



Australian
Competition &
Consumer
Commission

Decision

Australian Rail Track
Corporation's application to vary
the 2011 Hunter Valley Access
Undertaking – extension of term

22 June 2016

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1. Summary

The Australian Competition and Consumer Commission (**ACCC**) decided, on 22 June 2016, to consent to Australian Rail Track Corporation's (**ARTC's**) 16 June 2016 application to vary its 2011 Hunter Valley Coal Network Access Undertaking (**2011 HVAU**) to extend the term of the undertaking to 31 December 2016 (**Revised Application**).

The Revised Application seeks to extend the 2011 HVAU by six months while the assessment process for a new access undertaking is finalised. The application also seeks to include transitional arrangements, such as an amended rate of return, the ACCC's 2016 compliance assessment process and pricing for the extension period, that is, from 1 July 2016 to 31 December 2016.

The ACCC has made the decision to consent to this variation under subsection 44ZZA(7) of the *Competition and Consumer Act 2010* (Cth) (**CCA**), having regard to the matters listed under subsection 44ZZA(3) of the CCA.

2. Background

On 29 June 2011, the ACCC accepted ARTC's Hunter Valley Coal Network Access Undertaking under Part IIIA of the CCA.¹ The 2011 HVAU sets out the terms and conditions of access for parties seeking to run trains on ARTC's Hunter Valley Rail Network in New South Wales. The undertaking also sets out the financial model governing ARTC's revenues. The 2011 HVAU was originally due to expire on 30 June 2016.²

On 23 December 2015, ARTC submitted the proposed 2016 Hunter Valley Coal Network Access Undertaking (**2016 HVAU**) to the ACCC for assessment under Part IIIA of the CCA. The ACCC published the proposed 2016 HVAU on 24 December 2015 and released a consultation paper on 8 January 2016. Submissions were due on 22 February 2016.³

On 14 June 2016, ARTC withdrew the proposed 2016 HVAU from the ACCC's consideration. ARTC has advised the ACCC that it 'intends to resubmit a revised access undertaking providing for recent ACCC Compliance period decisions following implementation of the extension period and re-engaging with Customers on important aspects reflected in their submissions to the ACCC on the original submission'.⁴

2.1. ARTC's application to vary the 2011 HVAU

The CCA allows the provider of an access undertaking (in this case, ARTC) to vary that undertaking at any time after it has been accepted by the ACCC, but only with the ACCC's consent.⁵

¹ Division 6 of Part IIIA of the CCA provides that the ACCC may accept an undertaking from a person who is, or expects to be, the provider of a service, in connection with provision of access to the service.

² Documents relating to the accepted 2011 HVAU are available at: <http://www.accc.gov.au/regulated-infrastructure/rail/hunter-valley-access-undertaking-2011>

³ Documents relating to the proposed 2016 HVAU (withdrawn by ARTC on 14 June 2016) are available at: <http://www.accc.gov.au/regulated-infrastructure/rail/hunter-valley-access-undertaking-2016>

⁴ The letter from ARTC advising of the withdrawal of the proposed 2016 HVAU is available at: <http://www.accc.gov.au/regulated-infrastructure/rail/hunter-valley-access-undertaking-2016/application-withdrawn>

⁵ See subsection 44ZZA(7) of the CCA. ARTC has previously submitted a number of variations to the 2011 HVAU for the ACCC's consideration. Further information is available at: <http://www.accc.gov.au/regulated-infrastructure/rail/artc-hunter-valley-access-undertaking>

2.1.1. ARTC's original variation application

On 20 May 2016, ARTC submitted an application to vary the 2011 HVAU pursuant to subsection 44ZZA(7) of the CCA (**Original Application**).

The Original Application proposed variations to:

- extend the term of the 2011 HVAU by six months to 31 December 2016
- reduce the rate of return for the extension period, consistent with that submitted by ARTC for the proposed 2016 HVAU (to a real pre-tax rate of return of 6.74 per cent and a nominal pre-tax rate of return of 8.50 per cent)
- conduct a reconciliation as part of the ACCC's 2016 annual compliance process that has the effect of backdating any difference between the rate of return that is ultimately accepted by the ACCC for the new access undertaking and the rate of return that applies during the extension period, and
- make other amendments relating to transitional arrangements for the true-up test, compliance assessment and pricing for the extension period.

