



Public Competition Assessment

25 August 2022

Aurizon Holdings Ltd - proposed acquisition of One Rail Australia Holdings LP

The ACCC's decision

1. On 14 July 2022, the Australian Competition and Consumer Commission (**ACCC**) announced its decision not to oppose the proposed acquisition of One Rail Australia Holdings LP (**One Rail**) by Aurizon Holdings Ltd (**Aurizon**) (the **proposed acquisition**), after accepting a section 87B divestiture undertaking¹ (**Undertaking**).
2. The Undertaking requires Aurizon to divest all of One Rail's assets, operations, and contracts on the east coast, including the entirety of its coal rail haulage operations in New South Wales and Queensland (**One Rail East Coast**). This will leave Aurizon owning and operating One Rail's bulk rail haulage and intermodal services business in South Australia and the Northern Territory (**One Rail SA/NT**). The divestiture may occur by either a trade sale to an ACCC approved purchaser or via a demerger that would establish a new ASX listed entity.
3. The ACCC considers that the proposed acquisition, in the absence of the Undertaking, would be likely to have the effect of substantially lessening competition in contravention of section 50 of the *Competition and Consumer Act 2010* (the **CCA**). However, the ACCC considers that the Undertaking offered by Aurizon is likely to address the ACCC's competition concerns in this matter.
4. The ACCC considered the competitive effects of the proposed acquisition in the following markets:
 - the supply of coal rail haulage services (**coal haulage services**) in NSW and Queensland,
 - the supply of rail haulage services for non-coal bulk commodities/products (**bulk rail haulage services**) in various regions in Australia, and

¹ Merger parties can provide the ACCC with a court-enforceable undertaking under section 87B of the *Competition and Consume Act 2010* to remedy competition concerns identified by the ACCC.

- the supply of bulk rail haulage services or intermodal services on or along the Adelaide-Darwin corridor.
5. Without the divestment of One Rail East Coast, the ACCC considers that the proposed acquisition would reduce the number of main competitors in the supply of coal haulage services in New South Wales and Queensland from three to two, likely resulting in higher prices and/or decreased service levels. Aurizon is currently one of the major suppliers in these markets. However, the Undertaking will ensure that One Rail East Coast is preserved as a competitor.
 6. The ACCC also considers that the Undertaking will preserve One Rail East Coast as a potential competitor to Aurizon for the supply of bulk rail haulage services in the future.
 7. The ACCC also considers the proposed acquisition does not change the nature or degree of any vertical competition concerns on the Adelaide-Darwin corridor.
 8. This Public Competition Assessment outlines reasons for the decision by the ACCC not to oppose the proposed acquisition, taking into account the Undertaking.
 9. Please note that this and other public competition assessments are subject to the following qualifications:
 - The ACCC considers each transaction on a case-by-case basis and so the analysis and decision outlined in one assessment will not necessarily reflect the ACCC's view of another transaction, even where that other transaction may involve the same or a related market.
 - As assessments are relatively brief and do not refer to confidential information provided by the parties or other market participants, assessments do not necessarily set out all the issues and information considered by the ACCC, nor all the analysis of the matter and reasons for the decision by the ACCC.

The parties and the transaction

10. Aurizon entered into an agreement with various entities of Macquarie Asset Management (**MAM**), on behalf of MAM's funds, and PGGM Infrastructure Fund to acquire One Rail.

The acquirer: Aurizon

11. Aurizon is a provider of coal haulage, bulk rail haulage services and rail network services ('below-rail' services). Aurizon states that it is the largest rail freight operator for coal haulage and bulk rail haulage services in Australia. It is listed on the ASX.

Rail haulage services

12. Aurizon provides coal haulage and bulk rail haulage services for bulk commodities/products in Queensland, NSW and Western Australia.

