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**METRO PROPOSED ACCESS
ARRANGEMENT – FINAL
DECISION**

AUGUST 2011

An appropriate citation for this paper is:

Essential Services Commission, 'Metro Proposed Access Arrangement — Final Decision', August 2011

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CHAIRPERSON'S INTRODUCTION

The Essential Services Commission (the Commission) is Victoria's independent economic regulator of prescribed industries identified by the Victorian government. The Commission is responsible for administering an access regime for the Victorian rail industry.

The Commission's regulatory powers in relation to the Victorian rail industry derive from the *Rail Management Act 1996* (RMA). The RMA sets out the Victorian rail access regime that applies to providers of declared rail infrastructure. Metro Trains Melbourne Pty Ltd (Metro) is the provider of the declared Melbourne metropolitan rail network.

The objective of an access regime is to facilitate access to monopoly infrastructure such as the metropolitan rail network. The access regime requires Metro to have in place, at all times, an access arrangement which sets out the terms and conditions and process by which access to the rail network may be obtained, including the access price freight operators must pay to Metro to use their rail network. The access arrangement is primarily used by freight operators who need to travel through the metropolitan network.

Metro's access arrangement includes both price and non-price matters. The non-price matters include certain information that Metro must make available to an access seeker, protocols and procedures that govern access, and a standard access agreement which provides a basis for agreeing the contractual terms and conditions of access between Metro and an access seeker. The access arrangement must also specify what access price Metro will charge rail freight operators to use the railway track to provide a freight haulage service.

Under the RMA, the Commission must assess Metro's access arrangement and make a decision whether to approve or not approve it.

The Commission's final decision is to not approve Metro's access arrangement.

As a result of the Commission's decision to not approve Metro's access arrangement, the RMA requires the Commission to make the access arrangement for Metro. The Commission will do this by reflecting the Commission's final determined access price and non-price amendments into Metro's access agreement.

While Metro has attempted, on the whole, to address most of the matters outlined in the Commission's draft decision, the Commission's final decision to not approve Metro's proposed access arrangement is based on two main factors:

- a rejection of Metro's revised proposed access price of \$6.21 per '000 gross tonne kilometres in 2011-12 dollar value terms versus the

Commission's final decision price of \$6.14 per '000 gross tonne kilometres in 2011-12 dollar value terms, and

- the requirement for a number of amendments to Metro's access agreement to ensure a better balance between the rights and responsibilities of the parties to the agreement.

The legislation requires the Commission to determine an efficient price for rail access. The Commission has determined this to be a price that is no less than the incremental costs (such as wear and tear) imposed on the network by the relevant freight operator. Pricing at incremental cost is the lowest price the Commission can adopt within accepted regulatory principles in order to maximise the potential for freight's on-going use of the Metro rail network.

The Commission has not significantly increased its access prices since the last regulatory determination (2006/07 – 2010/11). The Commission's determined access price for 2011/12 of \$6.14 per '000 GTK is less than what the access price would have been if the previous determination had been rolled over.

Dr Ron Ben-David
Chairperson

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GLOSSARY

Above rail operator	A person or company that operates (runs) trains (rolling stock) for movement of freight/cargo.
Access agreement	A standard agreement between an access provider and an access seeker that sets out the contractual terms of access. Can be negotiated between the parties.
Access arrangement	Sets out the process and protocols and information for obtaining access to the rail network. It includes the access agreement.
Access arrangement information	Information provided by Metro to an access seeker.
Access provider	A provider of a declared rail transport service, in this case Metro.
Access regime	The overarching legislative framework for access (see Part 2A of the <i>Rail Management Act 1996</i>).
Access seeker	A person seeking access to a declared rail transport service. Usually an above rail operator.
Account Keeping Rules	A Commission Instrument which requires access providers to maintain and provide the Commission with accounting records and accounts.
Ballast	The material most commonly used to form the road bed of a railway track. It is laid on the base formation of the track with the track laid on top of it and provides a storm water drainage medium.
Ballast cleaning	The process of extracting the ballast from the railway track and shaking or washing the ballast to remove detrimental material, and then returning it back to the track. The process improves the performance of the ballast by removing the material that tends to lubricate the ballast particles. The process is most commonly performed using

a track mounted machine and the track is relatively undisturbed while it occurs.

Below rail	The rail track infrastructure.
Bridges (Over and Under the Track)	Overbridges are those that go over the track and are typically pedestrian footbridges or road bridges. Underbridges are under the track and typically convey rivers, subways, or roadways. The bridge structure is separate from the earth formation that is usually under the track but abuts the earth formation at the 'abutments'.
Capacity	The capability of the rail network, when used, to provide declared rail transport services.
Capacity Use Rules	A Commission Instrument which improves the functionality of a third party access regime by ensuring a fair and reasonable allocation of network capacity to access seekers and users.
Commission Instruments	Rules and guidelines made by the Commission which are intended to ensure that the Victorian Rail Access Regime is efficient and effective.
Culvert	A form of underbridge conveying a stream, but with a construction that is integral to the formation or embankment consisting of the earth under a railway track.
Declaration Order	An Order of the Governor in Council pursuant to section 38I of the <i>Rail Management Act 1996</i> that declares certain infrastructure available for access.
Draft decision	A decision of the Commission made under section 38ZB of the <i>Rail Management Act 1996</i> .
Final decision	A decision of the Commission made under section 38ZF of the <i>Rail Management Act 1996</i> .
Gross tonne kilometres (GTK)	The rail industry standard measure of track usage or output. GTK is the product of the tonnage carried (gross tonnes) and the distance travelled (kilometres).
Indemnity	A sum of money that is required to compensate a party for a particular loss or damage it may suffer during the

performance of the contract.

Interconnection	Connection to the access provider's declared railway track.
Intermodal	The use of various modes of transport to move cargo and or freight.
Inspections	This activity monitors the condition of the asset either visually or by electronic or mechanical means. It is usually performed on a regular and predictable basis and is 'routine' in nature. Inspections occur on train running assets such as bridges, track, signals, communications equipment and overhead traction equipment, as well as stations.
MPM (Major Programmed Maintenance)	Also known as Major Periodical Maintenance. Maintenance that is planned and requires the used of large machinery and disrupts train services. Includes replacing rail, sleepers, ballast, turnouts, rail grinding.
Negotiation Guidelines	A Commission Instrument that sets out requirements for each access provider to establish a process for negotiation of access agreements that is fair and equitable.
Net Tonne	Weight of the freight
Network Management Rules	A Commission Instrument which provides protocols for how access to the network will be managed in order that the access provider does not hinder third party access or discriminate against third party network users.
Non-reference service	A declared rail transport service that is not a reference service.
Operator	Freight operator — user of the metropolitan rail network.
Performance bond	An irrevocable bank guarantee, letter of credit or insurance bond callable by the access provider in a form approved by the access provider.
Pricing Order	An Order of the Governor in Council pursuant to section 38J of the <i>Rail Management Act 1996</i> specifying the principles and/or authorising the Commission to determine methodology for calculating prices for declared rail

transport services.

Proposed access arrangement	An access arrangement submitted to the Commission for approval under section 38W of the <i>Rail Management Act 1996</i> .
Rail joint	A mechanism to join two sections of rail by mechanical means, usually by bolts and side plates (fishplates). 'Insulated rail joints' are used to define the limits of an electrical section of the rail for signalling purposes. 'Mechanical rail joints' are used where the lateral stability of the track is not sufficient to resist forces generated in the heating and cooling of the rail in the summer and winter months respectively. Otherwise most rail is welded to form long lengths of 'continuously welded rail'.
Rail gauge	The distance or width between the inner sides of the rails.
(Rail) Grinding	The process of grinding the head of the rail with a machine equipped with grinding stones and which travels longitudinally along the railway while the stones perform their grinding transversely to the direction of the machine's travel.
Reactive maintenance	Maintenance that is a 'reaction' to a failure of the asset and is therefore unplanned with the failure not predicted. In a well-run railway this type of maintenance is minimised.
Reference service	A declared rail transport service that is likely to represent a significant proportion of demand by access seekers.
Renewals	As distinct from 'repair', a process that replaces large sections of the asset such as the replacement of rail or sleepers. Renewals are usually planned well in advance because the work requires large pieces of equipment and is likely to disrupt the train traffic. Unplanned renewals occur where catastrophic and otherwise undetected failure occurs.
Ring Fencing Rules	A Commission Instrument which aims to ensure that access is provided in a non-discriminatory way where an access provider is vertically integrated.
Rolling stock	A vehicle that operates on or uses a railway track or tramway track, and includes a locomotive, carriage, rail car, rail motor, light rail vehicle, train, tram, light inspection vehicle, road/rail vehicle, trolley, wagon or monorail

vehicle.

Routine maintenance	That maintenance which occurs on a regular basis, probably on a time cycle, and which involves minor train traffic disturbance and small machinery. A large part of routine maintenance is inspection of the condition of the asset.
Signalling	In a passenger railway a system of electrical circuits, detectors and electrical switches that detects the location of trains and provides visible commands to train drivers and information to other railway workers.
Sleeper	The component of the railway track that keeps the rails a specified distance apart and transmits the load from the rails to the ballast. In Melbourne timber sleepers are the dominant form, but a program of using concrete sleepers has begun and these will be progressively introduced. Timber sleepers display typically a 20 to 25 year life because they deteriorate with time. Concrete sleepers have a reasonably indefinite life.
Tamping	The process by which ballast is packed around the sleepers of a track to ensure the correct position for the location, speed and curvature. Can be done manually or mechanically by special 'tamping machines', usually independently powered track vehicles.
Terminal	A facility at which freight is loaded or unloaded from rolling stock, or stored, and includes hard stands, equipment and other infrastructure used for the loading or unloading of freight from rolling stock at the facility.
Traction equipment	Equipment used in the reticulation of electrical power to an electric train. The equipment includes substations containing transformers and rectifiers, where power is captured from main power grids and converted to power suitable for the trains, and the wires and fittings that transmit the power to the pantograph which is the collection mechanism on the train.
Train operator	A company that runs rolling stock (that is, an above rail operator).
Turnout (switch)	A section of track approximately 30 metres in length that permits the deviation of a train from one track to another. Two turnouts assembled back to back on parallel tracks constitute a 'crossover'.

Ultrasonic Flaw Detection (rail testing)	A system for examining the condition of rails to determine the integrity of the steel. The data is collected by an electronic instrument run along the track using ultrasonic pulses and the examination of the return signal from the rail.
Vertical integration	The degree to which a firm is integrated (that is, owns or controls both below rail and above rail operations in a market).

1 | SUMMARY OF FINAL DECISION

The Commission's final decision

The Commission's final decision is to **not approve** Metro's access arrangement in respect of the metropolitan rail network.

In making its final decision, the Commission has taken into account the matters it is required to as outlined in Section 38ZI of the *Rail Management Act 1996* (the RMA).

The legislation provides that where revisions have been submitted by Metro, the Commission must be satisfied that the revisions address the matters specified in the Commission's draft decision. Where the Commission is not satisfied, the legislation provides that the Commission must not approve the proposed access arrangement, and must make the access arrangement itself.¹

While Metro has attempted, on the whole, to address most of the matters outlined in the draft decision, the Commission's decision to not approve Metro's proposed access arrangement (as revised) is based on two main factors:

- a rejection of Metro's revised proposed access price of \$6.21 per '000 gross tonne kilometres in 2011-12 dollar value terms in favour of the Commission's final decision price of \$6.14 per '000 gross tonne kilometres in 2011-12 dollar value terms; and
- a number of non-price matters relating to Metro's access agreement (discussed below).

The Commission will therefore establish the access arrangement for Metro. The access arrangement will include the Commission's determined access price path as well as the non-price amendments.

This chapter provides a high level summary of the Commission's final decision in relation to both the price and non-price matters of Metro's access arrangement. Chapters 2 and 3 set out the reasons for the Commission's final decision in more detail.

¹ Sections 38ZF and 38ZJ of the RMA.

Background to this final decision

On 31 March 2011, Metro submitted to the Commission an application to renew its access arrangement. Metro's access arrangement was due to expire on 30 June 2011.² On 28 April 2011, the Commission released an issues paper and undertook a stakeholder consultation process which included meeting with stakeholders and seeking submissions to the matters raised in the issues paper.

Following further stakeholder consultation, the Commission released its draft decision on 15 June 2011 which was to not approve Metro's access arrangement. The draft decision outlined the Commission's views on Metro's proposed access arrangement and set out the amendments and matters that Metro was required to address in order for the Commission to approve Metro's proposed access arrangement.

On 6 July 2011, the Commission received submissions from stakeholders and Metro submitted its revised access arrangement in response to the Commission's draft decision. Metro also submitted a subsequent submission on 26 July 2011 which the Commission has taken in to account.

Following further consultation and meetings with stakeholders and Metro, the Commission has issued this final decision.

Price issues

The Commission is required to determine an efficient price for rail access. Given the current context within which rail freight operates – that is, given competition from road, the Commission has determined the efficient price as one that sets the access price for freight services equal to the incremental cost freight traffics impose on the Metro network. Pricing at incremental cost is the lowest price the Commission can adopt within accepted regulatory principles in order to maximise the potential for freight's on-going use of the Metro rail network.

In this final decision, the Commission has maintained its approach from the draft decision and determined a freight access price equal to the incremental costs that freight imposes on the Metro system. Following submissions and consultations from Metro and stakeholders and further refinement of cost data, the Commission has determined that the incremental costs directly attributable to freight, averaged over the 5 years of the Metro Annual Maintenance Plan (AMP), equates to \$1.257 million (increased from \$1.199 million in the draft decision).

Table A below sets out the Commission's determined price path and revenue requirement. Given Metro's demand GTK forecasts, an access price of \$6.00 per thousand GTK held constant in real terms (\$2010/11) will deliver the discounted revenue requirement of \$5.50 million over the regulatory period.

² The legislation provides that Metro's current access arrangement continues until the Commission issues its final decision.

The cost forecasts reflect the maintenance costs contained in the 2010/11 Metro AMP and actual operating and overhead costs for 2010/11. Although the Commission is satisfied that Metro's overall costs (quantums) are efficient based on the engineering review of the AMP by GHD, it is reasonable to expect continuous improvement will be maintained, and that some additional productivity benefits should flow through to freight customers in prices. Accordingly, an X-factor of 1 per cent per annum has been applied to the access price of \$6.00 to create the determined access price path. The X factor has been applied from 2010/11 rather than the first year of the next regulatory period (2011/12) to allow for productivity improvements since the AMP was constructed.

Table A: Commission determined access price, price path and revenue requirement

	2010/11	2011/12	2012/13	2013/14	2014/15	2015/ 16	Total
Freight forecast GTK	207	210	216	223	229	236	
Access price (\$/000 GTK) (\$2010/11)	6.00	6.00	6.00	6.00	6.00	6.00	
Revenue (\$ million)		1.260	1.298	1.337	1.377	1.419	
Discount factor		0.94	0.88	0.83	0.78	0.73	
Discounted required revenue (\$ million)		1.184	1.146	1.109	1.073	1.038	5.50
Access price path ¹ (\$/000 GTK) (\$2010/11)	6.00	5.94 ²	5.88	5.82	5.77	5.71	
Revenue (\$ million)		1.248	1.272	1.297	1.323	1.349	
Discounted required revenue (\$ million)		1.172	1.123	1.076	1.031	0.987	5.39

1. Price path is discounted by an X factor of 1 per cent.
2. As per the variation for inflation clause (clause 3.1 of the access arrangement) this price becomes \$6.14 once adjusted for inflation.

Have access prices significantly increased?

For comparison purposes, Table B shows the last regulatory period's access price path determined by the Commission. It is clear that the Commission has not significantly increased its access prices since the last determination. In fact, the Commission's proposed access price for 2011/12 (\$6.14 per '000 GTK) is less than it would have been if the previous determination had been rolled over.

Table B: Previous (last regulatory period) ESC determination price path (2006/07 – 2010/11)

<i>\$2005/06</i>	<i>2006-07</i>	<i>2007/08</i>	<i>2008/09</i>	<i>2009/10</i>	<i>2010/11</i>
\$/ '000 GTK ¹	5.58	5.52	5.46	5.41	5.36
Adjusted for inflation ²	5.75	5.82	6.00	6.10	6.21

1. Price path is discounted by an X factor of 1 per cent.
2. Adjustment for inflation as per clause 3.1 of the access arrangement

Summary of price issues: final decision

The Commission does not accept the access price or revenue cap (forecast revenue requirement) proposed by Metro. The Commission will make the access arrangement reflect the following:

- forecast revenue cap outlined in Table A, and
- access price path outlined in Table A.

Non-price issues

The non-price matters of Metro's access arrangement include certain information that Metro must make available to persons seeking access, such as information regarding prices and train paths, various protocols and procedures regarding the governance and provision of access and an access agreement, which is a template contract that provides the basis for agreeing the contractual terms and conditions of access between Metro and a freight operator.

The Commission's draft decision required a number of amendments to Metro's proposed access arrangement to address non-price issues in order for it to be approved. These amendments related to Metro's compliance with:

- the Network Management Rules, and
- amendments to Metro's standard access agreement.

In its revised access arrangement to the Commission, Metro has made the necessary changes to its access arrangement regarding the Commission's draft decision requirements in relation to the Network Management Rules. However, for accuracy and clarity, clause 6.5 of Metro's train operating protocol, which mistakenly refers to 'The Victorian Rules & Operating Procedures', is to be amended to refer to the 'Book of Rules and Operating Procedures'.

In relation to the access agreement, Metro has accepted the majority of the amendments required by the Commission. However, a few issues remain outstanding. Six required amendments will be made by the Commission and are summarised as follows:

- A definition for Passenger Weighted Minutes is to be inserted in section 1.1 (with respect to delay payment indemnity in clause 14.6).
- Clause 2.3 relating to the option to extend the access agreement is to be amended to reflect the intent that the access provider and operator are to enter into good faith negotiations in order to determine the terms of an extension of the access agreement (including price).
- In line with the amendment to clause 2.3, clause 4.3 relating to variation of the access charge during the extension of the access agreement is to be removed.
- Clause 4.4 (now 4.3) relating to incremental costs is to be amended to provide that where incremental costs are attributed to any *users of the network*, the access provider will make a reasonable allocation of these costs between these *users of the network* (including Metro in its capacity as an above rail operator).
- Clause 4.10 (now 4.9) relating to the payment of a performance bond is to be amended to clarify the circumstances where Metro will require an operator to pay a performance bond.
- Clause 12.4 relating to the reporting of incidents is to be amended to include a reasonableness requirement – that is, the operator must provide any information requested by the access provider to meet its *reasonable* internal accident investigation requirements.

In addition to the amendments to the standard access agreement, Metro submitted a number of additional revisions to the regulatory accounts templates (Attachment E of Metro's access arrangement) and the operating handbook at (Attachment G of Metro's access arrangement). These included revised versions of the following attachments:

- Pro-forma regulatory accounts templates (Attachment E)
- Train operating protocol (Attachment G.3)
- Track occupation protocol (Attachment G.4), and
- Operational interface procedures (Attachment G.5).

The Commission has reviewed these documents and is satisfied that the changes that have been made are acceptable.

Summary of non-price issues: final decision

The Commission does not accept Metro's proposed standard access agreement (Attachment A of Metro's proposed access arrangement) and train operating protocol (Attachment G.3 of Metro's proposed access arrangement). The Commission will make the access arrangement reflect the following:

- the six outstanding amendments to the standard access agreement outlined above, and
- the correct title of the 'Book of Rules and Operating Procedures' referred to in Clause 6.5 of Metro's train operating protocol.

2.1 Introduction

Like any business that offers a service, costs are incurred in order to provide that service. In this assessment, the service of interest is access to the Melbourne metropolitan rail network. Metro is the operator of this network and provides access to freight operators in return for a fee (an access price) so that freight operators can use the rail network to provide a freight haulage service.³

Metro's access price is made up of three main categories of costs: maintenance costs, operations costs and overhead costs.⁴ Three main users use the metropolitan rail network, namely: Metro passenger trains, V/Line passenger trains and freight trains. Costs must thus be allocated between freight services and the other users in order to determine a revenue cap for freight access.

In particular, while the Commission is satisfied that Metro's overall costs (quantums) are efficient, the Commission was concerned about the way Metro allocated these costs to freight services. The Commission wants to ensure that in deriving an access price, that price is based only on costs *directly attributable to freight's* use of the metropolitan network.

As a result, in its draft decision, the Commission set out a methodology to establish the costs directly attributable to freight's use of the metropolitan network. This involved an assessment of the maintenance and operations costs which are incremental with respect to usage of the system as a whole as well as an appropriate basis for estimating and allocating the proportion of those costs directly attributable to freight's usage of the system.

The costs included in this assessment of incremental costs cover routine maintenance of track, structures and signalling and communications infrastructure, periodic or cyclic maintenance which is carried out on a regular basis every few

³ It would be inefficient for freight operators to each build their own railway track. This is the thrust of access regimes, to open up or provide access to monopoly infrastructure which cannot be economically duplicated.

⁴ The return on assets and regulatory depreciation components of the revenue cap are set to zero. The Metro regulatory asset base (RAB) was set to zero at the outset of the regime and Metro has indicated that no capital expenditure eligible for the RAB (that is, excluding asset replacement or renewal expenditure) has been funded either by itself or its predecessor (Connex) since then, nor has any future capital expenditure of this type been proposed. Metro's proposed WACC is assessed at Appendix B of this decision.

years and asset renewal when assets becomes life-expired.⁵ It does not include maintenance related to the traction electricity system, as no freight services use electric traction, nor maintenance associated with passenger-specific infrastructure such as stations. It also does not include expenditure on assets which are increasing the capacity of the network for passenger services such as new lines, triplication or junction improvements. It also includes the cost of operating the network, that is, train planners and schedulers, train controllers and signallers as well as regulatory-related costs and a share of general corporate overheads.

This chapter summarises the Commission's draft decision on pricing matters, sets out Metro's and stakeholder responses to the Commission's draft decision in relation to the price matters, and the Commission's final consideration and decision on access pricing.

2.2 Commission's draft decision – price issues

2.2.1 Maintenance costs

Maintenance costs are the costs to repair and maintain the network in order to support the continued availability of rail services. For example, in the case of Metro, these include routine inspection and maintenance, cyclic maintenance (for example, tamping, rail testing and grinding, ballast cleaning) and asset renewal. Metro must undertake its maintenance activities in accordance with the Government's Asset Management Plan (AMP) for the network and the Annual Works Plan for each year.

Assessment of maintenance costs

Metro's proposed maintenance spend for track, signals and bridge maintenance over the five year regulatory period is approximately \$684 million.⁶ The Commission's engineering consultant, GHD, assessed the efficiency of Metro's maintenance costs by reviewing Metro's Asset Management Plan and Asset Works Plan, the nature of work to be performed and the process for generating the maintenance estimates. The Commission was satisfied that the expenditure levels are efficient, but a primary consideration for the Commission was the extent to which these costs are allocated to freight services.

⁵ All asset renewal expenditure funded by the franchising arrangements is expensed in the year it is incurred and has been treated as operating expenditure by the Commission. Asset renewal normally includes an element of improvement or upgrading. All expenditure associated with upgrading in the Metro Asset Management Plan is designed to benefit passenger services and it has therefore been excluded from any consideration of incremental costs for freight services.

⁶ See page 22 of Metro's Access Arrangement Information, which gives \$634 million for track and signals maintenance. This figure was based on the current Metro network plus the inclusion of the section from Sydenham to Sunbury, which is expected to be completed within the regulatory period. The Commission has included a further \$50 million for the estimated spend on bridge maintenance and renewal over the regulatory period based on the advice of its technical advisor.

In its draft decision, the Commission’s view was that Metro’s proposed allocation of maintenance costs to certain traffics such as freight relied too heavily on a high level apportionment of aggregate system wide costs. As a result, the Commission determined an alternative, more targeted, approach which estimated the incremental costs directly attributable to freight’s use of the metropolitan network, and then assessed the impact of any additional allocation of the remaining fixed costs to freight users (that is, those costs which do not vary with usage of the network).

Establishing the incremental costs directly attributable to freight’s use of the metropolitan network firstly involves an assessment of the variability of maintenance costs with respect to usage of the *system as a whole*.

In practice, the variability of maintenance costs with respect to usage varies significantly between the different maintenance activities. For example, track inspection costs in the metropolitan area do not vary significantly with usage, but the costs of unplanned renewals (such as breakages) are highly correlated with usage. Track routine maintenance and renewals have a significant component which is variable with usage, while the maintenance of signals and structures such as bridges is only variable to a limited extent.

Table 1: Incremental maintenance cost by activity (draft decision) (\$2010/11)

Activity	5 Year AMP (\$A millions)	% variable with usage	Annual cost (\$A millions)		
			Variable	Fixed	Total
Track					
Inspections	15.5	0	0.0	3.1	3.1
Reactive maintenance	5.1	50	0.5	0.5	1.0
Routine maintenance	145.8	10	2.9	26.2	29.1
Planned renewals	260.1	20	10.4	41.6	52.0
Unplanned renewals	3.4	80	0.5	0.1	0.6
Subtotal	429.9		14.4	71.6	86.0
Signals	204.1	5	2.0	38.8	40.8
Structures	50.0	15	1.5	8.5	10.0
Total	684.0		17.9	118.5	136.8

Source: GHD report for ESC

As detailed in the draft decision, the Commission engaged engineering firm GHD to determine these variabilities (summarised in Table 1). These were based on the inherent variability of each activity but adjusted in some cases to remove the significant component of the Asset Work Plan that represented ‘catch-up’ maintenance that compensated for under-maintenance in previous years.⁷ The

⁷ For example, track renewals (including turnouts) would normally be expected to be about \$25 million per annum for a network of Melbourne’s size and complexity and to be about 40 per cent variable with usage, that is, an annual cost of about \$10 million. The AMP includes \$52.6 million per annum for the same items. Accordingly, around half of the AMP renewals program could be expected to be either ‘catch-up’ maintenance or upgrading (for

estimate of *total incremental costs* incurred across the system by *all users* of the system was assessed as \$17.9 million per annum.

Cost drivers

Cost drivers are the factors that influence the cost of a particular activity. Rail infrastructure maintenance is principally driven by three such factors:

- The first is elapsed time, with many activities needing to be done to a greater or lesser extent solely due to the passage of time; the classic example is vegetation control, either by the side of the track or in the ballast and impeding drainage.
- The second is gross tonnage (that is, the total weight of the trains⁸ passing over the line) which affects track maintenance costs, and
- The third is the number of trains passing over the line, which affects signalling costs, including level crossings, to some extent.

Allocation of incremental maintenance costs to freight

Where the users are similar types of services, incremental track maintenance costs can be simply allocated on the basis of the gross tonne kilometres (GTK) of each user.⁹ However it is acknowledged that, other things being equal, the wear and tear imposed on the track (and hence the incremental maintenance costs) by different types of train types is also a function of their operating characteristics – in particular their axle load and speed. This is much the same as heavy road vehicles causing relatively more pavement damage on roads than passenger cars, due to their heavier axle loads. This is particularly the case with respect to structures (bridges), where the heavier axle loads of freight services typically drive a higher maintenance requirement.

Attributing incremental track maintenance costs to freight and passenger services on the basis of relative GTK – that is, unadjusted for the axle loads and speeds of the different types of service – would therefore generally tend to underestimate the

example, replacing wooden sleepers with concrete sleepers). This was confirmed by examination of individual components of the program and the incremental cost from current usage was therefore assessed at 20 per cent of the total expenditure on renewals in the AMP.

⁸ The gross tonnes are the sum of the weight of the locomotive, carriages and wagons (known as the tare weight) as well as the weight of any freight they may be carrying (known as the net tonnes).

⁹ GTK is the rail industry standard of track usage. GTK is the product of the gross tonnes of the train and the distance travelled (kilometres). A single gross tonne-km is not very much – it's like a watt-hour. Generally thousand GTK is used when calculating charges and other usage-related indicators as the cost is then something reasonable – much as electricity charges are generally quoted 'per kwh' rather than 'per wh'.

relative damage to the rail network from freight services. As a result, the Commission has adopted the approach of UK regulator (the Office of Rail Regulation) to estimate the incremental costs imposed by freight trains on a rail network.

Much work has been done in the UK rail sector in establishing the link between maintenance costs and vehicle characteristics through estimating equivalent gross tonne kilometres (EGTKs) and equivalent structures gross tonne kilometres (ESGTKs).¹⁰ EGTK takes account of the differences in vehicle characteristics between passenger and freight services when applied to track maintenance costs¹¹, while ESGTK performs the same role when applied to the cost of maintaining bridges and other track structures.¹²

The Commission's technical consultant, Booz & Company adopted the UK framework to estimate the EGTKs and ESGTKs performed on the network. These operating statistics were derived from the characteristics (axle load, speed and unsprung mass) of the rolling stock used by freight services, Metro services and V/Line passenger services that use the Metro rail network and then applied to the services operated on the network in 2010 (Table 2).

Table 2: Operating statistics by service type 2010 (draft decision)

Operating statistic	Metro (1)	V/Line (2)	Freight (3)	Total (4)	% freight (5) (3)/(4)
Train-km (000)	20 746	3 019	170	23 935	0.71%
Gross tonne-km (mill)	5 699	632	223	6 553	3.40%
EGTK (mill)	8 960	1 450	441	10 851	4.06%
ESGTK (mill)	27 094	13 694	4 668	45 457	10.27%

Column 3 of Table 2 shows that freight services generated 170 000 train kilometres (TK) on the Metro network in 2010, or 0.71 per cent of the total of 23 395 million train kilometres as shown in Column 5. However, they represented 3.40 per cent of the gross tonne kilometres (GTK) because of their much larger weight per train. The impact of the higher axle loads of freight trains is clearly seen, with freight accounting for 3.4 per cent of the gross tonne-kilometres but 4 per cent of the EGTK and 10.3 per cent of the ESGTK.

The incremental maintenance cost attributable to freight was then derived by splitting the various components of each of the identified maintenance activities

¹⁰ See, for example, Review of Variable Usage and Electrification Asset Usage Charges, Final Report Booz Allen Hamilton and Transport Technology Centre Incorporated (TTCI) 2005.

¹¹ It is a measure of the damage to track. An equivalent gross tonne kilometre (EGTK) adjusts for axle loads, operating speeds and the unsprung mass of different users of the track, based on a series of studies and analyses undertaken by the research arm of British Railways, supplemented by research commissioned from various groups of consultants. See Appendix 2 of the Booz & Company report for more details.

¹² It is a measure of the damage to structures. An equivalent structures gross tonne kilometre (ESGTK) adjusts for axle loads and operating speeds of different users of the track. See Appendix 2 of the Booz & Company report for more details.

using the relevant resource cost driver (that is, operating statistic in Table 2). Thus the incremental track maintenance costs were distributed between services on the basis of their relative EGTK (with freight thus being allocated 4.06 per cent), incremental signal maintenance costs on the basis of train kilometres (with freight being allocated 0.71 per cent) and variable bridge maintenance costs on the basis of ESGTK (with freight being allocated 10.27 per cent). The freight share of the total incremental maintenance costs of \$17.915 million in the draft decision is thus \$0.753 million or 4.2 per cent of total variable maintenance costs as shown in Table 3.

Table 3: Allocation of incremental infrastructure maintenance costs by service type (draft decision)

	Basis	Incremental costs (\$ million 2010/11)				Freight Share (%)
		Metro	V/Line	Freight	Total	
Track	EGTKM	11.870	1.920	0.584	14.374	4.1%
Signals	Train-km	1.769	0.257	0.014	2.041	0.7%
Structures	ESGTKM	0.894	0.452	0.154	1.500	10.3%
Total		14.533	2.630	0.753	17.915	4.2%

Notes: Track is allocated on the basis of EGTK therefore 0.584 is calculated from table 2 for freight EGTK $(441/10,851) \times 14.374$

2.2.2 Operations costs

Operations costs represent the cost of operating the network, which includes the network operations costs (that is, planning and scheduling trains¹³ and train control) and, in a few locations, physically signalling trains and operating level crossings.

Assessment of operations costs

Operations costs cover both Metro services and other users of the metropolitan rail network and separating these costs between users of the system is difficult given the integrated way in which rail systems operate. Thus, in the case of Metro, the train planners produce an integrated working timetable covering all movements on the metropolitan network by all users. Similarly the train controllers control all movements on a given stretch of line, regardless of whether they are freight, suburban passenger or V/Line passenger.

The Commission's technical consultant, Booz & Company, assessed the efficiency of Metro's operations costs and reviewed Metro's accounts. Booz estimated a total operations cost (which includes train control and train planning) of \$25.3 million per annum, including labour on-costs. This cost does not include regulatory/advisory/legal costs associated with negotiating access agreements or

¹³ Train planning and scheduling includes the preparation of the working timetable, which is a master timetable normally updated annually but sometimes more frequently. It also includes periodic updates to the working timetable and, on a more short-term basis, the preparation of changes to the timetable to reflect such things as maintenance possessions, when no trains can operate as planned, or changes in freight train requirements

the costs of regulatory submissions and approvals which are included as a direct overhead cost. On the basis that the operations costs will predominantly support Metro's own operations, and that the cost allocated to freight is small, the Commission is satisfied that the quantum of costs is reasonable.

Allocation of operations costs

While train control and operations costs are often considered to be unaffected by small changes in system usage, there is no doubt some savings in these costs that may be achieved if freight services no longer used the metropolitan rail network.

