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**Draft Decision on  
QR's Draft Undertaking**

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***Volume 2 - The Draft Undertaking***

*December 2000*

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## DIRECTORY

Item	Draft Undertaking	Draft Decision
<b>Part 1 - Preamble</b>		
	Paras (a) – (e)	Accepted
<b>Part 2 - Scope and administration of Undertaking</b>		<b>Chapter 2</b>
Coverage of stations, platforms and marshalling yards' services	Para 2.1(a)	Section 4.2
Coverage of above-rail or below-rail standard gauge services	Paras 2.1(b) & (c)	Section 2.1
Access to rail lines on land not controlled by QR	Para 2.1(d)	Section 2.2
Term	Cl 2.2	Section 2.3
Review	Cl 2.3	Section 2.4
Contractual arrangements	Cl 2.4	Section 2.5
Public reporting of compliance	No provisions	Section 2.6
<b>Part 3 - Ring-fencing arrangements</b>		<b>Chapter 3</b>
Organisational structure	Cl 3.2	Section 3.2
Accounting arrangements	Cl 3.3	Section 5.4
Internal access agreements for existing QR train services	Sub-cl 3.4.1	Sub-sect 3.7.1
Internal access agreements for new QR train services	Sub-cl 3.4.2	Sub-sect 3.7.3
Ring-fencing Guidelines	Cl 3.5	Sections 3.3, 3.5, 3.6
<b>Part 4 - Negotiation framework</b>		<b>Chapter 4</b>
QR's negotiating party with respect to marshalling yards	Sub-paras 4.1.1(a) & (b)	Section 4.2
QR's negotiating party with respect to stations & platforms	Sub-paras 4.1.1(a) & (b)	Section 4.3
Access seekers' negotiating party	Sub-para 4.1.1(c)	Section 4.4
Conditions to negotiation	Sub-cl 4.1.2	Section 4.5
Confidentiality	Cl 4.2	Section 3.4
Access application - Schedule C	Para 4.3(b)	Sub-sect 4.6.1
Access application - Schedule D	Para 4.3(c)	Sub-sect 4.6.2
Currency of Schedule D information	Para 4.3(e) & sub-para 4.7.2(b)	Sub-sect 4.6.3
Fees for information provision	Para 4.3(e) & sub-para 4.7.2(c)	Sub-sect 4.6.4
Acknowledgment of access application	Cl 4.4	Sub-sect 4.6.5
Indicative access proposal	Cl 4.5	Accepted
Notification of intent to progress access application	Cl 4.6	Sub-sect 4.6.5
Negotiation period	Sub-para 4.7.1(a), (b), (c)(i), (ii), (iv), & (v), (d) & (e)	Accepted
Negotiation period – events causing cessation	Sub-para 4.7.1(c)(iii)	Section 6.6
Issues to be addressed during negotiations	Sub-para 4.7.2(a), (i), (ii), (iii), (iv), (vi), (vii), (viii), (x) & (xi)	Not discussed
Access agreement – parties to agreement	Para 4.8(a)	Section 4.4
Access agreement	Para 4.8(b)-(e)	Accepted
Dispute resolution	Cl 4.9	Section 4.7
<b>Part 5 - Pricing principles</b>		<b>Chapter 5</b>
Revenue adequacy	Sub-cl 5.1.1	Sub-sect 5.2.1
Non-discriminatory pricing	Sub-cl 5.1.2	Sub-sect 5.2.2
Rail infrastructure utilisation	Sub-cl 5.1.3	Sub-sect 5.2.3
Pricing limits - definition	Sub-cl 5.2.1	Section 5.3
Pricing limits – for individual train services & train service combinations	Sub-cl 5.2.2 & 5.2.3	Section 5.3
Pricing limits – definition of revenue limit	Sub-cl 5.2.4	Volume 3
Reference tariffs - establishment	Sub-para 5.2.2(a)-(d)	Accepted

Reference tariffs – for train services in Schedule G	Sub-para 5.2.2(e)	Volume 3
Reference tariffs – for train services not identified in Undertaking	Sub-para 5.3.1(f) & (g)	Section 5.4
Reference tariffs – review	Sub-cl 5.3.2	Volume 3
Structure of access prices	Cl 5.4	Accepted
Cost allocation	Cl 5.5	Section 5.5
Performance regime	No provisions	Section 5.6
<b>Part 6 - Capacity management</b>		<b>Chapter 6</b>
Service specification & train scheduling	Cl 6.1	Sections 6.2 - 6.4
Capacity analysis	Cl 6.2	Section 6.5
Capacity allocation – register of interested parties	Sub-cl 6.3.1	Accepted
Allocation of capacity	Sub-cl 6.3.2	Section 6.6
Capacity resumption	Paras 6.4(a), (b) & (d)	Section 6.7
Capacity relinquishment	Paras 6.4(c) & (e)	Section 6.8
Capacity transfer	Para 6.4(f)	Section 6.8
<b>Part 7 - Interface considerations</b>		<b>Chapter 7</b>
Rolling stock interface standards	Sub-cl 7.1.1 & sub-para 4.7.2(a)(ix)	Section 7.2
Rolling stock authorisation	Sub-cl 7.1.2	Section 7.3
Rolling stock suspension	Revised Schedule E (Principle 5)	Section 7.4
Operating plan	Cl 7.2	Accepted
Safety management	Cl 7.3	Section 7.5
Suspension of third party operators' staff	Revised Schedule E (Principle 10)	Section 7.5
Assistance to third party operators to fulfil rolling stock and safety requirements	No provisions	Section 7.6
Safety and rolling stock audits	Paras 7.5(a) - (c)	Section 7.7
Allocation of environmental responsibilities under EPA Act	No provisions	Section 7.8
Environmental management plan	Cl 7.4 & sub-para 4.7.2(a)(v)	Section 7.9
Environmental audits	Paras 7.5(a) & (b)	Section 7.9
Assistance to third party operators concerning environmental requirements	No provisions	Section 7.10
Interface coordination plan	Cl 7.6	Section 6.2-6.4
Adjoining infrastructure	Cl 7.7 & sub-para 4.7.2(e)	Section 7.11
<b>Schedule E - Summary of standard access agreement</b>		<b>Chapter 8</b>
Dispute resolution prior to access agreement	No principle	Section 8.4.1
Obligations on the access holder	No principle	Section 8.4.2
Obligation to act in good faith and in a non-discriminatory manner	No principle	Section 8.4.3
Accreditation	Revised Principle 9	Section 8.4.4 & Ch 7
Access charges	Revised Principle 2	Section 8.4.5
Train service entitlements	Revised Principle 3	Section 8.4.6 & Ch 6
Day-to-day train movements	Revised Principle 4	Section 8.4.7 & Ch 6
Train operations	Revised Principle 5	Section 8.4.8 & Ch 6
Infrastructure management	Revised Principle 6	Section 8.4.9 & Ch 6
Incident management	Revised Principle 7	Section 8.4.10
Environmental protection & other issues	Revised Principle 8	Section 8.4.11 & Ch 7
Third party's staff	Revised Principle 10	Section 8.4.12 & Ch 7
Inspection & audit rights	Revised Principle 12	Section 8.4.13 & Chs 2 & 7
Indemnities & liabilities	Revised Principle 14	Section 8.4.14
Limitation of liability	Revised Principle 15	Section 8.4.15

Material change	Revised Principle 16	Section 8.4.16
Default, suspension & termination	Revised Principle 18	Section 8.4.17
Confidentiality & ring-fencing	Revised Principle 21	Section 8.4.18
Access rights	Revised Principle 1	Chs 4 & 6
Safety risk management	Revised Principle 11	Ch 7
Insurance	Revised Principle 13	Accepted
Disputes	Revised Principle 17	Ch 4
Force majeure event	Revised Principle 19	Accepted
Assignment	Revised Principle 20	Accepted

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**GLOSSARY**

<b>ABS</b>	Australian Bureau of Statistics
<b>above-rail business groups</b>	QR Coal and Mainline Freight and Metropolitan and Regional Services groups which provide and operate the equipment running on the infrastructure providing the services to the railway customer. These groups have track under their control and will be accessing the common user infrastructure such as the mainline.
<b>above-rail costs</b>	Costs and/or assets associated with the provision of above-rail services.
<b>above-rail services</b>	Activities, other than below-rail services, required to provide and operate train services including rollingstock provision, rollingstock maintenance, non-train control related communications, train crewing, terminal provision and services, freight handling and marketing and administration of those services.
<b>ACCC</b>	Australian Competition and Consumer Commission
<b>access</b>	Utilisation of a specified section of rail infrastructure for the purposes of operating train services.
<b>access agreement</b>	Agreement between QR and a railway operator for the provision of access.
<b>access application</b>	Request for access by a third-party operator which has been prepared in writing and which complies with the information requirements of paragraph 4.3(b) of the Draft Undertaking.
<b>access charge</b>	Price paid by a railway operator for access under an access agreement.
<b>access co-ordination plan</b>	Plan prepared by Network Access and the scheduling and train control officers detailing operational and interface requirements for a specific railway operator.
<b>access plan</b>	Access Co-ordination Plan
<b>access rights</b>	Entitlement of a railway operator to access in accordance with a specified capacity entitlement.
<b>access seekers</b>	Third-party operator or an end user who proposes to gain access to the network under the terms of the Undertaking.
<b>Access Undertaking or Undertaking</b>	Document approved by the Queensland Competition Authority in accordance with the Queensland Competition Authority Act 1997 (Qld) in respect of QR.

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<b>accreditation</b>	Rail safety accreditation in accordance with Part 4, Chapter 6 of the Transport Infrastructure Act 1994 (Qld).
<b>AD</b>	Accelerated depreciation
<b>additional information</b>	Information that is to be provided by QR to a third-party operator during the negotiation period as set out in Schedule D, excluding any information that is provided as part of the preliminary information, but only to the extent required either by the third-party operator or as part of the access agreement.
<b>allocation</b>	Sharing of joint costs/assets between functions/services.
<b>AMC</b>	Australian Magnesium Corporation
<b>AME</b>	AME Consulting Pty Ltd
<b>APT</b>	Arbitrage pricing theory
<b>ARTC</b>	Australian Rail Track Corporation
<b>attribution</b>	Sharing of costs between functions/services on a basis of cost causality where there is a causal relationship between the resources used and the function/service provided.
<b>available capacity</b>	Capacity that is not committed capacity including committed capacity which will cease being committed capacity prior to the time in respect of which capacity is being assessed.
<b>axle load</b>	Weight limit applied to trains passing over a line by the railway engineer. It is the limit allowed to be applied to any one axle on the train.
<b>backbone telecommunications</b>	The telecommunications assets that provide major trunk telecommunications and are used by many groups simultaneously.
<b>ballast</b>	Material upon which the sleepers bear; normally a load distributor to the formation or sub-grade.
<b>balloon loop</b>	Rail line terminus that backs upon itself in a circular shape.
<b>BCM</b>	Ballast cleaning machine
<b>below-rail costs</b>	Costs and/or assets associated with the provision of below-rail services.

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<b>below-rail service</b>	Activities associated with the provision and management of rail infrastructure, including the construction, maintenance and renewal of rail infrastructure assets, and the network management services required for the safe operation of train services on the rail infrastructure, including train control and the implementation of safeworking procedures.
<b>block</b>	In signalling terminology, a physical length of track protected by a fixed signal which indicates to a driver whether it is safe to proceed into the section.
<b>bottleneck</b>	A track section that limits the throughput of the network by restricting the number of trains able to pass through it.
<b>breakdown</b>	Mechanical or electrical breakdown, where the particular piece of equipment is rendered inoperable.
<b>bridgemaster</b>	A supervisor with resources suitable for bridge works and generally available to a district.
<b>broad-gauge</b>	General name given to gauges of track greater than standard-gauge of 1435mm
<b>BSNF</b>	Burlington Northern Sante Fe Corporation
<b>cant</b>	The term used to denote the raising of the outer rail on curved track to allow higher speeds than if the two rails were level. Cant compensates for the centrifugal force arising from a train traversing a curve.
<b>capacity</b>	Capability of a specified section of rail infrastructure to accommodate train services within a specified time period. This is after providing for QR's reasonable requirements for the exclusive utilisation of that specified section of rail infrastructure for the purposes of performing activities associated with the repair or enhancement of the rail infrastructure, including the operation of work trains.
<b>capacity analysis</b>	Assessment of the available capacity of a specified section of rail infrastructure including an assessment of whether that capacity is sufficient for the proposed access requirements. If the available capacity is not sufficient for the proposed access requirements the term includes an assessment of rail infrastructure expansion or other capacity enhancement required to meet those proposed access requirements.

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<b>capacity entitlement</b>	Railway operator's entitlement under an access agreement to operate a specified number and type of train services over the rail infrastructure within a specified time period and in accordance with specified scheduling constraints for the purpose of either carrying a specified commodity or providing a specified transport service. Until such time that access agreements have been developed for all existing QR operated train services, the term includes capacity that is demonstrably required for the purpose of QR operated train services and in respect of which access charges are applicable.
<b>CAPM</b>	Capital asset pricing model
<b>capping</b>	A layer of material between the ballast and the sub-grade which prevents the sharp rocky material of the ballast from degrading the sub-grade.
<b>centralised traffic control</b>	A generic term for remote monitoring and control of field signalling systems.
<b>CEO</b>	Chief Executive Officer
<b>CIB</b>	Capital indexed bonds
<b>clip fastener</b>	Similar to track spike, but are spring clips which secure the rail to concrete sleepers.
<b>Coal and Mainline Freight</b>	QR's above-rail business group whose major customers are the mining industry, minerals processors, electricity generators and freight forwarders.
<b>coefficient of adhesion</b>	The factor used to determine the maximum tractive effort which can be applied by a locomotive under a given rail condition before slipping off the wheels occurs.
<b>commencing date</b>	Date from which the Undertaking takes effect.
<b>committed capacity</b>	Portion of capacity required to meet the capacity entitlements of railway operators.
<b>common costs</b>	Costs associated with the provision of rail infrastructure that are not incremental costs for any particular train service using that rail infrastructure.

<b>confidential information<sup>1</sup></b>	<p>that information which is not publicly available and the disclosure of which might reasonably be expected to affect materially the commercial affairs of a person, where such information:</p> <ul style="list-style-type: none"> <li>• is not already in the public domain;</li> <li>• does not become available to the public through means other than a breach of confidentiality;</li> <li>• was not in the other party's lawful possession prior to such disclosure; and</li> <li>• is not received by the other party independently from a third party free to disclose such information.</li> </ul>
<b>consist</b>	Composition of a train, in terms of locomotive and wagon identification and its loading.
<b>corporate overhead costs</b>	Costs that relate predominantly to the overall management, strategy and governance of the corporation including, for example, head office, internal audit, corporate strategy and planning, corporate finance, information strategy, safety and industrial relations.
<b>corporate services costs</b>	Costs of services that are provided at the corporation wide level to groups and divisions within QR including, for example, legal services, computer services, motor vehicle fleet management, administration building services, payroll preparation and employee relations;
<b>corporations law</b>	The meaning given to that term in the Corporations (Queensland) Act 1990.
<b>cost allocation manual or costing manual</b>	Manual prepared by QR which identifies the matters outlined in Paragraph 5.5(a) of the Draft Undertaking.
<b>CPI</b>	Consumer Price Index

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<sup>1</sup> QR defines confidential information as any information, data or other matter marked confidential by a party when disclosed to the other party or disclosed to the other party with an express requirement in writing that the information, data or other matter be treated as confidential, where such information data or other matter

- is not already in the public domain;
- does not become available to the public through means other than a breach of confidentiality;
- was not in the other party's possession prior to such disclosure; and
- is not received by the other party independently from a third party free to disclose such information, data, or other matter.

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<b>crewing</b>	Manning of the locomotive at the front of the train with a crew. The crew is usually one or two locomotive drivers and/or assistant.
<b>cross-subsidy</b>	<p>The shortfall contributed by another train service or combination of train services where one train service or combination of train services pays access charges which are insufficient to meet:</p> <ul style="list-style-type: none"> <li>• the incremental cost imposed on the rail infrastructure by that train service or combination of train services; and</li> <li>• in respect of a group of train services, the common costs related specifically to sections of rail infrastructure that are used solely for the purpose of train services within that combination of train services.</li> </ul>
<b>CSO</b>	Community service obligation
<b>CSX</b>	CSX Corporation
<b>CTC</b>	Centralised traffic control
<b>DAC</b>	Depreciated actual cost
<b>daily train plan</b>	<p>Daily train schedules for all train services operating on QR's infrastructure together with the track possessions and train paths allocated to infrastructure maintenance providers on a daily basis. The master train plan will form the basis for development of the daily train plan which may be varied as a result of:</p> <p>the capacity entitlements of railway operators under current access agreements;</p> <p>business requirements,</p> <ul style="list-style-type: none"> <li>• project and maintenance works; and/or</li> <li>• any other planned or unplanned event which may lead to a requirement for alteration to the plan</li> </ul>
<b>DCE</b>	Deputy Chief Executive
<b>declared infrastructure</b>	Infrastructure declared available for access by third-party operators in accordance with the Queensland Competition Authority Act 1997 (Qld).
<b>DED</b>	Dragging equipment detector

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<b>delay</b>	The time a train is prevented from operating at the speed it would operate if it did not need to stop at passing sidings, signals or stations.
<b>depot</b>	Rollingstock depot or workshop depot. A rollingstock depot is a place where maintenance is carried out and where components are swapped in and out of equipment. A workshop depot is a place where components are manufactured or modified to be subsequently swapped in and out of equipment. Sometimes it is the sign-on location for infrastructure gangs.
<b>Deputy Chief Executive</b>	A corporate group within QR whose major responsibilities include finance, employee relations, information systems and telecommunications, legal and property issues.
<b>district</b>	A geographic area, a number of which make up a region in the infrastructure organisation. District resources or gangs are available to the entire district, whereas local gangs and resources are generally confined to a small infrastructure length within the district.
<b>DNR</b>	Department of Natural Resources
<b>DORC</b>	Depreciated optimised replacement cost
<b>double track or dual track</b>	A railway line consisting of two parallel tracks usually used for trains travelling in opposite directions.
<b>draft amending undertaking</b>	One or more documents specifying amendments to the Draft Undertaking, or the undertaking submitted to the QCA in circumstances envisaged in Part 5 of the Act.
<b>Draft Undertaking</b>	The document lodged with the QCA by QR on January 23, 1999.
<b>dragging equipment detector</b>	A track-mounted device capable of detecting whether a piece of rollingstock equipment has fallen or is not in its design configuration, such as derailed wheels or hanging brake-gear.
<b>duplication</b>	The construction of a second parallel track over section(s) of the network.
<b>EBA</b>	Enterprise bargaining agreement
<b>end-user</b>	A purchaser of train services (for example, a mine, a livestock producer, a power station).

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<b>environmental investigation</b>	Study of the likely short-term and long-term beneficial and detrimental effects on the environment of the third-party operator's operations insofar as they interact with the rail infrastructure and other train services.
<b>environmental management system</b>	Third-party operator's plan of management to address all environmental risks and ensure compliance with all environmental laws and licences.
<b>environmental risk management plan</b>	Plan identifying the controls and measures agreed between QR and the third-party operator to address risks identified through the environmental investigation. The plan identifies the party responsible for implementation of those controls and measures.
<b>EPA</b>	Environmental Protection Agency (Qld)
<b>EPA Act</b>	Environmental Protection Act 1994 (Qld)
<b>ER</b>	Employee relations
<b>evaluation period</b>	<p>In relation to:-</p> <ul style="list-style-type: none"> <li>• an individual train service - the period which is equal to the length of the expected duration of the existing or proposed access agreement in respect of the relevant train service;</li> <li>• a group of train services - the period which is equal to the length of the expected duration of the longest existing or proposed access agreement in respect of any of the train services comprising the combination of train services;</li> </ul> <p>provided that such period does not exceed ten years.</p>
<b>expansion</b>	An increase in network or system capacity.
<b>explanatory guide</b>	Document developed for the purpose set out in Paragraph 1(d) of the Draft Undertaking.
<b>failure mode effect analysis</b>	An analysis of work functions designed to ensure levels of maintenance are appropriate to the consequences of failure.

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<b>financial statements</b>	Annual accounts prepared in accordance with the requirements of the Financial Administration and Audit Act (1997) and audited by the Queensland Auditor-General.
<b>flange</b>	Larger part of wheel form used as the principal means of the railway guidance system.
<b>FMEA</b>	Failure mode effect analysis
<b>FMS</b>	Freight management system
<b>freight management system</b>	Mainframe computer based application that monitors overall train performance.
<b>frog</b>	The component in a turnout where one rail from one line crosses the other rail from the other line. The shape of the two rails coming together and diverging apart is in the shape of a frog. Also, swing nose frog relates to an arrangement where the continuity of each rail is maintained.
<b>geographic region</b>	Sections of the rail infrastructure identified as such in the cost allocation manual.
<b>geographic system</b>	Sections of the rail infrastructure identified as such in the cost allocation manual.
<b>geotextile</b>	A man-made fabric used in earthwork applications to constrain movement of material whilst allowing water drainage.
<b>GHD</b>	Gutteridge Haskins and Davey Pty Ltd
<b>GOC</b>	Government owned corporation
<b>gross tonne kilometres</b>	Total weight of a train multiplied by the distance travelled.
<b>gross-to-tare ratio</b>	Ratio of the total weight of a loaded wagon to the weight of the empty wagon.
<b>GSA</b>	Government service agreement
<b>GST</b>	Goods and services tax
<b>GTK</b>	Gross tonne kilometres
<b>HBD</b>	Hot box detector
<b>head-hardened rail</b>	Rail that has been heat-treated so that the head is approximately 30% harder than standard carbon rail.

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<b>headway</b>	The distance or time between train wishing to use the same section of the track, either in the same direction or in opposite directions.
<b>healthy train</b>	A train that has experienced no deviation – in excess of agreed tolerances – from the path in the daily train plan
<b>heavy-haul</b>	Rail transport associated with the movement of bulk commodities, for example, coal and iron ore, hauling in excess of 20 million gross tonnes per annum.
<b>hot box detector</b>	A track-mounted device with the function of measuring the axle box temperatures of a passing train. Axle box bearings have a risk of failing, causing bearing heating and eventual axle box shearing, resulting in a derailment.
<b>identification</b>	Where costs are directly incurred, or assets directly used in the performance of a function/service, the identification of those costs to that function/service.
<b>impact assessment study</b>	A detailed study of the short and long-term beneficial and detrimental effects on the environment of the third-party operator’s operations insofar as they interact with the rail infrastructure. The study includes an assessment of all relevant environmental factors, including social, economic and biophysical factors related to such operations.
<b>incident</b>	Any rollingstock derailment, rollingstock disablement or breakdown, accident, collision or any other unplanned occurrence on the infrastructure that causes or could cause injury to any person, damage to property, environmental harm or a loss to process including a cancellation by QR of any train movement.
<b>incident management</b>	Reporting, management and investigation of incidents occurring on or affecting the rail infrastructure.
<b>incremental costs<sup>2</sup></b>	The costs to an efficient network provider of providing access that would not be incurred if the particular train service or group of train services did not operate.

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<sup>2</sup> QR defines incremental cost as the costs of providing access, including capital (renewal and expansion) costs, that would not be incurred (including the cost of bringing expenditure forward in time) if the particular train service or group of train services (as appropriate) did not operate.