13. Coal haulage is the supply and operation of locomotives and rail wagons by rail operators to load coal into wagons at an origination site, transport the coal by rail and unload the coal at a destination site, including at port terminal facilities.
14. Aurizon hauls around half of Australia's export coal volume. It transported 202 million tonnes of coal in the 2020/21 financial year. It provides coal haulage services on:
 - the Central Queensland Coal Network (**CQCN**), servicing Queensland's Bowen Basin coal region,
 - the Hunter Valley and Illawarra coal systems in NSW, and
 - the Collie coal system in WA.
15. In addition to coal haulage, Aurizon currently also transports, and/or is capable of transporting, other bulk commodities/products by rail such as iron ore, cement, bauxite, alumina, base metals, refined metals, grain, livestock, fertiliser and dangerous goods.

Rail network services

16. Aurizon also operates the CQCN. As the operator, its responsibilities include: managing access to the network by coal haulage operators; safety, signalling and communication systems; train control; rail construction and maintenance.
17. Aurizon's conduct as operator of the CQCN is subject to an access undertaking approved by the Queensland Competition Authority. The current access undertaking under which Aurizon operates was approved in 2019.

The target: One Rail

18. One Rail is a provider of coal haulage, bulk rail haulage and intermodal services and rail network services. One Rail SA/NT provides below-rail and bulk rail haulage and intermodal services in SA and the NT on the Adelaide-Darwin corridor and One Rail East Coast provides coal haulage services in NSW and Queensland.

Coal haulage in NSW and Queensland

19. One Rail East Coast provides coal haulage services in the Hunter Valley from numerous mine sites to the Port of Newcastle in NSW. This coal haulage is predominately from Glencore mines, but also includes coal haulage for other miners in the Hunter Valley, as well as for domestic end users. It also provides coal haulage services in the Mackay region of Queensland.

Bulk rail haulage and intermodal services in SA and the NT

20. One Rail SA/NT provides bulk rail haulage services for bulk commodities for customers in SA and the NT, including iron ore, manganese, gypsum, copper and grain.

21. One Rail SA/NT also provides intermodal services on the Adelaide-Darwin corridor, transporting consumer goods, general cargo and bulk liquids. In contrast to coal haulage or bulk rail haulage services, intermodal freight is typically packed in shipping containers, which allows the freight to be more easily transferred between modes of transport such as road, rail and/or sea.

Rail network services

22. One Rail SA/NT also operates two regulated rail networks, together spanning from Tarcoola in SA to Darwin in the NT.
23. Access to One Rail SA/NT’s SA rail lines is managed under the *Railways (Operations and Access) Act 1997 (SA)*, while access to One Rail SA/NT’s NT rail lines is managed under the *AustralAsia Railway (Third Party Access) Act 1999 (SA)*. The Essential Services Commission of South Australia regulates both Acts and the access regime for One Rail Network’s rail lines.

Review timeline

24. The following table outlines the timeline of key events for the ACCC in this matter.

Date	Event
7 December 2021	The ACCC commenced a review of the proposed acquisition under its Merger Process Guidelines.
28 February 2022	The ACCC requested additional information from Aurizon. The timeline was suspended pending receipt of this information.
9 June 2022	The ACCC issued a Statement of Issues regarding the proposed acquisition. The ACCC also commenced market consultation on a draft proposed s87B undertaking.
14 July 2022	The ACCC announced it will not oppose the proposed acquisition following the acceptance of the Undertaking by the ACCC.

Market inquiries

25. The ACCC conducted market inquiries with a range of industry participants, including competitors, potential competitors, customers, input suppliers, industry bodies, other regulatory agencies and other interested parties. Submissions were sought in relation to the potential competition issues arising from the proposed acquisition and a draft section 87B undertaking proposed by Aurizon.

Market definition

26. The ACCC’s starting point for considering which markets will be affected by a proposed acquisition is to identify the areas of overlap between the products and/or services actually or potentially supplied by the merger parties. The ACCC then considers other actual or potential suppliers of those products and/or services, as well as what other products and/or services constitute sufficiently

close substitutes to provide a significant source of constraint on the merged entity.