In its draft decision, the Commission determined that train kilometres is a reasonable cost driver for allocating operations costs to determine the incremental use of the system as it proxies the time trains are spent being controlled on the network. Train kilometres is thus a reasonable basis for assessing the operations costs attributable to freight services. As detailed in the draft decision, the Commission determined the annual incremental operations costs at \$179 000 (0.71 per cent of the total cost (\$25.3 million) in line with the share of train kilometres given in Table 2).

2.2.3 Overhead costs

Overhead costs consist of two main categories: costs directly associated with the provision of access and the regulatory process (referred to as regulatory and access administration) and a share of the other corporate costs such as corporate management activities, including finance, human resources and corporate planning which support the operations and maintenance functions.

Assessment and allocation of overhead costs

Metro's regulatory and access administration costs were reviewed by Booz & Company and estimated to be approximately \$160 000 per annum. Booz & Company has advised that these costs are associated with the administration of access including negotiating access with freight operators and access agreements and the regulatory process. These costs are directly attributable to third party users of the metropolitan network and it is appropriate that reasonable access related costs are recovered directly from users of the network.

In relation to other overhead costs (which are not directly attributable), Booz & Company reviewed and assessed Metro's overheads costs and assessed them to be 7.2 percent of their direct costs (largely operations and maintenance but also including a few service-specific activities such as passenger ticketing and access administration). This is a reasonable proportion compared to comparable figures for other rail operators, which are typically between 7 and 10 percent. In addition, a profit margin of 3 per cent was allowed, consistent with the 2006 Commission decision. The corporate overheads and profit attributable to freight is thus 10.2 percent of \$1.090 million or \$112 000 per annum.

2.3 Summary of Commission draft decision

In its draft decision, the Commission determined that the reference price should be set at the incremental cost of freight's use of the Metro network. The reference

price of \$5.39 '000 GTK was therefore calculated by dividing the total incremental costs attributable to freight of \$1.202 million by Metro's five year average demand forecast of 223 000 GTK. Table 4 (column 5) shows the total variable costs for maintenance, operations and overheads costs for the network as a whole. Column 4 shows the *allocated* incremental maintenance, operations and overhead costs to freight.

Table 4: Draft decision annual variable maintenance, operations and overhead costs (\$m 2010 prices)

	(1) <i>Basis</i>	(2) <i>Metro</i>	(3) <i>V/line</i>	(4) <i>Freight</i>	(5) <i>TOTAL</i>
Maintenance	EGTK, ESGTK, TK	14.53	2.63	0.75	17.9
Operations costs	TK	21.94	3.19	0.18	25.3
Regulatory and access administration	Direct		0.04	0.16	0.2
Other overheads	10.2%	3.65	0.59	0.11	4.4
TOTAL variable cost		40.12	6.45	1.20	47.8
Cost per '000 GTK (\$)		7.04	10.21	5.39	

2.4 Asciano's response to draft decision

In response to the draft decision, Asciano indicated that it remained concerned that pricing at the level proposed in the draft decision would not be competitive with road transport.¹⁴ Asciano submits that the \$5.39 per '000 GTK proposed by the Commission remains significantly above current prices paid by Asciano, and questions the ability of network freight users to bear the proposed prices. Asciano indicated that a number of traffics are at risk of moving to road should the access price stay high.

In addition, Asciano submitted that the Commission should consider tariff sculpting options over the term of the access arrangement to minimise potential price shocks to freight users.

Asciano also argues that, while the Commission has considered Metro's cost structures and cost levels in some detail, the Commission should consider the impact of the following points on its cost allocations:

- all Asciano freight services operate outside of Metro peak times and therefore minimal MTM staff costs should be allocated, and

¹⁴ Asciano response to the ESC draft decision on Metro Trains Melbourne rail access arrangement renewal (public submission) p.4.

- freight services receive minimal benefit from additions to network infrastructure.

Commission response

Regarding Asciano's argument about cost allocation, although most Asciano freight services operate outside peak times, based on advice from its technical advisors, the Commission believes that its approach to allocating these costs on the basis of train kilometres gives an appropriate allocation of freight's use of the Metro network.

The Commission also notes Asciano's argument that freight services receive minimal benefits from additions to network infrastructure. However, the Commission points out that the costs attributable to freight in its methodology exclude any capital costs or capital expenditure for augmentation or upgrading of the network and provide for a zero return on existing infrastructure. Moreover, no significant contribution to fixed costs is included in the access price.

Affordability of rail access

Asciano provided some information in relation to its assertion that pricing access at the level proposed by the Commission in the draft decision would not be competitive with road transport but has been unable to provide the critical information that the Commission would require in order to do a rigorous quantitative assessment (that is, to determine the competitive road prices and Asciano's relevant costs).

The Commission is required to determine an efficient price for rail access. Normal regulatory principles require an efficient price to be no less than the incremental costs (for example wear and tear) imposed on the access provider by the relevant traffic and no more than the full economic costs of providing the service to the relevant traffic, both calculated on an efficient cost basis. Pricing between the bounds of incremental cost and full economic cost ensures that prices are cost reflective and free from cross-subsidy.

If access prices were set to recover the full economic costs of the rail network (that is incremental plus fixed costs) the cost of using road transport would be cheaper and many traffics would shift to using road. Given this context, the Commission chose to set the access price for freight services equal to the efficient incremental cost freight traffics impose on the Metro network. Pricing at incremental cost is the lowest price the Commission can adopt within accepted regulatory principles in order to maximise the potential for freight's on-going use of the Metro rail network

Finally the Commission notes that Asciano have argued for tariff sculpting over the term of the access agreement in order to minimise potential price shocks to users. In other words, to phase in the increase in access prices in order to minimise the price shock to users¹⁵. The Commission is constrained in determining a price less than incremental cost.

¹⁵ The Commission understands that Asciano's access prices are transparent to its freight customers and are in effect a direct pass through.

2.5 Metro's response to draft decision

Metro submits that it accepts the current model used by the Commission as being quantitative and impartial for all parties involved.

However, in regards to the calculation of the reference price of \$5.39 per '000 GTK recommended by the Commission in its draft decision, Metro has raised four main issues:¹⁶

1. Operating costs — Metro submits that the Commission has calculated the operating costs from Metro's submitted seven month regulatory accounts to June 2010 and therefore not used the full twelve month costs.
2. Calculation of train kilometres — the calculation of the V/Line train kilometres in the ESC's modelling was disputed,
3. Revenue cap calculation — Metro does not agree with the revenue cap calculations proposed by the ESC.
4. No allowance or contribution for fixed costs.

Each of these issues is addressed in turn below.

2.5.1 *Issue 1: Operating costs*

In relation to Metro's first issue regarding operations costs, Metro argues that in its draft decision, the Commission has determined the total operations costs as \$25.3 million by extracting the operation labour costs of \$20.7 million from regulatory accounts and applying a further 22 per cent (\$4.5 million) for on-costs.¹⁷ These on-costs comprise superannuation, payroll tax and Workcover, totalling 15 per cent, together with other staff-related costs¹⁸ of 7 per cent.

However, Metro has argued that the \$20.7 million costs for operations labour costs is only for a seven month period to 30 June 2010 and not for a full twelve month period. Metro believes this was an inadvertent interpretation error based on Metro only providing regulatory accounts to the Commission for five months to 30 November 2010 for Connex Melbourne Pty Ltd and seven months for Metro.

In response to the draft decision, Metro has clarified the appropriate regulatory accounts and proposed \$33.584 million for operation labour costs as the basis for calculating total operations costs.

¹⁶ Metro's response to the Essential Services Commission's Draft Decision, July 2011 pp.4-6.

¹⁷ Wages and salaries of staff engaged in planning, controlling and signalling trains. These are specifically identified in the Metro regulatory accounts.

¹⁸ These cover FBT, medical, training, uniforms, bonuses, PPE, packaged vehicles, staff amenities, staff recruitment, temporary staff and professional memberships

Commission response

The Commission has reviewed Metro's figures and has noted the error in the interpretation of the regulatory accounts and has accepted the \$33.584 million (\$40.919 million with the inclusion of labour on-costs) as reasonable for the purposes of calculating operating costs. This adds \$0.55 cents to the final 2010/11 price determined at the draft decision stage.

2.5.2 Issue 2: Calculation of train kilometres

The network usage by the various operators was used to establish the link between costs and vehicle characteristics, defined in terms of train kilometres (TK), equivalent gross tonne kilometres (EGTK) and equivalent structures gross tonne kilometres (ESGTK). These statistics were used to allocate the various incremental costs. Train kilometres are used to allocate operations costs and signalling maintenance costs and are also an input to estimating gross tonne-kilometres, EGTK and ESGTK, which are the basis for allocating track and bridge maintenance costs.

In response to the draft decision, Metro submitted that the calculations for percentage usage by freight for TKs, EGTKs and ESGTKs were calculated on the basis of totals which used an estimate of V/Line's annual TKs of 3.019 million (see Table 2). However, Metro submits that the appropriate estimate of V/Line's TKs is 2.591 million.

Commission response

The Commission has reviewed the revised detailed estimates provided by Metro and accepts that Metro's estimate of V/Line TKs is a more accurate estimate.

As a result, the Commission has also reviewed its associated calculations for freight and Metro services to ensure they are all consistent with the assumptions of the Asset Management Plan (AMP).¹⁹

Table 5 shows the revised operating statistics. This table also includes a small allowance for other users of the network such as heritage operators and maintenance trains.

¹⁹ The Metro AMP assumed the 2010 level of traffic throughout the forecast period, with the exception of Metro services being extended to Sunbury. The freight operating statistics used for the allocation of costs have thus been revised to the 2010 actual usage (rather than the usage in the middle of the control period) and the Metro statistics have also been revised to the 2010 actual usage, but including the planned extension of services to Sunbury.

Table 5: Revised operating statistics by service type 2010¹

Operating statistics	Metro	V/Line	Freight	Other	Total	% freight
Train-km (000)	21 429	2 591	170	20	24 210	0.70%
Gross tonne-km (mill)	5 889	552	207	8	6 655	3.11%
EGTKM (mill)	9 295	1 262	417	15	10 989	3.80%
ESGTKM (mill)	28 262	11 806	4,702	150	44 921	10.47%

¹ Metropolitan resources include proposed Sydenham – Sunbury services

At the same time, following further review of the Metro AMP and discussions between the Commission's technical consultants and Metro, the Commission has revised the variable costs associated with bridges downwards by \$0.5 million, reducing the overall total variable maintenance cost downwards from \$17.9 million to \$17.42 million per annum. Table 6 shows the revised allocation of variable infrastructure maintenance costs to freight of \$0.67 million (reduced from \$0.75 million in Table 2), largely driven by the revised freight usage. These revisions result in a net reduction of \$0.02 to the final price compared to that determined in the draft decision.

Table 6: Allocation of variable infrastructure maintenance costs by service type (\$ million 2010) (revised)

	Metro	V/Line	Freight	Other	Total	Basis
Track	12.16	1.65	0.55	0.02	14.37	EGTK
Signals	1.81	0.22	0.01	0.00	2.04	TK
Structures	0.63	0.26	0.10	0.00	1.00	ESGTK
Total	14.59	2.13	0.67	0.02	17.42	

2.5.3 Issue 3: Revenue cap calculation

In its response to the draft decision, Metro submitted that the Commission had calculated the annual average variable costs attributable to freight at \$1.2 million however Metro has argued these were amended in the calculations to deliver an average of only \$1.17 million.

In its draft decision, the ESC calculated the revenue cap based on the following approach:

- setting the access price for year 1 of the regulatory period as \$5.39 '000 GTK (that is, the average annual incremental cost of \$1.20 million divided by the *average GTK* over the 5 year AMP period of 223 000 GTK – see Table 7)
- applying an X factor of 1 per cent to the freight access price for years 2 to 5 of the five year period, and
- calculating the revenue required in each year by multiplying the factored access price by the applicable GTK for each year (taken from the Metro Model 2011 Submission – see Tables 7 and 8).

The resulting total cost of supply averages to \$1.177 million over the 5 year period. When discounted the revenue requirement in present value terms is \$4.889 million as set out in Table 7.

Table 7: Required revenue (draft decision) (\$2010/11)

	2011-12	2012-13	2013-14	2014-15	2015-16	TOTAL
Total annual variable cost for freight (\$M) (see Table 4)						1.20
Access Price (\$'000 GTK)	5.39	<i>(1.20 divided by average GTK of 223 000)</i>				
Apply x-factor of 1%		5.34	5.28	5.23	5.18	
Freight GTK ('000) (se Table 8)	210.0	216.3	222.8	229.4	236.3	223.0
Total cost of supply (\$M)	1.132	1.154	1.177	1.200	1.224	1.177
Discounted cost of supply (\$M)	1.064	1.019	0.976	0.935	0.896	0.978
WACC	6.44%					
Revenue Requirement (\$M)	4.889					

Table 8: Metro's freight volume forecasts (GTKs)

	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	Average
Freight GTK	207 000	209 974	216 273	222 761	229 444	236 328	223 000

Source: Metro 2011 Submission

Commission response

The point of difference between the Commission's calculation in its draft decision and Metro's submission is the extent to which the X factor should impact on the annual revenue requirement.

The Commission's calculations reflect a presumption that the access prices should additionally reflect an annual productivity improvement of at least 1 per cent each year and the revenue requirement has been adjusted downwards accordingly. The Metro submission makes no additional adjustment for productivity other than what may have already been factored into the 5 year AMP.

The Commission has already stated that it is satisfied that Metro's overall costs (quantums) are efficient given the practices and circumstances at present. It is reasonable to expect, however, that a process of continuous improvement will be maintained and that some additional productivity benefits should flow through to freight customers in prices.

Metro's standard access agreement provide for escalation of the access price according to a CPI-X formula, whereby the 'X factor' is the productivity factor approved by the Commission. The discussion of the X factor is taken up again in the discussion of the final decision below in section 2.6.1.

2.5.4 Issue 4: Fixed cost issue

Metro does not agree with the Commission's draft decision with respect to the exclusion of fixed maintenance costs in formulating the reference price. The Commission's draft decision reference price that consists of incremental costs plus a proportion of fixed costs attributable to freight is \$9.26 per '000 GTK. Metro submits that this reference price would not be viable in the current market for freight operators.²⁰

Although the Commission has determined that inspections have no variable component, Metro disagrees with this treatment. Metro believes inspections on the track sections that service freight operations are greater than for those track sections that only carry passengers. Therefore, Metro has requested that the Commission include a 5 per cent allocation to variable costs for inspections.

Commission response

In principle, the Commission agrees that if freight's use of the rail network increased track inspection frequency, and it was an efficient practice, then some adjustment to the incremental costs attributable to freight would be warranted. The Commission has not, however, been provided with any quantitative evidence that supports such an adjustment and, given the cost is minimal, the Commission has chosen not to make any allowance for additional track inspection costs.

However, the Commission has accepted that the fixed cost of maintaining the short branch to Long Island should be included in the cost attributable to freight. As this line is freight-only, then the full costs of the line section (that is, including those costs that do not vary with usage) are incremental to freight and the fixed cost should be recovered from freight users. This inclusion is estimated at \$29 000 per annum. This adds \$0.15 cents to the access price determined by the Commission at the draft decision stage.

2.6 Final decision - revenue requirement and reference price

The Commission is required to determine an efficient price for rail access.

In its draft decision, the Commission chose to set the access price for freight services equal to the efficient incremental cost freight traffics impose on the Metro network. To promote the use of rail, the Commission chose to go as low as possible within accepted regulatory principles in order to maximise the potential for freight's on-going use of the Metro rail system.

In this final decision, the Commission has maintained its approach from the draft decision and determined a freight access price equal to the incremental costs that freight imposes on the Metro network. However, a number of adjustments have been made to the calculation of incremental cost as discussed above.

²⁰ Metro's response to the Essential Services Commission's Draft Decision, July 2011 p.8.

In summary these changes are:

- Incremental maintenance costs — the incremental maintenance costs of \$0.75 million in the draft decision have been reduced to \$0.67 million due to the revision in operating statistics and the revision of bridge-related maintenance costs
- Fixed costs – the Commission has included an allocation for fixed costs of \$29 000 per annum for the freight-only Long Island branch line
- Incremental operations costs for freight services have been adjusted upwards to \$0.29 million (0.70 per cent, as given in Table 5, of the revised total operations cost of \$40.919 million) to reflect the error in the interpretation of the regulatory annual accounts, and
- Overhead costs and an allowance for profit have been included as a 10.2 per cent mark-up on other costs and accordingly these costs have changed in line with movements in other costs.

As a consequence the total average annual incremental cost attributable to freight services has increased from \$1.199 million from the draft decision to \$1.257 million. The final assessment of the incremental costs attributable to freight is set out in Tables 9 and 10 and the Commission determined forecast revenue requirement is presented in Table 11.

Table 9 gives the cost per '000 GTK for the tonnage on which the AMP is based, calculated by dividing the average annual revenue requirement of \$1.26 million by the 2010/11 freight GTK of 207 million, as given in Tables 5 and 8.

Table 9: Average annual incremental maintenance, operations and overhead costs (\$M 2010/11 prices) (revised)

	(1) <i>Basis</i>	(2) <i>Metro</i>	(3) <i>V/line</i>	(4) <i>Freight</i>	(5) <i>Other</i>	(6) <i>TOTAL</i>
Incremental maintenance	EGTK, ESGTK, TK	14.59	2.13	0.67		17.42
Freight fixed maintenance	Direct			0.03		
Incremental operations costs	TK	36.20	4.38	0.29	0.03	40.90
Regulatory and access administration	Direct		0.04	0.16		0.20
Overheads	10.2%			0.12		-
TOTAL cost				1.26		-
Cost/'000 GTK (\$)				6.07		

Table 10 shows how this cost varies for each year of the regulatory period, based on the forecast freight GTK given in Table 8.

The incremental infrastructure maintenance and operations costs increase directly with traffic volume. The fixed infrastructure maintenance costs and the regulatory and access administration costs do not change and overhead costs remain the same percentage (10.2 per cent) of the total fixed and variable costs.

Table 10: Annual freight costs (2010-2016) (\$2010/11)

	<i>2010-11</i>	<i>2011-12</i>	<i>2012-13</i>	<i>2013-14</i>	<i>2014-15</i>	<i>2015-16</i>
Incremental maintenance	0.665	0.675	0.695	0.716	0.737	0.759
Incremental operations costs	0.288	0.292	0.301	0.310	0.319	0.329
Fixed maintenance costs on freight lines	0.029	0.029	0.029	0.029	0.029	0.029
Regulatory and access administration	0.158	0.158	0.158	0.158	0.158	0.158
Corporate overheads	0.116	0.118	0.121	0.124	0.127	0.130
Total freight cost (\$m)	1.257	1.272	1.304	1.336	1.370	1.405

The total freight cost then becomes the annual revenue requirement for each year in the regulatory period (2011/12 to 2015/16).

The present value of the revenue is calculated by discounting at the WACC of 6.44 per cent. The changes in total freight costs increase the aggregate revenue requirement (discounted to 2010/11) from \$4.89 million (Table 7) to \$5.50 million over the period. Table 11 below summarises the revenue requirement.

Table 11: Metro forecast revenue requirements (2011/12-2015/16 regulatory period) (\$2010/11) (final decision)

	<i>2011-12</i>	<i>2012-13</i>	<i>2013-14</i>	<i>2011-15</i>	<i>2015-16</i>	<i>Total</i>
Regulatory asset base	0	0	0	0	0	
WACC	6.44%	6.44%	6.44%	6.44%	6.44%	
Return on assets	0	0	0	0	0	
Regulatory depreciation	0	0	0	0	0	
Operations, maintenance & overhead costs (\$m)	1.272	1.304	1.336	1.370	1.405	
Total cost of supply	1.272	1.304	1.336	1.370	1.405	
Discounted cost of supply (\$m) at 6.44% (WACC)	1.195	1.151	1.108	1.068	1.029	5.500
Discounted revenue requirement (\$m)						5.500

2.6.1 Access price

An access price of \$6.00 per '000 GTK (\$2010/11) held constant in real terms would produce the equivalent forecast revenue requirement over the five-year period of \$5.50 million, as shown in Table 12 below. Applying an X factor of 1 per cent per annum to the access price will result in a 2 per cent reduction in the aggregate revenue requirement measured in present value terms (to \$5.39 million).

The access price of \$6.00 per '000 GTK in Table 12 is slightly less than the average cost of \$6.07 per '000 GTK in Table 9. This is due to the former reflecting changes in variable cost and GTK over the forecast period, as shown in Table 10, whereas the \$6.07 per '000 GTK is based on the average annual cost over the AMP period and the 2010/11 task (noting the 5 year AMP was based on the 2010/11 task).

The X factor discount of 1 per cent per annum has been applied from 2010/11 rather than the first year of the next regulatory period (2011/12). The Commission believes this is appropriate given the analysis was based on historical costs rather than forecast or budgeted costs.

The Commission was unable to verify Asciano's assertion that the proposed increase in rail access prices posed a risk that a number of existing rail freight traffics would move to road. Pricing at incremental cost is the lowest price the Commission can adopt within accepted regulatory principles in order to maximise the potential for freight's on-going use of the Metro rail network.

Table 12: Reference price for freight services (\$ 2010/11)

	2010/11	2011/12	2012/13	2013/14	2014/15	2015/ 16	Total
Freight forecast GTK	207	210	216	223	229	236	
Access price (\$/000 GTK) (\$2010/11)	6.00	6.00	6.00	6.00	6.00	6.00	
Revenue(\$ million)		1.260	1.298	1.337	1.377	1.419	
Discount factor		0.94	0.88	0.83	0.78	0.73	
Discounted revenue (\$ million)		1.184	1.146	1.109	1.073	1.038	5.50
Adjusted Access price path ¹ (\$/000 GTK) (\$2010/11)	6.00	5.94 ²	5.88	5.82	5.77	5.71	
Revenue(\$ million)		1.248	1.272	1.297	1.323	1.349	
Discounted revenue (\$ million)		1.172	1.123	1.076	1.031	0.987	5.39

1. Price path is discounted by an X factor of 1 per cent.

2. As per the variation for inflation clause (clause 3.1 of the access arrangement and clause 4.2 of the access agreement) this price becomes \$6.14 once adjusted for inflation.

The non-price matters of Metro's access arrangement include certain information that Metro must make available to persons seeking access, such as information regarding train paths, various protocols and procedures regarding the governance and provision of access and an access agreement, which is a template contract that provides the basis for agreeing the contractual terms and conditions of access between Metro and a freight operator.

The Commission's draft decision required a number of amendments to Metro's proposed access arrangement to address non-price issues. These amendments related to Metro's compliance with the Network Management Rules and amendments to Metro's standard access agreement.

This chapter outlines Metro's and stakeholder responses to the draft decision, and provides the Commission's final decision.

This chapter is organised into four main sections:

- Metro's compliance with the Network Management Rules
- access agreement amendments
- issues on which further comments were sought by the Commission in its draft decision, and
- additional revisions proposed by Metro — relating to operating protocols and regulatory accounts.

3.1 Network Management Rules

The Network Management Rules provide protocols for how access to the network will be managed by Metro,²¹ such as protocols for managing the network and operational conflicts, communication protocols between rail safety workers (any person employed or engaged to carry out rail safety work, as defined by the *Rail Safety Act 2006*, which includes train drivers, signallers, track managers, rolling stock engineers, etc), rolling stock interface standards, documentation of safe working systems, and a protocol for addressing complaints.

The Network Management Rules are intended to ensure that the network management practices are not used to hinder third party access or discriminate

²¹ Section 38X(5)(d) of the Rail Management Act (RMA) requires an access arrangement to be consistent with the Network Management Rules. The Network Management Rules were established by the Commission in 2006 under section 38U of the RMA when the Victorian Access Regime was introduced in 2006.

against third party network users, thereby distorting competition between above rail freight operators.

Commission's draft decision

The Commission's draft decision was that Metro's proposed access arrangement was consistent with all of the Commission Instruments except the Network Management Rules. In relation to the Network Management Rules, the Commission's draft decision required Metro to:

- (i) submit a protocol relating to the clearing of network blockages and failed trains (as is required under section 4.4 of the Network Management Rules);
- (ii) submit a protocol for the management of certain activities on the rail network as is required under section 4.7 of the Network Management Rules; and
- (iii) amend the Matrix for Managing Operational Conflict (the Matrix) to be consistent with section 4.3(c) of the Network Management Rules. The purpose of the Matrix is to set out the process for managing prioritisation of operational conflicts between trains.

Metro's response to the draft decision on the above issues, and the Commission's final decision, are outlined below.

(i) Clearing of network blockages and failed trains

The Network Management Rules (clause 4.4) require Metro to prepare and maintain protocols for giving directions or taking action for the purpose of clearing network blockages and failed trains or rolling stock.

Metro's response to the draft decision

Metro has amended its proposed Train Operating Protocol to insert a clause (clause 6.5) dealing with the clearing of network blockages and failed trains. Clause 6.5 states that all response and recovery activity is to be conducted in accordance with 'The Victorian Rules & Operating Procedures' (1994 as amended).

Commission's final decision

The Commission requested from Metro a copy of the document referred to in clause 6.5, and notes that the document provided by Metro was titled 'Book of Rules and Operating Procedures'.

The Commission has reviewed Metro's proposed amendment and considers that Metro has satisfied the requirement to include in its access agreement protocols for giving directions or taking action for the purpose of clearing network blockages and failed trains or rolling stock. However, for accuracy and clarity, clause 6.5 should be amended to refer to the 'Book of Rules and Operating Procedures'.

The Commission's final decision is that Metro's proposed access arrangement is consistent with rule 4.4 of the Network Management Rules: however, the first paragraph of clause 6.5 be amended as follows:

The Metro Trains Emergency & Crisis Management Plan is applied for all network disruptions and all response and recovery activity is conducted in accordance with ~~The Victorian Rules & Operating Procedures~~ the Book of Rules and Operating Procedures [1994 as amended].

(ii) Protocols for the management of certain activities on the rail network

The Network Management Rules (clause 4.7(b)(i)) requires Metro to prepare and maintain procedures for the following matters:

- (A) *the management of historic trains, special loadings or the carriage of certain loads on the rail network, including dangerous goods or hazardous materials*
- (B) *the use of the rail network of the access provider for military or defence purposes, and*
- (C) *the use of a rail network of the access provider for safety or testing or driver training or other similar purposes.*

Metro's response to the draft decision

Metro has amended its proposed Master Working Timetable Addenda to include a section dealing with use of the metropolitan rail network for transporting dangerous or hazardous goods. The Addenda requires a train operator to ensure that the proper documentation accompanies any dangerous goods consignment. This documentation must be faxed to Metro Network Planning Section, Metrol and the destination location, before the original papers are provided with the consignment to the train crew.

Metro stated that all historic trains are operated by V/line, who is the accredited rail operator to Metro, and that V/line has procedures for acting as the train operator for the historical operators such as Steamrail.²²

In regard to the use of the network for military or defence purposes, Metro stated that, under its Franchise Agreement, it is required to submit an Emergency Management Plan (EMP) to the Department of Transport that satisfies the legislative requirements of the *Rail Safety Act*, the *Terrorism (Community Protection) Act* and the *Emergency Management Manual Victoria*.²³ Metro stated that its EMP provides that, in the event of a crisis situation (for example armed intrusion), it must act as a support agency and conduct all activities at the direction of the lead control agency.

²² Metro response to the ESC's queries dated 26 July 2011, p.1.

²³ Metro response to the ESC's queries dated 26 July 2011, p.2.

Lastly, Metro submitted that driver training is carried out as on-the-job training during train runs, and that access to the network to conduct safety/testing regimes is managed through its Management of Change Process policy.²⁴ The Management of Change Process, which Metro has submitted to the Commission, sets out the key steps to be taken to ensure that changes are managed appropriately and in compliance with Victorian Rail Safety legislation.

Commission's final decision

The Commission has reviewed Metro's submission and considers that Metro has included and referred to in its access arrangement the relevant policies and protocols to address clause 4.7 of the Network Management Rules (management of certain activities on the rail network).

The Commission's final decision is that Metro's proposed access arrangement is consistent with rule 4.7 of the Network Management Rules.

(iii) Protocols for managing operational conflicts

The Network Management Rules (section 4.3(c)) requires an access provider to:

- (i) First, give priority to a regular passenger train service, and to use all reasonable endeavours to facilitate that:
 - o if it is running on or ahead of time, that it exits the relevant line on time and
 - o if it is running late, that it makes up time.
- (ii) Second, having complied with the first, in respect of any freight train service, to use all reasonable endeavours to facilitate that:
 - o if it is running on or ahead of time, that it exits the relevant line on time and
 - o if it is running late, that it makes up time.

Metro's response to the draft decision

Metro has amended its Train Operating Protocol, specifically the operational control principles (section 6.4), to reflect the priorities in section 4.3(c) of the Network Management Rules.

Commission's final decision

The Commission has reviewed Metro's proposed amendment to its Train Operating Protocol and considers that the operational control principles in section 6.4 of the protocol now reflect the requirements of section 4.3(c) of the Network Management Rules. The Commission's final decision is that Metro's proposed access arrangement is consistent with section 4.3(c) (protocols for managing operational conflicts) of the Network Management Rules.

²⁴ Ibid.

The Commission's final decision is that Metro's proposed access arrangement is consistent with rule 4.3 of the Network Management Rules.

3.2 Access agreement amendments

The purpose of an access *agreement* is to provide a basis for agreeing the contractual terms and conditions of access once they have been negotiated through the access *arrangement* process.

An access agreement, once signed by the access provider (Metro) and an access seeker (for example, a freight operator), becomes the binding terms and conditions that govern how access is granted to the rail network.²⁵

Commission's draft decision

In its draft decision, the Commission considered Metro's access agreement in its entirety and required a number of amendments be made to ensure it was more balanced in the rights and responsibilities it grants to operators and the access provider.

The Commission required 26 amendments to be made to Metro's access agreement and sought further comments on a number of other issues.

Metro's response to the draft decision

In response to the draft decision, Metro re-submitted a revised standard access agreement which sought to address many of the Commission's recommendations.

Commission's final decision

The Commission has examined Metro's revised marked up standard access agreement (at Appendix C) and notes that Metro has accepted many of the Commission's draft decision recommendations. Table 13 (at the end of this chapter) summarises the amendments required by the draft decision, Metro's response to the draft decision and the Commission's final decision.

Metro's revisions, stakeholder responses and the Commission's final decision on the access agreement amendments are discussed below.

Clause 1.1 – Definitions

Section 1.1 of the standard access agreement outlines a number of definitions that are used throughout the document. In its draft decision, the Commission's view

²⁵ It should be noted that both access seeker and access provider are free to negotiate outside the standard access agreement and reach a different access agreement (including a different access price) providing that both parties agree. However, where such negotiations fail, the standard access agreement becomes the fall back agreement.

was that the definition of incremental costs should be amended to ensure that costs incurred are efficient and reasonable and reflect the service being provided.

Metro's response to the draft decision

Metro amended the definition to read that:

Incremental Costs means additional costs that are reasonably incurred by the Access Provider as a direct result of providing access to the Operator, where these costs are over and above the costs that have been taken into account in setting the Access Charge. Without limitation, Incremental Costs may be one-off costs incurred by the Access Provider in providing a requested path to the Operator.

For the avoidance of doubt, there are no such additional costs as at the commencement of this Agreement.

Commission's final decision

On further review, the Commission believes Metro's amendment to the definition for incremental costs and considers it to be acceptable.

The Commission's final decision is that it accepts Metro's amendment to the definition of incremental costs in clause 1.1.

Clause 3.2 — *Unscheduled train paths*

Clause 3.2(c) establishes a series of network priority rules for the allocation of unscheduled train paths. In Metro's proposed access agreement, this clause provided that priority was given to *any trains* operated by the access provider.

Asciano has argued that priority should be given to only *passenger trains* operated by Metro, as opposed to *any train* operated by Metro regardless of whether it is a passenger or non-passenger train. Asciano has argued that, while Metro does not operate freight trains and compete in the above rail market, Metro does operate various non-passenger trains such as empty train movements, repair trains and works trains. These trains typically operate within the same non-peak time windows as freight trains and prioritising these trains impacts on freight services.²⁶ Asciano submitted that the intent of clause 3.2(c) is that passenger trains receive priority; however, the clause as drafted provides priority to all Metro trains.

In its draft decision, the Commission required that the clause be amended to give priority to passenger trains, rather than all trains operated by Metro.

Metro's response to the draft decision

Metro has amended clause 3.2(c) to read that priority be given 'first, to the Access Provider for any train movements associated with passenger trains.'

²⁶ Asciano submission to the draft decision, p.6.

Commission's final decision

The Commission notes that Metro's drafting of clause 3.2(c) provides for priority to be given not only to passenger trains, but also to train movements associated with passenger trains, and therefore only partially gives effect to the requirement of the draft decision. However, while the Commission notes the concerns of freight operators, it considers that Metro's response to the draft decision is appropriate.

The Commission's view is that giving priority to train movements associated with passenger trains (such as the movement of empty trains and repair and works trains associated with the provision of passenger services) is necessary for the provision of passenger transport services. The Commission considers this is consistent with the general principle of passenger priority, which is enshrined in law. Therefore, the Commission accepts that it is reasonable for priority to be given to train movements associated with passenger trains for unscheduled train paths under clause 3.2(c).

The Commission's final decision is that it accepts Metro's amendment to clause 3.2(c).

Clause 3.3 – Ancillary movements

Ancillary movements refer to train movements that are not part of an ordinary train path, but are necessary for the ordinary train path to operate. Ancillary movements would normally apply to the movement of empty trains and engines for operative or maintenance purposes to workshops, locomotive depots and fuel points.

