

**ECONOMICS AND INDUSTRY
STANDING COMMITTEE**

**INQUIRY INTO THE MANAGEMENT OF
WESTERN AUSTRALIA'S FREIGHT RAIL NETWORK**

**TRANSCRIPT OF EVIDENCE
TAKEN AT PERTH
WEDNESDAY, 11 JUNE 2014**

SESSION ONE

Members

**Mr I.C. Blayney(Chair)
Mr F.M. Logan (Deputy Chair)
Mr P.C. Tinley
Mr J. Norberger
Mr R.S. Love**

Hearing commenced at 10.01 am**Mr PAUL LARSEN****Chief Executive Officer, Brookfield Rail, examined:****Mr ALLAN JAMES ROSE****Chief Adviser, Commercial, Brookfield Rail, examined:**

The CHAIR: Thank you. On behalf of the Economics and Industry Standing Committee, I would like to thank you for your appearance before us here today. The purpose of this hearing is to assist the committee in gathering evidence for its inquiry into the management of Western Australia's freight rail network. You have been provided with a copy of the committee's specific terms of reference. At this stage I would like to introduce myself and the other members of the committee. I am Ian Blayney, the member for Geraldton; next to me is the deputy chair, Hon Fran Logan; my other committee members are Jan Norberger, Peter Tinley and Shane Love. The Economics and Industry Standing Committee is a committee of the Legislative Assembly of the Parliament of Western Australia. This hearing is a formal procedure of the Parliament and therefore commands the same respect given to proceedings in the house itself. Even though the committee is not asking witnesses to provide evidence on oath or affirmation, it is important that you understand that any deliberate misleading of the committee may be regarded as contempt of Parliament. This is a public hearing and Hansard is making a transcript of the proceedings for the public record. If you refer to any documents during your evidence, it would assist Hansard if you provide the full title for the record. Before we proceed to the inquiry's specific questions we have for you today, I need to ask you the following: have you completed the details of witness form?

The Witnesses: Yes.

The CHAIR: Do you understand the notes at the bottom of the form about giving evidence to a parliamentary committee?

The Witnesses: Yes.

The CHAIR: Did you receive and read the "Information for Witnesses" sheet provided with the details of witness form today?

The Witnesses: Yes.

The CHAIR: Do you have any questions in relation to being a witness at today's hearing?

Mr Larsen: My only question, Mr Blayney, is whether I will be given the opportunity to make an opening statement.

The CHAIR: Yes.

The Witnesses: Thank you.

The CHAIR: Would you like to carry on with your opening statement?

Mr Larsen: Thank you, Mr Blayney. I also have with me today, Mr Matthew Benter, who is head of legal, to assist with any specific technical issues that might arise during today's hearing. I would like to note that we have made a substantial written submission to this process and I may refer to that submission during my statement and responses to any of your questions. I would like to start by making an overarching opening statement in response to the high-level question of whether the

current management of the Western Australian freight rail network facilitates or hampers state development.

In 2000 the Western Australian state government did privatise the freight rail network to increase volumes of freight on rail, facilitate investment in the rail network and increase the efficiency of the rail network to the benefit of the state. Our core purpose as an organisation is to be independent, be an open-access rail operator and ensure that we run a safe, efficient and reliable rail network that supports the economic growth of the southern half of Western Australia. Since privatisation there has been a lot of change. The freight task has constantly changed and we have provided details of that in our submission. We have continuously responded to these changes, improving our network to support these new projects and economic growth.

Over the last 13 years I am pleased to note some of these key outcomes. We have increased tonnages on the railway from 33 million tonnes to 71 million tonnes. That is a 113 per cent increase. We have invested \$2 billion into upgrading, maintaining and modernising the network and we have also introduced initiatives to improve the efficiency of rail, working with our customers to ensure their supply chains are operating at very high levels of reliability. This growth in volume could not have occurred without that level of investment that I just talked about—the \$2 billion. Our focus has been, across the entire network, the midwest, the south west, goldfields and wheatbelt regions. These projects have allowed us to deliver a modernised and upgraded rail network, which is enabling customers' projects to start to develop and in fact, expand in some cases. I think the best example of this is in Mr Blayney's own electorate in the midwest where, through a \$550 million investment we transformed a three-million-tonne railway into a 16-million-tonne railway carrying lots of iron ore through the port of Geraldton, which has been hugely beneficial for the customers, for the state and for the region much. Other examples include major upgrades to the vital link between Perth to Kalgoorlie and rebuilding the entire Esperance line.

