Australian Competition and Consumer Commission

Decision

in relation to Australian Rail Track Corporation's Interstate Rail Network Access Undertaking variation

18 April 2012

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Glossary

ACCC	Australian Competition and Consumer Commission
Act	The *Competition and Consumer Act 2010* (Cth)
ARTC	Australian Rail Track Corporation
Access Undertaking	The Undertaking accepted by the ACCC on 30 July 2008
HVAU	Hunter Valley Access Undertaking
Proposed Variation	ARTC's proposed variation to the 2008 Interstate Access Undertaking, submitted on 6 January 2012
RAB	Regulatory Asset Base
RCG	Rail Capacity Group

Summary

The Australian Competition and Consumer Commission (**ACCC**) has decided to accept the Proposed Variation to Schedule H of the Interstate Rail Access Undertaking submitted by the Australian Rail Track Corporation (**ARTC**) on 6 January 2012. The variation provides for the inclusion in Schedule H of the Interstate Access Undertaking (**Access Undertaking**) ARTC's estimates of capital expenditure proposed for the period 1 July 2012 to 30 June 2018.

The ACCC has made the decision to accept the variation under section 44ZZA(7) of the *Competition and Consumer Act 2010* (Cth) (**the Act**) taking into account the matters listed in section 44ZZA(3).

Prior to this decision, Schedule H was silent on the capital expenditure that could be incurred by ARTC during the period 1 July 2012 to 30 June 2018, thus providing no guide in the Access Undertaking on ARTC's proposed investments over the period.

ARTC sought the approval of the ACCC for the proposed capital expenditure to be considered prudent (as defined under the Access Undertaking). The ACCC notes that the Access Undertaking places an obligation on ARTC, not the ACCC, to assess the prudency of its capital expenditures once finalised. The Access Undertaking does not require an assessment of prudency to be made by either ARTC or the ACCC when ARTC submits its Proposed Variation.

In addition, due to the preliminary nature of the capital expenditure estimates proposed by ARTC, the ACCC has not formed a view on the prudency or otherwise of the proposed capital expenditure estimates for the period.

Section 4.4(d) of the Access Undertaking requires ARTC to assess its actual (not forecast) capital expenditures against the prudency criteria set out in the undertaking before it can roll these expenditures into the regulatory asset base (**RAB**) for the purposes of calculating the economic cost of the network, which is used in determining the ceiling limit for access prices.

Section 4.4(e) of the Access Undertaking requires that if ARTC's capital expenditure exceeds by 20 per cent the estimated amounts in Schedule H in any single year, it must seek the approval of the ACCC.

The prudency criteria in section 4.4(e) of the Access Undertaking include whether the capital expenditure incurred by ARTC:

- was needed to meet market demand for capacity and performance of the network;
- represents an efficient means to achieve that demand or extend the economic life of the network;
- was incurred efficiently; and
- has the support of industry.

Stakeholders have given qualified support for the Proposed Variation. However, during the ACCC's consultation on the Proposed Variation, stakeholders raised

concerns about the effectiveness of ARTC's consultation with industry to date on its proposed capital expenditure.

Consequently, the ACCC has reached the view that ARTC should consult more effectively with industry during the course of finalising and undertaking the proposed capital expenditure program. The ACCC considers that capital expenditure is more likely to be prudent if effective consultation has taken place during development and implementation of the capital expenditure program. To assist ARTC and industry, the ACCC has set out in this Decision its guidance on what it considers would constitute effective consultation.

This report sets out the ACCC's detailed reasons for deciding to accept the Proposed Variation.

1 Introduction

On 6 January 2012, ARTC submitted its forecast capital expenditure for the period 2012-13 to 2017-18 to the ACCC as envisaged under section 2.4(c) of the Interstate Rail Network Access Undertaking accepted by the ACCC on 30 July 2008 (**the Access Undertaking**).

The forecast capital expenditure was lodged as an application to vary Schedule H (**the Proposed Variation**) of the Access Undertaking in accordance with section 44ZZA(7) of the *Competition and Consumer Act 2010* (Cth) (**the Act**). Section 44ZZA(7) allows an access provider to vary an accepted access undertaking with the consent of the ACCC.

The ACCC conducted a public consultation process as part of its assessment of the Proposed Variation and sought submissions from interested parties. Three submissions were received.

1.1 ACCC's decision on ARTC's application to vary the Interstate Rail Access Undertaking

Having regard to the matters listed in section 44ZZA(3) of the *Competition and Consumer Act 2010* (Cth), the ACCC is of the view that it is appropriate under section 44ZZA(7) of the Act to accept ARTC's application, made on 6 January 2012, to vary the 2008 Interstate Rail Access Undertaking.

The ACCC's reasons for this decision are set out in the following chapters.

The ACCC has also accepted ARTC's consequential amendment in the Proposed Variation in order to remove clause 2.4(c) from the Access Undertaking. The ACCC made this decision as ARTC has complied with the clause and, therefore, the clause has no further effect.

The ACCC was required to make a decision on whether to accept the Proposed Variation by 1 August 2012. This took into account the four week consultation on the ACCC's Consultation Paper (released 25 January 2012) which acted as a clock-stopper to the 180-day statutory timeframe imposed by section 44ZZBC within which the ACCC is required to make a decision.

1.2 Effect of the decision to accept the variation

With the ACCC's acceptance of ARTC's application to vary the Access Undertaking:

- Schedule H of the Access Undertaking has been varied to include ARTC's capital expenditure estimates for the financial years 2012-13 to 2017-18.

- ARTC will now be able to roll into its regulatory asset base (RAB) all capital expenditure it prudently incurs each year in this period up to the estimates set out in Schedule H plus 20 per cent without further ACCC approval.

- Where ARTC's actual capital expenditure exceeds the forecast capital expenditure by 20 per cent (or more) in any single year, ARTC must obtain the ACCC's approval to roll the full amount of its actual expenditure into the RAB.

- The RAB value is used in determining the ceiling price that would allow ARTC to recover the full economic cost of providing access to the interstate network.

ARTC indicated in its supporting submission that it intends, at a later date, to seek the ACCC's approval for higher capital expenditure than the estimates in Schedule H in relation to:

- the 'substantial investment programme' for the 2006-07 to 2011-12 period, currently being undertaken; and

- additional expenditure of $434 million in 2012-13 and $18.5 million over the subsequent three years (2013-14 to 2015-16) for projects commenced prior to 2012-13 and currently underway.

The current decision to accept the variation does not include these additional expenditures. ARTC has indicated that it will submit a further application to vary the Access Undertaking for these proposed additional capital expenditures.

1.3 Prudency of the 2012-13 to 2017-18 capital expenditure estimates

In making this decision, the ACCC has not made an assessment of the prudency of ARTC's 2012-13 to 2017-18 capital expenditure estimates. The ACCC recognises that the proposed investment program for the period, and the proposed capital expenditure estimates, are at a preliminary stage. ARTC has stated that the development of its future capital expenditure program is at the 'Concept Assessment' stage of its internal project management procedures.

ARTC has made it clear that there will be further development and refinement of the proposed projects that make up the estimates through, in part, development of and consultation on its infrastructure strategy documents.

The ACCC notes that the prudency of ARTC's actual capital expenditure over the period must be assessed before it can be rolled into the RAB. Section 4.4(e) of the Access Undertaking sets out the factors relevant to determining whether or not actual capital expenditure has been prudent.

In making its decision to accept the Proposed Variation, the ACCC has noted the concerns raised by industry about whether effective consultation has occurred on the capital expenditure estimates to date. The ACCC has also noted ARTC's confirmation that it intends to consult with industry in developing its infrastructure strategy documents and the details of its capital expenditure program for the period. The ACCC expects that going forward there will be:

- effective engagement with industry, including at a number of critical decision making points within ARTC's project management procedures; and

- the provision of all necessary information related to specific proposals in order to enable effective engagement.

The ACCC is of the view that effective consultation will help ARTC inform its decision making process when developing and delivering specific projects. It will also assist ARTC to meet access seekers' demands efficiently. This will, in turn, contribute to protecting ARTC's legitimate business interests by increasing the likelihood that there will be sufficient demand to support ARTC's volume growth focussed approach to its business on the interstate rail network. It will also promote the interests of access seekers by better aligning ARTC's capital expenditure proposals with the requirements and priorities of access seekers, allowing for complementary investments to be made in a timely manner.

It is the ACCC's view that effective consultation will support the economically efficient operation of, use of and investment in the interstate rail network. The ACCC has set out its views as to what could constitute an appropriate level of consultation (and the types of information that should form part of that consultation) in Chapter 4.

2 Background

On 30 July 2008 the ACCC accepted, pursuant to Division 6 of Part IIIA of the then *Trade Practices Act 1974* (now the *Competition and Consumer Act 2010* (Cth)), an access undertaking submitted by ARTC for its interstate rail network. The Access Undertaking came into operation on 20 August 2008.

