Decision

Australian Rail Track Corporation's application to vary the 2011 Hunter Valley Access Undertaking

29 November 2018

Contents

Abbreviations and acronyms

Act	Competition and Consumer Act 2010 (*Cth*)
ACCC	Australian Competition and Consumer Commission
ARTC	Australian Rail Track Corporation
FTE	Full Time Equivalent
GTK	Gross Tonne Kilometres
HRATF	Hunter Rail Access Task Force
HVAU	Hunter Valley Access Undertaking
HVCCC	Hunter Valley Coal Chain Coordinator
IAHA	Indicative Access Holder Agreement
IAU	Interstate Access Undertaking
IPART	Independent Pricing and Regulatory Tribunal
NSW	New South Wales
NSWRAU	New South Wales Rail Access Undertaking
OSA	Operator Sub-Agreement
PZ1	Pricing Zone 1
PZ2	Pricing Zone 2
PZ3	Pricing Zone 3
RAB	Regulatory Asset Base
RCG	Rail Capacity Group
ROR	Rate of Return
TOP	Take or Pay
Train Km	Train Kilometres
Tribunal	Australian Competition Tribunal
TUT	True Up Test
WIK	WIK-Consult

Executive Summary

On 29 November 2018, the Australian Competition and Consumer Commission (**ACCC**) consented to the Australian Rail Track Corporation's (**ARTC's**) 28 September 2018 application (**September 2018 Variation**) to vary its 2011 Hunter Valley Coal Network Access Undertaking (**2011 HVAU**) under section 44ZZA(7) of the *Competition and Consumer Act 2010* (Cth) (**the Act**), having regards to the matters listed under section 44ZZA(3) of the Act.

The September 2018 Variation incorporates a number of unresolved matters from the previous 2016 HVAU and 2017 HVAU assessments, as well as the recommended amendments for clarity and certainty set out in the ACCC's 28 June 2018 Draft Decision on ARTC's 21 December 2017 application to vary the 2011 HVAU (the **December 2017 Variation**).

These amendments include the introduction of an incremental cost methodology, the introduction of path based pricing, a review mechanism with respect to the pricing framework to apply after the current term of the HVAU expires, and a mechanism for the Rail Capital Group (**RCG**) and ACCC oversight regarding the process for allocating capital costs as either Fixed and/or Incremental Capital Costs.

Although the ACCC has significant concerns with elements of ARTC's amendments to the 2011 HVAU, it has decided to consent to the September 2018 Variation in light of the support by a majority of stakeholders who submit that the 'package' of proposed amendments is preferable to the current HVAU. Based on its extensive consultation with stakeholders, including ARTC, Access Holders from all pricing zones, and above rail operators, the ACCC is confident that stakeholders are fully aware of the implications of the variation on the operation of the HVAU.

In providing their support however, stakeholders have accepted ARTC's assurances that their agreement to the September 2018 Variation will not set a precedent for a revised undertaking when the current term of the HVAU expires in 2021, and that all relevant terms of the undertaking will be reconsidered. It is on this basis that the ACCC considers it appropriate to consent to the September 2018 Variation.

The ACCC has provided a detailed explanation of its concerns with the amendments that have been supported by industry in this Decision and in its Draft Decision on the December 2017 Variation.

Finally, the ACCC also notes that although regulatory consistency is a relevant consideration under Part IIIA of the Act, previous decisions of the Commission are not binding on it. As such, the views set out in this Decision would be reconsidered in the assessment of any future regulatory instrument proposed to cover the Hunter Valley rail network, taking into account all relevant considerations at the time.

ACCC view

The ACCC considers it important to clearly set out its concerns with the amendments to facilitate future negotiations between ARTC and stakeholders when ARTC undertakes its review of the pricing framework under the review mechanism in section 2.3(d), and in developing the revised regulatory instrument that will replace the current HVAU in December 2021. A summary of the ACCC's concerns regarding ARTC's key proposals is set out below.

Floor Contribution and Ceiling Limits

Pricing Zone 3 (**PZ3**) is currently unconstrained and subject to a capitalised loss account. The September 2018 Variation introduces new provisions that contemplate what will happen once PZ3 becomes a Constrained Network. ARTC has provided assurances to stakeholders, that have been accepted by the majority of Access Holders, that a capitalised loss balance will remain at the end of the term of the September 2018 Variation and consequently, the Floor Contribution and Ceiling Limits provisions will not come into operation during the current term.

This decision sets out a number of concerns with the substance of ARTC's proposal, and the proposed review mechanism. This includes the view that:

- once Constrained, PZ3 producers will not contribute to their Fixed Costs in PZ1
- once Constrained, ARTC may be able to shift revenue from PZ1 to contribute to costs in PZ3
- there is no binding assurance that PZ3 will not become Constrained during the current term of the HVAU; and
- the proposed review mechanism does not specify the scope or timeframe for the review, and is ambiguously worded.

Incremental Capital Cost allocator

The September 2018 Variation allocates Incremental Capital Costs on the basis of an Access Holders' contracted usage, rather than actual usage. The ACCC considers this position to be inconsistent with the ACCC's 2013 Annual Compliance Final Determination, which determined that actual usage was the appropriate allocator.[1] As such, this Decision sets out the ACCC's view that this proposal is economically inefficient, as it is actual usage, not contracted capacity that drives costs on the Network.

Capital allocation decisions at RCG

The September 2018 Variation introduces changes to how ARTC will consult with industry on Capital Allocation decisions, including introducing different processes at RCG depending on whether a project is Expansion Capital or Sustaining Capital–new cost categories. Under ARTC's changes, it must seek endorsement from the RCG over whether Expansion Capital is treated as a Fixed Cost or Incremental Capital Cost. In the event of an objection, RCG members have recourse to resolution by the ACCC. In this Decision, the ACCC notes its concerns that whether a capital cost is treated at a Fixed Cost or an Incremental Capital Cost affects which users ultimately pay for those costs. For clarity and certainty, this Decision also sets how the ACCC will approach a resolution in the event of a raised objection. Particularly, that the ACCC will have regard to any submissions from stakeholders as well as the methodology set out in the 2013 Annual Compliance Final Determination.

Path based pricing

The September 2018 Variation alters the structure of Access Charges to a new three part tariff comprising the following components:

[1] See ACCC, *Final determination: Australian Rail Track Corporation's compliance with the Hunter Valley coal network access undertaking financial model for the 2013 calendar year*, 6 June 2016.

- Non-Take or Pay (**non-TOP**): allocated on actual gross tonnes kilometres (**GTK**), and intended to recover Variable Maintenance Costs
- TOP 1: allocated on contracted GTK, and intended to recover Incremental Capital Costs
- TOP 2: allocated on contracted train kilometres (**Train Km**), and intended to recover Fixed Costs.

ARTC submitted that charging a component of Access Charges on the basis of Train Km will maximise the efficient consumption of network capacity.[2] This decision notes that ARTC has not provided sufficient evidence that Fixed Costs are driven by Train Km. Therefore, the decision outlines the implications on the economically efficient use of, and investment in, the Hunter Valley rail network, if Access Charges are not reflective of the costs they are intended to recover.

[2] ARTC, *2011 Hunter Valley Coal Network Access Undertaking Variation – Explanatory Guide*, 21 December 2017, p. 10.

1. Introduction

On 28 September 2018, ARTC submitted an application to the ACCC to vary the 2011 HVAU pursuant to section 44ZZA(7) of the Act.

The September 2018 Variation is a revised version of the December 2017 Variation, with amendments to improve clarity and certainty, as identified in the ACCC's Draft Decision on the December 2017 Variation. As such, the September 2018 Variation carries over the same changes proposed in the December 2017 Variation – the introduction of an incremental cost methodology and path based pricing.

The major amendments to improve clarity and certainty in the September 2018 Variation relate to the process for RCG endorsing Capital Allocation decisions, including recourse to resolution by the ACCC in the event of an objection over Capital Allocation.

ARTC additionally submitted the following amendments:

- amending the Variation Effective Date, at section 2.3(b)
- introducing a new provision that requires ARTC to undertake a review of the pricing framework after Loss Capitalisation ends, at section 2.3(d)
- reinstating clause 11.5(d) of the indicative Access Holder Agreement (**IAHA**)
- removing redundant provisions
- correcting minor drafting errors.

On 29 November 2018 the ACCC consented to this variation under section 44ZZA(7) of the Act, having regard to the matters listed under section 44ZZA(3) of the Act.

1.1. Further information

The Application and other relevant material, including supporting submissions from ARTC, and stakeholder submissions are available on the ACCC's website at the following link:

https://www.accc.gov.au/regulated-infrastructure/rail/artc-hunter-valley-access-undertaking/september-2018-variation-of-the-2011-hunter-valley-access-undertaking

Alternatively, go to the ACCC's homepage at https://www.accc.gov.au/ and follow the links to 'Regulated Infrastructure Rail', to the 'September 2018 variation of the 2011 Hunter Valley Access Undertaking'.

Previous undertaking applications to replace the 2011 HVAU and prior variation applications are also available on the ACCC's website at:

https://www.accc.gov.au/regulated-infrastructure/rail/artc-hunter-valley-access-undertaking

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2. Background

2.1. ARTC

ARTC was established in 1997 to provide below-rail access services, as a result of an Inter-Governmental Agreement between State and Commonwealth Transport Ministers. This was intended to improve, among other things, the efficiency and competitiveness of the rail industry by providing a single point of access for the standard gauge interstate rail network.

In 2004, ARTC entered a 60-year lease over the interstate and Hunter Valley rail networks in NSW. As a condition of this lease, ARTC was required to submit an access undertaking to the ACCC for its Hunter Valley rail network. Prior to this, the Hunter Valley rail network was subject to the NSW Rail Access Undertaking (**NSWRAU**), administered by the Independent Pricing and Regulatory Tribunal (**IPART**).

2.2. 2011 Hunter Valley Access Undertaking

On 29 June 2011, the ACCC accepted the 2011 HVAU under Part IIIA of the Act. 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 NSW and comprises the following key features:[3]

- preliminary sections on the operation and interpretation of the HVAU
- a process for parties to apply for access with ARTC, and a negotiate/arbitrate framework, with ACCC arbitration as a back-stop, to facilitate agreement of mutually acceptable terms and conditions of access
- a revenue cap and pricing methodologies to promote access pricing that is efficient and that reflects the cost of providing access to the network
- numerous provisions regarding network capacity management, including provisions designed to facilitate alignment of capacity management on the Hunter Valley rail network with other components of the supply chain
- a framework for governing investment in the network and creation of additional network capacity. The framework allows for endorsement of investment proposals by the RCG, and a user funding option where Access Holders can fund a project if ARTC ceases or refuses to contribute to its development
- liability and performance accountability/incentive measures with implications for both ARTC and access seekers
- operational provisions regarding management of trains on the network.

2.3. 2016 and 2017 HVAU assessments

On 23 December 2015, ARTC submitted the proposed 2016 HVAU to the ACCC for assessment as an intended replacement to the 2011 HVAU. However, on 14 June 2016 ARTC withdrew the 2016 HVAU prior to the ACCC finalising its assessment process. On 20 May 2016, ARTC submitted a variation application to extend the term of the 2011 HVAU to 31 December 2016. On 16 June 2016, ARTC submitted a revised variation application–which the ACCC consented to on 22 June 2016. On 18 October 2016, ARTC submitted an additional variation application to extend the term of the 2011 HVAU to 30 June 2017–which the ACCC consented to on 23 November 2016.

3 ACCC, *Decision – in relation to Australian Rail Track Corporation's Hunter Valley,* 29 June 2011, p. 7.

On 9 December 2016, ARTC submitted the proposed 2017 HVAU to the ACCC for assessment. On 20 April 2017, the ACCC published a draft decision to not accept the 2017 HVAU, providing detailed recommendations as to how the various issues may be resolved by ARTC.[4] On 8 May 2017, ARTC withdrew the 2017 HVAU prior to the ACCC finalising its assessment process.

2.4. June 2017 Variation

On 6 June 2017, ARTC submitted a variation application to the ACCC for assessment (**June 2017 Variation**). The June 2017 Variation sought to extend the term of the HVAU until 31 December 2021, and vary the real pre-tax Rate of Return to 5.38 per cent and the remaining mine life to 23 years. On 16 June 2017, ARTC submitted a revised variation application– which the ACCC consented to on 29 June 2017. While the ACCC ultimately consented to the June 2017 Variation, it did so on the basis that it had the support of a majority of stakeholders. However stakeholders submitted that their support of the June 2017 Variation was to ensure regulatory certainty. In particular, if the ACCC did not consent to the June 2017 Variation, then the 2011 HVAU would have expired on 30 June 2017 and regulation of the Hunter Valley rail network would have transferred to the NSWRAU. However, the Hunter Rail Access Task Force (**HRATF**) submitted that:[5]

> *The HRATF does not consider the commercial parameters and allocation principles set out in the Variation [are] consistent with regulatory practice, including as identified by the ACCC in its recent draft decision.*

In addition to varying the term and commercial parameters, section 2.3(d) of the June 2017 Variation required ARTC to engage in good faith negotiations with Access Holders to develop and submit a further variation application to the ACCC by 31 December 2017 to:

- incorporate path based pricing
- apply an incremental cost methodology such that:
  - PZ3 Access Holders contribute incremental costs for PZ1
  - incremental maintenance costs are allocated on the basis of actual usage and Incremental Capital Costs are allocated on the basis of contracted capacity
  - TOP Charges include incremental capital based on contracted capacity
  - a dual ceiling limit applies.

In its June 2017 Variation application, ARTC stated that the obligation to submit a subsequent variation application under section 2.3(d) would 'ensure that the HVAU is updated to include the various matters on which there was previously general agreement between ARTC and the majority of stakeholders'.[6] These are matters that ARTC had previously proposed and consulted on as part of the 2016 HVAU and 2017 HVAU assessment processes.

2.5. December 2017 Variation

On 21 December 2017, ARTC submitted the December 2017 Variation to the ACCC for assessment. In addition to the amendments specified at section 2.3(d) of the June 2017 Variation, the December 2017 Variation sought to amend provisions relating to the commencement and administration of the HVAU, the treatment of costs and cost allocations

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[4] ACCC, *Draft Decision – Australian Rail Track Corporation's 2017 Hunter Valley Access Undertaking,* 20 April 2017, available at: https://www.accc.gov.au/regulated-infrastructure/rail/hunter-valley-access-undertaking-2017/draft-decision

[5] HRATF, *HRATF response to 2011 Hunter Valley Access Undertaking (HVAU) variation application*, p. 1.

[6] ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term,* 6 June 2017, p. 2.

at RCG, and the annual compliance process. The December 2017 Variation also sought to remove some provisions from the HVAU that ARTC considered to be redundant.

On 23 May 2018, ARTC lodged a supplementary submission to the ACCC that flagged its intention to amend the December 2017 Variation to incorporate a new review mechanism provision (discussed further in chapter 5).

On 28 June 2018, the ACCC issued a Draft Decision to consent to ARTC's December 2017 Variation, subject to ARTC making amendments for clarity and certainty.[7] The ACCC's Draft Decision was considered in light of support by a majority of stakeholders who had submitted that the 'package' of proposed amendments were preferable to the status quo–being the current 2011 HVAU continuing unchanged until its expiry on 31 December 2021.

On 27 July 2018, ARTC withdrew the December 2017 Variation from the ACCC's consideration.

2.6. Timeline of HVAU assessments

Table 1 below provides a timeline of the key stages of the ACCC's assessment.

Table 1: Timeline of ACCC assessment

Date	Event
29 June 2011	The ACCC accepts the 2011 HVAU under Part IIIA of the Act. The original expiry date of the 2011 HVAU was 30 June 2016.
23 December 2015	ARTC submits the 2016 HVAU to the ACCC for assessment as a replacement to the 2011 HVAU.
20 May 2016	ARTC submits a variation application to extend the term of the 2011 HVAU to 31 December 2016.
14 June 2016	ARTC withdraws the 2016 HVAU from the ACCC's assessment process.
16 June 2016	ARTC submits a revised variation application to extend the term of the 2011 HVAU to 31 December 2016.
22 June 2016	The ACCC consents to the variation application.
18 October 2016	ARTC submits a variation application to extend the term of the 2011 HVAU to 30 June 2017.
23 November 2016	The ACCC consents to the variation application.
9 December 2016	ARTC submits the 2017 HVAU to the ACCC for assessment.
20 April 2017	The ACCC publishes a draft decision to not accept the 2017 HVAU.
8 May 2017	ARTC withdraws the 2017 HVAU from the ACCC's assessment process.
6 June 2017	ARTC submits the June 2017 Variation application to extend the term of the 2011 HVAU to 31 December 2021, vary the commercial parameters and introduce an obligation to submit a subsequent variation application.
16 June 2017	ARTC submits a revised variation application, which includes finalised Access Charges.
29 June 2017	The ACCC publishes a final decision to consent to the variation application.
21 December 2017	ARTC submits the December 2017 Variation application to incorporate the amendments proposed under section 2.3(d) of the June 2017 Variation.

[7] See the ACCC's Draft Decision on the December 2017 Variation at https://www.accc.gov.au/regulated-infrastructure/rail/december-2017-variation-of-the-2011-hunter-valley-access-undertaking/draft-decision

Date	Event
23 May 2018	ARTC lodges a supplementary submission flagging its intention to amend the December 2017 Variation to incorporate a new review mechanism provision.
28 June 2018	The ACCC publishes a Draft Decision to consent to the December 2017 Variation, subject to ARTC incorporating drafting amendments for clarity and certainty.
27 July 2018	ARTC withdraws the December 2017 Variation from the ACCC's assessment process.
28 September 2018	ARTC submits the September 2018 Variation application to incorporate the amendments proposed under section 2.3(d) of the June 2017 Variation, as well as amendments to improve clarity and certainty.

3. Legislative framework

3.1. Part IIIA of the Competition and Consumer Act

The legislative framework for the ACCC's consideration of the September 2018 Variation is set out in Part IIIA of the Act. Division 6 of Part IIIA states that a provider of a service (or a person who expects to be the provider of a service) may give an undertaking to the ACCC in connection with the provision of access to that service. The Act also 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.[8]

Section 44ZZA(7) of the Act 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 section 44ZZA(3) of the Act. This chapter discusses, in general, how the ACCC has had regard to the matters under section 44ZZA(3) of the Act in making its Decision in relation to the September 2018 Variation.

3.2. Threshold for accepting an access undertaking

Section 44ZZA(3) of the Act provides that the ACCC may accept an access undertaking if it thinks it appropriate to do so, having regard to the following matters:

- the objects of Part IIIA in section 44AA of the Act, which are to:
    - promote the economically efficient operation of, use of and investment in the infrastructure by which 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 Act, which provide 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; and
    - access prices 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.
- 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)

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[8] See section 44ZZA(7) of the Act. 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.

- 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
- any other matters that the ACCC thinks are relevant.

Section 44ZZA(3AA) of the Act provides that the ACCC must not accept an undertaking if a decision of the Commonwealth Minister is in force under section 44N that a regime for access to the service is an effective access regime. The ACCC notes that there is currently no effective access regime in place that applies to the Hunter Valley rail network that is the subject of the 2011 HVAU.

Lastly, section 44ZZA(3A) provides that the ACCC must not accept an undertaking unless:

- the provider or proposed provider of the service is a corporation (or partnership, or joint venture consisting solely of corporations); or
- the undertaking provides for access only to third parties that are corporations; or
- the undertaking provides for access that is (or would be) in the course of, or for the purposes of constitutional trade or commerce.

The ACCC is satisfied that the section 44ZZA(3A) requirements have been met.