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<b>indicative access proposal</b>	Non-binding response from QR to an access application of a third-party operator, prepared in writing, including the information set out in CI 4.5 of the Draft Undertaking.
<b>infrastructure improvement</b>	Physical works applied to the infrastructure to increase the number of paths available on the system.
<b>infrastructure payments</b>	Payments to QR from the Queensland Government to enable QR to provide specified sections of rail infrastructure.
<b>Infrastructure Services Group</b>	QR's business group which supplies track maintenance and construction services to QR's above-rail business groups and Network Access.
<b>interlocking</b>	Generally signalling interlocking where various functions such as points switching cannot occur without other conditions occurring, such as the passage of a train. Proprietary systems for this function are known as VPI, Westrace, Microlok and Relay.
<b>initial capacity assessment</b>	Preliminary capacity analysis undertaken in a manner that gives an indicative assessment only and which will require further analysis as part of a final capacity analysis.
<b>interface coordination plan</b>	Plan which identifies the procedures to be followed and the responsible officers from both QR and the third-party operator, in respect of all regular operational interfaces between the parties that arise in the exercise of rights and the performance of obligations under the access agreement.
<b>interface plan</b>	Interface co-ordination plan
<b>intermediate loops/signals</b>	Passing loops or signals constructed at an intermediate point between two existing loops or signals to assist in increasing the capacity of the system.
<b>internal access agreement</b>	Arrangement between Network Access and another QR business group for the provision of access for the purpose of QR operated train services.
<b>IPART</b>	Independent Pricing and Regulatory Tribunal of New South Wales
<b>ISG</b>	Infrastructure Services Group
<b>IT</b>	Information technology

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<b>KPI</b>	Key performance indicator
<b>linear tariffs</b>	Tariffs that vary with a dependent variable, such as distance travelled or tonnes hauled, and which are portrayed as a single price without differentiation between fixed and variable elements.
<b>Line-section</b>	Section of railway route as defined in QR's chart of accounts from time to time and that is identified for the purpose of classifying the rail infrastructure into line sections with reasonably consistent traffic and reasonably consistent track standards.
<b>Line-section specific</b>	Costs and assets able to be specifically identified or attributed to a line section.
<b>LNG</b>	Liquefied natural gas
<b>local resources</b>	Resources of gangs whose field of work is confined to a relatively small geographic part of the district, which in turn is a subset of the region.
<b>MA</b>	Moving average
<b>Manual</b>	Costing manual
<b>marshalling</b>	Process of joining or separating locomotives and rail wagons to make up or split train consists.
<b>marshalling yard</b>	Typically, a train yard in which wagons are shunted to or from a train consist. Marshalling yards perform other functions including stabling, light maintenance, train inspection, and queuing.
<b>master train plan</b>	<p>Collectively, the train schedules for all train services contracted to operate on QR's infrastructure from week to week, together with the track possessions and train paths allocated to infrastructure maintenance providers for that same time. Specifically, the master train plan will detail:</p> <ul style="list-style-type: none"><li>• the contracted capacity entitlements of operators using or planning to use the relevant infrastructure from week to week, including train service paths, pathing determination and railway operator specific requirements;</li><li>• maintenance windows/possessions; and</li><li>• the available capacity of the network being the difference between maximum capacity and capacity entitlements.</li></ul>

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**material change event**

The occurrence of any of the following events on or after the date upon which the QCA approves the relevant reference tariff/s:

- any amendment, repeal, modification or enactment of any acts, ordinances, regulations, by-laws, proclamations and subordinate legislation made under, by or pursuant to any Commonwealth or State statute or any relevant Authority ('legislation');
- any binding change in the interpretation or application of any legislation resulting from a decision of a court or tribunal;
- the making of any new policy, instruction, direction or order ('directive') of an Authority (including without limitation QR's shareholding ministers) which impacts on QR, or the modification, extension or replacement of any existing directive;
- the imposition of a requirement for any licence, permit, approval, consent or other authority ('Authorisation') not required as at the date upon which the QCA approved the relevant reference tariff;
- after the date of grant of any authorisation, a change in the terms and conditions attaching to that authorisation or the attachment of any new terms or conditions;
- the imposition or abolition of, increase or reduction in the rate of, or change in the basis of calculating, any Commonwealth, State or Local Government-imposed tax, charge, levy, duty, impost, rate, royalty or imposition ('tax') imposed on, or payable by, QR including, without limitation, any tax relating to the protection of the environment imposed on users of electricity or imposing a form of consumption, value added or sales tax, but excluding any income tax; or
- a change in the Commonwealth Government 10-year bond rate of more than one hundred (100) basis points from the time that the reference tariff:
  - was endorsed by the QCA; or
  - was varied in accordance with Paragraph 5.3.2(b) of the Draft

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	Undertaking to reflect a change in the Commonwealth Government 10-year bond rate;
	whichever is the later.
<b>material default</b>	<ul style="list-style-type: none"> <li>• repeated failure to comply with the terms and/or conditions of any of the agreements specified in Paragraph 4.1.2(c) of the Draft Undertaking; or</li> <li>• any breach of a fundamental term and/or condition of any of the agreements specified in Paragraph 4.1.2(c) of the Draft Undertaking.</li> </ul>
<b>MEERA</b>	Modern engineering equivalent replacement asset
<b>Metropolitan and Regional Services</b>	QR's above-rail business group whose major customers are metropolitan, long distance and tourist passengers, and the grain, livestock and small/express freight sectors.
<b>MGT</b>	Million gross tonnes
<b>multi-part tariff</b>	Tariff that consists of at least two components (but generally more) which individually indicate the price of different parts of the service being purchased, inclusive of or in addition to fixed cost elements.
<b>NAG</b>	Network Access Group
<b>narrow-gauge</b>	General name given to gauges of track, less than standard-gauge of 1435mm. QR operates a narrow-gauge network of 1067mm.
<b>National Development Unit</b>	A corporate group within QR, its role being to identify business opportunities in other Australian rail jurisdictions.
<b>NCC</b>	National Competition Council
<b>Neck</b>	A section of track built to accommodate a locomotive involved in shunting operations which are carried out from one end of a yard.
<b>negotiation period</b>	Period during which the terms and conditions of an access agreement will be negotiated and which commences upon the third-party operator providing QR with a notification of intent to proceed with negotiations pursuant to cl 4.6 of the Draft Undertaking and concludes upon any of the events set out in Paragraph 4.7.1(c).

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<b>net tonne kilometres</b>	Weight of the payload multiplied by the distance travelled in the loaded section of the cycle.
<b>Network Access</b>	Business group established within QR to manage the provision of below-rail services with the exception of stations, platforms and selected marshalling yards.
<b>network wide costs</b>	Costs and assets associated with the provision of below-rail services not able to be identified or attributed to a line section or a geographic region.
<b>NPC</b>	Network Planning Centre
<b>NSC</b>	Norfolk Southern Corporation
<b>NTK</b>	Net tonne kilometres
<b>NTS</b>	New tax system
<b>ODV</b>	Optimal deprival value
<b>operating plan</b>	Description of how the proposed train services are to be operated, including the matters identified in Schedule H of the Draft Undertaking.
<b>operational systems</b>	An organisational sub-group of ISG comprising signalling and communications, asset maintenance and construction.
<b>ORG</b>	Office of the Regulator General
<b>other activities</b>	Activities undertaken by QR that are neither above-rail services nor below-rail services including for example, consulting activities and treasury activities.
<b>other activities costs</b>	Costs and/or assets associated with the provision of other activities.
<b>out-of-course running</b>	Occurrence where the movement of a train service differs from the train schedule for that train service as provided in the daily train plan.
<b>passing loop</b>	Section of track that has two ends, both of which lead onto the mainline which enables two trains travelling in the opposite direction on a single track to pass.
<b>PCI</b>	Pulverised coal injection
<b>preliminary information</b>	Information required to be provided by QR, prior to the submission of an access application, by a third-party operator.

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<b>price index</b>	A composite measure of the prices of items expressed relative to a defined base period.
<b>production resources</b>	In the context of major track program maintenance, those resources available to the whole district and designed for rapid output of finished work, such as mechanised equipment and large gangs concentrating on specific jobs. This contrasts with routine or caretaker maintenance local track gangs.
<b>protocols</b>	Scheduling and train control protocols
<b>provisioning</b>	Supply of consumables to a locomotive such as fuel, water, sand, crew consumables and the crew itself.
<b>QCA</b>	Queensland Competition Authority
<b>QCA Act</b>	Queensland Competition Authority Act 1997 (Qld)
<b>QMC</b>	Queensland Mining Council
<b>QR business groups</b>	Above-rail business groups, Network Access, Infrastructure Services, Technical Services and Workshops.
<b>QRCMF</b>	QR Coal and Mainline Freight
<b>QR's information systems</b>	Systems used by QR for recording the planned and actual performance of train services operating on QR's rail infrastructure, including, but not limited to, consist specification, running times and the occurrence and management of incidents.
<b>QRNA</b>	Network Access
<b>QT</b>	Queensland Transport
<b>QTC</b>	Queensland Treasury Corporation
<b>Queensland Transport</b>	Department of Transport for the State of Queensland.
<b>queuing</b>	Time spent by train consists at terminals or intermediate points waiting on rail traffic to clear.
<b>RAC</b>	Rail Access Corporation
<b>rail</b>	Steel wheel guide with a head, stem and base.

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<b>Rail Access Corporation<sup>3</sup></b>	A vertically separated below rail service provider that owns the NSW intrastate and interstate rail network.
<b>rail anchors</b>	On wooden sleepers track fitted with track spikes, a steel fitting that grips the rail base and prevents the rail sliding longitudinally with respect to the sleepers by wedging against sleepers. For concrete and steel sleepers, the mechanism of restraint is incorporated into the clip fasteners.
<b>rail creep</b>	Lengthwise movement of rail forcing buckles in rail and misalignment of sleepers.
<b>rail grinding</b>	Process performed by a machine whilst on the track where the head of the rail is shaped and surface defects removed by means of grinding wheels.
<b>rail infrastructure</b>	Rail transport infrastructure as defined in the Transport Infrastructure Act 1994 (Qld) for which QR is the railway manager.
<b>railway manager</b>	Meaning given to that term in the Transport Infrastructure Act 1994 (Qld).
<b>railway operator</b>	Person who has, or is seeking, access from QR to operate train services on the rail infrastructure and who is, or who will become, accredited in respect of those train services.
<b>RAMS</b>	Rail Access Management System
<b>RCAF</b>	Rail cost adjustment factor
<b>RCS</b>	Radio controlled signalling
<b>reference tariff</b>	Access charge applicable for a specified reference train service, established in accordance with Cl 5.3 of the Draft Undertaking. The purpose of the reference tariff is to provide information to third-party operators as to the likely level of access charge for train services of a similar type as the specified reference train service.

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<sup>3</sup> . The Transport Administration Amendment (Rail Management) Bill 2000 provides for the amalgamation of RAC and Rail Services Australia (which provides track maintenance services to RAC, FreightCorp, the State Rail Authority and other business clients) to form the Rail Infrastructure Corporation. The amalgamation is part of the NSW Government's recently announced reforms to the institutional arrangements, industry structure and operating structure of rail entities in the NSW rail sector. Given that the rail reform is yet to be fully effected, RAC rather than RIC will be referred to throughout the Draft Decision.

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<b>reference train service</b>	Notional train service conforming to certain criteria, including carrying a specified commodity type, operating between specified geographical points and conforming to specified technical characteristics, operational characteristics and contract terms and conditions.
<b>region specific</b>	Costs and assets associated with the provision of below-rail services not able to be identified or attributed to a specified line section, but able to be identified or attributed to a geographic region.
<b>re-railing</b>	Carried out where the rail needs replacing but the sleepers still have reasonable life.
<b>re-sleepering</b>	The replacement of sleepers which are life expired.
<b>re-surfacing</b>	Maintenance of the geometry of the track using a machine called a tamper which lifts, lines and levels the track and packs the ballast to accommodate the new position of the track.
<b>revenue limit</b>	Maximum revenue which QR should be entitled to earn from the provision of access to the train service or train service group over the evaluation period.
<b>RHA</b>	Rail haulage agreement
<b>Ring-fencing guidelines</b>	Guidelines prepared by QR in accordance with Cl 3.5 of the Draft Undertaking.
<b>RIS</b>	Rollingstock Interface Standards
<b>RMS</b>	Rail Management Services Pty Ltd
<b>road</b>	In a marshalling yard situation, a track long enough to store, stage or marshal a train. A yard is generally composed of a set of roads which come together at either end of the yard. A road is usually double-ended in contrast with a neck and a siding which are single ended.
<b>Roadmaster</b>	A senior supervisor within a district allocated the responsibility of supervising resources that work across the district or are common across the district, in contrast to a track supervisor who supervises resources allocated to a sub-section of the district.
<b>Rollingstock</b>	Locomotives, carriages, wagons, rail cars, rail motors, light rail vehicles, light inspection vehicles, rail/road vehicles, trolleys and any other vehicle which operates on or uses the track.

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<b>Rollingstock configuration</b>	Combination of rollingstock comprising a train that includes an identification number and a gross mass of individual items of rollingstock and the order in which those rollingstock items are placed in the train.
<b>Rollingstock interface standards</b>	QR's standards relating to the interface between rollingstock and the rail infrastructure with which the rollingstock and rollingstock configurations must comply in order for them to be able to be operated on the relevant parts of the rail infrastructure, including standards relating to the criteria identified in Part 2 of Schedule D of the Draft Undertaking.
<b>Rollingstock standards</b>	Rollingstock interface standards that relate to the design and performance of rollingstock.
<b>ROR</b>	Rate of return
<b>RSAU</b>	Rail Safety Accreditation Unit
<b>RTBU</b>	Rail, Tram and Bus Union
<b>running inspection</b>	Inspection of a train prior to the train starting its journey where no faults are expected to be found or at least the faults are very minor.
<b>safety management system</b>	<p>In respect of:-</p> <ul style="list-style-type: none"><li>• a railway operator - a system developed by the railway operator to manage all risks associated with the operation of train services including specifically those risks identified in the safety risk assessment; and</li><li>• a railway manager - a system developed by the railway manager to manage all risks associated with the provision of rail infrastructure and safe management of train operations on the rail infrastructure, including specifically those risks identified in the safety risk assessment;</li></ul> <p>and which forms the basis upon which the railway operator or railway manager becomes accredited.</p>
<b>safety regulator</b>	The Chief Executive of Queensland Transport or delegate operating in accordance with Part 4 of the Transport Infrastructure Act 1994.

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<b>safety risk assessment</b>	Assessment of the operational and safety risks associated with the third-party operator's operations insofar as they interface with the rail infrastructure and other train services.
<b>safety risk management plan</b>	Plan identifying the set of controls and measures agreed between QR and the third-party operator to address risks identified through the safety risk assessment, and the party responsible for the implementation of those controls and measures.
<b>safety standards</b>	Standards relating to safety, including occupational health and safety, established in published guidelines, industry practice or QR policies and all standards relating to safety, including occupational health and safety, prescribed by any laws.
<b>safeworking procedures</b>	Procedures and systems, including supporting communications systems, for the safe operation of trains and protection of work sites on rail infrastructure.
<b>S &amp; P</b>	Standard and Poors
<b>scheduling</b>	Process of determining arrival and departure times for train services at the origin, intermediate locations and the destination of a journey to meet the requirements of individual railway operators and the integration of such times with the other planned and unplanned activities necessary for the management of QR's infrastructure. Scheduling also includes entering these times into QR's information systems.
<b>scheduling and train control officers</b>	Officers who provide train control and prepare the daily train plan.
<b>scheduling and train control protocols</b>	Protocols prepared by QR outlining the approach QR will adopt with respect to the matters outlined in Paragraph 3.2(e) of the Draft Undertaking.
<b>sectional running time</b>	The time it takes a train to traverse a section travelling at the speed it would be travelling if it did not have to stop at passing loops or stations.
<b>shunting</b>	The movement of locomotives and wagons in a yard situation. Normally associated with the creation or separation of specific train consists.
<b>Siding</b>	Storage road leading nowhere
<b>single track</b>	A railway line that consists, for the most part, of only one track and punctuated by passing loops.

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<b>sleepers/ties</b>	The transverse members of trackwork, made of wood, concrete or steel which are used to secure the rail at the correct gauge.
<b>solvent<sup>4</sup></b>	<p>None of the following events have happened in relation to the third-party operator:</p> <ul style="list-style-type: none"> <li>• the third-party operator is unable to pay all its debts as and when they become due and payable or it has failed to comply with a statutory demand as provided in Section 459F(1) of the Corporations Law;</li> <li>• a meeting is convened to place it in voluntary liquidation or to appoint an administrator, unless the resolution is withdrawn within 14 days or the resolution fails to pass;</li> <li>• an application is made to a court for it to be wound up and the application is not dismissed within one month;</li> <li>• the appointment of a controller as defined in the Corporations Law of any of its assets, if that appointment is not revoked within 14 days after it is made; or</li> <li>• the third-party operator proposes to enter into or enters into any form of arrangement formal or informal with its creditors or any of them, including a deed of company arrangement.</li> </ul>
<b>SPI</b>	Share price index
<b>SRA</b>	State Rail Authority
<b>stabling</b>	Taking a train out of service and parking it in a siding without a crew.

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<sup>4</sup> QR defines solvency as none of the following events have happened in relation to the third-party operator:

- the third-party operator is unable to pay all its debts as and when they become due and payable or it has failed to comply with a statutory demand as provided in Section 459F(1) of the Corporations Law;
- a meeting is convened to place it in voluntary liquidation or to appoint an administrator;
- an application is made to a court for it to be wound up and the application is not dismissed within one month;
- the appointment of a controller as defined in the Corporations Law of any of its assets; or
- the third-party operator proposes to enter into or enters into any form of arrangement formal or informal with its creditors or any of them, including a deed of company arrangement.

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<b>staging</b>	Very short-term storage, where the train is required to wait for its train path on the mainline or at a terminal. Staging is built into timetables. During this time the train may be inspected and other non-invasive forms of maintenance and provisioning may be carried out.
<b>stand-alone costs<sup>5</sup></b>	The costs that an efficient network provider would incur if the relevant train service or group of train services was the only service or group of services being provided access.
<b>standard-gauge</b>	Nominal gauge between rails of 1435 mm.
<b>standard train path</b>	One of a number of similar hypothetical paths, in combination representing the least time-distance trajectories of trains over a network and therefore permitting the maximum number of trains of a given specification to be operated over the network.
<b>STB</b>	Storage Transportation Board
<b>storage</b>	Parking of the wagons of a train. Storage can range from short-term to long-term depending on the reason for their storage. Short-term storage may be necessary during an industrial dispute, inclement weather or port equipment breakdown. Very short-term storage is better known as ‘staging’.
<b>stowage</b>	The temporary storage of trains off the running mainline. This occurs in unplanned circumstances due to operational interruptions arising from weather conditions, loading and unloading problems and derailments, as well as in planned circumstances that relate to the operators’ operational patterns. The unplanned circumstances could exist for up to a week or more, while planned stowage is in accord with the operators’ capacity entitlements.
<b>STP</b>	Standard train path
<b>Surfactant</b>	Spray to stabilise loose particles
<b>sub-grade</b>	The prepared earth upon which the trackwork is built.
<b>tamping</b>	Process by which ballast is packed around the sleepers of a track to ensure the correct position for the location, speed and curvature.

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<sup>5</sup> QR defines stand-alone cost as the costs that it would incur if the relevant train service or combination of train services (as appropriate) was the only train service or group of train services provided access by QR.

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<b>Technical Services Group</b>	QR's business group that supplies engineering, project management and supply services to QR's above-rail business groups and corporate groups.
<b>terminal</b>	Any facility that is used for the loading and unloading of goods onto a train.
<b>TFP</b>	Total factor productivity
<b>third-party</b>	QR's terminology for an access seeker in Schedule E.
<b>third-party operator</b>	Railway operator other than QR
<b>TI Act</b>	Transport Infrastructure Act 1994 (Qld)
<b>TLM</b>	Track laying machine
<b>track</b>	Part of the rail infrastructure comprising the rail, ballast, sleepers and associated fittings upon which trains operate.
<b>track gauge</b>	Distance between the inner faces of the rail heads of a railway track. A narrow gauge railway is designed for 1067 mm whilst a standard gauge railway is designed for 1435mm. The measurement is made 16 mm below the top of the rail on the inner face.
<b>track geometry</b>	The position of the two rails transversely and longitudinally with respect to the alignment of the track.
<b>track laying machine</b>	A track-mounted machine designed to be able to place or replace rails and sleepers simultaneously and continuously.
<b>track occupation</b>	The presence of a train on a section of track that precludes the presence of another train in order to maintain safe separation between trains. Occupation can occur by other means such as a maintenance occupation.
<b>track relaying</b>	The complete replacement of the track structure, usually carried out by track-laying machines, except where relatively small lengths are involved.
<b>track section supervisor</b>	Usually a supervisor with a geographic allocation of the track asset.
<b>trackside systems</b>	All assets, their maintenance and construction, comprising signalling, communications and overhead power provision.

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<b>track spikes</b>	Large iron ‘nails’ with enlarged heads for securing rail to wooden sleepers.
<b>traction current</b>	Term used for electric power supply used on electric railways for trains. Normally supplied by overhead wire or third rail.
<b>traction motor</b>	Electric motor that drives the axle of a locomotive.
<b>tractive effort</b>	Power that a locomotive is able to deliver to the rail through its wheels notwithstanding the ability of the wheels to grip the rail.
<b>tractive force</b>	Longitudinal force that can be applied to the rails by the locomotive wheels, influenced by locomotive horsepower and wheel to rail adhesion.
<b>train</b>	Any configuration of rollingstock operating as a unit on the track.
<b>train control</b>	<p>The control of train movements and of all other rollingstock operations in accordance with the daily train plan, QR’s safety management system and other pre-determined procedures and of any other activities, including track possessions and other infrastructure maintenance activities, affecting or potentially affecting such train movements or rollingstock operations. In addition, train control includes:</p> <ul style="list-style-type: none"><li>• recording train running times in QR’s information systems;</li><li>• reporting incidents occurring on the infrastructure;</li><li>• scheduling;</li><li>• management of incidents from within the control centre; and</li><li>• exchanging information with railway operators.</li></ul>
<b>train cycle</b>	The period of time required for a train consist to load, transit, unload and return to load again.
<b>train path</b>	Defined entry, exit and transit time for a train consist on a particular network or corridor.
<b>train schedules</b>	The arrival and departure times for a particular train service at specified locations as contained in the master train plan and/or the daily train plan and entered into QR’s information systems.

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<b>train service</b>	Operation of a train between specified origins and destinations on the rail infrastructure.
<b>train service group</b>	Specified combination of train services that operate over discrete parts of the rail infrastructure and which is nominated as such in Schedule F of the Draft Undertaking.
<b>train standards</b>	Rollingstock interface standards that relate to rollingstock configurations.
<b>transit time</b>	The time it takes a train to run from an origin to a destination, usually over a number of sections, and composed of sectional running times, stopping allowances, starting allowances and waiting at passing sidings.
<b>TSG</b>	Technical Services group
<b>TSS</b>	Track section supervisor
<b>turnout</b>	Trackwork where a single track splits to become two tracks and is equipped with moving rails to change the route.
<b>two-part tariff</b>	Tariff that is divided into two components – a variable component, typically reflecting marginal costs, and a fixed component.
<b>Undertaking or Access Undertaking</b>	The document approved by the Queensland Competition Authority in accordance with the Queensland Competition Authority Act 1997 (Qld) that sets out the principles for negotiating access to QR's declared infrastructure.
<b>UPC</b>	Union Pacific Corporation
<b>VERS</b>	Voluntary early retirement scheme
<b>WACC</b>	Weighted average cost of capital
<b>working groups</b>	Meetings of stakeholders, convened by QCA in April and May 2000, to assist in the assessment of the Draft Undertaking. Participants were representatives from QR, QMC, FreightCorp, Toll, National Rail, ARTC, Queensland Treasury, QT, ACCC, NCC, Stanwell, WA Rail Freight Sale Task Force, RTBU and the QCA.
<b>Workshops</b>	QR's business group that undertakes maintenance, modifications, major overhaul, component exchange and manufacturing support for the rollingstock requirements of QR's above-rail business groups.

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## CHAPTER 1. BACKGROUND

### KEY ASPECTS

**March 1998** - Queensland Government declares the services provided by QR's intrastate rail transport infrastructure for third-party access purposes.

**June 1998** - Queensland Government extends declaration by removing the exemption relevant to access to coal lines.

**January 1999** - QR voluntarily submits a Draft Undertaking in relation to certain services relating to the use of rail transport infrastructure that it owns to the QCA.

**January 1999 – October 2000** - QCA undertakes an extensive process of consultation in relation to the Draft Undertaking.

**Certainty** - for the Undertaking to be approved it is necessary that it provide certainty for all parties to reduce the scope for disputes.