Under section 44ZZA(7) of the Act, the ACCC may consent to a variation of an accepted access undertaking if it thinks it appropriate to do so having regard to the matters listed in section 44ZZA(3). As noted above, ARTC submitted a variation request in accordance with section 44ZZA(7) on 6 January 2012.

2.1 Services provided by ARTC

ARTC is a Commonwealth Government owned corporation, established in 1998 for the purpose of managing and providing access to the National Interstate Rail Network. ARTC is vertically separated, providing only 'below-rail' track access services and not 'above-rail' services such as haulage.

The interstate network covers the mainline standard gauge track linking Kalgoorlie in Western Australia; Adelaide, Wolseley and Crystal Brook in South Australia; Melbourne and Wodonga in Victoria; Cootamundra, Albury, Macarthur, Moss Vale, Unanderra, Newcastle (to the Queensland border) and Parkes in New South Wales.[1] The Access Undertaking does not cover access to the rail network in the Hunter Valley, which is covered by the Hunter Valley Access Undertaking accepted by the ACCC on 29 June 2011.

The interstate network is used by both general freight services (such as manufactured goods) and bulk freight services (such as mining and agricultural products), as well as long distance and regional passenger services.

2.2 The 2008 Access Undertaking – Schedule H

Prior to this decision, Schedule H of the Interstate Access Undertaking outlined ARTC's estimated capital expenditure for the six year period 2006-07 to 2011-12. Capital expenditure is specified for each network segment and disaggregated forecasts are provided for network improvement works (for example, track works), train control and corridor infrastructure improvement. Capital expenditure is also disaggregated by forecast expenditure on track investment, signalling and communications investment for each segment.

The Access Undertaking has a ten year term expiring in 2018. At the time the Final Decision on the 2008 Access Undertaking was released, the ACCC recognised the difficulty in reasonably forecasting capital expenditure over ten years. It accepted that ARTC would submit forecast capital expenditure for the six year period 2012-13 to 2017-18 by 31 December 2011.[2]

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1 http://www.artc.com.au/Content.aspx?p=98

2 Schedule H of the Access Undertaking includes capital expenditure estimates for two years—2006-07 and 2007-08—prior to the commencement date of the undertaking. Therefore Schedule H

Clause 2.4(c) of the Access Undertaking states that 'by 31 December 2011, ARTC will develop and submit to the ACCC, Capital Expenditure in the form of an extended Schedule H, applicable to the period 1 July 2012 to 30 June 2018'.

On 20 December 2011 ARTC requested an extension of time to submit the Proposed Variation to the ACCC. The ACCC agreed to ARTC's request and ARTC submitted its variation application on 6 January 2012.

2.3 Application to vary the 2008 Interstate Access Undertaking

As envisaged under clause 2.4(c) of the Access Undertaking, ARTC lodged an application to vary Schedule H of the Access Undertaking. ARTC's revised Schedule H is included at **Attachment A**.

The application set out the proposed 2012-13 to 2017-18 capital expenditure estimates that would form the basis for ARTC determining its annual revaluation of the network and associated facilities in respect of calculating ARTC's annual economic cost under the Access Undertaking.

The Proposed Variation is in respect of new investments that amount to $626 million over the six years, or an average spend of $104 million per year. The major projects included in the capital expenditure estimates covered by the Proposed Variation are as follows:

- *Advanced Train Management System* (**ATMS**)

  The ATMS is a communications based signalling system designed to improve both productivity and safety. ARTC is currently finalising its Signalling & Communications Strategy, which suggests that there will be an economic case for the roll-out of the ATMS on the interstate network. Expenditure over the six year period is forecast at approximately $181.1 million.

- *East-West Capacity*

  Capacity constraints are beginning to emerge in the north-east and north-west areas of South Australia, and continued growth in east-west minerals and intermodal traffic is expected to place further pressure on transit times. ARTC intends to address these issues through the East-West Corridor Capacity Strategy. Expenditure is estimated at $377 million.

- *Port Augusta – Tarcoola Track Configuration*

  The current track configuration between Port Augusta and Tarcoola limits the speed/axle load configurations that can be operated. Operators have flagged an interest in exploring options to go to higher axle loads by strengthening the track, which is expected to improve productivity and increase capacity. Expenditure is estimated at $68 million.

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will cover twelve years of capital expenditure estimates when it is extended to include the years from 2012-13 to 2017-18.

ARTC has also stated that total expected capital expenditure includes small amounts of miscellaneous corridor capacity works. These projects relate to items that have reached the end of their economic lives and require renewal but which in the process of renewal are upgraded to a modern equivalent standard, enhancing their capability in the process.

2.3.1 What the proposal did not cover

For the purposes of ARTC's application, approval was only sought to vary the Access Undertaking in relation to new investments which are anticipated to receive approval and funding during the period 1 July 2012 to 30 June 2018.

The application does not include additional expenditure that ARTC has indicated will be undertaken over the period 2012-13 to 2015-16 (of $434 million in 2012-13 and $18.5 million over the subsequent three years) for investment projects envisaged in 2008 but not yet completed and projects not envisaged in 2008 but now underway.

The variation application also did not cover possible revised expenditure for the period 2006-07 to 2011-12. ARTC stated in its supporting submission that:

> *The substantial investment program undertaken by ARTC since 2006-07 has changed and expanded significantly. New projects that were not anticipated in 2008 have since been funded and projects forecasted in 2008 have changed and/or been expanded due to funding being made available.*[3]

ARTC has stated that it intends to 'seek to vary the Capital Expenditure [in relation to the 2006-07 to 2011-12 period in Schedule H] in accordance with Clause 4.4(e) … in due course, once the substantial investment program for the 2006-12 period, currently being undertaken, has been completed.'[4]

2.3.2 Minor drafting change

ARTC has also proposed a minor consequential drafting amendment in the Proposed Variation to remove clause 2.4(c) from the Access Undertaking, on the grounds that it is no longer necessary, and subsequent renumbering of clause 2.4.

Clause 2.4(c) provides that ARTC develop and submit to the ACCC capital expenditure in the form of an extended Schedule H, applicable to the period 1 July 2012 to 30 June 2018.

The ACCC is of the view that the proposed amendment will have no operative effect given that the Proposed Variation has been accepted by the Commission. The ACCC has therefore decided to accept the proposed drafting amendment.

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[3] ARTC, Variation to Schedule H to incorporate Capital Expenditure 1 June 2012 – 30 June 2018 - Supporting Submission, p. 8.

[4] ARTC, Variation to Schedule H to incorporate Capital Expenditure 1 June 2012 – 30 June 2018 - Supporting Submission, p. 8.

2.4 Public consultation process

The Act provides that the ACCC may invite public submissions on an access undertaking application.[5]

The ACCC published a Consultation Paper on 25 January 2012 inviting submissions on the Proposed Variation. The Consultation Paper indicated that ARTC should consider providing further information on its forecasting assumptions and estimated capital expenditure incurred during the 2006-2007 to 2011-12 period. The ACCC received public submissions from the following parties:

- Asciano – 22 February 2012
- QR National – 22 February 2012
- ARTC – 1 March 2012

In addition, ARTC provided confidential information to the ACCC in response to the submissions received from industry and the information highlighted in the ACCC's Consultation Paper.

All of these submissions have been considered and taken into account in the ACCC's assessment of the variation to the Access Undertaking.

2.5 Confidential submissions

As noted above, some confidential information was submitted by ARTC as part of its March submission. In this regard, the ACCC notes that a party may request that the ACCC not make the whole or part of a submission public for confidentiality reasons. In the current context, limited weight has been given to information provided to it on a confidential basis as the information did not raise any new issues beyond those raised in public submissions.

Information about the collection, use and disclosure of information provided to the ACCC is set out in the ACCC publication "*Australian Competition and Consumer Commission / Australian Energy Regulator Information Policy – the collection, use and disclosure of information*", available on the ACCC website.

2.6 Further information

The application to vary the 2008 Interstate Access Undertaking, other relevant material and submissions from ARTC and stakeholders are available on the ACCC's website at the following link:

http://www.accc.gov.au/content/index.phtml/itemId/789738

Alternatively, go to the ACCC's homepage at www.accc.gov.au and follow the links to 'For regulated industries' and 'Rail' and 'ARTC Interstate Rail Access Undertaking 2008.'

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[5] *Competition and Consumer Act 2010*, s. 44ZZBD(1).

If you have any queries about any matters raised in this document, please contact:

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3 Assessment framework

The chapter provides an overview of the framework under which the ACCC has made its decision on ARTC's Proposed Variation. It also sets out the parts of the Access Undertaking that are relevant to the current decision.