27. As indicated above, Aurizon and One Rail presently overlap in the supply of coal haulage services in each of NSW and Queensland. The parties do not presently overlap in the supply of bulk rail haulage services. However, as explained below, the ACCC also considered the potential for Aurizon and One Rail to become close competitors in one or more regional markets for the supply of bulk rail haulage services in the future if the proposed acquisition did not proceed.
28. In this matter, the ACCC considers that there are separate markets for coal haulage and bulk rail haulage services and that these markets are principally state-based. This conclusion is based on the following product and geographic considerations.

Product dimension

29. The ACCC considered the extent to which suppliers of bulk rail haulage services could switch to supplying coal haulage in the event of a sufficient price incentive, or vice versa. For example, locomotives and wagons used for bulk rail haulage tasks may, in some circumstances, also be capable of being repurposed to haul coal. However, for reasons outlined later in this document, the ACCC is of the view that there are weak prospects of substitution from bulk rail haulage into coal haulage. Accordingly, the ACCC considered the proposed acquisition in separate markets for coal haulage services and bulk rail haulage services.

Geographic dimension

30. The ACCC has also considered the relevant geographic scope of markets for the supply of coal haulage and bulk rail haulage services. The ACCC considers that the extent to which suppliers can switch between supplying rail haulage services in one geographic region to another is limited by:
 - differences in rail gauge between States and Territories and corridors. In particular, many rail networks in Australia are standard gauge, including in the Hunter Valley in NSW. However, rail haulage in Queensland is on narrow gauge tracks. Market feedback has indicated that standard gauge assets cannot easily be repurposed to operate on narrow gauge networks,
 - the time and cost involved in both (a) moving existing rail haulage assets between States or Territories to operate along different rail corridors and (b) obtaining regulatory approvals in each jurisdiction for the use of rail assets from other jurisdictions, and
 - requiring access to existing maintenance/provisioning facilities, and if access is unavailable, the time and cost involved in building new maintenance/provisioning facilities.
31. Therefore, the ACCC's view is that aside from the Adelaide-Darwin corridor (which operates as a single system), the geographic dimension of markets for coal haulage and bulk rail haulage services is generally state-based for the purpose of analysing the proposed acquisition.

Competition analysis

Lessening of competition in coal haulage in NSW and Queensland

Market concentration

32. The ACCC considers that the supply of coal haulage services in NSW and Queensland is highly concentrated because:
- in NSW, there are three main suppliers in Pacific National, Aurizon and One Rail East Coast, and
 - in Queensland, there are two main suppliers in Aurizon and Pacific National. One Rail East Coast entered Queensland in 2020 and has been successful in supplying a small share of coal haulage services. Separately, Queensland coal miner BHP-Mitsubishi Alliance, the third largest in Queensland, owns and operates its own coal haulage trains but does not provide coal haulage services for other miners.
33. The ACCC received various estimates of the volume of coal hauled by each of the market participants, based on broadly-available information about export volumes and train network usage. Table 1 provides approximate market share figures in NSW and Queensland in the financial year 2020-21, based on these estimates.

Table 1: Market share estimates for coal haulage in NSW and Queensland

Operator	NSW	Queensland
Pacific National	40-50%	25-30%
Aurizon	30-35%	60-70%
One Rail East Coast	20-30%	0-5%
BHP-Mitsubishi Alliance	Does not haul coal in NSW	5-10%
Southern Shorthaul Railroad	0-5%	Does not haul coal in QLD

Closeness of competition

34. The ACCC considers that Aurizon and One Rail East Coast exert a strong and effective competitive constraint on each other and on Pacific National in both states. While most of the coal volumes One Rail East Coast transports is under contracts with Glencore, it has also been successful in obtaining coal haulage contracts with other miners.
35. Market participants submitted to the ACCC that One Rail East Coast is currently a strong competitor in NSW based on its proven record of performance in that state, and that they would likely consider One Rail East Coast for their future needs and/or expect that One Rail East Coast will participate in upcoming tender processes.