**Balancing interests** - in assessing the Draft Undertaking, it is necessary for the QCA to balance the legitimate interests of QR with the interests of access seekers, knowing that in doing so it must take appropriate account of the public interest considerations relevant to development of competition in the above-rail market in Queensland.

## 1.1 Introduction

The Queensland Competition Authority (QCA) was established by the *Queensland Competition Authority Act 1997* (the QCA Act). The creation of the QCA arose out of a series of Council of Australian Government agreements, which aimed to forge a national approach to the implementation of competition policy.

The QCA is an independent statutory authority consisting of members appointed by the Queensland Governor-in-Council. The QCA seeks to provide a recognised avenue whereby all stakeholders can rely on an independent, objective appraisal of the issues subject to its review. It also seeks to produce sensible commercially-focused solutions and recommendations which are capable of practical implementation and which facilitate compliance within Queensland with the principles of national competition policy.

## 1.2 Queensland Rail

### *QR Structure*

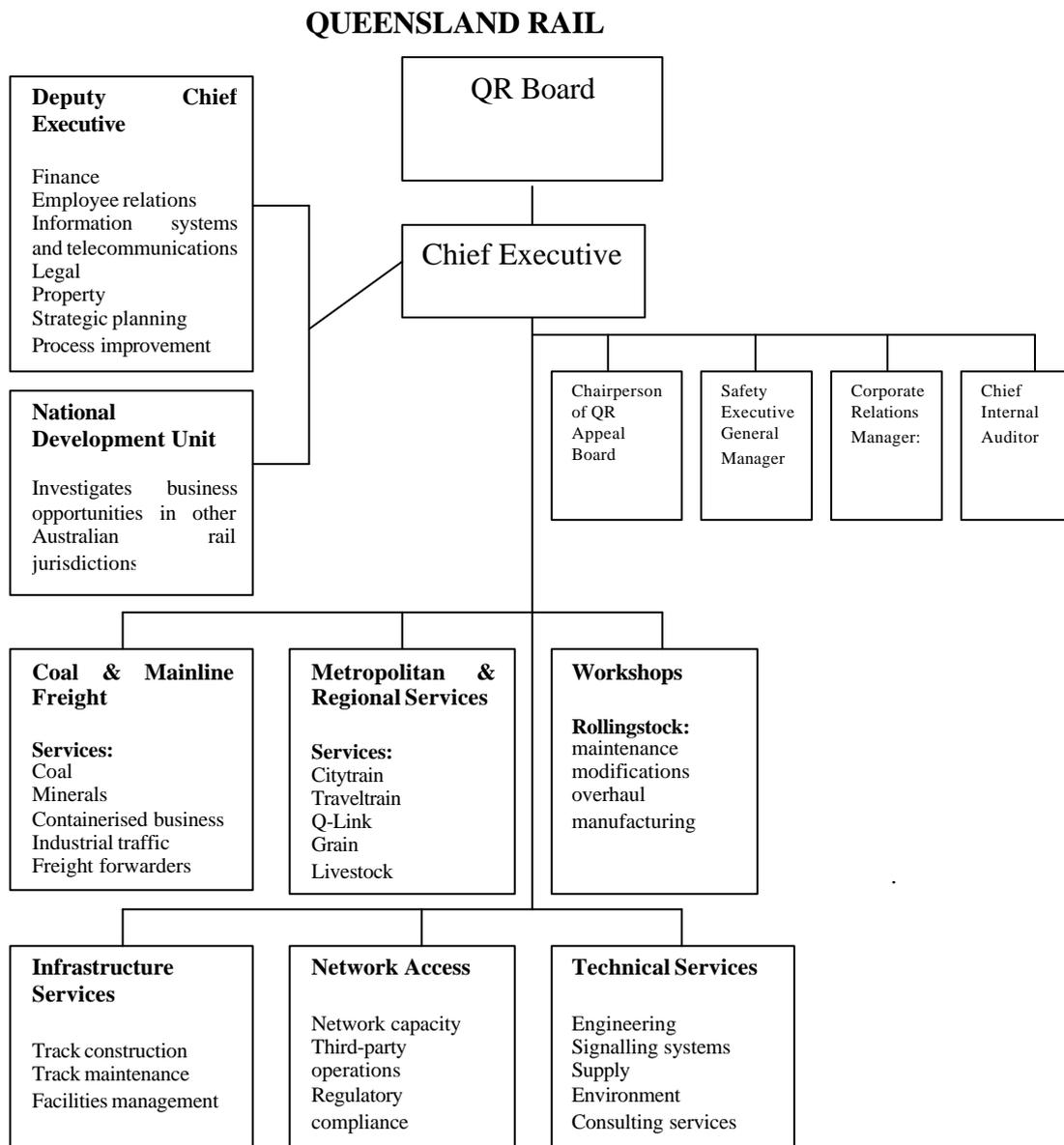
QR is a government owned corporation under the *Government Owned Corporations Act 1993* having become so on 1 July 1995. Under this Act, the Treasurer and the Minister for Transport hold all the shares in QR on behalf of Queensland taxpayers. QR is required to pursue an unambiguous commercial charter, subject to complying with government directions.

The Queensland Government decided in 1998 that QR would remain an integrated rail service provider. This decision may be contrasted with the position in New South Wales and at the Commonwealth level. In July 1996, the New South Wales Government created the Rail Access Corporation (RAC) as part of the establishment of the NSW Rail Access Regime under the *Transport Administration Amendment (Rail Corporation and Restructuring Act) 1996*. RAC is exclusively a below-rail service provider. In February 1998, Australian Rail Track Corporation (ARTC) was created as a Commonwealth government business enterprise. It commenced operation on 1 July 1998 also as an exclusive below-rail service provider having inherited the functions of the former Australian National Track Access Unit.

QR is structured into the six business groups and two corporate support groups. QR also has four other positions reporting directly to the Chief Executive: Chairperson of QR Appeal Board; Safety Executive General Manager; Corporate Relations Manager; and Chief Internal Auditor.

This structure is illustrated in Table 1.

**Table 1: QR Structure**



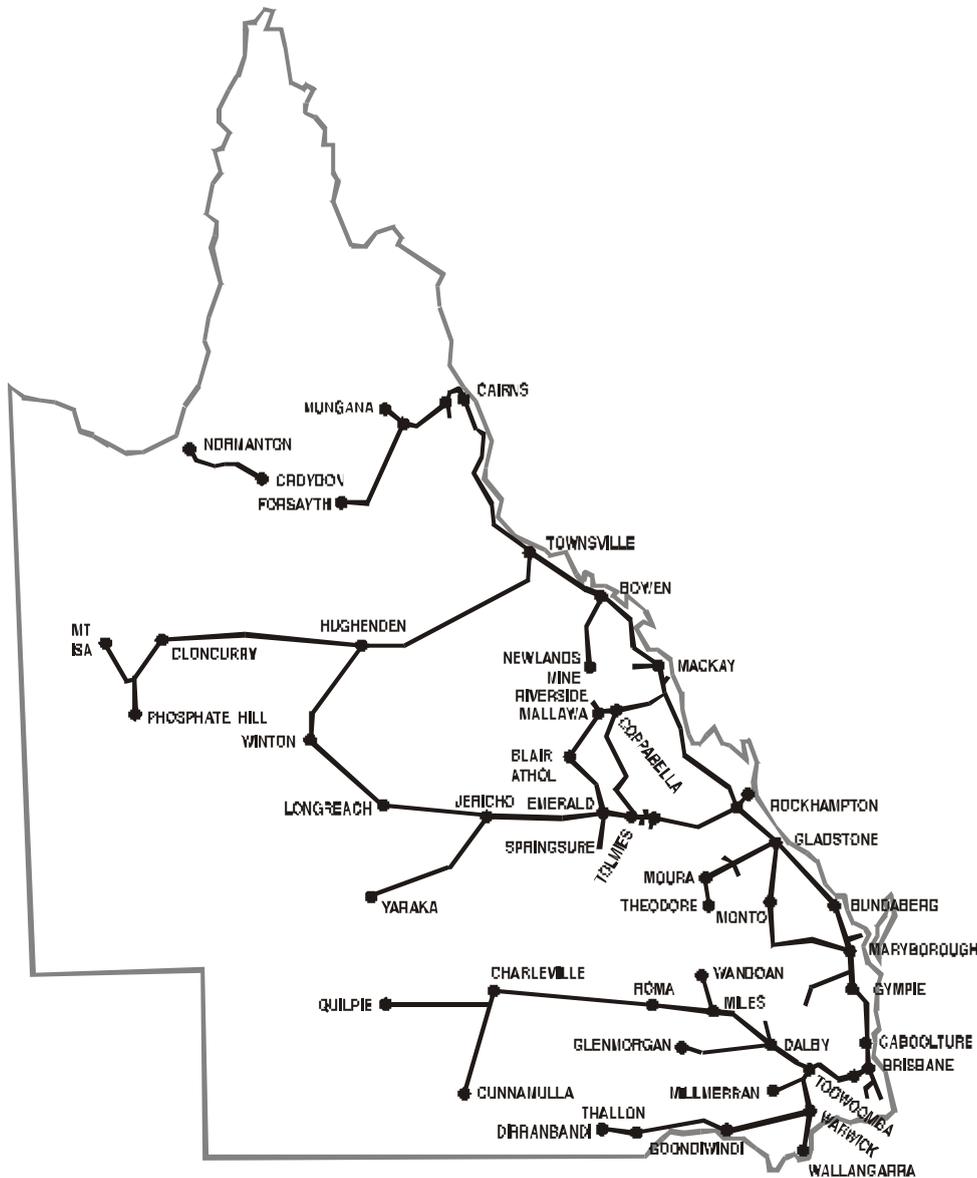
Under the new corporate structure, the Coal and Mainline Freight and Metropolitan and Regional Services business groups are principally above-rail operators which will be in direct competition with third-party operators. The Draft Undertaking proposes that these business groups will also be responsible for the provision of certain below-rail services on behalf of Network Access, including train scheduling, train control and associated incident management services, and the management of stations, platforms and selected marshalling yards. This raises important ring-fencing issues, which are discussed in Chapter 3.

***QR Network***

QR is a provider of below-rail and above-rail services via a geographically widespread narrow-gauge network of around 9,400 km (see figure 1). The track infrastructure is supplemented by related infrastructure necessary for a railway’s operation, such as signalling facilities and equipment, train control facilities, a communications system and overhead electrical-supply system. These facilities fall within the definition of rail transport infrastructure under the *Transport Infrastructure Act 1994*.

In addition, QR owns the 98km standard-gauge interstate rail link from the NSW border to the intermodal freight terminal at Acacia Ridge in South Brisbane. From Acacia Ridge, a standard gauge link is provided to the Brisbane metropolitan rail terminal at Roma Street and the Port of Brisbane. Sections of this track are dual gauge. However, QR does not operate interstate services on the standard-gauge line.

**Figure 1 - QR's Rail Network**



Source: QR

QR provides almost all rail services in Queensland.<sup>6</sup> It employs just over 14,700 staff and has total assets of around \$7.8 billion. During 1999-00, QR's network carried 131.5 million tonnes (Mt) of freight and catered for 43.4 million passenger journeys. This makes QR by far the largest rail operator in Australia, being almost twice as large as its nearest rival (FreightCorp).

<sup>6</sup> Comalco Minerals & Alumina is a private rail owner/operator on the Weipa to Andoom line. In addition, there are a number of privately-operated heritage train services in the State.

However, QR is not a large railway by world standards, carrying about one-half of the freight of large US rail operators.<sup>7</sup>

The services delivered by the rail infrastructure are commonly referred to as ‘below-rail’ services. The services provided by rollingstock, for example, locomotives, wagons and carriages, on the rail infrastructure are commonly referred to as ‘above-rail’ services. Accordingly, the application of third-party access to QR’s network results in an unbundling of the transportation service for freight and passengers into:

1. below-rail services (relating to the track and associated infrastructure); and
2. above-rail services (relating to the use of below-rail infrastructure by rollingstock).

It is generally accepted that it would be uneconomic to duplicate much of the rail infrastructure in Queensland given the current level of demand for rail services. In contrast, above-rail services are potentially contestable as there is scope to introduce competition into the supply of these services through the entry of new above-rail operators.

As one of the largest railway manager/operators in Australia, measured in terms of rail infrastructure under management, traffic task and revenues, the development of third-party access arrangements for QR’s rail infrastructure is an important milestone in the on-going national rail-reform process. The performance and growth of the rail sector compared to other transport modes is likely to be significantly affected by the final shape of QR’s Undertaking.

### ***QR’s Traffic Task***

In 1999-00, 87 per cent of the 131.5 million tonnes (Mt) of freight carried was coal and 97.6 per cent of the 43.4 million passenger journeys catered for were in Brisbane’s metropolitan rail system. The different types of QR’s rail traffic impacts on the average haul length of train trips. Table 2 provides an overview of QR’s freight and passenger task for 1999-00.

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<sup>7</sup> The traditional measure of output for rail operators is net tonne kilometers (NTK) – in this respect QR’s operation is less than one-tenth of the size of major US operators such as Burlington Northern Santa Fe.

**Table 2: QR freight and passenger traffic task for 1999-00**

	Volume	Change On 1998-99	Net Tonne Km	Change On 1998-99	Average haul length
	Net Tonnes (M)	%	Billion Km	%	Km
Coal and Minerals Services					
Export Coal	104.5	11.1	25.3	11.0	240
Domestic Coal	9.9	-5.1	1.9	-14.5	192
<b>Total Coal</b>	<b>114.4</b>	<b>9.5</b>	<b>27.2</b>	<b>8.8</b>	
Minerals	7.5	2.0	1.7	3.4	223
<b>Total Coal and Minerals</b>	<b>121.9</b>	<b>9.0</b>	<b>28.9</b>	<b>8.4</b>	
General Freight	9.6	11.5	5.2	4.0	543
<b>Total Coal &amp; Minerals &amp; General Freight</b>	<b>131.5</b>	<b>9.2</b>	<b>34.1</b>	<b>7.7</b>	
	Trips (M)		Passenger Km (M)		
Total Citytrain Services	42.4	3.1	889.2	7.5	21
Total Traveltrain Services	1.0	16.1	375.6	13.7	359
<b>Total Passengers</b>	<b>43.4</b>	<b>3.4</b>	<b>1,264.8</b>	<b>9.3</b>	

Source: Queensland Rail Annual Report 1999-00

The nature of QR's total traffic task and the significantly different market conditions within which its above-rail services are being delivered have important implications for usage of the network and the development of third-party access arrangements.

It is possible to identify three dense systems and a number of thinner systems within QR's network. Of the dense systems: the Brisbane metropolitan system has a heavy concentration of urban passenger and a reasonably significant volume of general freight traffic; the Goonyella and Blackwater systems handle almost all of Queensland's export coal and around half of the State's domestic coal, and a reasonably significant volume of general freight traffic; the North Coast line from Brisbane to Cairns is important for the carriage of general freight between Brisbane and central and north Queensland. A reasonably significant volume of long distance passenger trips are also completed on this system.

Of the thinner systems, the largest by traffic volume is the Mount Isa line, which carries almost all minerals traffic in the State and some general freight traffic.

Of QR's above-rail services, the freighting of bulk commodities over long distances, such as coal and minerals, is subject to little competition from other transport modes. On the other hand, QR's passenger services and small/express freight services face significant competition from other services, particularly road transport. Private operators in the freight forwarding sector in Queensland currently utilise QR's rail services in the containerised and general freight market for hauls in excess of 500km (predominantly freight moving up the Brisbane-Cairns corridor) with QR providing and operating dedicated freight trains under contract.

**Table 3: QR Sales Revenues for 1999-00**

	Sales Revenue	% of QR's Total Sales Revenue excluding government subsidies
	(\$M)	
Coal and Mainline Freight	1034.5	79.6
Metropolitan and Regional Services	187.3	14.4
Traveltrain	56.8	4.4
Other (1)	20.6	1.6
<b>Total sales excluding government subsidies</b>	<b>1299.3</b>	
<b>Government subsidies (2) (3)</b>		
Metropolitan and Regional Services	346.1	
Traveltrain	59.5	
Network Access Group	263.0	
Other	2.2	
<b>Total government subsidies</b>	<b>670.8</b>	
<b>TOTAL QR SERVICES</b>	<b>1970.1</b>	

Source: *Queensland Rail Annual Report 1999-00*

Notes:

- (1) QR received amounts from developers by way of non-refundable capital contributions for the provision of necessary infrastructure. This accounts for around 87% of the other category. The residual is made up by external access fees.
- (2) Government payments to QR for the delivery of certain loss-making services are referred to as government community service revenue in QR's annual accounts. QR also receives funding from various State Government Departments as direct reimbursements for concessions provided to senior citizens, pensioners and school children which are recorded as sales revenue.
- (3) QR has broken down its government community services revenue into above and below-rail activities as agreed by its relevant business groups.

As a result of the recent restructuring of business groups within QR, it is not possible to effectively compare sales revenues over time. Moreover, the reporting of sales revenue against QR's new business groups does not allow a full picture to emerge of the importance of coal and minerals sales to QR's revenue base. In 1997-98, under its previous organisational structure, QR reported coal and minerals sales revenues of \$866.7m, which accounted for 72% of total sales revenue excluding government subsidies.

In contrast to its coal and minerals operations, QR's metropolitan passenger (Citytrain) and general freight operations, within its Metropolitan and Regional Services business group, receive significant levels of government funding for the delivery of 'community services'. In addition, Network Access received \$263.0m of government funding in 1999-00 to keep open commercially non-viable rail lines.

### 1.3 Declaration of QR's infrastructure

The Queensland Government declared the services provided by QR's intrastate rail transport infrastructure for third-party access purposes in March 1998. The declaration was extended in June 1998 with the removal of the exemption on access to coal lines. The main effect of the declaration of a service is that it triggers a right for an access seeker to negotiate access with the facility owner, backed by the compulsory dispute resolution provisions of the QCA Act if the parties are unable to agree on the terms of an access agreement. Division 7 of Part 5 of the

QCA Act provides the framework within which access providers can prepare and the QCA can approve draft undertakings for declared and non-declared services.

#### 1.4 QR Draft Undertaking

On 23 January 1999, QR voluntarily submitted to the QCA a Draft Undertaking covering certain services relating to the use of the rail transport infrastructure it owns. A document entitled *An Explanatory Guide* accompanied that Draft Undertaking. It sought to clarify the intent of selected provisions in the Draft Undertaking. On the basis of advice received by the QCA, it has interpreted the Explanatory Guide as if it formed a part of the Undertaking.

#### 1.5 Assessment process for approval of Undertaking

Under the provisions of s136 of the QCA Act, the Authority must either approve, or refuse to approve, an undertaking given to it. If the Authority refuses to approve a draft undertaking, it must give the party who submitted the undertaking a written notice stating the reasons for the refusal and the way in which the Authority considers it is appropriate to amend the undertaking.

Ss138(3) of the QCA Act sets out certain pre-requisites to the approval of a draft undertaking by the QCA. The QCA must be satisfied that an undertaking is consistent with any access code for the service. The Authority must publish the draft undertaking and invite submissions on it within a stipulated time. Finally the Authority must consider the submissions within the stipulated time. Additionally, it is necessary that the QCA observe its natural justice obligations under the *Judicial Review Act 1991* and at common law.

In order to acquit the legislative and common law requirements the QCA undertook an extensive consultation process. Table 4 identifies the papers produced by the QCA and which were widely circulated for comment and submission. Table 5 sets out the names of the respondents to those papers.

**Table 4: Papers produced by QCA**

*Queensland Rail Draft Undertaking*  
(April 1999);

*Asset Valuation, Depreciation and Rate of Return* (May 1999);

*Treatment of Past Capital Contributions*  
(July 1999);

*Reference Tariffs, Reference Train Services and Rate Regulation* (October 1999);

*QR's Scheduling and Train Control Protocols and Proposed Assignment of Marshalling Yards* (February 2000); and

*QR's Draft Undertaking – Costing Manual* (March 2000)

**Table 5: Respondents to QCA Papers**

<i>Queensland Rail Draft Undertaking</i> (April 1999);	MIM Group Queensland Mining Council QR Stanwell
Agforce Australian Magnesium Corporation Australian Rail Track Corporation Easton Business Consultants Environmental Protection Agency FreightCorp Great Southern Railway MIM Group National Rail Corp Queensland Government Queensland Mining Council QR Rail Tram & Bus Union Shell Coal Stanwell Corporation Ltd Toll Group	<i>Reference Tariffs, Reference Train Services and Rate Regulation</i> (October 1999);  Australian Rail Track Corporation FreightCorp Queensland Government National Rail Corporation Queensland Mining Council QR Stanwell
<i>Asset Valuation, Depreciation and Rate of Return</i> (May 1999);	<i>QR's Scheduling and Train Control Protocols and Proposed Assignment of Marshalling Yards</i> (February 2000);
Australian Rail Track Corporation Easton Business Consultants FreightCorp Queensland Government Greenwood Kendalls MIM Group Queensland Mining Council QR Stanwell	Australian Rail Track Corporation FreightCorp Queensland Mining Council QR Queensland Transport Stanwell Toll Group
<i>Treatment of Past Capital Contributions</i> (July 1999);	<i>QR's Draft Undertaking - Costing Manual</i> (March 2000)
Australian Rail Track Corporation Curragh Queensland Mining Council FreightCorp Queensland Government	ARTC FreightCorp QR Queensland Treasury Stanwell

The April 1999 paper raised a number of issues relating to all aspects of the Draft Undertaking. The asset valuation, past capital contributions, reference tariffs and costing papers dealt principally with issues relevant to the development of reference tariffs for the use of QR's below-rail transport infrastructure for coal haulage. The February 2000 paper raised issues associated with QR's proposed protocols regarding its performance of scheduling and train control functions, and its assignment of management responsibility amongst its business groups for its rail infrastructure, including marshalling yards.

The papers were produced to assist interested parties comment on the Draft Undertaking and invited them to make submissions to the QCA. High-quality submissions were received from interested parties in response to the papers. The input from interested parties has made an important contribution to the development of this Draft Decision.

Once the QCA has approved an undertaking, it cannot subsequently review that decision in the light of future events that might lead it to a different conclusion.<sup>8</sup> A review process can only be undertaken on termination of the undertaking. The limited role for the QCA following approval of an undertaking has been an important determinant of the nature of the Authority's Draft Decision on QR's Draft Undertaking.

Finally, s150A of the QCA Act establishes a primary obligation on responsible persons to comply with the terms of approved undertakings. Consequently, under s158A, the QCA may make an application to the Court in respect of a responsible person's alleged breach of an approved undertaking.

## 1.6 Undertaking – Role

An undertaking for a service sets out details of the terms and conditions on which an owner undertakes to provide access to the service. Those terms and conditions necessarily must deal with price and non-price matters relevant to access. An undertaking which has been approved by the QCA is intended to establish binding provisions to guide negotiations. Its legal effect is to:

1. constrain the QCA from making a determination in relation to an access dispute which is inconsistent with the undertaking: s119(1); and
2. provide the owner with the capacity to create a safe harbour from provisions of the QCA Act which prohibit preferential self-dealing: ss104 & 105 This is because conduct that is in accordance with an approved undertaking will be deemed not to breach these provisions.

For an undertaking to be approved, it is necessary it provides certainty for all parties and reduces the scope for disputes. That though may not be at the expense of commercial negotiation. All parties must be able to negotiate a position outside the terms of the undertaking. To facilitate that, it is necessary that to the maximum intent possible, each party should have access to the same level of information. It is only through the creation of such an environment that third-party access will contribute in a positive way to the well being of Queenslanders.

## 1.7 Undertaking – Content

The content and degree of specification of undertakings may vary from service to service. The QCA Act indicates the types of matters to be included in an Undertaking which are set out in Table 6 below.

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<sup>8</sup> Once an undertaking has been approved, s139 allows the QCA to require the owner to give the QCA a draft amending undertaking only if it considers it necessary to make the undertaking consistent with a provision of the QCA Act or an access code for the service.