For background on the ACCC's assessment of the capital expenditure estimates proposed in the original 2008 Access Undertaking, **Attachment B** summarises relevant aspects of the ACCC's Draft and Final Decisions in relation to the 2008 Access Undertaking.

3.1 Legal test under Part IIIA

Under paragraph 44ZZA(7)(b) of the Act, an access provider may withdraw or vary an access undertaking at any time after it has been accepted by the ACCC, but only with the consent of the ACCC.

If the ACCC consents to the variation, the provider is required to offer third party access in accordance with the varied access undertaking. An access undertaking is binding on the access provider and can be enforced in the Federal Court upon application by the ACCC.

Subsection 44ZZA(7) allows the ACCC to consent to a variation of an accepted access undertaking if it thinks it appropriate to do so, having regard to the matters contained in subsection 44ZZA(3). These are:

- the objects of Part IIIA 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 (see further below);
- the legitimate business interests of the provider of the service;
- the public interest, including the public interest in having competition in markets (whether or not in Australia);
- the interests of persons who might want access to the service;
- whether the undertaking is in accordance with an access code that applies to the service; and
- any other matters that the ACCC thinks are relevant.

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

- regulated access prices should:
  - be set so as to generate expected revenue for a regulated service that is at least sufficient to meet the efficient costs of providing access to the regulated service or services; and
  - include a return on investment commensurate with the regulatory and commercial risks involved; and
- access price structures should:
  - allow multi-part pricing and price discrimination when it aids efficiency; and
  - not allow a vertically integrated access provider to set terms and conditions that discriminate in favour of its downstream operations, except to the extent that the cost of providing access to other operators is higher; and
- access pricing regimes should provide incentives to reduce costs or otherwise improve productivity.

The ACCC notes as a general comment that section 44ZZA(3) lists matters to which the ACCC is required to have regard, not criteria on which the ACCC must be satisfied. The test under section 44ZZA(3) is whether the ACCC thinks it 'appropriate' to accept the undertaking (or the variation to the undertaking), having regard to the matters in section 44ZZA(3).

3.2 Timeframes for ACCC decisions and clock-stoppers

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

If the ACCC does not publish a decision on an access undertaking application under section 44ZZBE of the Act within the expected period, it is taken, immediately after the end of the expected period, to have:

- made a decision to not accept the application; and
- published its decision under section 44ZZBE and its reasons for that decision: see section 44ZZBC(6).

The Act contains 'clock-stoppers' that mean certain time periods are not taken into account when determining the expected period (see subsection 44ZZBC(2)). In particular, the clock may be stopped:

- by written agreement between the ACCC and the access provider (in this case, ARTC), and such agreement must be published: subsections 44ZZBC(4) and (5);

- if the ACCC gives a notice under subsection 44ZZBCA(1) requesting information in relation to the application;

- if a notice is published under subsection 44ZZBD(1) inviting public submissions in relation to the application;

- if a decision is published under subsection 44ZZCB(4) deferring consideration of whether to accept the access undertaking, in whole or in part, while the ACCC arbitrates an access dispute.

3.3 The 2008 Interstate Access Undertaking – Relevant sections

ARTC's Proposed Variation sought to comply with the requirement in section 2.4(c) of the Access Undertaking, which states that:

> *(c) By 31 December 2011, ARTC will develop and submit to the ACCC, capital expenditure in the form of an extended Schedule H, applicable to the period 1 July 2012 to 30 June 2018.*

These capital expenditure estimates form the basis for ARTC determining its annual revaluation of the network and associated facilities in respect of calculating ARTC's annual economic cost under the Access Undertaking, subject to actual expenditures being prudent.

Clause 4.4(d) of the Access Undertaking requires that only capital expenditure that is incurred on a prudent basis will be included in the regulatory asset base. Prudent expenditure is defined as expenditure incurred having regard to:

> *(a) the need to meet market demand for capacity and performance of the Network, or the need to extend the economic life of the Network;*
>
> *(b) whether the scope of works is consistent with that identified in the applicable ARTC Corridor Strategy current as at the Commencement Date or as varied from time to time;*
>
> *(c) what is considered to represent an efficient means to achieve that demand or extend that economic life;*
>
> *(d) what is consistent with existing standard and configuration of adjacent and/or existing infrastructure with similar utilisation and market requirements, or its modern engineering equivalent;*
>
> *(e) expenditure incurred efficiently in implementing the project, in the context of prevailing access and operating requirements, and input costs;*
>
> *(f) adjustments in relation to the timing of commencement and/or commissioning of projects; and*
>
> *(g) support by the industry.*

In addition, section 6.5 of the Access Undertaking requires ARTC, when planning for Additional Capacity on the Network sought by Applicants or itself, to:

- provide operators with a reasonable opportunity to present their views regarding Additional Capacity;
- outline its views regarding Additional Capacity; and
- circulate a summary of the results of consultation regarding Additional Capacity to the Operators including, where applicable, reasons for disagreeing with Operators' views.

4 Assessment of the Proposed Variation

This chapter sets out the ACCC's views on ARTC's Proposed Variation and responses to the ACCC's Consultation Paper. In assessing the Proposed Variation, the ACCC has had regard to the matters listed in section 44ZZA(3).

4.1 ACCC's Consultation Paper

In the 2012 Consultation Paper on the Proposed Variation, the ACCC noted in relation to ARTC's forecast estimates that it intended to conduct a review process similar to that followed in its 2008 assessment of ARTC's Access Undertaking.[6] In its 2008 assessment, the ACCC conducted a high-level review of the capital expenditure program proposed by ARTC in Schedule H for the years 2006-07 to 2011-12. **Attachment B** describes the review process conducted by the ACCC in 2008.

The ACCC also highlighted in its Consultation Paper that it intended to consider evidence of effective consultation by ARTC and industry support for its proposed capital expenditure program.

In this regard, the ACCC noted that section 4.4(d) of the Access Undertaking requires that only capital expenditure incurred on a prudent basis will be included in the regulatory asset base, and that the definition of prudent expenditure requires that ARTC have regard to, amongst other things, 'support by the industry'. In addition the ACCC noted that section 6.5 of the Access Undertaking also requires ARTC, when planning for additional network capacity, to undertake specified consultation (see section 3.3 of this Decision paper).

The ACCC noted further that it had not received specific information from ARTC on the nature of the consultation undertaken by ARTC in developing its proposed forecasts for new capital expenditure over 2012-13 to 2017-18.

As a result, the ACCC's view when it released the Consultation Paper was that it was 'not currently in a position to assess whether ARTC's consultation with industry has been effective and whether there is industry support for the proposed capital expenditure forecasts'.[7] The ACCC sought industry views on whether the level of consultation carried out by ARTC in developing its investment strategies was appropriate, and whether ARTC had provided sufficient information to facilitate industry assessment and comment on its capital expenditure forecasts.[8]

It was the ACCC's view that effective consultation would likely be facilitated by the provision of certain information on how the capital expenditure forecasts were formulated. The ACCC set out, in its Consultation Paper, the various types of information that it considered would facilitate an effective consultation process, including estimates of total capital expenditure, explanations of the assumptions and investment drivers underlying ARTC's capital expenditure forecasts, and the estimated impact of the proposed capital expenditure program on access prices.

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6 ACCC Consultation Paper, p. 5.
7 Consultation Paper, p. 10.
8 Consultation Paper, p. 12.

4.2 Submissions to the ACCC Consultation Paper

The ACCC received three submissions on the Proposed Variation in response to its Consultation Paper. Submissions were received from Asciano, QR National (**QR**) and ARTC.

While Asciano and QR both expressed general support for the Proposed Variation to include capital expenditure, concerns were raised in relation to:

- the nature and level of consultation conducted by ARTC with industry;
- the amount and type of information provided by ARTC to industry;
- accountability of ARTC and expected outcomes of capital investment; and
- ARTC's consideration of market demand and industry investment priorities.

ARTC's additional submission reiterated and expanded on the views included in its supporting submission to its Proposed Variation.

Stakeholder views are discussed in more detail in the rest of this chapter.

4.3 ACCC's assessment

In its application to the ACCC, ARTC submitted that '[i]n determining the proposed capital expenditure estimates for the period 1 July 2012 to 30 June 2018, ARTC has had regard to the 'Prudent' requirements set out in the Access Undertaking.'[9]

Further, in its submission to the ACCC's Consultation Paper, ARTC stated that it 'seeks the approval of the ACCC for [the proposed] Capital Expenditure to be considered Prudent and therefore able to be included in the annual revaluation of the Network and Associated Facilities.'[10]

However, as noted in chapter 1 of this Decision paper, the ACCC has not made an assessment of the prudency of the capital expenditure estimates included in the Proposed Variation. The ACCC recognises that the proposed investment program for the period, and the proposed capital expenditure estimates, are at a preliminary stage. The ACCC considers that it does not have sufficient information, or certainty about the actual expenditures that are likely to be incurred, to assess prudency at this early stage in the ARTC's development of its capital program for the period.