All this has been achieved with the oversight of three regulatory bodies, the PTA, the Office Of Rail Safety and the Economic Regulatory Authority. The growth has been achieved with their oversight but without any need for their intervention. In fact, we know that one of these bodies was subject to the Office of the Auditor General's inquiry last year—the PTA. This report recognised the success of privatisation, that there had been investment and growth in the network and that the state's interests are being protected. More specifically with our network, when it comes to grain, we are currently supporting the transportation of grain at record rates—10 million tonnes per annum annualised is what is moving on our network through to the Western Australian ports. These are record tonnages of grain being moved today. So I would like to make some more specific comments about WA's grain freight task.

We know that today WA growers do benefit from very competitive rail freight charges. Recently the Australian Export Grains Innovation Centre, or AEGIC for short, examined the supply chain costs of each of the states around Australia and determined that WA was in fact 20 per cent cheaper than the other states. AEGIC also found that grain supply chain costs have reduced from around 30 to 35 per cent of the free-on-board price of the 1980s to now around 18 to 20 per cent, so a significant reduction as a proportion of the FOB price. AEGIC also established that WA's rail freight cost is substantially lower than all the other states and was a substantial contribution to why the supply chain costs in WA are better than the other states. This comparison is even before we consider the subsidies provided by governments in the eastern states; for example, and I have made reference to these reports in our submission. The government of New South Wales spends \$40 million a year maintaining a 1 200-kilometre grain network and recovers \$800 000 in access fees per annum from the farmers. In essence, they are providing a huge \$39.2 million annual subsidy to the rail network. This is on top of the \$277 million of capital investment they announced a couple of years ago that they are in the throes of completing.

So why has government had to provide subsidies? In essence, road freight transport does not pay for the true cost of its use of roads. The roads are there, anyway, to service the regional communities and trucks do not pay a fee that represents their usage. As a result, the mostly private rail industry is competing with a competitor subsidised by the taxpayer, so to level the playing field, the governments of Australia have also had to subsidise rail, particularly grain on rail.

I now want to talk more specifically about grain on rail in WA.

The CHAIR: We have got quite a few questions.

Mr Larsen: Yes; I have got about two minutes to go.

The CHAIR: Okay because I have got two minutes on my clock there. That is good, thank you.

Mr Larsen: For Brookfield Rail, the grain on average is around six million tonnes, using around half the network. The other half of our network we have 65 million tonnes of freight running on it. We know grain is a very volatile task due to whether it rains or not and much of our network is significantly underutilised. This is then compounded by the issue of the road competition that I mentioned, so the reality is that grain on rail in Western Australia also requires help from the government and this was recognised when the government privatised the railway in 2001.

[10.10 am]

The lease included clauses that allowed financial assistance to be sought. Following a process led by the government—the SGNR process—the government satisfied itself that Brookfield Rail was in fact entitled to this financial assistance and this committee, which comprised all levels of government, industry and farming groups, agreed and supported the government's policy decision to invest \$165 million into tier 1 and tier 2 lines and that, in the case of tier 3 lines, road transport would be used instead, because at that point it was cheaper. So, ladies and gentlemen, the solution that was endorsed by industry and government, which became government policy, is exactly what has been implemented to this day, and in order to effect these decisions, we did vary our lease agreement with the state government to reflect the investment into tier 1 and tier 2 and a time line was placed for setting tier 3 lines into care and maintenance post the completion of the \$120 million investment into the local roads. We will remain committed to exploring a commercial solution to try to keep the tier 3 lines open to an operational status, but the reality is, in the absence of agreement between Brookfield Rail and CBH that underwrites an agreed and appropriate level of investment into these lines, these lines cannot continue to be safely and sustainably operated. Unfortunately, there have not been any negotiations or an agreement concluded in this regard, including from the current ERA process. As a result, there is no agreement between Brookfield Rail and CBH for the continued operation of tier 3 lines past 30 June.

I would like to summarise by saying that back in 2000, the government's motivation was to privatise, find an owner who would introduce efficiencies and grow and invest in the network. Thirteen years later, we have grown the volumes from 33 million tonnes to 71 million, we have invested over \$2 billion directly into the network and we have increased the efficiency of the network. We are moving grain at record tonnages—10 million tonnes per annum. I think with the focus of this committee's questions around tier 3, we need to recognise it does represent around four per cent of those current total annual movements. I am happy to stop there and take questions.

The CHAIR: Thanks very much.

Mr F.M. LOGAN: Thanks, Paul. Thanks for coming along. If tier 3 lines are uneconomic, as you pointed out, and the company is determined to close them on 30 June, why do you not just hand those lines back to the government?

Mr Larsen: Our company is the party that has the contractual right with government to operate those lines, which includes the right to sell access, so we are willing to negotiate with any party that wants to seek access to those lines. We believe we are the party that has the best expertise and

proven capability, we are independent of any freight owners and train operators and, as I said, we remain willing and open to negotiate with any party wanting to seek access to those lines.