3.3. Objects of Part IIIA

The ACCC is required to have regard to the objects of Part IIIA set out in section 44AA of the Act, which are to:

- promote the economically efficient operation of, use of and investment in the infrastructure by which 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.

Promotion of efficiency and competition

Efficient operation of, use of and investment in the Hunter Valley rail network may promote effective competition in a range of upstream and downstream markets. The ACCC has not conducted a market definition analysis (such as would occur under Part IV of the Act), and therefore has not reached a conclusive view on what constitutes a particular upstream or downstream 'market'. However, the ACCC notes that access to the Hunter Valley rail network may have significance to competition between above-rail operators for services to coal and non-coal users of the network, and to competition between coal producers for upstream inputs to mining (e.g. mining tenements, labour) and sales to export and domestic customers.

ARTC sets this out in the preamble to the 2011 HVAU. Specifically, section 1.1(d) states:

> *ARTC recognises that the operation, maintenance, and investment in the development of, the Network is primarily to improve utilisation and performance of such rail services and to optimise coal export throughput in the Hunter Valley.*

Further, ARTC recognises that it is a 'Hunter Valley coal industry objective to ensure that Coal Chain Capacity is maintained, developed and utilised efficiently.'[9]

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[9] See section 1.1(h) of the 2011 HVAU.

The ACCC notes that section 14.1 of the 2011 HVAU defines 'Efficient' as:

> *…in respect to costs and operating expenditure, costs incurred by a prudent service provider managing the Network, acting efficiently, having regard to any matters particular to the environment in which management of the Network occurs…*

In having regard to 'economic efficiency' under the Act, the ACCC takes into account the following:

- Technical or productive efficiency–achieved when firms produce the goods and services that they offer to consumers at least cost.
- Allocative efficiency–achieved when firms employ resources to their highest valued uses to produce goods and services. That is, those that provide the greatest benefit relative to costs.
- Dynamic efficiency–achieved when firms have appropriate incentives to invest, innovate and improve the range and quality of services, increase productivity and lower costs over time. Dynamic efficiency will be promoted by access prices that facilitate entry and competition in the supply of services in dependent markets.

A consistent approach to access regulation

The second object of Part IIIA is to provide a framework and guiding principles to encourage a consistent approach to access regulation in each industry.

ARTC's rail network in NSW is currently regulated by three access undertakings:

- 2011 HVAU
- 2008 Interstate Access Undertaking (**2008 IAU**)[10]
- NSWRAU.

In the current context, ARTC notes it has submitted the September 2018 Variation to address concerns raised by the ACCC regarding clarity and certainty of the operation of sections of ARTC's December 2017 Variation.[11] ARTC submitted the December 2017 Variation to fulfil the commitment it made in the June 2017 Variation to lodge a variation to incorporate path based pricing and an incremental cost methodology into the HVAU.[12]

In its June 2017 Variation application, ARTC acknowledged that these amendments were previously proposed in the 2017 HVAU. However, in the draft decision on the 2017 HVAU the ACCC stated that it did not have sufficient information from ARTC in order to make a determination on ARTC's proposed amendments. ARTC stated that 6 months between the acceptance of the June 2017 Variation and the submission of the December 2017 Variation would provide enough time to have good faith negotiations with producers, and prepare and provide further information.[13]

The ACCC also recognises that its consideration of the September 2018 Variation must have regard to the particular features and circumstances of the Hunter Valley rail network. Therefore, the ACCC has taken into account:

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[10] On 30 July 2008, the ACCC accepted the 2008 IAU, with an expiry date of 21 August 2018. On 6 March 2018, ARTC submitted the 2018 IAU, intended to replace the 2008 IAU. The 2018 IAU is currently under ACCC assessment.

[11] ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term*, 28 September 2018, p. 2. For clarity and certainty, the ACCC notes that ARTC's September 2018 Variation does not include a proposal to extend the term of the undertaking.

[12] ARTC, *2011 Hunter Valley Coal Network Access Undertaking Variation – Explanatory Guide*, 21 December 2017, p. 4.

[13] ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term*, 6 June 2017, p. 3.

- the current regulatory framework; and
- the significance of the Network to the Hunter Valley coal supply chain overall, including the existing commercial arrangements across the Hunter Valley coal export chain; and the change in relevant market conditions from those during the initial development of the 2011 HVAU.

The ACCC considers that consistency between the regulatory instruments applied to ARTC (the HVAU, IAU and NSWRAU) is desirable. However, consideration must be given to whether the proposed changes in the September 2018 Variation are appropriate in the current circumstances taking into account all relevant matters.

3.4. Pricing Principles in section 44ZZCA

The ACCC is required to have regard to the pricing principles specified in section 44ZZCA of the Act. The 2011 HVAU contains provisions setting out pricing principles and methodologies relevant to the calculation of charges for access to the Hunter Valley rail network. The pricing principles are particularly relevant to the amendments that ARTC is seeking in respect of the introduction of path based pricing, and the application of a new incremental cost methodology, discussed further in chapters 9, 5 and 6, respectively.

3.5. Legitimate business interests of the provider

Section 44ZZA(3)(a) of the Act requires the ACCC to have regard to the legitimate business interests of the provider, in this case ARTC. ARTC made a submission in support of its December 2017 Variation and the September 2018 Variation, which the ACCC has had regard to as part of its assessment. The ACCC references this submission as it relates to particular issues.

The ACCC notes the relationship between the legitimate business interests of ARTC and the pricing principles specified in section 44ZZCA(a), which 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; and
- include a return on investment commensurate with the regulatory and commercial risks involved.

The ACCC also notes that the legitimate business interests of ARTC sometimes differ from the interests of access seekers, though this does not necessarily imply the interests are always in direct conflict. As a general consideration, the ACCC is of the view that the September 2018 Variation and the 2011 HVAU should provide an appropriate balance between the interests of ARTC and access seekers.

3.6. The public interest

Section 44ZZA(3)(b) of the Act requires the ACCC to have regard to the public interest, including the public interest in having competition in markets (whether or not in Australia).

The Hunter Valley coal supply chain is predominantly used for the export of coal from Australia, allowing Australian-based coal producers to sell coal to overseas customers. The ACCC therefore considers that the provision of effective access to the Hunter Valley rail network via the 2011 HVAU has the potential to enhance the efficiency of Australian coal producers seeking to compete with international rivals for the sale of coal to global customers. Domestic purchasers of Hunter Valley coal may similarly benefit from the enhanced efficiency and competitiveness of coal producers.

3.7. Interests of access seekers

Section 44ZZA(3)(c) of the Act requires the ACCC to have regard to the interests of persons who might want access to the service.

To assess the interests of access seekers, the ACCC has conducted a public consultation process on the September 2018 Variation, the December 2017 Variation, the three previous extension applications and the 2016 and 2017 HVAU applications, during which the ACCC sought and received submissions from a range of interested parties. As part of this Final Decision, the ACCC has had regard to relevant stakeholder submissions on these previous HVAU assessment processes. The ACCC has also met with interested parties to further discuss submissions and keep parties updated on the assessment process. Submissions by access seekers made during consultation are particularly relevant in having regard to section 44ZZA(3)(c).

The ACCC considers that access seekers include those persons seeking access to the Hunter Valley rail network for the purpose of hauling coal, either to the Port of Newcastle for export or to domestic customers. The preamble to the 2011 HVAU recognises that the predominant usage of the Hunter Valley rail network is for rail haulage of export coal to the Port of Newcastle. Further, the HVAU contemplates coal producers entering agreements directly with ARTC for access rights, provided that those rights are exercised via an above-rail operator.

While the predominant usage of the Hunter Valley rail network is for the transport of coal, the ACCC also considers that access seekers include those parties seeking access to the network for purposes other than hauling coal.

The ACCC also considers it important to recognise above-rail operators as access seekers or potential access seekers, noting that above-rail operators may share common interests with both coal and non-coal access seekers.

The ACCC has had regard to submissions from access seekers, and references these submissions as they relate to particular issues.

3.8. In accordance with an access code

Section 44ZZAA of the Act provides that a prescribed industry body may give a written code (known as an access code) to the ACCC setting out rules for access to a service. The ACCC may accept the code if it think it appropriate to do so having regard to matters set out in section 44ZZAA(3).

In having regard to this matter in the current context, the ACCC notes that there is currently no access code in place that applies to the Hunter Valley rail network.

3.9. Any other matters the ACCC thinks are relevant

Section 44ZZA(3)(e) of the Act provides that, in deciding whether to accept an undertaking, the ACCC may have regard to any other matters it thinks are relevant.

For the reasons set out below, the ACCC considers it appropriate to have regard to stakeholder support for ARTC’s proposed amendments, the alignment of the Hunter Valley Coal Chain, and the extent to which the HVAU is sufficiently clear and certain in its terms, effect, and operation.

Stakeholder support for ARTC's proposed approach

The ACCC considers it relevant where proposed amendments have the support of the majority of stakeholders. The ACCC notes that HRATF's submission supports the 'package' of amendments proposed by ARTC.[14] This is consistent with HRATF's submissions to the December 2017 Variation, where it stated that the December 2017 Variation is preferred to the status quo of the current HVAU continuing unchanged until the end of its term on 31 December 2021.[15] The ACCC also notes the support of other stakeholders in submissions on the December 2017 Variation and the September 2018 Variation.

The ACCC has had regard to the number of stakeholders that have submitted that they endorse ARTC's proposed amendments in the December 2017 Variation, which are reflected in the September 2018 Variation, as an 'other matter' it thinks is relevant under section 44ZZA(3)(e) of the Act. However the ACCC also considers that the extent of stakeholder support also reflects that the September 2018 Variation is in the interests of access seekers (section 44ZZA(3)(c)).

Coal supply chain alignment

The ACCC acknowledges that the Hunter Valley rail network is an important part of the overall Hunter Valley coal supply chain, in that it links the coal mines in the Hunter Valley with the coal export terminals at the Port of Newcastle. Consequently, consistent with its views in the final decision on the 2011 HVAU, the ACCC continues to view the promotion of alignment between the Hunter Valley rail network and other elements of the Hunter Valley coal supply chain as a relevant matter in the assessment of the September 2018 Variation.[16]

The HVAU was designed to promote the efficiency of the overall Hunter Valley coal supply chain. It is accepted by parties at all levels of the coal supply chain (mines, below-rail, above-rail, and port terminals) that stand alone capacities of the different elements of the supply chain do not translate into whole system capacity. The HVAU therefore includes several mechanisms designed to facilitate coordination and cooperation between various constituents of the Hunter Valley coal supply chain.

The ACCC has had regard to alignment as an 'other matter' it thinks is relevant under section 44ZZA(3)(e) of the Act. However, the ACCC also considers that coal supply chain alignment is in the interests of access seekers, is in the public interest, and promotes the economically efficient operation of, use of and investment in infrastructure (sections 44ZZ(3)(aa), (b) and (c)).

Clarity and certainty of the HVAU

The ACCC considers it relevant that the HVAU provides for sufficient clarity and certainty in its terms, effect and operation, as to enable the following:

- ARTC and access seekers to be sufficiently aware of their respective rights and obligations, and so avoid unnecessary costs, monetary and non-monetary, when using the processes set out in the HVAU. In this regard, the ACCC notes that a sufficiently clear and certain HVAU is in the interests of ARTC and access seekers.

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14 HRATF, *HRATF supplementary submission,* 19 October 2018, p. 1.

15 HRATF, *HRATF supplementary submission*, 30 May 2018, p. 2.

16 ACCC, *Decision – in relation to the Australian Rail Track Corporation's Hunter Valley Rail Network Undertaking,* 29 June 2011, p. 10.

- The mediator appointed pursuant to the HVAU, or the arbitrator being the ACCC, to quickly and effectively resolve any dispute that may arise between an access seeker and access provider.
- The ACCC to quickly and effectively resolve any potential enforcement concerns that may arise regarding potential non-compliance with the HVAU by ARTC.

The ACCC has had regard to clarity and certainty of the HVAU as an ‘other matter’ it thinks is relevant under section 44ZZA(3)(e) of the Act. However, the ACCC also considers that clarity and certainty of the HVAU is in the legitimate business interests of ARTC and the interests of access seekers (sections 44ZZA(3)(a) and (c)).

ARTC notes in its application that it has proposed a number of amendments in the September 2018 Variation to address the concerns raised by the ACCC in the Draft Decision on the December 2017 Variation relating to clarity and certainty of some provisions.[17]

[17] See ACCC, *Draft Decision – Australian Rail Track Corporation’s December 2017 Variation to the 2011 Hunter Valley Access Undertaking,* 20 June 2018.

4. Commencement and Administration of the Undertaking

Section 2 of the September 2018 Variation sets out the administrative matters for the HVAU. The September 2018 Variation proposes changes to sections relating to the commencement of the varied Undertaking (section 2.3 of the September 2018 Variation) and existing rights and agreements (section 2.4). These proposed changes are discussed in this chapter.

The September 2018 Variation also proposes, in section 2.3, a commitment for ARTC to consult on the appropriate economic model for the ceiling limit to apply for future versions of the HVAU. This is discussed in further detail in chapter 5 of this Decision. ARTC also proposes minor changes to details set out in section 2.6, which relate to the proposed introduction of path based pricing and the Floor Reconciliation and Ceiling Limits. These are discussed further in chapters 9 and 5 of this Decision.

Scope and Administration of the Undertaking

4.1. ARTC proposal

Under section 2.3(b) of the September 2018 Variation, ARTC proposes that all provisions as varied in the September 2018 Variation are to commence on 1 January 2019 (the Variation Effective Date). The exception to this are provisions that are necessary for ARTC to determine Charges to apply on and from 1 January 2019.

Section 2.3(b)(ii) states that if the Variation Effective Date is after 1 January 2019, then all provisions in the September 2018 Variation are taken to have commenced operation on 1 January 2019.

ARTC submits that this approach to the Variation Effective Date and commencement date meets the ACCC's legislative requirements and provides a clear timeframe for the commencement of operation of the September 2018 Variation.[18] Further, ARTC submits that its proposed approach to the Variation Effective Date and commencement date allows for path based pricing to start on 1 January 2019, but allows ARTC to determine this pricing prior to 1 January 2019.[19]

ARTC also proposes to remove section 2.3(d), which was included as part of the June 2017 Variation, which set out the issues and timing of the December 2017 Variation 'package' and forms the basis of the subsequent September 2018 Variation. Section 2.3(d) has been replaced by a separate review mechanism, which is discussed further in chapter 5 of this Decision.

4.2. Comparison to December 2017 Variation

Under section 2.3(b) of the December 2017 Variation, ARTC proposed that the Varied Undertaking would take effect on the first day of the month, which is three full months after the date on which it is approved. This was subject to any review of the ACCC's decision by the Australian Competition Tribunal (**Tribunal**), set out in section 2.3(c), and the treatment of the Compliance Assessment for the 2018 calendar year, set out in section 2.3(d). ARTC did not propose a specific variation commencement date.

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18 ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term*, 28 September 2018, p. 2.

19 Ibid, p. 6.

ARTC submitted that section 2.3(b) of the December 2017 Variation would allow path based pricing to start during 2018 while giving stakeholders sufficient time to prepare for the change, prior to the Undertaking taking effect.[20]

4.3. Comparison to current HVAU

Section 2.3(b) of the current HVAU states that the Varied Undertaking takes effect 21 days after the ACCC publishes its decision to accept the Varied Undertaking under section 44ZZA(3) of the Act (the Variation Effective Date), which was on 29 June 2017. Additionally, all provisions of the Varied Undertaking are taken to have commenced on the Variation Commencement Date, which was 1 July 2017.

Section 2.3(d) of the current HVAU sets out an obligation for ARTC to submit a variation to the HVAU to incorporate path based pricing and an incremental costs methodology that includes a dual ceiling limit. This section forms the basis for ARTC submitting the previous December 2017 Variation and the current September 2018 Variation application to the ACCC for assessment.

4.4. Stakeholder submissions

HRATF previously submitted that there was ambiguity about the proposed Variation Effective Date of the December 2017 Variation for two reasons.

First, HRATF submitted that it is unclear whether ARTC's proposed Variation Effective Date was consistent with the Act.[21] In particular, HRATF noted that the Act did not appear to contemplate an alternative commencement date by agreement. However, HRATF submitted that it did not object to a delayed commencement date if the ACCC considered it legally permissible.[22]

Second, HRATF submitted that it was not clear whether the proposed Variation Effective Date was intended to be the first day of the next month following three months from the commencement date, or the first day of the month that is three months following the commencement date. HRATF understood the drafting in the December 2017 Variation to mean the former.[23]

Pacific National submitted that it understood that the December 2017 Variation was to come into effect on the first day of the month which is three months after the approval date. Pacific National proposed that, for the avoidance of doubt, this date should be confirmed in the ACCC's approval documentation.[24]

HRATF did not specifically refer to ARTC's proposed amendments to the Variation Effective Date and commencement date included in the September 2018 Variation other than to submit that it 'supports the September Variation … and would welcome … a final decision to accept it in order to provide ARTC with the certainty required in order to reflect the amendments in 2019 tariffs.'[25]

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20 ARTC, *2011 Hunter Valley Coal Network Access Undertaking Variation – Explanatory Guide*, 21 December 2017, p. 54.

21 HRATF, *HRATF response to 2011 Hunter Valley Access Undertaking (HVAU) 2017 variation application*, 14 February 2018, p. 8.

22 Ibid.

23 Ibid.

24 Pacific National, *Pacific National Submission to the ACCC in Relation to the ARTC's Proposed Variation to the 2011 HVAU*, February 2018, p. 10.

25 HRATF, *HRATF supplementary submission – September HVAU Variation*, 19 October 2018, p. 1.

Pacific National submits that it has no concerns with the proposed amendments to section 2.3(b) that set out when the September 2018 Variation will be effective, and the provisions will commence, provided the regulatory process is 'concluded in a timely manner'.[26]

4.5. ACCC view

The ACCC considers that a variation to an access undertaking comes into operation in accordance with the statutory timeframe set out in 44ZZBA(4) of the Act, which is:

- 21 days after the Commission publishes its decision to consent to a variation, if no person has applied to the Tribunal for review of the Commission's decision; or
- if a person applies to the Tribunal for review of the Commission's decision and the Tribunal affirms the Commission's decision, the time of the Tribunal's decision.

The ACCC considers section 2.3(b)(i) of the September 2018 Variation is appropriate as it complies with the statutory requirements set out in 44ZZBA(4) of the Act. As the ACCC's Decision was published on 29 November 2018, this means the Variation Effective Date is 20 December 2018 (subject to any appeal to the Tribunal).

The ACCC notes that the current section 2.3(b) and proposed section 2.3(b)(i) of the HVAU inadvertently refer to the ACCC's acceptance under section 44ZZA(3) rather than consent under section 44ZZA(7). The ACCC considers that this is a typographical error and does not affect the interpretation of the provisions relating to the commencement of the undertaking.

The ACCC also considers that section 2.3(b)(ii), which clarifies that all provisions varied by the September 2018 Variation will commence on 1 January 2019, apart from those provisions necessary for ARTC to determine Charges to apply as of 1 January 2019, to be appropriate as it provides administrative certainty for ARTC and access seekers as to the date the relevant amended provisions of the HVAU will commence operation.

The ACCC considers that these amendments, as well as the proposed removal of redundant section 2.3(d), provides for sufficient certainty and clarity in the terms, effect and operation of the HVAU in order to enable ARTC and access seekers to be adequately aware of their respective rights and obligations. This approach avoids unnecessary costs, monetary or otherwise, when utilising the processes set out by the HVAU and provides clarity and certainty for both ARTC and access seekers, which is both in the legitimate business interests of ARTC and the interests of those seeking access to the Hunter Valley rail network (sections 44ZZA(3)(a), (c) and (e)).