ARTC stated that the application:

- 'provides regulatory certainty to ARTC and [coal] producers while the new HVAU is negotiated',⁶ and
- has been submitted 'following consultation with relevant stakeholders as well as the ACCC as part of the 2016 HVAU application process.'⁷

ARTC's Original Application is available at: <http://www.accc.gov.au/regulated-infrastructure/rail/extension-of-the-2011-hunter-valley-access-undertaking/variation-application>

2.1.2. ACCC consultation on ARTC's original variation application

On 23 May 2016, the ACCC invited submissions on ARTC's Original Application pursuant to subsection 44ZZBD(1) of the CCA. Submissions were due on 6 June 2016.⁸

In response, the ACCC received submissions from:

- Asciano, 6 June 2016
- the Hunter Rail Access Task Force (HRATF),⁹ 8 June 2016

Overall, submitters supported ARTC's proposal to extend the term of the 2011 HVAU to 31 December 2016.

Submissions are available at: <http://www.accc.gov.au/regulated-infrastructure/rail/extension-of-the-2011-hunter-valley-access-undertaking/consultation-letter>

2.1.3. ARTC's revised variation application

On 16 June 2016, ARTC submitted the Revised Application pursuant to subsection 44ZZA(7) of the CCA, taking into account submissions to the ACCC's consultation process on the Original Application.

⁶ ARTC, *Application – 2011 HVAU extension*, 20 May 2016, p. 1.

⁷ Ibid.

⁸ Documents relating to the ACCC's consultation process are available at: <http://www.accc.gov.au/regulated-infrastructure/rail/extension-of-the-2011-hunter-valley-access-undertaking>

⁹ The Hunter Rail Access Task Force is an associated group representing major coal producers in the Hunter Valley.

In particular, the Revised Application incorporates HRATF's proposed drafting amendments to clarify the reconciliation of ARTC's revenues under the ACCC's 2016 annual compliance process.

The ACCC did not invite further submissions on the Revised Application as the proposed variations are substantially similar to those in the Original Application (as outlined above at section 2.1.1).

ARTC's Revised Application is available at: <http://www.accc.gov.au/regulated-infrastructure/rail/extension-of-the-2011-hunter-valley-access-undertaking/revised-variation-application>

3. ACCC's views on ARTC's variation application

The ACCC's view is that, having regard to the matters listed in subsection 44ZZA(3) of the CCA, it is appropriate to consent to ARTC's proposed variations to the 2011 HVAU as set out in the Revised Application. The ACCC's reasons for its decision are below.

As noted, ARTC submitted the Revised Application taking into account submissions to the Original Application. This means that submitters' views on ARTC's proposals for the Original Application are also applicable to the Revised Application, and have been taken into account by the ACCC in making this decision on the Revised Application.

Further information about the ACCC's decision-making framework under Part IIIA of the CCA is set out below in section 5.

3.1. Extending the term of the 2011 HVAU

ARTC proposes to vary section 2.2(b) of the 2011 HVAU to extend the term of the undertaking to 31 December 2016.

ARTC submits that:

- the proposal 'will allow more time for a new HVAU to be agreed',¹⁰ and
- the six month extension 'has the effect of aligning the term of the HVAU with its contractual and compliance obligations that are on a calendar year basis.'¹¹

Submissions support the proposal:

- Asciano submits that the extension to 31 December 2016 'ensures ongoing certainty of regulated rail access on the Hunter Valley coal network'.¹²
- HRATF supports the extension and alignment of the HVAU term with a calendar year approach.¹³

The ACCC considers that the certainty provided by the proposed six-month extension and the alignment of ARTC's obligations with the calendar year is in the legitimate business interests of ARTC and the interests of Access Holders and Operators, having regard to subsections 44ZZA(3)(a) and 44ZZA(3)(c) of the CCA. This is likely to promote the efficient operation and use of the Hunter Valley Rail Network while a new access undertaking is finalised, having regard to subsection 44ZZA(3)(aa) of the CCA.

¹⁰ ARTC, *Revised Application – 2011 HVAU extension*, 16 June 2016, p. 2.

¹¹ Ibid.

¹² Asciano, *Response to the ARTC Proposed Extension and Variation to the 2011 HVAU*, 6 June 2016, p. 1.

¹³ HRATF, *ARTC proposed extension and variation of 2011 Hunter Valley Coal Network Access Undertaking (2011HVAU)*, 8 June 2016, pp. 1-2.

3.2. Financial model for the extension period

The 2011 HVAU includes:

- a financial model (a revenue cap) that regulates ARTC's revenues and access charges in accordance with the application of a building block model, and
- an annual compliance assessment process that the ACCC conducts to ensure ARTC's compliance with the HVAU financial model.¹⁴

3.2.1. Rate of return

ARTC proposes to vary section 4.8 of the 2011 HVAU to specify that for the extension period, that is, from 1 July 2016 to 31 December 2016:

- the real pre-tax rate of return shall be 6.74 per cent, and
- the nominal pre-tax rate of return shall be 8.50 per cent.

