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V/LINE ACCESS ARRANGEMENT VARIATION

FINAL DECISION

SEPTEMBER 2007

An appropriate citation for this paper is:

Essential Services Commission (2007), 'V/Line Access Arrangement Variation: Final Decision'

1 Proposed Variation

On 22 June 2007, V/Line Passenger Pty Ltd (**V/Line**) applied to the Essential Services Commission (**Commission**) to vary its existing access arrangement applying to the Victorian country network. This application was made pursuant to s38ZO of the *Rail Corporations Act 1996 (RCA)* which permits an access provider to apply to the Commission to vary its access arrangement.

V/Line's Access Arrangement has been in place since 24 April 2007, when the Commission agreed to substitute V/Line as the access provider under the binding access arrangement previously applying to Pacific National (Victoria) Limited (**Pacific National**). V/Line has been the manager of the Victorian country rail network since 4 May 2007, when the Victorian Government completed its acquisition of the network from Pacific National.

At the same time as the rail network was acquired, an access agreement was entered into between V/Line (as access provider) and Pacific National (as access seeker) (**V/Line/PN access agreement**). The V/Line/PN access agreement has a term of 10 years.

On 12 June 2007 V/Line published a revised set of reference prices for its reference services. It has explained to the Commission that these reference prices reflect the prices agreed with Pacific National in the V/Line/PN access agreement.

V/Line proposed to amend its Access Arrangement and the Standard Access Agreement (that forms part of its Access Arrangement) to reflect the key terms and conditions agreed with Pacific National, as contained in the V/Line/PN access agreement. V/Line explained its proposed variations in its letter to the Commission dated 22 June 2007.

2 Process

At the outset the Commission concluded that the proposed variation is a material variation for the purposes of s38ZO(6) of the RCA. It therefore adopted the process as set out in s38Y through to s38ZI of the RCA (with alterations and modifications to that process as necessary to reflect that the process is a variation process). Among other things, this process imposes a 90 day timeframe for the Commission to make its final decision, and requires public consultation on the initial proposed variation and on the Commission's draft decision.

The proposed access arrangement and application for variation were published on the Commission's website on 28 June 2007. Also on 28 June 2007 the Commission issued a letter to interested persons notifying them of the application for variation of an access arrangement by V/Line, and inviting them to make submissions. A notice was published in *The Age* on 30 June 2007 and in the *Weekly Times* on 4 July 2007.

An Issues Paper was released on 3 July 2007 to assist interested persons in making submissions, and one submission was received on 21 July 2007 from Pacific National.

The Commission released its VLine Access Arrangement Variation Draft Decision (**Draft Decision**) on 15 August 2007. The Commission's draft decision was to not approve V/Line's proposed variation to its Access Arrangement. The reasons were set out in chapter 4 of the Draft Decision.

Consistent with s38ZB(5) of the RCA, copies of the Draft Decision were provided to V/Line and Pacific National as the only two parties entitled to make a submission in relation to the Draft Decision under s38ZD of the RCA. The two parties were invited to make their submissions by the 30 August 2007. By the same date V/Line could submit a revised proposed access arrangement variation (s38ZC).

A further submission was received from Victoria Farmers Federation (**VFF**). A copy of the submission is on the Commission's website. V/Line did not make a submission or submit a revised proposed access arrangement variation.

3 Final Decision

The Commission's final decision is to not approve V/Line's application for variation of its Access Arrangement.

4 Reasons

The Commission's draft decision was not to approve V/Line's proposed variation to its Access Arrangement.

Under s38ZB(2)(c) of the RCA and because the Commission had proposed not to approve the proposed access arrangement variation, the Commission specified the amendments it considered should be made, or matters it considered should be addressed, for it to approve the proposed access arrangement variation.

The amendments and matters that the Commission specified are repeated below.