Existing agreements and rights

4.6. ARTC proposal

Section 2.4 of the September 2018 Variation sets out the effect of the HVAU on new and existing Access Agreements. ARTC proposes to include an additional condition in relation to the effect of the September 2018 Variation on existing Access Agreements and Access Rights. This proposed addition to section 2.4(a) states that:

> *Subject to an Access Agreement being required to incorporate those clauses from the Indicative Access Holder Agreement identified as Tier 1 (Mandatory) Provisions for Coal Access Rights in Schedule A:1 and Tier 1 (Mandatory) Provisions for Non-Coal Access Rights in Schedule A:2 as applicable, nothing in this Undertaking can require a party to an existing Access Agreement to vary a term or provision of that agreement.*

[26] Pacific National, Pacific National Submission to the ARTC Variation Application to ACCC to Vary the 2011 HVAU, 15 October 2018, p. 3.

ARTC submits that this proposed inclusion clarifies that Access Agreements incorporate the relevant clauses from the IAHA identified as Tier 1 (Mandatory) Provisions for Coal and Tier 1 (Mandatory) Non-Coal Provisions.[27] ARTC notes that path based pricing will be applied to existing Access Agreements through the Tier 1 (Mandatory) Provisions.[28]

ARTC also proposes removing paragraph 2.4(b) from the current HVAU, which set out the reservation of train paths for non-coal traffic around the Commencement Date. ARTC submits that this was a transitional arrangement related to the introduction of the 2011 HVAU.[29]

4.7. Stakeholder submissions

The ACCC did not receive any submissions on these proposed amendments.

4.8. ACCC view

The ACCC considers ARTC's proposed changes to section 2.4 are appropriate on the basis that they provide clarity and certainty to those seeking access to the Hunter Valley rail network, which is also in the interests of access seekers (sections 44ZZA(3)(c) and (e)).

The ACCC notes ARTC's submission that the proposed change to section 2.4(a) clarifies that existing Access Agreements incorporate Tier 1 (Mandatory) Coal and Non-Coal provisions from the IAHA. Further, the ACCC notes that path based pricing (as set out in schedule 3 of the IAHA) forms a Tier 1 (Mandatory) Coal Provision.

Under section 19.1(b)(i) of the IAHA, Access Holders agree that changes or additions to Tier 1 (Mandatory) Provisions resulting from new or varied access undertakings will be automatically incorporated into an AHA. The ACCC considers that ARTC's proposed changes to section 2.4(a) of the HVAU ensures consistency between the HVAU and IAHA. Providing consistency across the HVAU and IAHA provides clarity and certainty to existing Access Holders and access seekers, which the ACCC also considers is to the benefit of those seeking access to the Hunter Valley rail network (sections 44ZZA(3)(c) and (e)).

Similarly, the ACCC considers ARTC's proposed removal of section 2.4(b) on the basis that it is a redundant clause that applied during the transition from the NSWRAU to the 2011 HVAU prevents confusion that might arise from Access Holders or access seekers who might understand that this section remains operative. The ACCC considers that the removal of redundant clauses provides clarity and certainty, which is to the benefit of those seeking access to the Hunter Valley rail network (sections 44ZZA(3)(c) and (e)).

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27 ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term*, 28 September 2018, p. 7.

28 Ibid.

29 Ibid.

5. Floor Contribution and Ceiling Limits

5.1. ARTC proposal

Floor Contribution

Under section 4.2 of the September 2018 Variation, ARTC sets out the Floor Contribution that Access Holders must meet.

For Access Holders that are Constrained Coal Customers from PZ1 or PZ2, the Floor Contribution is equal to the Variable Maintenance Costs they impose when traversing PZ1 and PZ2 and the Incremental Capital Costs they impose traversing PZ1.

For PZ3 Access Holders, the Floor Contribution is equal to the Variable Maintenance Costs they impose when traversing PZ1 and PZ3, plus the Incremental Capital Costs they impose when traversing PZ1.

ARTC submits that it amended section 4.2 to define the concept of Floor Contribution, by reference to the new terminology and concepts of Variable Maintenance Costs and Incremental Capital Costs.[30] These terms are defined as:

- Variable Maintenance Cost – 'maintenance expenditure, including major periodic maintenance that varies with usage'.[31]
- Incremental Capital Cost – 'the capital costs that are reasonably identifiable… as avoidable in the long term'[32], but excludes capital costs incurred before 1 July 2008 and those approved by RCG as fixed costs. Incremental Capital Costs are limited to PZ1 only.
- Fixed Cost – costs '…other than Variable Maintenance Costs and Incremental Capital Costs'. [33]

ARTC also submits that the Floor Contribution is primarily a revenue concept.[34]

Ceiling Limit

Under section 4.3 of the September 2018 Variation, ARTC sets out the Ceiling Limit or maximum revenue that can be recouped from Train Paths operated on behalf of Access Holders. The Ceiling Limit is the Economic Cost of Segments as determined under section 4.5 of the September 2018 Variation (discussed further in chapter 6 of this Decision), required for the provision of any Train Path or group of Train Paths operated on behalf of a relevant Access Holder or group of Access Holders. The ACCC notes that the Economic Cost of Segments is assessed on a stand alone basis. Stand alone basis is not defined in the September 2018 Variation.

ARTC proposes two reconciliations where Access revenue must not exceed the Ceiling Limit. These are for Train Paths traversing:

- PZ1 and PZ2, where these Train Paths are operated on behalf of Access Holders who are Constrained Coal Customers for the PZ1 and PZ2 Constrained Network

30 Ibid, pp. 9–10.

31 Section 14 of the September 2018 Variation.

32 Ibid.

33 Ibid.

34 ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term,* 28 September 2018, p. 10.

- PZ3, where these Train Paths are operated on behalf of Access Holders who are Constrained Coal Customers for the PZ3 Constrained Network.

Currently, PZ3 is not a Constrained Network and a Ceiling Limit does not apply. However, the September 2018 Variation states the PZ3 Ceiling Limit applies when the Regulatory Asset Base (**RAB**) for PZ3 is equal to or less than the RAB Floor Limit for PZ3.[35]

Section 4.3(d) of the September 2018 Variation states that revenue for the purposes of reconciling against a particular Ceiling Limit excludes:[36]

- Access revenue from an Access Holder who is not a Constrained Coal Customer for the relevant Constrained Network to which that Ceiling Limit applies; or
- revenue returned to a Contributor as a result of a user funding agreement between the Contributor and ARTC.

Section 4.8A of the September 2018 Variation sets out how ARTC will reconcile revenue from Constrained Coal Customers in the event PZ3 becomes a Constrained Network. ARTC states this section has been included 'to make clear that there is a reconciliation between Access revenue and Economic Cost in the Compliance Assessment'.[37]

First, under section 4.8A(b), ARTC proposes the Floor Contribution of PZ3 Access Holders traversing the PZ1/2 Constrained Network is removed from the Economic Cost of the PZ1/2 Constrained Network. This Floor Contribution is not added to the Economic Cost of PZ3.

Second, under section 4.8A(c), in allocating and reconciling Access revenue from a PZ3 Access Holder, ARTC proposes it must:

- *first allocate and recover an amount of Access revenue equal to the Floor Contribution for each Segment traversed by that Pricing Zone 3 Access Holder and, for Segments in Pricing Zone 1, such Access revenue is to be allocated and recovered outside any Ceiling Limit and is not further taken into account for the purpose of reconciling Access revenue against the Ceiling Limit for either the PZ1/2 Constrained Network or the PZ3 Constrained Network;*
- *not allocate Access revenue to a Segment in Pricing Zone 1 in excess of the Floor Contribution for that Segment for that Pricing Zone 3 Access Holder; and*
- *allocate remaining Access revenue to Segments in Pricing Zone 3 for the purpose of determining compliance with any Ceiling Limit for those Segments in Pricing Zone 3.*

ARTC submits that the proposed amendments to introduce two separate Ceiling Limits reflects the introduction of Incremental Capital Costs from the ACCC's 2013 Annual Compliance Final Determination.[38]

Under a new provision at section 2.3(d) of the September 2018 Variation, ARTC notes that its proposed separate Ceiling Limit and Constrained Network for PZ3 is not to be taken as the mechanism that will be included beyond the current term of the HVAU. ARTC will review the terms that apply to a revised undertaking after the expiry of the current term, having

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35 Section 4.3(c) of the September 2018 Variation.

36 Contributor is defined under section 10.1 of the September 2018 Variation, unchanged from the 2011 HVAU.

37 ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term,* 28 September 2018, p. 15.

38 Ibid, p. 10.

regard to whether the proposed pricing approach is appropriate for all stakeholders after loss capitalisation in PZ3 ends.

ARTC submits that section 2.3(d) was developed in consultation with HRATF, and:[39]

> *…commits ARTC to consulting on the appropriate economic ceiling model to apply for future versions of the HVAU as part of its engagement ahead of the renewal or replacement of the HVAU from 1 January 2022.*

5.2. Comparison to the December 2017 Variation

ARTC's proposed approach to the Floor Contribution and Ceiling Limits in the September 2018 Variation is largely the same as that in the December 2017 Variation. The December 2017 Variation did not include a mechanism for reviewing the approach to Ceiling Limits and the Constrained Network for PZ3 for a future revised HVAU. However, prior to its withdrawal of the December 2017 Variation, ARTC notified the ACCC that it intended to include the review mechanism set out in section 2.3(d) of the September 2018 Variation.[40]

In setting out its proposal, ARTC noted that the development of this proposed section followed a workshop on 30 April 2018 between ARTC, HRATF producers and the ACCC. ARTC submitted that it will:[41]

> *…engage with its customers in respect of the effectiveness and efficiency of the operation of the HVAU to ensure it has maximized the ability to achieve stakeholder consensus of any renewed HVAU submitted to the ACCC for approval to replace the current HVAU on its expiry.*

ARTC noted its expectation that the review will commence in the second half of 2019. However, ARTC submitted that the timing and scope would 'become clearer at the relevant time'.[42]

5.3. Comparison to the current HVAU

Floor Contribution

The ACCC understands that the main differences between ARTC's proposed approach to the Floor Contribution in the September 2018 Variation and the Floor Revenue Limits in the current HVAU relate to explicitly setting out the Floor Contribution that Access Holders originating from PZ1, PZ2, PZ3 and outside the Hunter Valley rail network contribute to a Train Path.

Under the current HVAU, the Floor Revenue Limit states that every Access Holder must at least meet its Direct Cost of using the Network.[43] The current HVAU also states that Access revenue from Access Holders should meet the Incremental Cost of a Segment or group of Segments. This objective has been expanded in the September 2018 Variation.

The September 2018 Variation also includes changes to defined terms, reflecting the revised definition of costs (discussed further in chapter 6 of this Decision).

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39 Ibid, p. 2.

40 ARTC, *Re: December 2017 HVAU Variation,* 23 May 2018, p. 1.

41 Ibid.

42 Ibid, p. 2.

43 'Direct cost' is defined in section 6.3 of this Decision.

Ceiling Limits

Broadly, the main differences between the current HVAU and September 2018 Variation relate to:

- defining two Constrained Networks and Ceiling Limits
- Access revenue only being reconciled against one Ceiling Limit[44]
- PZ3 Access Holders only paying the Incremental Capital Cost and Variable Maintenance Cost of their usage of PZ1, both when constrained and unconstrained.[45]

As noted previously, ARTC submits that the proposed amendments to introduce two separate Ceiling Limits reflects the introduction of Incremental Capital Costs from the ACCC's 2013 Annual Compliance Final Determination.[46] In the 2013 Annual Compliance Final Determination, the ACCC determined that PZ3 producers should contribute their Incremental Cost (including maintenance and capital) for traversing PZ1. Previously, PZ3 producers only contributed Direct Costs (a subset of Incremental Cost) when traversing PZ1.[47]

In its explanatory guide to the December 2017 Variation, ARTC submitted that the current HVAU already incorporates a dual ceiling through:[48]

- *The reconciliation of Access revenue with the Ceiling Limit for the Constrained network and subsequent overs and unders accounting process for Constrained Coal Customers;*
- *Access revenue from Pricing Zone 3 Access Holders being applied to meet their Variable Maintenance Costs and Incremental Capital Costs in Pricing Zone 1 and the determination of the RAB for Pricing Zone 3 whilst Pricing Zone 3 is economically constrained.*

5.4. Stakeholder submissions

HRATF supports the inclusion of section 2.3(d) in the September 2018 Variation:[49]

> *to make clear that the approach taken by any economic ceiling model (and all other aspects of the current pricing structure) will be a matter reviewed by ARTC in the course of the 2022 HVAU process, having regard to the loss capitalisation position in Pricing Zone 3 at the time.*

In its supplementary submission to the December 2017 Variation, HRATF noted that its support for the package of amendments, including ARTC's proposed approach to the Floor Contribution and Ceiling Limits, was limited to when loss capitalisation was in place in PZ3.[50] In particular, HRATF submitted that it did not necessarily accept that the proposed tariff framework would continue to be appropriate once the entire Hunter Valley rail network becomes constrained.[51]

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44 Section 4.8A(d) of the December 2017 Variation.

45 Section 4.8A(b) of the December 2017 Variation.

46 ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term,* 28 September 2018, p. 10.

47 ACCC, *Final determination: Australian Rail Track Corporation's compliance with the Hunter Valley coal network access undertaking financial model for the 2013 calendar year*, 6 June 2016, pp. 5–6.

48 ARTC, *2011 Hunter Valley Coal Network Access Undertaking Variation – Explanatory Guide*, 21 December 2017, p. 19.

49 HRATF, *HRATF supplementary submission – September HVAU Variation,* 19 October 2018, p. 2.

50 HRATF, *HRATF supplementary submission*, 30 May 2018, p. 2.

51 Ibid.

HRATF noted that a number of HRATF members would object to continuing the proposed Floor Contribution and Ceiling Limits model once the PZ3 loss capitalisation account has been paid down.[52]

HRATF also stated in its supplementary submission that ARTC had provided assurances that it does not expect that the loss capitalisation balance will be repaid prior to the end of the current term of the HVAU. HRATF submitted that it accepted these assurances.[53] As a result, HRATF considered that any discussion about the pricing approach to apply after the loss capitalisation balance has been paid down should occur as part of the assessment of the next HVAU.[54]

Pacific National submits that it ‘has no major concerns’ with the proposed drafting of section 2.3(d) of the September 2018 Variation.[55] However Pacific National submits that this review mechanism should allow for consultation with third parties including Access Holders, access seekers and operators.[56]

5.5. ACCC view

The ACCC notes that ARTC’s proposed approach to calculating and reconciling the Floor Contribution and Ceiling Limits is largely the same as that proposed in the December 2017 Variation. Accordingly, the ACCC has taken into consideration HRATF’s submissions to the December 2017 HVAU that the majority of its members support ARTC’s proposed approach to the Floor Contribution and Ceiling Limits as it is part of an agreed package.[57]

The ACCC also notes that, consistent with its stated intention prior to withdrawing the December 2017 Variation, ARTC has included a review mechanism relating to the proposed pricing approach set out in the September 2018 Variation. This review mechanism is supported by both stakeholder submissions to the September 2018 Variation.[58]

Consistent with the view presented in the Draft Decision on the December 2017 HVAU, the ACCC considers that ARTC’s proposed approach to the Floor Contribution and Ceiling Limits is appropriate for the duration of the current HVAU. This is on the basis that it is endorsed by the majority of stakeholders who submit that it provides a package of changes preferable to the current HVAU (section 44ZZA(3)(e)). The ACCC is confident that stakeholders are aware of the implications of the variation on the calculation and reconciliation of the Ceiling Limits once PZ3 becomes constrained.

However the ACCC continues to have concerns regarding ARTC’s proposed approach to calculating and reconciling the Floor Contribution and Ceiling Limits. The ACCC outlined these concerns in the Draft Decision on the December 2017 HVAU.[59] A summary of the ACCC’s key concerns with the Floor Contribution and Ceiling Limits provided below.

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52 Ibid.

53 Ibid.

54 Ibid.

55 Pacific National, *Pacific National Submission to the ARTC Variation Application to ACCC to Vary the 2011 HVAU,* 15 October 2018, p. 2.

56 Ibid.

57 HRATF, *HRATF response to 2011 Hunter Valley Access Undertaking (HVAU) 2017 variation application*, 14 February 2018, p. 11; HRATF, *HRATF supplementary submission*, 30 May 2018, p. 2.

58 See HRATF, *HRATF supplementary submission – September HVAU Variation,* 19 October 2018 and Pacific National, *Pacific National Submission to the ARTC Variation Application to ACCC to Vary the 2011 HVAU,* 15 October 2018.

59 See ACCC, *Draft Decision – Australian Rail Track Corporation’s December 2017 Variation to the 2011 Hunter Valley Access Undertaking,* 28 June 2018, pp. 34–8.

Floor Contribution

ARTC's proposed definition of Incremental Capital Costs suggest that these costs only apply in PZ1, and are therefore not included in the calculation of the Floor Contribution for PZ3 Access Holders in PZ3.[60] However, ARTC has not provided evidence to suggest that there are no Incremental Capital Costs in PZ3. If it is the case that there are Incremental Capital Costs in PZ3, the proposed definition of the Floor Contribution in PZ3 suggests that PZ3 Access Holders are not contributing to these costs. As a result, the ACCC considers that ARTC's proposed definition of the Floor Contribution in PZ3 is too low, which introduces a cross subsidy in order for ARTC to recover the Floor Contribution in PZ3. This, in turn, leads to the economically inefficient operation of, use of and investment in the Network (section 44ZZA(3)(aa)).

Ceiling Limits

When the proposed approach to Ceiling Limits becomes effective

The ACCC and Access Holders outside of PZ3 are not privy to the terms of repayment of the loss capitalisation account. There is therefore some uncertainty regarding when the loss capitalisation account will be repaid and thus when PZ3 will be constrained. Further, if PZ3 is not going to become constrained during the current term of the HVAU, it is unclear to the ACCC why section 4.8A has been included as part of the September 2018 Variation. This is particularly the case given section 2.3(d) states that the proposed mechanism is not necessarily the mechanism that will be adopted in the next HVAU.

The Floor Contribution and Ceiling Limits proposal

The ACCC notes ARTC's December 2017 Variation application submits that the Floor Contribution and Ceiling Limits proposal is intended to incorporate the principles set out in the 2013 Annual Compliance Final Determination.[61] However, the ACCC does not consider that the 2013 Annual Compliance Final Determination necessitates ARTC's proposed approach when PZ3 becomes constrained. Further, the ACCC considers that ARTC has not provided a clear rationale for its proposal.

PZ3's contribution to costs in PZ1 once PZ3 becomes constrained

Currently, PZ3 Access Holders do not contribute to Fixed Costs for Segments traversed in PZ1. Under the proposed approach in the September 2018 Variation, PZ3 would continue to not contribute to Fixed Costs in PZ1 once it becomes constrained. However, PZ3 Access Holders currently are (and will continue to be) charged a TOP Charge intended to recover Fixed Costs in PZ1. The ACCC is concerned that this will lead to PZ1 revenue exceeding the stand alone cost ceiling in PZ1. In addition, the ACCC understands that the revenue from PZ3 Access Holders' contribution to a portion of TOP Charges in PZ1 is then transferred back to PZ3 prior to the reconciliation of revenue for the purpose of the Ceiling Limit tests. The ACCC considers ARTC's propose approach could lead to cross subsidisation and the economically inefficient operation of, use of and investment in the Network (section 44ZZA(3)(aa)).