ARTC submits that:

- this is consistent with its proposed rate of return for the 2016 HVAU,¹⁵ and
- it understands that this 'is acceptable to the ACCC in light of the proposed true-up'.¹⁶

HRATF submits that:

- for the reasons in its submission to the ACCC's consultation on the proposed 2016 HVAU, the proposed rate of return 'significantly overstates an efficient and appropriate [weighted average cost of capital]',¹⁷ and
- it should be made clear that this rate of return is only a transitional measure and that the rate of return that will ultimately apply from 1 July 2016 will be that approved by the ACCC as part of the assessment process for a new access undertaking.¹⁸

The ACCC notes that ARTC also proposes to include new section 4.10(g)(iii)(B), which provides that for the extension period, there will be a reconciliation for the revised rate of return ultimately approved by the ACCC in a new access undertaking. This will be conducted through the ACCC's annual compliance process for the 2016 calendar year.

In its assessment of the new access undertaking, the ACCC will consider whether ARTC's proposed rate of return is commensurate with the commercial and regulatory risks borne by ARTC, having regard to the pricing principles specified in section 44ZZCA of the CCA.

The ACCC considers that, as ARTC's proposed variations allow the ACCC-approved rate of return for the new access undertaking to effectively be backdated, this will be in the legitimate business interests of ARTC and the interests of Access Holders and Operators, having regard to subsections 44ZZA(3)(a) and 44ZZA(3)(c) of the CCA. This is because any overpayment by users of the Hunter Valley Rail Network will be returned as part of the 2016 annual compliance assessment process.

¹⁴ ARTC, *Hunter Valley Coal Network Access Undertaking*, 23 June 2011, section 4.

¹⁵ ARTC, *Revised Application – 2011 HVAU extension*, 16 June 2016, p. 1.

¹⁶ *Ibid.*, p. 2.

¹⁷ HRATF, *ARTC proposed extension and variation of 2011 Hunter Valley Coal Network Access Undertaking (2011HVAU)*, 8 June 2016, p. 2.

¹⁸ *Ibid.*, p. 4.

3.2.2. Annual compliance assessment for 2016

ARTC proposes to include new sections 4.10(g) and 4.10(h) in the 2011 HVAU to provide for the ACCC's annual compliance assessment for the 2016 calendar year. In particular, the compliance process will:

- reflect the different rate of return applying in each half year period for 2016, and
- allow the ACCC to conduct a reconciliation to effectively backdate any difference between the rate of return ultimately approved by the ACCC for the new access undertaking and the specified rate of return for the extension period.

ARTC also proposes to include new section 4.10(i) to provide certainty that the new access undertaking will give effect to the above transitional arrangements.

ARTC submits that:

- the proposal 'ensures that ARTC is required to undertake the compliance requirement and true-up test for the 2016 calendar year',¹⁹ and
- the true-up for the outcomes of the new approved undertaking means that 'the extension does not prejudice [coal] producers'.²⁰

HRATF submits that:

- it supports the general principles proposed by ARTC, but considers that any necessary adjustments to transitional tariffs should not be delayed until the 2016 annual compliance assessment process,²¹ and
- it has discussed this issue with ARTC, and is of the view that ARTC is prepared to consider approaches for a specific adjustment following commencement of a new access undertaking.²²

The ACCC notes that ARTC's Revised Application has incorporated HRATF's proposal to leave open the possibility of an alternative process for adjusting the transitional tariffs for the extension period. In light of this, the ACCC does not consider that it is necessary to include a separate reconciliation process (in addition to the 2016 annual compliance process) in the 2011 HVAU to make this adjustment.

The ACCC considers that the certainty and transparency provided by specifying the process for the ACCC to determine ARTC's compliance with the financial model for the 2016 calendar year, including to make adjustments to reflect the ACCC-approved rate of return for the new access undertaking, is in the legitimate business interests of ARTC and the interests of Access Holders and Operators, having regard to subsections 44ZZA(3)(a) and 44ZZA(3)(c) of the CCA. This is likely to promote the efficient operation, use of and investment in, the Hunter Valley Rail Network, having regard to subsection 44ZZA(3)(aa) of the CCA.

3.2.3. Pricing

ARTC proposes to include new sections 4.22 and 4.23 in the 2011 HVAU and to vary clause 5.4 of Indicative Access Holder Agreements to determine the indicative access charges for the extension period based on the amended rate of return.