Mr F.M. LOGAN: But that was not the point. It was not about access; it was about the fact that your statement and your submission to the committee is that those lines are uneconomic. Why does the government not simply apply a use-it-or-lose-it approach to that contract, and why does your company not simply hand them back if they are uneconomic and of no use to the company?

Mr Larsen: I cannot answer the first question that you posed in relation to the question for government; I think that is a question government can answer, Mr Logan. I think I have answered the question in relation to our position, which is that we are the party that has the contractual right to sell access to these lines. We remain willing to do so. In the absence of an agreement between two parties as to how those lines might be used, without an agreement, there is no legal basis for investment to occur and for trains to run.

Mr J. NORBERGER: Mr Larsen, with what you have described, is that not the perfect monopolistic behaviour? Basically, you are saying that if you do not get the price that you want, you will take your toys and go home—you will shut down the tier 3 rail, but you will not hand them back either. We have been told that CBH has made at least two proposals to Brookfield to lease the tier 3 lines off Brookfield, to take over the maintenance of them, and to basically sublease them, and our understanding is that they have been rejected. Can you maybe shed some light on whether that is the case?

Mr Larsen: I think those discussions and conversations are confidential between the parties. I do not think we are saying we are not going to provide access; I think we are saying negotiations that are satisfactory to both parties have to occur for an access agreement to be concluded. Those negotiations have not occurred and have not been concluded.

Mr J. NORBERGER: But when you said negotiations, you are talking about a monopoly. CBH have got no other option but to deal with Brookfield. It is not an open market; it is not a free market. It is a monopoly. You can reject any offer that they make continually until you get what you want, and presumably you are quite happy to put the lines into care and maintenance rather than hand them back to the government.

Mr Larsen: Mr Norberger, we are railway people. We would love to find a way to keep the railway lines open. The lines do require investment. There needs to be agreement reached between the parties to an appropriate level and an agreed level of investment. Those negotiations have not occurred. CBH is seeking access to some of the tier 3 lines through the ERA process and, in fact, negotiations have not commenced under that process yet and cannot until the ERA has done its job. So, again, I come back to the point that we are the party that has the right; we did pay government for that right. We have invested in the lines, and we remain willing and open to negotiate with any party, including CBH, for access to those lines.

Mr P.C. TINLEY: I note you say—correct me if I am wrong—about four per cent of your total tonnage is off tier 3. That is accurate. Has it been constant? That would actually be a decline because of the closure of the tier 3, I would imagine.

Mr Larsen: There have been actually some quite drastic changes in the level of usage, particularly in the last four years. I have actually got some data here. In 2010, there were 600 000 tonnes moved; in 2011, 275 000 tonnes moved on tier 3; in 2012, 173 000; and then in 2013, 752 000. So there has been quite some volatility, obviously due to harvest sizes and other reasons.

Mr P.C. TINLEY: So a trend is not necessarily there, given that your total tonnages—so, your global tonnage moved across this network—are not necessarily reflective of how they get through. That will remain unchanged. I put to you that to get into particular points within the rail network, you do not care how they get there. I do not want to be prescriptive about that. You do not care how they get to the particular part of the rail network that you have as most profitable. Do you

understand or accept that the method by which the increased tonnages of that grain are getting to your nodes, if you like, through your part of the network is by road and that by closing tier 3 and removing that capacity of that infrastructure, you are actually transferring the cost of moving that grain onto the road and road network?

Mr Larsen: I do understand the point you have made, because that was the deliberation of the SGNR committee, which decided that investment in road would be preferred over investment in rail, and that is exactly the decision of the committee and the policy decision that was implemented by Minister Simon O'Brien that we have now implemented on behalf of the government.

Mr P.C. TINLEY: But in terms of your business and business model, it is quite attractive, surely.

Mr Larsen: As I have said, we are railway people. Our preference would be to find a way to keep all the lines open —

Mr P.C. TINLEY: I understand that, but I am talking about profitability now. The fact is you do not pay for the road infrastructure; you do not have to pay for it. All you have done is mothball, if you like, or put into care and maintenance a particular part of your infrastructure that is not as profitable as another part of your infrastructure, and your tonnages are unchanged. In fact, you still get the benefit; you get all the upside but you do not have to pay for any of the downside.

Mr Larsen: I am not clear on what your actual question is.

[10.20 am]

Mr P.C. TINLEY: The question I am putting to you is that the government and the taxpayer is now having to increase its spend on road infrastructure in order to get the same tonnages—increasing tonnages—to your business and you and your business have remained unchanged. I would even argue you are a significant beneficiary of that taxpayer-funded subsidy via the roads because you have been able to put your tier 3 lines into care and maintenance that are low profit making.

Mr Larsen: The situation you have just exactly described was the deliberation of the SGNR committee involving state government, local government and industry and farmer groups, which concluded that that decision was best for the industry. That is what has been implemented.

Mr P.C. TINLEY: And clearly best for your business.