In its draft decision, the Commission required Metro to amend clause 3.3(a) such that ancillary movements be allowed only when they are necessary or reasonably required. In addition, the Commission required that clause 3.3(b) be amended to provide that the conditions for when ancillary movements are required be set out in the relevant procedures and protocols, rather than being set from time to time by Metro.

Metro's response to the draft decision

Metro has amended clause 3.3(a) such that ancillary movements are allowed when they are necessary or reasonably required. In addition, clause 3.3(b) has been amended to provide that the conditions for ancillary movements are set out in the procedures and protocols listed in clause 11.1.

Commission's final decision

The Commission has reviewed Metro's amendments and considers them to be acceptable.

The Commission's final decision is that it accepts Metro's amendments to clause 3.3.

Clause 3.5 — Alternative train path

In its draft decision, for the purposes of clarity, the Commission required that clause 3.5 of Metro's standard access agreement should be amended to require

that where an operator's train path is varied according to clause 3.5, Metro will use reasonable endeavours to make a similar alternative train path available to the operator.

Metro's response to the draft decision

Metro has amended clause 3.5 to include a requirement that where a train path is varied the access provider will use reasonable endeavours to make alternative train paths available to the operator.

Commission's final decision

The Commission has reviewed Metro's amendment and considers it to be acceptable.

The Commission's final decision is that it accepts Metro's amendment to clause 3.5.

Clause 4.4 (previously clause 4.3) – Incremental costs

Incremental costs are defined in the access agreement as additional costs that are reasonably incurred by the access provider as a direct result of providing access to a freight operator where these costs are over and above the costs that have been taken into account in setting the access charge.

In its draft decision, the Commission required Metro to explain to the operator the nature of incremental costs that may be incurred and the method of calculation for these costs.

The Commission also noted that item (a) of the proposed incremental costs clause provides that incremental costs are allocated between the operator and any other third party operator (defined to exclude Metro) where appropriate. The Commission stated in the draft decision that Metro, in its capacity as above rail passenger operator on the metropolitan network, should also be subject to the allocation of incremental costs where it is appropriate.

Therefore, the Commission required item (a) of the incremental costs clause to be amended to provide that where incremental costs are attributable to the operator and any other *users of the network*, the access provider will make a reasonable allocation of those incremental costs as between the operator and the other *users of the network*.

Metro's response to the draft decision

Metro inserted clauses 4.4(c) and 4.4(d) to require Metro to explain to the operator the nature of incremental costs that may be incurred and the method of calculation for these costs.

However, Metro did not accept the Commission's draft decision regarding item (a) of the incremental costs clause, arguing that:

If passenger trains are unable to use a section of track, the requirements to enable it to be used would be inserted into the Annual Works Plan and be completed as part of the maintenance and repair. The costs would not be

allocated to any other operator although they may gain benefit. Therefore, if the operator requires upgrades to existing infrastructure to enable them to use a section of track that is already being used by passenger trains then Metro should not be allocated any of the incremental costs.²⁷

Commission's final decision

The Commission has reviewed Metro's inclusion of clauses 4.4(c) and 4.4(d) to address the Commission's concerns regarding the nature of incremental costs and the method of calculation for these costs and accepts these amendments.

However, while the Commission accepts that incremental costs should not be allocated to Metro if the costs are not attributable (in whole or in part) to Metro, the Commission does not accept the argument that incremental costs should never be allocated to Metro. For example, if both Metro and an operator were to increase their use of a particular section of track, additional equipment or staffing may be required that had not been inserted into the Annual Works Plan. In such a case, the additional cost should be apportioned appropriately between Metro and the operator.

The Commission is of the view that any user (including Metro) should be allocated a proportion of any incremental costs that are attributable to that user. As a result, the Commission requires that clause 4.4 should refer to '*users of the network*' so as not to exclude Metro from the operation of this clause, and therefore preventing Metro from being allocated incremental costs that are wholly or partially attributed to Metro.

Of course, where additional expenditure has been required to accommodate Metro's needs, and has been included in the Annual Works Plan, any further expenditure would be attributable to the operator(s) only, and thus would not be allocated to Metro.

The Commission's final decision is that it accepts Metro's insertion of clauses 4.4(c) and 4.4(d), however clause 4.4(a) be amended as follows:

The Operator must pay any Incremental Costs to the Access Provider. Where any Incremental Costs are attributable to both the Operator and any ~~Third Party Operator~~ other users of the Network, the Access Provider will make a reasonable allocation of those Incremental Costs as between the Operator and the ~~Third Party Operator~~ other users of the Network (based on a causal allocator).

Clause 4.6 (previously clause 4.5) – Objection to invoiced amount

Clause 4.6 provides for the case where an amendment to an incorrect invoiced amount needs to occur. Previously, the onus was on the operator to make this amendment.

²⁷ Metro submission to the draft decision, p.11.

Asciano argued this to be a confusing condition, given that invoices are issued by the access provider, and therefore Asciano believes it is more practical and appropriate that the *access provider* be required to make any necessary adjustment to an invoice.²⁸

Metro's response to the draft decision

Metro has amended clause 4.6 such that the access provider may set off invoiced amounts when there is an objection.

Commission's final decision

The Commission has reviewed Metro's amendment and considers it to be acceptable.

The Commission's final decision is that it accepts Metro's amendment to clause 4.6.

Clause 4.8 (previously clause 4.7) – Set off

Clause 4.8 refers to the right to set off amounts payable between the operator and the access provider. Previously, only the access provider had the right to set off. However, the Commission considered it fair and reasonable that both parties should have this right.

Metro's response to the draft decision

Metro has amended clause 4.8 such that both parties may set off amounts payable. This clause has been significantly reworded and now reads:

4.8 Set off

- (a) *A party (the first party) may set off against any amount due and payable under this Agreement by the first party to the other party, any amount due and payable under this Agreement by the other party to the first party. The first party must notify the other party in writing if it exercises this right.*

Commission's final decision

The Commission has reviewed Metro's amendment and considers it to be acceptable.

The Commission's final decision is that it accepts Metro's amendment to clause 4.8.

Clause 4.10 (previously clause 4.9) – Performance bond

In its proposed access agreement, Metro included a requirement for a performance bond (security deposit). The purpose of the performance bond is to offer a level of protection against the risk arising from potentially financially unstable freight operators accessing the network.

²⁸ Asciano submission to the issues paper, p.16.

In its submission to the issues paper, Asciano argued that it is appropriate to require a performance bond in some circumstances (that is, where the operator is a new entrant or has a low credit rating, or has failed to make payments in the past and is seen as a risk); however, Asciano noted that it does not fall under any of these categories. Therefore, Asciano argued it should not be required to pay a performance bond. Moreover, Asciano argued the requirement of a performance bond acts a disincentive for above rail operators to operate on the Metropolitan network.

In addition, Asciano argued that the performance bond requirement was unacceptable because item (h) of the proposed performance bond clause allows Metro to make a demand under the performance bond regardless of whether the parties are in dispute or the circumstance leading to the demand are the subject of court or other proceedings.

In its draft decision, the Commission considered that it is appropriate for the standard access agreement to contain provisions for a performance bond to allow the access provider to determine if the operator seeking access has the financial ability to make payments under the access agreement. The Commission was of the understanding that if an operator has the financial ability, then the operator will not be required to pay a performance bond – that is, the performance bond clause would be removed in the negotiated access agreement. Therefore, the Commission considered that Metro’s proposed requirements in relation to the performance bond were appropriate.

Response to the draft decision

In response to the draft decision, Asciano further argued that Metro’s current access agreement does not support the Commission’s interpretation, and requested that the Commission obtain legal advice before making a final decision. Asciano’s reading of the clause is that all operators are required to pay a bond regardless of their financial standing or credit history with the track provider.²⁹

Commission’s final decision

While the Commission remains of the view that an operator with appropriate financial stability would be able to negotiate the removal of the performance bond requirements under clause 4.10, it agrees that on the face of the clause, all operators are required to pay a bond regardless of their financial standing.

Although Metro may agree not to insist on the clause if the operator in question is financially sound, there is nothing in the access arrangement requiring it to do so. Should a dispute arise, the Commission must not make a dispute resolution decision that is inconsistent with the binding access arrangement (which would include the terms of the draft access agreement).³⁰ Hence, the Commission believes Metro should only require a performance bond in circumstances where there is doubt about the ability of the operator to pay, and as such requires that clause 4.10 be amended to reflect this intent.

²⁹ Asciano submission to the draft decision, p.7.

³⁰ Section 38ZZD of the Rail Management Act.

The Commission also notes paragraph 4.3(d) of the Train Path Request Process and Protocol, which allows Metro to reject an application for access if:

the Access Operator does not have the necessary financial capacity to meet its financial obligations to the Access Provider under the Access Agreement and the financial obligations it owes to any other persons (including, but not limited to, excesses under insurance policies).

This provision is consistent with the negotiation guidelines developed by the Commission.

The Commission is of the view that while this provides some protection to Metro in the case where a new applicant may not have a sound financial reputation, it is preferable to have a standard defined in the arrangement so that access seekers can more estimate their likely liabilities with greater certainty, and so that the performance bond does not become a barrier to entry.

Accordingly, the Commission is of the view that Metro should be entitled to require a performance bond in certain circumstances, and that the maximum amount of such a bond should be capped to an amount specified in the access arrangement.

The Commission's final decision is that clause 4.10 should be amended to include the following clarification:

For the avoidance of doubt, this clause 4.10 only applies to an Operator who does not have an Acceptable Credit Rating, or who has defaulted in payment of any monies owed by it to the Access Provider under this Agreement and has not remedied that default before the expiry of seven (7) days.

The Commission's final decision is that clause 4.10(a) should be amended as follows:

(a) ~~The operator must, on or before the Effective Date~~ If the Operator at any time does not have or ceases to have an Acceptable Credit Rating, or has defaulted in payment of any monies owed by it to the Access Provider under this Agreement and has not remedied that default before the expiry of seven (7) days, the Access Provider may issue a notice to the Operator requesting that the Operator procure the issue to the Access Provider of a Performance Bond within seven days of receiving the notice which:

- (i) is issued by an Issuer with a Required Rating and approved by the Access Provider (which approval must not be unreasonably withheld);***
- (ii) has a face amount which is no less than the Performance Bond Amount;***
- (iii) expires no earlier than the second anniversary of the Effective Date date of issue to the Access Provider; and***
- (iv) is payable at an office of the Issuer in Melbourne.***

The Commission's final decision is that clause 1.1 should be amended to include the following definitions:

Acceptable Credit Rating means a minimum long term credit rating of BBB from Standard & Poor's or Baa2 from Moody's.

Trigger Date means the date on which a Performance Bond provided under clause 4.9 expires.

The Commission's final decision is that clause 1.1 should be amended to replace the definitions of CPI Multiplier and Performance Bond Amount with the following:

CPI Multiplier between any two times means:

- (a) the CPI for most recent March Quarter at the more recent time, divided by,***
- (b) the CPI for the most recent March Quarter at the less recent time.***

Performance Bond Amount means \$[insert], multiplied by the CPI Multiplier between the date on which the relevant Performance Bond is provided and the Effective Date.

The Commission's final decision is that clause 4.2(a) should be amended as follows:

On and from 1 July each Financial Year (commencing on 1 July 2011), each dollar figure component of the Access Charge set out in Schedule 1 will be varied in accordance with the following formula:

$$A_n = A_{n-1} \times \text{CPI Multiplier} \times (1-X)$$

where,

A_n = The relevant element of the Access Charge to apply from 1 July of the Financial Year 'n' (commencing on 1 July TBC).

A_{n-1} = The relevant element of the Access Charge that applied from 1 July of the Financial Year 'n-1'

X = The "x factor = 1%" as approved by the ESC for the Reference Service.

CPI = The CPI Multiplier between the date the Access Charge is varied and the date one year before that date.

The Commission's final decision is that the access arrangement should specify an upper limit on performance bond amounts as follows:

For access seekers that have an Acceptable Credit Rating, as defined in the standard Access Agreement, the maximum Performance Bond Amount is four weeks' access charges. This maximum amount is consistent with the level used by ARTC in its approved access undertaking.

For access seekers that do not have an Acceptable Credit Rating, as defined in the standard Access Agreement, the Performance Bond Amount is to be determined by Metro after having regard to the risk level and frequency of access requested by the Operator, but must be no more than \$500,000.

Clause 5.4 — Variation or surrender due to operator breach

Clause 5.4(a) of the proposed access agreement concerns the circumstances under which the access provider can require an operator to vary or surrender a train path. The operator may be required to surrender a train path if the operator breaches a relevant law or standard, has its accreditation suspended or cancelled, or fails to comply with operating procedures or protocols. In its draft decision, the Commission was of the view that, given the ability of the access provider to vary or surrender a train path, it is not onerous to also require Metro to act reasonably and take into account all relevant circumstances. As such, in its draft decision, the Commission required Metro to amend the access agreement to include a requirement in clause 5.4(a) that the access provider act reasonably and take into account all relevant circumstances.

The Commission also required that clause 5.4 should be amended to provide that only a material breach or failure to comply may result in the variation or surrender of a train path. This would provide that train paths would not be subject to variation or surrender for mere technical breaches of laws, standards or other requirements, where the relevant breach is not material

Metro's response to the draft decision

Metro has included a requirement to act reasonably and take into account all relevant circumstances in clause 5.4(a). In relation to clarifying material versus non-material breaches, through consultation with the Commission, Metro explained that it is not able to list in its access agreement all the instances whereby a non-material breach will justify a variation or surrender of a train path.

Commission's final decision

Metro has amended clause 5.4(a) to require Metro to act reasonably, taking into account *all relevant circumstances* and after consultation with relevant authorities (if required). The Commission is of the view that this amendment is sufficient to address the Commission's concern that minor technical breaches should not result in the variation or surrender of the train paths (because the technical nature of the

breach would, presumably, be a relevant matter that the access provider should take into account).

The Commission’s final decision is that it accepts Metro’s amendment to clause 5.4(a).

Clause 5.5(a) — Variation or surrender due to capacity use issues

Clause 5.5(a) requires Metro to provide freight operators with not less than 30 days notice of any change to scheduled and unscheduled train paths. As the power of Metro to require variation or surrender of a train path under this clause is discretionary, the Commission’s draft decision required Metro to amend clause 5.5(a) such that variations ‘may’ be required, rather than ‘must’, to clarify how the clause should be read.

Metro’s response to the draft decision

Metro has amended its access agreement to read that variations ‘may’ be required.

Commission’s final decision

The Commission has reviewed Metro’s amendment and considers it to be acceptable.

The Commission’s final decision is that it accepts Metro’s amendment to clause 5.5(a).

Clause 5.6 – Temporary variations by the access provider

In response to the issues paper, Asciano argued that temporary variations to train paths should be ‘to the extent necessary’ to effect repairs and maintain and upgrade the network. Asciano suggested that this wording is required to minimise disruption to train operators.³¹

In addition, Asciano argued that in order to avoid any communication issues, clause 5.6(d) should require the access provider to ‘provide reasonable notice to affected rail operators.’ It stated that this requirement would provide information to operators and end users planning operations and production.³²

The Commission agreed with Asciano, and its draft decision was that both clauses be amended as suggested by Asciano.

Metro’s response to the draft decision

Metro has amended its access agreement to address the Commission’s concerns.

Commission’s final decision

The Commission has reviewed Metro’s amendment and considers it to be acceptable.

³¹ Asciano submission to Issues Paper, p.18.

³² Asciano submission to Issues Paper, p.19.

The Commission's final decision is that it accepts Metro's amendment to clause 5.6.

Clause 6.4 – Communication responsibilities

In its draft decision, the Commission was of the view that, in line with similar amendments designed to improve communication and transparency between the operator and access provider, clause 6.4 should be amended such that the access provider will notify the operator of any variations to the Metro website which directly relate to protocols to be followed, or other obligations on the operator.

Metro's response to the draft decision

Metro has amended its access agreement to address the Commission's draft decision.

Commission's final decision

The Commission has reviewed Metro's amendment and considers it to be acceptable.

The Commission's final decision is that it accepts Metro's amendment to clause 6.4.

Clauses 7.2 and 7.3 – Axle weight and track speeds

In its draft decision, the Commission required that clauses 7.2 (relating to axle weight) and 7.3 (relating to track speed) of the access agreement be amended to require the access provider to use reasonable endeavours to consult with the operator about any proposed change to the maximum axle weights or track speeds, in addition to notifying the operator of any such changes.

Metro's response to the draft decision

Metro has amended the access agreement by including additional clauses (7.2(b) and 7.3(b)) to provide that it will use reasonable endeavours to consult where practical with the freight operator about proposed changes to maximum axle weights and track speeds.

Commission's final decision

The Commission has reviewed Metro's amendment and considers it to be acceptable.

The Commission's final decision is that it accepts Metro's amendments to clauses 7.2 and 7.3.

Clause 12.3 – Dealing with incidents

Clause 12.3(d) of Metro's access agreement addresses the issue of public comment by the operator when an incident occurs on the network. Metro's initial

drafting of the clause required the operator to get *written* approval from Metro before making any public comment concerning an incident.

In its draft decision, the Commission required clause 12.3(d) of Metro's access agreement be amended to remove this requirement, and instead provide that where the operator is required by ASX listing rules to disclose information about an incident, the operator must use reasonable endeavours to consult with the access provider as to the form and content of the comment prior to making any public disclosure.

Metro's response to the draft decision

Metro has rewritten clause 12.3(d) to read:

Where the Operator is required by ASX listing rules to disclose information about an Incident, the Operator must consult with the Access Provider as to the form and content of the comment prior to making any public disclosure.

Commission's final decision

The Commission has reviewed and further considered Metro's amendment and considers it to be acceptable.

The Commission's final decision is that it accepts Metro's amendment to clause 12.3(d).

Clause 13.1(c) – Environment

Clause 13.1(c) concerns the situation where compliance by an operator with an environmental law results in incremental costs that should reasonably be shared amongst all users of the network. This clause allows the operator to claim a contribution from other users.

In its draft decision, the Commission was of the view that if the costs incurred by one operator complying with an environmental law or standard have flow on benefits to other operators, then the access provider should be required to allocate those costs amongst the other users of the network, rather than the operator having to recover the costs from other operators.

Metro's response to the draft decision

Metro has responded to the draft decision by amending clause 13.1(c) and including the following wording:

costs will be allocated between those users in accordance with clause 4.4.

Clause 4.4 relates to the allocation of incremental costs between users of the network. This clause has been referred to in clause 13.1 to reflect that environmental costs will be allocated in the same manner as other incremental costs.

Commission's final decision

Providing clause 4.4 is amended as per the Commission's requirements above, then the Commission considers Metro's proposed amendment to clause 13.1 to be acceptable.

The Commission's final decision is that it accepts Metro's amendment to clause 13.1(c), subject to the amendment of clause 4.4 as required above.

Clause 14.1 and 14.2 – Indemnity and release

Clauses 14.1 and 14.2 provide mutual indemnities in relation to damage sustained by one party to the extent that the damage was caused or contributed to by a breach of the agreement by the other party, or a negligent act or omission of the other party. The clauses, as initially proposed, provided that the operator 'indemnifies and releases' the access provider against any claim, loss, liability, cost and expense that may be incurred (and vice-versa).

In its draft decision, the Commission's view was that clauses 14.1 and 14.2 appear unclear and should be amended to clarify that mutual *indemnity* is granted in relation to damage sustained by one party to the extent that the damage was caused or contributed to by a breach of this agreement by the other party or a negligent act or omission of the other party. That is, that the operator *indemnifies* the access provider against any claim, loss, liability, cost and expense that may be incurred (and vice-versa).

Metro's response to the draft decision

Metro has amended clauses 14.1 and 14.2 to reflect the Commission's recommendations.

Commission's final decision

The Commission has reviewed Metro's amendments and considers them to be acceptable.

The Commission's final decision is that it accepts Metro's amendments to clauses 14.1 and 14.2.

Clause 14.3(b)(ii) — Exclusion of indirect or consequential loss

Clause 14.3 of Metro's proposed access agreement relates to indirect or consequential loss. It states that neither the access provider nor the operator is liable to the other in respect of any indirect or consequential loss, with 'indirect or consequential loss' being defined to mean:

economic loss, consequential loss, loss of profits, loss of business opportunity, payment of liquidated sums, penalties or damages under any agreement (other than this Agreement).

However, clause 14.3(b) of Metro's proposed access agreement provided that the following losses do not constitute indirect or consequential loss (and therefore, may be recovered by a party in the event of breach):

- (i) amounts payable under clause 14.5 (TAC premium) and 14.6 (delay payment indemnity)
- (ii) reduction of access revenue receivable by the access provider from a third party operator, and
- (iii) property damage or losses arising from third party claims in respect of property damage, personal injury, nervous shock or death.

Item (ii) on this list introduced an additional carve out from indirect and consequential losses that is normally included as a consequential loss (and therefore excluded from recovery).

In its draft decision, the Commission stated that it was of the view that the additional carve out was unbalanced because it provided that only one party (the access provider) may recover lost revenue. Any exclusion of consequential loss should apply equally to both parties to the agreement.

Accordingly, the Commission required item (ii) to be removed from clause 14.3(b) of Metro's access agreement given the unbalanced nature of the carve out, and that loss of revenue is ordinarily considered an indirect or consequential loss and not customarily excluded in this manner.

Metro's response to the draft decision

Metro has accepted the Commission's draft decision and removed the additional carve out in clause 14.3(b).

Commission's final decision

The Commission has reviewed Metro's amendment and considers it to be acceptable.

The Commission's final decision is that it accepts Metro's amendment to clause 14.3(b).

Clause 14.4 – Insurance

In its draft decision, the Commission's view was that the access provider need not approve the insurer used by the operator, given the requirement that the insurer be reputable and solvent.

The Commission recommended that the standard access agreement be amended such that insurance need only be effected with a reputable and solvent insurer – in other words, deleting the words 'approved by the access provider' in clause 14.4(b).

Metro's response to the draft decision

Metro has amended clause 14.4 to remove the requirement for the insurer to be approved by the access provider.

Commission's final decision

The Commission has reviewed Metro's amendment and considers it to be acceptable.

The Commission's final decision is that it accepts Metro's amendment to clause 14.4.

Clause 14.7 – Exclusion of indirect or consequential loss

In its draft decision, the Commission was of the view that clause 14.3 adequately dealt with the exclusion of indirect or consequential loss, and recommended that clause 14.7, which duplicated clause 14.3, be omitted from the standard access agreement.

Metro's response to the draft decision

Metro has removed clause 14.7 from the access agreement.

Commission's final decision

The Commission has reviewed Metro's amendment and considers it to be acceptable.

The Commission's final decision is that it accepts Metro's removal of clause 14.7.

Clause 15 – Variation of protocols

In its draft decision, the Commission was of the view that operators should be kept informed of, and consulted with in regard to any variations or replacements to operating protocols, as these changes have the potential to significantly impact on freight operations. The Commission recommended that clause 15(b) be amended such that when the access provider amends or replaces a protocol, the access provider must first consult with the operator.

Metro's response to the draft decision

In order to make the required amendment, Metro significantly altered the wording of clause 15 to read:

(b) In preparing any amendment or replacement of a protocol referred to in clause 15(a), the Access Provider must:

- (i) provide reasonable notice to the Operator of the amendment or replacement;*
- (ii) where the amendment or replacement is reasonably likely to have a significant impact on Services or operations of the Operator, consult with the Operator regarding the amendment; and*

this paragraph (b) does not prevent the Access Provider from amending or replacing the protocols if a failure to make such

amendment or replacements would compromise the safety, operational or commercial requirements of the Network or the Access Provider, provided it has otherwise complied with this paragraph (b).

(c) The Access Provider must promptly make available on its website updated copies of any amended or replaced protocols.

Commission's final decision

The Commission has reviewed Metro's amendment and considers it to be acceptable.

The Commission's final decision is that it accepts Metro's amendment to clause 15.

Clause 16.4 – Disclosure to the State

Clause 16.4 provides for confidential information to be provided to the Director, or any Minister, officer, employee, agent, advisor or consultant of the State or a governmental agency of the State. Asciano was concerned that there was no requirement for such disclosure to be on a confidential basis.³³

In its draft decision, the Commission was of the view that any confidential information provided to the State should be kept on a confidential basis given the nature of this information and its value to the freight operator, and therefore that clause 16.4 should be amended to reflect that provision of this information must be on a confidential basis.

Metro's response to the draft decision

Metro has amended clause 16.4 such that any confidential information provided to the Director, or any Minister, officer, employee, agent, advisor or consultant of the State or a governmental agency of the State would be disclosed 'on a confidential basis'.

Commission's final decision

The Commission has reviewed Metro's amendment and considers it to be acceptable.

The Commission's final decision is that it accepts Metro's amendment to clause 16.4.

Clause 18.2 – Sub-contracting

In its draft decision, the Commission was of the view that given there is a requirement on the operator for written approval by Metro for sub-contracting of

³³ Asciano submission to issues paper, p.23.

obligations under the access agreement, then in order to aid in the facilitation of sub-contracting, the result of this approval should not be delayed beyond reason.

The Commission therefore required that the standard access agreement should state that this approval must not be unreasonably delayed or withheld.

Metro's response to the draft decision

Metro has amended clause 18.2 to ensure that it will not unreasonably delay or withhold the approval to the operator to sub-contract any of its obligations, assuming the sub-contractor meets all the requirements of the operator.

Commission's final decision

The Commission has reviewed Metro's amendment and considers it to be acceptable.

The Commission's final decision is that it accepts Metro's amendment to clause 18.2.

Clause 21 – Notices

Clause 21(b) allows notices regarding an incident to be given orally. In response to the issues paper, Asciano proposed that, if oral notice is given, the access provider should be required to provide a supporting written notice within three days of that oral notice. This would help improve communication between the operator and the access provider and further clarify incident management and rectification.³⁴

The Commission supported this view, on the basis that it would avoid potential communication issues. As such, it required clause 21(b) to be amended to require that if oral notice of an incident is given by the access provider, the access provider must give a supporting written notice within three days of that oral notice.

Metro's response to the draft decision

Metro has amended clause 21(b) by including the following statement:

Where oral Notice is provided under this paragraph (b), the party that gives oral Notice must provide to the other party a written copy of that Notice within 3 Business Days of the oral Notice being given.

Commission's final decision

The Commission has reviewed Metro's amendment and considers it to be acceptable.

The Commission's final decision is that it accepts Metro's amendment to clause 21(b).

³⁴ Asciano submission to issues paper, p.24.

3.3 Issues on which further comment was sought

In the draft decision, the Commission sought further comment from stakeholders on a number of issues in Metro's access agreement before the Commission could make a decision. These issues related to:

- an option to extend the term of an access agreement upon expiry (clause 2)
- Metro's proposed wording in relation to reporting of incidents on the network such as breakdowns, accident, emergency, events or circumstances on or affecting the network (clause 12.4), and
- how delay payment indemnities are addressed – that is, when an operator causes or contributes to a delay in the network, it must reimburse the access provider for any delay loss (defined as payments Metro must make under its Franchise Agreement with Government should Metro not meet its performance targets, for example, running passenger on time).

Each of these issues and stakeholder responses and the Commission's final decision on these issues are discussed below.

Clause 2 – Option to extend term

Clause 2 deals with the commencement and term of the access agreement. The Commission sought further comment on whether clause 2 should be amended to include an option to extend the term of an existing access agreement.

Response to the draft decision

Both Metro and Asciano agreed that an option to extend the term of the agreement should be available at the agreement of both parties.³⁵ Metro has inserted clause 2.3, which reads:

2.3 Option to extend term

- (a) At least 6 months prior to the expiry of the Initial Term, the Operator may give the Access Provider notice that it proposes to extend the term.*
- (b) On receipt of the notice described in paragraph (a), the parties agree to meet to negotiate the period for which this Agreement will be renewed (Extended Period).*
- (c) This Agreement will continue to apply for the duration of the period of negotiation, which must not be longer than 2 months (Negotiation Period), and any agreed Extension Period, and this Agreement will expire on the earlier of:*

³⁵ Asciano submission to the draft decision, p.6: Metro submission to the draft decision, p.13.

- (i) *end of the Negotiation period if no agreement on the Extended Period;*
 - (ii) *end of the Extended Period; or*
 - (iii) *termination or expiry of the Infrastructure Lease.*
- (d) *The Operator cannot exercise the option in paragraph (a) if the Initial Term is expiring because the Infrastructure Lease has been terminated or expired.*

In addition to this clause, Metro included a new clause 4.3 in its revised access agreement.

4.3 Variation for Extended Period

The Access Charge may be varied for the Extended Period to reflect any change in the Reference Tariff during the Extended Period due to a new ESC approved Access Provider's Access Arrangement.

Commission's final decision

The Commission is of the view that the intent of clause 2.3 should be that the term of the agreement can only be extended by mutual agreement between the parties, and therefore the clause should require that the access provider and operator enter into good faith negotiations in order to determine the terms of the extension (including price, term, etc.). This may include the agreement to accept a change to the access charge if the Commission approves a change to the reference tariff. As a result, the Commission requires clause 4.3 to be removed and clause 2.3 to be amended to reflect this intent.

The Commission's final decision is that, in order to clarify the intention of the option to extend an access agreement, clause 4.3 of the proposed access arrangement be removed and clause 2.3 be amended as follows:

2.3 Option to extend term

- (a) At least 6 months prior to the expiry of the Initial Term either the Access Provider or Operator may by notice to the other require the parties to enter into good faith negotiations in relation to a possible extension of this agreement.***
- (b) If a notice is given under paragraph (a) the Access Provider and the Operator must negotiate in good faith an extension to the term of this agreement and any changes to be made to this agreement during any agreed extension period, although nothing in this clause 2.3 requires either party to agree to any such extension.***

Clause 12.4 — Reporting incidents

In its draft decision, the Commission sought comment on Metro's proposed rewording of clause 12.4. This clause relates to the reporting of incidents on the network such as breakdowns, accident, emergency, events or circumstances on or affecting the network.

Metro proposed the following:

Clause 12.4 (c) - When requested by the Access Provider, the Operator must provide in writing, information relating to the incident including:

1. *the time and location of the Incident,*
2. *available details of all loss or damage to the train operated by the Operator or injuries to any person,*
3. *any data relevant to the incident, including on train recordings, charts or other recording devices,*
4. *the primary cause of the Incident and any contributing factors,*
5. *actions proposed and taken by the Operator to prevent a re-occurrence of the Incident in the future; and*
6. *all other information as required by the Access Provider to meet information requests from TSV or other relevant investigating bodies or the Access Provider's internal accident investigation requirements, to enable the Access Provider to meet any of its obligations in relation to its Accreditation or under the Rail Safety Act 2006 (Vic).*

Response to the draft decision

Asciano argued that item 6 in clause 12.4(c), in effect, gives Metro 'carte blanche' to ask for any information it seeks, for the purpose of Metro's internal accident investigations. It suggested that item 6 be reworded to provide that Metro may request:

any other information required by the Access Provider to meet any of its obligations in relation to its Accreditation or under the Rail Safety Act 2006 (Vic).

Metro submitted that it requires the level of information outlined in clause 12.4(c) to enable it to complete the necessary internal and regulatory reports required after an incident.³⁶

Commission's final decision

While the Commission accepts Metro's reasoning for requiring the level of information outlined in clause 12.4(c), it is of the view that item 6 should be amended to require that the information requirements for the purpose of Metro's internal accident investigation be reasonable.

³⁶ Metro submission to the draft decision, p.13.

The Commission's final decision is that item 6 in clause 12.4(c) be amended as follows:

all other information as required by Access Provider to meet information requests from TSV or other relevant investigating bodies or the Access Provider's reasonable internal accident investigation requirements, to enable the Access Provider to meet any of its obligations in relation to its Accreditation or under the Rail Safety Act 2006 (Vic).

Clause 14.6 – Delay payment indemnity

Clause 14.6 of Metro's proposed access agreement relates to a delay payment indemnity. The delay payment indemnity requires an operator, if it causes or contributes to a delay in the network, to reimburse the access provider for any 'delay loss' (incentive payments Metro must make under the Operational Performance Regime in its Franchise Agreement) resulting from the delay.

Metro submitted a rewording of clause 14.6 to include the following clause:

Without limiting any other provision of this Agreement, if:

- (i) the Operator or any Train or Rolling Stock operated by the Operator causes or contributes to any delay in the Network; and*
- (ii) the delay referred to in paragraph (i) results directly in an OPR Incentive Payment; ('Delay Loss'); and*
- (iii) the Access Provider provides to the Operator written evidence of the Delay Loss,*

then the Operator must reimburse the Access Provider for the Delay Loss, to the extent that the Operator or the Train or Rolling Stock caused or contributed to such delay in the Network.

All payments by the Operator to the Access Provider under clause 14.6(a) will be calculated proportionately each calendar month as follows:

$$DL = (PWMO/PWM) \times OPRIP$$

where:

DL *is the Delay Loss payable by the Operator;*

PWM *is the Passenger Weighted Minutes (as determined within Schedule 7 for the Franchise Agreement – Train dated 31 August 2009) incurred by the Access Provider across the Network in the relevant calendar month;*

PWMO *is the PWMs attributed to the Operator in a calendar month; and*

OPRIP *is the OPR Incentive Payment payable by the Access Provider.*

In its draft decision, the Commission sought stakeholder feedback on the proposed rewording of clause 14.6(b). The Commission noted that a definition for 'performance weighted minutes' was not provided by Metro.