**Table 6: Undertaking - Content**

- |   |   |
|---|---|
| 1. How charges for access to the service are to be calculated;  | 9. Accounting requirements to be satisfied by the owner and a user in relation to the service or separate parts of the service;   |
| 2. Information to be given to access seekers;   | 10. Arrangements to be made by the owner to separate the owner's operations concerning the service from other operations of the owner concerning another commercial activity; |
| 3. Information to be given to the QCA or another person;  | 11. Terms relating to extending the facility;   |
| 4. An obligation on the owner to comply with decisions of the QCA or another person about disputes about matters stated in the undertaking; | 12. Requirements for the safe operation of the facility;  |
| 5. Information to be given to the QCA about compliance with the undertaking and performance indicators stated in the undertaking;           | 13. How contributions by users to the cost of establishing or maintaining the facility will be taken into account in calculating charges for access to the service;           |
| 6. Time frames for giving information in the conduct of negotiations about access to the service;   | 14. Provisions to be included in access agreements in relation to the service; and  |
| 7. How the spare capacity of the service is to be calculated;   | 15. Review of the undertaking.  |
| 8. Arrangements relating to the operation of secondary markets;   |   |

*Source : QCA Act s137(2)*

Other matters the QCA may require to be included in an undertaking may be implied from the subject matter, scope and purpose of the QCA Act. Hence, the QCA may include other matters where there is a logical connection between the purpose of the legislation and the considerations relevant to ensuring the provisions of the legislation are given effect.

## **1.8 Undertaking – Approval**

The Authority must consider the following matters under ss138(2) of the QCA Act in deciding whether to approve a draft undertaking:

1. the legitimate business interests of the owner of the service;
2. the public interest, including the public interest in having competition in markets (whether or not in Australia);
3. the interest of persons who may seek access to the service; and
4. any other issues the Authority considers relevant.

The QCA's interpretation of these matters, as applied in considering whether to approve QR's Draft Undertaking, is set out below.

### ***Legitimate business interests of the owner***

The term 'legitimate business interests' is not defined in the QCA Act. In its broad assessment of this term, the QCA focussed on an examination of the rights and obligations provided by QR for itself under the Draft Undertaking and compared them to the rights and obligations provided for access seekers. This necessitated a consideration of the measures QR proposed for its own protection from risk exposure in the context of third-party access to the network.

The QCA's consideration of QR's legitimate business interests took account of QR's obligations to its shareholder, the Queensland Government, in relation to its financial performance. This included the need for QR to recover the efficient costs incurred in providing services over the expected lives of the assets employed and to earn a risk-adjusted rate of return on the value of those assets. Some of QR's financial obligations take the form of specific financial requirements, such as rate of return targets and prescribed dividend-payment ratios. All were taken into account by the QCA.

Other factors the QCA considered to be in QR's legitimate business interests included:

1. establishing a negotiation framework that protects QR from negotiating with insolvent access seekers;
2. establishing a right to resume under or unutilised capacity;
3. allowing a transitional period for the development of internal access agreements for existing train services;
4. requiring the competition processes to identify risks and associated control measures regarding safety and environmental matters prior to the commencement of a third-party operator's train services; and
5. ensuring QR's above-rail business groups are not disadvantaged in competing with third-party operators.

The Authority recognised that the terms and conditions of the Draft Undertaking should preserve QR's incentive to undertake investment in, and maintenance of, its infrastructure. This included recognising that existing rail contracts between QR and other parties are not subject to the provisions of the Draft Undertaking.

The QCA recognised that QR delivers a number of CSOs on behalf of the Queensland Government.

Finally, in undertaking its analysis, the QCA did not regard QR's business interests as being legitimate if they inhibited competition or imposed requirements on access seekers in excess of relevant legislation, unless they did so in a manner that was in the public interest or was otherwise able to be justified.

### ***Interests of access seekers***

The requirement of the QCA Act that the QCA is to consider the interests of access seekers in addition to the legitimate business interests of the access provider recognises the potential for their respective interests to be in conflict. As a vertically integrated provider of rail services operating in both a monopoly market for below-rail services and a potentially contestable

market for above-rail services, QR will effectively provide access to third parties in one market and compete with them in another.

As noted above, the Draft Undertaking establishes rights of and obligations for access seekers. The nature of these rights and obligations underpins the interests of access seekers.

Factors the QCA considered to be in the interests of access seekers concerning QR's Draft Undertaking included whether:

1. all declared services, including the services which third-party operators require, are covered;
2. appropriate ring-fencing arrangements are established to protect confidential information;
3. an effective negotiation framework is established, including provision of information to third-party operators in a timely manner, clearly defined boundaries to access negotiations and effective dispute resolution procedures;
4. QR's proposed pricing framework does not allow QR to exploit its monopoly position in certain markets including through preferential pricing and charging access prices that are too high;
5. barriers to entry, such as excessive safety and environmental requirements, have not been incorporated; and
6. there are incentives for QR to improve its efficiency and service performance over time.

A further consideration relates to access seekers who operate across jurisdictions. The Authority is conscious of the need to recognise that the interests of access seekers include interoperability across jurisdictions.

### ***Public interest considerations***

Section 138 of the QCA Act provides that the Authority may approve a draft undertaking only if it considers it appropriate to do so having regard to, amongst other things, the public interest, including the public interest in having competition in markets whether or not in Australia. However, the term the public interest is not defined in this section.

Table 7 sets out a listing of matters relevant to a consideration of public interest as it applies to the Undertaking by QR. The list contains some degree of overlap in that it represents an amalgamation of the views of the QCA, the Queensland Government as expressed in its submissions, the contents of the Competition Principles Agreement and the QCA Act: s76(3) and case law.

**Table 7: Public interest considerations**

- |   |   |
|---|---|
| 1. Promoting competition within a fair and equitable regulatory framework;  | 8. Legislation and government policies relating to occupational health and safety and industrial relations; |
| 2. Ensuring rail safety;  | 9. The interests of consumers or any class of consumers;  |
| 3. Achieving an adequate return on taxpayer's investment;   | 10. The efficient allocation of resources;  |
| 4. Ensuring regional communities are adequately serviced;   | 11. Industrial harmony;   |
| 5. Promoting regional development, including economic development and opportunities for employment generation;                                | 12. The competitiveness of Australian business; and   |
| 6. Legislation and government policies relating to ecologically sustainable development;  | 13. Transitional issues created by reform programs.   |
| 7. Social welfare and equity considerations, including community service obligations and the availability of goods and services to consumers; |   |

*Source: QCA; QCA Act s76(3); case law; submissions of Queensland Government and the RTBU*

Table 7 is not an exhaustive list. However it has allowed the QCA to make a thorough assessment of the public interest in considering whether or not to approve QR's Draft Undertaking.

The QCA considered that establishing what may or may not be in the public interest requires a broad assessment of the proposed matters, including balancing what can, in practice, be competing interests. Nevertheless, the overriding imperative of the Authority's consideration must be that, in total, its decisions contribute to, rather than detract from, the well-being of Queenslanders.

The way in which the Authority addressed each of the factors in assessing QR's Draft Undertaking is outlined under the following headings.

#### *Ecologically sustainable development*

The Draft Undertaking imposes a number of environmental requirements upon third-party operators, including investigations, risk management plans and audits.

In its Request for Comments Paper *Queensland Rail Draft Undertaking*, the QCA sought comments on the requirements QR should adopt to ensure that any restrictions on access to its network on environmental grounds are consistent with the public interest, having regard to the public interest in competition and environmental protection. Stakeholders raised the points identified in Table 8.

### Table 8: Stakeholder Comments – Environmental Issues

**FreightCorp** - the public interest is best served by the Undertaking being restricted to requiring an operator to conform with all legislation, and to have an environmental management plan suitable to conform with the requirements of the *Environmental Protection Act 1994* (the EPA Act). An operator's efforts are likely to be less effective if it were required to conform to Network Access' environmental requirements which may be inconsistent with those of the EPA. An increase in efficient utilisation of the rail system would have positive environmental spin-offs, such as lower greenhouse gas emissions, lower particulate pollution, less road traffic congestion and lower noise levels.

**QMC** - the restriction of access to the coal and minerals network on environmental grounds should not arise because the environmental risks associated with train operations should be manageable to the point where the benefit/cost equation is comfortably in favour of enhanced above-rail competition; and

**Toll** - most third-party operators' activities will not have any significant impact on environmental issues as they will fall within existing or contemplated traffic levels.

In considering whether or not to approve QR's environmental requirements, the QCA took account of the interaction of the environmental responsibilities of QR and third-party operators under the EPA Act, as administered by the EPA. The QCA consulted the EPA in developing the QCA's position on QR's environmental requirements to clarify both the roles and responsibilities of QR and third-party operators under the EPA Act and to ensure consistency with how the EPA itself administers and enforces the EPA Act.

The Queensland Parliament established the EPA Act in 1994 to provide a framework for the management and protection of the environment in the State. The object of the EPA Act is to protect Queensland's environment while allowing ecologically sustainable development in the State. This object reflects the balancing of environmental protection and economic development through the concept of ecologically sustainable development.

In assessing the public interest, the QCA is required to draw a balance between legislation and government policies relating to ecologically sustainable development and the promotion of competition in Queensland's above-rail market. The danger of QR's environmental requirements going further than those under the EPA Act is that they could become a barrier to entry, which would undermine above-rail competition. Nevertheless, environmental requirements beyond the EPA Act could be justified under a public interest test by reference to generally accepted industry practice, recent government policies that are not necessarily reflected in the legislation and QR's own environmental practices.

On the basis of there being no evidence of generally accepted industry practice or recent government policies that go beyond current legislative standards, the Authority has taken the view that QR's environmental requirements should be consistent with, but not in excess of, those currently imposed under Queensland's environmental regulatory framework.

Consequently, the QCA has proposed a number of amendments to the Draft Undertaking to refine environmental requirements, including with respect to accreditation of third-party operators' environmental management systems under international standards and to audits.

#### *Occupational health and safety and industrial relations*

The Draft Undertaking imposes a number of rail safety requirements on third-party operators including rollingstock standards, safety risk assessments and audits. These requirements are in addition to those established under Queensland's rail safety accreditation arrangements.

The main theme to emerge in submissions to the Authority regarding the interaction of the safety responsibilities of QR, third-party operators and the Rail Safety Accreditation Unit

(RSAU) of Queensland Transport was that RSAU is the appropriate body to deal with rail safety issues in Queensland. A related issue raised was that the Undertaking needs to more clearly delineate the roles of QR and RSAU as far as rail safety is concerned.

In considering whether or not to approve these safety requirements, the QCA took account of the interaction of the safety responsibilities of QR and third-party operators under the *Transport Infrastructure Act 1994* (the TI Act), as amended by the *Transport Infrastructure Amendment (Rail) Act 1995*. The objectives of the TI Act include the introduction of a safety accreditation system to maintain appropriate levels of safety in the rail transport industry.

The RSAU administers the TI Act. It was created to administer the rail safety provisions of the TI Act, including assisting rail managers and operators to develop safety management systems in accordance with the TI Act. The QCA liaised extensively with the RSAU in developing its position. The RSAU's interpretation of the public interest in rail safety was particularly important to the QCA in this regard.

The QCA considers the rail safety regulatory framework established by the Queensland Parliament provides a relevant benchmark for assessing the consistency of third-party operators' activities with the public interest in rail safety in the State. Nevertheless, in assessing the public interest, the QCA drew a balance between this safety legislation and the promotion of competition.

In drawing this balance, the Authority had regard to the fact the RSAU has been specifically established to administer rail safety accreditation in this state. Accordingly, the Authority took the view that QR's rollingstock and safety requirements should be consistent with, but not in excess of, those currently imposed under Queensland's rail safety regulatory framework, including any guidelines and policies developed by the RSAU.

The danger of QR's safety requirements going further than those applied under this regulatory framework is that they could become a barrier to entry, which would undermine above-rail competition.

The RSAU advised the QCA it considers the QCA has taken a balanced and reasonable approach to the issue of safety.

The QCA is concerned that a number of the Draft Undertaking's safety requirements go further than those applied under the rail safety regulatory framework. Consequently, the QCA has proposed a number of amendments to the Draft Undertaking to refine its safety requirements, including with respect to rollingstock, the development of safety management systems and safety audits.

The QCA has not explicitly considered occupational health matters in the Draft Decision. Also, QR did not raise any occupational health issues in its submissions to the Authority. Nevertheless, the Authority understands that there is some overlap in the practical effects of rail safety and occupational health legislation. Indeed, the RSAU's accreditation guidelines provide that railway operators and managers will need to demonstrate that their rail safety policy recognises the obligations of the *Workplace Health and Safety Act 1995*. Accordingly, the Authority is satisfied that the wider regulatory framework within which QR's Undertaking will operate adequately addresses occupational health matters.

#### *Social welfare and equity considerations*

The QCA considers that the public interest in social welfare and equity has a number of dimensions. The QCA's role as an economic regulatory body limits the extent to which it can influence social welfare and equity outcomes. In many cases, the pursuit of such outcomes

through the tailoring of policies for particular groups in the community is appropriately a matter for the Queensland Government as the elected representative of the broader community. This view is consistent with the majority of submissions, which argued that non-commercial requirements imposed on QR by government should form part of explicit CSO payments.

The QCA believes that the Queensland and national economies are best served by the development of a regulatory framework for the rail sector that ensures resources are allocated to their most productive uses. The QCA has an important role through approving an Undertaking that establishes a sound regulatory framework within which a robust above-rail market can develop.

In addition, aggregate social welfare in the State will be enhanced by the approval of a pricing framework that facilitates the efficient use of QR's rail infrastructure. The QCA recognises that in addition to aggregate social welfare, the Queensland Government is concerned with the 'distribution of welfare' across sectors and/or individuals within the State. Under the *Government Owned Corporations Act 1993*, the Government may require QR to perform certain activities that would not be undertaken on commercial grounds. One means provided under the Act by which this could be accomplished is through CSO payments. Infrastructure payments received by QR are an example of a CSO.

A submission from the Queensland Government discussed the issue of CSOs performed by QR (in 1999-00 these were worth \$670.8m). These CSOs relate to the purchase by the Government of primarily passenger transport services and selected freight services and infrastructure services related to the maintenance of commercially non-viable rail lines. According to the Government, a large part of QR's network is not recovering the full economic cost of providing the infrastructure. However, the Government has identified the continued operation of these lines as a policy objective.

The QCA sought submissions on whether users should pay for Government directions to QR, for example, relating to there being no forced relocations or redundancies of QR staff.

The majority of submissions argued that non-commercial requirements imposed on QR by government should form part of explicit CSO payments. The Queensland Government stated that, in principle, it does not support users of the network paying for any non-commercial objectives required by the Government

In contrast, the RTBU argued that this was an example of the QCA suggesting there is no public interest in the way QR operates or the size of its operations, or that third-party users do not have to share in this public interest. The QCA notes that the public interest in social welfare is not necessarily best served by keeping existing resources within QR. In an aggregate sense, social welfare may be improved by a loss in QR's market share if such a loss were to go to more efficient third-party operators.

The QCA considers the Queensland Government's CSO policy is beyond the scope of the QCA's consideration of whether or not to approve QR's Draft Undertaking. Nevertheless, the practical effect of CSOs paid to QR is particularly relevant to the pricing framework the QCA believes the QR's Undertaking should establish.

The QCA believes that the delivery and costing of rail CSOs in a transparent manner would advance the public interest. This is particularly the case in the context of the development of reference tariffs for QR's coal corridors and, more broadly, the establishment of an access pricing framework based on users paying the efficient cost of declared services. In contrast, hidden CSOs are likely to detract from QR's efficiency and financial performance, and result in certain users facing excess charges so that non-commercial objectives can be pursued with

respect to other groups. This would likely undermine the competitiveness of the users forced to pay excess charges.

Consequently, the QCA believes the public interest in social welfare and equity is best served if users of QR's network are not required to pay for any non-commercial objectives the government may choose to ask QR to provide for the benefit of the community. Moreover, the QCA does not believe the public interest is served by it interfering with government decisions on CSO funding of the rail sector.

The link between these two objectives can be seen with respect to the proposed treatment of QR's infrastructure maintenance costs in the development of reference tariffs. The QCA has proposed a transition path to close the gap between QR's current costs and an efficient cost level. The QCA believes that if QR does not find the efficiencies foreshadowed in the transition path, users should not have to pay for the difference between actual and efficient costs. Rather, this should be an explicit CSO funded by the Government.

### *Industrial harmony*

The QCA has not received any submissions from stakeholders that directly addressed the issue of industrial harmony. Nevertheless, the RTBU's submission stated that it was especially concerned at the implications of the Draft Undertaking for jobs, training and training standards, and employees' rights to collective industrial agreements.

The QCA recognises that some proposed amendments to the Draft Undertaking would require adjustments in QR's labour force arrangements, the most significant being with respect to the reassignment of the train control function from the above-rail business groups to Network Access. In addition, the proposed pricing arrangements, including the phase-in of efficient infrastructure maintenance costs and application of incentive regulation, could be expected to put pressure on the performance of certain below-rail functions with associated effects on the work practices of certain QR personnel.

QR has advised the QCA that the proposed train control reassignment would pose industrial issues that would need to be managed.

The QCA believes the public interest in industrial harmony must be balanced against a number of other public interest considerations, such as the promotion of competition, the efficient allocation of resources, the interest of consumers, and the competitiveness of Australian business and businesses.

Nevertheless, to assist QR manage industrial issues associated with the proposed amendments to the Draft Undertaking, transitional arrangements have been proposed. For example, the QCA has proposed that there be phasing of the reassignment of the train control function and of the reflection of efficient maintenance costs in reference tariffs. This should assist in QR's management of industrial issues. Moreover, with respect to the proposed reassignment of staff performing train control, the QCA notes that Network Access is effectively a business group that has been created with staff from other business groups in QR. In this regard, the QCA's proposal is consistent with QR's past internal management decisions.

### *Promotion of competition*

Competition is concerned with rivalry, or potential rivalry, between firms in a market. It is different to competitiveness, which relates to the ability of a firm to sell its products in a market. The public interest in competitiveness of Australian business is discussed below. Promotion of competition is concerned about enhancing, in a non-trivial manner, the opportunities and environment for competition.

The QCA believes the declaration of the services of QR's rail infrastructure is intended to promote competition in Queensland's above-rail market. The approval of an approved Undertaking would further enhance opportunities and the environment for competition. It would provide a stable, certain regulatory framework within which the market may develop. An approved Undertaking could assist in narrowing the matters likely to result in disputes and thus minimise the need to resort to arbitration.

The QCA is conscious that Queensland's above-rail market is in a developmental stage and that an approved Undertaking could assist in its growth. A properly functioning above-rail market is the best way of advancing rail consumers' interests. The QCA believes it is important to distinguish between the creation of a regulatory environment that results in one or more third-party operators running train services on QR's network and the protection of the competitive process itself. In the long-run, protecting competitors rather than the competitive process will undermine the integrity of any market.

As the monopoly provider of below-rail services, QR is likely to have significant commercial power compared to most access seekers. The QCA recognises that this commercial power varies across the different markets in which QR operates, due to countervailing forces such as road competition. Nevertheless, in general, QR's commercial power is material. Moreover, QR's above-rail business groups provide the majority of above-rail services in the State. Both these factors are likely to have an important effect on the way the above-rail market develops.

Consequently, an overriding factor in the QCA's assessment of the Draft Undertaking has been whether it provides a reasonable balance between the interests of access seekers and QR's legitimate business interests. The thrust of the Authority's proposed amendments across Parts 2 to 7 of the Draft Undertaking is aimed at providing a better balance between the interests of access seekers and QR's legitimate business interests. Generally speaking the QCA believes the Draft Undertaking did not sufficiently take account of the interests of access seekers.

For example, the QCA has proposed amendments to significantly tighten the ring-fencing arrangements, through functional reassignment and the application of strict confidentiality arrangements. The Authority's proposed amendments regarding capacity management address the establishment of a more transparent scheduling and train control framework that provides additional rights for access seekers regarding changes to schedules, provision of relevant capacity information and to prevent capacity becoming a barrier to entry.

The importance of an approved Undertaking to the development of the Queensland above-rail market was demonstrated by the interest of major Australian above-rail operators in QR's Draft Undertaking. FreightCorp, Toll, National Rail and Great Southern Railway each made important contributions to the Authority's assessment of the Draft Undertaking through their submissions.

Finally, the joint tender for rail haulage services by Stanwell Power Corporation, Ensham and Jellinbah mines in mid-2000 provides evidence of significant business opportunities in the Queensland above-rail market. Initially, the tender will involve approximately 6 million tonnes per annum, being approximately 25% of the Blackwater system's tonnage.

#### *Efficient allocation of resources*

The public interest in an efficient allocation of resources is best served by the Authority approving an Undertaking that facilitates the delivery of below-rail services at efficient prices and establishes a stable, certain regulatory framework. Such a regulatory framework would provide sufficient confidence to underpin investment in the above-rail market and that allows the market to develop in a non-distortionary manner.

The key issues in relation to QR's pricing structure for its declared services are the development of access charges that reflect efficient costs of delivering services and which create an environment where capacity is efficiently rationed and appropriate signals are provided to above-rail operators and QR for use and augmentation of network capacity. In this way, rail operators that can provide the best price/service package to consumers will win market share. In addition, the QCA has proposed the application of incentive regulation that encourages QR to seek operational efficiencies

The promotion of an efficient allocation of resources is closely aligned to the public interest in promoting competition (in the above-rail market). This was discussed in the previous section.

*Interests of consumers or any class of consumers*

The QCA Act does not differentiate between access seekers and the consumers of transport services. Nevertheless, in developing its Draft Decision, the QCA recognised that drawing such a distinction can be important.

The development of access arrangements facilitates the use of the services of QR's track infrastructure by third-party operators. However, these operators will generally be performing rail transport services on behalf of end-users, for example, carrying coal on behalf of a coal mine. Whilst the interests of end-users and third-party operators may often be aligned, the QCA has been cognisant of the fact that the ultimate beneficiaries of the opening up of access to QR's infrastructure should be the consumers of rail transport services.

In broad terms, the QCA believes the facilitation of competitive pressure in above-rail markets where there is currently little competition, such as for bulk commodities, has the potential to benefit consumers through greater choice of rail supplier. The best way to promote consumer interests is to provide a regulatory environment that is sufficiently robust that above-rail operators have the confidence to invest.

Nevertheless, a more direct way that the QCA has recognised the interests of consumers is in its support for end-users having the option of exercising direct control over transportation of their freight. This though is subject to QR's legitimate business interests being protected.

'Unbundling' the access right and haulage element of access agreements is potentially an important means of achieving this objective. QMC, the representative body of the coal mining sector, one of QR's largest customer segments, has argued strongly in favour of customers holding access rights.

Consequently, the QCA has proposed the Undertaking should provide that both end-users and third-party operators should be able to execute access agreements with QR, provided that an appropriately accredited rail operator performs the train services. This proposal would not apply to existing rail haulage contracts. Whether it is appropriate to depart or provide relief from such contracts is an issue for QR and Government.

The QCA's development of guiding principles for the assignment of management responsibility for QR's rail infrastructure has explicitly recognised the interests of classes of consumers of rail services. The relevant principles are that Network Access should provide access - using its own infrastructure - to any private siding and Network Access should provide access to any end-user's facility not owned or leased by a rail operator and/or a facility where there is joint use by end-users.

### *Competitiveness of Australian business*

The QCA believes that competitiveness relates to the ability of a firm to sell its products in a market. A reduction in cost structures or improvement in quality of service could improve competitiveness. Competitiveness appears relevant both for rail operators accessing QR's declared services and consumers of above-rail services provided by those rail operators. The QCA has drawn a balance between promoting such competitiveness and the protection of QR's legitimate business interests as access provider.

The QCA received a number of submissions that specifically addressed the issue of competitiveness. Some are identified in Table 9.

#### **Table 9: Stakeholder Comments - Competitiveness**

**QMC** - rail reform is in the public interest, as Queensland's best interests are served by a competitive, viable mining industry. All inputs to mining, including transport and in particular rail, must be competitive in all respects. A 'status quo' outcome would not be in the public interest.

**Stanwell** - rail coal transportation is a significant cost component in the operation of the Stanwell Power Station and one which in the competitive electricity market cannot be easily passed on to electricity consumers. Effective rail transport will also be a critical factor in plans to develop an industrial park adjacent to the power station. Access to rail infrastructure on a fair and reasonable basis to allow genuine competition for rail haulage is therefore critically important to Stanwell.