Mr J. NORBERGER: Mr Larsen, it might be a good time to bring that up. If we are going to refer to the strategic grain network deliberations that took place, since that time, most of the parties that were part of that have since said, "Hang on a minute, that data really is outdated; it is no longer relevant." Apparently, one of the key inputs, if you like, that the decisions were predicated on was the price of diesel. One of the assumptions was that the price of diesel was going to stay at a particularly low level, which obviously is not the case, so the cost of diesel has risen significantly. A lot of the very same parties that you referred to that were part of those original deliberations—no-one is denying that those deliberations did not take place—are now saying, "Well, to refer to the data in the document now is not even remotely relevant anymore because the presumptions therein, we have moved way beyond, and to rely on that document that is no longer valid."

Mr Larsen: That is a very interesting comment, Mr Norberger, because my understanding of the intention of this process is that people on that side of the table actually review and critique that decision that was made by government. If that is your intention, I think government critiquing a decision that it made in 2009, it is fully entitled to do so. I think what has not changed is that the tier 3 lines, to stay safe and sustainable, still need significant investment, as did tier 1 and tier 2. In the absence of an agreement between a group of parties to see that investment occur, those lines cannot continue to be safe and sustainable. The references you make to the road transport side of things et cetera, if government wanted to review and re-critique that, I think that is government's prerogative to do so.

Mr J. NORBERGER: You have raised an interesting point, Mr Larsen. At the time when Brookfield and the previous entities took over the lease back in 2000, obviously, the network was handed over in a certain condition. We hear throughout your submission and even within the lease documents, the term “fit for purpose”. One would have to assume that the network was handed over in a state that was fit for purpose. Where does it become the responsibility for government to put more money in, as opposed to the requirement for Brookfield, because you are the one who is receiving the rail access fees, to be able to maintain those lines in an ongoing state of fit for purpose? You are charging the rail users to use the railway line. I can only imagine that part of your rail access fee surely must be an allowance for maintenance. At what point do you keep going back to the government and wanting hundreds of millions of dollars extra to apparently keep the lines in the same condition as they were handed over to you?

Mr Larsen: Certainly, the negotiations between Brookfield Rail and government around the investment into tier 1 and tier 2 have contemplated all the issues you just talked about. The point that I just made about tier 3 requiring investment to keep going is very relevant because in our agreement with government, what was reflected is that if that investment did not come for tier 3, the lines would be put into care and maintenance. Our agreements with government were varied to reflect the decision of SGNR and the policy direction of government, so we are fully compliant with all of our agreements with government.

Mr J. NORBERGER: Could you argue that even in that regard—credit to Brookfield—you have been able to get yourself into a lease position or you have been able to negotiate an agreement where really even you can hold the government to ransom? What you are basically saying is, “If you don’t give us \$120 million”, or whatever the amount might be, “We’re going to shut the rail down.” You can say to CBH, “If you don’t pay us this much, we’ll shut the rail down. We won’t hand it back. We’ll hold onto the corridor.” You might see some value in the corridor between now and 2049 for future mining. You do not want to hand it back but if you do not get what you want, you will basically just shut up shop.

Mr Larsen: I think the reality is that the decision was made to invest the money into the road system over the rail system. Our part to play in that was to keep the tier 3 going whilst the road system was invested in and then put it in care mode. We have delivered what the government asked us to deliver and what is reflected in our agreements. If, in 2009, the government said, “We prefer to keep the tier 3 rail going”, we would have implemented that decision also.

Mr J. NORBERGER: I am just interested to know why the government has to put hundreds of millions of dollars back in. You have obviously had the rail lines since 2000; you have had them for a long time, and the complete network. You are obviously isolating one particular segment. You are saying, “This segment is not as profitable”, which is exactly what Mr Tinley was saying, yet I think you have played your cards fairly well, but as a network, you are obviously making good money. You are charging railway access fees. A portion of that surely must be for maintaining and upgrading. You talk about sleepers, for example. You know that they need to be replaced. Why are you not covering that cost of maintenance with the money that you are generating? Why go back to the government and ask for hundreds of millions of dollars on top of that?

Mr Larsen: The issues I spoke about were road transport and the impact that has had on grain and rail around Australia. They were recognised by the government when it privatised the railway, hence the clauses around seeking financial assistance were built into the lease, which really revolved around those lines and the cash load that is generating. If it is going to be negative, the government would play a role; hence, the government did not get involved in tier 1 and tier 2. Clearly, tier 3 is not a lot different from tier 1 and tier 2; in fact, it has a lot less volume than tier 2. So tier 3 passes all the same tests. The decision of government was to invest in a road system and not the rail system. It was called the Brookton strategy. If government wants to review that decision, that is the government’s prerogative.