In its response to the draft decision, Asciano explained that, whilst it had initial concerns with clause 14.6, the wording substantially changed during the draft decision phase, with the major change including the requirement for any delay loss to be calculated proportionately to an applicable cap that is in place, and the requirement for Metro to provide written evidence of the delay loss. Asciano has stated that the amendment deals with its initial issues and is an improvement from the previous drafting.³⁷

Metro's response to the draft decision

In its response to the draft decision, Metro stated that the definition of passenger weighted minutes (PWM) is defined under Schedule 7 of the Franchise Agreement – Train dated 31 August 2009.³⁸

Commission's final decision

The Commission has reviewed the wording of clause 14.6 and the feedback from stakeholders, and considers that the amendment to clause 14.6 is acceptable.

However, the Commission notes Metro's claim that the definition of Passenger Weighted Minutes (PWM) is defined under Schedule 7 of the Franchise Agreement – Train dated 31 August 2009. The Commission also notes that the definition does not appear in the definitions section of Metro's revised access agreement. As such, for completeness, the definition of PWM should be included in the access agreement.

The Commission's final decision is that it accepts Metro's amendment to clause 14.6. However the definition of PWM should be included in section 1.1 of the standard access agreement, as follows:

PWM is the Passenger Weighted Minutes (as determined within Schedule 7 for the Franchise Agreement – Train dated 31 August 2009) incurred by the Access Provider across the Network in the relevant calendar month.

3.4 Additional revisions proposed by Metro

Metro also proposed a number of additional revisions to its access arrangement relating to its operating handbook and regulatory accounts templates.

3.4.1 Revisions to the operating handbook

Section 3 of the Network Management Rules requires Metro to prepare an operating handbook, which must include a number of protocols and documentation as specified in sections 4 to 8 of the Network Management Rules. Metro has

³⁷ Asciano submission to the draft decision, p.9.

³⁸ Franchise Agreement – Train, p.53.

revised three of these protocols in its network operating handbook (Attachment G of its proposed access arrangement):

- Train operating protocol (Attachment G.3)
- Track occupation protocol (Attachment G.4), and
- Operational interface procedures (Attachment G.5).

In addition to the changes to the train operating protocol discussed in chapter 3.1, Metro has made minor changes to the format of these operating protocols, and replaced specific titles with more generic titles, enabling the document to maintain accuracy when organisational changes are made.

The Commission has examined the changes made by Metro to the protocols and procedures in its operating handbook and is satisfied that none of the changes are material. Therefore, it is satisfied that, subject to the changes required in chapter 3.1, Metro's revised proposed operating handbook satisfies the requirements of the Network Management Rules.

The Commission's final decision is that it accepts Metro's proposed amendments to the operating protocols in its operating handbook, subject to the amendment of clause 6.5 of its train operating protocol as specified above.

3.4.2 Revisions to the regulatory accounts templates

Metro's proposal

In its response to the Commission's draft decision, Metro has proposed a new regulatory accounts pro-forma. Metro submits that the pro-forma is consistent with the accounts provided to the Department of Transport each year and it is therefore more efficient for Metro to provide them in the revised format to the Commission.

Metro states that the main changes relate to format changes to the Metro account mapping to satisfy the Department of Transport's reporting requirements. The mapping changes include the service delivery expenses section and the state sourced income section. These mapping changes do not include any new costs to the category of operation labour costs. The revised pro forma for the regulatory accounts are set out in metro's response to the Commission draft decision³⁹.

The Commission's Account Keeping Rules require the access provider to:

- prepare, maintain and keep separate accounts and accounting records for access activities from unregulated activities and to keep these for a minimum of five years (section 2.1), and
- annually provide financial and business information to the Commission, and provide other information on request.

³⁹ www.esc.vic.gov.au see Metro submission to draft decision, Attachment E.

The annual reporting of information to the Commission includes the following specific requirements:

- the annual provision of financial and business records to the Commission (sections 2.2 to) including:
 - o statements of financial performance and position;
 - o a cost allocation statement;
 - o disaggregated information on maintenance and capital works;
 - o service standards performance indicators; and
 - o details of the source of revenues from access activities.
- the financial statements, cost allocation statement, and maintenance and capital works information provided annually to the Commission must be audited and certified
- the annual reporting information must be submitted within four months of the end of the financial year (section 2.7), and
- the provision of other information to the Commission either regularly or on request.

Commission's response

Section 6.2 of the Account Keeping Rules provides that the Commission can waive requirements under the Rules where the Commission considers this would be consistent with the Commission's statutory obligations and that compliance is not necessary to achieve the purpose of the Rules.

The Account Keeping Rules, and indeed the entire VRAR, were developed at a time when the non-metropolitan network, with the exception of the ARTC-controlled lines, had been sold to an integrated freight operator (Pacific National) who was competing with other potential third-party freight operators. Much of the detail of the regime was therefore aimed at providing a transparent framework to ensure the integrated operator is not obtaining an advantage over a competitor. However, the situation has now changed and there are no such potential conflicts.

In the metropolitan area, Metro does not operate either freight services or non-metropolitan passenger services. While Metro's total direct costs associated with maintaining and operating infrastructure are identified in its current regulatory accounts, the share of indirect costs and overheads associated with the management of the business as a whole cannot be specifically identified and can only be estimated by applying a mark-up to the direct costs.

The allocation of costs between the various users (that is V/Line passenger, freight and Metro passenger services) is similarly difficult within a conventional accounting system. This is exacerbated by the current practice within the metropolitan statutory accounts of combining routine and renewal infrastructure expenditure.

It appears detailed reporting is of little practical value. No costs have been recorded for regulatory activities or corporate overheads and all other costs appear

to have been allocated on the basis of a common allocator (other than for rounding errors) which appears to be train kilometres.

The Commission therefore considers, consistent with the Government's objective of reducing the regulatory burden and taking into account the general move toward light-handed regulation foreshadowed in the 2010 VRAR review and the provisions of Section 6.2 of the Account Keeping Rules, that detailed analysis of access-related costs on an annual basis be discontinued and that a simple statement of expenditure by function be provided in the same format as supplied to DoT for concession monitoring purposes. This should be accompanied by a statement providing gross tonne kilometres and train kilometres by all users of the network so that the Commission can do its own analysis if so minded.

Therefore, the Commission is of the view Metro's proposed new regulatory account template is acceptable.

The Commission's final decision is that it accepts Metro's proposed new regulatory account template.

3.5 Summary of access agreement amendments

Table 13 summarises the amendments that have been made to the standard access agreement. It outlines the Commission's draft decision on the relevant clauses, Metro's response to the draft decision, and the Commission's final decision.

Table 13: Summary of access agreement amendments

Clause	Draft decision	Metro’s final revision	Commission final decision
<p>Section 1.1 – Definitions</p>	<p>The definition of incremental cost in section 1.1 of Metro’s access agreement should be amended to require incremental costs to be efficient and reasonable and incurred as a direct result of providing access.</p>	<p>Metro adopted the Commission’s recommendation.</p>	<p>The Commission accepts Metro’s revision.</p>
<p>Clause 2 – Term</p>	<p>The Commission sought further comment from Metro and stakeholders on the option to extend the term of the access agreement, and the words proposed by Metro.</p>	<p>Metro included an option to extend the term of the access agreement in its revised documents. The Commission negotiated with Metro and stakeholders as to the wording of this new clause.</p>	<p>The Commission requires a further amendment to clause 2.3, in conjunction with the removal of clause 4.3.</p> <p>See page 59.</p>
<p>Clause 3.2 – Unscheduled train paths</p>	<p>During the consultation period, stakeholders expressed the view that this clause should read that ‘passenger trains’ are given first priority, as oppose to ‘trains run by the Access Provider’ and as such the Commission made an interim recommendation to Metro to adjust this clause.</p>	<p>Metro partially adopted the Commission’s recommendation and reworded clause 3.2 to specify that priority will be given to the access provider for any train movements associated with passenger trains.</p>	<p>The Commission accepts Metro’s revision.</p>

Clause	Draft decision	Metro's final revision	Commission final decision
<p>Clause 3.3 – Ancillary movements</p>	<p>Clause 3.3(a) of Metro's access agreement should be amended so that ancillary movements are allowed if they are 'necessary or reasonably required'.</p> <p>Clause 3.3(b) of Metro's access agreement should be amended to provide that the conditions are set out in the relevant procedures and protocols, rather than being set from time to time.</p>	<p>Metro adopted the Commission's recommendation.</p> <p>Metro adopted the Commission's recommendation.</p>	<p>The Commission accepts Metro's revision.</p> <p>The Commission accepts Metro's revision.</p>
<p>Clause 3.5 – Alternative train paths</p>	<p>Clause 3.5 of Metro's access agreement should be amended to specify that where an operator's train path is varied according to clause 3.5 the access provider will use reasonable endeavours to make a similar alternative train path available to the operator</p>	<p>Metro adopted the Commission's recommendation.</p>	<p>The Commission accepts Metro's revision.</p>

Clause	Draft decision	Metro's final revision	Commission final decision
<p>Clause 4.4 – Incremental costs (previously clause 4.3)</p>	<p>Clause 4.3 of Metro's access agreement should be amended to include a requirement on the access provider to explain the nature of incremental costs that may be incurred and the method of calculation for these costs, and take into account any information the operator may have in relation to these costs.</p> <p>Clause 4.3(a) of Metro's access agreement should be amended to provide that where incremental costs are attributable to the operator and any other <i>users of the network</i>, the access provider will make a reasonable allocation of those incremental costs as between the operator and the other <i>users of the network</i>.</p>	<p>Metro partially adopted the Commission's recommendation and is now referred to as clause 4.4.</p> <p>Metro partially adopted the Commission's recommendation and is now referred to as clause 4.4(a).</p>	<p>The Commission accepts Metro's revision.</p> <p>The Commission requires further amendment to clause 4.4(a).</p> <p>See page 44.</p>
<p>Clause 4.6 – Objection to invoice (previously clause 4.5)</p>	<p>Clause 4.5(c) of Metro's access agreement should be amended to ensure that where an adjustment to an invoice is required this is done by the access provider.</p>	<p>Metro adopted the Commission's recommendation and is now referred to as clause 4.6(c).</p>	<p>The Commission accepts Metro's revision. Note that this clause is now referred to as clause 4.6.</p>

Clause	Draft decision	Metro's final revision	Commission final decision
<p>Clause 4.8 – Set off (previously clause 4.7)</p>	<p>Clause 4.7 of Metro's access agreement should be amended to allow both parties to set off from payments any amounts due and payable by the other party.</p>	<p>Metro adopted the Commission's recommendation and is now referred to as clause 4.8.</p>	<p>The Commission accepts Metro's revision. Note that this clause is now referred to as clause 4.8.</p>
<p>Clause 4.10 – Performance bond (previously 4.9)</p>	<p>The Commission sought further comment from stakeholders, Metro and lawyers as to the interpretation of clause 4.9.</p>	<p>The clause is now referred to as clause 4.10.</p>	<p>The Commission requires further amendment to clause 4.9, as well as various consequential amendments.</p> <p>See pages 47-49.</p>

Clause	Draft decision	Metro's final revision	Commission final decision
<p>Clause 5.4 – Variation or surrender due to operator breach</p>	<p>Clause 5.4 of Metro's access agreement should be amended to provide that only a material breach or failure to comply may result in the variation or surrender of a train path.</p> <p>Clause 5.4(a) of Metro's access agreement should be amended to require the access provider to 'act reasonably and take into account all relevant circumstances' when requiring an operator to vary or surrender a train path.</p>	<p>Metro did not adopt the Commission's recommendation.</p> <p>Metro adopted the Commission's recommendation.</p>	<p>The Commission accepts Metro's amendment of clause 5.4(a) addresses the Commission's concerns.</p> <p>The Commission accepts Metro's revision.</p>
<p>Clause 5.5(a) – Variation or surrender due to capacity use issues</p>	<p>Clause 5.5(a) of Metro's access agreement should be amended to state that variations 'may' be required, rather than 'must'.</p>	<p>Metro adopted the Commission's recommendation.</p>	<p>The Commission accepts Metro's revision.</p>

Clause	Draft decision	Metro's final revision	Commission final decision
<p>Clause 5.6 – Temporary variations by the access provider</p>	<p>Clause 5.6(a)(ii) of Metro's access agreement should be amended so that temporary variations to train paths should be 'to the extent necessary' to effect repairs and maintain and upgrade the network.</p> <p>Clause 5.6(d) of Metro's access agreement should be amended to require that, where temporary path variations are made by the access provider, the access provider provide reasonable notice to affected rail operators.</p>	<p>Metro adopted the Commission's recommendation.</p> <p>Metro adopted the Commission's recommendation.</p>	<p>The Commission accepts Metro's revision.</p> <p>The Commission accepts Metro's revision.</p>
<p>Clause 6.4 – Communication responsibilities</p>	<p>Clause 6.4 of Metro's access agreement should be amended to require the access provider notify the operator of any variations to the Metro website which directly relate to any protocols which must be followed by or relate to other obligations of the operator.</p>	<p>Metro adopted the Commission's recommendation.</p>	<p>The Commission accepts Metro's revision.</p>

Clause	Draft decision	Metro's final revision	Commission final decision
<p>Clauses 7.2 and 7.3 – Axle weight and track speed</p>	<p>Clauses 7.2 and 7.3 of Metro's access agreement should be amended to require Metro to use reasonable endeavours to consult with the operator about any proposed change to the maximum axle weight and track speed, in addition to notifying the operator of any such changes.</p>	<p>Metro adopted the Commission's recommendation.</p>	<p>The Commission accepts Metro's revision.</p>
<p>Clause 12.3 – Dealing with incidents</p>	<p>Clause 12.3(b) of Metro's access agreement should be amended to require that the costs referred to in 12.3(b) are reasonable and that the access provider endeavours to minimise costs incurred under paragraph 12(b).</p> <p>Clause 12.3(d) of Metro's access agreement should be amended such that where the operator is required by ASX listing rules to disclose information about an incident, the operator must use reasonable endeavours to consult with the access provider as to the form and content of the comment prior to making any public disclosure.</p>	<p>Metro adopted the Commission's recommendation.</p> <p>Metro adopted the Commission's recommendation.</p>	<p>The Commission accepts Metro's revision.</p> <p>The Commission accepts Metro's revision.</p>

Clause	Draft decision	Metro's final revision	Commission final decision
Clause 12.4 – Other consequences of incident	The Commission sought further comment from Metro in regard to the proposed wording of clause 12.4, in particular the point regarding public comments by the operator involved in an incident.	Metro has adopted the Commission's interim advice to alter the wording of clause 12.4 to allow a more balanced arrangement in regard to publicly commenting on an incident.	The Commission requires further amendment to clause 12.4. See page 61.
Clause 13.1 – Environment	Clause 13.1(c) of Metro's proposed access agreement should be amended to require the access provider to allocate costs among users.	Metro adopted the Commission's recommendation.	The Commission accepts Metro's revision.
Clause 14.1 and 14.2 – Indemnity and release	Clauses 14.1 and 14.2 appear unclear and should be amended to clarify that mutual <i>indemnity</i> is granted in relation to damage sustained by one party to the extent that the damage was caused or contributed to by a breach of this agreement by the other party or a negligent act or omission of the other party.	Metro adopted the Commission's recommendation.	The Commission accepts Metro's revision.
Clause 14.3 – Exclusion of indirect or consequential loss	Clause 14.3(b)(ii) of Metro's access arrangement should be removed.	Metro adopted the Commission's recommendation.	The Commission accepts Metro's revision.

Clause	Draft decision	Metro's final revision	Commission final decision
Clause 14.4 – Insurance	Clause 14.4 of Metro's proposed access agreement should be amended to provide that insurance may be effected with any reputable and solvent insurer.	Metro adopted the Commission's recommendation.	The Commission accepts Metro's revision.
Clause 14.6 – Delay payment indemnity	The Commission sought further comment from Metro in regard to the proposed wording and clarification of clause 14.6.	Metro has adopted the Commission's interim advice to alter the wording of clause 14.6 to include a definition of PWM.	The Commission requires further amendment to clause 14.6. See page 62.
Clause 14.7 – Exclusion or indirect or consequential loss	Clause 14.7 of Metro's proposed access agreement should be deleted given it duplicates clause 14.3.	Metro adopted the Commission's recommendation.	The Commission accepts Metro's revision.
Clause 15 – Variation of protocols	Clause 15(b) of Metro's proposed access agreement should be amended such that when the access provider amends or replaces a protocol which is likely to have a significant impact on freight operations, the access provider must first consult with the operator.	Metro adopted the Commission's recommendation.	The Commission accepts Metro's revision.

Clause	Draft decision	Metro's final revision	Commission final decision
Clause 16.4 – Disclosure to state	Clause 16.4 of Metro's proposed access agreement should be amended to provide that confidential information may only be disclosed on a confidential basis.	Metro adopted the Commission's recommendation.	The Commission accepts Metro's revision.
Clause 18.2 – Subcontracting	Clause 18.2 of Metro's proposed access agreement should be amended to provide that where an operator wishes to sub-contract any of its obligations, the written consent required from the access provider must not be 'unreasonably delayed or withheld'.	Metro adopted the Commission's recommendation.	The Commission accepts Metro's revision.
Clause 21 – Notices	Clause 21 of Metro's proposed access agreement should be amended to require that, if oral notice is given, the access provider must provide a supporting written notice within three days of that oral notice.	Metro adopted the Commission's recommendation.	The Commission accepts Metro's revision.

APPENDIX A | LEGISLATIVE REQUIREMENTS & APPROVAL PROCESS

The sections below highlight the material that an access provider is required to prepare and submit to the Commission, as well as the Commission's approval process.

Obligation to submit a proposed access arrangement

Under section 38ZR of the RMA, an access provider must not less than 90 days before expiry of a binding access arrangement apply to the Commission for the renewal of that access arrangement.

The contents of proposed access arrangements are set out in section 38X(1) of the Act and reproduced in **Box 2**.

Section 38X(3) to 38X(5) of the RMA requires a proposed access arrangement to be consistent with the:

- Pricing Order;
- any pricing methodology made by the Commission;
- Negotiation Guidelines;
- Account Keeping Rules;
- Ring Fencing Rules;
- Capacity Use Rules; and
- Network Management Rules.

A proposed access arrangement can include any other matter, in addition to the above requirements, that the access provider considers relevant (section 38X(2)).

Box 2: Section 38X of the RMA – Contents of proposed access arrangements

- (1) A proposed access arrangement must—
- (a) in relation to every reference service to which the arrangement relates, include—
 - (i) a description of the service; and
 - (ii) information as to whether that service is being provided by the access provider to itself or a related body corporate of the access provider; and
 - (iii) the terms and conditions for the provision of that service; and
 - (iv) the price, or methodology for the calculation of the price, to be charged in respect of the provision of that service; and
 - (b) include information in relation to the availability and the indicative terms and conditions, for the provision of declared rail transport services that are not reference services; and
 - (c) include a description of the information that the access provider will make available to an access seeker; and
 - (d) set out the procedure for the making of an application by an access seeker for the provision to them of a declared rail transport service; and
 - (e) describe the procedure and method how the access provider will assess and determine an application for the provision by them of a declared rail transport service; and
 - (f) specify a date for the expiry of the access arrangement, being a date that is not less than 3 years, and not more than 5 years, after the date on which the access arrangement may be approved by the Commission under this Part in a final decision.
- (2) A proposed access arrangement may also include any other matter that the access provider considers relevant.
- (3) The price or methodology referred to in sub-section (1)(a)(iv) must be consistent with the pricing principles and any methodology for the calculation of prices determined by the Commission under the Pricing Principles Order.
- (4) Information referred to in sub-section (1)(c), the procedure referred to in sub-section (1)(d) and the procedure and method referred to in sub-section (1)(e) must be consistent with the negotiation guidelines.
- (5) The proposed access arrangement must also be consistent with—
- (a) the account keeping rules; and
 - (b) the ring fencing rules; and
 - (c) the capacity use rules; and
 - (d) the network management rules.

Obligation to submit access arrangement information

A proposed access arrangement must also contain access arrangement information, which is defined in section 38W(2) of the RCA to be 'information that an access seeker would reasonably require to understand the derivation of the elements of the access arrangement so as to form an opinion as to whether the access arrangement complies with Part 2A of the RCA.'

The Commission considers that information included in the access arrangement information must be made available to access seekers and the public.

Supporting information and material

In addition to the access arrangement information, the access provider should provide supporting information and material to establish compliance of their proposed access arrangement with the requirements of the RCA and, in particular, that the proposed access arrangement is consistent with, among other things, the Pricing Order and any pricing methodology made by the Commission.

Furthermore, the access provider should provide details of any consultation with industry stakeholders on the proposed access arrangement, or drafts of the proposed access arrangement.

Other material to accompany the proposed access arrangement

When an access provider submits a proposed access arrangement to the Commission for approval, it must at the same time, submit a:

- 'cost allocation policy' and 'templates' for providing accounting information to the Commission under the Account Keeping Rules;
- 'separation arrangement' under the Ring Fencing Rules;
- statement of 'capacity management protocols' under the Capacity Use Rules; and
- 'network operating handbook' and 'rolling stock interface standards' under the Network Management Rules.

In addition, pursuant to section 38ZZZB of the RMA, an access provider must, on the same day as it submits a proposed access arrangement, submit to the Commission for approval, system and business rules for:

- (a) The use or handling of information supplied to the access provider in confidence by an access seeker or a user, including the use or handling of that information by an officer, employee or agent of the access provider, and
- (b) The disclosure of information supplied to the access provider in confidence by an access seeker or a user, including the disclosure of that information by an officer, employee or agent of the access provider.⁴⁰

The Commission's approval process

The table below summarises the process for access arrangement approval. The process begins when the Commission receives a proposed access arrangement from an access provider and ends when the Commission publishes its final decision, or appeals on the final decision are determined.

⁴⁰ Section 38ZZZB of the RMA.

Step	Summary of procedure
1	The access provider prepares and submits a proposed access arrangement under section 38W along with any required accompanying material.
2	<p>The Commission receives a proposed access arrangement from the access provider under section 38W.</p> <p>The Commission must, as soon as practicable, acknowledge receipt of the proposed access arrangement by notifying every interested party in writing and by publication on its website and in a state newspaper (section 38Y(1)).</p> <p>The Commission must provide no less than 21 days for written submissions to be made in respect of the proposed access arrangement from the date of notification (section 38Y(2)).</p>
3	<p>Before making a Draft Decision, the Commission must consider all written submissions received within the specified time, and may, but is not required to, consider late submissions (section 38ZA).</p> <p>The Commission must make a Draft Decision to approve or not approve the proposed access arrangement, stating reasons for its decision. When making a Draft Decision, the Commission must take into account matters listed in section 38ZI. If the Commission does not approve the proposed access arrangement it needs to specify any amendments that should be made and any matters that should be addressed for approval (section 38ZB).</p> <p>The Commission must give a copy of the Draft Decision to every party who submitted comments to the proposed access arrangement and to the access provider. The Commission must also publish the Draft Decision on its website and make it available for inspection at its offices (section 38ZB(5)).</p> <p>The Commission must provide no less than 14 days, from the date the Draft Decision is published, for written comments to be submitted (section 38ZB(6)).</p>
4	The access provider may, within 14 days of being given a copy of the Draft Decision, submit revisions to the initial proposal (section 38ZC).
5	<p>Before making a Final Decision, the Commission must consider all written submissions received within the specified time, and may, but is not required to, consider late submissions (section 38ZE).</p> <p>The Commission must make a Final Decision to approve or not approve the proposed access arrangement, stating reasons for its decision (section 39ZF). When making a Final Decision, the Commission must take into account matters listed in section 38ZI. The Commission is required to give notice of its Final Decision as specified in section 38ZH.</p> <p>The Commission's Final Decision must be made within 90 days of the access provider submitting the initial proposed access arrangement (section 38ZG).</p>

Step	Summary of procedure
6	Appeals on the Final Decision can be made pursuant to section 55 of the <i>Essential Services Commission Act 2001</i> (Vic).

Matters that the Commission must take into account

Section 38ZI of the RMA requires the Commission to take certain matters into account. These include:

- the rail-specific objectives in section 38F of the RMA (section 38ZI(a));
- the matters that reflect clause 6(4)(i) of the Competition Principles agreement (**CPA**) (see section 38ZI(b) to (i) of the RMA); and
- any other matter that the Commission considers relevant (section 38ZI(j)).

Each of these is discussed in turn below:

Rail-specific objectives

The regulatory objectives of the Commission, as stated in section 38F of the RMA:

in addition to the objectives under section 8 of the Essential Services Commission Act 2001 (but subject to section 5(2) of that Act):

(a) to ensure access seekers, and any other person the Commission considers may want to be provided declared rail transport services, have a fair and reasonable opportunity to be provided declared rail transport services; and

(b) to promote competition in rail transport services to achieve an increase in the use of, and efficient investment in, rail infrastructure or tram infrastructure (as the case requires).

Matters in section 38ZI(b) to (i) of the RMA

The matters that reflect the CPA and to which the Commission must have regard (as set out in section 38ZI(b) to (i)) are:

- (b) the access provider's legitimate business interests and investment in the rail network owned or operated by that access provider, and*
- (c) the costs to the access provider of providing access, including any costs of extending the rail network owned or operated by that access provider but not including costs associated with losses arising from increased competition in upstream or downstream markets, and*
- (d) the economic value to the access provider of any additional investment that an access seeker or the access provider has agreed to undertake, and*
- (e) the interests of users, and*

- (f) existing contractual obligations of the access provider and users of the rail network owned or operated by that access provider, and*
- (g) the operational and technical requirements necessary for the safe and reliable operation of the rail network owned or operated by the access provider, and*
- (h) the economically efficient operation of the rail network owned or operated by the access provider, and*
- (i) the benefit to the public in having competitive markets*

Other relevant matters

Under section 38Z1(j), the Commission must have regard to any other matter that the Commission considers relevant.

APPENDIX B | WEIGHTED AVERAGE COST OF CAPITAL

Weighted Average Cost of Capital (WACC)

The Weighted Average Cost of Capital (WACC) is the internal cost of capital of a firm, and in the regulatory context is the rate of return that is to be earned on the regulatory asset base.

Given Metro's regulatory asset base is zero and no capital expenditure is proposed over the regulatory period, an assessment of the WACC for this draft decision is largely irrelevant. However, for completeness the Commission has assessed it Metro's proposed WACC in the event future capital expenditure is proposed.

Metro's proposal

Metro has used a capital asset pricing model (CAPM) approach to calculate the WACC. Metro's proposed WACC parameters (compared to the 2006 determination) are summarised in the Table 16.

Table 16 Components of WACC

<i>Parameter</i>	<i>Metro proposed 2011</i>	<i>Metro 2006</i>
Real risk free rate	2.26%	2.26%
Debt risk margin	3.0	1.285
Market risk premium	6.0%	6.0%
Equity beta	0.74	0.74
Imputation credits	0.5	0.5
Real pre tax WACC	6.44%	5.71%

Source: Metro access arrangement information 31 March 2011, p.18.

Metro reviewed each of the component parameters of the WACC. Updated estimates were obtained for the nominal risk free rate (based on the 20 day average yield of 10 year government bonds) and inflation (based on the Melbourne – All Groups Index over the past year to the end of December 2010 quarter). Together these give an estimate of the real risk free rate of 2.26 per cent.⁴¹

⁴¹ Metro, 31 March 2011, access arrangement information, p.16.

Metro also proposed an increased debt risk margin, based on the experience of other rail jurisdictions. For all other WACC parameters Metro proposes to use the same values as in the last determination.

The debt margin represents the difference between the cost of debt capital to the business and the risk free rate. Metro has proposed a debt risk margin of 3.0. Metro argued that this is supported by the Economic Regulation Authority of Western Australia in its final decision of the 2008 Weight Average Cost of Capital for Freight (Westnet Rail) and Urban (Public Transport Authority) Railway Networks.⁴²

Stakeholder views

Stakeholders made no submissions in relation to this matter.

Commission's draft decision

Real risk free rate

The approach proposed by Metro, using estimates for a nominal risk free rate and inflation to derive a real risk free rate, is consistent with current regulatory practice.

Capital structure

Metro's proposal for gearing is the same as that used for the determination of the 2006 access arrangements. The Commission considers that Metro's proposal of 55 per cent gearing is reasonable, given that the risk profile of the business has not changed significantly since the previous review.

It is also consistent with other recent rail access determinations, notably by IPART, the ACCC and the QCA:

ACCC's 2010 decision assumed 50 per cent gearing for the Hunter Valley Rail Network⁴³

QCA's 2010 decision assumed 55 per cent gearing for QR's coal network⁴⁴

IPART's August 2009 decision for the NSW Rail Access Undertaking used a range for gearing of 50 to 60 per cent⁴⁵

Equity beta

Metro proposed an equity beta of 0.74, consistent with the equity beta used by the Commission in its 2006 Determination. Other recent rail access decisions on beta include:

⁴² Metro access arrangement information p.17.

⁴³ ACCC, March 2010, Australian Rail Track Corporation Limited Hunter Valley Coal Network Access, Undertaking, Draft Decision, p.580.

⁴⁴ QCA, June 2010, Draft Decision, QR Network's 2010 DAU - Tariffs and Schedule F, p.56.

⁴⁵ IPART, August 2009, New South Wales Rail Access Undertaking - Review of the rate of return and remaining mine life from 1 July 2009, Rail Access — Final Report and Decision, p.6.

ACCC's 2010 decision for the Hunter Valley Coal Network which used an equity beta of 1.00⁴⁶

QCA's 2010 determination of an equity beta of 0.80 for QR⁴⁷

IPART's August 2009 decision for the NSW Access Undertaking which used a range of 0.7 to 1.0 for equity beta⁴⁸, and

ERA's 2008 decision to apply an equity beta of 0.46 for WA's urban rail network and an equity beta of 1.00 for Westnet Rail's freight network.⁴⁹

The Commission would expect the degree of systematic risk to be greater for coal, mineral and interstate freight rail networks than for an urban rail network. This is supported by ERA's choice of a significantly lower equity beta for WA's urban rail network.

The Commission considers that an appropriate range for Metro's equity beta is 0.45 to 0.7. Since the overall risk profile for Metro has not changed compared to the previous franchise arrangement, and in the interest of consistency, the Commission considers that Metro's proposal to use the same beta as agreed in 2006 is reasonable.

Market risk premium

Metro proposed a market risk premium of 6 per cent. Metro's proposal is based on the considerable research supporting a market risk premium of this range, and the 2008 decision of ERA regarding the appropriate cost of capital for freight and passenger services.⁵⁰

Other more recent rail decisions have likewise used an assumption of 6 per cent for the market risk premium. These include the ACCC's draft determination for the Hunter Valley Network, ERA's determinations for the urban and freight networks, and QCA's decision for QR's coal network. For the NSW Access Undertaking, IPART assumed a range of 5.5 to 6.5 per cent for the market risk premium.

Against this background, the Commission considers that Metro's proposal for a 6 per cent equity market premium is reasonable.

Value of imputation credits

Metro proposed a gamma of 0.5, based on regulatory precedent.⁵¹

The appropriate choice of gamma is an area of some controversy. The Commission recognises that many of the recent rail decisions adopted a gamma of 0.5, including:

⁴⁶ ACCC, March 2010, Op cit.

⁴⁷ QCA, June 2010, Op cit.

⁴⁸ IPART, August 2009, Op cit.

⁴⁹ ERA, June 2008, Final Determination 2008 Weighted Average Cost of Capital for the Freight (WestNet Rail) and Urban (Public Transport Authority) Railway Networks, p.37.

⁵⁰ Metro access arrangement information p.17.

⁵¹ Ibid.

ERA's 2008 determination for the urban and freight rail networks⁵²
QCA's 2010 decision for QR⁵³
ERA's 2009 decision for TPI⁵⁴, and
IPART's 2009 decision to use the range 0.3 to 0.5 for the NSW Rail Access Undertaking.⁵⁵

However, the ACCC's 2010 draft determination for the Hunter Valley Coal Network adopted a gamma of 0.6556, consistent with the AER's May 2009 determination of the weighted average cost of capital (WACC) parameters for electricity transmission and distribution network service providers.⁵⁷ The AER's decision was subsequently appealed to the Australian Competition Tribunal by Energex, Ergon and ETSA. In a statement of reasons released in May 2011, the Tribunal determined that the AER had erred in setting gamma at 0.65, and determined a gamma of 0.25 as appropriate.⁵⁸

Given the weight of regulatory precedent in favour of a gamma of 0.50, and bearing in mind the need for consistency in decision making, the Commission considers that Metro's proposal of a gamma of 0.5 is reasonable.

Debt margin

Metro proposed a debt margin of 300 basis points. The approach typically used by the Commission for estimating debt margins is to assume a credit rating of BBB+, consistent with the benchmark gearing level, and deriving a margin for a BBB+ rated company from Australian corporate bond yields (using information sourced from CBASpectrum and/or Bloomberg fair yield curves).

A similar approach has been used for several of the recent rail decisions, notably: IPART's 2009 decision which used a debt margin of 2.0 to 3.4 per cent for the NSW Rail Access Undertaking⁵⁹

The ACCC's 2010 draft decision of a margin of 3.36 per cent for the ARTC's Hunter Valley network⁶⁰

ERA's 2008 decision of a margin of 3.02 per cent for freight and 2.51 per cent for urban rail networks⁶¹

⁵² ERA, June 2008, Op cit.

⁵³ QCA, June 2010, Op cit.

⁵⁴ ERA, June 2009, The Pilbara Infrastructure (TPI), Final Determination on the 2009 Weighted Average Cost of Capital for TPI's Railway Network, p.55.

⁵⁵ IPART, August 2009, Op cit.

⁵⁶ ACCC, March 2010, Op cit.

⁵⁷ AER, May 2009, Final Decision, Electricity transmission and distribution network service providers: Review of the weighted average cost of capital (WACC) parameters.