Review mechanism

The ACCC notes HRATF's submission that the proposed review mechanism provided comfort for all stakeholders, and formed part of HRATF's support for the December 2017 Variation.[62] However, the ACCC considers that there is some ambiguity about the scope and

[60] This is additionally the case in PZ2.

[61] ARTC, *2011 Hunter Valley Coal Network Access Undertaking Variation – Explanatory Guide*, 21 December 2017, p. 16.

[62] HRATF, *HRATF supplementary submission*, 30 May 2018, p. 2.

timing of the review mechanism set out in section 2.3(d). ARTC submits that 'further details on timing and scope will become clearer at the relevant time'[63], but states that the review would commence in the second half of 2019.[64]

The ACCC notes that as drafted, the review will include but is not limited to, 'the current pricing approach'.[65] The ACCC considers that it is unclear which sections of the September 2018 Variation are included in the 'current pricing approach'.

The ACCC also notes that the results of the review are not binding on ARTC. Although the review relates to the approach to be taken after loss capitalisation in PZ3 ends, there is no obligation for ARTC to make any changes to the approach set out in the September 2018 Variation. There is also no obligation to publish the results of the review, or take them into account as part of the development of the next HVAU.

Consistent with the above concerns regarding ARTC's proposed approach to the Floor Contribution, the ACCC considers that the review should include an assessment of the categories of costs that apply in each Pricing Zone. Additionally, the ACCC considers the review should include consideration of how ARTC determines Access Charges for Services that use adjoining networks. This issue is discussed further in chapter 9 of this Decision.

The ACCC notes that ARTC proposed an opex efficiency mechanism as part of the 2017 HVAU. The ACCC expected this mechanism to form a key component of the replacement to the 2011 HVAU. ARTC has not incorporated a similar mechanism into any of its variation applications since withdrawing the 2017 HVAU. As an opex efficiency mechanism could have implications for pricing, the ACCC considers this should be an issue for consideration in the review.

Along with incorporating the results of the review into the next HVAU, the ACCC considers ARTC should incorporate amendments proposed in the 2016 HVAU and 2017 HVAU, which had the support of stakeholders, and which the ACCC had accepted in the Draft Decision on the 2017 HVAU. These outstanding issues are outlined in chapter 12 of this Decision.

The ACCC notes Pacific National's submission that ARTC should consult with Access Holders, access seekers and operators in undertaking its review. The ACCC also notes HRATF's submission that a number of its members would object to continuing the proposed Floor Contribution and Ceiling Limits proposal once the PZ3 loss capitalisation balance has been paid down.[66]

The ACCC expects that ARTC will consult with all stakeholders on the scope of the review, using stakeholder submissions as guidance for the issues considered. Further, the ACCC expects that ARTC will commence this process with sufficient time for the results of the review to be incorporated into ARTC's application for the next HVAU. The ACCC considers that ARTC should publish the results of its review of the current pricing approach ahead of the submission of the next HVAU application to the ACCC, and indicate how it has drawn upon this review in its submission to the ACCC. The ACCC considers that this would be in the interests of clarity and certainty for all relevant stakeholders in relation to negotiations for the next HVAU (section 44ZZA(3)(e)). Further, ARTC should submit its application for any replacement undertaking with sufficient time to avoid a regulatory gap, or the threat of a regulatory gap, between the expiry of the existing HVAU and the commencement of a new undertaking.

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63 ARTC, *Re: December 2017 HVAU Variation,* 23 May 2018, p. 2.

64 Ibid, p. 1.

65 Ibid.

66 HRATF, *HRATF supplementary submission*, 30 May 2018, p. 2.

6. Economic Cost

6.1. ARTC proposal

Section 4.5 of the September 2018 Variation sets out the method for determining the Economic Cost of Segments and its allocation to Access Holders as part of the Compliance Assessment process. This method encompasses four parts:

- initial make-up of costs, depreciation and return on assets to Segments
- allocating these costs to Variable Maintenance Costs, Incremental Capital Costs and Fixed Costs
- allocating Variable Maintenance Costs and Incremental Capital Costs to Access Holders
- costs excluded from Segments.

In addition, the September 2018 Variation includes:

- a method of determining and allocating Non-Segment Specific Costs
- a new role for RCG in relation to the allocation between Incremental Capital Costs and Fixed Costs. This is discussed in further detail in chapter 0 of this Decision.

Initial make-up of costs, depreciation and return on assets

Section 4.5(a) of the September 2018 Variation sets out the initial make-up of the Economic Cost into the following categories:

- **Segment Specific Costs**, which are the operating costs that ARTC can directly identify with a Segment (including losses or gains incurred on an asset's disposal)
- **depreciation of Segment Specific Assets**, the value of which is determined in accordance with section 4.4(b)
- **a return on Segment Specific Assets**, being determined by applying the real pre-tax Rate of Return (**ROR**) to (RAB Floor Limit$_{t-1\ start}$ + RAB Floor Limit$_{t-1\ end}$)*0.5, where the value of the RAB Floor Limit is determined in accordance with section 4.4(b)
- an allocation of **Non-Segment Specific Costs**
- an allocation of **depreciation of Non-Segment Specific Assets**, determined on a straight line basis, by reference to a reasonable estimate of the economic useful life of Non-Segment Specific Assets, and determined from the time the assets become serviceable
- an allocation of **return on Non-Segment Specific Assets**, being determined by applying a real pre-tax ROR to the value of Non-Segment Specific Assets, from the time the assets become serviceable, capitalised at that time and determined by reference to the relevant ROR.

These costs are assessed on a stand alone and Efficient basis.

Allocating to Variable Maintenance Costs, Incremental Capital Costs and Fixed Costs

The September 2018 Variation then defines and seeks to allocate costs, depreciation and return on assets into the following three categories:

- **Variable Maintenance Costs,** which is defined as 'maintenance expenditure, including major periodic maintenance that varies with usage'.[67]
- **Incremental Capital Costs,** which is limited to PZ1 and defined as 'the capital costs that are reasonably identifiable…as avoidable in the long term'[68], but excludes capital costs incurred before 1 July 2008 and those approved by RCG as Fixed Costs.
- **Fixed Costs,** which is defined as costs 'other than Variable Maintenance Costs and Incremental Capital Costs'.[69]

Under section 4.5(d)(i) of the September 2018 Variation, ARTC will determine whether Segment Specific Costs and Non-Segment Specific Costs are Variable Maintenance Costs and/or Fixed Costs. ARTC proposes to allocate between these costs 'having regard to the purpose, causal factors, and cost drivers for the projects or costs as reasonably determined by an engineering assessment'.[70]

Under section 4.5(d)(ii) of the September 2018 Variation, ARTC will determine whether depreciation and return on Segment Specific Assets and Non-Segment Specific Assets are Incremental Capital Costs and/or Fixed Costs. Where:

- 'capital costs incurred before 1 July 2008 are taken to be Fixed Costs'[71]
- 'for Sustaining Capital incurred on or after 1 July 2008, ARTC must determine the Capital Allocation (between Incremental Capital Costs and Fixed Costs) in accordance with section 9.8 and include it in the Compliance Assessment for the year in which they are included in the asset base'[72]
- 'for Expansion Capital incurred on or after 1 July 2008, ARTC must seek endorsement of the Capital Allocation (between Incremental Capital Costs and Fixed Costs) in accordance with section 9.9'[73]

ARTC defines Expansion Capital as 'Capital Expenditure in relation to a Project that provides Additional Capacity'[74], with Sustaining Capital being 'Capital Expenditure that is not Expansion Capital'.[75] The treatment of Expansion and Sustaining Capital in relation to the RCG endorsement process is discussed further in chapter 0 of this Decision.

Allocating to Access Holders

Section 4.5(f) of the September 2018 Variation sets out ARTC's approach for allocating Incremental Capital Costs and Variable Maintenance Costs between Access Holders. Where:

- Incremental Capital Costs are allocated on the basis of either Contracted Coal GTK or Contracted Coal Km
- Variable Maintenance Costs are allocated on the basis of either GTK (weighted for axle load) or Train Km.

67 Section 14 of the September 2018 Variation.
68 Ibid.
69 Ibid.
70 Section 4.5(e)(iv) of the September 2018 Variation.
71 Section 4.5(e)(i) of the September 2018 Variation.
72 Section 4.5(e)(ii) of the September 2018 Variation.
73 Section 4.5(e)(iii) of the September 2018 Variation.
74 Section 14 of the September 2018 Variation.
75 Ibid.

In allocating costs between Variable Maintenance Costs, Incremental Capital Costs and Fixed Costs and then to Access Holders, under section 4.5(g) of the September 2018 Variation, ARTC proposes that:

- 'the same Capital Allocation should be consistently used for projects of Capital Expenditure of a similar nature or purpose'[76]
- 'once a particular Capital Allocation for a particular project or category of Capital Expenditure has been assessed as compliant by the ACCC, it will not be reviewed in future Compliance Assessments and will continue to apply for the life of that project or Capital Expenditure'[77]
- 'once a particular variable proportion or allocation method for a particular category of maintenance expenditure has been assessed as compliant by the ACCC, that variable proportion and allocation method will be used for similar categories of maintenance expenditure'[78]
- 'if the RCG endorses a Capital Allocation under section 9, then that Capital Allocation will be applied for the relevant Compliance Assessment and will continue to apply for the life of the Capital Expenditure or relevant project'.[79]

Under section 4.5(i) of the September 2018 Variation, ARTC will maintain a Historical Capital Allocation List. This list includes the projects or Capital Expenditure that the RCG has endorsed, or the ACCC has approved, a particular capital allocation for. It will include:

- the applicable Capital Allocation
- a summary of an engineering assessment (if applicable)
- the purpose, causal factors and cost drivers identified as relevant to the choice of Capital Allocation.

The objective of the Historical Capital Allocation List is to identify the appropriate Capital Allocation for future projects or Capital Expenditure which have a similar nature or purpose to those in the list. ARTC must provide the list to the RCG after each update and to Access Holders or the ACCC on request. ARTC submits that the purpose of the Historical Capital List is to assist with future allocations and endorsements.[80]

Costs excluded from the Economic Cost of a Segment

Under section 4.5(h) of the September 2018 Variation, ARTC seeks to exclude the following when determining the Economic Cost of a Segment:

- Variable Maintenance Costs by Access Holders that do not hold Coal Access Rights
- Variable Maintenance Costs by Access Holders holding Coal Access Rights and who are not Constrained Coal Customers
- for Segments in PZ1, the Incremental Capital Costs imposed by PZ3 Access Holders.

Non-Segment Specific Costs and Assets

In regards to the allocation of Non-Segment Specific Costs, and depreciation of, and return on, Non-Segment Specific Assets to Segments and Access Holders, section 4.6 of the

76 Section 4.5(g)(i) of the September 2018 Variation.

77 Section 4.5(g)(ii) of the September 2018 Variation.

78 Section 4.5(g)(iii) of the September 2018 Variation.

79 Section 4.5(g)(iv) of the September 2018 Variation.

80 ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term,* 28 September 2018, p. 15.

September 2018 Variation states these will be allocated directly to a Segment where possible. Where this is not possible, costs will be allocated in accordance with Schedule I. The ACCC notes Schedule I is a part of the current HVAU and is not a proposed change under the September 2018 Variation. However, the ACCC considers it a key component in determining the Economic Cost of Segments under the September 2018 Variation.

Schedule I sets out three steps for allocating Non-Segment Specific Costs, depreciation of, and return on, Non-Segment Specific Assets. These are identifying and allocating costs between:

- ARTC's Interstate and Hunter Valley businesses
- coal and non-coal Access Holders
- Segments.

First, ARTC initially identifies and allocates costs between the Hunter Valley rail network and its other businesses (including the Interstate rail network). If the cost is exclusively identifiable with the Hunter Valley rail network, ARTC will allocate it to the Hunter Valley rail network.

If not exclusively identifiable with the Hunter Valley rail network, ARTC will allocate a proportion of the cost categories with the corresponding allocators, set out in Table 2Table 2:. ARTC will identify the share of a cost category attributed to the Hunter Valley rail network by calculating its share of the relevant allocator, over the total of that allocator (where the total of that allocator includes costs attributed to the Hunter Valley rail network as well as ARTC's other businesses).

Table 2: Allocation methods

Cost category	Allocation method	Cost category	Allocation method
Executive	Direct Stay-in-Business Costs[81]	Information Technology infrastructure & systems	FTE
Finance	Direct Stay-in-Business Costs	Management of enterprise services	Direct Stay-in-Business Costs
Strategy & corporate development	Train Km	Environment	Train Km
People	FTE	Engineering services	GTK
Insurance	Premium based	Corporate safety	GTK
Safety accreditation	Track Km	Workplace health & safety	FTE
Property	Track Km	Risk	GTK
Communications	Train Km	Allowance for efficiency projects	Direct Stay-in-Business Costs

Note abbreviations: Train Kilometres (Train Km); Full Time Equivalent (FTE); Track Kilometres (Track Km).
Source: Schedule I of the September 2018 Variation and current HVAU.

By example, ARTC identifies the share of the Hunter Valley rail network in the 'Executive' cost category by first calculating the share of Direct-Stay-in-Business Costs attributed to the Hunter Valley rail network as a function of the Direct-Stay-in-Business Costs attributed to all its businesses, or:

$$Executive_{Hunter\ Valley\ rail\ network} = \frac{Direct\text{-}Stay\text{-}in\text{-}Business\ Costs_{Hunter\ Valley\ rail\ network}}{Direct\text{-}Stay\text{-}Business\ Costs_{All\ ARTC\ businessess}}$$

Second, after ARTC has identified the share of the Hunter Valley rail network (under step 1), ARTC will allocate to its Coal Customers in the Hunter Valley rail network as follows:

- Where it is associated with indirect maintenance and indirect operational costs, ARTC will allocate based on the proportion that the GTK for its Coal Customers bears to the GTK for the entire Hunter Valley rail network.
- Where it is not associated with indirect maintenance and indirect operational costs, ARTC will allocate based on the proportion that the Direct-Stay-in-Business Costs for its Coal Customers bears to the Direct-Stay-in-Business Costs for the entire Hunter Valley rail network.

Third, after ARTC has identified the share of costs allocated to its Coal Customers in the Hunter Valley rail network (under step 2), ARTC will allocate to Segments as follows:

- Where it is associated with maintenance, ARTC will allocate based on the proportion that the GTK for a Segment bears to the GTK for the Network.

[81] Defined under Schedule I as costs identifiable with the function of a corridor, or part of a rail network, being the operating and maintenance expenses plus corridor capital, non-infrastructure capital and incidents, but excluding indirect management labour and capital for the purpose of increasing capacity and performance.

- Where it is not associated with maintenance, ARTC will allocate based on the proportion that the Train Km for a Segment bears to the Train Km for the Network.

As noted above, the proposed cost allocators at the Segment level (step 3) are unchanged from those in the current HVAU.

6.2. Comparison to December 2017 Variation

The approach to Economic Cost in the September 2018 Variation is largely the same as that in the December 2017 Variation. However, the December 2017 Variation did not include the concepts of Sustaining and Expansion Capital. Further, the December 2017 Variation did not include ARTC's proposed Historical Capital Allocation List.

In its December 2017 Variation application, ARTC stated that the overall benefits of its proposed approach to the allocation of Economic Cost were:[82]

- *it provides price structure stability;*
- *it makes the majority of the price known by way of the magnitude of the TOP charge in the price makeup, ahead of annual production decisions;*
- *it removes the short and medium run production decisions of competitors as a variable in the below rail cost function of other Access Holders; and*
- *provides certainty in the treatment of Incremental Capital Costs throughout the term of the HVAU.*

ARTC submitted that it proposed this method to incorporate the 2013 Annual Compliance Final Determination (the findings of which are presented in Box 1). In particular, ARTC stated the approach used in the 2013 Annual Compliance Final Determination to:[83]

> *…assess the purpose, causal factors and cost drivers in order to determine the proportion of costs that are Variable Maintenance Costs and Incremental Capital Costs based on an engineering assessment has been embedded in the HVAU.*

In addition, ARTC stated:[84]

> *…precedents set for the variable / incremental proportion of costs and the allocator (ie GTK or [Train Km]) for apportioning those costs to relevant Access Holders in a compliance assessment will apply to ongoing for projects/costs of a similar nature.*

ARTC proposed one change to the 2013 Annual Compliance Final Determination. That is, allocating Incremental Capital Costs based on contracted commitments rather than actual use. ARTC outlined the following two reasons for this:

- changing the share of TOP and non-TOP Charges; and
- the causation of capital investment.

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82 ARTC, *2011 Hunter Valley Coal Network Access Undertaking Variation Explanatory Guide,* 21 December 2017, pp. 5–6.

83 Ibid, p. 17.

84 Ibid.

Box 1: 2013 Annual Compliance Final Determination

The 2011 HVAU provides for the ACCC to conduct an annual assessment to determine whether ARTC has correctly calculated the revenue floor and ceiling limits and reconciled these with revenues received from Access Holders to determine any 'unders and overs' amount (that is, whether ARTC is entitled to receive additional revenues or is required to refund monies to Access Holders).

In the course of assessing ARTC's compliance with the 2011 HVAU for the 2013 calendar year, the ACCC identified some concerns with ARTC's method for allocating costs used in the calculation of the revenue ceiling limits for reconciliation of revenue received from Access Holders. In particular, ARTC proposed that the proportion of the Prudent and Efficient costs incurred within the Constrained Network to be reconciled with revenues received from Constrained Coal Customers should be calculated by subtracting the Direct Costs (a subset of incremental costs) associated with coal producers originating in PZ3 from the costs of the Constrained Network.[85] The ACCC considered that Incremental Costs, rather than Direct Costs, should be subtracted.

The ACCC was concerned that ARTC's approach led to it overstating the proportion of costs and resulting shortfall in revenue to be recovered from Constrained Coal Customers and that they were being asked to pay more than their stand alone costs.

As part of the 2013 Compliance Assessment, the ACCC engaged an independent consultant, WIK-Consult (**WIK**), to review the costs of ARTC's Hunter Valley Coal Network and estimate the Incremental Costs of PZ3 Access Holders' use of PZ1. Under the WIK methodology, Incremental Costs attributed to each Access Holder or group of Access Holders were allocated using actual volumes.

On 6 June 2016, the ACCC released its Final Determination for the 2013 Annual Compliance assessment. The ACCC determined that PZ3 Access Holders should at least contribute their Incremental Costs (including maintenance and capital costs) for traversing PZ1. Further, the ACCC found that Incremental Costs should be determined using the WIK methodology that applies actual volumes, which represents Access Holders' actual usage of the network and cost causation.

First, ARTC submitted that a consequence of the 2013 Annual Compliance Final Determination regarding the allocation of Incremental Capital Costs on actual use was:[86]

> *…the relativity between the TOP and Non-TOP components of the access charges has changed in Pricing Zone 1. The TOP charge has historically been in the order of 85-90% of the access charges, however pricing reflecting the outcome of the 2013 compliance decisions has resulted in the TOP charge reducing to approximately 50% of the Pricing Zone 1 access charges. Access Holders are now exposed to volume reductions of other Access Holders which leads to a high degree of price uncertainty through the unders and overs process.*

Second, ARTC considered that the allocation of Incremental Capital Cost on actual usage is inconsistent with the causation of investment. In particular:[87]

> *Decisions to fund incremental capacity are made based upon forecasts of future network utilisation which were underpinned by contractual commitments at the time of the investment. The critical causal factor for the capital investment is therefore the contracted volume. Use of a contractual allocator for this cost provides a direct causal link and a clear financial incentive to ensure that the contracted capacity most efficiently reflects the volume needs of the Access Holder.*

[85] 'Direct Cost' is defined in section 6.3 of this Decision.