Mr F.M. LOGAN: Can you clarify something for the committee? Coming out of the Brookton strategy, on the basis of the decision to put the tier 3 lines into care and maintenance and the original lease obligation that in 2049 the lines will be handed back to the government in the same condition as they were in 2000, how can you actually deliver on that part of the contract or was that part of the contract modified as a result of the Brookton strategy; that is, you do not have to hand those lines back in that condition?

Mr Larsen: To clarify, Mr Logan, your question is in reference to tier 3?

Mr F.M. LOGAN: Tier 3. We cannot understand: if you are obliged to hand the lines back to the government in the same condition they were in 2000, and on 30 June you will close them down and they will go into care and maintenance and never open up again, how can they be handed back in the same condition they were in 2000?

Mr Larsen: I think I have said a number of times today—the OAG also reviewed all our contracts last year—our contract with government was varied to reflect the tier 3 lines being wound down in a performance standard and put into care and maintenance.

The CHAIR: So what is the cost of putting it into care and maintenance?

Mr Larsen: Mr Blayney, you are looking at things like fire protection and these sorts of things. It is an entirely different matter to maintaining the railway at an operational and safe standard.

Mr R.S. LOVE: If I might turn to a tier 2 line—the Miling line. As you know, it did not receive funding under the SGNR process, but it was the subject of an upgrade following the purchase of the rail network in the early 2000s. The SGNR report, at finding 17, recognised that the line needed to be the subject of a review at about this time—2014—I am just wondering what your understanding is of the process in the conduct of this review, who is responsible for conducting the review, will Brookfield be undertaking such a review, and will government be approached to fund a transport solution for Miling?

[10.30 am]

Mr Larsen: Mr Love, I think it is the responsibility of the users of the line and the operators of the line, being ourselves, to traditionally develop an understanding of what the freight task might look like going forward, including how much of the grain that goes into those bins would go on rail versus road. Once we understand the nature of the task, what times of year it might run, what the preferred model of operation is in terms of train length and size and those sorts of things, we could then establish an agreed and appropriate level of investment to sustain that operation into the future. If that level of investment meant that the subsidised road alternative was substantially cheaper, I think that, like tier 1 and tier 2, may then require a discussion with government about what interest government might have in helping to close that commercial gap.

Mr R.S. LOVE: Okay. In regard to that particular finding, it makes note of that review being conducted in conjunction with an assessment of their success—I am reading the findings of the Brookton strategy. The Brookton strategy is a strategy that involved the use of road to come together at certain sites. That has not actually been implemented, has it? If that has not yet been implemented, where does that leave finding 17 in regard to the future of Miling?

Mr Larsen: I think the reality is that part of the Brookton strategy had been implemented—I referred to the levels of volume on tier 3 earlier. Clearly in some years, particularly 2011, when there was 275 000 tonnes, and in 2012 when there was 172 000 on rail, a lot of the other tonnes from those bins have gone on road somewhere and they may have all gone to parts of what was included in the Brookton strategy—that is, taking tonnes to Brookton or Kellerberrin. So what has not happened as part of the Brookton strategy is the investment that was required in the terminals—the CBH terminal at Brookton and the CBH terminal at Kellerberrin. The road investment has been implemented, obviously, by WALGA and the local governments over the course of the last three years. I think the answer to your question is that it has been partially implemented.

Mr F.M. LOGAN: Can I just respond to that and just put some evidence to you that we received when we were at Bruce Rock? As you know, we were out there taking evidence from both shires and farmers from around the central wheatbelt area. We drove up there, and we drove up Quairading Road, past the site of the derailment on that tier 3 line from Quairading. It was quite obvious that Quairading Road has not been upgraded at all, much; some parts have been upgraded where they have put strips along the side of the road for the size of the trucks, but apart from that it has not been upgraded to the standard that would be needed to shift everything via road. The evidence we received from the shires themselves from across the central wheatbelt area confirmed that that investment had not been made. You pointed yourself to the fact that that investment was not made at the Brookton terminal and it was not made at the Kellerberrin end either. Would you like to express a view about the failure to comply with that aspect of the Brookton strategy, given that as of 30 June, as you know, there will still be hundreds of thousands of tonnes of grain in the wheatbelt ready to be moved to port, and we are facing, hopefully, the biggest harvest Western Australia has ever seen?

Mr Larsen: Mr Logan, I cannot recall the exact detail of every individual road that was intended to be upgraded under the SGNR report. My memory may fail me here, but I think the tonnes from the Quairading bin were intended to be taken north to Cunderdin. I have driven that road a number of times, and that has been upgraded although there may be an issue with the culvert that needs to be addressed.

The CHAIR: Nothing has been done with the culvert.

