations. In particular Pacific National seeks that the pricing for non-coal access rights remains consistent with the pricing structure and levels which apply for the ARTC interstate network (that is, that the proposed variations to the 2011 HVAU will not apply to non-coal trains). Such an approach ensures pricing consistency and removes the potential for pricing anomalies.

Pacific National recognises that ARTC are aware of this matter and appreciates ARTC's support in ensuring that pricing consistency across the ARTC interstate and Hunter Valley networks applies to non-coal trains which utilise the Hunter Valley network.

Deletion of Indicative Access Holder Agreement Clause: The Indicative Access Holder Agreement has been amended by the removal of clause 11.5 d). This clause previously provided protection from Take or Pay charges if an access holder shifted towards a service which provided for more efficient use of rail capacity such that the access holder used fewer paths. Pacific National sees no strong reason for this clause to be removed.

The removal of this protection reduces the incentive for train operators to adopt more efficient forms of rolling stock and train configurations. Pacific National believes the clause should be reinstated or a similar clause inserted.

## 5. Conclusion

Pacific National strongly supports the ARTC's proposed variations to the 2011 HVAU and the move towards an access pricing model based on both train kilometres and GTK rather than having access pricing solely based on GTKs. The proposed variations will act to incentivise more efficient trains in the Hunter valley coal rail network.

Pacific National has consistently put forward a position that longer and higher payload trains configured with sufficient power to operate within system assumptions are the most efficient trains for the Hunter Valley coal supply chain. ARTC's proposed access price structure will now provide improved incentives for the operation of longer and higher payload trains within the services envelope.

While Pacific National strongly supports the ARTC's proposed variations to the 2011 HVAU Pacific National believes that several improvements (as outlined in section 4 of this submission) may be made to the ARTC's proposed variations which will further increase incentives for the introduction of more efficient trains.

# Attachment 1 – Pacific National Response to the Questions in the ACCC Issues Paper

Pacific National notes that the Consultation Paper includes thirty three explicit questions regarding the ARTC's proposed variations to the 2011 HVAU. Pacific National's responses to these ACCC questions are shown below

*Question 1. If accepted, is it clear when the variation would come into effect?*

*Question 2. Is the proposed approach to backdating the Proposed Variation for the purposes of Annual Compliance for 2018 appropriate?*

*Question 3. Are there any concerns about applying the Proposed Variation for the purposes of Annual Compliance starting from the 2019 compliance period?*

Pacific National has elected to address the Questions 1, 2 and 3 in a single response as below.

Pacific National believes that it is clear that the variation comes into effect on the first day of the month which is three months after the approval date. Pacific National believes that for the avoidance of doubt this date should be confirmed in the ACCC's approval documentation.

Given that a single compliance model should apply for the entire compliance period Pacific National has no major concerns with compliance arising from the proposed variation being either backdated to January 2018 or applying from January 2019. Pacific National's concern is that if the regulatory process is delayed to the point that the variation is not in effect by January 2019 then consideration should be given to basing the annual compliance for 2018 on the current HVAU rather than the proposed variation to the HVAU.

Pacific National also recognises that access holders may have concerns regarding the need for making provision for the backdated variation.

*Question 4. Are the definitions of Variable Maintenance Costs, Incremental Capital Costs and Fixed Costs clear?*

*Question 5. Is the approach for allocating costs to Variable Maintenance Costs, Incremental Capital Costs and Fixed Costs appropriate?*

*Question 6. Is it clear how Fixed Costs will be allocated to Access Holders?*

*Question 7. Is the use of Contracted Coal GTK or Train Km rather than actual GTK or Train Km commitments appropriate as the method of allocating Incremental Capital Costs to Access Holders?*

Pacific National has elected to not to address these Questions 4, 5, 6, and 7 in detail.

Question 8. *Given section 4.5(h) of the Proposed Variation, is it appropriate these costs are excluded from the Economic Cost of a Segment?*

Question 9. *In addition to that set out in section 4.5(h) of the Proposed Variation, should any other costs be excluded from the Economic Cost of a Segment?*

Pacific National has elected to address Questions 8 and 9 in a single response as below.

Section 4.5 h) states that the following costs are excluded when determining the cost of a segment:

- Variable maintenance costs attributable to access holders that do not hold coal access costs (i.e. variable costs attributable to non-coal traffic);
- Variable maintenance costs attributable to access holders that hold coal access rights but who are not constrained coal customers; and
- In pricing zone 1, incremental capital costs imposed by pricing zone 3 access holders.

In relation to these exclusions Pacific National will only comment on the first exclusion. Pacific National holds non-coal access rights in the Hunter Valley and has no issue with the variable maintenance costs associated with these rights being excluded from the coal access pricing approach. Pacific National's main concern is that the separate regulatory processes applying to coal access costs and non-coal access costs do not double count these costs.