[86] ARTC, *2011 Hunter Valley Coal Network Access Undertaking Variation Explanatory Guide,* 21 December 2017, p. 17.

[87] Ibid, p. 18.

6.3. Comparison to current HVAU

Initial make-up of costs, depreciation and return on assets

Section 4.5(a), which sets out the initial make-up of the Economic Cost of a Segment, is unchanged between the current HVAU and September 2018 Variation. In addition, both the current HVAU and September 2018 Variation state costs are to be assessed on a stand alone and Efficient basis.

Allocating to cost components

A difference between the current HVAU and the September 2018 Variation is the allocation of the components of the Economic Cost of a Segment. As previously stated, the September 2018 Variation defines and allocates costs as Variable Maintenance Costs, Incremental Capital Costs or Fixed Costs.

In contrast, section 4.13(a) of the current HVAU defines the following costs:

- Variable component of costs, which is Direct Costs. Direct Costs are defined as:[88]

> *…maintenance expenditure, including major periodic maintenance that varies with usage of the Network, and may include other costs that vary with the usage of the Network but excluding Depreciation, assessed on an Efficient basis*

- new capital component of costs, which is Depreciation of, and return on, assets commissioned during the Term; and
- fixed component of costs, which is fixed operating costs and Depreciation of, and return on, assets existing as at the Commencement Date and the New Segments Commencement Date (as applicable).

Allocating to Access Holders and Segments

Unlike the September 2018 Variation, the current HVAU does not set out how costs are allocated to Access Holders and Segments. In particular, the current HVAU does not explicitly set out the allocation method for Incremental Capital Costs.

Non-Segment Specific Costs and Assets

Both the current HVAU and September 2018 Variation use the same method for determining and allocating Non-Segment Specific Costs and depreciation of, and return on, Non-Segment Specific Assets to Hunter Valley coal Access Holders and Segments. This method is set out in Schedule I of the current HVAU and September 2018 Variation.

6.4. Stakeholder submissions

The ACCC received no submissions that specifically addressed ARTC's proposed approach to Economic Cost in the September 2018 Variation. The ACCC notes that submissions in relation to Expansion and Sustaining Capital are summarised in chapter 0 of this Decision.

As noted above, ARTC's proposed approach to Economic Cost is largely the same as that proposed in the December 2017 Variation. Accordingly, the ACCC has taken into account relevant submissions from previous HVAU assessment processes, including the December 2017 Variation, in forming its view.[89] In particular, the ACCC notes HRATF's supplementary

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[88] Section 14 of the 2011 HVAU.

[89] See ACCC, *Draft Decision – Australian Rail Track Corporation's December 2017 Variation to the 2011 Hunter Valley Access Undertaking,* 28 June 2018, pp. 48-50.

submission to the December 2017 Variation that stated the majority of its members supported the overall 'package' of changes proposed as preferable to the alternative–being the HVAU continuing in its current form until the end of its term.[90] This view is reflected in HRATF's submission to the September 2018 Variation, when HRATF endorses the ACCC approving the application.[91]

In its submission to the December 2017 Variation, Anglo American's stated that it did not support the changes to the allocation of Incremental Capital Costs.[92] The ACCC understands that Anglo American has since completed the sale of its coal assets in the Hunter Valley.[93]

6.5. ACCC view

The ACCC notes the majority of industry submitted their support for ARTC's proposed amendments in respect of Economic Cost in the December 2017 Variation. These amendments have been reflected in the subsequent September 2018 Variation. Additionally, no stakeholder submitted on this specific issue in consultation on the September 2018 Variation. On the basis that the majority of industry agreed to the proposal as part of the package of amendments in the December 2017 Variation, which was adopted in the September 2018 Variation, the ACCC considers the proposed changes to allocating the Economic Cost of a Segment are appropriate. This is because they form part of a negotiated commercial agreement between ARTC and industry for the duration of the current HVAU (section 44ZZA(3)(e)).

Although the proposal has support from the majority of industry for a number of different reasons, the ACCC has the following concerns with ARTC's proposed approach, which relate to the:

- treatment of Non-Segment Specific Costs
- allocation of Incremental Capital Costs to Access Holders.

These concerns are consistent with the concerns set out in the Draft Decision for the December 2017 Variation, and are summarised below.[94]

Treatment of Non-Segment Specific Costs

The ACCC considers that ARTC has not provided evidence to support its proposed approach to allocating Non-Segment Specific Costs between Access Holders and between the Hunter Valley rail network and ARTC's other businesses.

The ACCC notes that ARTC has not provided evidence in support of the cost allocators in Schedule I of the September 2018 Variation, unchanged from the current HVAU. ARTC initially proposed these cost allocators in the June 2017 Variation, which the ACCC consented to as it had the strong support of the majority of stakeholders. However ARTC has not provided sufficient explanation about the demand for work done by these cost categories (overhead resources consumed and overhead costs caused by the Hunter Valley operations), including:

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90 HRATF, *HRATF supplementary submission*, 30 May 2018, p. 2.

91 HRATF, *HRATF supplementary submission – September HVAU Variation,* 19 October 2018, p. 2.

92 Anglo American, *Submission to the Australian Competition and Consumer Commission: December 2017 Variation to Hunter Valley Access Undertaking*, 13 February 2018, p. 7.

93 Anglo American, Media release, 'Anglo American Completes Sale of Drayton Coal Mine in Australia', 26 February 2018, see <https://australia.angloamerican.com/media/press-releases/pr-2018/20180226>.

94 See ACCC, *Draft Decision: Australian Trail Track Corporation's December 2017 Variation to the 2011 Hunter Valley Access Undertaking*, 28 June 2018, pp. 50–4.

- a definition and explanation of cost drivers; and
- the rationale for the driver assignment to cost category.

As a result, the ACCC is unable to determine whether the Non-Segment Specific Costs allocated the Hunter Valley rail network reflects the costs that the Network causes to ARTC's business.

The ACCC is also concerned that the definition of Non-Segment Specific Costs in the September 2018 Variation implies that all Non-Segment Specific Costs will be allocated as Fixed Costs. The ACCC does not consider that all Non-Segment Specific Costs are entirely Fixed Costs. For example, the ACCC considers that at least a portion of several of the Non-Segment Specific Costs set out in Schedule I of the current HVAU and September 2018 Variation should be incremental costs rather than fixed. That is, if the Hunter Valley network was no longer operated by ARTC, then a proportion of these costs would not be incurred by ARTC.

If Non-Segment Specific Costs are determined to be Fixed Costs when there is at least a portion that is incremental, Access Holders that incur Fixed Costs in PZ1 will be paying for Non-Segment Specific Costs that should also be charged to Access Holders that do not pay Fixed Costs in PZ1.

In both instances, the ACCC considers that ARTC's approach could lead to cross-subsidisation-either between Access Holders traversing PZ1, or between ARTC's businesses. This, in turn, could result in the economically inefficient operation of, use of and investment in the Network (section 44ZZA(3)(aa)).

Allocation of Incremental Capital Costs to Access Holders

The ACCC notes that ARTC proposes to allocate Incremental Capital Costs on the basis of contracted commitments rather than on the basis of actual usage, and that this approach is supported by the majority of stakeholders.

Consistent with the 2013 Annual Compliance Final Determination, the ACCC considers that the appropriate allocator of Incremental Capital Costs is on the basis of actual usage, rather than contracted commitments. The ACCC considers that allocating Incremental Capital Costs on this basis of actual usage represents how costs are incurred on the Hunter Valley rail network. The ACCC considers that allocating costs such that they reflect how those costs are caused ensure that Access Holders get a clear signal about the costs they are contributing to. This, in turn, promotes the economically efficient operation of, use of and investment in the Network (section 44ZZA(3)(aa)).

The ACCC notes HRATF's support for allocating Incremental Capital Costs on the basis of contracted commitments in part relates to the effect on the proportion of TOP Charges as part of Access Charges. The ACCC understands that there is no requirement in the September 2018 Variation, the criteria set out in section 44ZZA(3) of the Act, or the pricing principles set out in 44ZZCA of the Act, which requires ARTC to align its tariff structure with its cost structures. The ACCC therefore considers that ARTC could set a TOP charge, based on Access Holders' contracted commitments, that is intended to recover Incremental Capital Costs from Access Holders. As part of the annual reconciliation of revenue and costs, ARTC could allocate Incremental Capital Costs on the basis of actual use data for that year.

The ACCC also notes HRATF's view that ARTC's proposed approach to allocating Incremental Capital Costs better reflects the relationship between capital investment and TOP commitments. The ACCC understands that concerns regarding allocating Incremental Capital Costs on the basis of actual usage relates to instances where Access Holders' use of the Network deviates from contracted commitments. The ACCC notes that there are a number of provisions in the September 2018 Variation that provide incentives for Access Holders to minimise the difference between actual usage and contracted commitments.

In the Draft Decision to the December 2017 Variation, the ACCC sought views on whether these provisions provide an effective constraint on large variations between contracted commitments and actual usage. The ACCC continues to seek views on this issue. In particular, where stakeholders consider that these provisions do not provide an effective disincentive, the ACCC is interested in views on how such an incentive could be strengthened. The ACCC considers that such information would be useful in considering the appropriateness of these provisions as a disincentive for over-contracting capacity in future variations to the HVAU and/or future HVAU applications.

7. Industry consultation in Capital Allocations

7.1. ARTC proposal

ARTC proposes a number of amendments to the process of industry consultation in relation to capital allocations, set out in section 9 of the September 2018 Variation. In particular, ARTC proposes changes to the following sections:

- Overview (section 9.1 of the September 2018 Variation)
- The RCG (section 9.2)
- Project Feasibility (section 9.4)
- Capital Allocation for Sustaining Capital in PZ1 (section 9.8)
- Capital Allocation for Expansion Capital in PZ1 (section 9.9)
- RCG endorsement (section 9.10).

ARTC also proposes to make changes to the approach to allocating costs as either Variable Maintenance Cost or Incremental Capital Costs, and between users, in determining the Economic Cost of a Segment (section 4.5). Further, under section 14 of the September 2018 Variation, ARTC has proposed the following definitions, related to industry consultation in Capital Allocations:

- **Expansion Capital**–capital expenditure in relation to a Project that provides Additional Capacity
- **Sustaining Capital**–capital expenditure that is not Expansion Capital
- **Capital Allocation**–the proportion of capital expenditure that is allocated as Incremental Capital Costs rather than Fixed Costs and the method for allocating those Incremental Capital Costs to Access Holders in accordance with section 4.5 of the September 2018 Variation.

The definitions of Incremental Capital Costs and Fixed Costs are discussed in further detail in chapter 6 of this Decision.

ARTC's proposed amendments to sections 4.5 and 9 are discussed in further detail below.

Economic Cost

Under section 4.5(e) of the September 2018 Variation, ARTC must seek endorsement from RCG as to whether Expansion Capital (incurred on or after 1 July 2008) is to be treated as a Fixed Cost or Incremental Capital Cost.

Under section 4.5(i), ARTC must maintain a Historical Capital Allocation List, which will contain all the projects or capital expenditure that the RCG has endorsed, or the ACCC has approved. This list will include the applicable Capital Allocation, a summary of any relevant engineering assessment, and the purpose, causal factors and cost drivers identified by ARTC as relevant for the choice of Capital Allocation.

Overview

Section 9.1 of the September 2018 Variation sets out the process for industry consultation in relation to:

- Projects that provide Additional Capacity (set out in section 8 of the September 2018 Variation)

- the process to obtain endorsement for projects that do not involve Additional Capacity. The September 2018 Variation cites asset replacement, cost reduction and safety-related projects as examples of such projects.

Section 9.1(c) states that the objectives of the consultation process are to:

- inform Hunter Valley Coal Chain participants of Additional Capacity requirements and investment strategies
- provide a process for Hunter Valley Coal Chain participant input, aimed at, among other things the alignment of Projects to provide Additional Capacity with projects to expand capacity at the coal terminals at the Port of Newcastle
- provide a process for the applicable industry participants to participate in the development and management of projects and to endorse Expansion Capital and Sustaining Capital as Prudent
- in relation to projects in PZ1, endorse Capital Allocations for Expansion Capital and to be informed of the proposed Capital Allocations for Sustaining Capital.

The RCG

Section 9.2 sets out that ARTC will convene and conduct regular monthly meetings with the RCG for the purpose of:

- consulting with applicable industry representatives and obtaining endorsement of Expansion Capital and Sustaining Capital on the Network
- in relation to projects in PZ1, obtaining endorsement of Capital Allocations for Sustaining Capital and informing RCG of Capital Allowances for Sustaining Capital.

Section 9.2(c) also sets out RCG membership for Access Holders and Operators to be determined on the basis of Contracted Coal KM, a change from Contracted GTK in the current HVAU. ARTC's proposed change to RCG membership and voting thresholds to Contracted Coal KM reflects the introduction of path based pricing. The ACCC's views on path based pricing are set out in chapter 9 of this Decision.

Project Feasibility

Under section 9.4 of the September 2018 Variation, ARTC will provide a project feasibility report to the RCG for each project that has been endorsed at the concept assessment stage.

Section 9.4(b) sets out what will be included in the project feasibility report. If the project relates to Expansion Capital in PZ1, ARTC proposes to include information relating to Capital Allocation, as required in section 9.9(b), in the project feasibility report. The elements of section 9.9(b) are discussed further below.

ARTC may seek formal endorsement from the RCG to proceed to the project assessment phase. Under section 9.4(d)(ii) of the September 2018 Variation, ARTC proposes to include the Capital Allocation, as applicable, as part of this endorsement.

Capital Allocation for Sustaining Capital in PZ1

Section 9.8 sets out how Capital Allocation decisions for Sustaining Capital will be made in PZ1.

Section 9.8(b) states that, at the appropriate stage in the project consultation process, ARTC must inform the RCG of its proposed Capital Allocation for Sustaining Capital. As applicable to the project, ARTC will include the following information as set out in sections 9.8(c) and 9.8(d), respectively:

- If ARTC considers that the ACCC has previously approved a Capital Allocation for projects or Sustaining Capital of a similar nature or purpose to the project, then ARTC must provide information to the RCG as to the similarities (having regard to the Historical Capital Allocation List) and why that Capital Allocation is appropriate to be applied.
- If ARTC considers that the ACCC has not previously approved a Capital Allocation for projects or Sustaining Capital of a similar nature or purpose to the project or Sustaining Capital, then ARTC must provide an independent engineering assessment of the appropriate Capital Allocation (having regard to the purpose, causal factors and cost drivers for the project or Sustaining Capital) and the instructions provided to the expert.

Section 9.8(e) notes that the information on Capital Allocation is provided for information only. Further, ARTC is not required to seek endorsement for Capital Allocations for Sustaining Capital. However, section 9.8(f) states that nothing in section 9.8 prevents an Access Holder from making submissions on the Capital Allocation in the relevant Compliance Assessment.

Capital Allocation for Expansion Capital in PZ1

Section 9.9 outlines how Capital Allocation decisions for Expansion Capital in PZ1 will be made. This process is as follows:

- At the project feasibility stage, ARTC will propose the Capital Allocation for the Expansion Capital project, along with an independent engineering report in support of its Capital Allocation proposal. Section 9.9(b) notes that ARTC will provide this information to the RCG at least 28 days prior to the RCG meeting where ARTC intends to seek endorsement for the project.
- Under sections 9.9(c) and (d), a RCG member can raise a written objection to ARTC's proposed Capital Allocation at least two days prior to or at the relevant RCG meeting. If ARTC reasonably considers the RCG would otherwise endorse the Project, it will seek to resolve the objection at the relevant RCG meeting. Under section 9.9(e), a RCG member can raise a written objection up to 10 Business Days after the relevant RCG meeting. In raising an objection, RCG members must also provide reasons and supporting submissions.
- Where a RCG member has raised an objection to ARTC's proposed Capital Allocation, under sections 9.9(c) and (e) ARTC must notify other RCG members of the objection, and provide any material related to the objection.
- Under section 9.9(f), if ARTC cannot resolve the objection at the relevant RCG meeting, or ARTC receives the objection after the relevant RCG meeting, ARTC must refer the decision about Capital Allocation to the ACCC for resolution within 20 Business Days of the relevant RCG meeting.
- If an objection is referred to the ACCC, under section 9.9(g) ARTC must provide the ACCC with the project feasibility report, independent engineering assessment, details of the RCG member's objection, the latest Historical Capital Allocation List, and any other relevant information. ARTC must additionally notify the RCG of the referral.
- Under section 9.9(h), the ACCC will use reasonably endeavours to make a decision within 4 weeks of the referral and publish its decision on its website, subject to confidentiality restrictions.
- Sections 9.9(j), (k) and (l) describe how any costs associated with the ACCC's resolution of an objection may be allocated to ARTC and/or Access Holders. Specifically:

- The ACCC may charge for any hearings conducted as part of the objection resolution process, consistent with the amounts and rates prescribed by the *Competition and Consumer Regulations 2010* (Cth), and the amounts of any out of pocket expenses incurred by the ACCC in making its decision.
- The ACCC can make determinations regarding the proportion of costs that will be borne by ARTC and the objecting Access Holder(s) in relation to the objection resolution process. ARTC and the objecting Access Holder(s) may make submissions to the ACCC on this issue. If the ACCC does not make a determination on the apportioning costs to the disputing parties, ARTC will bear the costs of the ACCC's decision.
- In the event of costs arising from a determination, if ARTC bears the costs of the ACCC's decision, it will include those costs in the RAB where a Project is endorsed by RCG. Where the Project is not endorsed by RCG, those costs will be expensed in the year incurred and deemed Efficient.

- Section 9.9(i) states that following the ACCC's resolution of an objection, ARTC may seek endorsement from the RCG of the Capital Allocation approved by the ACCC. If the RCG endorses that decision, it will be taken to be compliant for the purposes of Compliance Assessments.

RCG Endorsement

Section 9.10 sets out the thresholds for RCG endorsement for project or Capital Expenditure. These thresholds are:

- **For a project or Capital Expenditure in relation to a particular Pricing Zone**–at least 50 per cent of Contracted Coal KM in that Pricing Zone. This comprises coal producers that hold Coal Access Rights under an Access Holder Agreement and any coal Train Km that ARTC considers will reasonably become Contracted Coal KM within 10 years of the completion of the proposed project (as set out in section 9.2(g)).
- **Where Additional Capacity, provided in particular Pricing Zone, results in an increase in the Standard Access Charge in that Pricing Zone of more than 10 per cent**–at least 70 per cent of Contracted Coal KM in that Pricing Zone and any coal Train Km that ARTC considers will reasonably become Contracted Coal KM within 10 years of the completion of the proposed project (as set out in section 9.2(g)).[95] The 70 per cent of Contracted Coal KM comprises of coal producers that hold Coal Access Rights under an Access Holder Agreement and any coal Train Km that ARTC considers will reasonably become Contracted Coal KM within 10 years of the completion of the proposed project (as set out in section 9.2(g)).

ARTC's submission

ARTC notes that it has made amendments to the involvement of the RCG in capital allocation decisions in PZ1 in response to the ACCC's Draft Decision on the December 2017 Variation, and discussions with Customers.[96] ARTC submits that it has developed the RCG consultation processes set out in the September 2018 Variation in consultation with HRATF.[97]

ARTC considers that the proposed RCG consultation processes ensure that:[98]

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95 The ACCC notes that prospective Contracted Coal KM set out in section 9.2(g) has been noted twice in section 9.10(b). This appears to be a typographical error.