The ACCC notes that section 4.4(d) of the Access Undertaking requires that the prudency of ARTC's actual capital expenditure over the period must be assessed before it can be rolled into the RAB. Prudency will therefore be assessed at a later date in relation to the capital expenditures actually incurred by ARTC.

In the ACCC's view, ARTC's actual capital expenditures are more likely to satisfy the prudency criteria in section 4.4(e) of the Access Undertaking if there has been

[9] Application by ARTC to vary the ARTC Interstate Access Undertaking, p 2.
[10] ARTC's submission to the ACCC's Consultation Paper, p 3.

effective consultation in developing and implementing the capital expenditure program.

One of the ACCC's key concerns during the 2008 assessment of the Access Undertaking was whether in determining its capital expenditure program, ARTC had consulted interested parties who are likely to be affected by the program. The ACCC noted then that ARTC's capital expenditure will affect operators' costs, the services they receive, and/or have implications for their investments in above rail infrastructure.[11]

In line with these considerations, the ACCC stated in its Consultation Paper that in conducting its assessment of the Proposed Variation, it would consider evidence of effective consultation by ARTC and whether ARTC has had regard to industry support for its proposed capital expenditure program as required under the terms of the Access Undertaking.

In submissions from stakeholders in response to the Consultation Paper, Asciano noted that while it supports 'the ARTC application to vary the 2008 Interstate Access Undertaking … [it has] some concerns with current ARTC capital expenditure processes'.[12] Similarly QR submitted that it supports the proposed variation on the basis that ARTC's capital expenditure processes are expanded on to include reviews of capital expenditure as infrastructure strategies are completed and updated, and the provision of more detailed information (including impacts on ceiling price) to stakeholders.[13]

Consequently, in assessing this Proposed Variation, the ACCC's focus has been to assess whether the estimates form an appropriate basis for further development of, and consultation on, ARTC's capital expenditure program for 2012-13 to 2017-18. The ACCC has therefore examined the process by which ARTC develops its proposed capital expenditure estimates, their current status, and ARTC's engagement with industry in developing those estimates.

4.3.1 ARTC's Investment Strategy Development Process

ARTC submitted that its process for developing its infrastructure investment strategies includes substantial ongoing consultation with industry. ARTC has noted that it 'aims to maintain a rolling strategy for infrastructure development to provide the framework for capital investment decisions. These … aim to both address emerging capacity bottlenecks and to identify opportunities for productivity enhancements.'[14]

ARTC's approach to developing its infrastructure strategies has a number of common themes, including:

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11 ACCC Draft Decision, April 2008, p. 211.

12 Asciano, Submission to the ACCC in Relation to the ACCC Consultation Paper on the ARTC's Interstate Access Undertaking Capital Expenditure Variation, February 2012, p. 4.

13 QR National, Submission on ARTC Interstate Rail Network Access Undertaking variation, February 2012, p. 2.

14 ARTC's supporting submission, p. 5.

- Forecast volumes are based on detailed modelling of both existing and potential future traffic.
- The strategies are based on achieving market-driven outcomes.
- The strategies aim to facilitate integrated and long-term solutions.
- Solutions are designed to achieve market outcomes at the lowest cost.
- Solutions are supported by appropriate modelling.[15]

ARTC also submitted that in developing its investment strategies, it undertakes stakeholder consultation in accordance with section 6.5 of the Access Undertaking.[16]

With regard to the current status of the various infrastructure strategies, ARTC noted that the following are either 'released or in advanced draft':[17]

- North-South Corridor Capacity Strategy
- East-West Corridor Capacity Strategy
- Clearances Strategy
- Signalling and Communications Strategy.[18]

In addition, the following strategies are being developed:

- Route and Alignment Strategy
- Speed / Axle Load Strategy
- Metropolitan (including ports and terminals) Strategy.

ARTC submitted that it 'intends that once all of the strategies have been developed they will be reviewed and updated on a regular basis'.[19] Further, ARTC stated that 'the strategies only provide the context for investment decision making and that individual projects will undergo further rounds of review and engagement with stakeholders before a final approval is granted.'[20]

ARTC submitted further that it undertakes a six stage process to manage projects that are identified through the strategy development process. These stages, which are described in ARTC's project management procedure, PP157, comprise:

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15 ARTC's supporting submission, p. 5.
16 Application by ARTC to vary the ARTC Interstate Access Undertaking, pp. 2-3.
17 ARTC supporting submission, p. 22.
18 The North-South Corridor Capacity Strategy is available on ARTC's website. There are other documents relating to the National Train Communication System and East-West upgrades, but there do not appear to be any additional investment strategy documents publicly available. ARTC notes at p 24 of its supporting submission that its 'investment strategy documents are generally endorsed by … [ARTC's] Board for public release following review by the ARTC Executive'.
19 ARTC supporting submission, p. 22.
20 ARTC's supporting submission, p. 6.

- Phase 1 – Concept Assessment
- Phase II – Project Feasibility
- Phase III – Project Assessment
- Phase IV – Project Approval
- Phase V – Project Implementation
- Phase VI – Project Closeout.[21]

ARTC stated that these phases represent a further strengthening of 'its internal procedures for project identification and development, project delivery and cost management, and project reporting' that has taken place since acceptance of the 2008 Access Undertaking.[22]

ARTC submitted that '[f]or efficiency reasons … [it] has elected not to change its ongoing investment strategy development and consultation in order to better align to [the current] … one-off regulatory obligation' that is imposed by section 2.4(c) of the Access Undertaking.[23]

Stakeholder submissions

Asciano submitted that ARTC should be required to publish its capital expenditure process, as it was of the view that the project evaluation procedure used by ARTC should not be confidential (with the exception of data relating to user specific projects or sensitive financial data). Asciano argued that publishing the capital expenditure process would improve the transparency of the ARTC capital expenditure evaluation procedure which in turn would improve industry input.[24]

In its submission to the ACCC's Consultation Paper, ARTC provided a public summary of its six stage internal project management process that all individual projects are required to go through. A flowchart describing the various stages of ARTC's internal project management process, and a checklist of matters that must be included in investment proposals submitted to ARTC's internal management, are set out at Attachments 1 and 2 of ARTC's submission to the ACCC's Consultation Paper.

ARTC stated that it had described the various stages of project management in order to 'further improve transparency'.[25]

ACCC view

The ACCC notes that there are a number of stages within ARTC's internal processes for approving capital expenditure projects that require consideration of stakeholder

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21 ARTC's supporting submission, p 6; ARTC's submission to the Consultation Paper, Attachment 1.
22 ARTC's submission to the Consultation Paper, p. 4.
23 ARTC's submission to the Consultation Paper, p. 13.
24 Asciano, Submission to the ACCC in Relation to the ACCC Consultation Paper on the ARTC's Interstate Access Undertaking Capital Expenditure Variation, February 2012, p. 6.
25 ARTC's submission to the Consultation Paper, p. 4, Attachment 1.

views. As such, the ACCC considers that ARTC's internal processes provide a suitable framework for conducting effective consultation.

The ACCC accepts that the capital expenditure estimates that make up the Proposed Variation are a very preliminary estimate of the expenditure that ARTC may actually incur in delivering the anticipated projects. The ACCC accepts ARTC's statement that the capital expenditure proposals are generally at the 'Concept Assessment' stage of its internal project management procedures.

The ACCC further notes ARTC's statement that the infrastructure strategy documents are a work in progress and are not fully developed at this stage. The ACCC also notes ARTC's submission that its infrastructure strategies only provide the context for investment decision making, and that further rounds of review and engagement with stakeholders will be undertaken prior to final approval being granted for capital expenditure projects.

As stated above, the ACCC considers that effective industry consultation is necessary to ensure that ARTC's capital expenditure projects are prudent and efficient. The ACCC considers that ARTC's decision to release details of its internal management processes will assist industry in understanding how ARTC develops its capital expenditure program and may facilitate industry involvement in those processes.

The ACCC's views on ARTC's consultation process are discussed in section 4.3.2 below.

4.3.2 Consultation on ARTC's infrastructure strategies and proposed capital expenditure estimates

The ACCC noted in its Consultation Paper that ARTC had not provided information on the specific consultation undertaken by ARTC in developing its proposed capital expenditure forecasts for the period 2012-13 to 2017-18.