36. In Queensland, One Rail East Coast entered in 2020 with one coal haulage train set to provide services to Glencore. One Rail has since won a small amount of work with other coal miners in Queensland. It is in the process of expanding its capacity in Queensland through the acquisition of a second train set. Market feedback suggested that in Queensland One Rail East Coast has been aggressive on price, flexible on other contractual terms, and performed more favourably than Aurizon or Pacific National on key operational metrics. Its entry is said to have created new competitive tension in the supply of coal haulage services in Queensland.

Barriers to entry and expansion

37. The ACCC considers that barriers to new rail haulage suppliers entering coal haulage in NSW or Queensland are high.
38. Some market participants referred to and reiterated the observations in the ACCC's Statement of Issues in a previous matter when commenting on the likelihood of new entry or expansion by existing suppliers.² As previously identified by the ACCC, the main barriers faced by a new entrant include:
- an entrant must outlay significant capital on rollingstock, with a lead-in time for delivery often measured in years. A substantial proportion of this investment may be 'sunk' – irrecoverable on exit – discouraging entry,
 - recruiting and training train drivers can be difficult, due to a lack of supply,
 - gaining access to provisioning facilities can be challenging and building such facilities can be costly,
 - a rail operator must meet regulatory requirements, such as operator accreditations and licences, before it can bid for tasks,
 - coal producers place a high value on the bulk rail hauler's demonstrated reliability at scale, which favours incumbents as coal haulage is a critical input to coal exports, with any delays or problems in delivering coal to port significantly impacting producers, and
 - there are significant competitive advantages for incumbents, based on scale and scope (breadth-of-service), including having larger train fleets and a range of customers.
39. The ACCC considered that while these barriers may be lower for an existing supplier of bulk haulage services that is considering entering coal haulage, they would still constitute a significant impediment to scaled entry. Notably, the scale of the operations undertaken by existing coal haulage operators in NSW and Queensland is significantly larger than the bulk rail haulage services operations in those states. This may mean that bulk rail haulage services operators find it hard to demonstrate their reliability at scale to large coal customers.
40. The ACCC also received submissions that there is increased uncertainty about the long-term future of coal. Similarly, there has been an increase in 'societal

² Statement of Issues (Aurizon and Pacific National acquisitions of GRail)
(<https://www.accc.gov.au/system/files/public-registers/documents/MER16%2B9857.pdf>)

risk' associated with coal projects, including an increased reluctance of banks to finance coal-exposed businesses and increased shareholder activism on the issue. This would affect investment decision-making for potential new entrants into coal haulage and might make it challenging for a firm to obtain finance to enter these markets. The ACCC understands that this uncertainty is greater for projects in NSW, where the majority of coal produced is thermal coal (for use in power stations), than in Queensland, where the majority of coal produced is metallurgical coal (for use in smelters).

41. In this context, the ACCC considers One Rail East Coast's entry into Queensland, expanding its coal haulage operations from its NSW base, to be a unique occurrence that is not indicative of low barriers to entry. One Rail entered the Queensland market in 2020 with one coal haulage train set to provide services to Glencore.

Conclusion

42. Based on the high levels of market concentration, the importance of One Rail East Coast to current competitive dynamics, and barriers to entry and expansion in relation to the coal haulage services markets in NSW and Queensland, the ACCC considers that the proposed acquisition, absent the Undertaking offered by Aurizon, would be likely to have the effect of substantially lessening competition in the supply of coal haulage services in both NSW and Queensland.

Loss of potential future competition in the supply of bulk rail haulage services

43. As noted above, Aurizon and One Rail do not presently directly compete to any significant extent in the supply of bulk rail haulage services. This is because they currently supply these services in different regions: Aurizon provides these services in Queensland, NSW and WA, while One Rail provides them in SA and the NT.
44. However, the ACCC considered the potential for Aurizon and One Rail to become close competitors in one or more regional markets for the supply of bulk rail haulage services in the future if the proposed acquisition did not proceed.
45. In assessing this potential loss of future competition the ACCC considered:
 - whether One Rail's recent entry into the supply of coal haulage services in Queensland would provide it with the platform to begin supplying bulk rail haulage services in Queensland in the absence of the proposed acquisition,
 - whether Aurizon would have the commercial incentive to expand its supply of bulk rail haulage services in the absence of the proposed acquisition, given its publicly-stated intentions to grow its bulk haulage business,
 - the prospects of significant entry into bulk rail haulage services in either NSW or Queensland by current suppliers of coal haulage services in those states are greater than the reverse,