96 ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term,* 28 September 2018, p. 2.

97 Ibid, p. 3.

98 Ibid.

- RCG are aware of the proposed Capital Allocation when the projects are voted on
- there is a timely objection resolution mechanism to ensure project implementation is not delayed.

ARTC notes that the RCG process for Sustaining Capital reflects that it is 'effectively stay in business capital needed to maintain the safe and reliable operation of the network and is relatively lower in dollar value'.[99] ARTC submits that as a result, the RCG process for Sustaining Capital needs to be such that it avoids affecting operational delivery of such projects. As such, ARTC notes that the proposed process does not give RCG an endorsement right.[100]

ARTC submits that the development of the Historical Capital List set out in section 4.5(i) is to assist with future Capital Allocations and endorsements.[101]

In addition, ARTC submits a number of changes to RCG membership and endorsement thresholds reflect the proposed use of path based pricing based on Contracted Coal KM.[102]

7.2. Comparison to the December 2017 Variation

The December 2017 Variation did not contemplate categorising capital projects, for the purposes of Capital Allocation, as either Sustaining or Expansion Capital. Under section 9.2(a) of the December 2017 Variation, ARTC proposed to inform the RCG on the proportions and allocations for Project costs or other Capital Expenditure associated with Incremental Capital Costs. This would occur at the 'appropriate stage at the consultation process'.[103] Under this process, ARTC was not required to obtain RCG endorsement on proportions and allocation methods.

ARTC could also consult with RCG and seek endorsement for treating capital costs as Fixed Costs rather than Incremental Capital Costs.

As in the September 2018 Variation, the December 2017 Variation includes a number of amendments to RCG membership and endorsement thresholds to reflect the proposed use of path based pricing based on Contracted Coal KM.[104]

7.3. Comparison to the current HVAU

The current HVAU and September 2018 Variation differ in the role given to the RCG in determining the Economic Cost of a Segment. In particular, the current HVAU does not include a mechanism for ARTC to consult with the RCG in regard to the treatment and allocation of cost components.

7.4. Stakeholder Submissions

HRATF submits that it worked with ARTC in relation to the design of the RCG consultation processes, and notes its support of the approach and drafting.[105] In providing its overall support of ARTC's proposed approach to RCG consultation, HRATF submits that it accepts ARTC's rationale for different approaches to consultation on Sustaining Capital and

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[99] Ibid.

[100] Ibid, p. 37.

[101] Ibid, p. 36.

[102] Ibid, pp. 34–5, 39.

[103] See section 9.2(a)(ii) of the December 2017 Variation.

[104] See sections 9.2(c) and 9.8 of the December 2017 Variation.

[105] HRATF, *HRATF supplementary submission – September HVAU Variation,* 19 October 2018, p. 1.

Expansion Capital.[106] In particular, HRATF notes that RCG members can raise objections to ARTC's approach to Sustaining Capital projects through the ACCC's annual compliance process.[107] HRATF also supports the proposed process and timeframes for escalating objections relating to Cost Allocations for Expansion Capital. HRATF considers that it appropriately balances the interests of RCG members and ARTC.[108]

However, HRATF's support is subject to comments in relation to the ability for the ACCC to recoup costs incurred through resolving objections. HRATF notes that the default position for allocating the ACCC's costs is for ARTC to bear the costs and subsequently capitalise them in its RAB.[109] HRATF considers that this should be the position adopted in all bar exceptional circumstances. Further, HRATF submits that in instances where an objection raised by a producer is not vexatious, it is inappropriate for a producer to be required to bear any of the ACCC's costs of resolving an objection. HRATF cites the following reasons for its view:[110]

- The modified objection process brings forward the ACCC's consideration of the cost allocation of particular Expansion Capital projects, which it would ordinarily undertake as part of the annual compliance process.
- Such an approach is likely to provide a disincentive for producers to raise concerns, undermining the policy intent of the process. This may also disadvantage smaller producers.

Pacific National submits it has 'no major concerns' regarding the inclusion of sections 9.8 and 9.9 in the September 2018 Variation, and changes to other sections to incorporate ARTC's proposed approach to consulting with RCG on cost allocation.[111] Further, Pacific National submits that the distinction between Expansion Capital and Sustaining Capital is sufficiently clear.[112]

Pacific National reiterated concerns raised in previous assessment processes[113], that train operators are not voting members of the RCG, but are directly affected by ARTC's capital expenditure and capacity enhancements on the Network.[114] However, Pacific National also submits that it considers the proposed amendments to the RCG process is consistent with the current operation of the RCG.[115]

7.5. ACCC view

The ACCC notes that ARTC's proposed approach to consulting with the RCG regarding Cost Allocation of capital expenditure in the September 2018 Variation is intended to address concerns raised by the ACCC in its Draft Decision to the December 2017 Variation.[116,117] The ACCC also notes that both HRATF and Pacific National have submitted their support of ARTC's proposed approach. On the basis of the support expressed in

106 Ibid, p. 2.

107 Ibid.

108 Ibid.

109 Ibid.

110 Ibid.

111 Pacific National, *Pacific National Submission to the ARTC Variation Application to ACCC to Vary the 2011 HVAU*, 15 October 2018, p. 3.

112 Ibid.

113 Including submissions to the 2016 HVAU, 2017 HVAU and December 2017 Variation.

114 Pacific National, *Pacific National Submission to the ARTC Variation Application to ACCC to Vary the 2011 HVAU*, 15 October 2018, p. 3.

115 Ibid, pp. 3–4.

116 ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term,* 28 September 2018, p. 2.

117 For the ACCC's views regarding the involvement of RCG in capital allocation decisions, see ACCC, *Draft Decision – Australian Rail Track Corporation's December 2017 Variation to the 2011 Hunter Valley Access Undertaking,* 28 June 2018, pp. 53–4.

submissions to the September 2018 Variation, the ACCC considers that ARTC's proposed approach to consulting with the RCG regarding the Cost Allocation of capital expenditure is appropriate (section 44ZZA(3)(e)).

The ACCC notes that any decision on whether to treat Expansion Capital or Sustaining Capital projects as either Fixed Cost or Incremental Capital Cost affects which Access Holders will pay for those costs. That is, if a capital expenditure project is considered a Fixed Cost, only PZ1 and PZ2 Access Holders will contribute to those costs. However, if that project is considered to be Incremental Capital Costs, then PZ1, PZ2 and PZ3 Access Holders will contribute to those costs. Further discussion regarding the definition of, and contribution to, Incremental Capital Cost and Fixed Cost are discussed further in chapter 6 of this Decision.

The ACCC also notes that categorising capital expenditure projects as either Expansion Capital or Sustaining Capital results in a different level of RCG involvement in decisions regarding Capital Allocation. The ACCC acknowledges ARTC's stated rationale for its approach to consulting with the RCG regarding the allocation of Sustaining Capital. However, the ACCC considers that such different processes highlights the importance of clear definitions for Expansion Capital and Sustaining Capital, to minimise ambiguity regarding which RCG consultation process should be used for a particular capital expenditure project. The ACCC notes that Pacific National considers these definitions are clear. The ACCC notes that if an RCG member disagrees with a categorisation of capital, it can access the dispute resolution provisions under section 3.15 of the HVAU, unchanged in the September 2018 Variation.

The ACCC notes ARTC's commitment, set out in section 4.5(i) to maintain a Historical Capital Allocation List, which it will provide to the RCG after each update, and to Access Holders or the ACCC upon request. The ACCC considers that ARTC's commitment to develop and maintain such a list improves clarity and certainty of the operation of the Hunter Valley rail network, which is in the interests of those who might want access to the Network (sections 44ZZA(3)(c) and (e)).

The September 2018 Variation sets out a role for the ACCC in assessing the incremental proportion or allocation method for a capital project through the ACCC's annual compliance assessment. The ACCC notes that in making such assessments, it will have regard to any submissions from stakeholders, as well as the methodology set out in the 2013 Annual Compliance Assessment Final Determination, and the appropriate application of that methodology.

The ACCC notes HRATF's concerns regarding the provisions in the September 2018 Variation relating to the ACCC determining the proportion of costs to be borne by ARTC and the disputing Access Holder. The ACCC will consider the appropriate distribution of costs between ARTC and the disputing Access Holder, based on the nature of the matter in objection. As noted in section 9.9(k), the ACCC will have regard to any submissions ARTC and the disputing Access Holder may make on the issue of costs. The ACCC considers that the ability for the ACCC to apportion costs, related to resolving objections, to ARTC and/or disputing Access Holders, provides an incentive for ARTC to provide sufficient information and rationale for a proposed cost allocation to RCG. Similarly, it provides a disincentive for parties to raise vexatious objections. The ACCC considers that this is both in the legitimate business interests of ARTC and the interests of those who might want to access the Network (44ZZA(3)(a) and (c)).

8. ACCC Compliance Assessments

8.1. ARTC proposal

Consistent with the current HVAU, section 4.10 and schedule G of the September 2018 Variation set out the requirements for the ACCC to conduct a Compliance Assessment each year to determine whether ARTC has complied with the financial model in the HVAU.

ARTC proposes changes to the annual Compliance Assessment provisions, at sections 4.10(a), (d)(iii), (h) and Schedule G of the September 2018 Variation.

Under sections 4.10(a) and (h) of the September 2018 Variation, ARTC proposes to amend the date by which it must submit its compliance documentation to the ACCC. Specifically, ARTC would be required to submit documentation for the Compliance Assessment, by the later of 30 April each year and four months from the ACCC's final determination of the previous calendar year's Compliance Assessment.

Section 4.10(h) provides further clarification, proposing that:

> *The Compliance Assessments for 2016, 2017 and 2018 will be undertaken in accordance with the relevant Undertaking before its variation by the Varied Undertaking except that ARTC must submit to the ACCC the documentation for:*
>
> *(i) the 2016 and 2017 Compliance Assessments by 4 months after the ACCC's final determination of the previous year's Compliance Assessment; and*
>
> *(ii) the 2018 Compliance Assessment by the later of 30 April 2019 and 4 months after the ACCC's final determination of the 2017 Compliance Assessment.*

ARTC submits that the proposed changes to section 4.10(a) 'reflects the current backlog in Compliance Assessments and that a Compliance Assessment for a year depends on previous Compliance Assessments being completed.'[118]

ARTC further submits that the proposed amendments to 4.10(h) 'confirms that Compliance Assessments for years pre-dating Path Based Pricing will continue under the former Undertaking provisions applicable to those years and acknowledges different timing given the backlog in compliance.'[119]

The ACCC notes that the September 2018 Variation also proposes amendments to 4.10(d)(iii) to reflect its intention that where Capital Expenditure or Capital Allocations have been endorsed by the RCG in accordance with section 9 of the HVAU, the ACCC will not consider whether that Capital Expenditure is Prudent or review the Capital Allocation as part of its annual Compliance Assessment. ARTC's proposed amendments to section 9 are discussed further in chapter 0 of this Decision.

Finally, ARTC proposes an amendment to section 2(b) of Schedule G of the September 2018 Variation to refer to section 4.1(a) of the HVAU. The ACCC notes that this proposed amendment appears to be an error and should instead refer to section 4.4 of the HVAU.

8.2. Comparison to the December 2017 Variation

Under section 2.3(d) of the December 2017 Variation, ARTC had proposed to undertake the Compliance Assessment for the 2018 calendar year as if the December 2017 Variation had

118 ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term*, 28 September 2018, p. 16.

119 Ibid, p. 17.

come into effect on 1 January 2018 (other than the provisions at sections 4.11–4.23 and 9).[120] Section 2.3(d) stated its objective was to avoid the need for two sets of compliance modelling for part years for the first Compliance Assessment after the December 2017 Variation came into effect.

ARTC submitted that it had proposed this approach as 'it is not feasible to model the new incremental capital costs changes on a part year basis, particularly for 2018 incremental capital costs.'[121]

With the December 2017 Variation having been withdrawn and the September 2018 Variation now specifying a future commencement date of 1 January 2019 for the proposed amendments, the previously proposed section 2.3(d) is no longer relevant.

As recommended in the ACCC's Draft Decision on the December 2017 Variation, ARTC proposes to amend section 1 of Schedule G to ensure the amended timeframes under section 4.10 are consistently reflected in Schedule G.

8.3. Comparison to current HVAU

Under section 4.10(a) of the current HVAU, ARTC must submit documentation by 30 April each year with respect to compliance in the previous calendar year.

8.4. Stakeholder submissions

Two stakeholders provided submissions in respect of the previously proposed version of section 2.3(d) of the December 2017 Variation.

At the time, HRATF relevantly submitted that it would not support applying the December 2017 Variation from the 2019 compliance period, noting that: [122]

> *…the original intention of requiring ARTC to develop, consult on and submit the Variation by the end of 2017 was so that there would not need to be any further delay in moving to the modified and preferred approach*.

HRATF did not specifically discuss this issue in its submission to the September 2018 however does note that it 'would welcome the ACCC moving directly to a final decision to accept' the September 2018 Variation.[123]

In its submission on the December 2017 Variation, Pacific National submitted that a 'single compliance model should apply for the entire compliance period…either backdated to January 2018 or applying from January 2019'.[124] Pacific National also expressed concern that: [125]

> *…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.*

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120 Sections 4.11–4.23 govern the structure of Access Charges for both Coal and Non-Coal access, as well as providing annual forecast aggregate coal volumes, the rate of Standard Access Charges and the forecast RAB for PZ3 to PZ3 users. Section 9 governs industry consultation on Additional Capacity projects.

121 ARTC, *2011 Hunter Valley Coal Network Access Undertaking Variation – Explanatory Guide*, 21 December 2017, p. 55.

122 Ibid, p. 8.

123 HRATF, *HRATF supplementary submission – September HVAU Variation*, 19 October 2018, p. 1.

124 Pacific National, *Pacific National Submission to the ACCC in Relation to the ARTC's Proposed Variation to the 2011 HVAU*, February 2018, p. 10.

125 Ibid.

The ACCC received no submissions that address ARTC's proposed changes to section 4.10(a) or (h). However, HRATF expressed concern as part of its submission on the December 2017 Variation that undue delays in the annual compliance process affect the timing of rebate payments to producers.[126]

8.5. ACCC view

In respect of section 4.10(a) and (h) of the September 2018 Variation, the ACCC considers ARTC's amendments are appropriate.

The ACCC acknowledges that ARTC's Compliance Assessment submission depends on the ACCC's final determination for the previous year's Compliance Assessment. The ACCC also considers it necessary that ARTC has adequate time to prepare its Compliance Assessment submission following the previous year's final determination. Therefore the ACCC considers that the proposed amendments are in ARTC's legitimate business interests (section 44ZZA(3)(a)). The ACCC further considers that the proposed amendments provide clarity and certainty for Access Holders regarding the commencement date of Compliance Assessments (section 44ZZA(3)(e)).

However, the ACCC also considers it is in access seekers' interests to receive any rebates resulting from the 'unders and overs' adjustments in the Compliance Assessment process in a timely manner (section 44ZZA(3)(c)). While the ACCC considers ARTC's proposal to be appropriate, the ACCC strongly encourages ARTC to provide its Compliance Assessment submission as soon as possible following the ACCC's final determination of the previous year's Compliance Assessment.

Based on its experience with previous Annual Compliance assessments, the ACCC considers that the process can be considerably expedited if ARTC provides the ACCC with all relevant information required for the ACCC's assessment up-front. For example, the ACCC will routinely require the following information in order to undertake its assessment:

- actual and contracted Train Km and GTK for the Hunter Valley rail network (broken down into coal traffic by Pricing Zone and non-coal traffic) and for the Interstate rail network
- all endorsements (that is, for all project stages) by the RCG of capex
- detailed explanations for minor and major projects where capex exceeds RCG endorsed values
- detailed explanations of ARTC's processes and procedures relating to disposal values.

The ACCC expects that ARTC provides this information up-front in its initial submission.

The ACCC notes that the dates provided at section 4.10(a) have been reflected in Schedule G of the September 2018 Variation, which sets out the information provision timeframes and guidelines, and are now internally consistent. The ACCC considers that this amendment promotes clarity and certainty in the operation of the HVAU (section 44ZZA(3)(e)).

The ACCC notes that the proposed variation to section 2(b) of Schedule G refers to section 4.1(a) of the HVAU. This appears to be an error as it is clear that the section is intended to refer to section 4.4 of the HVAU. In this regard the ACCC considers 2(b) of Schedule G should be interpreted by reference to section 4.4 of the HVAU, not section 4.1(a) of the HVAU.

[126] HRATF, *HRATF response to 2011 Hunter Valley Access Undertaking (HVAU) 2017 variation application*, 14 February 2018, p. 6.

9. Structure of Access Charges

9.1. ARTC proposal

In the September 2018 Variation, ARTC proposes a 'path based pricing' methodology for Access Charges for Coal Customers. This methodology comprises two components:

- Pricing unit for TOP and non-TOP Charges
- Services Envelope.

ARTC's proposed implementation of path based pricing also affects other sections of the HVAU, including RCG membership and voting, and the IAHA. ARTC's proposed path based pricing methodology, and its implications for other parts of the HVAU and IAHA are set out below.

ARTC does not propose to make any changes to the structure of Non-Coal Access Charges, as set out in section 4.12 of the September 2018 Variation.

Pricing Unit for TOP and non-TOP Charges

Under section 4.11(a) of the September 2018 Variation, ARTC seeks to set Charges for Coal Access Rights on the basis of a combination of a:

- non-TOP component based on actual usage ($/GTK) for the recovery of Variable Maintenance Costs for each Pricing Zone.
- TOP component comprising of:
  - $/Contracted Coal GTK for the recovery of Incremental Capital Costs incurred in the PZ1/2 Constrained Network; and
  - $/Train Km for each Pricing Zone for the recovery of Fixed Costs.

In the pricing objectives set out in section 4.13(a) of the September 2018 Variation, ARTC will have regard to the following when determining Charges:

- achieving the full recovery of Variable Maintenance Costs from all Access Holders on the basis of the actual GTK usage weighted for the axle load;
- through the application of the TOP component of Charges, achieving the maximum permitted recovery of Incremental Capital Costs and Fixed Costs; and
- the proportion of Fixed Costs and Incremental Capital Costs recovered through a TOP component to be consistently applied to all Access Holders holding Coal Access Rights within a Pricing Zone.

In addition, section 4.13(b) states that in determining Charges, ARTC will have regard to the objective of providing for an open and equitable mechanism for the application of TOP Charges.

The Access Charges associated with the Service Envelope characteristics are referred to as Standard Access Charges in the September 2018 Variation and IAHA. Under section 4.20(c), Standard Access Charges for a particular calendar year will be based on:

- TOP Charges–Contracted Coal Km and Contracted Coal GTK for that calendar year and any additional Train Kms or GTK that ARTC considers likely to be Contracted Coal Km or Contracted Coal GTK for that relevant year

- non-TOP Charges–forecast coal volumes that ARTC considers likely to be railed for that calendar year
- ARTC's annual forecast costs for the Network in each Pricing Zone, as determined under 4.20(b).

Services Envelope

TOP and non-TOP Charges will apply to all train configurations with the range (Services Envelope) specified in section 4.14(c), which are given in Table 3 below.