- Remove the minimum charge of \$100.
- With regard to the use of the Somerton Sidings, Melbourne Arrival Sidings and Tottenham Yard for wagon or locomotive storage, and use of the Geelong Grain Loop, V/Line should:
 - identify whether these services are reference or non-reference services, and provide a description of these services in its Access Arrangement in accordance with s38X(1)(a)(i) or s38X(1)(b) as applicable; and
 - include in the Access Arrangement the charges that apply for use of these sidings and tracks under the V/Line/PN access agreement the price for the purpose of s38X(1)(iv), if these are reference services, or provide appropriate indicative terms and conditions for the purpose of s38X(c) if these are non-reference services.
- V/Line's proposed formula in Appendix 11 of its proposed access arrangement should be changed to replace the reference to the 'CPI' with the percentage change in the CPI between two dates. The SAA should have a corresponding definition of CPI, and similarly revised formula for price escalation.

- Change the freight services Revenue Cap in clause 4.3.b to \$32.723 million.
- The SAA should include a clause that makes the track standards subject to the Rail Freight Network Review outcomes.
- Change the definition of Maximum Average Operating Speed in the SAA to include the word “Safety” before “Accreditation” and change the definition of Maximum Average Operating Speed in the proposed Access Arrangement to be the same.
- Change Appendix 6 of the proposed Access Arrangement and Schedule 4 of the proposed SAA to include the existing track Maximum Average Operating Speeds contained in Appendix 6 of the current Access Arrangement.
- Replace clauses 6.1 to 6.3 of the proposed SAA with clause 6.1 of the current SAA.
- Change the definition of Network in Appendix 5 to explicitly include the Somerton Sidings and any other railway tracks covered by the Declaration Orders that are now with V/Line following the buy-back.

As mentioned, s38ZC of the RCA enabled V/Line to submit a revised proposed access arrangement variation within the stipulated timeframe, with the revisions to incorporate or substantially incorporate the amendments, or otherwise address the matters, specified by the Commission in the Draft Decision.

The effect of s38ZF(3) of the RCA is that, in its final decision in relation to a proposed access arrangement variation, the Commission must not approve a proposed variation unless the access provider has incorporated or substantially incorporated each of the amendments identified or otherwise addressed the matters specified by the Commission in its draft decision.

Because V/Line did not submit any such revisions, the Commission is not permitted to approve the proposed variation.

The VFF raised a number of matters in its submission including:

- concerns about the level of prices in terms of the affordability of the impact on freight rates;
- concerns about the degree of price differentiation between grain freight and non-grain freight contained in V/Line’s currently published reference tariffs;
- concerns about the price escalation formula proposed by V/Line;
- concerns about the network operating standards proposed by V/Line, and also that the standards established in the current Access Arrangement may not be adequate; and
- concerns about the ability of V/Line to “book lines out of service”.

While the Commission has considered the matters raised by the VFF, because the Commission is not approving the V/Line proposed variation due to V/Line not having submitted revisions to the proposed access arrangement, the Commission’s consideration of those matters does not form part of the reasons for the Commission’s final decision.

5 Further Reflections on V/Line's Access Arrangement

The Commission is of the view that a number of aspects of the V/Line Access Arrangement still need to be addressed and for this reason it is of practical value to reflect on the steps that might be taken. It may also be helpful for the Commission to address certain of the concerns raised by the VFF.

5.1 Non-compliance with the V/Line Access Arrangement

Under the reference prices that V/Line published on 12 June 2007 – which are the same as those in the V/Line/PN access agreement – the prices for grain freight tasks are more than 20% higher than for non-grain freight tasks. While this may be consistent with s38ZZY(1) of the RCA, it conflicts with clause 4.4.b of the V/Line Access Arrangement.

Therefore, V/Line may not be in compliance with s38ZZT (compliance with access arrangement), a penalty provision which the Commission is responsible for enforcing under Division 8 of Part 2A of the RCA.

A similar issue arises in relation to the price escalation, with the formula contained in the V/Line/PN access agreement not being consistent with clause 4.5 of the V/Line Access Arrangement.

5.2 Prices; task differentiation of prices

VFF was of the view that the proposed prices have driven grain freight costs up by \$2-8 per tonne when compared with the prices set by Pacific National in August 2006. The VFF proposed that there should be a subsidised access regime similar to NSW and Queensland.