In its supporting submission to its application, ARTC stated generally that it:

> *maintains a continuous dialogue with rail operators … Specific discussions in respect of ARTC's investment strategy are held with rail operators on an ad hoc basis as appropriate and drafts of ARTC's investment strategies are regularly circulated to relevant industry stakeholders for consultation purposes. It is ARTC's general practice to release its investment strategies to industry as consultation documents and feedback on such strategies is encouraged.*[26]

The ACCC noted that ARTC had not provided specific information on the extent and nature of the consultation undertaken, details of industry feedback received and how ARTC had regard to that feedback. The ACCC sought industry views on whether:

- the consultation undertaken by ARTC was effective in allowing industry to assess the proposals and provide feedback to ARTC; and

[26] ARTC supporting submission, p. 5.

- ARTC had provided sufficient information to allow industry to address the matters relevant to the ACCC's assessment of the proposed capital expenditure forecasts.

Stakeholder submissions

Asciano

Asciano submitted that its support for the Proposed Variation is qualified as 'there has been insufficient consultation by ARTC and … there is insufficient detail for Asciano to be confident that the proposed capital expenditure will assist ARTC improve the interstate network's capacity and efficiency.'[27]

Asciano submitted that past capital expenditure consultation undertaken by ARTC has not been effective. Further, Asciano stated that consultation typically only occurs after an extended internal ARTC review involving internal ARTC approvals. As such, Asciano argued that 'feedback via the ARTC-industry consultation processes is marginalised and in many instances … undertaken too late to have any impact on the nature of the capital works, as these works have already been internally approved by ARTC'.[28]

QR National

QR submitted that it has participated in consultations with ARTC regarding development of the North-South Corridor Strategy and the submission to Infrastructure Australia. However QR was of the view that 'the extent of that participation was somewhat limited'.[29] It has also participated in quarterly strategy meetings with ARTC where the capital programme is discussed informally.[30]

QR argued that ARTC can improve the productivity and competitiveness of the rail industry by engaging in 'ongoing consultation and engagement with rail operators through all phases of project evaluation to ensure below and above rail investment is targeted and optimised through value engineering principles.'[31]

QR noted that it supports the Proposed Variation provided that:

- '[i]ndustry is consulted during the relevant phases of the project governance and delivery process', particularly the Proof of Concept stage, as this will enable projects to be 'continually assessed to determine whether objectives will be met'[32]; and

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27 Asciano, Submission to the ACCC in Relation to the ACCC Consultation Paper on the ARTC's Interstate Access Undertaking Capital Expenditure Variation, February 2012, p. 5.

28 Asciano, Submission to the ACCC in Relation to the ACCC Consultation Paper on the ARTC's Interstate Access Undertaking Capital Expenditure Variation, February 2012, p. 6.

29 QR National, Submission on ARTC Interstate Rail Network Access Undertaking variation, February 2012, p. 2.

30 QR National, Submission on ARTC Interstate Rail Network Access Undertaking variation, February 2012, p. 2.

31 QR National, Submission on ARTC Interstate Rail Network Access Undertaking variation, February 2012, p. 2.

32 QR National, Submission on ARTC Interstate Rail Network Access Undertaking variation, February 2012, p. 2.

- ARTC 'consult[s] with all operators so that they may be more involved in the choice and prioritisation of projects, with particular emphasis on how the projects improve the reliability of service delivery to the end customer.'[33]

ARTC

ARTC submitted that it 'is and will continue to, bear substantial market risk in investing in the network' and has a 'commercial incentive to mitigate this risk, as much as possible, by ensuring that its investment strategies are designed to meet the known market need for infrastructure performance and capacity.'[34]

ARTC stated that the development of its infrastructure strategies does not arise out of one or a series of 'formal, purpose built, clearly defined consultation forums conducted with industry'.[35] ARTC argued that this would not be practical given 'the diversity in uses, priorities and objectives and confidentiality needs of users'.[36] Rather, consultation generally occurs 'on a continuous basis … in a variety of more informal settings'.[37]

Where there are more substantive one-off developments, ARTC stated that it works cooperatively with key users on substantial and strategic network performance and investment programs intended to deliver a more holistic proposal.

In relation to the 2012-13 to 2017-18 capital expenditure program, ARTC submitted that industry consultation is generally at an early state and that further consultation will occur during the process of finalising specific projects.

ARTC also submitted that in relation to the projects that make up the capital expenditure in the Proposed Variation, its proposals are consistent with a 2007 blueprint prepared by the Freight Rail Operators Group and are consistent with the 2008-2024 Interstate and Hunter Valley Rail Investment Strategy prepared by ARTC in 2008. Further, ARTC stated that it has only recently begun development of its specific East-West Corridor Strategy, following discussions with rail operators between December 2011 and February 2012.[38]

Once the East-West Corridor Strategy is finalised, ARTC noted that stakeholders will be 'invited to make comments in relation to … investment benefits and outcomes provided in relation to these sets of works.'[39] In doing so (and in developing its Signalling and Communications Strategy), ARTC noted that should ARTC receive any views from operators, it will comply with the requirements in Clause 6.5 of the Access Undertaking.[40] However, at the current stage of investment strategy development (and the estimates that are based on those investment strategies), ARTC

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33 QR National, Submission on ARTC Interstate Rail Network Access Undertaking variation, February 2012, p. 3.
34 ARTC Submission to ACCC Consultation Paper, February 2012, p. 7.
35 ARTC Submission to ACCC Consultation Paper, February 2012, p. 11.
36 ARTC Submission to ACCC Consultation Paper, February 2012, p. 11.
37 ARTC Submission to ACCC Consultation Paper, February 2012, p. 11.
38 ARTC Submission to ACCC Consultation Paper, February 2012, pp. 11-12.
39 ARTC Submission to ACCC Consultation Paper, February 2012, p. 12.
40 ARTC Submission to ACCC Consultation Paper, February 2012, p. 15.

‘is not committed to implementing any projects, but rather has sought conceptual endorsement of the programme of CAPEX envisaged at a strategic level.’[41]

ACCC view

In the ACCC’s view, ARTC has not demonstrated that it has, to date, engaged in effective consultation with interested parties who are likely to be affected by the proposed capital expenditure program. This view is supported by the concerns raised in industry submissions about the effectiveness of ARTC’s consultations to date.

The ACCC has also had regard to ARTC’s statements that it has relied on past consultations with operators on the general direction of future investment, and informal discussions on potential operational benefits of investment options, rather than specific consultation on the investment projects proposed to be undertaken over the period 2012-13 to 2017-18.

The ACCC acknowledges that ARTC has stated that it intends to conduct further consultation as it develops its infrastructure strategies and the details of its capital expenditure program for the period. However, two main factors give rise to concerns about the likely effectiveness of that consultation.

First, ARTC submitted that it ‘finds it difficult to establish an interest that users may have in whether ARTC invests in the most cost efficient means to achieve an objective or whether ARTC delivers an investment in a cost efficient manner.’[42] ARTC’s reasoning for this statement was its view that it, rather than users of the interstate network, is most exposed to investment risk.

The ACCC notes that as capital expenditure is anticipated to be rolled into the RAB (provided it is prudent), it is likely that ARTC’s capital expenditure will go into determining future access prices. Consequently, network users have a legitimate interest in the proposed capital expenditure estimates as they may give rise to concerns in relation to the interests of access seekers under section 44ZZA(3)(c) of the Act. The ACCC also notes that ARTC is compensated for investment risks through the risk premium included in the return it is allowed to earn on the RAB (the weighted average cost of capital).

Second, the ACCC notes stakeholder submissions that in the past, consultation has been conducted too late, occurring after a comprehensive ARTC review has already been completed and projects have already been approved.

It is the ACCC’s view that effective consultation will help promote the economically efficient operation of, use of and prudent investment in the interstate rail network. This view is consistent with the ACCC’s approach in relation to investment in other infrastructure networks. Two examples of this approach—for the Hunter Valley Access rail network and for Airservices Australia—are discussed below.

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41 ARTC Submission to ACCC Consultation Paper, February 2012, pp. 12-13.
42 ARTC Submission to ACCC Consultation Paper, February 2012, p. 8.

Hunter Valley Access Undertaking

The Hunter Valley Access Undertaking (**HVAU**) contains a detailed process governing ARTC's development of additional capacity. The process requires industry consultation and endorsement at each of the key stages of a project's development to promote effective consultation with the aim of ensuring the proposed project is prudent.

Section 9 of the HVAU sets out the industry consultation process that must be followed by ARTC for projects creating additional capacity on the Hunter Valley network. The HVAU also notes that this consultation process may be used by ARTC for projects which do not involve the creation of additional capacity on the Hunter Valley network.

The process requires ARTC to consult and seek the endorsement of the Rail Capacity Group (**RCG**) (a group made up of representatives of access holders transporting coal on the Hunter Valley network) at five stages of a project's development. The consultation reports for endorsement by the RCG at each stage include:

- Concept assessment – a preliminary assessment of the potential costs, benefits and risk involved, including broad objectives and indicative timeframes for the development and delivery of the project.

- Project feasibility – includes confirmation of project objectives, identification of estimated project costs and a preliminary project management plan.