- market feedback received during the review suggesting some, albeit limited, historical competition between Aurizon and One Rail in bulk rail haulage services, and
 - the strength of competition from other suppliers already competing in the relevant regions. Depending on the product and region being considered, other existing competitors may include one or more of Pacific National, Qube, Watco, Southern Shorthaul Railroad, or Bowmans Rail.
46. The ACCC did not reach a concluded view on whether, in the absence of the Undertaking, the proposed acquisition would be likely to have the effect of substantially lessening competition in one or more markets for the supply of bulk rail haulage services.
47. Having taken all the relevant information into account, the ACCC formed the view that the Undertaking will resolve any potential concerns in these markets. This is because the divestment of One Rail East Coast will preserve it as a potential competitor to Aurizon for the supply of bulk rail haulage services in the future.

Vertical foreclosure by the operator of above and below rail services in SA/NT

48. Concerns were raised with the ACCC that One Rail's ownership of rail networks in South Australia and the Northern Territory allow it to favour its own bulk rail haulage services on those networks to the detriment of competitors. The concerns expressed included that:
- One Rail's access charges to these networks are not transparent,
 - it had been difficult to get timely quotes from One Rail for rail-access charges, and
 - One Rail required commercially sensitive information from rail operators seeking access to use the networks that was unnecessary to meet the access request.
49. Concerns were also raised about the ability of the regulation in place to adequately address the competitive effects of vertical integration in these regions.
50. However, the ACCC's merger assessment is limited to competition effects that are the result of the proposed acquisition and cannot address concerns with the existing rail industry or its regulation.
51. The ACCC is satisfied that the proposed acquisition does not result in Aurizon having a materially greater ability and incentive, than One Rail currently has, to prevent or impede a rival rail operator from competing on the SA and the NT networks. Since Aurizon does not presently provide above-rail services on any track operated by One Rail in those regions, the proposed acquisition would not lead to any structural change to the supply of above or below rail services in SA or the NT – it would simply transfer One Rail's existing business in those regions to Aurizon.

Undertaking

52. As outlined above, Aurizon offered a court enforceable undertaking pursuant to section 87B of the Act at the outset of the ACCC's review to proactively address any potential ACCC competition concerns.
53. The Undertaking requires Aurizon to divest One Rail East Coast by either trade sale or demerger. The ACCC does not often accept demerger remedies as they carry a higher level of risk, greater uncertainty and require a greater degree of scrutiny than standard divestiture remedies.
54. These risks largely arise from difficulties in assessing whether the proposed demerged business would become an effective, stand-alone and long-term competitor, capable of replacing the competition that would otherwise be eliminated by a proposed acquisition. The management team and board of directors of a demerged entity are generally not settled prior to a demerger, therefore this makes it more difficult to assess their business plan, motivation and capabilities compared with assessing an existing purchaser put forward as part of a standard divestiture remedy.
55. Even after additional, potentially significant scrutiny, the ACCC may conclude that a demerger remedy is not acceptable in many circumstances.
56. After extensive assessment of the risks associated with the Undertaking offered in relation to the transaction under consideration here, particularly the demerger, the ACCC considers that the Undertaking is acceptable and is likely to address its competition concerns.
57. A copy of the Undertaking is available on the ACCC mergers register and undertakings register.