Mr Larsen: In summary, my understanding is that the York–Quairading road was not a road that was identified for investment. All I can say is that during the SGNR process, which involved a lot of people sitting around the table, local government was represented by WALGA. They were asked by Minister O’Brien, “Is that \$120 million enough to implement what’s in here?” And it was a categorical yes. I am not a road expert, but what I do know is that from the party that was taking on that task there was an emphatic yes.

Mr J. NORBERGER: With some of the discussions we have had with a variety of parties there has been considerable frustration expressed to the committee in relation to the non-disclosure of the terms of the lease arrangement, and the subsequent lease amendments. We know the original lease documents are in the public domain now, but obviously the annexures and the schedules and then the subsequent amendment are not. What is Brookfield Rail’s response to such frustrations from the community out there that they believe that by not being able to see what is in the lease, they are running blind? How will publication of the lease instrument, associated schedule and annexures and the lease variations affect Brookfield Rail’s operations?

Mr Larsen: I was not present, but there was a hearing at which two of the gentlemen with me here today attended on 27 May, where I think we provided sufficient response to that question around our reasoning as to the status of those documents. I do not think we actually have anything further to add.

Mr J. NORBERGER: Does it worry you as a corporate brand—you obviously want to maintain your brand image—what that is doing? You are coming across within the community—this is a bit of free feedback here—as being highly secretive, by virtue of it being all hidden and secretive and commercial-in-confidence. All that is doing is making people believe you have something to hide and that you are the big mean monopoly.

Mr Larsen: Mr Norberger, I accept that feedback. I also regularly meet with groups of farmers myself, with local shires, and I can tell you the feedback from a lot of our customers on our network, with what we have done to grow the volume from 33 to 71 million tonne, is the polar opposite to some of the feedback you are providing today. I think the reality is in the corporate world you have got to take the good feedback with the bad feedback. We take the bad feedback on the chin and try to do the best we can. I honestly believe our organisation, in relation to this whole

issue of grain on rail, has nothing to hide. In fact I am proud of what we have done and where we have got to. Record tonnages are being moved today. Yes, tier 3 is an issue, we would love to find a solution, but I do not think that means we are a big, bad, horrible monopoly. I think we have actually done a lot of good as well.

Mr J. NORBERGER: Okay, sure. The committee just notes that rail access pricing in Queensland—that is just as an example—is much more transparent than what is the case in Western Australia. Lack of transparency obviously in WA is owing to the operation of section 50(3) of the Railways (Access) Code 2000 which permits Brookfield Rail as a rail operator to require information provided to the Economic Regulation Authority regarding network operation costs to be kept confidential. If section 50(3) of the code were to be removed and rail access agreements registered with and published by the ERA, how would greater transparency into network access pricing affect Brookfield Rail?

Mr Larsen: As I mentioned before, we have three regulatory bodies that provide oversight of us, and the ERA is one of them. There is nothing in that regime that has stopped the freight task being grown from 33 million tonne to 71 million tonne. I think it is the ERA's job. They do have regular process checks to check all elements of the code. I think their approach is “if it ain't broke, don't try to fix it”. But they do consult with the public, that is their job, and everyone gets to have their say as part of that. If parties want to express the views that you have just expressed, they are entitled to within those processes run by the ERA.

[10.40 am]

Mr P.C. TINLEY: Just going back to the submission you made to the committee about the 2010 track audit: we understand that was the second such audit. Your first audit was made public—why was the 2010 not made public? Can you shed some light as to why that was the case?

Mr Larsen: Mr Tinley, that is actually news to us. We are not aware that the 2005 audit report was made public. I cannot help with that question any further than that, unfortunately.

Mr P.C. TINLEY: If it was possible, would you like to see it made public? Would you have an objection to it?

Mr Larsen: I have not thought about that. I would be happy to take that question on notice and respond at a later time.

Mr P.C. TINLEY: Sure. I look forward to it.

The CHAIR: The current situation, as we understand it, is that Brookfield want to close these tier 3 lines and do not appear to want CBH or someone else to operate or maintain them. What would you say—that it is not really appropriate for a state-owned asset to be treated like that, and we would say that it probably does not facilitate state development to do that?

Mr Larsen: Mr Blayney, I think I have said a number of times this morning that it is actually not Brookfield Rail's decision to close these lines. We are implementing the decision of government and a policy direction of government. We would love to find a way to keep the lines open through an agreed approach with the users, which could be multiple users of those lines. I do not think it is our decision that is being implemented. We are implementing the decision and policy direction announced by Simon O'Brien in November of 2010. We remain willing and open to negotiate for access to any lines in our network. That is the business we are in.

The CHAIR: One of the other comments that we had was that one frustration of the operators is that they do not get very much notice when maintenance is to be done on lines and it causes them considerable disruption at harvest. They were wondering if it would be possible to have a more transparent process where they get more warning of maintenance that is going to be carried out on the lines.