⁵⁸ Australian Competition Tribunal, 12 May 2011, Application by Energex Limited (Gamma) (No 5) [2011] ACompT 9.

⁵⁹ IPART, August 2009, Op cit.

⁶⁰ ACCC, March 2010, Op cit.

ERA's 2009 decision for TPI of a debt margin of 3.76 per cent⁶²

QCA's 2010 decision of a 3.62 per cent debt margin for QR.⁶³

The size of the debt margin will reflect the level of risk inherent in the benchmark as well as the conditions in the debt market at the time of the pricing determination.

Since the global financial crisis, the market for long term bond markets has become very illiquid. As a consequence, recent regulatory decisions have used a variety of approaches to estimating the debt margin. For example, in recent decisions for electricity distribution and gas pipelines, the AER used an average of the Bloomberg fair yield curve and the yield on an APT bond.⁶⁴ Following a consultation process, IPART has decided to determine the debt margin by reference to a sample of yields from Australian and US bond markets, combined with Bloomberg fair yield curves.⁶⁵

The most recently available decisions on debt margins are:

A margin of 3.93 per cent for a BBB+ benchmark for Envestra Ltd, determined in Feb 2011 by the AER⁶⁶

A margin of 3.79 per cent for a BBB+ benchmark for NT Gas, determined by the AER in Feb 2011⁶⁷, and

A debt margin of 3.30 per cent for a BBB+ rated benchmark for WA Gas Networks, determined by ERA in Feb 2011.⁶⁸

Given this range of evidence on debt margins, the Commission believes that Metro's proposal to increase the debt margin to 3.0 per cent is reasonable.

The Commission's preliminary view is Metro's approach to calculating its WACC is consistent with the Pricing Order, and therefore does not raise objections under section 38X(3) of the RMA.

⁶¹ ERA, June 2008, Op cit.

⁶² ERA, June 2009, Op cit.

⁶³ QCA, June 2010, Op cit.

⁶⁴ AER, April 2011, N.T. Gas Access arrangement proposal for the Amadeus Gas Pipeline.

⁶⁵ IPART, Developing the approach to estimating the debt margin Other Industries — Final Decision April 2011.

⁶⁶ AER, Feb 2011, Draft Decision, Envestra Ltd, Access arrangement proposal for the SA gas network, 1 July 2011 – 30 June 2016.

⁶⁷ AER, April 2011, Op cit.

⁶⁸ ERA, Feb 2011, Final decision on WA Gas Networks Pty Ltd proposed revised access arrangement for the Mid-West and South-West Gas Distribution Systems.

APPENDIX C | METRO'S REVISED ACCESS AGREEMENT – MARKED UP

Access Agreement

Metro Trains Melbourne Pty Ltd
and

[insert Operator's name] Pty Ltd

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This Access Agreement

is made on **[insert date]** between the following parties:

- 1 **Metro Trains Melbourne Pty Ltd**
ABN 43 136 429 948
of Level 24, 1 Spring Street, Melbourne VIC 3000
(Access Provider)
- 2 **[insert Operator's name] Pty Ltd**
ABN [insert Operator's ABN]
of **[insert Operator's address]**
(Operator)

Recitals

- A. The Access Provider leases the Network from the Director pursuant to the Infrastructure Lease.
- B. The Access Provider has agreed to provide the Operator with access to the Network for the purpose of operating trains on the terms set out in this Agreement.

The parties agree

in consideration of, among other things, the mutual promises contained in this agreement:

1 Definitions and Interpretations

1.1 Definitions

In this Agreement the following definitions apply unless the context requires otherwise:

ACCC means the Australian Competition and Consumer Commission or its successor.

Access Arrangement has the meaning given in the *Rail Corporations Act*.

Access Charge means those charges as described in Schedule 1.

Access Provider's Protocols means the protocols described in Clause 15.

Accreditation means accreditation obtained in accordance with the requirements of Part 5 of the *Rail Safety Act 2006 (Vic)*, including any guideline, regulation or ordinance made pursuant to that Part;

Addenda means the most up to date addenda to the Metropolitan Master Working Timetable published from time to time as contained in the document entitled "Metro Trains Working Timetable System Description [WTT Addenda] dated **May 2011**".

Adjustment Note has the meaning given in the GST Law.

Ancillary Movements means Train movements which are not part of a Train Path but which are necessary or reasonably required to use the Train Path, including for Stabling purposes and movement of empty Trains and light engines for operative or maintenance purposes to workshops, locomotive depots and fuel points.

Associate means, in relation to a party; and

Deleted: Accreditation means accreditation obtained in accordance with the requirements of Division 3, Part VI of the Transport Act, including any guideline, regulation or ordinance made pursuant to that Division.¶

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- (a) any Related Body Corporate of that party;
- (b) any officer, employee, agent, contractor, consultant or adviser of that party.

Book of Rules means the book of rules that applies to operations on the Network, PTC Book of Rules and Operating Procedures 1994, as those rules and operating procedures are amended or replaced from time to time with the approval of the Director, Public Transport Safety.

Business Day means a week day on which trading banks are open for the transaction of banking business in Melbourne.

Capacity Allocation Protocol means the Access Provider's protocol made pursuant to the Capacity Use Rules.

Capacity Use Rules means the rules made by the ESC under section 38T of the *Rail Corporations Act*.

Communications Protocol means the communications protocol issued by the Access Provider from time to time.

Confidential Information has the meaning given in Clause 16.

Consideration has the meaning given by the GST Law.

Corporations Act means the *Corporations Act 2001* (Cth).

Country Network means the Victorian country rail network which connects with the Network.

CPI means the Consumer Price Index (All Groups Index Number, weighted average of 8 Capital Cities) as published by the Australian Bureau of Statistics. In this definition:

- (a) the reference to the Consumer Price Index (All Groups Index Number, weighted average of 8 Capital Cities) means:
 - (i) the same number but with different names at any time;
 - (ii) the same number adjusted mathematically to take account of a change at any time in the base period provided that indices of the same base year are used throughout the calculations; and
- (b) the reference to the Australian Bureau of Statistics includes a reference to:
 - (i) the Australian Bureau of Statistics but with a different name at any time; and
 - (ii) a Governmental Agency in Australia (in the absence of the Australian Bureau of Statistics) at any time having similar functions.

CPI Multiplier at any time means:

- (a) the CPI for most recent March Quarter at that time, divided by,
- (b) the CPI for the March Quarter immediately preceding the most recent March Quarter referred to in (a).

Cure Period has the meaning given in Clause 17.3.

Cure Plan means a plan by a party to remedy a material breach of this Agreement which:

- (a) is proposed during the Cure Period; and

- (b) details:
- (i) the reasonable time required to cure the relevant material breach; and
 - (ii) a work plan setting out each task to be undertaken in order to rectify the material breach and the time for each task to be completed.

Daily Train Plan means the timetable maintained by the Access Provider that sets out planned Train movements on the Network on a particular day.

Dangerous Goods Code means the Australian Code for the Transportation of Dangerous Goods by Road or Rail published by the National Road Transport Commission (or its successor) from time to time.

Default Notice has the meaning given in Clause 17.3.

Default Rate means the rate of interest prescribed from time to time under section 2 of the *Penalty Interest Rates Act 1983* (Vic).

Defaulting Party has the meaning given in Clause 17.3.

Director means the Director of Public Transport under the *Transport Integration Act 2010* (Vic) or his successor.

Effective Date means the date of execution of this Agreement.

Emergency Response Plan means the Emergency Response Plan issued from time to time by the Access Provider.

Environment includes the meaning given to that term at common law and in any Law in force in Victoria, including any land, water, atmosphere, climate, sound, odours, tastes, the biological factors of animals and plants and the social factors of aesthetics.

Environmental Hazard means a state of danger to human beings or the Environment whether imminent or otherwise resulting from the location, storage or handling of any substance having toxic, corrosive, flammable, explosive, infectious or otherwise dangerous characteristics.

Environmental Law means any Law relating to the Environment, including any Law relating to land use, planning, pollution of air, water, soil or groundwater, chemicals, waste, the use of transport, the storage and handling of dangerous goods, the health or safety of any person, or any other matters relating to but not limited to the protection of the Environment, health or property.

ESC means the Essential Services Commission or its successor.

Extended Period has the meaning given in clause 2.3(b).

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Force Majeure means any circumstances beyond the reasonable control of a party which occurs without the negligence of that person including (without limitation):

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- (a) inevitable accident, act of God, lightning, storm, flood, landslide, fire or earthquake, peril of navigation;
- (b) high temperatures resulting in the imposition of operating restrictions pursuant to the Metropolitan Master Working Timetable or the Daily Train Plan;
- (c) strikes, lockouts or other industrial action;

- (d) act of public enemy, hostility, war (declared or undeclared), terrorism, sabotage, blockade, revolution, riot, insurrection, civil commotion, epidemic;
- (e) the effect of any change in applicable Laws of any government or other competent authority;
- (f) executive or administrative order or act of either general or particular application of any government, prohibition or restriction by domestic or foreign laws, regulations or policies (other than laws specifically for that purpose passed by the Commonwealth of Australia), quarantine or customs restrictions;
- (g) breakdown or damage to or confiscation of property (but not including breakdown or delay of any Rolling Stock operated by the Operator); or
- (h) embargo or power or water shortage.

Franchise Agreement means the document titled “Franchise Agreement – Train” between the Director and the Access Provider dated 31 August 2009, as amended.

Freight Trains means rail services that are not passenger rail services.

Governmental Agency means any government or any governmental, semi-governmental or judicial entity or authority, including any self regulatory organisation or any stock exchange.

GST has the meaning given by the GST Law.

GST Amount means in relation to a Taxable Supply the amount of GST payable in respect of that Taxable Supply.

GST Group has the meaning given by the GST Law.

GST Law has the meaning given by the *A New Tax System (Goods and Services Tax) Act 1999* (Cth).

Guidelines means the guidelines made by the ESC under the *Rail Corporations Act*.

Hazardous Substance means any substance, which would or might reasonably be expected to cause injury to any person exposed to that substance.

Incident means a breakdown, accident, emergency, event or circumstance on or affecting the Network that causes, or may reasonably be expected to cause:

- (a) the safety of a Train or any persons to be jeopardised;
- (b) serious injury to or death of any person;
- (c) material damage to the property of any person;
- (d) delay or obstruction to the use of the Network; or
- (e) collision, derailment, signalling failure or serious safeworking breach,

and any other railway accident or incident that the Access Provider or the Operator is required to investigate under any applicable Law.

Incremental Costs means additional costs that are reasonably incurred by the Access Provider as a direct result of providing access to the Operator, where these costs are over and above the costs that have been taken into account in setting the Access Charge. Without limitation, Incremental Costs may be one-off costs incurred by the Access Provider in providing a requested path to the Operator.

For the avoidance of doubt, there are no such additional costs as at the commencement of this Agreement.

Indirect or Consequential Loss means economic loss, consequential loss, loss of profits, loss of business opportunity, payment of liquidated sums, penalties or damages under any agreement (other than this Agreement).

Industrial Waste means any waste arising from commercial, industrial or trade activities and any waste containing substances or materials, which are potentially harmful to human beings or the Environment.

Infrastructure Lease means the lease titled "Infrastructure Lease - Train" between the Director, VRTC and the Access Provider dated 31 August 2009, as amended

Initial Term means the term described in clause 2.2.

Input Tax Credit has the meaning given by the GST Law.

Issuer means:

- (a) an authorised deposit-taking institution, as defined in section 5(1) of the *Banking Act 1959* (Cth); or
- (b) any other person whose usual business includes the issue of performance bonds or insurance bonds (as the case may be) and who is approved by the Access Provider.

Law means any statute, regulation, order, rule, subordinate legislation or other document enforceable under any statute, regulation, order, rule or subordinate legislation.

Metropolitan Master Working Timetable means the timetable and Addenda showing all of the scheduled train paths for Trains on the Network, as amended from time to time.

Negotiation Guidelines means the Guidelines made by the ESC under section 38V of the *Rail Corporations Act*.

Network means the land and infrastructure leased by the Access Provider under the Infrastructure Lease from time to time, including railway track, associated track structures and works (such as cuttings, tunnels, bridges, sidings, excavations, landfill, track support earthworks and drainage works), pedestrian crossings, over-track structures, under-track structures, service roads, signalling, notices and signs and overhead electrical power supply systems, but excluding:

- (a) buildings (including stations, platforms, sheds and shelters);
- (b) carparks;
- (c) terminals, storage and receival facilities;
- (d) workshops, depots, yards and fuel points; and
- (e) private sidings that are not leased to the Access Provider,

but includes any infrastructure leased to the Access Provider which passes through, or is immediately adjacent to, any of the infrastructure or facilities referred to in paragraphs (a) to (e) above.

Network Operating Requirements means the regulations and standards set out in the Metropolitan Master Working Timetable and Addenda, as published by the Access Provider from time to time.

Deleted: Incremental Costs means additional costs that may be incurred by the Access Provider in providing access to the Operator, where these costs are over and above the costs that have been taken into account in setting the standard Reference Service Access Charge.¶

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Notice has the meaning given in Clause 21.

Operating Procedures means the procedures that apply to operations on the Network, as published by the Access Provider from time to time.

Operational Control means the control exercised, or which may be exercised, by the Access Provider with regard to the management, continuity and safeworking of the Network and all operational matters incidental to that control and includes procedures and requirements relating to Train control, Train and Rolling Stock movements, track restrictions, Track Occupations, safeworking practices, operating restrictions, emergency response procedures, notification of authorities, network restoration procedures, maintenance of the Network, evacuation procedures and Incident investigation procedures.

Operational Directions means the lawful instructions, directions and notifications from time to time issued by the Access Provider with regard to Operational Control.

Operational Interface Procedures means the procedures that apply to operational interfaces on the Network as published by the Access Provider from time to time.

Operational Performance Regime or **OPR** means the Operational Performance Regime established by the Franchise Agreement

Operator's Scheduled Train Path means each Train Path described in Schedule 2, as varied from time to time under this Agreement.

Operator's Unscheduled Train Path means a Train Path allocated to the Operator pursuant to Clause 3.2, as varied from time to time under this Agreement.

OPR Incentive Payment means any amount payable by the Access Provider to the Director, or reduction of an amount payable to the Access Provider by the Director, under the Operational Performance Regime.

Passenger Train means a Train used to carry passengers for reward and includes such a Train when it is empty.

Performance Bond means an irrevocable bank guarantee, letter of credit or insurance bond callable by the Access Provider in a form approved by the Access Provider.

Performance Bond Amount means:

- (a) at the Effective Date \$[insert]; and
- (b) at each Trigger Date, the amount set out in paragraph (a) multiplied by the CPI Multiplier as at the Trigger Date.

Quarter means any calendar quarter commencing on 1 January, 1 April, 1 July or 1 October in any year, provided that:

- (a) the first Quarter commences on the Effective Date and ends on the next 31 December, 31 March, 30 June or 30 September (whichever first occurs); and
- (b) the last Quarter commences on the last 1 January, 1 April, 1 July or 1 October (whichever last occurs) and ends on the termination of this Agreement.

Rail Corporations Act means the *Rail Corporations Act* 1996 (Vic).

Reference Service has the meaning given in the Access Arrangement.

Reference Tariff means the ESC approved access charge submitted in Metro's Access Arrangement.

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Related Body Corporate has the meaning given in the *Corporations Act*.

Required Rating means a credit rating of at least A (Standard & Poor's) or A2 (Moody's)

Rolling Stock means any vehicle that operates on or uses a railway track including a locomotive, light rail vehicle, light inspection vehicle, road/rail vehicle, trolley, carriage, diesel multiple unit and wagon (but does not include a vehicle designed to operate both on and off a railway track when the vehicle is not operating on a railway track).

Rolling Stock Standards means Australian Standard AS4292 in so far as it applies to Rolling Stock, as amended from time to time.

Safety Interface Agreement has the meaning given to that term in the Rail Safety Act 2006 (Vic).

Scheduled Train Path means a Train Path that is set out in the Metropolitan Master Working Timetable.

Service means a freight rail service provided by the Operator by utilization of rights conferred under this Agreement.

Special Event means a sporting, cultural, musical or other event which requires additional or varied services to be provided by passenger train operators.

Stabling means the parking or laying up of Rolling Stock which is necessary or expedient for giving full effect to the movements of the Rolling Stock required for the operation of Services.

Standards means any applicable standards and codes issued from time to time by Standards Australia including, without limitation, the Rolling Stock Standards.

State means the State of Victoria.

Taxable Supply has the meaning given in the GST Law.

Third Party Operator means a person other than the Access Provider or the Operator who has the right to access the Network for the provision of rail services.

Track Occupation means access to the Network in order to carry out inspections, repairs, maintenance, up-grade work, improvements, additions or any other works, which could interfere with the Operator's Services.

Track Occupation Protocol means the Metropolitan Track Occupation protocol published by the Access Provider from time to time.

Train means Rolling Stock coupled together to operate as a single unit.

Train Manifest has the meaning given in Clause 3.8.

Train Operating Protocol means the Metropolitan Train Operating Protocol issued by the Access Provider, as amended from time to time.

Train Path means the particular time interval, including an entry time and day and an exit time and day, through which a Train may travel over a segment of the Network from an origin to a destination, including stopping points, and includes an:

- (a) Operator's Scheduled Train Path; and

(b) Operator's Unscheduled Train Path.

Train Path Request Process and Protocol means the Access Provider's process and protocol for seeking Train Paths under the Negotiation Guidelines.

Transport Act means the *Transport Integration Act 2010 (Vic)*.

Unscheduled Train Path means a Train Path that is not a Scheduled Train Path.

Valid Request has the meaning given in Clause 3.2.

VLP means V/Line Pty Ltd

VLP Access Agreement means the access agreement between the Access Provider and VLP.

VRTC means Victorian Rail Track Corporation.

Working Instruction means an operational or safety instruction issued by the Access Provider from time to time as a requirement under the documents listed in Clause 11.1 of this agreement.

1.2 Interpretation

Headings are for convenience only and do not affect interpretation. The following rules apply unless the context requires otherwise.

- (a) The singular includes the plural and conversely.
- (b) A gender includes all genders.
- (c) If a word or phrase is defined, its other grammatical forms have a corresponding meaning.
- (d) A reference to includes or including should be construed without limitation.
- (e) A reference to a person, corporation, trust, partnership, unincorporated body or other entity includes any of them.
- (f) A reference to a Clause, Schedule or Annexure is reference to a clause of, or a schedule or annexure to, this Agreement and a reference to a paragraph is to a paragraph of the same Clause or Schedule unless the context requires otherwise.
- (g) A reference to an agreement or document (including a reference to this Agreement) is to the agreement or document as amended, varied, supplemented, novated or replaced, except to the extent prohibited by this Agreement or that other agreement or document.
- (h) A reference to a party to this Agreement or another agreement or document includes the party's successors, permitted substitutes and assigns (and, where applicable, the party's legal personal representatives).
- (i) A reference to legislation or to a provision of legislation includes a modification or re-enactment of it, a legislative provision substituted for it and a regulation or statutory instrument issued under it.
- (j) A reference to conduct includes an omission, statement and undertaking, whether or not in writing.

- (k) A reference to an agreement includes any undertaking, deed, agreement and legally enforceable arrangement whether or not in writing and a reference to a document includes an agreement (as so defined) in writing and any certificate, notice, instrument and document of any kind.
- (l) A reference to writing includes a facsimile transmission and any means of reproducing words in a tangible and permanently visible form.
- (m) A reference to any professional body includes the successors of that body.
- (n) A reference to a year or to a month is a reference to a calendar year or a calendar month respectively.
- (o) A reference to dollars and \$ is to Australian currency.
- (p) A reference to *party* is a reference to a party to this Agreement.

1.3 Consents or approvals

If the doing of any act, matter or thing under this Agreement is dependent on the consent or approval of a party or is within the discretion of a party, the consent or approval may be given or the discretion may be exercised conditionally or unconditionally or withheld by the party in its absolute discretion unless express provision to the contrary has been made.

1.4 Payments due on Business Days

If any amount becomes payable under this Agreement on a day which is not a Business Day, that amount is payable on the next Business Day.

1.5 Inconsistency

If there is any inconsistency between this Agreement and any of the documents listed in Clause 15, this Agreement will prevail to the extent of any inconsistency and the documents listed in Clause 15 will be construed accordingly.

1.6 Good Faith

The parties must act co-operatively and in good faith with respect to performance of their obligations under this Agreement.

1.7 Trust Provision

The benefit of any release or indemnity in favour of the Access Provider's Associates contained in this Agreement is held on trust for each of them by the Access Provider and may be enforced for each of their benefit by the Access Provider.

2 Term

2.1 Commencement Date

This Agreement commences on the Effective Date.

2.2 Expiry Date

Unless otherwise terminated or extended in accordance with clause 2.3, this Agreement will expire on:

- (a) [TBC]; or
 - (b) termination or expiry of the Infrastructure Lease,
- (whichever first occurs).

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2.3 Option to extend term

- (a) At least 6 months prior to the expiry of the Initial Term, the Operator may give the Access Provider notice that it proposes to extend the term.
- (b) On receipt of the notice described in paragraph (a), the parties agree to meet to negotiate the period for which this Agreement will be renewed (**Extended Period**).
- (c) This Agreement will continue to apply for the duration of the period of negotiation, which must not be longer than 2 months (**Negotiation Period**), and any agreed Extension Period, and this Agreement will expire on the earlier of:
 - (i) end of the Negotiation period if no agreement on the Extended Period;
 - (ii) end of the Extended Period; or
 - (iii) termination or expiry of the Infrastructure Lease.
- (d) The Operator cannot exercise the option in paragraph (a) if the Initial Term is expiring because the Infrastructure Lease has been terminated or expired.

3 Access Rights

3.1 Scheduled Train Paths

- (a) The Access Provider must allow the Operator to have access to the Network by way of the Operator's Scheduled Train Paths, subject to and on the terms and conditions of this Agreement.
- (b) The Operator's Scheduled Train Paths may only be permanently varied pursuant to Clause 5.
- (c) The Operator may only apply for additional Scheduled Train Paths pursuant to clause 5.

3.2 Unscheduled Train Paths

- (a) The Operator and the Access Provider may each request an Unscheduled Train Path in accordance with the procedure set out below. In order to be valid such a request (a **Valid Request**) must:

- (i) be received in writing by the Access Provider or the Operator (as applicable) at least 48 hours in advance of the proposed operation of each such Unscheduled Train Path;
 - (ii) specify the Train Path sought and provide details of the Train sought to be run;
 - (iii) in the case of a request by the Operator, include such evidence as the Access Provider reasonably requires of the Operator's Accreditation in respect of operation of the particular Train; and
 - (iv) be consistent with the Network Operating Requirements and the Book of Rules and Operating Procedures or other agreed specifications or procedures as determined by the Access Provider.
- (b) Subject to the Capacity Use Rules (if relevant), the Access Provider may not allocate an Unscheduled Train Path the subject of a Valid Request from itself, the Operator or any other person if that Unscheduled Train Path would conflict with:
- (i) a Scheduled Train Path of the Operator;
 - (ii) a Train Path of the Access Provider that is set out in the Metropolitan Master Working Timetable;
 - (iii) a Train Path for a Passenger Train;
 - (iv) compliance rules set out in the Addenda; or
 - (v) a Train Path that the Access Provider is contractually obliged to provide to, or reserve for, a Third Party Operator (including an "ad hoc" Train Path).

The Access Provider must make a determination as to whether Train Paths conflict in accordance with the matters set out in the Addenda to the Metropolitan Master Working Timetable.

- (c) Subject to the Capacity Use Rules, if the Access Provider receives a Valid Request for an Unscheduled Train Path from the Operator which it may allocate under paragraph (b), then the Access Provider must allocate to the Operator the Unscheduled Train Path requested by the Operator, unless the Unscheduled Train Path requested would conflict with an Unscheduled Train Path the subject of another Valid Request from the Access Provider or a Third Party Operator in which case the Access Provider must allocate an Unscheduled Train Path in accordance with the following priority rules:
- (i) first, to the Access Provider for any train movements associated with passengers trains;
 - (ii) secondly, to the Operator or a Third Party Operator wishing to run Passenger Trains (with the Access Provider to determine any conflict between such persons acting reasonably); and
 - (iii) thirdly, to the Operator or a Third Party Operator wishing to run Freight Trains (with the Access Provider to determine any conflict between such parties acting reasonably).

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- (d) The Access Provider must respond to any request for an Unscheduled Train Path by the Operator at least 24 hours prior to the entry time of the Unscheduled Train Path requested.
- (e) If the Access Provider refuses to allocate the Operator an Unscheduled Train Path requested by the Operator, the Access Provider must provide the Operator with a written statement of the Access Provider's reasons for refusing to allocate the Operator the Unscheduled Train Path requested and, if requested to do so by the Operator, offer the Operator the closest available Unscheduled Train Path (applying the priority rules in paragraph (c)).
- (f) If the Access Provider allocates the Operator an Unscheduled Train Path, the Access Provider must allow the Operator to have access to the Network by way of that Unscheduled Train Path, subject to and on the terms and conditions of this Agreement.
- (g) The Access Charge payable by the Operator will continue to be calculated in accordance with Clause 4 and as set out in Schedule 1 even if the Operator is allowed an Unscheduled Train Path pursuant to this Clause 3.2. An Unscheduled Train Path will be paid for on the basis set out in Clause 4 and Schedule 1.
- (h) The Operator must notify the Access Provider as soon as practicable after it becomes aware that it will not use an Unscheduled Train Path. The Access Provider will then be free to allocate that Unscheduled Train Path to any other person providing freight, passenger or any other services on the Network whether on the same or different terms and conditions to those offered to the Operator.
- (i) The Operator acknowledges that the allocation of an Unscheduled Train Path on any particular occasion does not represent an ongoing entitlement to that Train Path or any indication that the Train Path will be available in the future.
- (j) Nothing in this Clause 3.2 prevents the Operator from requesting more than one Unscheduled Train Path.

3.3 Ancillary Movements

- (a) The Access Provider must allow the Operator access to the Network to make Ancillary Movements that are necessary or reasonably required for the operation of Train Path allocated to the Operator subject only to Operational Directions.
- (b) Without limiting paragraph 3.3(a) the Access Provider must allow the Operator:
 - (i) to enter, with or without vehicles other than Rolling Stock; and
 - (ii) to bring and keep other equipment,
 on the Network subject to any conditions set by the Access Provider in the procedures and protocols listed in clause 11.1.
- (c) When accessing the Network in the manner described in paragraph (a);

- (i) the Operator must obtain the prior consent of the Access Provider; and
- (ii) the Operator must comply with any Operational Direction made by the Access Provider relating to the moving of any vehicle or other equipment brought onto the Network.

3.4 Use of Access Rights

- (a) The Operator may not access or use any part of the Network except for the purpose of:
 - (i) operating Freight Trains, or
 - (ii) making Ancillary Movements,as may apply to the Operator requiring access.
- (b) The Operator must not access or attempt to access the Network in any way other than is authorised by this Agreement.

3.5 Limits on Train Path Availability

The availability of a Train Path is subject to:

- (a) daily variations to a scheduled Train Path made by the Access Provider in creating a Daily Train Plan;
- (b) Operational Directions given by the Access Provider; and
- (c) the matters contained in Clause 5.

If an Operator's Train Path is varied according to this clause 3.5 the Access Provider will use reasonable endeavours to make a similar alternative Train Path available to the Operator.

3.6 Safe Network

The Access Provider must maintain the Network and exercise Operational Control so as to allow the Operator to provide its Services safely.

3.7 Non Exclusive

The Operator's right to access the Network is non-exclusive. Subject to the Access Provider providing access in accordance with this Agreement, nothing contained or implied in this Agreement prevents or limits the Access Provider or any other person from conducting freight, passenger or other services on the Network whether on the same or on different conditions to those enjoyed by the Operator.

3.8 Train Manifest

Prior to operating a Train on the Network (other than an Ancillary Movement) the Operator must provide the Access Provider with a written notice (a *Train Manifest*) specifying:

- (a) the number and type of vehicles in the Train;
- (b) the gross mass of the Train;
- (c) the length of the Train;

- (d) the motive power employed by the Train;
 - (e) any disclosure required under the Dangerous Goods Code; and
 - (f) such other reasonable information as the Access Provider requires,
- which will be accurate in all material respects.

3.9 Updates to manifest

The Operator must notify the Access Provider in writing immediately if it wishes to alter any of the information given to the Access Provider under Clause 3.8.

4 Access Charge

4.1 Access Charge

The Operator must pay to the Access Provider the Access Charge set out in **Schedule 1** as varied in accordance with this Agreement.

4.2 Variation for Inflation

- (a) On and from 1 July each Financial Year (commencing on 1 July ~~2011~~), each dollar figure component of the Access Charge set out in Schedule 1 will be varied in accordance with the following formula:

$$A_n = A_{n-1} \times \text{CPI Multiplier} \times (1-X)$$

where,

A_n = The relevant element of the Access Charge to apply from 1 July of the Financial Year 'n' (commencing on 1 July TBC).

A_{n-1} = The relevant element of the Access Charge that applied from 1 July of the Financial Year 'n-1'

X = The "x factor = 1%" as approved by the ESC for the Reference Service.

- (b) If CPI is not published for any reason the parties will endeavour to agree on a substitute index. If the parties fail to agree by 30 April in any given year, either party may refer the question of an appropriate substitute index to an independent expert for resolution under Clause 19.3.

4.3 Variation for Extended Period

The Access Charge may be varied for the Extended Period to reflect any change in the Reference Tariff during the Extended Period due to a new ESC approved Access Provider's Access Arrangement.

4.4 Incremental costs

- (a) The Operator must pay any Incremental Costs to the Access Provider. Where any Incremental Costs are attributable to both the Operator and any Third Party Operator, the Access Provider will make a reasonable

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allocation of those Incremental Costs as between the Operator and the Third Party Operator (based on a causal allocator).

- (b) The Access Provider must use all reasonable endeavours to ensure that the Operator is informed of the nature and likely amount of any Incremental Costs before they are incurred.
- (c) Upon request the Access Provider will provide the Operator with an explanation of both the costs incurred and the method used to allocate the Incremental Costs.
- (d) The Access Provider will take into account any additional information the Operator provides that it believes could materially change the method of allocation of the Incremental Costs.

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4.5 Invoices

- (a) The Access Provider must deliver to the Operator within a reasonable period after the end of each month (commencing on the Effective Date) a Tax Invoice setting out the Access Charge or other amounts payable by the Operator to the Access Provider under this Agreement with respect to the previous month or such other period as may be described in the invoice. The invoice must be accompanied by a statement setting out in reasonable detail the calculation of the amounts shown in the invoice so that they can be determined to be in accordance with the provisions of this Agreement.
- (b) The Operator must pay the amount invoiced in accordance with paragraph (a) within 20 Business Days after the day the invoice is delivered.
- (c) The amount claimed in the Access Provider's invoice will be conclusive in the absence of manifest error demonstrated by the Operator.

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4.6 Objection to invoiced amount

- (a) If the Operator has a bona fide objection to the amount claimed under any invoice it may notify the Access Provider of the objection in writing, but must pay the invoice in full.
- (b) The failure by the Operator to object to an invoice prior to the due date for payment or actual payment will not prejudice the Operator's right to dispute the amount of the invoice.
- (c) If an adjustment is subsequently agreed between the parties or determined under clause 19, the Access Provider may set-off the amount of the adjustment in a subsequent invoice. Except where the amount that the Access Provider sets-off to the Operator results from incorrect information provided by the Operator to the Access Provider, the Access Provider must pay interest to the Operator at the Default Rate on that amount accrued daily from the time that the Operator paid the amount until the Access Provider allows an adjustment in a subsequent invoice.
- (d) If the Access Provider makes an error in an invoice, it may adjust a subsequent invoice to correct the error. The Access Provider must provide a reasonable explanation to the Operator of the nature of any such error.

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4.7 Interest on late payment

- (a) If the Operator fails to pay any amount payable by it under this Agreement by the due date, the Operator must, if demand is made by the Access Provider, pay interest at the Default Rate on the unpaid amount accrued daily from the time it falls due until the amount has been paid in full.
- (b) The right to demand payment of interest under this Clause 4.6 is without prejudice to any other rights and remedies that the Access Provider may have in respect of a payment default under this Agreement.

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4.8 Set Off

- (a) A party (the first party) may set off against any amount due and payable under this Agreement by the first party to the other party, any amount due and payable under this Agreement by the other party to the first party. The first party must notify the other party in writing if it exercises this right.

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4.9 Resetting of Access Charge

Subject to clause 4.2, Access Charge for the Reference Service will be reset at the expiry of the Access Arrangement and (if applicable) if the Access Arrangement is varied by the ESC pursuant to the *Rail Corporations Act*.

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4.10 Performance Bond

- (a) The Operator must, on or before the Effective Date, procure the issue to the Access provider of a Performance Bond which:
 - (i) is issued by an Issuer with a Required Rating and approved by the Access Provider (which approval must not be unreasonably withheld);
 - (ii) has a face amount which is no less than the Performance Bond Amount;
 - (iii) expires no earlier than the second anniversary of the Effective Date; and
 - (iv) is payable at an office of the Issuer in Melbourne.
- (b) The Operator must, on or prior to each Trigger Date, procure the issue to the Access Provider of a replacement Performance Bond which:
 - (i) complies with the requirements of Clauses 4.9(a)(i) and (iv);
 - (ii) has a face amount which is no less than the Performance Bond Amount as at the relevant Trigger Date; and
 - (iii) expires no earlier than the second anniversary of the relevant Trigger Date.
- (c) The Access Provider may make a demand under the Performance Bond on account of, and apply the Performance Bond against, any amount which the Access Provider considers is due and payable or will be due and

payable by the Operator to the Access Provider due to a breach of this Agreement by the Operator.