**AMC** - competitively priced rail transport is critically important to the AMC's proposed magnesium plant. To achieve this, the QCA will need to vigorously implement regulatory measures, which will provide efficiency in the provision of rail infrastructure and fair pricing for access which will promote genuine competition among rail hauliers. If the current monopoly situation is allowed to persist, then developments such as AMC's proposed magnesium plant will be at a serious disadvantage with its competitors overseas and could be placed in jeopardy as a result.

**Toll** - it is important to consider the role which rail plays in Australia's transport network and the ability of rail to compete with road. The QCA must consider the likelihood of the rail industry surviving given current government policies and the structure of QR's Draft Undertaking.

**FreightCorp** - identified the positive benefits of greater competition in the Queensland rail system as including the link between an increase in efficient utilisation of the system leading to a reduction in prices to end-customers and ultimately promoting rail's competitive position with respect to road transport.

**RTBU** - was especially concerned about the implications of the Draft Undertaking with respect to the environmental, social and economic impact of the transfer of freight from rail to road.

The QCA believes that the terms and conditions on which third-party operators negotiate access to QR's declared services affect their ability to compete with each other, QR's above-rail business groups and potentially other transport modes. In turn, the price and quality of service provided by these rail operators affects the competitiveness of the consumers of those services. QR's above-rail business groups currently provide freight services for traffics such as coal and minerals, grains, sugar, livestock and freight forwarders.

A number of these consumers of rail services are selling their products in international markets or face intense competition in their domestic markets. The ability of such consumers to pass on rail transport costs is likely to be constrained.

Consequently, to improve the competitiveness of all rail operators, the QCA believes that the pricing objectives, which are necessary to facilitate efficient resource allocation are highly

relevant. While it would be possible to regulate access prices below efficient levels in the short-term to improve the competitiveness of rail operators and end-users, by destroying QR's incentive to invest in its network, competitiveness over the medium to long-term would be adversely affected.

To protect the competitiveness of third-party operators compared with QR's above-rail business groups, the QCA believes that equivalence of the terms and conditions of internal and external access agreements should be a key objective of the ring-fencing framework established by an approved Undertaking.

Amendments to the Draft Undertaking have been proposed to facilitate achievement of that objective. Also, providing end-users with a right to hold access rights themselves and hence exert more control over the delivery of their products could facilitate improvements in their competitiveness.

#### *Economic and regional development issues*

QR is a provider of below-rail and above-rail services via a geographically widespread narrow gauge network of around 9,400 km. The opening up of access to QR's network to third-party entry, with the associated development of an above-rail market in Queensland, is likely to generate economic effects both at the aggregate level and across regions given the coverage of QR's network.

Some stakeholders specifically addressed the public interest in economic and regional development in their submissions as set out in Table 10.

#### **Table 10: Stakeholders Comments – Development Issues**

**FreightCorp** - there may be a negative short-term effect on employment and regional development, but overall it would be positive in the long run. If government has a desire to subsidise regional communities, it is not obvious why this should be done indirectly through subsidising railway employment. On the positive side, reductions in transport costs and improvements in service levels could improve the competitiveness of regional industry.

**QMC** - it should not be up to Network Access to encourage development in the public interest, if it risks distorting competition in coals and minerals markets by providing favoured rail access arrangements to new mines over existing mines. That role, if there is to be one, should be reserved for the Government and carried out on the basis of whole-of-government consideration.

**RTBU** - was especially concerned about the implications of the Draft Undertaking for regional jobs and regional development impacts.

In the context of the development of reference tariffs for QR's coal corridors, the QCA commissioned and independent report that examined the potential impacts on the Queensland and national economies of a 30% reduction in the rail freight rate for black coal in Queensland.<sup>9</sup>

This report effectively provides a range of possible outcomes for the reduction, which the Authority has labelled as the 'optimistic scenario' and the 'conservative scenario'. For each of these scenarios, Professor Mangan modelled the impact for the State economy of the change, based on two different assumptions, namely:

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<sup>9</sup> *Assessment of income, output and employment effects of increased coal production in Queensland*: Professor John Mangan, University of Queensland, October 2000 ("The Mangan Report").

- the impact of the estimated coal production increases assessed independently of any freight revenue losses or royalty gains. Implicit in this assumption is a judgement that QR could effectively absorb the loss through pursuing efficiency gains without a loss to the State Budget; and
- the impact of the estimated coal production increases inclusive of the effect of the potential freight revenue losses (that is, assuming that there was no scope for productivity improvements in QR, such that the reduction would directly impact on the State Budget).

The results of this modelling are presented in working paper 1. In interpreting these results, it is difficult to precisely identify the scope for efficiency gains within QR in order to offset the impact of this revenue reduction. The QCA believes that the most likely outcome lies somewhere between the two assumptions. Accordingly, for both the conservative and optimistic scenarios, the Authority has set out below in Table 11 the potential impact based on the mid-point between the two sets of assumptions outlined above. The Authority believes that this approach provides a reasonable guide as to the likely impact.<sup>10</sup>

**Table 11: Summaries of potential effects of a 30% rail freight rate reduction**

**Conservative scenario**

	<b>Output (\$Am)</b>	<b>Regional income (\$Am)</b>	<b>Value added (\$Am)</b>
<b>Annual average for period 2002-2010</b>	146	34	65
<b>Post 2010 annual average</b>	300	70	133

**Optimistic scenario**

	<b>Output (\$Am)</b>	<b>Regional income (\$Am)</b>	<b>Value added (\$Am)</b>
<b>Annual average for period 2002-2010</b>	1,205	280	531
<b>Post 2010 annual average</b>	1,717	399	756

The Mangan report indicates that, under the conservative scenario and taking the mid-point of the alternative assumptions, over the period 2002 – 2010 a cumulative annual average value-added effect is \$65 million. This average annual increase accumulates over the period such that at the end of 2010, the Queensland economy would be 0.7% greater as a consequence of the change assuming no other impacts. In other words, if, based on 1997/98 prices, the state economy was \$90 billion today, it would be expected to grow to approximately \$90.6 billion at the end of 2010 as a consequence of these reforms.

Under the optimistic scenario, the impact is much greater. The midpoint of the assumptions under the optimistic scenario modelled in the Mangan Report indicates that cumulative growth over the period represented 5.2%. Consequently, based on 1997/98 prices, if the state economy

<sup>10</sup> Professor Mangan has indicated that in his view, the potential for efficiency gains for QR are at the upper end of the range and accordingly this approach should be considered to be a conservative presentation of likely impacts.

was \$90 billion today, it would be expected to grow to approximately \$94.7 billion at the end of 2010 as a result of these reforms.

The Mangan Report notes that employment estimates are notoriously difficult to estimate. The midpoint of the impact under the pessimistic scenario is a creation and maintenance of 1,206 full-time equivalent positions over the 2002-10 period, while under the optimistic scenario the equivalent figure is 9,954.<sup>11</sup>

Around 60% of the jobs created or maintained would be in the Central Queensland region as a result of the significant coal activity occurring there. Given its role as a financial and administrative centre, Brisbane would attract around 20% of the new or maintained jobs.<sup>12</sup>

Finally, the QCA does not believe that an undertaking is the appropriate vehicle to target specific regional development objectives that are better addressed by government policies.

#### *Transitional issues created by reform programs*

The QCA recognises that a number of its proposed amendments to the Draft Undertaking would require operational changes by QR, for example, reassigning management responsibility for its train control function and the calculation of efficient infrastructure maintenance costs in reference tariffs. There may be cost or other grounds for such changes to be phased in rather than effected in full from the commencement of an approved undertaking. In making its assessment, the Authority has balanced the need for transitional arrangements against any potential adverse effects on the promotion of competition in the above-rail market.

Transitional arrangements proposed by the QCA include the phase-in of efficient infrastructure maintenance costs with respect to reference tariffs on QR's coal network. The Authority proposes that there be a six-month period after commencement of an approved Undertaking in which QR would reassign management responsibility of its train control functions at Mackay and Rockhampton. Nine-month periods are proposed for corresponding changes at Townsville and Brisbane Central. Finally, a two-year transitional period for QR to develop internal access agreements for its existing services where there are no external contracts currently in place, has been proposed.

The QCA sought submissions on whether the Undertaking should include any overall transitional arrangements and if so what would be appropriate. Proposals raised in submissions included the uncoupling of existing coal and minerals rail agreements into their separate access and haulage components, such that access rights implicit in existing coal and rail agreements would be vested in the mining companies. MIM Group supported reductions in access charges identified by the reference tariffs approved as part of the Undertaking flowing through to existing coal and minerals contracts. The QCA though has no power under the QCA Act to revisit existing rail haulage agreements as part of its review of QR's Draft Undertaking.

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<sup>11</sup> Projections of productivity improvements in direct coal industry labour of upwards of 30% were used to adjust downwards the estimated employment impacts.

<sup>12</sup> The Queensland Multi-Regional Model (QMRM) allows the economic effect of the production and export increases from rail freight reductions to be spatially distributed across Queensland regions. The QMRM uses hierarchically balanced input-output tables for Queensland and Queensland regions constructed by the former Government Statistician's Office (GSO). For a given input I, exporting regions are assumed to export all their surplus and importing regions are assumed to import a total amount T of input i in proportion to the surplus from each region. Actual data on inter-regional imports are allocated across regions on the basis of data supplied by GSO or where hard data is not available, it is assumed that regions import in proportion to total production in exporting industries. As a result, input-specific trade vectors can be generated and spliced together to form the inter-regional trade matrix. The Mangan Report argued that QMRM performs well in diagnostic tests and provides an efficient means of estimating industrial significance and allocation of economic effects across regions and to the rest of Australia.

The Authority anticipates that the implementation of the arrangements contained in this Draft Decision will have, over time, a major financial impact on QR. However, the QCA has not been in a position to seek submissions on appropriate transitional arrangements until the Authority's assessment of reference tariffs was completed as part of the release of this Draft Decision. Consequently, the Authority would welcome submissions on this issue in response to this Draft Decision.

### *Other relevant issues*

The QCA places a high priority on approving an Undertaking that establishes a stable, certain regulatory framework which allows QR's above-rail business groups and third parties to identify and pursue investment opportunities in the above-rail market.

A pertinent issue in facilitating such an outcome is the balance created by the Draft Undertaking between flexibility and prescription. There may be matters where the Authority's discretion in future arbitrations could be removed to provide certainty, by setting them out in the Undertaking. On the other hand, there may be matters where it is appropriate the Authority retains flexibility either in future arbitrations or by explicitly defining disputes about matters contained in the Undertaking that should be referred to the Authority for consideration.

The Authority considers that there are threshold issues that will be of concern to all access seekers that must be incorporated in QR's Undertaking through provisions of a transparent and enforceable nature. These would include the negotiation framework, scheduling and train control procedures and reference tariffs. On the other hand, there are other matters that are likely to be better addressed through commercial negotiation between QR and access seekers/third-party operators because they will relate to the particular characteristics of a third-party operator's proposed train services. It is neither possible nor desirable to attempt to address all possible issues through the Undertaking.

Moreover, the Authority considers that a number of relevant matters have not yet been resolved, including:

1. the terms of a standard access agreement;
2. the assignment of management responsibility for QR's infrastructure south of Gladstone; and
3. the assessment of reference tariffs for the West Moreton system (and other parts of QR's network).

Attempting to prescribe such matters in the Undertaking would significantly delay the finalisation of the Authority's assessment of the Draft Undertaking. The Authority has concluded that the benefit in progressing the assessment through release of this Draft Decision outweighs any detriment from the delay in resolving these issues.

The Authority recognises that where matters are left to commercial negotiation, resort to arbitration remains an option. However, resort to arbitration under the formal procedures of the QCA Act is likely to be a time consuming and expensive process.

The Authority anticipates there are a range of matters that could arise during an access negotiation that become the subject of dispute but which are ill-suited to resolution through formal arbitration. There are likely to be benefits to both Network Access and access seekers from being able to resort to shorter, less expensive dispute resolution processes. In this context the QCA has powers in relation to mediation of access disputes: s115A; and resolution of disputes with regard to specified matters in an undertaking: s137.

The QCA understands that its performance of a mediation role in a dispute which it later arbitrates under the QCA Act may jeopardise the efficacy of the QCA's determination. Consequently, if the QCA believed that a mediated resolution of an access dispute during an access negotiation could be achieved, it would refer the dispute to a professional mediator. The QCA believes that application of the mediation power could significantly shorten the period between the commencement of an access negotiation and the signing of an access agreement.

The QCA has identified several matters in the Draft Undertaking that it has proposed should be subject to tailored dispute resolution processes defined in an approved Undertaking. These dispute resolution processes relate to:

1. reassignment of management responsibility within QR for a certain piece of declared rail infrastructure;
2. resumption of access rights by QR; and
3. matters to be addressed in the joint safety risk assessments by Network Access and each third-party operator in the context of access agreements,

which are discussed in Chapters 4, 6 and 7 respectively.

The QCA believes that defining a specifically tailored dispute resolution process for these matters will provide greater certainty to access seekers and third-party operators.

## CHAPTER 2. SCOPE & ADMINISTRATION

### KEY ASPECTS

**Coverage** - it is appropriate that the Draft Undertaking not cover the provision of above-rail services and below-rail standard gauge services used by interstate traffic.

**Land holder approval** - the Undertaking will need to address the provision of information in relation to property on which rail infrastructure is located and which is not controlled by QR.

**Term** - the three-year term of the Undertaking is adequate.

**Review** - the QCA and QR should meet one year after the commencement of the Undertaking to review its operation.

**Grandfathering** - the Undertaking may only operate in respect of future arrangements and not in relation to any existing arrangements.

**Reporting** - for the Undertaking to be effective it is necessary there be a regime of transparent reporting in relation to its operation.

## 2.1 Coverage of declared services

### *QR's Position*

The services of QR's track and associated rail infrastructure – including signalling, train control and associated communications, and if necessary, electric traction – essential to the use of the track will be subject to the Undertaking: para 2.1(a). However, some exceptions to this are identified, being when negotiations for access to stations, platforms and marshalling yards are not subject to the Undertaking: para 4.1.1(b).

The Undertaking does not cover the provision of:

- above-rail services; and
- below-rail services that are used for transportation between Queensland and another State and that utilise standard-gauge track and rollingstock: para (2.1)(a) & (b).

### *Stakeholder Comments*

Stakeholders' submissions expressed a wide range of views concerning the services that should be covered by the Undertaking.

#### **Table 1: Coverage of services**

**Queensland Government, QMC** - the terms and conditions of the Undertaking should apply to negotiations for access to all declared rail infrastructure. The Undertaking should not cover below-rail infrastructure explicitly excluded from the declaration - track with inter-jurisdictional characteristics should be covered by the national rail access regime.

**RTBU, National Rail** - QR's position is acceptable.

**Stanwell, AMC, FreightCorp, Great Southern Railway** - the Undertaking should cover a wider range of services than the Government's declaration, including those related to station yards, stabling facilities and storage, loading and unloading facilities.<sup>13</sup>

**FreightCorp** - the Undertaking should cover QR's dual-gauge track.

**ARTC** - it is unclear whether the Undertaking covers the interstate services using mixed-gauge track - standard and narrow gauge.

### *QCA's Analysis*

The QCA endorses above-rail services not being covered by the Undertaking. Such services are not covered by the regulation-based declaration of QR's rail transport infrastructure.<sup>14</sup> Similarly, the QCA endorses the Undertaking not covering below-rail standard gauge services used by interstate traffic, which are explicitly excluded from the declaration.

Nevertheless, QR manages around 35km of dual-gauge track upon which both narrow and standard gauge rollingstock may run.<sup>15</sup> The QCA understands interstate train services using this dual-gauge track would be covered by the national rail access regime administered by ARTC. ARTC has advised the QCA it is currently negotiating a wholesale arrangement with QR which

<sup>13</sup> The QCA understands that several of these services are, in fact, covered by the declaration.

<sup>14</sup> The declaration is based on the definition of rail transport infrastructure in the *Transport Infrastructure Act 1994*.

<sup>15</sup> This track runs from the Acacia Ridge terminal – located around 14km south of central Brisbane – both to the Port of Brisbane and to the Roma Street Station in central Brisbane.

will set out the terms and conditions under which this part of QR's network will be accessed by interstate rail services and how these services will interact with intrastate standard-gauge movements.

In contrast, the QCA understands that QR's Undertaking would cover intrastate services using the dual-gauge track. In other words, two access regimes would apply for the services of the dual-gauge track, the applicable regime dependent on whether the traffic using the track was of an intrastate or interstate nature.

The QCA recognises that administration of QR's Undertaking would need to have regard to interstate influences, in particular, inter-operability between Network Access' interstate and intrastate customers. This will occur where interstate trains link up with the intrastate network on the dual gauge track.

The QCA is concerned about the proposed exclusions from coverage by the Undertaking of some services provided by stations, platforms and marshalling yards. Acceptance of that would make the scope of the Undertaking narrower than the regulation-based declaration of QR's rail-transportation infrastructure services. The QCA's understanding of the scope of the declared rail services is discussed in section 4.1 of Chapter 4.

#### ***QCA's Position***

**The QCA notes that the Undertaking does not cover the provision of:**

- **above-rail services; and**
- **below-rail standard-gauge services used by interstate traffic.**

## **2.2 Rail infrastructure on privately-owned land**

### ***QR's Position***

QR leases the majority of the land upon which its rail network is constructed from Queensland Transport under a long-term arrangement.

However, in some parts of QR's network, QR does not own or lease the land upon which rail infrastructure is located. Consequently, QR does not have the authority to allow third-party operators to access its infrastructure on this land without the consent of the landowner. QR proposes that third-party operators would have to take responsibility for gaining the necessary landowner approvals. QR indicates that it will provide reasonable assistance in identifying the relevant landowners but does not indicate what form this assistance will take: para 2.1(d).

QR subsequently indicated in its initial submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* that s134 of the *Transport Infrastructure Act 1994* enables it to authorise access to the majority of land upon which its infrastructure is situated. It is only QR's infrastructure constructed since 1 July 1995 that could be situated on land in respect of which QR does not have authority to grant third-party access.

A majority of stakeholders were concerned about the potential number of lines affected by the need for third-party operators to obtain landowner approval. However, there were divergent views on how the matter should be addressed.

### *Stakeholder Comments*

Stakeholders' submissions identified the type of information that should be provided to access seekers with respect to QR's rail infrastructure located on privately-owned land.

#### **Table 2: Nature of assistance**

**AMC, Stanwell** - QR need not negotiate with these landowners but their names and details should be provided to third-party operators so negotiation between the operators and landowners are able to take place expeditiously.

**Toll** - for lines where it is necessary to obtain landowner consent, there should be a requirement on QR to:

- identify the land affected;
- provide details about the landowner, including contact details;
- advise the nature and extent of the rights which QR holds in relation to the infrastructure;
- give its consent to the access seeker's proposed use of the facility; and
- give reasonable assistance to facilitate negotiations between the parties.

**QMC** - Network Access should be obliged to obtain the necessary approvals from landowners to which it presently does not have the authority to grant access, so that it may grant that access to whomever is the party seeking it. The mere provision of contact names to non-QR access seekers would be insufficient and would continue to impose on those third parties a requirement not applied to QR above-rail business groups.

**Queensland Government** - QR could identify lines on an 'as required' basis, including details of the landowner.

**FreightCorp** - the problem was not likely to be significant, so the Undertaking would not necessarily need to specifically identify the affected locations.

**RTBU** - QR's commitment to facilitate the required permission is sufficient.

### *QCA's Analysis*

The QCA considers that the main issue is determining the amount of information QR should be expected to provide to potential access seekers to facilitate the access negotiation process. A number of subsidiary issues, such as the timing of the provision of this information and its impact on the negotiation of an access agreement, also arise.

The QCA recognises that QR incurs a cost in collecting this information, some of which may not be readily to hand. Nevertheless, as network owner/manager, it is far easier and more cost effective for QR to collect the information than for access seekers to be expected to do so. In light of this, the QCA considers that QR's proposed commitment to provide '*reasonable assistance*' in identifying the relevant landowners does not provide sufficient certainty to access seekers concerning the information they require.

The QCA considers that access seekers' interests would be protected if QR were to identify the land affected and provide the name and contact details of the relevant landowner. In addition, QR should advise the nature and extent of the rights, if any, which it holds in relation to the affected rail infrastructure. The Authority considers that provision of such information would not be contrary to QR's legitimate business interests. The QCA believes that it would be reasonable for QR to provide this information within 14 days of an access seeker lodging an access application.

QR's provision of contact details of landowners where its rail infrastructure is on land for which it is not authorised to provide access is likely to be of most use to a potential access seeker if it is received early in the negotiation process. This is because it poses a potential hurdle to

gaining access. Given the time and resources involved in negotiating an access agreement, it would be in both parties' interests to be able to determine whether there was a landowner problem, and have an opportunity to address that problem, before fully engaging in the negotiation process.

The QCA considers that this objective would be facilitated if QR were to provide a letter to the access seeker indicating whether or not QR has an objection to it negotiating access to the land within 14 days of it lodging an access application. The access seeker could then pass the letter to the affected landowner indicating that it was negotiating with QR with respect to the use of QR's rail infrastructure.

Nevertheless, QR has advised the QCA that the affected lines are at locations such as mines and ports. Therefore, those from whom permission would need to be sought would generally be inclined to provide it expeditiously. Whilst permission is being sought there would appear to be no justification in delaying negotiations.

#### ***QCA's Position***

**The QCA would favourably consider an Undertaking that:**

- **committed QR to provide an access seeker, seeking access to rail infrastructure on land to which QR is not authorised to grant access, with:**
  - **the name, address and contact details of the relevant landowner;**
  - **advice of the nature and extent of the rights, if any, which QR holds in relation to the infrastructure; and**
  - **a letter indicating that the access seeker is negotiating with QR with respect to the use of QR's rail infrastructure and whether or not QR has an objection to the third-party operator negotiating access to the land and in that event full details of the objections;**

**within 14 days of the lodgement of the access application by the access seeker.**

### **2.3 Term of QR's Undertaking**

#### ***QR's Position***

QR has proposed a three-year term for its Undertaking: cl 2.2

#### ***Stakeholder Comments***

Stakeholders' submissions generally supported the three-year term. However, that support tended to be conditional. There was support for shorter and longer terms.

**Table 3: Term of Undertaking**

**AMC, MIM Group, National Rail, Queensland Government, QMC, RTBU, Stanwell** - generally supported the proposed three-year term. However, the support tended to be conditional, in particular, on the QCA's ability to ensure QR's compliance with the Undertaking and make any necessary amendments to it.

**FreightCorp** - proposed a one-year term.

**ARTC** - proposed a five-year term.

**Great Southern Railway** - proposed an unspecified longer term.

***QCA's Analysis***

The QCA endorses the proposed three-year term of the Undertaking, which is equivalent to QR's proposed term for reference tariffs. This time frame is long enough to provide reasonable certainty to both access seekers and QR. A longer duration would appear to be inappropriate on the following grounds:

- it is QR's first Undertaking;
- it is difficult to anticipate the nature of future development in the above-rail market in Queensland; and
- the QCA has very limited powers to require changes to an approved undertaking during its term.

***QCA's Position***

**The QCA accepts the proposed three-year term of the Undertaking.**

**2.4 Review of the Undertaking*****QR's Position***

QR has proposed that it and the QCA meet approximately 12 months after the commencing date to review the operation of the Undertaking. This review will identify those provisions, if any, of the Undertaking that are not operating to the satisfaction of QR or the QCA. If this review identifies that amendments are required to the undertaking, QR will submit a draft amending undertaking following this process: cl 2.3.

***Stakeholder Comments***

Stakeholders' submissions reflected different understandings as to the power of the QCA to seek amendments to QR's Undertaking.

**Table 4: Amending QR's Undertaking**

**FreightCorp, Toll** - the QCA Act provides the necessary powers for the QCA to amend an Undertaking.

**QMC** - the QCA must ensure that it reserves the power to effect amendment of the Undertaking, including through provisions in the Undertaking if necessary.

**Queensland Government** - clear parameters should be in place to govern the circumstances in which, and the processes by which, the QCA can request amendments to the Undertaking.