VFF also opposed the removal of clause 4.4.b of the V/Line Access Arrangement and considered this removal inequitable as it will disadvantage farmers by increasing the costs of grain haulage. VFF pointed out that despite “grain being responsible for nearly 80 per cent of total rail freight, grain freight has access to less than a 40 per cent share of total Government subsidy”.¹

Whilst the Commission acknowledges the concerns and points raised by the VFF, it is not demonstrated that V/Line's proposed prices are unaffordable. The Commission remains of the view that the Victorian Government and Pacific National had incentives to set an affordable price structure to encourage access to the network when establishing these prices. Furthermore the recent rail freight agreement between AWB GrainFlow and El Zorro to deliver around 15-20% of the total Victorian rail grain task for the new season is indicative of access prices on the Victorian network being affordable.²

¹ p.3 of the VFF's submission.

² AWB/El Zorro media release dated 27 August 2007.

The Commission when approving reference prices under access arrangements is also required to do so consistently with relevant statutory provisions, including s38ZZY and with the Pricing Order. The Commission must also take into account the legitimate business interests of the access provider which, in the current context, would extend to full cost recovery taking into account the government subsidy of 60 per cent.

5.3 Price escalation

In regard to the price escalator, VFF opposed any variation in the price escalation formula as it is of the view that this might further increase the real cost of rail freight.

The question as to the adequacy and effect of the price escalation formula is relative to the level of the initial base period prices. Hence, once again, the Commission must have regard to relevant statutory provisions, including s38ZZY, and the requirement for full cost recovery taking into account the government subsidy.

5.4 Non-compliance with pricing methodology

The Rail Access Pricing Guideline states that where an access provider is the direct beneficiary of a Government contribution, or indirect beneficiary of a Government rail project, then it is incumbent on the access provider to apply to the Commission for a variation of its Revenue Cap under s38ZO of the RCA.

If the access has provider has been the beneficiary of a Government contribution and its Revenue Cap has not been adjusted accordingly the Commission may vary the access arrangement under s38ZP of the RCA.

Although on 8 June 2007³ the Government has announced that it will provide a subsidy to V/Line amounting to approximately 60 per cent of the cost to maintain the regional rail freight network, V/Line has not yet made an application to the Commission to vary its Revenue Cap. This is one of the matters that the Commission indicated in its Draft Decision was required to be addressed before the Commission could give its approval. As the Commission has not approved V/Line's proposed access arrangement variation, this remains to be addressed.

5.5 Service Standards

The VFF opposed any decrease in track maximum operating speeds and the changes to the definition of Maximum Average Operating speed. VFF preferred the adoption of a higher track maintenance standards than those currently contained in the Access Arrangement.

³ Media release "Bracks Government to Subsidise Regional Rail Freight Network" (8 June 2007)

The VFF argued that it is inappropriate to address safety issues by reducing train speeds, rather than maintaining the track in a safe condition. More government support should be provided to ensure appropriate standards are met.

The question of whether tracks standards should be higher than those already established in the V/Line Access Arrangement for its three year term does not arise in the context of V/Line's application for lower standards. As mentioned in the Draft Decision, the Commission would propose to adopt the service levels decided by the Rail Freight Network Review taskforce, when that process is completed.

5.6 Scope of Network

VFF was concerned about V/Line's ability to "book lines out of service".

The Commission is not aware of any constraint within the existing Access Arrangement or the Victoria Rail Access Regime on V/Line's ability to do this.

5.7 Variation of V/Line Access Arrangement

In light of its views on possible non-compliance by V/Line with s38ZZT of the RCA (see section 5.1 above), on prices and task differentiation of prices (see section 5.2 above) and on price escalation (see section 5.3 above), as well as the requirement to adjust the Revenue Cap to take into account the announced Government subsidy (see section 5.4 above) the Commission considers that the V/Line Access Arrangement ought to be varied.

The Commission's preference is for V/Line to seek the proposed variation under s38ZO of the RCA. In the absence of such a request the Commission may elect to initiate a variation under s38ZP, or other steps available or as required. For example, it is notable that under s38ZU, non compliance with a binding access arrangement can form the basis of an access regime dispute.