- (d) The Access Provider must return to the Operator an existing Performance Bond once it has received a replacement Performance Bond.
- (e) The Access Provider must, subject to any rights the Access Provider may have in relation to the Performance Bond, return the Performance Bond (less any amounts drawn under Clause 4.9(c)) to the Operator within 12 months after the termination or expiry of this Agreement.
- (f) The Access Provider must as soon as practicable after it has made a demand under the Performance Bond, give a notice to the Operator specifying the Access Provider's reasons for making the demand.
- (g) The Access Provider may only make a demand under the Performance Bond in accordance with this Clause 4.9.
- (h) The Access Provider may make a demand irrespective of whether or not the amount is or the circumstances relating to the amount are:
 - (i) in dispute between the parties;
 - (ii) subject to any court or other proceedings.
- (i) The Operator must not take any steps to restrain or injunct the Access Provider from making a demand under the Performance Bond or the Issuer paying any amounts under the Performance Bond.
- (j) If at any time after the Effective Date, the Issuer of the Performance Bond ceases to have the Required Rating, the Operator must procure the issue of a replacement Performance Bond which complies with Clause 4.9(a) or 4.9(b) (whichever is applicable).
- (k) If the Operator does not comply with Clause 4.9(b) or 4.9(j), the Access Provider may call down on the full value of the Performance Bond and hold the amount so drawn as cash until:
 - (i) the Operator complies with Clause 4.9(b) or 4.9(j), (whichever is applicable); or
 - (ii) if the Operator does not comply with Clauses 4.9(b) or 4.9(j), until 4.9(e) would have applied had a Performance Bond been held.
- (l) If the Access Provider is holding the amount of the Performance Bond as cash pursuant to Clause 4.9(k) and the Operator subsequently complies with Clause 4.9(b) or 4.9(j) (whichever is applicable), the Access Provider must as soon as is practicable return the cash to the Operator (for the avoidance of doubt, without any interest being owed in respect of such cash).
- (m) If the Access Provider makes a demand under the Performance Bond and receives payment of an amount which was not actually payable by the Operator to the Access Provider, the Access Provider will repay that amount together with interest at the Default Rate on that amount.

5 Variations to Train Paths

5.1 Variation Due to the Director

- (a) If the Director approves, varies or approves the variation of the Metropolitan Master Working Timetable in accordance with section 10 of the Transport Act, the Access Provider may vary the Operator's Scheduled Train Paths to the extent necessary to accommodate the variation to the Metropolitan Master Working Timetable.
- (b) In exercising its rights under clause 5.1(a) the Access Provider and the Operator must comply with the applicable requirements of the Capacity Use Rules.
- (c) If a Scheduled Train Path is cancelled by the Access Provider under clause 5.1(a), it will cease to be an Operator's Scheduled Train Path.

5.2 Permanent Variation Requested by Operator

- (a) If the Operator requests a permanent variation to an Operator's Scheduled Train Path, the Access Provider must:
 - (i) negotiate with the Operator in good faith; and
 - (ii) use all reasonable endeavours to vary the Scheduled Train Path so long as such variation does not interfere with a Train Path of the Access Provider or any Third Party Operator.
- (b) If the Operator is seeking an additional Scheduled Train Path it must make a fresh application to the Access Provider under the Train Path Request Process and Protocol.

5.3 Permanent Variations of Unscheduled Train Path

The Access Provider may, by giving not less than 30 days notice in writing to the Operator, vary an Operator's Unscheduled Train Path in order to make it available as a Scheduled Train Path for the Access Provider or any Third Party Operator.

5.4 Variation or Surrender due to Operator Breach

- (a) Without limiting clause 17 but subject to clause 5.4(b), the Access Provider may, acting reasonably, taking into account all relevant circumstances and after consultation with relevant authorities (if required), by notice in writing to the Operator permanently vary, temporarily vary or require the Operator to surrender a Train Path if the Operator:
 - (i) breaches a relevant Law;
 - (ii) breaches a relevant Standard;
 - (iii) has its Accreditation suspended or cancelled;
 - (iv) fails to comply with the Book of Rules and Operating Procedures;
 - (v) breaches the Access Provider's rolling stock interface standards as contained in the Addenda or the Rolling Stock Standards;

- (vi) fails to comply with the Access Provider's material requirements for the operation of Rolling Stock on the Network including any of the Access Provider's Protocols,
- (b) In relation to a breach by the Operator under clause 5.4(a)(iv) and in relation to a particular Train Path, the Access Provider may only temporarily vary Train Paths to the extent necessary to avoid the relevant breach.
- (c) If a Train Path is cancelled by the Access Provider under clause 5.4(a), it will cease to be an Operator's Scheduled Train Path or Operator's Unscheduled Train Path (as applicable).

5.5 Variation or Surrender Due to Capacity Use Issues

[Freight Only]

Subject to the Capacity Use Rules:

- (a) The Access Provider ~~may on giving not less than 30 days notice to the~~ Operator require variation of an Operator's Scheduled Train Path or an Operator's Unscheduled Train Path in accordance with Sections 5.5 or 5.6 of the Capacity Use Rules or the Capacity Allocation Protocols. Deleted: must
- (b) If a Train Path is cancelled by the Access Provider under clause 5.5(a), it will cease to be an Operator's Scheduled Train Path or an Operator's Unscheduled Train Path (as applicable) upon the expiration of the relevant notice period.

5.6 Temporary Variations by Access Provider

- (a) The Access Provider may temporarily vary an Operator's Scheduled Train Path or an Operator's Unscheduled Train Path by notice to the Operator in any of the following circumstances:
 - (i) for reasons related to safety (including, without limitation, because of an Incident, a Force Majeure Event or track speed restrictions);
 - (ii) ~~to the extent necessary to effect~~ the repair, maintenance, upgrading, extension, construction or alteration of the Network or rail infrastructure; Deleted: in connection with
 - (iii) in order to permit a Track Occupation;
 - (iv) at the request of the Operator, where the variation does not interfere with a Train Path of the Access Provider or any Third Party Operator; or
 - (v) where the variation is for the purpose of providing Passenger Train services for a Special Event.
- (b) In exercising its powers under clause 5.6(a) the Access Provider must:
 - (i) comply with the Access Provider's Protocols (as applicable) and the terms of any contractual obligations of the Access Provider to Third Party Operators; and

- (ii) vary and re-allocate Train Paths in accordance with Section 5.7(b) of the Capacity Use Rules, taking into account any contractual obligations of the Access Provider.
- (c) Subject to complying with clause 5.6(b), the Access Provider must use all reasonable endeavours to minimise disruption to rail services on the Network, including, without limitation, the Operator's Services.
- (d) Subject to complying with clause 5.6(c), the Access Provider must use all reasonable endeavours to provide satisfactory alternative Train Paths to affected rail operators, including the Access Provider, the Operator and Third Party Operators and to provide reasonable notice to affected rail operators.

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6 Operational Control

6.1 Nature of Exercise

- (a) In accordance with its Accreditation requirements, the Access Provider will:
 - (i) exercise Operational Control in accordance with the Train Operating Protocol and the Book of Rules (as amended) and Operating Procedures (as amended); and
 - (ii) maintain Operational Control over the Network in accordance with any Law from time to time applicable in Victoria with regard to such control.
- (b) The Access Provider may exercise Operational Control by issuing Operational Directions to the Operator.

6.2 Extent of Exercise

The Access Provider may in exercising Operational Control delay, add, cancel, re-route or re-schedule Train movements including any Train Path allocated under this Agreement to the extent necessary for the safety and operational efficiency of the Network. The Access Provider must use reasonable endeavours to minimise the extent of such changes and to accommodate any reasonable request made by the Operator as to the extent and nature of such changes.

6.3 Responsibility of Operator to Comply

The Operator must at all times promptly comply with all Operational Directions and the Communications Protocol.

6.4 Communication Responsibilities

- (a) In accordance with its Accreditation requirements, the Access Provider will:
 - (i) keep the Operator properly and promptly informed of any event, activity or Incident becoming known to the Access Provider that will,

or is reasonably likely to, prevent or materially limit the operation of a Service by the Operator;

- (ii) provide to the Operator in a timely manner (which it may do through publication on a website or other electronic means) all published regulations, standards, practices, instructions, directions and notifications from time to time applicable in Victoria relating to Operational Control or the Network Operating Requirements to the extent that those regulations, standards, practices, instructions, directions and notifications are relevant to the operation of the Services;
- (iii) operate and maintain a train control centre;
- (iv) operate and maintain, or cause another person to do so, a communications system in respect of the Network for the purposes of communications with the Operator and other rail users of the Network and facilitate the Operator's access to that communications system in accordance with the Communications Protocol; and
- (v) notify the Operator of any variations to the website which directly relate to any protocols which must be followed by or relate to other obligations of the Operator.

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(b) The Operator must:

- (i) notify the Access Provider promptly after the Operator becomes aware of any actual or potential changes to the Operator's Train movements which are not or which may not be in accordance with the Daily Train Plan; and
- (ii) ensure that all Trains under the control of the Operator are equipped with fully operational and compatible communications equipment to enable immediate communications between the Access Provider and the Trains of the Operator on the Network.

(c) The Access Provider must comply with the Communications Protocol.

7 Track Standard

7.1 Fit for Purpose

The Access Provider must at all times maintain those parts of the Network to which the Operator has access pursuant to the Scheduled Train Paths so as to ensure those parts of the Network are fit for the purpose of the Operator running Freight Trains on those parts of the Network in accordance with the Addenda to the Metropolitan Master Working Timetable.

7.2 Axle Weight

a) The Access Provider must maintain those parts of the Network to which the Operator has access pursuant to the Scheduled Train Paths so that a Freight

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Train can operate on the relevant part of the Network with the maximum axle weight specified in the Addenda to the Metropolitan Master Working Timetable for that part of the Network.

- b) The Access Provider will use reasonable endeavours to consult where practical with the Operator before reducing the maximum weight specified in the Addenda. Unless the reduction is required for safety reasons (as reasonably determined by the Access Provider), by a Law, a Government Agency, or the terms of Access Provider's agreement with a Government Agency.
- c) The Access Provider will notify the Operator of any reduction to the maximum axle weight.

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7.3 Track Speed

- a) The Access Provider must maintain those parts of the Network to which the Operator has access pursuant to the Scheduled Train Paths so that a Freight Train can operate on the relevant parts of the Network at the maximum speed specified in the Addenda to the Metropolitan Master Working Timetable for that part of the Network.
- b) The Access Provider will use reasonable endeavours to consult where practical with the Operator before reducing the maximum speed specified in the Addenda. Unless the reduction is required for safety reasons (as reasonably determined by the Access Provider), by a Law, a Government Agency, or the terms of Access Provider's agreement with a Government Agency.
- c) The Access Provider will notify the Operator of any reduction to the maximum track speed.

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8 Undertakings and Warranties

8.1 Undertakings and Warranties

In addition to and notwithstanding all other warranties express or implied in this Agreement, the Operator undertakes and warrants to the Access Provider that:

- (a) it is duly incorporated and is empowered to enter into this Agreement and to do all things that it is required to do by this Agreement;
- (b) it has the resources and ability to perform all of its obligations under this Agreement;
- (c) all things have been done or will be done as may be necessary to render this Agreement legally enforceable in accordance with its terms and fully valid and binding on it;
- (d) all authorisations by any Governmental Agency that are required or will be required in connection with the execution and delivery of, the performance of obligations under or the validity or enforceability of, this Agreement,

including the Accreditation, have been obtained or effected and are fully operative and in full force and effect;

- (e) there is no litigation, arbitration or administrative proceedings taking place, pending or, to its knowledge, threatened against it which could have a material adverse effect on its ability to perform its obligations under this Agreement;
- (f) it will as soon as practicable notify the Access Provider of the occurrence of, or pending or threatened occurrence of, any event that may cause or constitute a material breach of any of the acknowledgments, representations, warranties or covenants of the Operator under this Agreement and any event that could have a material adverse effect on its ability to perform its obligations under this Agreement;
- (g) it has prior to the date of this Agreement and after reasonable enquiry and investigation disclosed to the Access Provider all information that the Access Provider has requested under Clause 3(b) of the Negotiation Guidelines, being information that could reasonably be regarded as affecting to a substantial extent the decision of the Access Provider to enter into this Agreement or to allocate a Train Path to the Operator;
- (h) it has taken all reasonable steps to ensure that no statement or representation made by it or on its behalf to the Access Provider in negotiations antecedent to this Agreement or to the allocation of a Train Path is misleading or deceptive in any material respect.

8.2 Time of giving undertakings and warranties

The undertakings and warranties set out in Clause 8.1 will be taken to be given and made:

- (a) on the date of execution of this Agreement;
- (b) on the date of the Operator requesting access under this Agreement; and
- (c) on each day on which the Access Provider grants any access to the Operator or the Operator operates any Service on the Network.

9 Compliance with Laws and Standards

Without limiting any of its obligations under this Agreement, the Operator must comply with all requirements of any Law or Standards from time to time applicable to its operations.

10 Accreditation

10.1 Operator Accreditation requirements

- (a) The Operator must hold Accreditation to the extent required to operate its Services and perform its obligations under this Agreement.
- (b) The Operator must to the extent required by Law ensure that its employees, agents and contractors engaged in or in connection with the operation of

the Services are acceptable to or approved by the agency or authority from time to time responsible for Accreditation.

- (c) The Operator must keep the Access Provider promptly informed of all material variations in the Accreditation of the Operator and to the conditions of the Operator's Accreditation.
- (d) The Operator must comply with all requirements as to Accreditation, including all requirements relating to Rolling Stock.
- (e) The Operator must not operate Rolling Stock on the Network to the extent it does not hold Accreditation necessary to do so.

10.2 Information as to Accreditation

Without limiting any other provision of this Agreement, the Operator must give the Access Provider such evidence as the Access Provider reasonably requires to demonstrate that the Operator meets the requirements set out in Clause 10.1.

10.3 Access Provider Accreditation Requirements

The Access Provider must immediately notify the Operator if it ceases to hold the necessary Accreditation to enable it to provide access to the Network for the Operator under this Agreement.

11 Operator's obligations in using the Network

11.1 Familiarity with procedures and protocols

Before accessing the Network, the Operator must request and obtain from the Access Provider, the latest published versions of and provide to all relevant personnel the following documents:

- (a) Metropolitan Master Working Timetable;
- (b) Addenda;
- (c) Book of Rules;
- (d) Operating Procedures;
- (e) Rolling Stock Standards;
- (f) Network Operating Requirements;
- (g) Emergency Response Plan;
- (h) Train Operating Protocol;
- (i) Operational Interface Procedures;
- (j) Track Occupation Protocol;
- (k) Communications Protocol; and
- (l) such other procedures and protocols as the Access Provider publishes and makes available to operators of rail services on the Network.

11.2 Book of Rules and Operating Procedures

The Operator must, when accessing the Network, comply with the Book of Rules and the Operating Procedures.

11.3 Rolling Stock Specifications

The Operator must:

- (a) maintain all Rolling Stock used by the Operator on the Network so that it at least satisfies the Rolling Stock Standards;
- (b) ensure that all Rolling Stock used by the Operator on the Network is equipped with fully operational safety equipment, which is compatible with the safe working systems used by the Access Provider; and
- (c) comply with the Operational Interface Procedures.

11.4 Protocols

The Operator must when accessing the Network comply with the Access Provider's Protocols and any Working Instructions issued by the Access Provider.

11.5 Network Operating Requirements

- (a) The Operator must in accessing the Network pursuant to this Agreement comply with the Network Operating Requirements.
- (b) If the Operator wishes to operate Rolling Stock on the Network of a type which is not specifically dealt with in the Network Operating Requirements, the Operator may request the Access Provider to alter the Network Operating Requirements so as to specifically deal with such Rolling Stock. The Operator must also specify such requirements for the Rolling Stock as are reasonably necessary to ensure that the operation of such Rolling Stock on the Network does not have a material adverse effect on the Network or on the operation of Trains on the Network.

11.6 Directions by the Access Provider

If the Access Provider believes (on reasonable grounds) that any one or more individual vehicles comprised in the Rolling Stock used by the Operator on the Network are in breach of the Network Operating Requirements or the Rolling Stock Standards, then the Access Provider may do one or more of the following:

- (a) direct the Operator to cease using the vehicle or vehicles concerned on the Network and provide a statement of the grounds for such direction as soon as practicable after the direction has been given; or
- (b) direct the Operator to ensure the vehicle or vehicles concerned comply with the Network Operating Requirements and the Rolling Stock Standards prior to continuing to use the vehicle or vehicles on the Network.

11.7 Compliance

The Operator must comply with a direction of the Access Provider given or imposed in accordance with Clause 11.6 at its own cost and expense.

11.8 No Damage to Network

The Operator must not change, alter, repair, deface or damage the Network in any way.

11.9 Inspection of Rolling Stock

- (a) The Access Provider has the right to inspect the Operator's Rolling Stock at any time while the Rolling Stock is on the Network:
 - (i) for the purpose of checking the accuracy of the Train Manifest and compliance by the Operator with the provisions of this Agreement; or
 - (ii) as directed by a rail safety regulator or inspection authority duly authorised by Law,

provided that the Access Provider will not unreasonably interfere with that Rolling Stock and will take reasonable steps to conduct an inspection in a manner that minimises any disruption to the business activities of the Operator. The Access Provider must ensure that any inspection of the Operator's Rolling Stock is carried out by a person who is qualified to carry out such an inspection.

- (b) If an inspection reveals that the Operator is in breach of this Agreement:
 - (i) the Access Provider may direct the Operator to cease providing a Service or may vary the Scheduled Train Path for that Service to the extent necessary to ensure the breach does not continue (but a direction under this sub-clause will only be issued after prior discussion between the Access Provider and the Operator unless, in all the circumstances, such discussion is impossible or impractical);
 - (ii) the Access Provider may allow the Operator to continue the Service on the condition that a vehicle or vehicles believed to be in breach of the Addenda to the Metropolitan Master Working Timetable or the Rolling Stock Standards are removed and dealt with in accordance with the reasonable and appropriate directions of the Access Provider;
 - (iii) the Access Provider may direct the Operator to change the loading in a vehicle or vehicles to ensure the vehicle or vehicles comply with the Addenda to the Metropolitan Master Working Timetable or the Rolling Stock Standards before proceeding;
 - (iv) the Access Provider will notify particulars of the breach to the Operator and will reasonably assist in identifying the steps necessary to rectify that breach; and
 - (v) all costs and expenses incurred by the Access Provider as a result of the breach and its rectification will be borne by the Operator.

11.10 Safety Interface Agreement

- (a) The Operator must enter into a Safety Interface Agreement with the Access provider as required by s34 of the Rail Safety Act 2006 (Vic).

- (b) In the event of any inconsistencies between the Safety Interface Agreement and clause 11 of this Access Agreement, the Safety Interface Agreement will take precedence.

12 Incidents

12.1 Notification

- (a) The Access Provider will notify the Operator of any Incident that may impact on Services to be operated by the Operator as soon as possible after it comes to the Access Provider's attention.
- (b) The Operator must notify the Access Provider of any Incident as soon as possible after it comes to the Operator's attention.

12.2 Emergency Response Plan

In the event of an Incident, the Operator must comply with the Emergency Response Plan where relevant.

12.3 Dealing with Incidents

- (a) The Access Provider may take such steps as it considers appropriate to deal with an Incident. The Operator must comply with any directions of the Access Provider in connection with the Incident, including in relation to clearing tracks.
- (b) Without limiting any other provision of this Agreement, the Access Provider may move equipment or Rolling Stock of the Operator or require the Operator to do so, and may engage third party contractors for the purposes of moving or re-railing equipment or Rolling Stock. The Operator must reimburse the Access Provider for any reasonable costs incurred by the Access Provider as a result of the Incident to the extent that the Incident or those costs were caused or contributed to by the Operator or the Operator's Associates. The Access Provider must use reasonable endeavours to minimise costs incurred under this paragraph (b).
- (c) The Operator acknowledges and agrees that passenger train services will have priority over the Operator's Services in the case of an Incident.
- (d) Where the Operator is required by ASX listing rules to disclose information about an Incident, the Operator must consult with the Access Provider as to the form and content of the comment prior to making any public disclosure.

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12.4 Other consequences of an Incident

- (a) The Operator must not dispose of or part with possession of any Rolling Stock or equipment involved in an Incident unless given written permission to do so by the Access Provider (which written permission must be given by the Access Provider as soon as investigations in relation

to the Incident are completed) or, if in the reasonable opinion of the Access Provider, the Incident will not be subject to an ongoing investigation by any investigator or board of enquiry authorised to investigate the Incident.

(b) Subject to all applicable requirements of Law, the Operator may continue to use equipment involved in an Incident (including Rolling Stock) which still meets the Rolling Stock Standards on the condition that the Operator allows access to the equipment (including Rolling Stock) by any investigator or board of enquiry authorised to investigate the Incident.

(c) When requested by the Access Provider, the Operator must provide in writing, information relating to the Incident including:

1. the time and location of the Incident,
2. available details of all loss or damage to the Train operated by the Operator or injuries to any person,
3. any data relevant to the Incident, including on train recordings, charts or other recording devices,
4. the primary cause of the Incident and any contributing factors,
5. actions proposed and taken by the Operator to prevent a re-occurrence of the Incident in the future; and
6. all other information as required by the Access Provider to meet information requests from TSV or other relevant investigating bodies or the Access Provider's internal accident investigation requirements, to enable the Access Provider to meet any of its obligations in relation to its Accreditation or under the Rail Safety Act 2006 (Vic).

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12.5 Disablement

Without limiting the other provisions of this Clause 12, if any Rolling Stock of the Operator is disabled (whether through derailment, collision, locomotive failure or otherwise) while on the Network, the Operator must notify the Access Provider, as a matter of urgency, of the circumstances and other details relating to the disablement. Emergency recovery and rectification action must be conducted in consultation with the Operator and the Access Provider and must be carried out at the earliest practicable time in accordance with the Emergency Response Plan.

12.6 Notifications

Notifications required by this Clause 12 must be made by the quickest available means.

12.7 Rerailing

The Access Provider must take all reasonable steps to minimise overall delays on the Network arising following an Incident, including by providing to the Operator rerailing services using any available rerailing equipment of the Access Provider.

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<#>the cause(s) of the Incident and any contributing factors; ¶
<#>actions taken by the Operator to prevent a re-occurrence of the Incident in future; and¶
<#>copies of all documentation supplied to or received from Transport Safety Victoria or any other authority as a result of the Incident.¶
<#>When requested by the Access Provider, the Operator must provide in writing, information relating to the Incident including:¶
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13 Environment

13.1 Environmental Requirements

- (a) The Operator must not:
 - (i) abandon or dump any Industrial Waste or potentially Hazardous Substance on the Network; or
 - (ii) handle any Industrial Waste or potentially Hazardous Substance in a manner likely to create an Environmental Hazard.
- (b) The Operator must comply with all Environmental Laws and obtain and maintain in full force and effect and comply with the terms of all permits and licences required in order to release or emit anything into the air or water or on to the ground or otherwise into the Environment or to emit any substantial noise, in connection with the Services.
- (c) To the extent that compliance by the Operator with an Environmental Law results in Incremental Costs that should reasonably be shared amongst all users of the Network, the costs will be allocated between those users in accordance with clause 4.4.
- (d) If the Access Provider prepares and provides to the Operator a plan for dealing with the environmental effects of operating trains on the Network, the Operator must within a reasonable time prepare its own plan for dealing with the environmental effects of its operation on the Network, which plan must be consistent with the Access Provider's plan, and provide a copy of its plan to the Access Provider.

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13.2 Dangerous Goods

The Operator must comply with the Dangerous Goods Code at all times, including notification to the Access Provider of dangerous goods being carried by the Operator or any incident (whether or not an Incident) involving dangerous goods such as spillage, leakage or container damage associated with any Train operated by the Operator on the Network.

14 Indemnity and Insurance

14.1 Indemnity by the Operator

Subject to clause 14.3, the Operator indemnifies the Access Provider and the Access Provider's Associates against any claim, loss, liability, cost and expense that may be incurred or sustained by the Access Provider or the Access Provider's Associates to the extent that such claim, loss, liability, cost or expense is caused or contributed to by a breach of this Agreement by the Operator or any negligent act or omission of the Operator or the Operator's Associates.

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14.2 Indemnity by Access Provider

Subject to clause 14.3, the Access Provider indemnifies the Operator and the Operator's Associates against any claim, loss, liability, cost and expense that may

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be incurred or sustained by the Operator or the Operator's Associates to the extent that such claim, loss, liability cost or expense is caused or contributed to by a breach of this Agreement by the Access Provider or any negligent act or omission of the Access Provider or the Access Provider's Associates.

14.3 Exclusion of Indirect or Consequential Loss

- (a) Neither the Access Provider nor the Operator is liable to the other in respect of any Indirect or Consequential Loss.
- (b) For the purpose of clause 14.3(a), it is agreed that the following losses do not constitute "Indirect or Consequential Loss":
 - (i) amounts payable under clause 14.5 or 14.6;
 - (ii) ~~property damage or losses arising from third party claims in respect of property damage, personal injury, nervous shock or death.~~

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14.4 Insurance

- (a) The Operator must take out and maintain a public liability insurance policy for an amount not less than \$250 million for any one event with respect to any liabilities to the Access Provider and any third parties for:
 - (i) the death or injury of any person (except a person who at the time of the injury or death is defined as a worker of the Access Provider or the Operator under any statute relating to workers' compensation insurance); or
 - (ii) any loss, damage or destruction of any property (other than property of the Operator).
- (b) The insurance referred to in paragraph (a) must be effected with a reputable and solvent insurer.
- (c) As soon as reasonably practicable after a request is made by the Access Provider to the Operator, the Operator must produce a current insurance policy or certificate of currency in respect of its insurance conforming with the requirements of this Clause 14.4.
- (d) If the Operator fails to comply with its insurance obligations under this Clause 14.4, the Access Provider by notice may require it to do so, and, if within 5 Business Days of the request by the Access Provider, the Operator has not produced a current insurance policy or certificate of currency in respect of its insurance conforming with the requirements of this Clause 14.4, then the Access Provider may effect any insurance reasonably necessary to comply with the Operator's insurance obligations under this Clause 14.4. Any reasonable premiums due in relation to this insurance will be a debt due from the Operator to the Access Provider indemnifiable by the Operator on demand under Clause 14.1.
- (e) The requirements of this Clause 14.4 are without prejudice to and do not affect the operation of the indemnities and limitations of liability contained in this Agreement.

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14.5 TAC Premiums

- (a) The parties acknowledge and agree that the Access Provider should not be responsible for increased transport accident insurance premiums resulting from an Incident caused or contributed to by the Operator.
- (b) If as a result of an Incident that is caused or contributed to by the Operator or any employee, contractor or representative of the Operator:
 - (i) a payment is made to a person by the Transport Accident Commission (“TAC”); and
 - (ii) the payment results in the Access Provider having to pay increased premiums to TAC,

the Access Provider may impose a charge on the Operator equal to the portion of the payment caused or contributed to by the Operator or contractor or representative of the Operator. The parties acknowledge that such an amount is a reasonable amount to compensate the Access Provider for increased TAC premiums.

14.6 Delay payment indemnity

- (a) Without limiting any other provision of this Agreement, if:
 - (i) the Operator or any Train or Rolling Stock operated by the Operator causes or contributes to any delay in the Network; and
 - (ii) the delay referred to in paragraph (i) results directly in an OPR Incentive Payment (“Delay Loss”); and
 - (iii) the Access Provider provides to the Operator written evidence of the Delay Loss,

then the Operator must reimburse the Access Provider for the Delay Loss, to the extent that the Operator or the Train or Rolling Stock caused or contributed to such delay in the Network.
- (b) All payments by the Operator to the Access Provider under clause 14.6(a) will be calculated proportionately each calendar month as follows:

$$DL = (PWMO/PWM) \times OPRIP$$

where:

DL is the Delay Loss payable by the Operator;

PWM is the Passenger Weighted Minutes (as determined within Schedule 7 for the Franchise Agreement – Train dated 31 August 2009) incurred by the Access Provider across the Network in the relevant calendar month;

PWMO is the PWMs attributed to the Operator in the relevant calendar month; and

OPRIP is the OPR Incentive Payment payable by the Access Provider.

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15 Variation of Protocols

- (a) The Access Provider may amend or replace the following protocols from time to time:
- (i) the Train Operating Protocol;
 - (ii) the Track Occupation Protocol;
 - (iii) the Network Operating Requirements;
 - (iv) the Emergency Response Plan;
 - (v) the Capacity Allocation Protocol;
 - (vi) the Operational Interface Procedures;
 - (vii) the Communications Protocol; and
 - (vii) the Train Path Request Process and Protocol.

(b) In preparing any amendment or replacement of a protocol referred to in clause 15(a), the Access Provider must:

- (i) provide reasonable notice to the Operator of the amendment or replacement;
- (ii) where the amendment or replacement is reasonably likely to have a significant impact on Services or operations of the Operator, consult with the Operator regarding the amendment; and

this paragraph (b) does not prevent the Access Provider from amending or replacing the protocols if a failure to make such amendment or replacements would compromise the safety, operational or commercial requirements of the Network or the Access Provider, provided it has otherwise complied with this paragraph (b).

(c) The Access Provider must promptly make available on its website updated copies of any amended or replaced protocols.

16 Confidentiality

16.1 Confidential Information

The terms and conditions of this Agreement and all information provided under or in connection with this Agreement (the *Confidential Information*) are confidential.

16.2 Prohibition of disclosure of Confidential Information

Each party undertakes to the other that it, its officers, employees, agents and subcontractors will not, without the consent (which consent will not unreasonably be withheld or delayed) of the other party, disclose Confidential Information to any person, unless the disclosure:

- (a) is of Confidential Information already within the public domain other than as a result of a breach of this Agreement;
- (b) is of Confidential Information already known to that person (as evidenced by the person's written records) at the date of disclosure;
- (c) is to be made to the professional advisers of the disclosing party (including legal and financial advisers), provided that the disclosee agrees to keep the Confidential Information confidential;
- (d) is to be made to a Related Body Corporate of the disclosing party, provided that the disclosee agrees to keep the Confidential Information confidential;
- (e) is required by Law, or any Governmental Agency acting or purporting to act within its powers and functions, or by the requirements of Accreditation;
- (f) is reasonably necessary for the purposes of any mediation, expert determination, arbitration or legal proceeding involving one of the parties to this Agreement;
- (g) is by a party to this Agreement, in connection with its sale or the sale of all or a substantial proportion of that party's assets, provided that the disclosee agrees to keep the Confidential Information confidential;
- (h) relates to information consisting of aggregate freight or aggregate passenger volume data for all operators or other aggregate usage statistics provided by the Operator to the Access Provider (but this does not permit the disclosure by the Access Provider of information relating to costs, payments, receipts or profits of the Operator);
- (i) is to the ACCC for the purposes of Part IIIA of the *Trade Practices Act 1974* (Cth) or to the ESC for the purposes of the *Rail Corporations Act* or the Guidelines; or
- (j) is by the Access Provider to the manager of the Country Network as reasonably necessary for management of the interface between the Network and the Country Network (as confirmed by the manager of the Country Network together with its promise that the Confidential Information will be kept confidential).

16.3 Disclosure for purposes of this Agreement

Each party must take all steps reasonably necessary to ensure that Confidential Information is disclosed only to such of its or its Associate's officers, employees, advisers (legal or financial), agents or subcontractors as require that knowledge:

- (a) in order to carry out their duties in relation to this Agreement; or
- (b) in connection with a purpose referred to in Clause 16.2.

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16.4 Disclosure to State

Nothing in this Clause 16 prevents the disclosure of Confidential Information on a confidential basis to the Director or any minister, officer, employee, agent, adviser or consultant of the State or a Governmental Agency of the State.

16.5 Confidentiality continues

The obligation of confidentiality under this Clause 16 is a continuing obligation and remains in force during the term of this Agreement and afterwards for a period of 7 years.

17 Expiry and Termination

17.1 Preservation of other rights

If a party breaches or repudiates this Agreement, nothing in this Clause 17 will prejudice the right of the other party to recover damages or exercise any other right. The Access Providers rights under this Clause 17 are in addition to any other rights that it may have under this Agreement, including under Clause 5.

17.2 Breach of Payment Obligation

If either party commits a material breach of its payment obligations under this Agreement and fails to remedy the breach within 20 Business Days after being required to do so in writing, the other party may terminate this Agreement immediately by notice to the party in default.

17.3 Breach of Other Obligations

- (a) If a party commits a material breach of an obligation under this Agreement (not the subject of Clause 17.2) (the **Defaulting Party**) the other party may give the Defaulting Party a notice (a **Default Notice**) specifying:
 - (i) a material breach has occurred;
 - (ii) setting out reasonable details of the event or circumstances constituting the material breach; and
 - (iii) specifying a reasonable period of time in which to cure the material breach (the **Cure Period**).
- (b) Within 5 Business Days of receipt of a Default Notice, the Defaulting Party must provide to the other party a Cure Plan in respect of the material breach specified in the Default Notice.
- (c) Following receipt of a Default Notice, the Defaulting Party will be permitted to cure the material breach within the Cure Period and, if applicable, in accordance with the Cure Plan.
- (d) If the Defaulting Party requires an extension to the Cure Period it may, not later than the expiration of the current Cure Period, provide to the other party:
 - (i) a revised Cure Plan; and
 - (ii) evidence that:
 - (A) the Defaulting Party has diligently pursued and is continuing to diligently pursue a feasible and practicable programme of rectification; and

- (B) the material breach cannot, with reasonable diligence, be cured within the current Cure Period.
- (e) The other party must not unreasonably refuse to grant an extension of the Cure Period.
- (f) If the Defaulting Party commits a material breach and the material breach is not cured within the Cure Period then, the other party may terminate this Agreement immediately by notice to the Defaulting Party.
- (g) The provisions of this Clause 17.3 do not limit or reduce the rights of a party to claim damages for breach of this Agreement or the Access Provider's rights under Clause 5.