- Project assessment – includes financial evaluation and a developed projects management plan.

- Project implementation – a finalised version of the project assessment report.

- Project close out – includes formal acceptance of works, outstanding works and if necessary a completion plan, a cost report and verification of the benefits delivered.

If each stage of the project is endorsed by the RCG, then the costs incurred for the next stage are deemed prudent to the extent of the endorsement. On completion of the project close out report, any capital expenditure incurred by ARTC in providing additional capacity that is within the cost range or endorsed by the RCG will be taken to be prudent.

The HVAU also requires the development of a Hunter Valley Corridor Capacity Strategy.[43] This requires ARTC, on an annual basis, to develop a strategy for identifying constraints on the coal network's capacity in the Hunter Valley, the options to resolve these constraints and a proposed course of action to achieve increased coal throughput.

[43] Hunter Valley Access Undertaking, section 8.

Airservices Australia

The framework for industry consultation in developing capital expenditure projects for Airservices Australia (**Airservices**) also promotes effective industry consultation.

In its preliminary view on a price notification submitted by Airservices in March 2011, the ACCC expressed concern that Airservices had not undertaken adequate consultation with stakeholders to ensure that its proposed capital expenditure program was prudent and efficient. In particular, the ACCC was concerned that Airservices' existing consultation processes did not provide timely and sufficient information to its stakeholders to enable them to provide informed input on the benefits and costs of specific projects. In addition, the ACCC considered that formal mechanisms were needed in order to provide ongoing transparency to, and accountability for, Airservices' delivery performance on specific projects.

In response to the ACCC's concerns, Airservices proposed a range of measures to improve the robustness of consultation on its capital expenditure program through both the project development phase and ongoing monitoring phase.[44] These measures included:

- programs that set out expected project benefits, project costs and project milestones, against which delivery will be measured. Airservices committed to providing this information to industry stakeholders at least ten days in advance of consultative meetings.

- presenting business case information at an early stage (that is, prior to seeking endorsement and approval from Airservices' decision making body) to a consultative committee (including both Airservices staff and industry stakeholders) for all major projects (in this case, all projects greater than $10 million). This information covers project objectives, scope, benefits, cost and schedules, for the purpose of improving the transparency of, and industry input to, determining a preferred option.

- following endorsement and approval from Airservices' decision making body, providing further and more refined details of the capital expenditure projects to the consultative committee that includes a final scope, cost/benefit analysis and schedule that forms the basis against project performance can be measured. The format of this information was agreed to between Airservices and the consultative committee.

- committing to quarterly reporting to industry stakeholders on its capital program performance. Reports include financial analysis and tracking against its delivery schedule as agreed above.

- reporting on the benefits realised from capital works projects, including measurement against original project goals and objectives.

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[44] Submission from Airservices to ACCC, *Notification of price changes for Airservices' Enroute, Terminal Navigation and Aviation Rescue & Fire Fighting Services: effective 1 October 2011*, 22 August 2011, p. 10.

4.3.3 Provision of information to facilitate effective consultation

In its Consultation Paper, the ACCC noted that effective consultation on ARTC's capital expenditure program is likely to be facilitated by the provision of sufficient information to stakeholders. The ACCC suggested types of information that, in its view, would assist stakeholders in providing feedback to ARTC on proposed capital expenditure projects. This information was likely to include:

- estimates of total capital expenditure for the 2006-07 to 2011-12 period.
- an explanation of the basis for the capital expenditure forecasts, including information on traffic and market demand forecasts and other assumptions and investment drivers underlying ARTC's proposed capital expenditure forecasts.
- information on how current and forecast prices have been determined, and the estimated impact on access prices of the 2012-13 to 2017-18 capital expenditure program.

The ACCC sought comments as to whether industry considered ARTC's consultation process had provided this type of information and, if not, whether this information (or other types of information) would assist industry to provide feedback on ARTC's proposed capital expenditure projects.

Stakeholder submissions

Asciano

Asciano submitted that 'the information provided by the ARTC in relation to the capital expenditure forecasts is not sufficiently detailed to allow detailed comment on the proposed capital expenditure projects.'[45] More specifically, Asciano submitted that:

- The 'high level of aggregation [is] not conducive to allowing any specific comment on the proposed capital projects and capital expenditure levels'.
- There is either no information on 'specific capital costs attached to specific projects at any level of detail', or where costings are provided, no information on whether they are efficient or reflect market demand.
- There is no information on the assumptions and traffic forecasts which underpin the proposed capital expenditure.
- The lack of detail prevents stakeholders from being able to comment on what capital expenditure should be prioritised by ARTC.[46]

Asciano stated that effective consultation would be facilitated by the provision of more detailed information on:

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45 Asciano, Submission to the ACCC in Relation to the ACCC Consultation Paper on the ARTC's Interstate Access Undertaking Capital Expenditure Variation, February 2012, p. 7.

46 Asciano, Submission to the ACCC in Relation to the ACCC Consultation Paper on the ARTC's Interstate Access Undertaking Capital Expenditure Variation, February 2012, pp. 7-8.

- The capital projects that constitute the proposed capital expenditure.
- The manner in which the capital expenditure forecasts for these projects were developed and evaluated.[47]

In addition, Asciano submitted that the outcomes expected to be achieved by the proposed capital expenditure should be set out. It suggested that capital expenditure should be linked to outcomes via, for example, the following measurable and reportable outcomes:

- Growth in corridor traffics.
- Variation to existing transit times.
- Extent of deployment of ATMS.
- Changes to corridor capability such as train length, speed, axle loading and clearances.[48]

Asciano submitted that such information, in combination with 'involvement from rail operators … will allow an improved determination of the expected benefit of the capital expenditure to both ARTC and rail operators, and consequently will result in more efficient and effective capital investment'.[49] Asciano considered that the provision of this information would increase the accountability of ARTC to deliver these outcomes for the investment identified.[50]

QR National

QR submitted that it supports the Proposed Variation on the basis that more detailed information is provided, including information on the expected impacts on the ceiling price. QR also sought updated information on ARTC's capital expenditure during the period 2006-07 to 2011-12, particularly ongoing projects that are yet to be completed.[51]

QR stated that ARTC should explain how its proposed capital expenditure projects would improve the reliability of service delivery to the end customer.[52]

ARTC

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[47] Asciano, Submission to the ACCC in Relation to the ACCC Consultation Paper on the ARTC's Interstate Access Undertaking Capital Expenditure Variation, February 2012, p. 6.

[48] Asciano, Submission to the ACCC in Relation to the ACCC Consultation Paper on the ARTC's Interstate Access Undertaking Capital Expenditure Variation, February 2012, p. 8.

[49] Asciano, Submission to the ACCC in Relation to the ACCC Consultation Paper on the ARTC's Interstate Access Undertaking Capital Expenditure Variation, February 2012, p. 6.

[50] Asciano, Submission to the ACCC in Relation to the ACCC Consultation Paper on the ARTC's Interstate Access Undertaking Capital Expenditure Variation, February 2012, pp. 8-9.

[51] QR National, Submission on ARTC Interstate Rail Network Access Undertaking variation, February 2012, p. 3.

[52] QR National, Submission on ARTC Interstate Rail Network Access Undertaking variation, February 2012, p. 3.

ARTC submitted that rather than focusing on detailed aspects of project delivery and cost outcomes, its consultations should concentrate on matters such as:

- Establishing market need and assumptions.
- Determining infrastructure capacity and performance requirements to meet that need.
- Considering investment options that can deliver those capacity and performance requirements in a way that is complementary to overall rail improvement and can be delivered in a way that minimises disruption.[53]

ACCC view

The ACCC agrees with the views expressed in submissions that effective consultation on ARTC's capital expenditure program would be facilitated by the provision of additional information on how the capital expenditure forecasts were formulated, the specific projects that make up the estimates, and the expected benefits that will flow from the investments.

In the ACCC's view, the information that would assist industry in assessing ARTC's proposed capital expenditure forecasts and the specific projects that make up those estimates, would include:

- **Estimates of capital expenditure to date and expected expenditure on ongoing projects.** The ACCC notes that further information on ARTC's actual capital expenditure to date for projects identified in Schedule H for the period 2006-07 to 2011-12, and expected future expenditure on ongoing projects, would assist industry in identifying future investment needs and assessing ARTC's proposed capital expenditure program. In this regard, the ACCC notes ARTC's statement in its submission to the ACCC's Consultation Paper, ARTC stated that:

  > *The overall level of Corridor Infrastructure Investment could be expected to be less than levels needed ahead of the substantial investment that has now occurred on both the East West network and North South network not envisaged in 2008 that is likely to have the effect of improving overall asset quality and condition and generally reducing the requirement for asset replacement and renewal at least in the short to medium term.*[54]

- **An explanation of the basis for the capital expenditure forecasts.** Some information of this nature is provided by ARTC in Attachment 3 to its submission to the Consultation Paper. The ACCC considers that detailed information on the traffic forecasts and other assumptions and investment drivers underlying ARTC's proposed capital expenditure forecasts is relevant to the assessment of the forecasts.