Table 3: Service Envelope characteristics for each Pricing Zone

Segments	Service Envelope characteristics
Pricing Zone 1	Maximum length: 1 543 metres Maximum axle load: 30 tonnes Maximum speed (empty): 80 kmh Maximum speed (loaded): 60 kmh Section running times (must meet) – As published on ARTC website from time to time
Pricing Zone 2	Maximum length: 1 543 metres Maximum axle load: 30 tonnes Maximum speed (empty): 80 kmh Maximum speed (loaded): 60 kmh Section running times (must meet) – As published on ARTC website from time to time
Pricing Zone 3	Maximum length: 1 329 metres Maximum axle load: 30 tonnes Maximum speed (empty): 80 kmh Maximum speed (loaded): 60 kmh Section running times (must meet) – As published on ARTC website from time to time

Note: Schedule E of the September 2018 Variation provides a list of the Segments applicable to each Pricing Zone.

Source: Based on Section 4.14(c) of the September 2018 Variation.

Effect on other sections of the HVAU

ARTC's path based pricing proposal also has implications for other parts of the September 2018 Variation. In particular, ARTC proposes minor changes to the following sections to account for the proposed adoption of Standard Access Charges and the Service Envelope:

- contact details for further information (section 2.6(b) of the September 2018 Variation)
- Access Agreements (sections 3.14(b)(i)(A) and 3.14(c)(i))
- process for finalising Standard Access Charges, outside those changes set out in 4.20(c) outlined above.

Under section 9.2, ARTC proposes to adjust the weighting for voting at RCG from Contracted Coal GTK to Contracted Coal Km.

ARTC has proposed removing a number of sections relating to transitional arrangements from the start of the 2011 HVAU and Initial Indicative Services, as they no longer apply. The removal of these sections are discussed in more detail in chapter 11 of this Decision.

Effect on the IAHA

ARTC also proposes to make a number of changes to the IAHA to reflect the use of Train Km for part of the TOP Charge and the introduction of the Services Envelope. These proposed changes include the following:

- Amendments to clause 11.5(b) to clarify that if ARTC consents to the use or operation of a Non-Compliant Service that is outside the Services Envelope, then ARTC may update the TOP Charges to reflect the characteristics of the Non-Compliant Services used or operated by the Access Holder.
- Updating Schedule 3, which outlines the formulae used to calculate TOP and non-TOP Charges, to reflect the proposed change to charging a portion of the TOP component on the basis of Train Km. ARTC also seeks to update Schedule 3 to reflect the use of the Services Envelope and Standard Access Charges in the September 2018 Variation.

These proposed changes to the IAHA are discussed further in chapter 10 of this Decision.

9.2. Comparison to the December 2017 Variation

ARTC's proposed approach to Access Charges for Coal Customers in the September 2018 Variation is the same as that proposed in the December 2017 Variation. The only exception to this is Schedule 3 of the IAHA, which refers to the '2019 PBP Variation Date' rather than the '2018 PBP Variation Date' in the December 2017 Variation. The ACCC notes that this change appears consistent with a proposed commencement date of 1 January 2019 (discussed further in chapter 4 of this Decision).

In the December 2017 Variation, ARTC submitted that its objectives in implementing a path based pricing approach to Access Charges was to ensure that:[127]

- pricing provided an incentive for efficient consumption of network capacity in the context of the supply chain that it operates within; and
- the same pricing incentives encouraged efficient long-term investment in the below rail network infrastructure, as well as in downstream above rail infrastructure.

ARTC considered that path based pricing was simpler and more transparent than the Indicative Services approach used in the current HVAU.[128] ARTC also submitted that path based pricing provided an incentive to design and operate train configurations that maximised the capacity of the network.[129]

ARTC submitted that pricing Incremental Capital Costs on the basis of contracted GTK reflected the usage in PZ1.[130] ARTC also noted that there were capacity constraints in PZ2 and PZ3, and the use of Train Km in those Pricing Zones:[131]

> *…ensures that the incentive benefit of [path based pricing] to maximize per train coal volume is not diluted between the [indicative service] options but also maintains the cost causation link in [PZ1] where there is available capacity.*

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[127] ARTC, *2011 Hunter Valley Coal Network Access Undertaking Variation – Explanatory Guide*, 21 December 2017, p. 10.

[128] Ibid, p. 5.

[129] Ibid.

[130] Ibid, p. 10.

[131] Ibid, p. 15.

In relation to the proposed Services Envelope, ARTC submitted that setting a single tariff, which does not differentiate for each train configuration, for each Pricing Zone provided an incentive to design and operate train configurations to maximise the use and capacity of the Network.[132]

ARTC noted that under the current pricing approach in the current HVAU, the assessment of overall pricing for alternative train configurations requires ARTC to provide differentiated prices for that configuration before customers can evaluate the costs and benefits in third party commercial negotiations.[133] Under path based pricing, ARTC submitted that its involvement would be defining the characteristics of the Services Envelope, with customers determining 'how they can maximise their commercial position in congruence with efficient utilisation of rail network capacity within this envelope'.[134]

ARTC also noted that path based pricing would affect customers that originate from, or complete their journey on, an adjoining network. ARTC submitted that this effect is mitigated by moving to a three-part tariff, where part of the TOP Charge is levied on a GTK basis. ARTC also submitted that the removal of differentiation factors would have a positive effect on pricing for customers who have axle load constraints affecting train sizes.[135]

ARTC proposed to remove clause 11.5(d) of the IAHA in the December 2017 Variation, however has reinstated this clause in the September 2018 Variation. This is discussed further in chapter 10 of this Decision.

9.3. Comparison to the current HVAU

Under the current HVAU, Coal Access Charges are set out as a TOP and non-TOP Charge, both levied on a GTK basis. The TOP component of the Access Charge is intended to:

- fully recover new capital component of costs over the economic life of new investments; and
- recover some or all of the fixed component of costs from applicable Access Holders on the basis of forecast network usage. The proportion of fixed component of costs recovered through TOP Charges is to be consistently applied to all Access Holders holding Coal Access Rights within a Pricing Zone.[136]

The non-TOP component of Access Charges is designed to fully recover the variable component of costs and the proportion of the fixed component of costs that was based on actual network usage. These cost components are discussed further in chapter 5 of this Decision.

The current HVAU specifies Access Charges using the concept of the Indicative Service, which varies according to train characteristics. The characteristics are intended to represent the coal train configuration(s) that would contribute to achieving optimum utilisation of the Network.[137]

The Indicative Services characteristics are largely the same as those specified in the Services Envelope (see Table 3). Exceptions to this are:

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132 Ibid, p. 5.

133 Ibid, p. 13.

134 Ibid, p. 15.

135 Ibid.

136 Section 4.13(a) of the 2011 HVAU.

137 ACCC, *Position Paper – Australian Rail Track Corporation's Hunter Valley Coal Network Access Undertaking – Final Indicative Services variation,* 1 August 2014, p. 5.

- Indicative Services specify the maximum number of wagons for each service, whereas this is not included as a characteristic in the Services Envelope
- the length of trains in PZ3 is 1 350 metres in the current HVAU, and 1 329 metres in the September 2018 Variation.

ARTC noted that at the time the 2011 HVAU was developed, stakeholders raised concerns about whether GTK was the appropriate pricing unit for encouraging the efficient use of capacity. In response, ARTC noted that there was an absence of any reliable network or Coal Chain Capacity modelling that would enable access pricing (in particular pricing differentials) that would incentivise efficient use of capacity with any confidence.[138] On this basis, ARTC considered that GTK was a reasonable approach until pricing incentives could be determined in a reliable and robust manner.[139]

The 2011 HVAU provided for the following multi-stage approach to developing Indicative Services:

- Stage one – Interim Indicative Services, which applied from the commencement of the 2011 HVAU (in accordance with section 4.19 of the current HVAU)
- Stage two – Initial Indicative Services, which used existing Hunter Valley Coal Chain Coordinator (**HVCCC**) modelling, developed within 5 months of the commencement of the 2011 HVAU (in accordance with section 4.17 of the current HVAU)
- Stage three – Final Indicative Services, which used more advanced HVCCC modelling, developed within 30 months of the commencement of the 2011 HVAU (in accordance with section 4.18). This included a review of the appropriateness of GTK in promoting the efficient use of capacity in the Network.

In December 2011, ARTC submitted a variation to the 2011 HVAU to implement Initial Indicative Services characteristics and associated Access Charges for ACCC assessment, consistent with stage two noted above.[140] During the assessment process, ARTC proposed to defer the implementation of Initial Indicative Access Charges to 1 January 2013.[141] ARTC withdrew its application in August 2012.[142] ARTC submitted a new variation to the ACCC in September 2012, which the ACCC consented to in October 2012. The resulting characteristics of the Initial Indicative Services are presented in Table 4Table 4 below.

Table 4: Initial Indicative Services characteristics for each Pricing Zone

Segments	Initial Indicative Services characteristics
Pricing Zone 1	Maximum axle load: 30 tonnes Maximum speed (empty): 80 kmh Maximum speed (loaded): 60 kmh 96 wagon train length Maximum length: 1 543 metres Section run times as per applicable Hunter Valley standard working timetable

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138 ARTC, *Hunter Valley Access Undertaking – Section 4.18 Determination of the Final Indicative Service – is gtkm the appropriate pricing unit to encourage efficient consumption of Capacity?,* October 2013, p. 5.

139 Ibid, p. 6.

140 ARTC, *Application for variation for Hunter Valley Coal Network Access Undertaking,* 1 December 2011.

141 ACCC, *Further consultation on Initial Indicative Service variation – ARTC proposal to defer implementation of Initial Indicative Access Charges,* 26 July 2012.

142 ARTC, *Variation of Hunter Valley Coal Network Access Undertaking (HVAU) to incorporate the Initial Indicative Services – withdrawal of variation application,* 15 August 2012.

Segments	Initial Indicative Services characteristics
Pricing Zone 2	Maximum axle load: 30 tonnes Maximum speed (empty): 80 kmh Maximum speed (loaded): 60 kmh 96 wagon train length Maximum length: 1 543 metres Section run times as per applicable Hunter Valley standard working timetable
Pricing Zone 3	Maximum axle load: 25 tonnes Maximum speed (empty): 80 kmh Maximum speed (loaded): 60 kmh 82 wagon train length Maximum length: 1 350 metres Section run times as per applicable Hunter Valley standard working timetable

Note: Schedule E of the current HVAU provides a list of the Segments applicable to each Pricing Zone.

Source: ACCC, *Decision in relation to Australian Rail Track Corporation's Hunter Valley Rail Network Access Undertaking – Initial Indicative Service Variation*, 17 October 2012, pp. 19–20.

In January 2014, ARTC submitted a variation to the 2011 HVAU to implement Final Indicative Services and associated Access Charges for ACCC assessment, in line with stage three noted above.[143] Following two rounds of consultations, there remained divergent views within industry on the characteristics of the Final Indicative Services.[144] In light of this, ARTC withdrew the variation in November 2014.[145]

As part of the process for determining Final Indicative Services, ARTC consulted with the HVCCC, Access Holders and Operators on whether GTK was the appropriate pricing unit to encourage efficient consumption of Capacity.[146] As a result of these consultations, ARTC considered, in the context of Indicative Services, that GTK was the appropriate pricing unit as it did not consider that an alternative pricing unit would deliver any significant benefit in encouraging efficient use/consumption of Capacity.[147] The ACCC considered that there was not sufficient basis to change to an alternative pricing unit at the time, but noted that the appropriateness of GTK as a pricing unit should continue to be reviewed for future undertakings.[148]

9.4. Stakeholder submissions

No stakeholder submitted on path based pricing during consultation on the September 2018 Variation. However stakeholders submitted on this issue in consultation on the December 2017 Variation, as outlined below.

143 ARTC, *Application for variation of Hunter Valley Coal Network Access Undertaking,* 31 January 2014.

144 ACCC, *Re: ARTC Hunter Valley Network Access Undertaking – withdrawal of the proposed Final Indicative Services Variation,* 10 November 2014.

145 ARTC, *Variation of Hunter Valley Coal Network Access Undertaking (HVAU) to incorporate the Final Indicative Service – withdrawal of variation application,* 7 November 2014.

146 Section 4.18(b)(i) of the 2011 HVAU.

147 ARTC, *Application to vary the 2011 Hunter Valley coal network access undertaking to provide for adoption of the Final Indicative Services and charges in accordance with section 4.18(b) – Supporting Documentation,* January 2014, p. 50.

148 ACCC, *Position Paper – Australian Rail Track Corporation's Hunter Valley Coal Network Access Undertaking – Final Indicative Services variation,* 1 August 2014, p. 36.

In response to the Draft Decision on the December 2017 Variation, Origin submitted that ARTC's path based pricing proposal would result in increased costs for Segments it uses in PZ1 and PZ2.[149] Origin submitted that this increase was due to operating trains relatively shorter than those exporting coal. Origin noted that it was unable to run longer trains due to configuration restrictions in the Sydney Trains Network (which it uses as well as the Hunter Valley rail network) and the length of rail loops used to access its coal handling facilities.[150]

Origin considered that domestic coal operators using the Hunter Valley rail network should be excluded from path based pricing. In particular, Origin submitted that it would have only a small effect on Access Charges for export services, given the predominance of such services on the Network.[151]

Several stakeholders submitted on path based pricing in the proposed December 2017 Variation. HRATF noted that its members did not hold an agreed position on path based pricing, however accepted the proposal as part of the overall package of changes proposed in the December 2017 Variation.[152] However HRATF emphasised that a number of its members would potentially object to the continuation of path based pricing once loss capitalisation in PZ3 was paid down.[153]

In support of path based pricing:

- Aurizon endorsed path based pricing, highlighting that it was preferable to the Indicative Services approach in the current HVAU.[154]
- The HVCCC considered path based pricing increased the incentive for the efficient use of Coal Chain Capacity through the use of longer trains. Additionally, compared to the Indicative Services approach, the HVCCC considered path based pricing better encourages long term investment in the below-rail network.[155] The HVCCC submitted that the characteristics in the Services Envelope should be consistent with the HVCCC's System Assumptions.[156]
- IPART submitted that path based pricing provides sufficient incentive for the efficient use of the Hunter Valley rail network.[157]
- Pacific National strongly endorsed path based pricing, stating it would provide an incentive to operate more efficient trains on the Hunter Valley rail network.[158] However Pacific National also proposed amendments to the Services Envelope mechanism, including that ARTC should consult with stakeholders on any substantial changes to the section run times.[159] Additionally, Pacific National raised concerns with how Access Charges impact users facing infrastructure constraints in adjoining networks–noting that

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149 Origin Energy, *Variation to the 2011 Hunter Valley Access Undertaking – Draft Decision,* 16 July 2018, p. 1.

150 Ibid.

151 Ibid.

152 HRATF, *HRATF response to 2011 Hunter Valley Access Undertaking (HVAU) 2017 variation application*, 14 February 2018, p. 14.

153 HRATF, HRATF supplementary submission, 30 May 2018, p. 2.

154 Aurizon, ACCC Consultation Paper of ARTC's proposed variation to the 2011 HVAU – December 2017, 13 February 2018, p. 1.

155 HVCCC, Submission – Australian Rail Track Corporation's Proposed Variation to the 2011 Hunter Valley Access Undertaking – December 2017, 15 February 2018, p. 2.

156 Ibid, p. 3.

157 IPART, Consultation on ARTC proposed variation to 2011 HVAU December 2017, 8 February 2018, p. 4.

158 Pacific National, Pacific National Submission to the ACCC in Relation to the ARTC's Proposed Variation to the 2011 HVAU, February 2018, p. 9.

159 Ibid, pp. 7–8.

without detailed pricing information, it was unable to measure the extent that charging a portion of TOP Charges on the basis of GTK would reduce that impact.[160]

Whereas:

- Anglo American stated that it did not support path based pricing due to a lack of transparency regarding how it would affect individual user's Access Charges.[161] [162]
- Centennial expressed concerns with path based pricing, stating it may not achieve the described cost recovery outcome, although noted that in the worked examples provided by ARTC, there did not appear to be a significant monetary impact arising from the proposed change.[163] Centennial highlighted concerns with infrastructure constraints on adjoining networks.[164]

9.5. ACCC views

As noted in the Draft Decision for the December 2017 Variation, the ACCC acknowledges that stakeholders have varying positions on ARTC's proposed path based pricing approach. However, the ACCC also notes HRATF's submission to the December 2017 Variation, which states that although producers do not have an agreed position on ARTC's proposal, it ultimately supports it as part of an agreed package.[165] The ACCC considers ARTC's proposed path based pricing approach in the September 2018 Variation is appropriate, on the basis that it is endorsed by the majority of stakeholders who submit that it provides a package of changes preferable to the current HVAU (section 44ZZA(3)(e)).

Although the proposal has support from the majority of industry for a number of different reasons, the ACCC continues to have a number of concerns with ARTC's path based pricing proposal. As noted in the Draft Decision for the December 2017 Variation, these concerns relate to the following matters:[166]

Services Envelope

The ACCC considers that the Services Envelope improves clarity and certainty in the costs of accessing the Hunter Valley rail network, which benefits users who may want to access the Network. However, the ACCC considers that ARTC should ensure that the attributes set out in the Services Envelope are consistent with the HVCCC's System Assumptions. In addition, substantial changes to section run times should be subject to consultation with stakeholders.

Objectives of path based pricing and the structure of Access Charges

The ACCC notes that ARTC has set out a number of cost recovery objectives in setting Access Charges. However, ARTC has not provided evidence to the ACCC that Fixed Costs, intended to be recovered through TOP Charges levied on a Train Km basis, are predominately driven by Train Km, despite the ACCC requesting supporting evidence when

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160 Ibid, pp. 5–7.

161 Anglo American, Submission to the Australian Competition and Consumer Commission – December 2017 Variation to Hunter Valley Access Undertaking, 13 February 2018, p. 5.

162 The ACCC understands that Anglo American has since completed the sale of its coal assets in the Hunter Valley, see < https://australia.angloamerican.com/media/press-releases/pr-2018/20180226>.

163 Centennial Coal Infrastructure, Re: Consultation on proposed variation to the Australian Rail Track Corporation Limited 2011 Hunter Valley Coal Network Access Undertaking – December 2017, 9 February 2018, pp. 1–2.

164 Ibid, p. 2.

165 HRATF, *HRATF response to 2011 Hunter Valley Access Undertaking (HVAU) 2017 variation application*, 14 February 2018, p. 14.

166 See ACCC, *Draft Decision: Australian Trail Track Corporation's December 2017 Variation to the 2011 Hunter Valley Access Undertaking*, 28 June 2018, pp. 69–75.

ARTC proposed this change in the 2016 HVAU, 2017 HVAU and December 2017 Variation applications. The ACCC considers that if Train Km is not the predominant driver of Fixed Costs, then the proposed structure of coal Access Charges may be providing incentives resulting in the inefficient operation of, use of and investment in the Hunter Valley rail network (section 44ZZA(3)(aa)).

Charge differentiation for users of adjoining networks

The ACCC notes Pacific National and Origins' concerns regarding the effect of path based pricing on Access Holders whose train configurations are limited by infrastructure constraints on adjoining networks. Origin's concerns reflect those raised by Pacific National and Centennial Coal in submissions to the December 2017 Variation. The ACCC agrees with ARTC's position that basing a portion of TOP Charges on the basis of GTK goes some way to mitigating the effect of path based pricing for services outside of the Services Envelope. However, as noted by Pacific National, the ACCC considers that the extent to which the proposed structure of Access Charges mitigates this effect is unclear. While section 4.15 of the September 2018 Variation includes broad considerations that could address these concerns, the ACCC notes that this section does not explicitly refer to traffic from adjoining networks.