17.4 Termination on Insolvency

A party may terminate this Agreement immediately by notice to the other party if the other party:

- (a) is insolvent within the meaning of section 95A of the *Corporations Act*;
- (b) fails to comply with a statutory demand (within the meaning of section 459F(1) of the *Corporations Act*) unless:
 - (i) the debt to which the statutory demand relates is discharged within 15 Business Days of the date of the failure; or
 - (ii) the party demonstrates to the satisfaction of the other party (acting reasonably) that it is able to pay all its debts as and when they become due and payable;
- (c) has an administrator appointed in respect of it;
- (d) has a controller within the meaning of section 9 of the *Corporations Act* or similar officer appointed to the whole or a substantial part of assets or undertaking and that controller or similar officer is not removed within 15 Business Days of the appointment;
- (e) has an order made or a resolution passed for its winding up or dissolution or it enters an arrangement, compromise, or composition with or assignment for the benefit of its creditors or a class of them;
- (f) has any security enforced over, or a distress, execution or other similar process levied or served against, the whole or a substantial part of its assets or undertaking; or
- (g) is subject to any event which, under the Law of any relevant jurisdiction, has an analogous or equivalent effect to any of the events listed above.

17.5 Cessation of Rights

Upon expiry or termination of this Agreement, all rights of the Operator to use the Network will cease. The Operator must at the cost of the Operator on or prior to termination remove all of the Operator's Rolling Stock from the Network. If the Operator does not remove all Rolling Stock, the Access Provider may:

- (a) carry out the obligations of the Operator at the Operator's cost; and
- (b) store the Operator's Rolling Stock at the Operator's risk and cost.

17.6 Accrued Rights

Expiry or termination of this Agreement is without prejudice to and does not affect the accrued rights or remedies of any of the parties arising in any way out of this Agreement up to the date of expiry or termination.

17.7 Continuing Clauses

Clauses 1, 4, 14, 16, 17.1-17.6, 21 and 33 and this Clause 17.7 will continue to apply after termination of this Agreement.

18 Assignment and Subcontracting

18.1 Assignment

- (a) The Operator may not assign, transfer, delegate, encumber, pledge or otherwise dispose of or deal with any of its rights or obligations under this Agreement, including any Train Path allocated to it or attempt or purport to do so, without the prior written consent of the Access Provider, which consent must not be unreasonably withheld.
- (b) The Access Provider may assign or novate its rights or obligations under this Agreement to VTRC, the Director, a nominee of the Director, a successor operator of the Network or a subsequent purchaser of the Operator's business. The Operator must, upon request, execute any documentation necessary to facilitate or assist such assignment or novation.

18.2 Sub-contracting

The Operator may not sub-contract any of its obligations under this Agreement without the prior written consent of the Access Provider, which cannot be unreasonably delayed or withheld if the sub-contracting party meets all the requirements of the Operator under this Agreement. Notwithstanding the sub-contracting of the whole or any part of the Operator's obligations under this Agreement, the sub-contracting party will not be released from its liabilities to the Access Provider under this Agreement and the rights of the Access Provider under this Agreement are expressly reserved to the Access Provider.

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18.3 Change of Control

For the purposes of this Clause 18, and without limiting the meaning of the word *transfer*, a party will be taken to have transferred or to have attempted or purported to transfer its rights and obligations under this Agreement if at any time the power (whether formal or informal, whether or not having legal or equitable force and whether or not based on legal or equitable rights):

- (a) to exercise or control the right to vote attached to 50% or more of the issued shares or stock (whether fully, partly or nil paid) in the party;
- (b) to dispose of or exercise a right of disposal in respect of 50% or more of the issued voting shares or stock (whether fully, partly or nil paid) in the party;

- (c) to dominate or control the party or the financial or operating policies of the party (whether alone or in concert with others, and whether by any act or omission or otherwise),

resides with any persons other than those holding that power on the Effective Date.

19 Dispute Resolution

19.1 Procedure to settle disputes

- (a) If there is a dispute between any of the parties relating to or arising out of this Agreement, the parties must use reasonable endeavours acting in good faith to settle the dispute as soon as practicable.
- (b) The procedure that is to be followed to settle a dispute arising under this Agreement is as follows:
 - (i) first, negotiation of the dispute under Clause 19.2; and
 - (ii) second, determination of the dispute under Clause 19.3,
- (c) A party may not commence court proceedings in relation to a dispute arising in connection with this Agreement until it has exhausted the procedures in this Clause 19, unless the party seeks appropriate injunctive or other interlocutory relief to preserve property or rights or to avoid losses that are not compensable in damages.

19.2 Negotiation

If there is a dispute between the parties relating to or arising out of this Agreement then within 10 Business Days of a party notifying the other party of a dispute, senior representatives from each party must meet and use reasonable endeavours acting in good faith to resolve the dispute by joint discussions.

19.3 Independent Expert

- (a) If the parties are unable to resolve the dispute under Clause 19.2 the parties will submit to the following procedure prior to any other course of action being taken to resolve the dispute:
 - (i) the parties will jointly choose and appoint an independent expert;
 - (ii) in the absence of agreement by the parties as to the independent expert within 2 Business Days of notice of a dispute, the independent expert will be appointed on the application of any party by the President of the Institute of Arbitrators and Mediators Australia;
 - (iii) the independent expert must make a determination or finding on the issues in dispute as soon as practicable and in any event within 20 Business Days, or such longer period as may be agreed between the parties;
 - (iv) the independent expert will act as an expert and not as an arbitrator and may adopt such procedures as he or she sees fit;
 - (v) the independent expert's decision will be final and binding on the parties; and

- (vi) the costs of the independent expert will be borne by the parties equally or as the independent expert may otherwise determine and each party will bear its own costs relating to the independent expert's decision.

19.4 Amalgamation of Disputes

The parties may by agreement permit a dispute being dealt with under this Clause 19 to be amalgamated with any other dispute or disputes involving one or both parties.

20 Force Majeure

20.1 Notice of event of Force Majeure

If a party is prevented in whole or in part from carrying out its obligations under this Agreement as a result of Force Majeure, it will promptly notify the other party accordingly. The notice must:

- (a) specify the obligations and the extent to which it cannot perform those obligations;
- (b) fully describe the event of Force Majeure;
- (c) estimate the time during which the Force Majeure will continue; and
- (d) Specify the measures proposed to be adopted to remedy or minimise the effects of the Force Majeure.

20.2 Suspension of obligations

Following a notice of Force Majeure in accordance with Clause 20.1, and while the Force Majeure continues, the obligations, which cannot be performed because of the Force Majeure, will be suspended.

20.3 Remediating or Minimising Force Majeure

The party that is prevented from carrying out its obligations under this Agreement as a result of Force Majeure must remedy or minimise the effects of the Force Majeure to the extent reasonably practicable and resume performance of its obligations as soon as reasonably possible, including without limitation in the case of the Access Provider, by restoring any part of the Network damaged or affected by the Force Majeure event to at least the same standard as existing at the time of the Force Majeure event.

20.4 Mitigation

The party that is prevented from carrying out its obligations under this Agreement as a result of Force Majeure must take all action reasonably practicable to mitigate any loss suffered by the other party as a result of the party's failure to carry out its obligations under this Agreement.

21 Notices

- (a) Subject to paragraph (b), any notice, demand, consent or other communication (the *Notice*) given or made under this Agreement:
- (i) must be in writing and signed by a person duly authorised by the sender;
 - (ii) must be delivered to the intended recipient by hand or by prepaid post (if posted to an address in another country, by registered airmail) or fax to the address or fax number last notified by the intended recipient to the sender; and
 - (iii) will be taken to be duly given or made:
 - (A) in the case of delivery in person, when delivered;
 - (B) in the case of delivery by post, two Business Days after the date of posting (if posted to an address in the same country) or seven Business Days after the date of posting (if posted to an address in another country); and
 - (C) in the case of fax, on receipt by the sender of a transmission control report from the despatching machine showing the relevant number of pages and the correct destination fax machine number or name of recipient and indicating that the transmission has been made without error,

but if the result is that a Notice would be taken to be given or made on a day that is not a business day in the place to which the Notice is sent or is later than 4.00pm (local time) on any day it will be taken to have been duly given or made at the commencement of business on the next business day in that place.

Any Notice under this Agreement relating to an Incident, and not involving the payment of money, may be given orally where the informing party considers that the recipient party requires the information immediately and there is insufficient time to serve a written Notice. Where oral Notice is provided under this paragraph (b), the party that gives oral Notice must provide to the other party a written copy of that Notice within 3 Business Days of the oral Notice being given.

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22 GST

22.1 GST to be added to amounts payable

If GST is payable on a Taxable Supply made under, by reference to or in connection with this Agreement, the party providing the Consideration for that Taxable Supply must also pay the GST Amount as additional Consideration. This Clause does not apply to the extent that the Consideration for the Taxable Supply is expressly agreed to be GST inclusive.

22.2 Tax invoice and adjustment note

No payment of any amount pursuant to Clause 22.1 is required until the supplier has provided a Tax Invoice or Adjustment Note as the case may be to the recipient.

22.3 Liability net of GST

Any reference in the calculation of Consideration under this Agreement to a cost, expense or other liability incurred by a party, must exclude the amount of any Input Tax Credit entitlement of that party in relation to the relevant cost, expense or other liability. A party will be assumed to have an entitlement to a full Input Tax Credit unless it demonstrates otherwise prior to the date on which the Consideration must be provided.

22.4 Revenue exclusive of GST

Any reference in this Agreement to price, value, sales, revenue or a similar amount (*Revenue*), will be a reference to that Revenue exclusive of GST.

22.5 Cost exclusive of GST

Any reference in this Agreement (other than in the calculation of Consideration) to cost, expense or other similar amount, will be a reference to that cost, expense or other amount exclusive of GST.

23 Entire Agreement

This Agreement contains the entire agreement between the parties with respect to its subject matter and supersedes all prior agreements and understandings between the parties in connection with it.

24 Amendment

No amendment or variation of this Agreement is valid or binding on a party unless made in writing and executed by both parties.

25 No Waiver

No failure to exercise nor any delay in exercising any right, power or remedy by a party operates as a waiver. A single or partial exercise of any right, power or remedy does not preclude any other or further exercise of that or any other right, power or remedy. A waiver is not valid or binding on the party granting that waiver unless made in writing.

26 Severability

To the extent that any part of this Agreement may be invalid, illegal or unenforceable, it is intended that the remaining parts, insofar as possible and reasonable, must be effective and enforceable.

27 Further Assurances

Each party agrees to do all things and execute all deeds, instruments, transfers or other documents as may be necessary or desirable to give full effect to the provisions of this Agreement and the transactions contemplated by it.

28 No Merger

The rights and obligations of the parties will not merge on the completion of any transaction contemplated by this Agreement. They will survive the execution and delivery of any assignment or other document entered into for the purpose of implementing a transaction.

29 Rights Cumulative

Subject to any express provision in this Agreement to the contrary, the rights of a party under this Agreement are cumulative and are in addition to any other rights of that party.

30 Relationship

This Agreement does not constitute any partnership, trust, agency, joint venture or employment relationship between the parties.

31 Inurement

The provisions of this Agreement will inure for the benefit of and be binding upon the parties and their respective successors and permitted assigns.

32 Costs and Stamp Duty

Subject to any provision in this Agreement to the contrary, each party must bear its own legal and other costs and expenses including stamp duty relating directly or indirectly to the preparation of, and performance of its obligations under, this Agreement.

33 Governing Law

This Agreement is governed by the laws of Victoria. Each party submits to the non-exclusive jurisdiction of courts exercising jurisdiction there in connection with matters concerning this Agreement.

34 Counterparts

This Agreement may consist of a number of counterparts and if so the counterparts taken together constitute one and the same instrument.

35 Cross-Jurisdictional Issues

- (a) If at any time the Operator intends to provide the Services as part of or in conjunction with rail services conducted, or to be conducted, by the Operator on railways which do not constitute part of the Network, the Operator acknowledges that it is the obligation of the Operator to obtain any necessary agreements from the relevant track owners or authorities.
- (b) The Access Provider will reasonably cooperate with the Operator and with the relevant track owners or authorities in other railway territories in order to assist the granting to the Operator of all agreements and approvals necessary to enable the Operator to operate the Services as part of, or in conjunction with, access by the Operator to rail tracks or rail networks in one or more rail territories.

EXECUTED as an agreement

**Executed by
Metro Trains Melbourne Pty Ltd:**

.....
Director

.....
Director/Secretary

.....
Name (please print)

.....
Name (please print)

**Executed by
[insert Operator's name] Pty Ltd**

.....
Director

.....
Director/Secretary

.....
Name (please print)

.....
Name (please print)

Schedule 1

Access Charges:

- 1 The Access Charge comprises a tonnage charge of \$ [TBC] per 1000 GTK.

- 2 In this schedule:
“GTK” means the sum of the number of kilometres each tonne of Train (including locomotive, Rolling Stock and freight) operated by Operator travels on the Network (except in relation to Ancillary Movements).

Schedule 2

Operator's Scheduled Train Paths

APPENDIX D | BOOZ & COMPANY REPORT



Final Report

Metro cost allocation approach and incremental and stand-alone costs

Essential Services Commission

Melbourne

August 2011

*This document is confidential and is intended solely for
the use and information of the client to whom it is addressed.*

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1. Background

Most of the Melbourne metropolitan rail network, excluding a few freight-only lines in the central area, is concessioned as a vertically-integrated franchise to the urban passenger rail operator, Metro Trains Melbourne Pty Ltd (Metro). The network is also used by non-urban passenger operators and by several freight operators who pay access charges to for their use of the metropolitan network.

The current access charges were set as part of the last access review in 2006. The access regime, including the access charges, is now due for review as required by the *Rail Management Act 1996*.

This report has been commissioned by the Transport and Industry Sectors Branch of the Essential Services Commission (ESC) to provide technical and economic advice in the following areas:

- An economic assessment of Metro's cost allocation approach to operations and maintenance costs and in particular the use of Metro's proposed cost allocation percentages
- Options (and rationale) for alternative cost allocation approaches and percentages
- Metro's proposed demand volume forecasts
- Assistance in calculating the revised access reference prices
- Calculating and providing advice on an appropriate floor and ceiling price for freight services on the metropolitan network so that the Commission can obtain comfort that the access price for freight reference services that Metro may adopt is within this band and ad hoc advice as agreed.

The ESC's contact is Dominic L'Huillier – Ag Director, Transport & Industry Sectors Branch.

In parallel with this report, ESC have commissioned advice from engineering firm GHD on the efficiency of Metro's infrastructure maintenance and operations and on the level of variability of these costs with the overall traffic volume. The advice on the level of variability has been incorporated into the analysis included in this report.

The report contains four chapters in addition to this introduction.

- Chapter 2 describes the approach adopted by Metro in its submission and reviews the methodology and input parameters.
- Chapter 3 outlines an alternative approach to determining the reference price.
- Chapter 4 discusses the appropriate level of costs to be included in the reference prices, in view of the substantial change in the overall quantum of cost from the last control period, some at least of which is backlog maintenance. It also summarises the costs by corridor and the overall level of variability, drawing on the GHD advice, and allocates the costs between the various users: metropolitan passenger, suburban passenger and freight.
- Chapter 5 outlines a proposed revenue cap.

2. Metro's Approach in its Submission

2.1 Description of Network

The lines maintained by Metro on which freight operates to a greater or lesser degree, are summarised in Table 1.

Table 1 – Metro-maintained lines on which freight operates regularly

From	To	Freight
Viaduct Jc.	Pakenham	Maryvale paper Westall stone (partway) Bairnsdale logs (occasional)
Viaduct Jc.	Stony Point	Long Island steel
Long Island Jc	Long Island (freight-only line)	Long Island steel
West Tower	Albion	Westall stone Kensington grain
Tottenham Jc	Sunshine	Appleton Dock to/from Ballarat/north
Tottenham Jc	Albion	Appleton Dock to/from north-east
Albion	Brooklyn Jc	North-east to/from Geelong
Jacana	Donnybrook	Westall stone Tocumwal containers North-east/north central grain Somerton cement
Newport	Werribee	Warrnambool Mildura Waurm Ponds – Somerton cement Geelong grain ex north-east

The total Metro network is 420 route-km and freight trains travel over approximately 167 kilometres (40%) on a regular basis. However, freight trains only represent 0.70% of the total train-kilometres on the network (see Table 6 in Appendix 2).

Description of Metro's Approach

2.1.1 Summary

Metro's revenue model uses a real pre-tax approach to determine Total Revenue, setting a revenue yield to equal the present value of forecast costs.

The Total Revenue is determined by quantifying the Operations and Maintenance (O+M) Costs and forecasting from 2011/12 to 2015/16. The other key inputs normally included in Total Revenue are assumed to be zero because of the concession arrangements:

- Opening asset base;
- Capital expenditure (currently not in a position to forecast); and
- Depreciation (as asset base is zero).

The total tariff revenue over the 5 year period is discounted based on a weighted average cost of capital of 6.44% to estimate the present value of total revenue from 2011 to 2016.

Total Revenue 2011 to 2016 (present value) = \$16.20 ('000)¹

A tariff is estimated based on the forecast gross tonne kilometres (GTK) so as to be equivalent to the present value of the Total Revenue.

Freight Tariff (2011/2012) = \$17.86 / GTK ('000)

As that this tariff is a very significant increase from the previous Access Arrangement (2006 to 2011), Metro instead recommended use of the previous tariff uplifted by inflation.

Metro Recommended Tariff (2011/2012) = \$6.15 / GTK ('000)

2.1.2 Components

The O+M costs comprise Maintenance costs, Operations costs and Overheads and Margins costs.

Maintenance costs are derived from:

- Freight incremental maintenance costs (estimated at 5% of total track and signalling costs on freight lines with the total track and signalling cost on freight lines assumed to be 44% of total track and signalling costs);
- Total indirect costs (allocated according to freight share of train kilometres [TKs] on freight lines, i.e. 1.48%, and with total indirect costs estimated as 73% of total track and signalling cost on freight lines);

Operations costs are derived from total regulatory costs (80% of total regulatory compliance, advisory and legal costs) and operational control costs (e.g. planning of train paths, train control).

¹ Metro Model – 2011 Submission Model (Revenue Requirements and Tariffs Sheet)

Overheads and Margins costs comprise:

- Overhead costs (17% of total track and signalling costs); and
- Margin costs (3% of total operations, total regulatory, advisory and legal costs, total overhead costs and total track and signalling costs).

Overheads and Margins are allocated to freight according to relative TKs (i.e. freight TK as a percentage of total TK - 0.78%).

2.2 Review of Metro's Approach

The Metro approach closely follows the methodology of the 2006 decision. However, knowledge of the relationship between usage and rail infrastructure costs has advanced since then and a number of issues need to be addressed:

The overall quantum of costs

The total cost has increased by 150% compared to the last control period, principally in planned renewals. Much of this appears to be backlog maintenance. An issue is the extent to which freight access prices should be set with regard to actual expenditure being incurred over the future regulatory period, including any catch-up expenditure, or whether prices should instead be set with regard to more of a 'steady-state' level of expenditure.

The primary user of the metropolitan network is urban passenger services which are underpinned by large and explicit government subsidies. Track standards and the maintenance regime are set by passenger requirements and passenger services generally enjoy priority use of the network. Freight services are only minor users of the system and access charges are generally highly constrained by market affordability. It might be argued therefore that steady state expenditure is more appropriate as it is likely to be less distortionary, and more economically efficient, than more volatile charges that fluctuate with the Government's appetite to invest in the performance and reliability of metropolitan passenger services.

Nevertheless, it is reasonable to expect freight services to pay no less than the incremental costs that they impose on the system and to the extent maintenance and renewal expenditure in the previous regulatory period under-estimated what is required to maintain the network in a fit for purpose state, then some upward adjustment in the overall quantum of costs would seem warranted. With the higher quantum of expected costs planned for the next regulatory period there might also be some downward adjustment in the "variability" percentage in comparison to the previous analysis which would clearly mitigate the potential impact on minimum freight access charges. The total costs proposed by Metro have therefore been used in the analysis with the variability with usage adjusted downwards to allow for the embedded backlog maintenance. In other words, prices have been set with regard to a 'steady-state' level of expenditure.

The Metro submission only included track and signalling-related costs. While the other types of infrastructure will generally only have limited, if any, variability with usage, we believe structures-related costs at least ought to be included in the analysis.

The proportion of costs which are freight-related

Metro uses 44% as the proportion of network-wide costs that are incurred on lines used by freight. Whilst this was used in the 2006 Decision, it was used at that time in a different context, i.e. establishing the availability of the network for freight. In our view, this approach should be replaced by one which uses the costs associated with each section, whether they can be directly measured or whether they have to be estimated based on route and track-km.

The variability of costs with usage

Infrastructure maintenance costs are affected by passenger trains as well as freight trains. This is investigated further in the GHD report (MTM's Access Arrangements, Review of Maintenance & Operations Costs, 2011).

The relative impact of freight and passenger usage

Much work has been done on this in UK and there is now an established relationship between vehicle characteristics (axle-load, speed and so on) and the relative damage they cause. This relationship will provide a much more transparent basis for distributing variable costs between these different users.

The development of reference prices

Whilst the estimation of the variable cost of the different users can be done through a well-defined process, the allocation of joint costs is inevitably an arbitrary process and in practice the allocation selected is determined by general policy considerations, especially where some of the users are government-owned and being supported by subsidies.

3. Approach Adopted

The approach adopted has the following steps, as illustrated in Figure 1.

Traffic Volumes on Network

Current timetables were used to estimate the network usage by Metro trains, Vline and freight (defined in train-km (TK) and gross tonne- km (GTK)). Adjustments were made for:

- V/Line figures to include the effect of extending the Metro boundary to Sunbury; and
- Freight figures to match the actual TK and GTK for 2010, the year on which the maintenance costs in the Asset Management Plan (AMP) were based.

The network usage estimates were used to establish the link between maintenance costs and vehicle characteristics, defined in terms of equivalent gross tonne kilometres (EGTK) and equivalent structures gross tonne kilometres (ESGTK). The derivation and application of these terms is discussed in Appendix 1.

Allocation of Maintenance Costs

Disaggregated maintenance costs (e.g. track and signals) and their variability were based on GHD's analysis of the AMP. The variable element of maintenance costs was then distributed between Metro, V/Line and freight according to the relevant cost drivers (TK, EGTK and ESGTK).

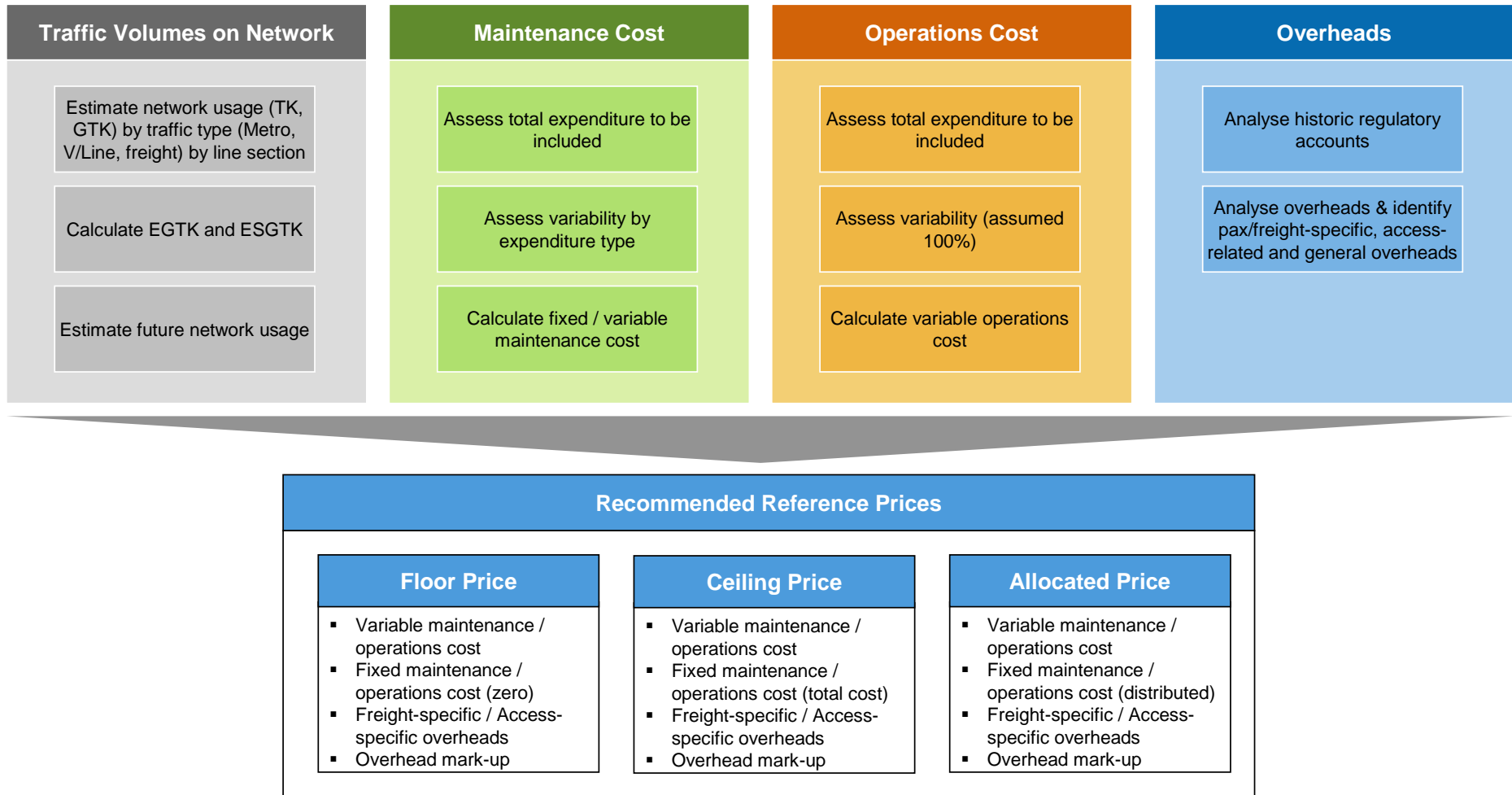
Allocation of Operation Costs

Variable operation costs were assessed based on total operation costs, including labour on-costs (\$40.9million), and distributed across modes by TK.

Allocation of Overhead

Booz & Company analysed the regulatory accounts (in absence of future budgets) to identify passenger-specific costs, freight-specific costs, access-related costs and general overheads. The general overheads, including a profit margin, were then distributed over all other expenditure. See Appendix 2 for more details of the approach.

Figure 1 Outline of total process



4. Results for 2010

Figure 2 shows the way in which the calculations in Section 3 are combined to create the floor price, ceiling price and an alternative allocated price in 2010. The allocated price allocates some of the fixed costs of the freight network to freight users.

Figure 2 Derivation of Floor, Ceiling Prices and Reference Price

Recommended Reference Prices		
Floor Price	Ceiling Price	Allocated Price
<ul style="list-style-type: none"> ▪ Variable maintenance / operations cost ▪ Fixed maintenance / operations cost (freight-only lines) ▪ Freight-specific / Access-specific overheads ▪ Overhead mark-up 	<ul style="list-style-type: none"> ▪ Variable maintenance / operations cost ▪ Fixed maintenance / operations cost (total cost) ▪ Freight-specific / Access-specific overheads ▪ Overhead mark-up 	<ul style="list-style-type: none"> ▪ Variable maintenance / operations cost ▪ Fixed maintenance / operations cost (distributed) ▪ Freight-specific / Access-specific overheads ▪ Overhead mark-up

The floor price is established by summing the variable maintenance cost, fixed maintenance cost of freight-only lines, variable operations cost and overhead mark-up.

Floor Price (2010): \$6.07 / GTK ('000)

The ceiling price is determined as the total costs of the relevant freight network less the usage related costs of passenger services. i.e. Freight services pick up all of the fixed costs of the freight-only lines.

Ceiling Price (2010): \$272.49 / GTK ('000)

The allocated price is assessed by adding to the price floor a share of the fixed maintenance costs on the other lines in the freight network, based on train kilometres.

Allocated Price (2010): \$9.75 / GTK ('000)

The primary use of the metropolitan network is for urban passenger services, with the fixed costs of the network underpinned by large and explicit government subsidies. Generally the most economically efficient pricing approach is to set access charges equal to the incremental costs a user imposes on the system. In this case, because passenger services are underwritten by government the use of the network by passenger services will not vary whatever the price set for freight services. Therefore the approach that is likely to be the least distortionary in respect of the total use of the metropolitan rail network is to set freight access prices equal to the incremental cost they impose on the system (i.e. \$6.07 / 000 GTK).

However, an argument may be made that the financial construct of the urban passenger use of the system is artificial and that a reasonable contribution to the fixed costs of the network used by freight services is appropriate. A reasonable apportionment of fixed costs based on relative use by passenger and freight services is presented in Table 2 below. In this case, a freight access charge of \$9.75 / 000 GTK is the result.

Table 2 – Summary of freight costs (\$ mill p.a.) in 2010 (\$2010/11)

Freight cost components	Floor	Ceiling	Allocated
Variable maintenance cost	0.665	0.665	0.665
Variable operations cost	0.288	0.288	0.288
Fixed maintenance cost on freight network	0.029	50.065	0.720
Fixed operations cost on freight network	0.000	0.000	0.000
Freight-specific overheads	0.000	0.000	0.000
Access-specific overheads	0.158	0.158	0.158
Mark-up (10%)	0.116	5.229	0.187
Total Variable Cost	1.257	56.405	2.018
Cost/000 GTK	6.07	272.49	9.75

Source: Booz & Company analysis 2011

5. Revenue Cap

A revenue cap has been calculated for the 2011-16 regulatory period by determining the appropriate access price based on the annual freight costs, and multiplying by the applicable GTK for each lease year.

The access price varies according to the total freight cost (i.e. operations, maintenance and overhead costs) and applicable GTK. The total freight cost is made up of variable costs, fixed costs and overhead costs. The variable costs change relative to the applicable GTK in that year. Fixed costs don't change relative to the applicable GTK, and overhead costs remain a percentage (10.2%) of the total fixed and variable costs. The total freight cost then becomes the annual revenue requirement for each year in the regulatory period (2011/12 to 2015/16).

The present value of the revenue is calculated by discounting at the WACC of 6.44%, resulting in a total revenue requirement of \$5.55M over the period. The annual and discounted freight cost (and hence the annual revenue requirement) from 2010 to 2016 is shown below in Table 3.

Table 3 – Annual and discounted freight costs (2010-2016) (\$2010/11)

	2011-2016 Regulatory Period						Total
	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	
Variable maintenance cost	0.665	0.675	0.695	0.716	0.737	0.759	
Variable operations cost	0.288	0.292	0.301	0.310	0.319	0.329	
Fixed maintenance cost on freight network	0.029	0.029	0.029	0.029	0.029	0.029	
Fixed operations cost on freight network	0.000	0.000	0.000	0.000	0.000	0.000	
Freight-specific overheads	0.000	0.000	0.000	0.000	0.000	0.000	
Access-specific overheads	0.158	0.158	0.158	0.158	0.158	0.158	
Corporate overheads	0.116	0.118	0.121	0.124	0.127	0.130	
Total freight cost (\$m)	1.257	1.272	1.304	1.336	1.370	1.405	
Discounted freight cost or annual revenue requirement (\$m)		1.195	1.151	1.108	1.068	1.029	5.550

Source: Booz & Company analysis 2011

An access price of \$6.00 (\$2010/11) held constant in real terms would produce the equivalent forecast revenue requirement over the five-year period of \$5.55M, as shown in Table 4 below. Applying an X factor of 1% per annum to the access price will result in a 2% reduction in the aggregate revenue requirement measured in present value terms (to \$5.39M).

The access price of \$6.00 per 000 gtk in Table 4 above is slightly less than the average cost of \$6.07 per 000 gtk in Table 2. This is due to the former reflecting projected changes in variable cost according to the change gtk over the forecast period, as shown in Table 3, whereas the \$6.07 per 000 gtk is based on the average annual cost over the AMP period and the 2010/11 task (noting the 5 year AMP was

based on the 2010/11 task). In other words, costs have increased at a slightly lower rate than the increase in task, leading to a slightly lower average cost when discounted over the regulatory period. The X factor discount of 1% p.a. has been applied from 2010/11 rather than the first year of the next regulatory period (2011/12).

Table 4 – Reference price for freight services (\$ 2010/11)

	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	Total
Freight forecast GTK	207,000	210,000	216,000	223,000	229,000	236,000	
Access price (\$/000 GTK) (\$2010/11)	6.00	6.00	6.00	6.00	6.00	6.00	
Revenue(\$m)		1.260	1.298	1.337	1.377	1.419	
Discount factor		0.94	0.88	0.83	0.78	0.73	
Discounted revenue (\$m)		1.184	1.146	1.109	1.073	1.038	5.55
Adjusted Access price (\$/000 GTK) (\$2010/11) ¹	6.00	5.94	5.88	5.82	5.77	5.71	
Revenue(\$m)		1.248	1.272	1.297	1.323	1.349	
Discounted revenue (\$m)		1.172	1.123	1.076	1.031	0.987	5.39

1. Discounted by an X factor of 1%

Source: Booz & Company analysis 2011

Appendix 1 Allocation of Costs to Users

In 2000, the UK rail regulator decided to introduce usage-related charges which reflected the variable cost imposed by the passage of specific types of vehicles. These were derived from a series of studies and analyses undertaken by the research arm of British Railways, supplemented by research commissioned from various groups of consultants.