- **Details of the expected costs and benefits of proposed capital projects.** As the details of projects are developed, more specific information, including expected

[53] ARTC Submission to ACCC Consultation Paper, February 2012, p. 8.
[54] ARTC Submission to ACCC Consultation Paper, February 2012, p. 13.

costs and outcomes, should be provided for industry comment. This information should include the efficiency benefits expected to flow from the specific projects. Such information would assist network users to rank projects in order of priority and to provide their views as an input to ARTC's development of its capital program.

- **Information on current and forecast prices and how they have been determined.** Information on the estimated impact on access prices of the proposed capital expenditure program would assist network users in assessing the potential financial implications of the capital expenditure program on their own operations. These expected financial impacts could then be compared with expected cost savings and/or increases in volumes of throughput resulting from the capital investments. More information on ARTC's methodology for estimating prices would assist industry in understanding how the proposed capital expenditures contribute to expected price changes.

4.3.4 Conclusion

The ACCC has decided to accept the Proposed Variation to allow capital expenditure estimates for the period 1 July 2012 to 30 June 2018 to be included in Schedule H of the Access Undertaking.

The ACCC has had regard to broad stakeholder support for the Proposed Variation.

Including estimates for the period in Schedule H will also allow for the operation of section 4.4(e) of the Access Undertaking which requires that if ARTC increases its capital expenditure by 20 per cent over the estimated amounts in Schedule H in any single year, it must seek the ACCC's approval before it can roll these amounts into the RAB.

As previously noted, ARTC sought 'the approval of the ACCC for [the proposed] Capital Expenditure to be considered Prudent and therefore able to be included in the annual revaluation of the Network and Associated Facilities'. However, due to the preliminary nature of the proposed capital expenditure estimates, the ACCC has concluded that it would be premature to comment on the prudency or otherwise of the capital expenditure estimates proposed for the period 2012-13 to 2017-18.

In addition, the ACCC notes that ARTC is required under the Access Undertaking to assess the prudency of its capital expenditure program once finalised, against the prudency criteria set out in the Undertaking. The Access Undertaking does not require an assessment of prudency to be made by either ARTC or the ACCC when ARTC submits the Proposed Variation.

The capital expenditure estimates in the Proposed Variation represent a basis for determining the capital expenditure program for the period 2012-13 to 2017-18. The Access Undertaking requires that ARTC assess prudency in relation to ARTC's actual capital expenditure to determine whether it can be rolled into the RAB.

The ACCC is of the view that capital expenditure is more likely to be prudent if effective consultation has taken place during the development and implementation of the capital expenditure program. This Decision paper sets out ACCC views on the key requirements for effective consultation going forward, including:

- the importance of timely and meaningful consultation with industry;
- the type of information that would enable industry to make more informed comments on proposed capital expenditure projects; and
- the level of detail required to facilitate industry assessment of capital expenditure proposals.

Such measures will increase the transparency of ARTC's capital expenditure program and assist ARTC to make investments that best meet industry demands and promote productivity and efficiency. These measures will, in turn, contribute to promoting the economically efficient operation of, use of and investment in the infrastructure by which track access services are provided on the interstate rail network.

Attachment A: ARTC's Variation

Segment/Activity	Estimated Expenditure*											
	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
1. Adelaide (Dry Creek) – Parkeston												
Improvement Project Works	597	1,629	1,913	1,913	1,913	-	14,000	54,825	40,825	-	-	-
ATMS Roll-out	-	-	-	-	-	-	-	-	36,200	36,962	-	-
Corridor Infrastructure Investment	9,476	10,151	10,313	10,243	10,363	10,563	5,754	6,189	6,591	6,321	6,399	6,399
Total Capital Expenditure	**10,073**	**11,779**	**12,226**	**12,156**	**12,276**	**10,563**	**19,754**	**61,014**	**83,616**	**43,283**	**6,399**	**6,399**
2. Adelaide (Dry Creek) – Melbourne (Spencer Street)												
Improvement Project Works	7,756	42,966	7,049	1,913	1,913	-	-	-	-	-	-	50,000
ATMS Roll-out	-	-	-	-	-	-	-	-	-	17,338	45,300	38,225
Corridor Infrastructure Investment	7,270	7,222	4,205	4,205	3,364	4,310	2,443	2,628	2,799	2,684	2,717	2,717
Total Capital Expenditure	**15,026**	**50,189**	**11,254**	**6,118**	**5,277**	**4,310**	**2,443**	**2,628**	**2,799**	**20,022**	**48,017**	**90,942**
3. Melbourne (Tottenham) – Macarthur												
Main South Track Improvement Works	118,322	300,807	194,873	-	-	-	-	-	-	100,000	100,000	50,000
Train Control Consolidation - South	48,852	5,691	-	-	-	-	-	-	-	-	-	-
Corridor Infrastructure Investment	6,783	11,586	2,330	2,082	2,405	2,170	4,511	7,560	4,600	6,410	6,353	6,353
Total Capital Expenditure	**173,957**	**318,084**	**197,203**	**2,082**	**2,405**	**2,170**	**4,511**	**7,560**	**4,600**	**106,410**	**106,353**	**56,353**
4. Newcastle (Islington Junction via mains) – Queensland Border (Border Tunnel)												
North Coast Improvement Works	80,266	125,752	27,799	728	-	-	-	-	-	-	-	-
North Coast Signals/Train Control Improvement Works	2,447	-	-	-	-	-	-	-	-	-	-	-
Northern Train Control Consolidation (allocation)	8,754	2,834	4,279	-	-	-	-	-	-	-	-	-
ATMS Roll-out	-	-	-	-	-	-	-	-	-	-	-	7,075
Corridor Infrastructure Investment	12,914	13,271	5,796	7,880	6,461	5,987	1,949	3,267	1,988	2,770	2,746	2,746
Total Capital Expenditure	**104,381**	**141,857**	**37,874**	**8,608**	**6,461**	**5,987**	**1,949**	**3,267**	**1,988**	**2,770**	**2,746**	**9,821**

5. Crystal Brook – Parkes												
Western NSW Improvement Works	8,834	9,986	417	-	-	-	14,000	21,000	-	-	-	-
Corridor Infrastructure Investment	3,569	3,775	2,166	4,256	3,723	1,616	3,082	3,314	3,530	3,385	3,427	3,427
Total Capital Expenditure	**12,403**	**13,760**	**1,749**	**4,256**	**3,723**	**1,616**	**17,082**	**24,314**	**3,530**	**3,385**	**3,427**	**3,427**
6. Cootamundra - Parkes												
Corridor Infrastructure Investment	1,771	783	3,660	2,807	1,399	970	569	612	651	625	632	632
Total Capital Expenditure	**1,771**	**783**	**3,660**	**2,807**	**1,399**	**970**	**569**	**612**	**651**	**625**	**632**	**632**
7. Adelaide (Dry Creek) – Pelican Point												
Corridor Infrastructure Investment	23	-	-	-	-	-	57	61	65	62	63	63
Total Capital Expenditure	**23**	-	-	-	-	-	**57**	**61**	**65**	**62**	**63**	**63**
8. Port Augusta – Whyalla												
Corridor Infrastructure Investment	-	50	50	-	-	-	216	232	247	237	240	240
Total Capital Expenditure	-	**50**	**50**	-	-	-	**216**	**232**	**247**	**237**	**240**	**240**
9. Moss Vale - Unanderra												
Corridor Infrastructure Investment	337	494	117	876	766	738	198	332	202	282	279	279
Total Capital Expenditure	**337**	**494**	**117**	**876**	**766**	**738**	**198**	**332**	**202**	**282**	**279**	**279**
10. Network (allocation)												
Track Investment (eg Wayside Detection, Wagons, Plant & Equipment)	2,520	2,558	-	5,677	5,722	-	-	-	-	-	-	-
Signals & Train Control Investment (ATMS Concept)	552	13,940	20,351	32,053	-	-	-	-	-	-	-	-
Communications Investment (eg 3G 850, NTCS, ICE)	3,670	28,330	17,920	-	-	-	-	-	-	-	-	-
Total Capital Expenditure	**6,742**	**44,828**	**38,271**	**37,730**	**5,722**	-	-	-	-	-	-	-
11. Other												
Southern Sydney Freight Line	3,464	94,518	143,651	-	-	-	-	-	-	-	-	-
Total Capital Expenditure	**3,464**	**94,518**	**143,651**	-	-	-	-	-	-	-	-	-

Attachment B: ACCC's assessment of 2006-07 to 2010-11 capital expenditure estimates

In its Draft Decision on the 2008 Interstate Access Undertaking (**2008 Draft Decision**), the ACCC noted that the Access Undertaking is intended to promote 'economically efficient investment' in the network (section 1.2(d)(ii)(B)). The ACCC noted that in this respect, capital expenditure needs to be reasonable and prudent (section 4.4(d)(ii)).[55]

In the 2008 Draft Decision, the ACCC conducted a high-level review of the capital expenditure program which focussed on ARTC's processes for generating the scope, standard and cost of ARTC's proposed capital expenditure for the interstate network. The ACCC examined the processes and criteria adopted by ARTC to determine and implement its capital expenditure program. The ACCC considered that if these processes and criteria were reasonable and prudent, they could be expected to promote efficient investment in and use of the network.[56]

The ACCC's preliminary view in its 2008 Draft Decision was that Schedule H, in setting out ARTC's proposed capital expenditure for the 2006-07 to 2011-12 period, did not raise objections under Part IIIA of the Act.[57] This view was maintained in the ACCC's Final Decision.[58]

Details of the assessment process as outlined in the 2008 Draft Decision are set out below. The 2008 Final Decision confirmed the ACCC's position in the Draft Decision.