Key obligations

58. The key obligations in the Undertaking require Aurizon to:
 - divest One Rail East Coast by either trade sale or demerger. If One Rail East Coast is divested by trade sale it must be to an ACCC-approved purchaser. If One Rail East Coast is divested by demerger it will be established as a standalone ASX-listed entity. If One Rail East Coast is not divested within the Initial Divestiture Period it will be divested to an Approved Purchaser at no minimum price,
 - offer One Rail East Coast a call option to purchase a refurbished narrow-gauge train set from Aurizon,
 - hold One Rail East Coast entirely separate from Aurizon during the Initial Divestiture Period,
 - appoint an ACCC-approved Independent Manager to manage One Rail East Coast during the Initial Divestiture Period, and
 - appoint an ACCC-approved Independent Auditor to audit Aurizon's compliance with the Undertaking.

Assessment of the Undertaking

59. The ACCC considers that the Undertaking addresses its competition concerns in respect of coal haulage services in NSW and Queensland. The divestment of One Rail East Coast ensures that three main suppliers of coal haulage services in NSW and Queensland remain following the proposed acquisition.
60. The ACCC also considers that the divestment of One Rail East Coast preserves it as a potential competitor to Aurizon for the supply of bulk rail haulage services in the future.
61. In reaching this view, the ACCC assessed the risks associated with the remedy, including an in-depth consideration of the risks associated with the demerger remedy. In assessing the risks, the ACCC considered:
- the demerged entity's incentives to compete and the capabilities of the proposed management team of the demerged entity – while it can be difficult to assess a demerged entity's management team and its business plan, motivation and capabilities prior to a demerger, the ACCC was satisfied regarding the qualifications and experience of One Rail East Coast's proposed management team to operate rail haulage businesses. Extensive interviews with the proposed management team indicated that they have thorough, well-developed business plans and a deep understanding of the One Rail East Coast business,
 - the demerged entity's financial standing and incentive to compete, taking into account information available pre-demerger regarding the demerged entity's incentives, shareholder preferences and financial standing – a particular focus for the ACCC was on One Rail East Coast's level of debt following a demerger and whether it would limit its ability to compete effectively. The ACCC assessed One Rail East Coast's debt facility, including an assessment of its free cash flows, ability to acquire additional financing and the terms of its finance agreements and concluded that One Rail East Coast's level of debt is unlikely to impact its ability to compete. The call option over an additional train set in Queensland provides additional comfort that One Rail East Coast will be able to compete effectively in the short term and become an effective long-term competitor following the divestment,
 - the independent oversight – the Undertaking contains extensive oversight provisions including the appointment of an Independent Manager and an Independent Auditor. The ACCC considers that these appointments provide appropriate oversight of the divestiture process and the ability to address issues if they arise. They also provide additional comfort that One Rail East Coast's confidential information will be appropriately ring-fenced from Aurizon,
 - third party consents – various third-party consents are required to implement a demerger including consents from shareholders, the ATO, ASIC, the ASX and the Court. The ACCC assessed the risk that third parties will withhold the consents necessary for a demerger to occur as low. A number of third parties provided in-principle consent and there is no additional evidence to suggest consents will be withheld,

- timing – the time period for the demerger to occur is the shortest reasonable period in which a demerger can be completed in this instance. This reduces the risk that One Rail East Coast will deteriorate during the divestiture process,
- dual-track process – the Undertaking outlines a dual-track divestment process by which One Rail East Coast can be divested by demerger or by trade sale. As such, the divestment does not rely entirely on a demerger. The divestment may occur via a trade sale and the ACCC would have oversight on that process under the terms of the Undertaking.

62. After a thorough assessment of these factors, the ACCC concluded that the Undertaking is likely to address the competition concerns. The ACCC considers each remedy on a case-by-case basis, and based on the particular circumstances of this matter, the ACCC decided to accept the Undertaking.

Conclusion

63. Based on the above analysis, the ACCC concluded that the proposed acquisition of One Rail by Aurizon, in the absence of the Undertaking, would be likely to have the effect of substantially lessening competition in the supply of coal haulage services in both NSW and Queensland. However, the ACCC considers that the Undertaking offered by Aurizon is likely to address the ACCC's competition concerns in these markets.

64. The ACCC did not reach a concluded view on the impact of the proposed acquisition, in the absence of the Undertaking, on bulk rail haulage services, but formed the view that the Undertaking resolved any potential concerns in these markets.