Mr Larsen: Mr Blayney, the process is that the ERA, in its early days, established what those notice periods were required to be, depending on how long you want to take the track for maintenance. The longer the period you need to take the track for maintenance, the greater notice you have got. All of those obligations are built into every single one of our access agreements and are adhered to and complied with. We have not had any breaches of those. We are audited on that by the ERA. We are in full compliance with the regulator's obligations on us and our contractual obligations, which narrow those regulatory obligations.

Mr F.M. LOGAN: With respect to the comment you made about Brookfield being available for negotiations with anybody who wants to lease tier 3 lines, has CBH approached Brookfield to lease tier 3 lines?

Mr Larsen: Just to clarify: the words that I used are that we are ready and willing to negotiate with any party for access to run trains on any line in the network.

Mr F.M. LOGAN: But not to lease the line or sublease the line?

Mr Larsen: We are the party that has the contractual right and the obligation to negotiate for access to those lines. That is different from leasing or subleasing parts of the network. That is not what I said.

Mr F.M. LOGAN: No. It is not what you said, but as you know that was clearly what I was driving at in much earlier questions, as well as the current one. Even though I obviously acknowledge, because you said it over and over again, that under the contract Brookfield has the responsibility for the lease of those lines, but what is to stop Brookfield either moving to sublease those lines, with agreement of the PTA, or negotiating a leasing out of those lines to other parties who may wish to use them?

Mr Larsen: It is a very interesting question that you pose. Clearly, in growing the freight volumes from 33 million tonne to 71 million tonne we have worked with the big end of town to negotiate arrangements—like Karara Mining, Mr Blayney, in your electorate. It facilitated investment into the network of our own and, in some cases, of our customers. We have had situations where our customers have invested their capital alongside us. These are sophisticated organisations. These arrangements were implemented into mature commercial agreements. We do not see that there would be anything stopping ourselves and CBH from having those sorts of discussions without us needing to hand the keys over. We have done it with the big end of town. We are happy to have those sorts of discussions with CBH if they want to have those.

Mr J. NORBERGER: Could you broadly describe the process that is undertaken by Brookfield Rail in determining network access fees?

Mr Larsen: That could be a long answer, Mr Norberger. Maybe if we go back to the Miling line example: the nature of the task and its duration, what then is required to occur in the infrastructure in terms of investment and maintenance, and other operating costs to support that task. Then there needs to be a return of, and a return on, capital invested to a level that is satisfactory to support both debt and equity being raised to facilitate that investment. I apologise if that is a —

Mr J. NORBERGER: That is fine. How practical would it be for network access fees to be based on a completely transparent equation combining tonnage, distance, specific line maintenance requirements, and a reasonable rate of return to the network operator?

Mr Larsen: The current access regime is based on a concept of a floor and ceiling, which are effectively, by line, the bookends from which Brookfield Rail and its total revenue must land in between those two numbers for agreements negotiated inside the access regime. That is the regime that exists here in WA. That is the law that is in place. As I said before, it is the ERA's job to consult with the users and the public as to whether or not that should change. Interestingly, of the 71 million tonne of freight we have got running on the network today, we have not had to negotiate

one agreement inside the access regime because we have actually been able to reach agreement with the parties to facilitate the levels of investment I talked about.

Mr R.S. LOVE: I have a question that sprung from your opening statement about the \$2 billion of investment that your company had made. Does that \$2 billion include all the scheduled maintenance as well as capital improvement? Do you include in the figure for capital improvement what was undertaken by you but essentially funded by the government in the current reinvestment in tier 1 and tier 2 lines, and in other things like the upgrade you spoke of to the line in my electorate, down past Mullewa, which would have been funded, I guess, by the customers through some arrangement with you? How do we, without any transparent public accounting of maintenance and investment, understand what that \$2 billion is comprised of and where that has gone?

Mr Larsen: There are a number of questions there, Mr Love. Firstly, if we were to include all maintenance, the majority of that expenditure has been expenditure made by us. There have been some elements of government investment in the network, as we know. With the line through to Geraldton and Mullewa down to Morawa, the investment that I mentioned before of \$550 million was entirely funded by ourselves. I think the real measure of investment should not be what it is actually being made into and is it the right investment, it should be the success in the lift in volumes on the network. Clearly, to lift the volumes on the network from 33 million tonnes per annum to 71 million is a substantial increase. That in itself is a good measure of the effectiveness of the investment.

[10.50 am]

Mr R.S. LOVE: Just to follow specifically from the difference between the grain freight part and general freight or other lines, the line down to Morawa and the mine at Karara has a different function and therefore has a different regime of costs, pricing and what-have-you. At the end of the day that is a state asset, so presumably the standard has now been recognised in your inventory as being of a higher standard. Do you anticipate that the fees charged will be able to keep that line at that level of performance, because typically this seems to be an industry where a cyclical sort of injection of capital occurs, depending on which line it is, and then a period of not much further investment until it needs another significant re-injection? For instance, in what is basically a brand-new line, such as the one that has just been constructed there, in the ordinary course of events will that now be kept at that level or will that generally be allowed to deteriorate to a point where it again needs a cyclical injection of capital to bring it back up to a standard? I am just trying to get an understanding of how these things are done.