¹⁹ ARTC, *Revised Application – 2011 HVAU extension*, 16 June 2016, p. 3.

²⁰ *Ibid*, p. 1.

²¹ HRATF, *ARTC proposed extension and variation of 2011 Hunter Valley Coal Network Access Undertaking (2011HVAU)*, 8 June 2016, p. 1.

²² *Ibid*, p. 2.

ARTC submits that this ‘provides pricing certainty to ARTC and [coal] producers while the new HVAU is negotiated’.²³

HRATF submits that provided the transitional pricing ‘involves only the consequential amendments necessary to reduce the rate of return’ and ‘is not used to introduce or modify other inputs or costs’, then it would be comfortable with the proposed approach.²⁴

As noted, ARTC also proposes other variations that will allow a recalculation and reconciliation of access charges for the 2016 calendar year, based on the ACCC-approved rate of return for the new access undertaking.

In light of this, the ACCC considers that the certainty provided by setting out the transitional access charges for the extension period is in the legitimate business interests of ARTC and the interests of Access Holders and Operators, having regard to subsections 44ZZA(3)(a) and 44ZZA(3)(c) of the CCA. This is likely to promote the efficient operation, use of and investment in, the Hunter Valley Rail Network, having regard to subsection 44ZZA(3)(aa) of the CCA.

3.3. Other variations

ARTC proposes to include a new section 13.1(c) in the 2011 HVAU to provide that ARTC will report on its performance against network key performance indicators for the 2016 calendar year, despite the expiry of the 2011 HVAU on 31 December 2016.

HRATF supports the intent of this provision.²⁵

The ACCC considers that the commitment to provide information and ensure transparency measures remain in place is in the interests of Access Holders and Operators, having regard to subsection 44ZZA(3)(c) of the CCA.

4. ACCC’s decision to consent to ARTC’s variation application

For the reasons set out above, the ACCC has decided to consent to ARTC’s 16 June 2016 application to vary its 2011 HVAU pursuant to subsection 44ZZA(7) of the CCA.

The ACCC has had regard to the matters set out in subsection 44ZZA(3) of the CCA. The matters that are particularly relevant to this decision are:

- the legitimate business interests of ARTC (subsection 44ZZA(3)(a))
- the interests of persons who might want access to the Hunter Valley Rail Network under the HVAU (subsection 44ZZA(3)(c)), and
- the objects of Part IIIA as set out in section 44AA (subsection 44ZZA(3)(aa)).

ARTC’s Revised Application does not directly affect the others matters set out in subsection 44ZZA(3).

The ACCC has met the timeframe in subsection 44ZZBC(1) of the CCA for making its decision on ARTC’s Revised Application.

²³ ARTC, *Revised Application – 2011 HVAU extension*, 16 June 2016, p. 1.

²⁴ HRATF, *ARTC proposed extension and variation of 2011 Hunter Valley Coal Network Access Undertaking (2011HVAU)*, 8 June 2016, p. 3.

²⁵ *Ibid*, p. 5.

5. ACCC's decision-making framework

5.1. Legal test for accepting an application to vary an access undertaking

Subsection 44ZZA(7) of the CCA provides that the ACCC may consent to a variation of an undertaking if it thinks it appropriate to do so, having regard to the matters set out in subsection 44ZZA(3) of the CCA.

The matters in subsection 44ZZA(3) include:

- the objects of Part IIIA of the CCA, which are to:
 - promote the economically efficient operation of, use of and investment in the infrastructure by which the 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 pricing principles specified in section 44ZZCA of the CCA (see further below)
- the legitimate business interests of the provider of the service
- the public interest, including the public interest in having competition in markets (whether or not in Australia)
- the interests of persons who might want access to the service
- whether the undertaking is in accordance with an access code that applies to the service, and
- any other matters that the ACCC thinks are relevant.

In relation to the pricing principles, section 44ZZCA of the CCA provides that:

- regulated access prices should:
 - be set so as to generate expected revenue for a regulated service that is at least sufficient to meet the efficient costs of providing access to the regulated service or services, and
 - include a return on investment commensurate with the regulatory and commercial risks involved
- access price structures should:
 - allow multi-part pricing and price discrimination when it aids efficiency, and
 - 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
- access pricing regimes should provide incentives to reduce costs or otherwise improve productivity.

5.2. Timeframe for ACCC decision

Subsection 44ZZBC(1) of the CCA provides that the ACCC must make a decision on an access undertaking application within the period of 180 days starting at the start of the day the application is received (referred to as 'the expected period'). A request made to the ACCC for the variation of an access undertaking is an access undertaking application.