Question 10. *Is the definition of the Floor Contribution clear?*

Question 11. *Is it appropriate that the Floor Contribution for Pricing Zone 3 producers traversing Pricing Zone 3 is equal to the Variable Maintenance Cost of those segments?*

Question 12. *Is it appropriate that Pricing Zone 3 Access Holders traversing Pricing Zone 1 meet their Variable Maintenance Costs and Incremental Capital Costs?*

Question 13. *Is the introduction of two Constrained Networks appropriate?*

Question 14. *Is the rationale and purpose for creating two Ceiling Limits for two Constrained Networks clear?*

Question 15. *Is it clear how the two Ceiling Limits will practically operate?*

Question 16. *Is it appropriate to determine the Ceiling Limits on a Train Path basis?*

Question 17. *Are there any concerns relating to RCG endorsement of a capital cost where RCG approves of the capital cost but does not agree with ARTC's proportions and allocation methods for Incremental Capital Costs?*

Question 18. *Is the distinction between section 9.2(a) (ii) and section 9.2(a) (iii) on proportions and allocation methods for Incremental Capital Costs and Fixed Costs and the role of ARTC and RCG clear?*

Question 19. *Is the role of the ACCC for assessing decisions relating to the proportion and allocation methods for Project costs or other Capital Expenditure clear?*

Question 20. *Is the proposed basis for TOP and non-TOP Charges appropriate?*

Pacific National has elected to not to address these Questions 10, 11, 12, 13, 14, 15,16, 17, 18, 19 and 20 in detail.

Question 21. *Does the proposed structure of charges provide sufficient incentive for the efficient use of the Network?*

Pacific National believes that the proposed structure of charges provides incentives for the efficient use of the network but it needs to be realised that rollingstock and locomotives are assets with relatively long lives and as such gains arising from increasingly efficient use of the network may take some time to be realised.

Question 22. *Does Train Km reflect how Fixed Costs are incurred?*

Question 23. *Does GTK reflect how Incremental Maintenance Costs and Incremental Capital Costs are incurred?*

Question 24. *Is it clear which activities are considered to be:*

- a. Incremental Capital Costs?*
- b. Variable Maintenance Costs?*
- c. Fixed Costs?*

Pacific National has elected to not to address these Questions 22, 23 and 24.

Question 25. *Are the proposed configurations in the Services Envelope appropriate?*

The proposed configurations in the services envelope are generally appropriate, although Pacific National has made some comments on the services envelope in the body of this submission. Pacific National believes that the services envelope parameters may need to be reconsidered as new rolling stock is introduced into the Hunter Valley.

Pacific National queries the need for an upper limit “maximum empty speed” in the services envelope characteristics. Pacific National believes that a lower limit for maximum empty speed capability is more relevant to a services envelope than maximum speed.

Question 26. *Is the introduction of the Services Envelope dependent on a portion of TOP Charges being levied on a Train Km basis?*

Pacific National has elected to not to address this Questions 26

Question 27. *Is the proposed approach to determining Access Charges for coal customers whose train configuration falls outside of the Services Envelope appropriate?*

The approach to determining Access Charges for coal customers whose train configuration falls outside of the Services Envelope appropriate in section 4.15 of the proposed HVAU remains broadly similar to the current approach.

As outlined in the body of the submission Pacific National continues to have concerns about the access pricing for coal train services where the train configuration is constrained by infrastructure constraints on adjoining rail networks.

Question 28. *Are the proposed changes to the basis for determining RCG membership and voting entitlements appropriate?*

Pacific National does not support the change in 9.2 e) of the HVAU. This change requires that where an access holder is an operator then operator must vote in accordance with the wishes of its customer. Pacific National believes that if an operator is an access holder then it should have the rights, including the voting rights of an access holder. The relationship between an access holder who is an operator and their coal customer is a matter for the parties involved rather than the HVAU.

Question 29. *What would be the effect of changing the basis of determining RCG membership and voting entitlements from contracted GTK to Contracted Coal KM?*

Question 30. *Is the proposed change to the basis for RCG endorsement thresholds appropriate?*

Question 31. *What would be the effect of changing the basis for RCG endorsement thresholds from contracted GTK to Contracted Coal KM?*

Pacific National has elected to address Questions 29, 30 and 31 in a single response.

Pacific National believes that answering these questions is problematic without information on both contracted GTK and contracted coal kilometres but it would seem that in the absence of this

information that Pricing Zone 3 access holders may potentially benefit from this approach on matters relating to Pricing Zone1.

*Question 32. Are there any concerns with any other changes in the Proposed Variation that have not been addressed in this consultation paper?*

*Question 33. Are there any other issues in the HVAU that have not been addressed in the Proposed Variation?*

Pacific National has elected to address Questions 32 and 33 in a single response. Pacific National has no other major concerns with matters raised in ARTC's proposed variation other than those raised in this Pacific National submission.