**Stanwell, AMC** - if the QCA were to intervene or to seek amendments to QR's Undertaking, then it would first require QR's agreement and be a matter of some significance that was impacting on the effectiveness of the Undertaking.

**MIM** - the means of determining success/failure of the Undertaking in achieving the defined objectives should be agreed between QCA and QR but need not form part of the Undertaking.

**RTBU** - the QCA already has significant power over the Draft Undertaking and any amending Undertaking as a result of the 12 month review.

### ***QCA's Analysis***

The QCA understands that it will not be able to require QR to change an approved Undertaking during the period that it is in force by relying upon the QCA Act. Consequently, it would not be possible for the QCA to require QR to lodge an amending undertaking following the 12 month review if the QCA identified problems in the operation of an approved Undertaking. The lodgement of an amending undertaking would be at QR's discretion.

To the maximum extent possible, its potential problems in the operation of the Undertaking must be identified and addressed prior approval. This objective has driven the consultative approach adopted by the QCA in assessing QR's Draft Undertaking. The Authority emphasises that stakeholders' assessment of, and comments on, the Draft Decision should recognise the QCA's limited powers in relation to amending approved undertakings.

#### ***QCA's Position***

**The QCA accepts that QR and it should conduct a review of the operation of the Undertaking 12 months after its commencement.**

## **2.5 Transitional arrangements**

### ***QR's Position***

The Draft Undertaking applies only to the negotiation of new access agreements or the negotiation of access rights additional to those subject to an existing access agreement. Nothing in the Undertaking can require a party to an existing access agreement or existing rail haulage agreement to vary a term or provision of that agreement: cl 2.4.

### ***Stakeholder Comments***

Stakeholders' submissions proposed a number of reasons for transitional arrangements.

#### **Table 5: Nature of transitional arrangements**

**QMC** - the Undertaking should provide for the 'uncoupling' of existing coal and minerals rail agreements into their separate access and haulage components, such that access rights implicit in existing coal and minerals rail agreements would be vested in the mining companies.

**MIM** - the existing coal and minerals contracts should be amended to reflect the Undertaking, with any reductions in access charges flowing through to end-users.

**ARTC** – QR should include a transitional period of 2-3 years over which current haulage agreements should be re-negotiated under the provisions of the Undertaking.

**Stanwell, AMC** - there may need to be a transitional period to allow a gradual introduction, perhaps over three years, of a market in rail capacity.

**FreightCorp** - any existing arrangements that are inconsistent with the Undertaking should be brought into conformance at the earliest opportunity.

**Queensland Government** - transitional arrangements could be an issue for negotiation between QR and its customers.

### *QCA's Analysis*

The QCA has no power under the QCA Act to revisit existing rail haulage agreements as part of its assessment of QR's Draft Undertaking. Consequently, the Authority accepts the Undertaking will only apply to the negotiation of new access agreements or the negotiation of access rights additional to those subject to an existing access agreement.

The QCA believes that transitional arrangements are most sensitive for QR's existing commercial agreements that will be converted to internal access agreements, in particular, the length of time that these commercial agreements should be protected from coverage by the Undertaking. Internal access agreements are discussed in Chapter 3.

#### *QCA's Position*

**The QCA acknowledges that the Undertaking will only apply to the negotiation of new access agreements and/or the negotiation of access rights additional to those subject to an existing access agreement.**

## 2.6 Public reporting of QR's compliance with the Undertaking

### *QR's Position*

The Draft Undertaking does not provide for any ongoing public reporting by QR on its compliance with an approved Undertaking.

Following discussions between the QCA and QR, QR has proposed that it will publish annually the following list of performance indicators in respect of its compliance with the Undertaking.

#### 1. Information provision

- percentage of requests for preliminary information responded to within the nominated timeframe.<sup>16</sup>

#### 2. Indicative access proposals

- percentage of access applications acknowledged within the nominated timeframe;<sup>17</sup>
- percentage of access applications in which an extension of time for provision of an indicative access proposal is sought by QR; and

<sup>16</sup> Where the Information Pack (Schedule E, preliminary information) has previously been compiled, the nominated time frame is 14 days. However, where the Information Pack has not previously been compiled, the nominated time frame is 30 days.

<sup>17</sup> The nominated timeframe is 7 days after QR receives the completed access application, including any necessary clarification.

- percentage of indicative access proposals provided within the nominated timeframe.<sup>18</sup>

### 3. Disputes

- number of non-ring-fencing related disputes, regarding an alleged procedural breach of the Undertaking, that are referred to the dispute resolution process;
- number of non-ring-fencing related disputes, regarding an alleged substantive breach of the Undertaking, that are referred to the dispute resolution process;
- number of disputes where QR was found to have committed a procedural breach of the Undertaking; and
- number of disputes where QR was found to have committed a substantive breach of the Undertaking.

### 4. Ring-fencing

- number of complaints received regarding an alleged breach of QR's ring-fencing obligations; and
- number of complaints where QR was found to have breached its ring-fencing obligations.

### *Stakeholder Comments*

A majority of stakeholders' submissions expressed strong support for comprehensive public reporting by QR. However, there was a divergence of views as to what aspects of the Undertaking QR should be required to report on.

#### **Table 6: Public reporting**

**Stanwell** - QR should report traffic on, and the costs and revenues from, each track section.

**QMC** - QR should prepare an annual statement of compliance for all aspects of the Undertaking in accordance with a framework established by the QCA. In addition, the Auditor-General should also separately evaluate and report on QR's accounts and compliance with the cost allocation manual.

**Toll** - QR should report on the number of access applications received, the period taken to provide indicative access proposals, the time taken for completion of negotiations, and concluded arrangements and substantial complaints.

**Queensland Government** - the QCA should monitor QR's compliance with reporting requirements. However, it is a matter for the QCA whether reporting should be public, although it may be preferable to incorporate all items of compliance reporting in a periodic (eg annual) report.

**RTBU** - opposed public reporting beyond QR's existing obligations, stating that QR already has legislative public reporting requirements and provides reports to the Transport Minister and Parliament.

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<sup>18</sup> The nominated time frame is 30 days after acknowledgment of an access application, unless an extension of time for provision of an indicative access proposal is sought in which case the nominated time frame is the extended period of time, either that advised to the operator within 7 days of the acknowledgment or that determined by the QCA in the event of a dispute.

### *QCA's Analysis*

Performance monitoring forms an important part of the regulatory environment. The dissemination of information through public reporting increases the transparency of a regulated entity's operations. It also creates an incentive to improve achievement of relevant standards. This transparency also assists the regulator to be accountable for its regulatory decisions.

A diverse range of stakeholders will make use of this information. The regulated entity will seek to demonstrate conformity with its obligations under the access regime and emphasise its commitment to maintaining and improving service quality. Customers and potential customers will use the data to make informed judgements as to the cost effectiveness of the service being offered and to facilitate future negotiations. Shareholders will be interested in the reasonableness of regulatory constraints in light of the entity's financial performance. The regulator will be concerned with the actual performance of the service provider under the imposed regulatory constraints.

A regular flow of relevant information engenders confidence in an access regime for all concerned. It provides the opportunity for the regulated entity to demonstrate its commitment to the regulatory process. Consequently, the QCA supports some form of ongoing reporting by QR in relation to compliance with the Undertaking. It considers that this will promote accountability on QR's part and provide evidence of the integrity and effectiveness of the Undertaking. These are likely to be important factors in the early stages of development of a competitive above-rail market.

However, the QCA recognises that public reporting is not a costless exercise for QR, although this concern may be ameliorated by adopting any indicators currently used for internal purposes in appropriate circumstances. As such, public reporting should be constrained to that information necessary to minimise the relevant disadvantages of interested parties other than QR.<sup>19</sup>

In this context, the Undertaking covers a wide range of issues including pricing, service quality, access applications and the negotiation framework. Accordingly, public reporting will be necessary on many of these aspects. Principally it can be broken into three categories:

- general undertaking related information;
- financial performance; and
- service performance.

Financial and service performance indicators are discussed in Chapter 5.

General undertaking-related indicators are measures that reflect QR's observance of commitments established in its Undertaking. QR has proposed that it annually report a suite of ten such indicators, broken into four categories:

- information provision;
- indicative access proposals;

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<sup>19</sup> Regulated monopolies have superior information compared to the regulator and customers with regard to their business operations, costs, efficiency, service delivery capabilities and future market prospects. This information asymmetry is common to all regulatory regimes and has the potential to bias regulatory outcomes in favour of the regulated monopoly and act as a barrier to entry for potential entrants.

- disputes; and
- ring-fencing.

The QCA considers that QR should report absolute and percentage figures for the information, rather than simply percentages as currently proposed. While QR argues that only percentage statistics are necessary to indicate its compliance with the Undertaking, the QCA regards both forms of presentation as revealing pertinent information.

Central to the negotiation process is QR's obligation to provide an indicative access proposal. The QCA considers that information should be gathered that reflects any discontent with the manner in which QR has prepared the document. Accordingly, the QCA believes that the compliance indicators, suggested by QR, should be supplemented by:

- the average number of days taken to acknowledge an access application, in those circumstances where QR has taken in excess of 7 days to respond to access seekers;
- the average number of days taken to provide the indicative access proposals, in those instances where QR has taken in excess of 30 days to provide the document to access seekers; and
- the number, and percentage, of instances in which an access seeker has notified QR that it believes the indicative access proposal has not been prepared in accordance with the Undertaking.

QR is reluctant to report statistics on the number of agreements that have been concluded. It has argued this in no way reflects its compliance with the Undertaking and may in fact be misleading, because:

- there will be a wide variety of issues that may result in a negotiation not reaching an agreement; and
- where a rail operator is already running train services on QR's network, it is likely a negotiation will result in a variation to an existing agreement, rather than a new agreement.

In practice, the transparency associated with QR's scheduling processes will indicate to third-party operators when access agreements are completed by virtue of variations that occur to the master and daily train plans. Accordingly, the QCA believes that there would appear to be little reason for this information not to be published by QR as part of periodic reporting.

#### ***QCA's Position***

**The QCA would favourably consider an Undertaking that reported to the QCA within the first half of each financial year, in respect of its previous financial year:**

- 1. the number, and percentage, of requests for preliminary information responded to within the nominated timeframe;**
- 2. the number, and percentage, of access applications acknowledged within the nominated timeframe;**
- 3. the number, and percentage, of access applications in which an extension of time for provision of an indicative access proposal is**

sought by QR;

4. the number, and percentage, of indicative access proposals provided within the nominated timeframe;
5. the average number of days taken to acknowledge an access application, in those circumstances where QR has taken in excess of 7 days to respond to access seekers;
6. the average number of days taken to provide the indicative access proposals, in those instances where QR has taken in excess of 30 days to provide the document to access seekers;
7. the number, and percentage, of instances in which an access seeker has notified QR that it believes that the indicative access proposal has not been prepared in accordance with the Undertaking;
8. the number of non-ring-fencing related disputes, regarding an alleged procedural breach of the Undertaking, that are referred to the dispute resolution process;
9. the number of non-ring-fencing related disputes, regarding an alleged substantive breach of the Undertaking, that are referred to the dispute resolution process;
10. the number of disputes where QR was found to have committed a procedural breach of the Undertaking;
11. the number of disputes where QR was found to have committed a substantive breach of the Undertaking;
12. the number of complaints received regarding an alleged breach of QR's ring-fencing obligations;
13. the number of complaints where QR was found to have breached its ring-fencing obligations;
14. the number of agreements concluded; and
15. the number of variations to existing agreements concluded.

## CHAPTER 3. RING-FENCING ARRANGEMENTS

### KEY ASPECTS

**Vertical integration** - QR's vertical integration gives rise to actual and perceived conflicts that could undermine the efficacy of the Undertaking in areas such as scheduling, train control and confidentiality.

**Ring-fencing** - due to the vertically integrated structure, it is necessary for there to be appropriate ring-fencing arrangements that protect the legitimate business interests of all parties. Those arrangements should be the subject of external audit and provision should be made for penalties if breaches occur.

**Train control** - the scheduling and train control function should be under the exclusive auspices of Network Access and not left as a function under the control of the QR above-rail groups.

**Confidentiality** - information provided by access seekers must be appropriately protected within the QR organisation, including through confidentiality deeds and acknowledgment registers.

**Internal access agreements** - principles to guide the development of internal access agreements for existing services should be incorporated in the Undertaking in place of Schedule A.

**Approved conduct** - Internal access agreements for new train services developed in accordance with approved reference tariffs and a proposed standard access agreement applicable for coal haulage services should not be subject to the preventing or hindering access provisions of the QCA Act.

### 3.1 Introduction

As a vertically integrated enterprise, QR could potentially use its monopoly power in the below-rail market to gain an unfair competitive advantage in the above-rail market. For example, QR's monopoly arm could pass confidential information about third-party operators to its competitive arm providing its above-rail business with an inappropriate competitive advantage.

The QCA believes that third-party operators' perception of this potential problem could seriously undermine confidence in the above-rail market which would distort the evolution of this market. In the QCA's view, the perception problem underlines the importance of QR having credible ring-fencing arrangements in the eyes of third-party operators such that these operators have confidence that QR's capacity to exploit an unfair competitive advantage is appropriately constrained.

Broadly, ring-fencing is the separation of business functions within an enterprise for organisational and accounting purposes, with management of information flows between the separated business functions. It is based on the premise that the operation and management of the monopoly assets are placed on a stand-alone basis to be managed independently of any other business arms, in particular the competitive arm, of the enterprise.

Part 3 and Schedule B of the Draft Undertaking outline the measures QR has already undertaken, and proposes to undertake, to establish ring-fencing arrangements within the organisation. The proposed ring-fencing measures address organisational structure, accounting arrangements, internal access agreements and limitations on information transmission. The QCA's assessment of these proposed measures is discussed below, with the exception of accounting arrangements, which are discussed as part of cost allocation in Chapter 5.

Given their importance to QR's ring-fencing arrangements, the Authority has chosen to discuss the confidentiality provisions established in Part 4 of the Draft Undertaking in this chapter of the Draft Decision.<sup>20</sup>

### 3.2 Organisational structure

#### *QR's Position*

QR has established its organisational structure to facilitate separation of the management of rail infrastructure from the operation of train services. In the event that QR varies its organisational structure during the term of the Undertaking and such variation impacts upon the contents of cl 3.2, QR will submit to the QCA a draft amending undertaking prior to the restructure being implemented: para 3.2(a).

Network Access has been established as a separate business group to those delivering train services (the above-rail business groups). In addition, there are service groups whose purpose is to provide support activities for both Network Access and the above-rail business groups: para 3.2(b).

The Group General Manager of Network Access reports directly to the Chief Executive. The function of Network Access is to manage the provision of below-rail services, with the exception of services associated with stations, platforms and selected marshalling yards. In performing this function, the responsibilities of Network Access will include:

- (a) negotiation of access agreements with railway operators;

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<sup>20</sup> Confidentiality is covered in cl 4.2 of the Draft Undertaking.

- (b) development and management of agreements with Queensland Transport regarding the provision of rail infrastructure that is supported by infrastructure payments;
- (c) provision and/or procurement of appropriate levels of maintenance and investment for the rail infrastructure to ensure that the rail infrastructure is provided at the standard required to meet QR's obligations to railway operators;
- (d) assessment and management of capacity and available capacity;
- (e) procurement of appropriate train control, including specifying scheduling and train control protocols, and monitoring the provision of train scheduling and control to ensure that it is provided in accordance with the Protocols; and
- (f) procurement of traction power on electrified sections of track, including the management of power supply from other parties: para 3.2(c).

The managers of the above-rail business groups report directly to the Chief Executive. The responsibilities of these business groups include:

- (a) operation of train services and other above-rail services;
- (b) provision and/or procurement of appropriate levels of maintenance of, and investment for, above-rail services;
- (c) the management of stations, platforms and selected marshalling yards;
- (d) provision or procurement of appropriate levels of maintenance and investment for stations, platforms and selected marshalling yards; and
- (e) provision of train scheduling, train control and associated incident management services on behalf of Network Access and in accordance with the Protocols specified by Network Access: para 3.2(d).

Within three months of the approval of the Undertaking, QR will develop Protocols that will specify:

- (a) the practice for determining train priority;
- (b) the practice for management of out-of-course running;
- (c) incident management practices;
- (d) train operation information and communication practices; and
- (e) practice for train scheduling.

These Protocols, once developed, will be made available to the QCA for review if the QCA requires: para 3.2(e).

*Supporting arguments for assignment of scheduling and train control function*

**Assignment options** - in its supplementary submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*, QR identified three options for the assignment of management responsibility for the scheduling (capacity management) and train control functions:

- capacity management function within Network Access, existing train control function within above-rail business groups (Option A);
- capacity management function and existing train control function within Network Access (Option B); and
- capacity management and below-rail element of train control function within Network Access, above-rail element of train control function within above-rail business groups (Option C).

While recognising that each of the options can be implemented effectively, QR argued that it adopted Option A on the grounds that:

- there is no potential for the above-rail business groups to manipulate the determination of capacity to prevent third-party entry;
- it requires minimal organisational change and minimal expenditure in achieving the desired objectives for train control;
- it allows Network Access to focus on the strategic objective of improving train scheduling and the use of the network, rather than being pre-occupied with the day-to-day movement of trains;
- it reduces the likelihood of significant impacts on communication effectiveness and the time responsiveness of QR resulting from the creation of another interface between train control and QR's above-rail business groups as a consequence of shifting day-to-day performance of scheduling and train control to Network Access;
- as third-party operators' train movements currently account for a small fraction of the total train movements over QR's network, QR considers it unnecessary to implement a costly organisational restructure when these train movements can be managed through the development of scheduling and train control protocols; and
- there is no clear evidence that an organisational restructure along the lines of Option C will lead to any substantive benefits to warrant the net cost and risk involved.

QR acknowledged that Option C has the advantage of minimising the perception amongst third-party operators that QR has the opportunity to advantage its above-rail business groups in providing scheduling and train control services. However, in its view, Option C would involve increased costs in service provision with potential implications for operational performance and safety. QR believed that, with effective management, the advantages of Option C could be gained through the adoption of Option A without incurring the same level of costs and at a lower risk to the operational performance of rail services.

QR was reluctant to move to Option B as it believed that it would result in an increase in costs and risks to the organisation, without the advantages of the improved alignment of functions and responsibilities that come from Option C.

**Capacity management** - QR argued in its initial submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* that it had separated the performance of the function of network capacity management from the performance of the scheduling and train control function. However, importantly, ultimate responsibility for both functions was with Network Access. QR subsequently advised the QCA that officers from its above-rail business groups not involved in commercial arrangements could still become involved in the capacity assessment process.

**Conflict of interest** - QR argued in its supplementary submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* that the perceived risk its above-rail business groups may manage day-to-day train conflicts in a way favouring its own trains could be managed through:

- the development of clear protocols governing the way in which day-to-day train conflicts are resolved;
- the requirement for regular reporting;
- the availability of records which will identify any instances where such protocols are breached; and
- the requirement for periodic auditing of the performance of such responsibilities.

**Third-party protection** - in August 2000, QR provided the QCA with a paper 'Why train control should remain as a contracted service provided to Network Access Group by the Above-rail Groups' in further support of its position. Amongst other things, the report outlined the following measures QR had taken to provide reassurance to third-party operators that the train control function would be performed in a non-discriminatory manner:

- an option for each operator to have a liaison officer located in train control centres in order to have on-the-spot input into any decisions affecting their trains;
- visitation rights to train control centres for operators' observers;
- access to replay tapes to view any decision made in regard to their trains, which would include train movement event recorders and train control voice tapes. Impartiality of train controllers' actions would be subject to review with replays; and
- weekly and monthly management reports for individual rail operators to allow them to monitor their train operations, which would include train control event recorders and train control voice tapes.

QR also offered that if after two years of its proposed assignment of management responsibility for train control an advantage had been conferred on QR by retaining day-to-day management of the train control function with its above-rail business groups, then it would restructure according to the QCA's requirements.

**Safety** - QR's August 2000 paper also focussed on rail safety matters. It argued that changing working railway arrangements that have 135 years of entrenched focus of safety and performance to meet appearance perceptions could destroy core competencies and would be detrimental to the long-term health of the organisation. Accordingly, customers, shareholders and stakeholders would suffer.

To illustrate its point, QR focussed on circumstances in NSW, where it argued a breakdown in communication and poor interfaces between the various railway groups had resulted in a significant reduction in operating and customer service performance, but probably more importantly, a breakdown in safety management. This was an argument for keeping train control as a contracted service provided to Network Access by the above-rail business groups. Notwithstanding its criticism of the safety performance of the NSW arrangements, QR supported NSW's decision to maintain the train control function within State Rail Authority, an above-rail operator, to be performed on a contractual basis for RAC, the track manager.

QR's raised the following general themes about the rail safety situation in NSW:

- when railways lose their safety culture and focus as a result of structural separation, divided responsibility and confusion, the safety implications are enormous;
- the long-term disintegration of basic operating and safety standards is detrimental to the quality of service and safety standards expected, and demanded, by customers; and
- safety should not be compromised, nor should service quality, just for appearance's sake.

QR argued that the deterioration in safety performance in NSW since 1995-96 could be seen in an increase in the following indicators:

- passenger deaths;
- passenger assaults;
- public deaths;
- employee deaths;
- mainline derailments; and
- mainline signals passed at danger.

*Train control reassignment costs*

QR wrote to the QCA on 28 September 2000 advising of its initial estimate of the long-term cost of reassigning its train control function to Network Access. The initial estimate was \$7.5 million per year, excluding the once-off costs associated with the implementation of the change. QR indicated that such costs included change management, communication, retraining, risk assessments, safety validations, and movement of personnel and equipment. Cost increases would be incurred by both the above and below-rail elements of QR's business.

QR outlined its methodology for this assessment as follows:

- detailed assessment of the current work practices and current roles of personnel within each work area;
- identification of additional positions that would be required in each area if the above and below-rail activities were separately performed;
- assessment of the additional costs (including labour, consumables and on-costs) of the additional positions identified above;
- identification of changes in other costs (such as accommodation); and
- comparison with existing total costs and existing cost allocations for above and below-rail activities used in the development of internal trading charges between Network Access and the relevant above-rail business group.

QR estimated the costs as follows:

- Coal and Mainline Freight operations - \$5,854,000

- Metropolitan and Regional Services operations- \$493,000
- Brisbane suburban operations - \$1,158,000

#### *Changes in QR's organisational structure since lodgement of Draft Undertaking*

Since lodging its Draft Undertaking with the QCA, QR has advised the Authority of a change in its approach to capacity management on its network.<sup>21</sup> QR has established a Network Train Planning Centre (Network Planning Centre) within Network Access. According to QR, the Network Planning Centre provides Network Access with the resources it requires to assess and identify capacity, produce a schedule for a rail operator and develop a master train plan concerning all operators on QR's network independently of QR's above-rail business groups.

With the introduction of the Network Planning Centre, it is no longer necessary for Network Access to seek the assistance of any segment of QR's above-rail business groups in assessing capacity or scheduling train services onto the master train plan.

#### *Other relevant changes since lodgement of Draft Undertaking*

Notwithstanding the commitment in the Draft Undertaking to develop Protocols within three months of the approval of the Undertaking, QR provided a copy of the Protocols to the QCA on 23 December 1999. In February 2000, the Authority released a Request for Comments Paper *QR's Scheduling and Train Control Protocols and Proposed Assignment of Marshalling Yards*. QR prepared two submissions in response to the QCA's paper.

#### *QCA's role in approving changes to QR's organisational structure*

In both its submissions to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*, QR argued that it did not believe there is a legal basis for the QCA to require a change in QR's organisational structure as a pre-condition to approving QR's Draft Undertaking. This was because ss137(2) of the QCA Act, regarding contents of undertakings, is focussed on organisational processes and procedures and does not extend to changes to organisational structure.

In QR's view, the movement of the performance of the scheduling and train control functions from within the scope of action of QR's above-rail business groups to within Network Access' scope of action would be a change in its organisational structure.

QR argued that the proposed twelve month review of an approved Undertaking should adequately provide for an evaluation of QR's ability to provide an effective and fair train control service. Alternatively, the proposed three year term of the Undertaking could also provide an opportunity to review this matter.