The resulting relationship derived relative a relative damage factor K for each vehicle type as:

$$\text{Equivalent Track Damage Factor } K = C_t A^{0.49} S^{0.64} \text{ USM}^{0.19} \quad (1)$$

Where C_t is 0.89 for loco-hauled passenger stock and multiple units, and 1 for all other vehicles, A is the axle load (tonnes), S is the operating speed (miles/hour), and USM is the unsprung mass (kg/axle). Further factors were developed for freight wagons to account for coal spillage and suspension types.

This relationship was first developed in 2001 but was retained in both 2006 and the most recent review in [2010]. This relationship is principally concerned with the vertical forces exerted by the vehicle but more recently, considerable research has been undertaken on lateral and longitudinal forces, exemplified by Rolling Contact Fatigue (RCF) which was the principal cause of the Hatfield Accident. However, this work is still in progress and it is in any event doubtful if it has the same significance on the Melbourne suburban network where speeds are slower and rails, in general, harder and less susceptible to RCF. The allocation of costs to users has therefore been based on vertical forces using the relationship (1).

Similar relationships were established for structures and for switches and crossings. Metro have not distinguished work on switches and crossings but the cost of structures has been identified and this can be allocated using damage factors defined by:

$$\text{Equivalent Structures Damage } K = A^{3.83} S^{1.52} \quad (2)$$

Using the same notation as in equation (1).

Appendix 2 Detailed Approach and Findings

Step 1: Aggregated expenditure and variability

Determine aggregate expenditure to be included and variability by type of infrastructure. This work has relied on the companion report by GHD. Table 5 below displays the total expenditure for maintenance over the 5 year regulatory period and their corresponding percentage variability component. The remaining expenditure is the fixed maintenance cost.

Gives total maintenance costs

Table 5 – Fixed and variable maintenance cost

Expenditure	AMP 5Y Total (\$A mill) [A]	% variable with usage [B]	Total cost (\$A mill p.a.)		
			Variable [A] x [B] / 500 = [C]	Fixed [A] ÷ 5 – [C]	Total
Track					
Inspections	15.5	0	0.00	3.10	3.10
Reactive maintenance	5.1	50	0.51	0.51	1.02
Routine maintenance	145.8	10	2.92	26.24	29.16
Planned renewals	260.1	20	10.41	41.62	52.03
Unplanned renewals	3.4	80	0.54	0.14	0.68
<i>Subtotal</i>	<i>429.9</i>		<i>14.38</i>	<i>71.61</i>	<i>85.99</i>
Signals	204.1	5	2.04	38.78	40.82
Structures	50.0	10	1.00	9.00	10.00
Total	684.0		17.42	119.39	136.81

Source: Booz & Company analysis 2011

Step 2: Operating statistics (traffic volumes) by user

Determine operating statistics across metropolitan network (Metro, Vline, freight) in terms of TK (train-km), GTK (gross tonne-km), EGTK (equivalent gross tonne-km) and ESGTK (equivalent structures gross tonne-km). EGTK adjusts for axle loads, operating speeds and the unsprung mass of different users of the track, as outlined in Appendix 1. ESGTK adjusts for axle loads and operating speeds of different users of the track. These traffic volume measures are used to distribute variable and fixed costs across the user types. Table 6 presents the summary operating statistics for the metropolitan network.

Table 6 – Summary operating statistics on metropolitan network 2010

Traffic volume measures	Metro [A]	V/Line [B]	Freight [C]	Other [D]	Total [E]	% freight [C] / [E]
TK (000)	21,429	2,591	170	20	24,210	0.70%
GTK (millions)	5,889	552	207	8	6,655	3.11%
EGTK (millions)	9,295	1,262	417	15	10,989	3.80%
ESGTK (millions)	28,262	11,806	4,702	150	44,921	10.47%

Source: Booz & Company analysis 2011

Step 3: Variable costs

Step 3a:

Calculate variable element of maintenance costs (from proportions in Step 2 against total for track maintenance in Step 1) and distribute between Metro, Vline and freight according to proportions cost drivers (EGTK, ESGTK, TK). The distribution of user type by EGTK is used for variable track maintenance costs, reflecting the relative damage caused to track by the different vehicles. Variable structure maintenance costs are allocated according to ESGTK, reflecting the relative damage to structures caused by the different vehicles. The distribution of user type by TK is used for signals, reflecting the wear and tear on the system resulting from using signals and related equipment as a train moves through the system. Table 7 shows the distribution of variable maintenance costs by user.

Table 7 – Distribution of variable maintenance cost by user (\$ mill p.a.)

	Metro	Vline	Freight	Other	Total [C] from Table 6	Basis
Track	12.16	1.65	0.55	0.02	14.38	EGTK
Signals	1.81	0.22	0.01	0.00	2.04	TK
Structures	0.63	0.26	0.10	0.00	1.00	ESGTK
Total (\$ million p.a.)	14.59	2.13	0.67	0.02	17.42	

Source: Booz & Company analysis 2011

Step 3b:

Determine operations and train control costs by extracting the 'Operations' staff from the accounts. The total operations costs was established at \$40.92million (this is including labour overheads, but not including management costs such as legal costs associated with negotiating access agreements or with the costs of regulatory submissions and approvals). This figure is the summation of costs for operations and on-costs of operations (which is the proportion of on-costs relative to operating / maintenance staff, operations, administration and on-cost costs, determined to be 22%).

The cost is distributed across users based on train-km (from Step 2). Table 8 shows the distribution of variable operations cost by user.

Table 8 – Distribution of variable operations cost by user (\$ million)

	Metro	V/Line	Freight	Other	Total	Basis
Operations	36.22	4.38	0.29	0.03	40.92	TK
Access-specific		0.04	0.16		0.20	
Total	36.22	4.42	0.45	0.03	41.08	

Source: Booz & Company analysis 2011

Step 4: Fixed costs

Step 4a:

Determine total fixed cost (excluding buildings) from Step 1 and distribute across route-km and track-km (with respective variable percentages of 20 and 80). Table 9 shows the distribution of fixed maintenance costs.

Table 9 – Distribution of fixed maintenance cost

	\$A million p.a.	Km	Unit cost p.a. (000)
Total network (excl buildings)	119.39		
% variable with route-km (20%)	23.88	430	56
% variable with track-km (80%)	95.51	871	110

Source: Booz & Company analysis 2011

Step 4b:

Estimate allocation of fixed costs on three bases – line by line, freight network as a whole and total network. Apply unit cost figures (from Step 4a) to route-km and track-km by line, freight network and whole network.

Model showed minor variability of distributed freight cost between base findings, and hence used the freight network as the most reasonable estimate. Table 10 shows the distribution of fixed maintenance costs on the shared network.

Table 10 – Distribution of fixed maintenance cost (excluding passenger-only network)

Basis	Train-km			Route-km	Track-km	Total Cost (\$ mill)	Distributed Cost (\$ mill)		
	Metro	V/Line	Freight				Metro	V/Line	Freight
Total line by line	9,802	1,914	171	167	395	50.07	40.5	8.7	0.9
Total freight network	9,802	1,914	171	167	395	50.07 ⁽¹⁾	41.3	8.1	0.7
Total network (excl buildings)	21,429	2,591	170	430	871	119.39	105.8	12.8	0.8

Source: Booz & Company analysis 2011

Step 5: Overheads

Determine proportion of corporate overhead costs relative to direct costs. These include insurance, IT, communications, property/accommodation, administration, professional fees, audit fees, legal fees, bank charges and other costs.

Direct costs include operating and maintenance staff, operations costs, Metlink and marketing.

This proportion (7.2%) along with a 3% profit margin gives the overhead mark-up of 10.2% which is applied to the access price (summation of component derived in Steps 3a, 3b and 4b).

Step 6: Reference Prices

Figure 3 illustrates the combination of these costs to create the floor price, the ceiling price and the price for 2010

Figure 3 Derivation of Floor, Ceiling Prices and Reference Price for 2010

Recommended Reference Prices		
Floor Price	Ceiling Price	Allocated Price
<ul style="list-style-type: none"> ▪ Variable maintenance / operations cost ▪ Fixed maintenance / operations cost (freight-only lines) ▪ Freight-specific / Access-specific overheads ▪ Overhead mark-up 	<ul style="list-style-type: none"> ▪ Variable maintenance / operations cost ▪ Fixed maintenance / operations cost (total cost) ▪ Freight-specific / Access-specific overheads ▪ Overhead mark-up 	<ul style="list-style-type: none"> ▪ Variable maintenance / operations cost ▪ Fixed maintenance / operations cost (distributed) ▪ Freight-specific / Access-specific overheads ▪ Overhead mark-up

Step 6a:

Determine floor price by summing the variable maintenance cost, variable operations cost and overhead mark-up and dividing by GTK of 207,000 from Table 6.

Floor Price: \$6.07 / GTK ('000)

Step 6b:

Determine ceiling price by summing the variable maintenance cost, variable operations cost, fixed maintenance cost on freight network (total) and overhead mark-up and dividing by GTK of 207,000 from Table 6.

Ceiling Price: \$272.49 / GTK ('000)

Step 6c:

Determine allocated price by summing the variable maintenance cost, variable operations cost, fixed maintenance cost on freight network (for freight) and overhead mark-up and dividing by GTK of 207,000 from Table 6.

Allocated Price: \$9.75 / GTK ('000)

Table 11 shows the summary of freight costs for the base year of 2010.

Table 11 – Summary of freight costs (\$ mill p.a.) 2010 (\$2010/11)

Freight cost components	Floor	Ceiling	Allocated
Variable maintenance cost ⁽¹⁾	0.665	0.665	0.665
Variable operations cost ⁽²⁾	0.288	0.288	0.288
Fixed maintenance cost on freight network ⁽³⁾	0.029	50.065	0.720
Fixed operations cost on freight network	0.000	0.000	0.000
Freight-specific overheads	0.000	0.000	0.000
Access-specific overheads ⁽²⁾	0.158	0.158	0.158
Mark-up (10.2%)	0.116	5.229	0.187
Total Variable Cost	1.257	56.405	2.018
Cost per '000 GTK	6.07	272.49	9.75

(1) As determined in Step 3a

(2) As determined in Step 3b

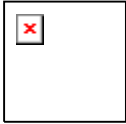
(3) As determined in Step 4b

APPENDIX E | GHD REPORT

Essential Services Commission

MTM's Access Arrangements Review of Maintenance & Operations Costs

May 2011



This review of MTM's Maintenance & Operations Costs ("Report"):

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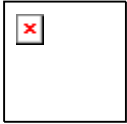
To the maximum extent permitted by law, all implied warranties and conditions in relation to the services provided by GHD and the Report are excluded unless they are expressly stated to apply in this Report.

The services undertaken by GHD in connection with preparing this Report:

- were limited to those specifically detailed in this Report;*
- did not include the Excel model provided by booz&co including its derivation of train kilometers and other parameters.*
- The opinions, conclusions and any recommendations in this Report are based on assumptions made by GHD when undertaking services and preparing the Report ("Assumptions"), and a re stated in the report*

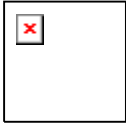
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Subject to the paragraphs in this section of the Report, the opinions, conclusions and any recommendations in this Report are based on conditions encountered and information reviewed at the time of preparation.



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1. Background and Scope

1.1 The Essential Service Commission's Role

The Essential Services Commission (the Commission) is the independent economic regulator of prescribed industries in Victoria. It is responsible for regulating and administering an access regime for the Victorian rail industry.

The Commission's regulatory powers in relation to the Victorian rail industry derive from the *Rail Management Act 1996* (RMA). The RMA sets out the access regime that applies to providers of declared rail infrastructure.

Metro Trains Melbourne Pty Ltd (Metro) is the operator and access provider for the Melbourne metropolitan rail network, which has been declared for third party access. Under the RMA, Metro must at all times have an approved access arrangement.

The Commission must assess the access arrangement in relation to certain criteria one of which is to determine an access price that recovers the efficient cost of the access services provided. Over the proposed five year regulatory period, Metro's maintenance costs are forecast at almost \$634 million, and operations costs are forecast at only \$2.4 million. As such, the reference tariffs proposed for the next regulatory period are predominantly driven by the level of maintenance costs

1.2 Scope of tasks required from consultant in the correspondence

The Commission requires written advice and a report in relation to:

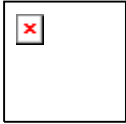
- . . . The reasonableness of Metro's operations costs (for train control operations, regulatory/advisory/legal and overheads) with a view to confirming that these represent a reasonable estimate of the efficient costs involved.
- . . . on what basis should overheads be allocated?
- . . . Metro's maintenance spend. That is, an assessment of whether the quantum it is efficient.
- . . . Other advice as agreed between the ESC and GHD.

1.3 Subsequent Discussions and Refinement of Scope

Some refinement of the Scope provided in section 1.2 has occurred and this section will indicate GHD's understanding.

At a workshop held on Friday 13th May, booz&co offered to provide support by way of constructing a model to quantify the usage of freight, VLine passenger and Metro services within the relevant network, and to propose a mechanism to allocate costs.

In addition, it was agreed by all parties that the definition of the Ceiling for Freight should be Total costs minus incremental Metro and VLine costs and the model would be used to calculate those data.



GHD's role would therefore be to review the MTM Asset Management Plan (AMP) and the Annual Works Plan (AWP) to draw conclusions about the nature of the work to be performed and its characteristics in relation to the part of the network where freight services operate and the degree of variability with usage that is embodied within that work plan. Combined with the usage data provided by booz&co, a calculation could then be completed in the spreadsheet model.

In addition GHD would provide a commentary of the AMP and AWP with respect to the efficiency of the works.

1.4 Previous ESC Decision

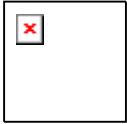
So as only to contrast the approach by the Franchisee and the rationale of the previous decision compared to this current review, this section will briefly elaborate on the overall methodology of the previous access arrangement.

The access arrangement and costs proposed by Connex reflected that of a "steady as you go" approach to the management of the system. Despite large expenditure on reactive maintenance Connex indicated a like for like replacement basis for their work program.

In terms of calculating the ceiling cost this was done on the basis of a stand-alone approach, with the ceiling calculated as the proportion of availability of the network. As suburban train services take most of the capacity during the day, the majority of the capacity available to freight services is after normal hours. In total 44% of the availability was calculated as being available to freight services. This calculation consisted of estimating the total capacity available for freight for each hour of the day. For example at 2am to 3am it was assumed the freight available capacity was 100% whereas at 7am to 8am there would be no capacity for freight. Other hours of the day attracted different proportions.

The previous decision also incorporated a calculated proportion of work associated with freight specific activities. This was arrived at by inspection of the work program and identifying specific work activities that were most likely to have been associated with freight traffic damage. Typical work identified as being caused through freight traffic includes rail wear, turnout deterioration and insulated joint defects or renewal. These are activities associated with heavier axle loads and freight bogie designs, and resulting in high impact forces. Track geometry deterioration is also impacted to some degree except that in the Melbourne soil context, most track geometry deterioration can be attributed to weather conditions and the reaction with the clays.

The assessed variability due to freight traffic was 5% of the total costs incurred on the part of the network where freight trains operate.



2. Context of the AMP and AWP

2.1 General Observations

These documents provide a clear strategy as to the works to be undertaken over an 11 year period of the franchise. The strategy is supported by MTM's own inspection of documentation provided in the Data Room at the time of tender and their own site observations as to the condition of the infrastructure and the perceived requirements for the future.

The works program outlined in the AMP is heavily oriented toward improving service standards compared to the previous franchise by way of improving infrastructure reliability. The term "improving reliability" is interpreted or presented by the documents as to mean a reduction in unplanned delays caused through infrastructure faults.

This requirement has been variously been attributed in the documents to both the government's desire to improve service levels, delays to timetable being one main Key Performance Indicator (KPI), and to MTM's own self imposed desire to improve reliability.

Whatever the justification for this approach it is very clear in all parts of the documentation that this is not a steady state, "continue as previous", strategy. This is a very deliberate, improvement strategy.

Consequently there are various elements of the work program that are designed to achieve this improvement. There are references to, and strong implications as well, that the plan is also designed to address a maintenance deficit which combined with a deliberate improvement beyond the desired standards of the previous franchise, result in works being undertaken that are akin to the rebuilding of parts of the network. This is not a plan of simply replacing life expired equipment in the normal course of steady state maintenance, but one which is to recover a severely degraded asset.

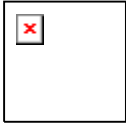
In addition, not only is the work itself oriented to these goals but the management systems have also been given emphasis for improvement to underpin those goals. A great deal of effort is planned to improve these systems, including updating and creating Standards.

Consequently, it is hardly surprising that the expenditure forecast by MTM is greater than the previous franchise in both the works and in the overhead area.

The context of the AWP is to provide more detail on a rolling annual basis for the works to occur in the next year. Consequently, while the AMP provides a year by year plan as to what works will satisfy the overall strategy, the AWP is reworked every year to take into account any urgencies or local variations.

2.2 Improved Maintenance Functionality

The AMP details a deliberate attempt to provide for equipment and materials which is of a higher standard than the equipment and materials currently in use.



The plan provides for each engineering element, track, signals, structures, electrical overhead & traction (not relevant for freight), "Improvement Initiatives", designed to respond to the government's desires or to MTM's own desires for improvement. These improvements have the characteristics of both a reaction to the degraded state of the asset as well as a desire to look to long term whole of lifecycle cost optimisation. The AMP refers to the basic approach of planning for asset lives of 40 years.

Innovations in the AMP include:

In Track

- Increase the frequency of Ultrasonic Testing by rail mounted vehicle
- Increase the frequency of ultrasonic testing in specific locations with hand held devices
- Put into place measures that will significantly reduce the risk of track buckles
- MTM will introduce a system to bar code all new welds
- Rubber surface panels will be used on all isolated pedestrian crossings
- MTM will increase track surfacing to 250km per year
- MTM will replace 200 bolts in the MURL tracks per year

In Structures:

- MTM will target the renewal of assets that have been too difficult or complex to complete in the past
- MTM have included retrofitting of fall protection to bridges

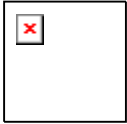
In Signals

- A review of the current set of plans and drawings
- Due to existing inconsistencies and omissions in the Asset Register this must be verified immediately to establish actual assets in service
- MTM will improve the overall capability of the Fault Recovery Centre
- MTM will re-instate remote air supply monitoring and switching capability
- Fault Centre Improvements - Increased staffing levels to 9 instead of 6 currently
- Planned Maintenance teams. - An additional team will be added to the Support Group.

In Operations:

- MTM will audit all of the OCS equipment for which it is responsible and include it in the Mincom Ellipse Asset Management System to ensure that all the assets are accounted for and subject to regular maintenance
- MTM will enhance infrastructure maintenance through the introduction of a new Mincom field computer platform
- operate a single Asset Management System (AMS) across the business for communications assets

These improvements not only require replacement maintenance with new and upgraded equipment but also increases in inspection regimes.



3. Efficiency Implications

Having foreshadowed a large increase in the target for infrastructure reliability in order to offer an improved train service, and in addressing a maintenance deficit, MTM have outlined a strategy that is not steady state in nature and is addressing many issues that have accumulated with time, as well as with usage.

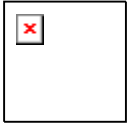
The model produce by booz&co indicates total track km for the whole Metro network on 851km and a total maintenance and operations budget of \$126.8m per annum average over 5 years of the regulatory period . This implies an annual average cost per km of \$146,000. This is considerably higher than freight networks, which range between \$20,000 to \$50,000 per annum¹ and while suburban railways have assets associated with stations and traction power, the quantum in the current AMP is considerably higher than could be expected if the assets were in a steady state maintenance condition.

In as much though that MTM is offering open tenders² for major works such as renewals, the market is continuously being tested for a very large part of the program. In house resources are associated with Inspections and Routine Maintenance as well as Reactive Maintenance.

Any further evaluation of efficiency would require a detailed analysis of unit rates and even then comparison with other railways is limited in its validity given the different operating environment of the Melbourne system to other systems.

¹ Working Paper 2, Usage-related infrastructure maintenance costs in railways, Queensland Competition Authority, 2000

² Personal communication 10th May 2011



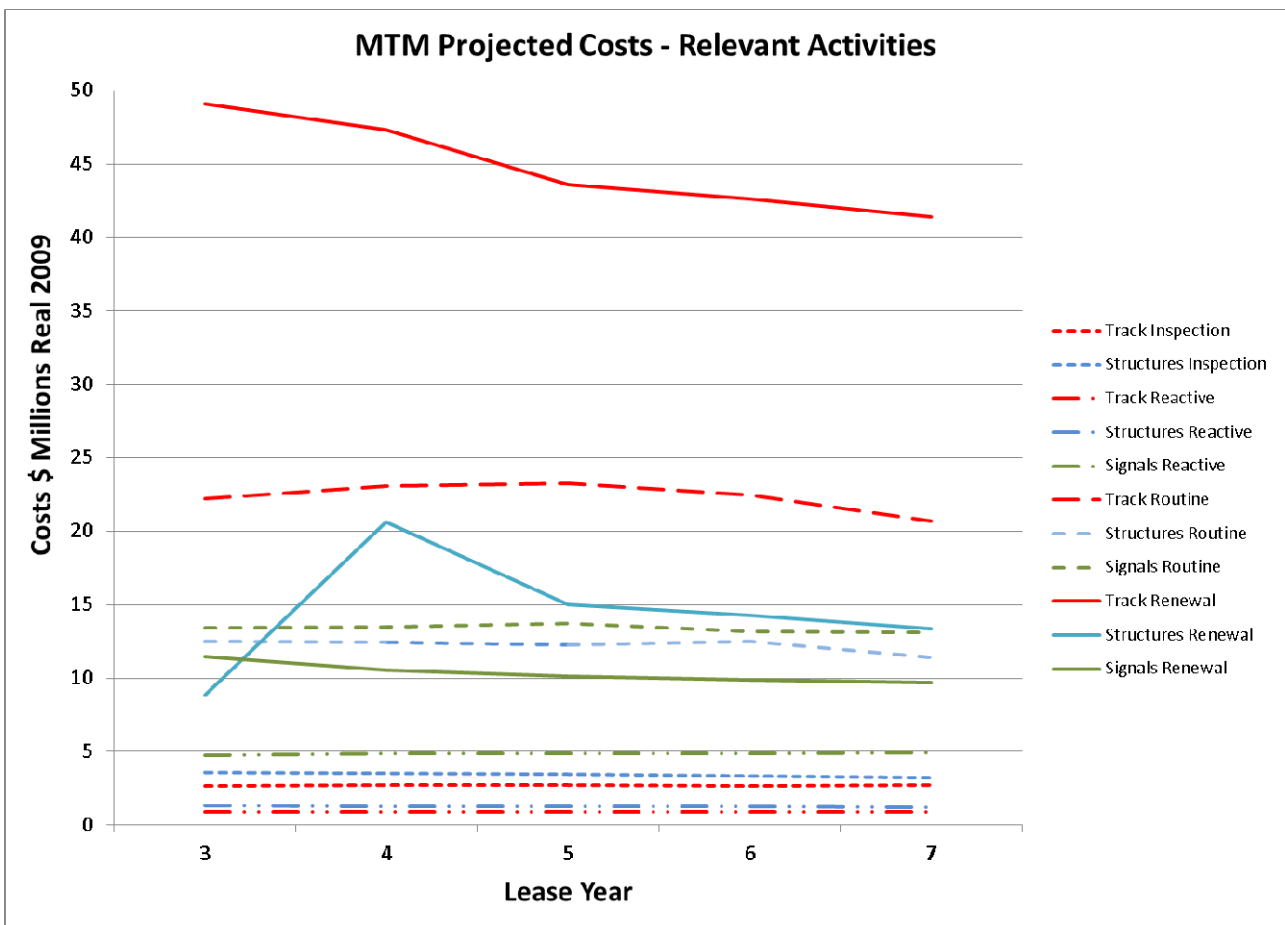
4. Work Program Content and Cost Variability

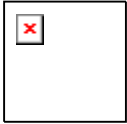
Each component of the work program displays its own characteristics as to the variability of cost with usage and for this analysis we have commented at the activity level to draw conclusions about the appropriateness of a variability factor given the unique circumstances of the current network.

Using Table C8 – Lease Year 1 to 11 – Summary – No CPI as the primary basis we have reviewed the dialogue in the AMP and AWP, and the estimates of cost for years 3 to 7. We have noted other expenditure both before and after that period in terms of the trends indicated.

In Figure 1 we have shown for the expenditure items relating to the freight task the trend and comparative level and we have used this data with the other detail of the AMP to draw our conclusions as to the variability of maintenance expenditure.

Figure 1 Expenditure in real \$ (2009) proposed in MTM's AMP





4.1 Track Inspections

In this activity a regime of inspections involving highly manual and automated machine measurements are combined to create a view about the condition of the asset and the work program, either for short term work related to correction or longer term program for preventative or for halting deterioration.

Many inspections are time based but we particularly note that MTM has a strategy to base inspection frequencies and work on the basis of condition. This is a modern approach. There still remains an aspect of due diligence where timely inspections underpins a safe railway.

Certainly for the regulatory period where it is expected that the condition of the network will still not be at a stable level given the maintenance deficit, the inspection regime is likely to be wholly time based where resources are allocated for this function on a continuous basis. This profile matches the profile of expenditure proposed by MTM.

Therefore we conclude that there is no variability with usage during the regulatory period or where there may be due to assets completing their lives and there being extraordinary attention, that the quantum is immaterial.

4.2 Track Reactive Maintenance

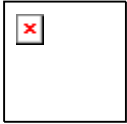
In this activity maintenance is performed due to a breakage or failure of a component such as a broken rail or defective signal.

The MTM AMP portrays a high level of reactive maintenance compared to planned maintenance. We would expect this to be the case at the beginning of the franchise and we would also expect that the level of reactive maintenance to that of planned maintenance would reduce toward the end of the franchise as the planned improvements give greater infrastructure reliability.

This later expectation is not shown and one could therefore conclude that the improvements are only keeping pace with the on-going deterioration or that resource levelling has been applied over the franchise period and during the regulatory period.

While reactive maintenance is required after a failure, and failures will normally occur when a train uses the infrastructure it would be reasonable to expect that a high variability exists with usage. However in the incremental sense, if a failure was going to occur anyway, because of poor condition that had accumulated over a long time, the failure is somewhat predictable.

The balance of whether a failure and the consequent reactive maintenance is predictable or whether it occurs “out of the blue” means that some of those resources are deployed on a permanent basis, in expectation that a failure will occur. In that sense they are fixed and that only when other resources, not usually used in that maintenance are deployed do they become variable. In fact many teams are positioned around the system at peak times to ensure they can be deployed quickly to attend a problem.



These resources are fixed but in that particular case they are able to get on with their other work attending to short term corrective but not critical maintenance.

For that reason our estimate of the variability is that about half those resources are fixed in nature.

4.3 Track Routine Maintenance

In this activity, resources are deployed “routinely” or with a high degree of knowledge of what they will be attending. These activities relate to periodic cleaning, adjusting, lubricating, and tightening. The work is therefore quite predictable.

The work does however respond to the incremental extra loading and traffic above a certain base level because some components may wear out faster or be vibrated one more time. Therefore a component of their otherwise base level, which is mainly based on time return periods, will be variable with traffic. In the Metro case, the passenger component is at such a large proportion of total traffic that it is that traffic that determines the return period or schedule of work. The variable component is small.

We conclude that only 10% of the work is variable and this is reflected in the profile of MTM expenditure during the regulatory period, whereas despite increasing passenger traffic being projected, the expenditure in this area remains flat.

4.4 Track Planned Renewals

In this activity, MTM has projected a work program that is designed to both lift the previous standard of reliability of infrastructure and to address the maintenance deficit.

The program is therefore determined by considering more long term objectives and this is reflected in the profile of expenditure where planned renewal expenditure is consistently high compared to the previous franchise.

In the normal course of events one would expect to see a peak of work to address maintenance deficits or to lift standards. The profile of expenditure is flat and high meaning that the program is a long term attempt to achieve those objectives.

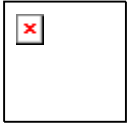
In addition, as the planned number of suburban trains is to increase these works do not respond to that relatively short term input. The MTM program is therefore relatively fixed to address these longer term issues.

We conclude, based on the quantity of rerailling, turnout renewals, rail adjustments and rail grinding, all activities most closely related to the number of weight of the traffic, that approximately 20% of this activity is variable

4.5 Track Unplanned Renewals

In this activity, an inspection has revealed the necessity to replace a component and this had not been observed as needing attention previously.

MTM does indicate that the work program in any one year will vary depending on a condition assessment at the time and this area of expenditure is particularly affected.



In as much as the failure to observe an impending infrastructure failure, a latent condition as such, is an indication of either a particular set of loading occurrences, such as with a flat³ wheel, or is an accumulation of circumstances out of the ordinary, this activity is highly variable.

We conclude that 80% of unplanned renewals is attributed to the variability of the loading and this is relevant particularly with freight vehicles which have unsophisticated bogie construction and are more prone to these types of defects.

4.6 Signals

In this activity, a combination of inspections and renewals occurs in much the same way as the track area. However signals do not wear out as such. In general signalling equipment, like any electronic and electrical equipment has a useful life, sometimes determined by exposure to the elements, UV deterioration and electrical fatigue as well as by the ability to obtain spare parts.

The matters are mostly time related matters and a very small proportion of the life of these components and the inspection frequency is determined by the actual traffic. A small number of components are subject to the vibration of trains, such as connecting cables and points (turnout) components.

Therefore we conclude that only 5% of the maintenance associated with signals is variable.

4.7 Structures

In this activity, maintenance of railway structures such as bridges as well as for retaining walls and other earth support structures is included.

The AMP indicates a large backlog of maintenance is required and it is apparent that a higher level of customer service is targeted at the stations.

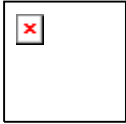
The relevant structures that may be impacted by the running of freight trains are the underbridges, that is, bridges that support the railway, not those that are above the railway.

The capital cost of bridges on freight routes would usually be designed for heavier axle loads than for suburban trains but it is unknown whether this has occurred and irrelevant for considerations of maintenance cost.

Maintenance for these structures includes inspection and repair that targets corrosion of the beams and structural elements as well as the bearing condition. The bearings are those parts of the bridge that support the beams onto the pylons and become dislodged, or the pads that support the bearings become cracked. In most cases both the corrosion and the bearings and their pads deteriorate due to weathering.

In some cases underbridges are damaged by road traffic where a road is under the bridge, and not usage dependent.

³ A wheel that has skidded and formed a flat piece on the circle and then gives large impact



Given the very small number of freight trains, estimated at approximately 1.5% of the total number of train kilometres by the booz&co model, the influence of freight trains on structures maintenance and the subsequent link to variability is immaterial and therefore our conclusion is that there is no discernable variable cost for structure.

4.8 Buildings

We have observed no buildings on the railway system, maintained by Metro, that would be relevant in the consideration of variability for freight purposes.

4.9 Power

This maintenance activity relates to the maintenance of the traction power assets, overhead catenary and associated infrastructure and has no relevance in the consideration of variable costs associated with freight or VLine passenger trains.

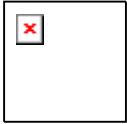
4.10 Operating Control Systems (OCS)

In this activity the assets associated with all the Metrol (train control) signals and communications systems and most other communications systems are inspected and maintained. These systems include train control, passenger information systems, train radio, CCTV and platform equipment.

The quantum of expenditure⁴ included in the AMP for OCS maintenance is similar to the quantum for signals maintenance. The AMP identifies a modernisation and asset management initiative and therefore there is a large proportion of the expenditure associated with upgrading. In addition the AMP highlights the need to improve those systems that are immediately in the public interface and improvement in reliability are targeted.

As it was, the variability of signals related costs were assessed at 5% and that these related to the much more closely aligned reference to the actual running of trains. Therefore for OCS expenditure the relationship is a small percentage of that base. As many of the systems are directly passenger related, that there is a conscious effort in the plan to improve the functionality and reliability, and that with the exception of train control there is no relationship with freight movements we conclude that the variability and relationship is immaterial.

⁴ Table C8 – Lease Year 1 to 11 – Summary – No CPI (Real\$)



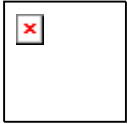
5. Summary

The Asset Management Plan and the Annual Works Plan for MTM's infrastructure assets has been reviewed and estimates have been made of the variability of the maintenance costs with usage.

Overall, the AMP is shown to portray a strategy which is heavily oriented toward an improvement of the reliability of the infrastructure and which also addresses a maintenance deficit.

Consequently, for most activities there is little relationship between usage and cost and therefore the variability proportion is low. Most of the costs are fixed in that longer term objectives are being sought and these overwhelm the objectives associated with the shorter term usage related activities.

In effect, the AMP is a strategy to rebuild the network, to permit a higher level of reliability and therefore improved train service reliability.



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Document Status

Rev No.	Author	Reviewer		Approved for Issue		
		Name	Signature	Name	Signature	Date
F	M Baggott			M Baggott	(signed)	20/05/2011