Scope of capital expenditure

The scope of the capital expenditure is the extent and number of capital projects. In its 2008 assessment the ACCC assessed whether the processes and criteria used by ARTC in developing its proposed capital expenditure were likely to identify and prioritise capital work projects that were of reasonable and prudent scope, such scope being that which:

- is appropriate given the geographic definition of ARTC's network and the forecast size of the market for above-rail services;
- does not include capital biases;
- is commercially sound; and
- has been subject to effective consultation with relevant stakeholders.[59]

The ACCC noted in its Draft Decision that the development of the scope of capital expenditure is subject to numerous ARTC governance mechanisms. Capital projects

55 ACCC Draft Decision, April 2008, p. 197.
56 ACCC Draft Decision, April 2008, p. 200.
57 ACCC Draft Decision, April 2008, p. 209.
58 ACCC Final Decision, July 2008, p. 67.
59 ACCC Draft Decision, April 2008, pp. 201-2.

require budget and project approval at a number of operational levels within ARTC and are subject to internal committee review.[60]

ARTC's Investment Committee assessed whether capital projects are commercially sound against the following criteria:

- whether the capital works will expand revenue;
- whether cost reductions will be achieved as a result of the capital expenditure;
- whether the capital project will reduce risks associated with the operational performance of the network;
- whether the capital expenditure is allocated to enhancement or renewal projects on a net present value basis;
- whether the capital project will promote the business objectives of ARTC; and
- whether the capital projects are in accordance with statutory requirements.

The ACCC concluded that ARTC's internal assessment of commercial soundness of capital projects was robust and was likely to promote reasonable and prudent investment in the network. The ACCC was of the view that:

- ARTC's assessment of commercial soundness of capital projects appeared to involve consideration of issues that were likely to promote efficient investment in the network and reflected industry practice;
- the geographic definition of the network and the forecast size of the above-rail market are important factors affecting the scope of capital works, and the processes and criteria adopted by ARTC were likely to promote capital expenditure that was appropriate in light of these factors;
- there was no evidence that the processes adopted by ARTC were inconsistent with industry practice or that capital expenditure had resulted in unwarranted capital projects.
- while there is the possibility for unintended capital biases to emerge in relation to an increase in standard train length sizes, there was no evidence that ARTC had deliberately sought to engage in capital expenditure projects related to extended train lengths other than to enhance efficient use of the network.

Standard of capital works

The standard of capital expenditure is the technical and operational characteristics of capital projects. The ACCC conducted its assessment on the framework that a reasonable and prudent standard of capital expenditure is one that:

- is not over-designed for the proposed traffic level;

[60] ACCC Draft Decision, April 2008, p. 203.

- meets a specified industry level of construction quality; and
- does not allow for an unwarranted level of investment.

In terms of the proposed traffic level at the time, ARTC's North-South Corridor Strategic Investment Outline (which accounted for a majority of ARTC's capital expenditure) indicated that ARTC had adopted design standards that related to its forecast volume growth, as the proposed investment would lead to improved network capacity and efficient use of the network.

The ACCC also noted that ARTC's 'Five Step Holistic Approach to Track Maintenance' helped to harmonise design standards across the network, as it co-ordinated and prioritised work over the network so that consistent and acceptable standards were implemented for all network infrastructure.

The ACCC did not conduct an audit of ARTC's specific design standards as part of its assessment. However, the ACCC had no information before it to believe that ARTC's design standards did not comply with any relevant Australian design standards or to believe that they raised any concerns with the Rail Industry Safety and Standards Board. The ACCC also concluded that the construction standards relating to track behaviour, such as by increasing the carry of heavier loadings, were intended to promote efficient use of the network by in turn increasing capacity on the network.

Given these conclusions, the ACCC considered that the design standards did not appear to be unreasonably over-designed or excessive for the proposed traffic levels over the term of the Undertaking.[61]

The stated standard of the capital works, coupled with the fact that project standards are reviewed under the processes and criteria that determine the scope of capital works, appeared to be consistent with both the forecast traffic level and standard industry practice, and so appeared to be reasonable and prudent.[62]

Cost of capital works

The cost of capital expenditure refers to the financial cost of the capital projects. The ACCC's 2008 assessment of the cost efficiency of investment focussed on the ARTC funded investment of $670 million as ARTC was only seeking to earn a return on these expenditures. Capital expenditure costs were considered reasonable and prudent if they reflected scope and standards that were appropriate for the proposed traffic level.

ARTC indicated that it assessed the cost efficiency of different project delivery mechanisms on a project-by-project basis, favouring a broad alliance model for major capital projects because it allowed for a competitive selection process, provided a guarantee of available services and known rates and allowed for flexibility in the execution of projects.

The ACCC was concerned that the capital expenditure cost estimates were likely to over-estimate required expenditure over the initial years of the Access Undertaking

[61] ACCC Draft Decision, April 2008, p. 207.
[62] ACCC Draft Decision, April 2008, p. 207.

and under-estimate expenditure in later years. However, it noted that cost estimates were frequently difficult to define precisely several years in advance, and so considered that they were reasonable.

The ACCC considered that the guiding principles used by ARTC to decide appropriate project delivery mechanisms appeared to reflect appropriate industry practice, and as such the cost estimates in Schedule H did not raise any Part IIIA concerns.[63]

Industry consultation

The ACCC noted in its 2008 Draft Decision on ARTC's proposed access undertaking that it had concerns regarding the effectiveness of ARTC's consultation process.[64] While ARTC's internal processes and criteria for approving capital expenditure projects required consideration of stakeholder endorsement/recommendations, the ACCC was concerned with the effectiveness of this consultation.

The ACCC set out that one of its key concerns is whether, in deciding its capital expenditure program, ARTC had consulted interested parties who are likely to be affected by the program, because it will affect their costs, the services they receive or have implications for their investments in above rail.

ARTC was of the view that it has significant commercial imperatives to consult with stakeholders about new network investments, particularly if it does not recover its stand-alone costs and faces inter-modal competition, which constrains its access prices. ARTC argued that the only way it can increase its revenue and eventually recover stand-alone costs is through volume growth, facilitated by new investment. Thus, to effectively model demand growth, encourage complementary above rail investments and to ensure that investment is cost efficient and prudent, ARTC must consult with stakeholders.[65]

The ACCC noted that ARTC had engaged in a series of processes that involve providing information to or requesting feedback from industry. Despite these processes, the ACCC noted that there was considerable industry concern about whether consultation is effective. Concerns were primarily around the *effectiveness* of consultation, rather than the extent of consultation (e.g. issuing papers for comment) [emphasis in original]. The ACCC also noted that this did not mean ARTC should be obliged to address all industry concerns, nor should it be bound to engage in ongoing and iterative industry consultation that is more likely to reflect the interests of individual access seekers than promote industry efficiency. However the ACCC did note that effective consultation and industry confidence in the effectiveness of those consultation processes is important. The ACCC therefore recommended building an obligation into the Access Undertaking for transparent consultation on ARTC's capital expenditure program.[66]

In response to the ACCC's concerns in its 2008 Draft Decision, ARTC modified the proposed undertaking by including clause 6.5, which obliged ARTC to outline its

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63 ACCC Draft Decision, April 2008, p. 209.
64 ACCC Draft Decision, April 2008, p. 211.
65 ACCC Draft Decision, April 2008, pp 211-12.
66 ACCC Draft Decision, April 2008, pp. 212-13.

views on additional capacity, give operators a reasonable opportunity to present their views and to circulate a summary of the results of the consultation. The ACCC considered that this proposal addressed its original concerns.