#### ***Stakeholder Comment***

The QCA has formally sought stakeholder comment regarding the performance of the train control function on two occasions.

First, in response to the Request for Comments Paper *Queensland Rail Draft Undertaking*. A majority of submissions considered that the allocation of responsibility for train control to QR's above-rail business groups was inappropriate.

**Table 1: Performance of train control function by QR's above-rail business groups**

**FreightCorp** - we have had extensive experience operating in an environment where train control is effectively owned and operated by another rail operator. The application of train control decisions are often subtle and can substantially impact on service levels without providing sufficient evidence to bring a case of hindrance such as might be contemplated under Part 5, Division 5 of the QCA Act.

FreightCorp agrees with QR that stakeholders are basing their concerns on perception that the train control structure will not work. However, what QR fails to note is that perception is reality in the minds of its (potential) customers. FreightCorp can attest to its unwillingness to invest in rollingstock to enable us to compete against QR until we have the assurances we seek regarding the delivery of unbiased train scheduling and train control. Such is the strength of perception, that one might regard it as a most powerful barrier to entry.

QR's suggestion that the separation of train control into Network Access would create an additional safety risk that would translate into a safety risk, is a most unfortunate argument that has no basis in fact. We consider safety as unrelated to the organisational structure in so far as the creation of an additional interface is concerned. QR itself argued in its supplementary submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* that each of its identified options for train control can be implemented effectively.

**QMC** - the management of any facility or service capable of conferring advantage on QR as a rail operator should ultimately rest with Network Access.

**National Rail** - all functions that are open to access by third parties should be included within Network Access. If the train control and scheduling functions are included in the above-rail component of the business, which competes with access seekers, the probability of breaches of ring-fencing arrangements will be greatly increased.

**Queensland Government** - the assignment of functions within the organisation should, prima facie, be a matter for the owner or QR Board. However, the QCA should closely monitor the effectiveness of QR's train control protocols in addressing any bias toward QR, or institute arrangements that it considers appropriate to address any potential for conflict of interest. Where organisational structure may give rise to a potential for a conflict of interest, it is necessary for the QCA to consider arrangements to separate the owner's operations concerning the service from other commercial operations of the owner.

**Agforce** - it would seem to be more efficient for access to all below-rail services to be controlled by Network Access as this would reduce possible impediments to third-party operators.

**AMC** - it is inappropriate that train control be undertaken by the above-rail business groups and this seriously jeopardises the effectiveness of the Draft Undertaking. Train control should be performed independently so that third-party operators are on equal terms with QR's above-rail business groups.

**Toll** - the train control function is a vital operational function providing significant scope for prioritising one rail operator's trains over another. If an above-rail unit has the train control function, there is a risk of internal QR trains being preferred over those of third-party operators. The train control function should be directly managed by Network Access and train control protocols should form part of the standard access agreement reflected in Schedule E to the Draft Undertaking.

**Stanwell** - placing train control with the above-rail business groups is totally inappropriate. It does not provide the level of certainty or confidence in the Undertaking that is required for effective third-party access. The train control function clearly should either be totally controlled and staffed by QR or preferably by a separate independent organisation.

<sup>21</sup> See QR's *Submission responding to QCA's Issues Paper on QR's Scheduling and Train Control Protocols* released in February 2000.

**ARTC** – QR’s primary argument for retaining the train control function in the respective business units is cost (minimal organisational change) and operational risk (better coordination of above and below rail activity by train control) related. ARTC considers these arguments to be internally focussed.

Firstly, whilst any organisational transfer involves some cost, it is possible that the ‘centralisation’ of this function may bring about some synergies of its own (board rationalisation/sharing). Any net cost may be considered by the industry as reasonable given the benefits. Many other previously integrated railways have either separated vertically, or at least have quarantined the train management function from the business despite initial cost impacts.

Secondly, and with regard to QR’s desire to have train control coordinate both below and above rail resourcing, ARTC’s experience is that operators prefer to do their own above rail decision making, leaving train control with the focus of train and safety management only. In fact, leaving decisions regarding usage of resources owned or hired by a third party operator (apart from normally contracted train management) in the hands of the network manager opens up that organisation to additional operational (and maybe financial) risk. In other words, having train control perform both above and below rail functions, may provide some economies to QR but is opposed to the way third party access currently works.

**RTBU** - QR’s assignment of responsibility is supported because there should be a seamless link between train control and train crews on safety grounds.

Second, in response to the Request for Comments Paper *QR’s Scheduling and Train Control Protocols and Proposed Assignment of Marshalling Yards*. Submissions commented both on the appropriateness of QR’s above-rail business groups performing the train control function and whether the Protocols adequately addressed the inherent conflict of interest. All submissions expressed concerns on both these fronts.

**Table 2: Performance of train control function by QR’s above-rail business groups**

**QMC** - Network Access should assume functional management of daily scheduling and train control as soon as practicable as they are core functions of any rail network provider in a non-discriminatory access environment. The practical concerns raised by Network Access as a cause for delaying their assumption of responsibility for daily train control and scheduling are not accepted for the following reasons:

- the daily train control and scheduling function is inextricably bound up with system utilisation and cannot be separated from it. QR Coal and Mainline Freight would not be motivated to improve train control effectiveness in the interests of network efficiency and system utilisation would suffer as a result;
- an increase in overall staff costs is not a valid reason for retaining the status quo. The implementation of effective access arrangements will involve new costs that will be outweighed by the benefits in terms of improved performance and lower costs to users; and
- it reflects a pre-occupation on Network Access’ part with the convenience of the above-rail business groups. This shows an essentially anti-access and pro status quo mindset on the part of Network Access.

**Toll** - the Protocols did not adequately address the conflict of interest inherent in QR’s above-rail business groups performing the train control function. This function must be under the direct control and management of Network Access. QR’s proposal is akin to allowing airline operators to have ‘real time’ control of their own and others’ flight paths rather than Air Traffic Control.

**FreightCorp** - there are no safeguards to provide comfort that the operation of the proposed Protocols will not be subverted at the detail level such that a third-party operator is continually disadvantaged. The Protocols fail to provide any mechanism for remedial action, immediate dispute resolution or even for hearing complaints.

No train operator is going to be willing to compete with QR unless it has demonstrable processes that would ensure the delivery of efficient, fair and unbiased train scheduling and

train control services. Such processes need to go far beyond an ability to take QR to court for hindrance. The operator will be out of business by the time such a remedy could be fought and effected and the difficulty in proving acts of sabotage at the detail level make such remedies impotent except for the most blatant examples. We would require very specific performance outcomes, remedies and procedures that gave us confidence that, not only did we receive the service expected, but that very real and immediate remedies were available in the case that we believed we had not received that service.

**Stanwell** - scheduling and train control are important functions in the operation of a rail network. These functions should be undertaken by an independent entity, clearly separated from QR's above-rail business groups. This is critical for the establishment of an appropriate third-party access regime for the following reasons:

- as QR's above-rail business groups will be simultaneously controlling their own and competing third-party operator's traffic, there are significant conflicts of interest;
- the proposed Draft Undertaking, Protocols and associated plans will not necessarily facilitate a commercially sound outcome. Given the discretion held by QR train controllers in the day to day scheduling and control of the rail network, the Protocols and Access Plans do not appear to be able to deal with potential issues relating to conflicts of interest, accountability and transparency;
- it is necessary to address rail customer concerns. This is a critical step to enable rail users to realise benefits associated with effective competition;
- any cost savings of an integrated structure would be far outweighed by the benefits to the establishment of a dynamic and healthy Queensland rail market; and
- information asymmetry will be a major obstacle for third-party operators as QR's above-rail business groups, as the incumbent operator, will have a better understanding of the below-rail network and likelihood of disruptions. Third-party operators would therefore be less prepared to respond to unplanned disruptions which could potentially affect haulage service quality.

The experience to date with ARTC and RAC suggests that the assignment of the train control function to an independent entity may be successfully implemented.

**Queensland Transport** - it was not desirable for train control functions to be allocated to above-rail business groups. However, there may be genuine management benefits in such an arrangement. Should above-rail business groups continue to have train control responsibilities, the need for rigorous train control protocols and transparency would be significantly increased.

**ARTC** - QR's proposal to perform the scheduling and train control functions within a framework established by the Undertaking, the Protocols, Interface Plan and Access Plan goes some way to mitigating the risk to third-party operators of QR's proposed allocation of train control within its vertically integrated structure. However, there are still sufficient 'grey' areas in many of the guidelines to enable the business groups to inconspicuously gain a competitive advantage. Many of the principles and guidelines incorporated in the Protocols and plans are worthwhile and would provide a very sound management process if these functions were carried out by a wholly below-rail entity. However, from a competitive neutrality viewpoint, a better outcome would be achieved if there was no direct commercial relationship between scheduling and train control functions and QR's above-rail business groups - this would instil greater confidence regarding access to the network in both incumbent third-party operators and new entrants. The benefits of the ensuing growth would flow to Network Access, and could far outweigh the up-front organisational expenditure needed. Moreover, the reasons provided by QR for not altering its organisational structure, namely cost and coordination, are internally focussed. It is not clear what incentive QR would have to alter its organisational structure if it is - or is seen to be - stifling competition on its network.

Submissions in response to the QCA's Request for Comments Paper *QR's Scheduling and Train Control Protocols and Proposed Assignment of Marshalling Yards* also commented on the performance of the scheduling function by the above-rail business groups. These comments were made prior to QR's decision to establish the Network Planning Centre to develop the master train plan.

**Table 3: Performance of scheduling function by QR’s above-rail business groups**

**Toll** - it is entirely inappropriate that officers from QR’s above-rail business groups be involved in the assessment of available capacity for third-party operators, as this is a matter for independent and impartial assessment by Network Access. Would QR’s above-rail business groups accept review of their capacity entitlements by third-party operators?

**Queensland Transport** - as a general rule, it would be desirable that QR’s above-rail business groups not be involved in the assessment of available capacity - these business groups should be treated like any other rail operator. QR intends to develop internal access agreements in respect of all existing QR train services. Once these agreements are established, available capacity could be determined solely by Network Access, based on the requirement of above-rail operators and infrastructure capacity issues.

**Stanwell** - QR’s proposal for its above-rail business groups to prepare and implement the daily train plan is not supported for the following reasons:

- there are inadequate safeguards to address conflict of interest concerns;
- there is no avenue for third-party operators to have input into this process; and
- there is an insufficient level of transparency under QR’s proposed approach to provide assurance that train path allocations are made in a competitively neutral manner.

**Toll** - it was ridiculous for QR to allow the daily train plan to be formulated by the above-rail business groups as this is entirely a matter for Network Access. To allow QR above-rail business groups to ‘fiddle’ with the train plans on a daily basis will not only cause confusion, it will also create potentially significant safety issues. Under QR’s proposed approach, how would the above-rail business groups coordinate their decision making process and how would they communicate with other rail operators and ensure they received safe, consistent and impartial decisions? QR’s proposed system is chaotic. The above-rail business groups should have no role to play in amending the daily train plans and all communication concerning desired amendments should be through Network Access who should decide whether any change is justified.

All stakeholder submissions considered that the QCA should approve any changes to QR’s organisational structure. However, different views were expressed as to how this should be achieved.

**Table 4: QCA’s role in approving changes to QR’s organisational structure**

**FreightCorp** - the QCA Act provides the QCA with the necessary powers to approve changes to QR’s structure.

**QMC** - to the extent there is uncertainty regarding the QCA’s legislative powers, the means for giving effect to the QCA’s deterministic role in regard to amending undertakings should be provided for in the initial Undertaking.

**AMC, Stanwell, Toll** - the issue of organisational restructures and draft amending undertakings should be addressed in the initial Undertaking.

**Queensland Government** - the Undertaking should clarify the powers of the QCA in this situation.

### *QCA’s Analysis*

Network Access, as network manager, is heavily reliant on internal service providers to perform its functions, in particular, for infrastructure maintenance and construction, train control, technical and safety services. From a ring-fencing perspective, the QCA would prefer that Network Access was less reliant on internal service providers. The QCA’s preference reflects its concern that, where other parts of QR are required to advise and/or perform functions on behalf of Network Access, the potential for conflicts of interest is magnified and/or it becomes

harder to control the flow of access seekers' confidential information within QR. This necessitates a more significant regulatory burden being imposed on QR.

The QCA considers that major sensitivities raised by QR's organisational structure relate to the assignment of management responsibility for:

- short-term scheduling and train control functions;
- marshalling yards; and
- stations and platforms.<sup>22</sup>

In addition, the respective roles of the following groups within QR's organisational structure warrant consideration:

- Technical Services Group;
- Infrastructure Services Group;
- Deputy Chief Executive's Group; and
- the Safety Executive.

#### *QR's assignment of management responsibility for scheduling and train control functions*

Network Access' role within QR, a Government Owned Corporation with a commercial charter, is the creation and sale of capacity on QR's network. The development of a train schedule is the means by which a rail network's capacity, defined in terms of train paths, is allocated. The performance of the train control function is the execution of the train schedule in real time and is itself contained within the declaration of QR's rail transport infrastructure.

In this context, the QCA believes that scheduling and train control unequivocally should be a core function of Network Access and not one that is contracted out to one of QR's above-rail business groups. A majority of stakeholders concurred with this view. Moreover, it is essentially a natural monopoly function within a specified rail network. In principle, such a function should be assigned to the rail manager, Network Access.

QR's decision to establish a Network Planning Centre (NPC) within Network Access is supported by the QCA. The QCA was concerned that, prior to the establishment of the NPC, QR's above-rail business groups could have become involved in assessing the amount of capacity that was available to their competitors and thus have early warning about competitors' proposed operational arrangements and relationships with, in general, QR's existing customers. 'Signalling' behaviour has proven to be a major anti-competitive influence in other sectors, such as telecommunications and electricity, with a corresponding adverse effect on the competitiveness of emerging markets.

Nevertheless, the NPC's role will only be to develop the long-term schedule - the master train plan. Once completed, QR proposes that the master train plan will continue to be provided to QR's above-rail business groups to develop the short-term schedules – the daily train plans – and they would subsequently execute the daily train plans through the performance of the train control function.

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<sup>22</sup> The implications of QR's assignment of management responsibility for marshalling yards and stations and platforms are discussed in Chapter 4.

Notwithstanding the QCA's support for the development of the master train plan being brought solely within Network Access' responsibilities, the Authority has outlined below what it considers to be a number of problems posed by QR's above-rail business groups performing the short-term scheduling and train control functions.

**Conflict of interest** - there is a clear conflict of interest in QR's above-rail business groups performing train control and scheduling functions as they will be simultaneously controlling their own and competing third-party traffic. This places these business groups in a position to advantage their own traffic over third-party operators. For example, by giving QR trains priority over those of its competitors, QR would confer upon itself a significant competitive advantage.

When trains are running in accordance with scheduled times, the train controller's task is to implement the daily train plan. However, train controllers regularly will be required to use their discretion to change the daily train plan in response to above-rail operators not adhering to sectional running times or to unforeseen events, such as derailments or track flooding. In this regard, it is evident that the conflict of interest faced by QR's above-rail business groups in performing the train control function poses particular difficulties. Every time a third-party operator runs train services on QR's network, it is effectively placing control of one of its key strategic assets – its rollingstock – in the hands of its competitor. QR's train control centres will be making decisions that affect the quality of the service that a third-party operator can deliver to its customer(s).

QR argued that a third-party operator's capacity entitlement will be specified in its access agreement with QR. Consequently, QR has an incentive to ensure even-handed provision of train control services to all operators on its network to avoid the legal consequences of breaching an agreement. However, in practice, it could be extremely difficult to definitively prove favouritism in a train controller's decision-making. Third-party operators are particularly exposed to the risk of competitive disadvantage through the accumulation of numerous minor favourable train control decisions being extended to QR's above-rail business groups.

The QCA is also concerned that, because of QR's strong corporate culture, it is likely that train controllers strongly identify with the above-rail business groups for which they work. The entry of new rail operators onto the network, which pose a threat to these business groups, could be viewed negatively. The QCA has received anecdotal evidence from a vertically integrated rail service provider in another jurisdiction confirming this likelihood.

**Performance monitoring of the train control function** - given the conflict of interest inherent in QR's proposed train control arrangements, there is a very important need to monitor the performance of this function. However, the performance of train control is difficult to monitor, even if the data is available. This is because the train-control process can involve split second decisions on matters that arise from events that occurred hours or even days beforehand.

The QCA recognises that train controllers often have to make decisions without the benefit of a full-scale simulation to guide their routing or priority decisions and consequently can make coordination mistakes. In this regard, decisions that adversely affect a third-party operator's train service may not have a malicious intent. However, that perception will persist while the train control function is assigned to the above-rail business groups.

**Efficiency of the scheduling process** - QR's argument that ultimate responsibility for scheduling and train control lies with Network Access overlooks the reality that it will be very difficult for it to adequately perform that function when day-to-day scheduling and train control is driven by the above-rail business groups. The day-to-day functioning will significantly influence the master train plan and the scheduling and train control protocols.

One of the major benefits of third-party access is the enhanced focus it potentially provides to QR's capacity management. Contrary to QR's argument that Network Access will be able to focus on the strategic objective of improving capacity management rather than being pre-occupied with day-to-day train movements, this objective may be compromised by assigning the responsibility for certain train control functions with its above-rail business groups. This is because these groups have a relatively limited incentive to improve the efficiency of the capacity allocation/management process, as this would facilitate the entry of potential competitors onto the network. Indeed, the QCA is puzzled by QR's concern that Network Access could become preoccupied with day-to-day train movements, because such movements are an integral part of a network manager's core business activities and ultimately its performance.

Furthermore, most Australian railways now see train control as the management and utilisation of the rail infrastructure, rather than just making sure the trains run smoothly or incidents are responded to. This suggests that the train control function should be aligned with the capacity management function within Network Access.

**Confidentiality** - another major concern with locating responsibility for day-to-day train control with QR's above-rail business groups is the potential for third-party operators' confidential information, including operational details of their service, to be conveyed to their potential competitors in these business groups. Railway managers in other jurisdictions, ARTC and RAC, have found that rail operators guard details of their train performance as closely as sensitive financial information, fearing that it could be used against them in the market. For example, a rail operator may use train performance data to indicate to potential customers that a competitor's services are unreliable. ARTC and RAC have both included confidentiality clauses in their agreements relating to train-performance information.

QR's Ring-fencing Guidelines are intended to limit the potential for inappropriate information flows to occur. However, the history of ring-fencing in other jurisdictions has highlighted the risk that the culture within QR's above-rail business groups, derived from its vertically integrated structure, could overwhelm the intent of the Ring-fencing Guidelines. Assigning train control to Network Access would facilitate a below-rail culture emerging in that business group.

**Organisational restructuring** - the QCA believes QR's argument that it is unnecessary to implement a costly organisational restructure because there are only a few third-party operators currently using its network ignores the importance of establishing an appropriate below-rail market structure prior to, or at least very early in, the development of the Queensland above-rail market. The assignment of management responsibility for the scheduling and train control functions is a key element of the below-rail market structure.

It is not possible to estimate exactly how many third-party operators will enter the Queensland above-rail market. However, in the QCA's view, the key issue is establishing a below-rail structure that does not distort the development of the above-rail market by raising barriers to third-party entry. The below-rail market should be such as to allow all rail operators to investigate and pursue profitable opportunities in the above-rail market.

However, the number of third-party operators that actually enter the market is not the key consideration. Rather, the major concern is to ensure an environment is created where vigorous rivalry determines above-rail charges. The QCA estimates that the above-rail component of rail-haulage charges is at least 50%, and in the absence of competition from road transport, the only constraint on the level of that above-rail charge is the competitive environment amongst

rail operators. The functional assignment of train control potentially substantially influences the emergence of this vigorous rivalry in the above-rail market and consequently the level of above-rail charges.<sup>23</sup>

Indeed, the essence of QR's justification for the retention of short-term scheduling and train control with its above-rail business groups is that these groups should be able to maintain a significant competitive advantage in a third-party access environment. Inevitably, and despite the absence of any overt intention to provide their own operations with an advantage, QR's above-rail business groups will have every incentive to organise below-rail schedules to suit above-rail priorities, such as crewing, locomotive availability and so on. That is, the below-rail function, which should be competitively neutral, could be subordinated to QR's above-rail business priorities regardless of whether the individuals performing the task intend it or not. However, such an outcome is clearly the antithesis of the environment third-party access is intended to engender.

**Review of train control arrangements** - QR has argued that it does not believe the terms of the QCA Act enable the QCA to examine the issue of structural change to QR in deciding whether or not to approve a Draft Undertaking. In contrast, the QCA understands that the QCA Act allows the Authority to examine the issue of structural change to QR in deciding whether or not to approve a Draft Undertaking. The train control service was covered in the rail-transportation declaration under Part 5 of the QCA Act.

Notwithstanding this difference in views, the QCA is concerned about QR's argument that the proposed 12 month review of an approved Undertaking should adequately provide for an evaluation of QR's ability to provide an effective and fair train control service. Any changes flowing from such a review would be at QR's discretion, because the QCA would not be able to impose a change in the allocation of the train control function at that time.

QR's suggestion that it would reassign train control to Network Access after two years if an advantage had been conferred on QR from its above-rail business groups performing the task would be too late for third-party operators that gain access to QR's network in that period and experience problems in the performance of the train control function. While such third-party operators would have recourse to arbitration under the QCA Act, the QCA believes that this would be an unnecessarily time consuming and expensive way of resolving a matter that could be addressed as part of the approval of the Undertaking.

**Effectiveness of the Protocols** - QR argued that the Protocols would govern the performance of the scheduling, train control and associated incident management services by the above-rail business groups and address the perceived risk that these business groups could manage day-to-day train conflicts in a way favouring QR's train services.

In February 2000, following receipt of the Protocols, the QCA released a Request for Comments Paper *QR's Scheduling and Train Control Protocols and Proposed Assignment of Marshalling Yards* that sought stakeholders' views on whether the Protocols met the objectives set by QR. The strong, unanimous view of stakeholders was that the Protocols did not achieve the objectives set by QR, including adequately addressing the conflicts of interest faced by the above-rail business groups. The Protocols are discussed in Chapter 6.

All of the issues discussed above highlight the potential for the effectiveness of the access arrangements to be brought into question because QR's above-rail business groups are proposed to perform the short-term scheduling and train control functions. By undermining confidence in

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<sup>23</sup> The size of the Stanwell consortium tender and the projected growth in coal and minerals tonnages – discussed in Chapter 5 - suggest that potentially large third-party entry could develop in Queensland.

the integrity of the access regime, both in terms of third-party operators' perceptions of the likelihood of receiving competitively neutral treatment and receiving protection for their confidential information, this has the potential to serve as a barrier to entry.

*QCA's proposed re-focussing of QR's train control centres*

The QCA believes that QR's argument for assignment of the train control function to its above-rail business groups is heavily based on the purported efficiency gains from its integrated structure. Consequently, the QCA regards the costs - including the loss of the efficiency gains - associated with reassigning the function to Network Access to be an important factor in determining its position on the assignment of short-term scheduling and train control responsibility. These costs can then be compared with the benefits of potential or actual competition in the above-rail market, reflected in lower prices to end-users. The QCA also believes that third-party operators and customers are interested in such details, as they ultimately would have to bear the costs of reassignment if it were to proceed. QR's costing estimates are discussed in the next section of this chapter.

Table 5 (below) outlines the key services performed by QR's train control centres.<sup>24</sup> The QCA has separated these services into those of an above and those of a below-rail nature. The below-rail services are core train control services that would need to be performed by train controllers regardless of QR's organisational structure and the assignment of functions within that structure. The above-rail services reflect the extent to which QR has integrated the train control centres into its above-rail business groups.