Mr Larsen: Sure. I think, first of all, I need to say that clearly Karara is a very important customer of ours and there are things that you have touched on there that are confidential between our two organisations, which if I were to discuss would be in breach of our agreements with Karara. Clearly the investment we have made up there is in assets that have a substantial life—concrete sleepers and heavy rail. The key point to make is that if the volume of iron ore is there, and my understanding is that Karara will be around for a long time Mr Blayney —

The CHAIR: One hundreds maybe.

Mr Larsen: If that is the case, I would expect the line to be at the same standard and maybe better. I think it is really a matter of when the volume is there and the revenue continues to be there to support the asset at that upgraded level—a level that is far greater than what we were obliged to maintain under the lease. Does that answer your question, Mr Love?

Mr R.S. LOVE: I am trying to see if a line that is generating a good solid income stream throughout its life and access fees has a different investment cycle than a line that is typically funded by some re-injection by government or someone else, as has happened on some of the grain lines, so that it does not have that cyclical sort of a nature of investment and re-investment at various stages.

Mr Larsen: It is a good question, because every line is different in terms of what makes it up—the weight and size of sleepers and rail et cetera—and in terms of the task it needs to support. The answer to your question is that we invest to support the operational requirements that we have agreed with our customer to deliver the outcome that they want to deliver. We are in the business of making sure that our railway is safe, reliable and efficient so that our customers can achieve their goals and that we are obliged to deliver under our contracts to our customers, so we invest to achieve those outcomes.

Mr P.C. TINLEY: I will pick up on what Shane is talking about, which is basically around performance standards and performance relative to the task. Given that your only competitor—I am not talking about the Karara line—across this entire business model is road transport, and at various points that becomes economic and uneconomic, the road transport as a competitor, if you like, is fairly transparent in its costs; we could work out its pricing model pretty easily. It would be fair to say that no other part of the industry can work out your pricing model because of the nature of the confidentiality. However, given that most of what we are talking about and what we are looking at here is around performance standards, do you think it would be helpful if we made the performance standards that you are required to maintain and how they are measured transparent and available to the whole market?

Mr Larsen: On our website, the performance standard of each and every line is listed.

Mr P.C. TINLEY: That is the performance standard at the end on the line, but in your contractual arrangements under the lease?

Mr Larsen: When it comes to pricing, I have worked in the trucking industry for a long time for a company called Toll and we were not required nor did we post on a website all of our detailed commercial contracts with our customers, so I am interested in your point that the trucking industry —

Mr P.C. TINLEY: They are known inputs. The business inputs for the trucking industry are known. The cost of fuel, wages and maintenance of the vehicle is a known known, but no other part of the market knows what your cost inputs are because you keep confidential the basis of the performance that you required to do.

Mr Larsen: I think that many parties out there are just as capable as us of establishing what a sleeper costs, what a piece of rail costs and what a tonne of ballast costs, so I dispute that point. If I come back to the issue of pricing, I do not see the trucking industry publishing its detailed pricing contracts between Toll and Shell, for example, to cart fuel. I have not seen the details of that being published anywhere. They are commercial-in-confidence agreements, which is the normal way of doing business.

The CHAIR: I will ask one other question, if I may. It was just mentioned to the committee in passing when we were out at Bruce Rock—I have not had much time to follow it up, but I would like to—that in a similar situation in Saskatchewan, which from my reading had similar lines and those were made available to another party to use. To me, that seemed like a win-win situation. I am curious to know whether you are aware of that and know anything about that situation.

Mr Larsen: I am aware of that model. I am not aware of the detail of it. I think I have made the point several times today about our willingness to negotiate with any party for access, including the opportunity for others to invest capital alongside our capital to find a solution to tier 3.

The CHAIR: That is a good positive note to finish on. With that I would like to thank you for your evidence before the committee today. A transcript of this hearing will be forwarded to you for correction of minor errors. Any such corrections must be made and the transcript returned within 10 days from the date of the letter attached to the transcript. If the transcript is not returned within this period, it will be deemed to be correct. New material cannot be added by those corrections and the sense of your evidence cannot be altered. Should you wish to provide additional information or

elaborate on particular points, please include a supplementary submission for the committee's consideration when you return your corrected transcript of evidence. We probably have not got through most of our questions today. Will you be agreeable, if we send you some more questions, to answer them for us?

Mr Larsen: Yes. Thank you, Mr Blayney, and the rest of the committee.

Hearing concluded at 10.58 am