The ACCC notes that in ARTC's previously proposed 2017 HVAU, since withdrawn, ARTC introduced an amendment at section 4.16(b) that the ACCC considers addressed concerns raised by Centennial Coal, Pacific National and Origin. The proposed section 4.16(b) stated that ARTC may consider the characteristics of adjoining networks, including axle load or train length restrictions, in formulating Access Charges for affected parties, irrespective of whether the Service was in or outside the Services Envelope. In the Draft Decision on the 2017 HVAU, the ACCC considered proposed section 4.16(b) was appropriate. The ACCC reiterated this position in the Draft Decision for the December 2017 Variation, where the ACCC stated that such drafting should be included in the HVAU to provide more clarity and certainty for Access Holders using adjoining networks with limiting infrastructure constraints. The ACCC notes that ARTC did not address this in the September 2018 Variation.

The ACCC considers ARTC should include this issue in the scope of its review of the 'current pricing approach' under section 2.3(d) of the HVAU, and incorporate findings from the revenue into the next HVAU. The section 2.3(d) review is discussed further in chapter 5 of this Decision.

Future review of pricing approach

The ACCC notes HRATF's submission that a number of its members would potentially object to the continuation of path based pricing once the loss capitalisation account in PZ3 is paid down.[167] The ACCC considers that ARTC should include the structure of access charges as a matter included in its review of the 'current pricing approach' under section 2.3(d) of the September 2018 Variation. ARTC's proposed review mechanism is discussed in further detail in chapter 5 of this Decision.

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167 HRATF, *HRATF supplementary submission*, 30 May 2018, p. 2.

10. Agreements – IAHA and OSA

The IAHA sets out the terms and conditions under which ARTC will grant Access Holders rights of Access to the Hunter Valley rail network for the purposes of coal transport.

The Operator Sub-Agreement (**OSA**) sets out the terms and conditions under which ARTC will grant an accredited rail operator rights to use and provide Services to an Access Holder.

10.1. ARTC proposal

ARTC proposes changes to the IAHA. ARTC has not proposed any changes to the OSA.

The key amendments to the IAHA are listed in Table 5Table 5 below.

Table 5: Key amendments to the IAHA

Impacts	Clause	Change proposed
Path based pricing	1.1	'2017 Rebate Process', 'New RML', 'New ROR', 'Original 2016 Rebates', 'Revised 2016 Rebates', and 'Second 2016 Period' removed. '2019 PBP Variation Date' added, and defined as 1 January 2019. 'Indicative Access Charges', 'Indicative Services', 'Interim Indicative Access Charges' and 'Interim Indicative Services' removed. 'Services Envelope', 'Standard Access Charges' and 'Train Path Schedule Spreadsheet' added.
	8.4	Clause removed.
	11.5(b)	'and that Non-Compliance Service is outside of the Services Envelope' added.
	1.2, 2.1, 3.1 and 4.1 of Schedule 3	Equations and definitions changed to reflect shift from GTK to contracted Train Km; references to the Services Envelope added, references to indicative services removed and contract dates changed including reference to '2019 PBP Variation Date'.
	3 of Train Path Schedule 1	Path description and service assumptions changed to reflect Services Envelope conditions.
Other	Annexure B	Train Path Schedule Spreadsheet included.
	1.1, 2.3(a), 3.2(a), 3.3(c), 3.5(a), 5.4(c) and 11.1(c) 1.2 and 2.1 of Schedule 3 1 of Train Path Schedule 1	'Train Path Schedule Spreadsheet' added and 'Train Path Schedule' changed to 'Train Path Schedule Spreadsheet'.
	1.1 – Definition of Train Path	'port' changed to 'Port of Newcastle'.

Impacts	Clause	Change proposed
	and 3.3(c) 2.1 of Schedule 3 3.2 of Train Path Schedule 1	
	3.3(e)	Clause removed–note review previously completed.
	5.4(c)	‘subject to clause 5.4(i)’ removed’.
	5.4(i), (j) and (k)	Clauses removed. ARTC originally submitted that these provisions were included as it ‘addresses the operation of the system wide true up test and ad hoc rebates given the different pricing applicable during the 2016 [and 2017] calendar year[s].’[168] ARTC submits that these provisions are redundant ‘now that the true up test has been completed for those years’.[169]
	5.7(a)	‘in the Australian Financial Review newspaper’ removed.
	16.8 and 16.4(d)	Clause removed, reference to clause removed–note review previously completed.
	20.1(d), 20.2(d) and 20.3(b)	Notice by email added.

The ACCC notes that ARTC has not provided an explanation for the majority of changes to the IAHA–with the exception of the changes to Schedule 3 of the IAHA.[170] However, they appear to be largely consistent with the changes proposed in the 2017 HVAU.[171] Accordingly, the ACCC understands that these changes relate to the introduction of path based pricing. Additionally, ARTC has removed clauses which reference reviews previously completed and additional provisions that are now redundant.

10.2. Comparison to the December 2017 Variation

With regard to clause 11.5(d) of the IAHA, which ARTC previously sought to remove as part of its December 2017 Variation, ARTC submits that it has reinstated this provision in the September 2018 Variation as it ‘allows customers to seek take or pay reductions arising from the path reduction caused by a change to the service assumptions’.[172]

10.3. Stakeholder submissions

Regarding the December 2017 Variation, HRATF made the broad statement that it does not hold a common position on path based pricing.[173] However HRATF also made the following

[168] ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term*, 6 June 2017, pp. 12–13.

[169] ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term*, 28 September 2018, p. 32.

[170] ARTC, *2011 Hunter Valley Coal Network Access Undertaking Variation – Explanatory Guide*, 21 December 2017, p. 103.

[171] ARTC, *2017 Hunter Valley Coal Network Access Undertaking Explanatory Guide*, 9 December 2016, pp. 81–100.

[172] ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term*, 28 September 2018, p. 2.

[173] HRATF, *HRATF response to 2011 Hunter Valley Access Undertaking (HVAU) 2017 variation application*, 14 February 2018, p. 3.

comments regarding the proposed amendments to the IAHA that the ACCC understands reflect the introduction of path based pricing:[174]

- The Train Path Schedule Spreadsheet under Schedule 3 of the IAHA 'appears to be sensible and appropriate.'
- HRATF accepted the consistency of the new tariff structure, resulting from path based pricing, being included in the IAHA. HRATF stated that it is imperative that all Coal Customers operate from the same pricing structure.
- The updated formulae in Schedule 3 of the IAHA are complex, however 'appear workable based on the worked examples provided by ARTC to producers.'

HRATF did not make any further submissions on ARTC's proposed amendments to the IAHA in its submission on the September 2018 Variation other than the general statement that it 'supports the September Variation as proposed by ARTC and would welcome the ACCC moving quickly to a decision to approve it'.[175]

In relation to the December 2017 Variation, Pacific National raised concerns with the proposed removal of clause 11.5(d) of the IAHA. Clause 11.5(d) states:

> *Despite clause 11.5(c)(iii), ARTC will not unreasonably withhold its consent to a permanent change to the Services Assumptions for a Train Path that would lead to a reduction in TOP Charges if, in ARTC's reasonable opinion reached in consultation with the HVCCC, the variation involves the transfer to a Service which provides for more efficient use of Capacity and Coal Chain Capacity.*

Pacific National noted that clause 11.5(d) protects Access Holders from TOP Charges if that Access Holder shifted to a more efficient use of rail capacity resulting in the use of fewer train paths. Pacific National argued that removing clause 11.5(d) would mean that above-rail operators are less incentivised to adopt more efficient forms of rolling stock and train configurations. Pacific National advocated for clause 11.5(d), or a similar clause, to be reinstated into the IAHA.[176]

In response to the September 2018 Variation, Pacific National submits that it:[177]

> *very strongly supports the reinstatement of this clause [11.5(d)] which protects access holders from take or pay impacts if they shifted to a service which use rail capacity more efficiently.*

10.4. ACCC view

The ACCC notes that the changes to the IAHA relate primarily to the introduction of path based pricing. As discussed in chapter 9, the ACCC accepts the introduction of path based pricing on the basis that the majority of stakeholders support this proposal as part of the broader 'package' of the September 2018 Variation. As such, the ACCC additionally accepts the proposed changes to the IAHA.

The ACCC notes that ARTC has responded to stakeholder concerns and the ACCC's view in the Draft Decision on the December 2017 Variation that clause 11.5(d), or a similarly effective clause, should be reinstated into the IAHA. The ACCC considers that this provision

174 Ibid.

175 HRATF, HRATF supplementary submission – September HVAU Variation, 19 October 2018, p. 2.

176 Pacific National, *Pacific National Submission to the ACCC in Relation to the ARTC's Proposed Variation to the 2011 HVAU*, February 2018, p. 8.

177 Pacific National, *Pacific National Submission to the ARTC Variation Application to ACCC to Vary the 2011 HVAU*, 15 October 2018, p. 4.

makes the incentive to Access Holders' clear and certain, which is in the legitimate business interests of ARTC and the interests of those who might want access to the Hunter Valley rail network (sections 44ZZA(3)(a), (c) and (e)).

The ACCC additionally notes that ARTC had previously sought to introduce the term '2018 PBP Variation Date' under clause 1.1 and Schedule 3 of the IAHA. This was a new undefined term that has since been replaced with the term '2019 PBP Variation Date', defined as 1 January 2019. This aligns with the amended section 2.3(b)(ii) of the HVAU which specifies that 'all provisions as varied by the Varied Undertaken are taken to have commenced operation on 1 January 2019'. The operation of 2.3(b) is discussed in further in chapter 4. The ACCC considers that this new definition clearly defines the term in reference to a particular date. This provides clarity and certainty for ARTC, Access Holders and access seekers, which is in the legitimate business interests of ARTC and the interests of those who might want access to the Hunter Valley rail network (sections 44ZZA(3)(a), (c) and (e)).

With these amendments, the ACCC considers the rest of the IAHA appropriate, as it provides clarity and certainty enabling ARTC, Access Holders, and access seekers to be sufficiently aware of their respective rights and obligations, and thereby avoid unnecessary costs, monetary or otherwise, when utilising the processes set out in the HVAU and IAHA (section 44ZZA(3)(e)). The ACCC considers that this is in the legitimate business interests of ARTC, and the interests of those who might want access to the Hunter Valley rail network (sections 44ZZA(3)(a) and (c)).

11. Removal of redundant sections from HVAU

11.1. ARTC proposal

In the September 2018 Variation ARTC proposes to remove several sections from the current HVAU due to redundancy. ARTC proposes three reasons for the removal of these sections:

- transitional arrangements from 2011 when the Hunter Valley rail network was regulated by IPART, which are no longer applicable
- change of pricing method from Indicative Services to path based pricing
- reviews that have been completed and will not be carried out during this term of the HVAU.

The sections proposed for removal from the September 2018 Variation are listed below in Table 6Table 6. For those sections proposed to be removed via the December 2017 Variation (and which are largely mirrored in the September 2018 Variation), ARTC submitted that it consulted with customer representatives about the removal of those sections.[178]

Table 6: Sections proposed for removal from the September 2018 Variation

Reason for removal	Section	Explanation of section
End of transitional arrangements	2.3(d)	Section 2.3(d) of the June 2017 Variation required ARTC to lodge a variation application to the ACCC by 31 December 2017 to incorporate path based pricing and apply an incremental cost methodology. ARTC met this requirement when it submitted the December 2017 Variation.
	2.4(b)	Specifies that ARTC will reserve train paths for Non-Coal Access Holders as part of a transitional arrangement.
	4.15(a)(iii)	Conditions ARTC must meet for its Charges of particular Interim Services during the Regulatory Transition Period.
Change to path based pricing	4.17	Outlines Initial Indicative Services and Initial Indicative Access Charges.
	4.18	Outlines the determination of Final Indicative Services.
	4.19	Outlines Interim Services and Interim Access Charges.
	4.20(h)	Interpretive provision relating to finalising Indicative Access Charges.
	4.20(i)	Process for disputing Interim Access Charges or Initial Indicative Access Charges.

[178] ARTC, *2011 Hunter Valley Coal Network Access Undertaking Variation – Explanatory Guide*, 21 December 2017, p. 22.

	4.22	Outlines Indicative Access Charges for the previous Extension Period.
	4.23	Set out that Clause 5.4 of the IAHA is a Tier 1 (Mandatory) provision that is automatically incorporated into Access Holder Agreements for the purposes of calculating ad hoc rebates and applying the system wide True Up Test (**TUT**) where there are two sets of pricing during the 2016 calendar year. ARTC submits that this section is redundant 'now that the true up test has been completed for those years'.[179]
Review completed	5.8	Outlines a review process to be undertaken within 12 months of the Commencement Date of the 2011 HVAU for identifying and assigning capacity losses.
	13.3	As identified by the ACCC in its Draft Decision on the December 2017 Variation, this provision required ARTC to prepare options for, and consult in relation to, the development of a non-TUT performance incentive scheme. This review was completed in June 2015 and ARTC provided a report to the ACCC.[180]
	13.4	As identified by the ACCC in its Draft Decision on the December 2017 Variation, the provision obliged ARTC within two calendar years of the commencement of the 2011 HVAU, to conduct a review of the operation and effectiveness of the system wide TUT that is set out in Schedule 2 of the IAHA. ARTC completed this review in September 2014.
	13.5	As identified by the ACCC in its Draft Decision on the December 2017 Variation, this provision required ARTC to prepare options for, and consult in relation to, the development of a TUT-related performance incentive scheme. This review was completed June 2015 and ARTC provided a report to the ACCC.[181]
Definitions	14	Removal of redundant defined terms: 'Direct Costs', 'FCC', 'Final Indicative Service', 'Incremental Costs', 'Indicative Access Charge', 'Indicative Services', 'Initial Indicative Access Charges', 'Initial Indicative Services', 'Initial Period', 'Interim Access Charges', 'Interim Services', 'Interim Period', 'Interim ROR', 'NCC', 'Variation Commencement Date' and 'VCC'.

179 ARTC, *Application by ARTC to vary the Hunter Valley Access Undertaking to extend term*, 28 September 2018, p. 32.

180 ARTC, *Hunter Valley Coal Network Access Undertaking Positive performance Incentive Scheme Report,* June 2015.

181 Ibid.

11.2. Stakeholder submissions

The ACCC did not receive specific submissions with regard to the proposed removal of redundant sections.

However, HRATF did make the general submission that it ‘supports the September [2018] Variation and, given the considerable consultation and engagement that has already occurred in relation to the December [2017] Variation, we would welcome the ACCC moving directly to a final decision to accept it.’[182]

Similarly, Pacific National makes the general submission that it ‘supports the ARTC September 2018 application to the ACCC to vary the 2011 HVAU’.[183]

11.3. ACCC view

The ACCC considers ARTC’s proposed removal of the sections outlined in Table 6Table 6, on the basis that they are redundant clauses, prevents confusion that might arise from Access Holders or access seekers who might take these sections to be operative. The ACCC considers the removal of redundant clauses provides clarity and certainty, which benefits those seeking access to the Hunter Valley rail network (sections 44ZZA(3)(c) and (e)).

The ACCC acknowledges ARTC’s statement that stakeholders were consulted on the removal of the redundant sections in Table 6Table 6 and notes the submissions from stakeholders in support of ARTC’s September 2018 Variation.

The ACCC also recognises ARTC’s clarification in response to the ACCC’s Draft Decision on the December 2017 Variation to remove sections 13.3, 13.4 and 13.5 of the HVAU. The ACCC considers the removal of these sections benefits those seeking access to the Hunter Valley rail network through added clarity and certainty (sections 44ZZA(3)(c) and (e)).

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182 HRATF, *HRATF supplementary submission – September HVAU Variation*, 19 October 2018, p. 1.

183 Pacific National, *Pacific National Submission to the ARTC Variation Application to ACCC to Vary the 2011 HVAU*, 15 October 2018, p. 4.

12. ACCC decision to consent to ARTC's variation application

The ACCC considers that, in the circumstances, it is appropriate to consent to the September 2018 Variation, having regard to the matters in section 44ZZA(3) of the Act. The ACCC notes that ARTC has incorporated the recommended amendments for clarity and certainty set out in its Draft Decision on the December 2017 Variation.

The ACCC also recognises that the majority of stakeholders have reached a commercial decision to accept ARTC's proposal for the duration of the current HVAU. This stakeholder support was subject to the inclusion of ARTC's proposed review mechanism at section 2.3(d). While different stakeholders have raised concerns with various elements of ARTC's proposal, the majority of stakeholders collectively view the 'package' proposed by ARTC as providing a preferable commercial outcome when compared to the current HVAU.

In providing their support, stakeholders have accepted ARTC's assurances that their agreement to the proposed variation will not set a precedent for a revised undertaking when the current term of the HVAU expires in 2021, and that all relevant terms of the undertaking will be reconsidered. The ACCC is confident that stakeholders are aware of the implications of the variation on the operation of the HVAU based on its extensive consultation with stakeholders over multiple years. It is on this basis that the ACCC considers it appropriate to consent to the September 2018 Variation.

While the ACCC's decision is to consent to the September 2018 Variation, it has significant concerns regarding a number of ARTC's amendments. The ACCC has provided detailed explanations of those concerns in this Decision and in its Draft Decision on the December 2017 Variation. In addition, as the scope of the proposed review mechanism at section 2.3(d) has yet to be determined, the ACCC considers it important to provide its views on each of the proposals in the September 2018 Variation. The ACCC considers that this will assist in facilitating discussions between ARTC and stakeholders regarding this review, and in the development of any replacement HVAU.

Outstanding issues

Further to this, the ACCC notes that a number of outstanding issues were considered to be appropriate in its assessment of the 2017 HVAU. However, aside from removing redundant clauses, ARTC decided not to seek to incorporate amendments other than those required under the now removed section 2.3(d) of the June 2017 Variation, into the September 2018 Variation.

Consequently, the ACCC considers that ARTC should give consideration to incorporating these changes into the next HVAU. To facilitate the negotiation of the next HVAU proposal, Table 7Table 7 provides a summary of the ACCC's views on these outstanding issues, which were also discussed in greater detail in the ACCC's draft decision on the 2017 HVAU.

Table 7: ACCC views on outstanding issues from the 2017 HVAU draft decision

Outstanding Issue	ACCC view expressed in 2017 HVAU draft decision
Membership and operation of the RCG	The ACCC considered ARTC's proposal to extend the membership of RCG to all Access Holders to include a greater level of consultation was appropriate.[184]

[184] ACCC, *Draft Decision – Australian Rail Track Corporation's 2017 Hunter Valley Access Undertaking*, 20 April 2017, p. 214.

Outstanding Issue	ACCC view expressed in 2017 HVAU draft decision
Access Charges for users on adjoining networks	The ACCC considered ARTC's proposed amendments to provide for flexibility in determining Access Charges when users faced infrastructure restrictions on adjoining networks, were appropriate.
Improvements in the operation of the TUT	The ACCC considered ARTC's proposed changes to the TUT auditor provisions, to provide a limit on the number of consecutive years an auditor can perform the annual TUT audit, were appropriate.[185]
Changes to the IAHA and OSA	The ACCC considered a number of amendments to the IAHA, proposed by ARTC and stakeholders, to be appropriate.[186]
HVCCC consultation principles	The ACCC considered ARTC's proposed amendments to the HVCCC consultation principles provided additional clarity around the HVCCC consultation process as they would strengthen obligations on ARTC.[187]
Performance measures	The ACCC considered ARTC's proposed Network Key Result Areas were appropriate.[188]

Finally, the ACCC recognises the extensive work undertaken by ARTC in developing the September 2018 Variation, the various iterations of the HVAU and the December 2017 Variation through 2015 to 2018. The ACCC also recognises the ongoing contribution of stakeholders in consulting with, providing submissions to, and working with ARTC and the ACCC throughout this process.

185 Ibid, p. 234.

186 Ibid, pp. 242–4.

187 Ibid, pp. 207–8.

188 Ibid, p. 221.