**Table 5 Functions of QR's train control centres**

Below-rail	Above-rail
<p><b>Short-term train scheduling</b></p> <p>Short-term schedules are prepared 24 to 48 hours in advance by planning officers in the respective above-rail business groups. Network Access does not have any input into these schedules beyond preparation of the master train plan.</p>	<p><b>Coordinating train crew change-overs</b></p> <p>Ensuring that the rostered train crews make their scheduled change-overs and do not work beyond the length of their shift.</p> <p>If train-running times depart from the schedules, train controllers must use their discretion to effect the crew change-over at the most convenient revised time and location.</p>
<p><b>On-track train/traffic management</b></p> <p>QR's train control centres manage traffic movements in real time utilising the short-term schedules, however, train controllers use their discretion to change these plans in response to unforeseen events eg unloading delays at a port, a train derailment.</p>	<p><b>Coordinating the marshalling of rollingstock</b></p> <p>Ensuring that the wagons and locomotives of QR's above-rail business groups are available when and where they are needed.</p>

<sup>24</sup> QR has five train control centres located in Brisbane (Mayne and Central), Rockhampton, Mackay, and Townsville. The structure (and number of personnel) of each train control centre varies somewhat. This appears to be driven by the nature and volume of the train traffic each centre is responsible for managing and resource decisions within QR.

Below-rail	Above-rail
<p><b>Electrical control coordination</b></p> <p>Management of the electricity overhead system on the electrified parts of QR's network, including ensuring that there are no electricity overloads on track sections and coordinating maintenance work on the electrical system.</p>	<p><b>Coordinating the accumulation of loads for general freight trains</b></p> <p>Ensuring that that small consignments of general freight from different locations are consolidated in a particular location for transport to a different location.</p>
<p><b>Rollingstock defect coordination</b></p> <p>Facilitating the removal of traffic blockages in the event of locomotive break-downs (but not accidents).</p>	<p><b>Station security</b></p> <p>Non-business hours video surveillance at Brisbane metropolitan train stations.</p>

QR has advised the QCA that the performance of above-rail tasks by train controllers is greater in non-business hours than during business hours. This is as a result of the train control centres operating 24 hours a day, with train control staff working under a three-shift roster system, whereas the majority of staff in the above-rail business groups work standard business hours. Hence, certain tasks performed by above-rail business groups during standard business hours are handed over to the train control centres to be managed overnight.

QR has advised the QCA that crewing is a more difficult issue for its coal and minerals trains than for the metropolitan passenger trains because there is both considerably more variation in train-running times and longer train journeys. Nevertheless, from the QCA's perspective, train crewing is fundamentally an above-rail task and critical to the performance of the above-rail business groups. In contrast, such a task has no relevance to the on-track traffic-management task of the train control centre.

QR has implicitly recognised this in its Brisbane Mayne and Mackay train control centres. The QCA understands that, as a result of the heavy traffic flows on the Goonyella coal and Brisbane metropolitan systems and hence the demanding nature of the train control task, certain train controllers in these operational centres are dedicated to traffic management tasks and do not perform any crewing tasks.

QR probably gains some cost savings from piggy backing the crewing function onto the core tasks of its train controllers, subject to traffic flows not being too heavy. The flexibility gained by train controllers working on a 24 hour roster system also allows crewing tasks to be performed by these staff outside of standard business hours. If train control were to be assigned to Network Access, QR's above-rail business groups would be responsible for undertaking the crewing task from inception to implementation, liaising with the train control centres regarding the scheduling of its crew change-overs.

This would place the above-rail business groups in exactly the same situation as third-party operators. The coordination within QR would be broadly the same, except that the train controllers would be reporting to a different manager than the above-rail business groups, whereas currently both report to the same manager. In addition, this would likely require greater flexibility in the staffing arrangements of the above-rail business groups, although the QCA understands that certain staff from these groups already work shifts.

The collection and dissemination of information on wagon/locomotive availability and freight consolidation is a function of the quality of QR's communications systems. Improvements in information technology are expanding the quality and quantity of information available to

network owners and above-rail operators concerning real-time reporting of freight and rollingstock movements. For example, there are now communications systems, such as RAMS (Rail Access Management System), that allow rail operators to directly access information on trains, rollingstock, containers and incidents on a confidential-user basis, as well as allowing for billing of track users. The QCA considers that the use of such communications systems has the potential to improve co-ordination between a network manager and multiple rail operators using its network.<sup>25</sup> Moreover, as a result of the increasing use of sophisticated communications systems, the efficiency gains from integrating the train control and above-rail functions are correspondingly reduced.

The QCA considers that QR's rollingstock marshalling and freight consolidation functions are clearly important determinants of the overall performance of QR's above-rail business groups. In the context of third-party entry on QR's network, the QCA does not believe that QR's train control centres should be taking prime responsibility for managing these tasks. As with the crewing task, it is difficult to see QR's train control centres developing an organisational culture consistent with a track manager handling multiple rail operators when its staff perform critical tasks for QR's above-rail business groups.

*QCA's proposed reassignment of operational responsibility for scheduling and train control functions*

The QCA requested that QR provide information on the scope of staff movements and associated costs involved in separating the core train control functions from the above-rail tasks and reassigning the core train control function to Network Access at all QR's train control centres.

QR's response to this request was outlined in the statement of QR's position above. For its coal operations, the cost is approximately \$2.9m out of QR's reassignment figure for the whole of Coal and Mainline Freight of \$5.8m. This represents a 20% increase in the current cost of performing the short-term scheduling, real-time train control and incident-management functions at the train control centres.

Such a high cost implies that reassignment at all of QR's train control centres in the coal network entails significant efficiency losses for both Network Access and Coal and Mainline Freight.

The QCA has a number of concerns with the underlying assumptions made by QR in estimating the reassignment costs in that the data concerning the number of personnel required in the new group structures was made on the basis of a 'zero-base' assessment of their respective needs. Such an assessment assumes the new group structures are built from the 'ground up' and as a result:

- ignores the existence of any other business groups within QR, assuming the new above-rail business groups and Network Access are self-sufficient;
- attempts to replicate the performance of the functions of the host business groups (the above-rail groups with train control and Network Access without train control). This fails

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<sup>25</sup> QR's Coal and Mainline Freight group has a mainframe-based information-management system (called the Freight Management System (FMS)) that allows coal customers to track where on a corridor the train carrying their product is located and the estimated time of arrival at the journey's end point. The FMS is discussed in more detail in section 3.4 of this chapter in the context of third-party operators accessing confidential operational information.

to take into account the change of focus of the new business groups and their integration with the host business groups;<sup>26</sup> and

- ignores the interaction of individuals within these group structures. This results in a tendency to exaggerate the required resources of the two new groups.

Overall, the QCA considers that it is unreasonable to assume the new business group structures will not achieve some level of internal economies. Indeed, QR's own analysis reveals that in some train control locations the number of personnel required for below-rail functions decreases from that required under the old group structures, especially with the adoption of the universal train control system. This result brings into doubt the robustness of the zero-based assessment of the reassignment cost.

If train control were to remain with QR's above-rail business groups, issues would arise concerning:

- a reduction in Network Access' costs arising from the stand-alone cost of service provision currently allowed being overstated due to it contracting the above-rail business groups to perform the scheduling and train control function;<sup>27</sup> and
- adjustments being necessary to maintain competitive neutrality between QR's above-rail business groups and third-party operators. For example, it may be necessary to take account of the above-rail economies QR argues arise from vertical integration. QR has argued that diseconomies of scale as a result of Coal and Mainline Freight reassigning the train control function are approximately 20%.

The QCA has concerns with the large differences in the implied above-rail train control diseconomies of scale across QR's business groups, ranging from 5% for Metropolitan and Regional Services to 20% for Coal and Mainline Freight. While differences between business groups could be expected given the varying nature of their operations, the magnitude of such a difference is surprising. Whilst the Authority accepts that there are costs associated with the integration of train control in Network Access, it has assessed those costs as being relatively low. In the case of QR's coal services, these costs are estimated at below 0.1% of the total revenue earned by its coal operations.<sup>28</sup> Furthermore, the Authority expects that these costs are likely to fall over time as new economies emerge from the integration of the entire scheduling and train control function within Network Access.

In light of strong stakeholder concerns about potential conflicts of interest and what would appear to be relatively small reassignment costs, the QCA believes that Network Access should perform the core scheduling and train control function at Brisbane Central, Mackay, Rockhampton and Townsville train control centres. The one exception is Brisbane Mayne train control centre, which is part of QR's Citytrain urban passenger operations.

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<sup>26</sup> The QCA recognises that QR would need to make a conscious effort to more closely align the reassigned functions with their host business groups, including some restructuring and re-skilling of the workforce.

<sup>27</sup> The QCA has endorsed QR's estimate of the stand-alone cost of providing the train control function on the coal network in the context of the development of reference tariffs.

<sup>28</sup> This figure takes the QCA's \$2.9m stand-alone cost estimate of the coal portion of the train control function on the coal network, which reflects QR's assumption of 20% diseconomies due to reassignment, and instead uses the Authority's assumption of 5% diseconomies due to reassignment. The 5% figure reflects an adjustment for the extreme assumptions the QCA considers QR has used in deriving its reassignment diseconomies. The adjusted reassignment cost (\$725,000) is divided by \$846m, QR's total coal revenues in 1999-00, to give a figure of 0.1%. If the \$2.9m stand-alone cost estimate was used without the QCA's adjustments, the reassignment cost would be around 0.3% of the total revenue earned by QR's coal operations. The QCA recognises that these figures are not precise estimates, but rather provide a reasonable estimate of the order of magnitude of the cost of reassigning the train control function on QR's coal network.

The QCA believes that the benefits of potential or actual competition in the Brisbane urban passenger market are not sufficiently great at present to warrant reassignment of this function within QR. Therefore, the QCA would not object to the scheduling and train control function for the Citytrain network being performed by QR's above-rail business groups.

The Productivity Commission similarly argued in its *Progress in Rail Reform Inquiry Report* of August 1999 that in Australia, there is no urban passenger market where consumers have a choice between competing rail operators, although there may be some competition between urban passenger, non-urban passenger and freight operators for train schedules. In addition, it argued that urban passenger services require that trains run frequently and to a complex timetable, consequently, coordination of services to meet the timetable is likely to be more effectively undertaken by a single operator.

The Productivity Commission noted that vertically integrated urban passenger operators in all States except NSW undertake train scheduling. The QCA agrees with the Productivity Commission that the relatively small size of urban passenger markets in Australia – and strong competition from other transport modes – is likely to limit the scope of competition between train operators for customers.

The QCA considers it is possible the balance of costs to benefits from the integration of the Citytrain train control centre with Network Access may change over time. However, the QCA does not believe that this is likely to occur within the proposed three year term of QR's Undertaking.

The QCA recognises that the proposed reassignment of the train control function will have operational effects on both the above-rail business groups and Network Access. This could justify the development of transitional arrangements to assist these business groups to manage the change without negatively impacting on QR's above-rail operational performance or more generally on rail safety.

The proposed transitional arrangements are driven by QCA's expectations of the likelihood of third-party entry onto particular systems on QR's network and hence the need for an appropriate below-rail market structure to be put in place on those systems:

- Mackay and Rockhampton should be moved within Network Access' responsibilities within six months of the Undertaking being approved; and
- Townsville and Brisbane Central (freight) should be moved within Network Access' responsibilities within nine months of the Undertaking being approved.

#### *Safety implications of reassigning train control function to Network Access*

The thrust of QR's paper 'Why train control should remain as a contracted service provided to Network Access Group by the Above-rail Groups' is that reassigning management responsibility for train control to Network Access threatens safety management on QR's network. QR focuses particularly on NSW, where it argues that a breakdown in communications and poor interfaces between the various railway organisations has resulted in a breakdown in safety management. QR implies that reassigning train control to Network Access will result in a similar outcome in Queensland.

The NSW Department of Transport has advised the QCA that it has serious concerns about QR's analysis of the NSW data:

- it is dangerous to discern trends in annual data because the same trend is not evident in the underlying monthly data;

- the data has been aggregated to such a degree that causal factors have been eliminated and incidents that bear no relevance to the performance of the train control function have been included, in particular, incidents associated with derailments, assaults and public deaths; and
- the recording of data early in its history was not as rigorous as it has been in recent years, which is likely to lead to a natural trend increase in safety incidents.

In addition to the serious concerns raised by the NSW Department of Transport about QR's presentation of the NSW rail safety data, the QCA believes that QR has incorrectly implied that reassigning its train control function to Network Access is akin to the arrangements applying in NSW. In fact, an above-rail operator performs the train control function in NSW. The track manager, RAC, was required to contract the State Rail Authority (SRA) (supplier of metropolitan and country passenger services) to deliver train control services for both passenger and freight above-rail operations. This is essentially the train control model favoured by QR, except that RAC and SRA are independent entities rather than being part of a vertically integrated entity.

The NSW Parliament recently passed the Transport Administration Amendment (Rail Management) Bill 2000 – it is awaiting assent – which, amongst other things, establishes Rail Infrastructure Corporation (the entity merged from RAC and Rail Services Australia) as the body responsible for network control of the NSW rail network.<sup>29</sup> The only exception to this is if the Minister designates a rail operator as the body responsible for network control. The Minister's Second Reading Speech noted that this would allow SRA to be responsible for network control in the Sydney area and Rail Infrastructure Corporation to be responsible for network control elsewhere in the State. The Minister noted that the Special Commission of Inquiry into the Glenbrook Rail Accident recommended this assignment of responsibilities.

In terms of a comparison with train control models adopted in other Australian jurisdictions, the closest one to that proposed by the QCA is Westrail, a vertically integrated organisation whose train control function has been amalgamated with its network management function. Westrail's Network Division provides train control services to interstate operators and internal Westrail operators. The Australian Rail Track Corporation provides a somewhat different model because it is a dedicated track manager, nevertheless, its train control centre in Adelaide manages all train movements from Kalgoorlie to Albury on the interstate line. Moreover, ARTC was formed from the Track Access Unit, which performed the train control function within the vertically integrated Australian National prior to its sale.

The QCA believes it is not currently feasible to make a sound comparison of actual and measured safety performance of the 'integrated with above-rail' and 'integrated with below-rail' train control models given the relatively recent structural changes that have taken place within the Australian rail sector. As a result, the QCA believes that it is not possible to unambiguously endorse one model over the other as having a sounder safety performance.

Nevertheless, the QCA recognises that the train control function is a vital part of the safety system on a rail network and its proposal for reassignment is not intended to trade-off rail safety for third-party entry on QR's network. Indeed, the Authority believes, from a safety perspective, the integration of the network management and train control functions within

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<sup>29</sup> The Bill establishes *network control* with respect to any part of the NSW rail network as: service planning (the timetabling of rolling stock, including standard working and daily timetables, and planning the occupation of railway track for maintenance and other service requirements); and real-time control (the actual control of the movement of rolling stock, including train signalling and incident management).

Network Access would be well suited to a network potentially handling multiple rail operators safely.

Train control is the central point for access to a railway, both by trains and other workers that need access to the railway's infrastructure. The most important role of the train control centre is the coordination of activities when a disruptive incident occurs on a corridor. Where an incident occurs that disrupts the train schedule, train control becomes quite interventionist, directing activities to return train running to the schedule. It is at these times that breaches of safety protocols are more likely because of unusual events. Such events necessitate accuracy and clarity of communication.

Communication protocols involving call signs, repeat back, confirmation and clarification require strict discipline. The QCA understands that this discipline has been somewhat lacking in Australian railways generally. Over-familiarity, where assumptions are made concerning the conveyor and receiver of information, has been a dominant factor in the cause of train accidents. The best examples of strict communications protocols occur in air traffic control centres, which internationally have a totally hands-off relationship with airline operators.

The QCA believes that an improvement in any system will only occur when the parties involved discuss issues, analyse data and trial new methods. The emergence of multiple rail operators in other jurisdictions has brought new pressures onto the train control function particularly with regard to priority allocation, but also in ensuring that commercial rail operators are not disadvantaged as a result of increased safety risk. The QCA believes that a train control centre integrated with the network management function is best suited to managing these pressures.

*Roles of Technical Services Group, Infrastructure Services Group, Deputy Chief Executive's Group and the Safety Executive*

In managing access to QR's network, including processing access applications, preparing indicative access proposals and negotiating over the terms and conditions of an access agreement, Network Access will need to draw on advice from other QR business groups and corporate segments, in particular, Technical Services Group and the Safety Executive. It is also possible that advice could be sought from Infrastructure Services Group and the Deputy Chief Executive's Group. As a result, there is the potential for conflicts of interest to emerge and/or it may become harder to control the flow of access seekers' confidential information within QR.

Technical Services Group provides a range of services to both the above-rail business groups and to Network Access, including engineering, signalling systems, supply, environment and consulting services. Technical Services Group will generally need to be consulted by Network Access once a access seeker has lodged an access application and subsequently moves beyond that point in the negotiation framework established by the Draft Undertaking. The segments within Technical Services Group that will be consulted are the Environmental Unit regarding the development of the environmental risk management plan and the Rollingstock Engineering Unit regarding rollingstock standards and the development of the joint safety risk assessment. The Rollingstock Engineering Unit may be required to provide advice on a third-party operator's rollingstock where it differs from the standards applicable for reference tariffs.

It is possible, but considerably less likely, that other segments within Technical Services Group may need to be consulted by Network Access during the course of an access negotiation process. These are the Civil Engineering and Signalling segments. The likelihood of such consultation being necessary will depend on the nature of the access proposal, including the third-party operator's operational requirements, and can only be assessed on a case-by-case basis.

A similar situation emerges with the Deputy Chief Executive's Group. Its functions are generally internally focussed. For example, employee relations, property and strategic planning. However, it also manages the network communications system and performs a legal function. Depending on a third-party operator's operational requirements, consultation with Network Access may be required on a network communications matter. The issue of legal advisers within QR facing conflicts of interest through possibly advising both Network Access and the above-rail business groups is discussed in section 3.4 of this chapter.

The Safety Executive within QR reports directly to the Chief Executive Officer. The Safety Executive has responsibility for developing and controlling the implementation by business groups of QR's safety management system. The Safety Executive will always be consulted by Network Access in the development of the joint safety risk assessment between QR and a third-party operator.

The QCA believes that Infrastructure Services Group's role within QR is purely as a below-rail service provider. Network Access has signed internal-service contracts with Infrastructure Services Group for the development and maintenance of the network to agreed standards. In the context of an access negotiation process, Infrastructure Services Group may be consulted regarding an enhancement to the infrastructure proposed by a third-party operator. This could provide an early signal of third-party entry, something the third-party operator would normally want kept confidential. The potential exists for Infrastructure Services Group to 'flag' potential third-party entry on a corridor to the relevant above-rail business group.

It is clear there is the potential for segments within Technical Services, Infrastructure Services or the Safety Executive to receive information supplied to Network Access by a third-party operator in the course of an access negotiation process which the operator perceives to be confidential, for example, the characteristics of the operator's rollingstock or elements of its environmental management system. The potential also exists for a access seeker or third-party operator's confidential information to flow from groups such as Technical Services to QR's above-rail business groups in the course of their dealings.

In the absence of Infrastructure Services Group, the relevant segments of Technical Services Group, and the Safety Executive being brought within Network Access, the QCA is only prepared to approve the Draft Undertaking if strict, enforceable confidentiality arrangements regarding the flow of third-party operators' confidential information within QR can be established. Such confidentiality arrangements are necessary to protect third-party operators' legitimate business interests and are discussed section 3.4 of this chapter.

Nevertheless, the QCA believes, over time, as the above-rail market in Queensland matures, Network Access should become less reliant on other QR business groups to deliver its below-rail services. This is likely to be a significant issue in the consideration of future draft undertakings of QR.

#### *QCA's role in approving QR's organisational structure*

From a ring-fencing perspective, QR's organisational structure is of concern to the QCA first in considering whether or not to approve QR's Draft Undertaking and second if, after an Undertaking has been approved, QR decides to change its initial approved structure.

With respect to approving or not approving QR's Draft Undertaking, the QCA understands that paragraph 137(2)(ea) of the QCA Act permits the Authority to require a provision relating to 'arrangements to be made by the owner to separate the owner's operations concerning the service from other operations of the owner concerning other commercial activity'. This would allow an approved Undertaking to provide a substantive obligation on QR to separate staff performing rail-infrastructure functions from those performing train-service functions.

In addition, the QCA believes that it must retain the ability to react to organisational restructures during the term of an approved Undertaking that have fundamental implications for third-party access to QR's network, for example, the abolition of Network Access. While QR committed in para 3.2(a) that it would lodge an amending undertaking if it effected an organisational restructure that impacted on the contents of cl 3.2, this nonetheless is at QR's discretion.

In other words, there is no guarantee that access seekers' interests will be factored into QR's decision whether or not to lodge an amending undertaking. For example, QR may perceive an organisational restructure to raise no competition concerns for access seekers and not lodge an amending undertaking.

In order to protect access seekers' interests, the QCA has identified a number of functions within QR that it considers are sufficiently sensitive from a third-party access perspective that, if QR decides to reassign these functions during the life of an approved Undertaking, QR must submit a draft amending undertaking to the QCA for approval before implementing the reassignment.

The QCA believes that specifying these functions protects QR's legitimate business interests by providing certainty to QR as to the functions it performs that the QCA considers have significant third-party access implications. Any changes QR makes to its organisational structure not involving these functions would not require QCA approval via an amending undertaking.

The functions the QCA has identified as requiring a draft amending undertaking if reassigned are currently performed by Network Access, Infrastructure Services Group, Technical Services Group and the Safety Executive and are as follows:

- Network Access is abolished;
- any of Network Access' current functions, including the scheduling and train control functions, are reassigned to any other QR business group;
- any construction, maintenance or associated functions performed by Infrastructure Services Group are assigned to the above-rail business groups;
- any functions performed by Technical Services Group associated with the processing of access applications are assigned to the above-rail business groups; and
- the Safety Executive is subsumed within an above-rail business group.

The QCA's main concern is that Network Access' existing functions are maintained and that the scheduling and train control functions are not reassigned to the above-rail business groups. As noted above, the QCA expects, that over time, Network Access will take on additional functions currently performed in other parts of QR. The QCA's subsidiary concern is that functions clearly of a below-rail nature, for example, all functions performed by Infrastructure Services Group, and/or functions directly involved in the processing of third-party access applications, for example, Safety Executive, Rollingstock Engineering and Environmental Units, should not be assigned to the above-rail business groups.

***QCA's Position***

The QCA would favourably consider an Undertaking that:

- assigned management and operational responsibility for the performance of the scheduling function and train control function to Network Access with the exception of the Brisbane Mayne (Citytrain) centre;
- if at any time during the life of an approved Undertaking, QR proposes to make any of the following changes to its organisational structure which would adversely affect the capacity of Network Access to reform its functions, including if:
  - Network Access is abolished;
  - any of Network Access' current functions, including the scheduling and train control function, is reassigned to any other QR business group;
  - any construction, maintenance or associated functions performed by Infrastructure Services Group are assigned to the above-rail business groups;
  - any functions performed by Technical Services Group associated with the processing of access applications are assigned to the above-rail business groups;
  - the Safety Executive is subsumed within an above-rail business group,

it must submit a draft amending undertaking to the QCA for approval;

The QCA seeks comments on the appropriateness of the proposed transitional arrangements for the reassignment of responsibility for the short-term scheduling and train control function at the following train control centres:

- Mackay and Rockhampton to be moved within Network Access' responsibilities within six months of the Undertaking being approved;
- Townsville and Brisbane Central (freight) to be moved within Network Access' responsibilities within nine months of an Undertaking being approved;

### 3.3 Ring-fencing Guidelines

QR has advised the QCA that, in addition to the organisational, accounting and internal trading arrangements established in Part 3 of the Draft Undertaking, it envisages its ring-fencing arrangements operating at three levels. First, a set of principles - along the lines of Schedule B of the Draft Undertaking - will be incorporated as a schedule to the approved Undertaking. Second, Ring-fencing Guidelines will be developed that explain the application of the ring-fencing arrangements across the whole of QR and will be made available to access seekers. Third, detailed internal procedural documents, possibly at the business group level, will be developed.

The issue of how QR proposes to manage the flow of third-party operators' confidential information (cl 4.2) is closely linked to its Ring-fencing Guidelines and is discussed in this section of the Draft Decision.

#### *QR's Position*

QR originally proposed to develop Ring-fencing Guidelines within three months of the approval of the Undertaking. The Guidelines were to reflect the principles and address the issues identified in Schedule B: para 3.5(a).<sup>30</sup> The Guidelines would be made available to the QCA for review if required. The QCA could require QR's performance in complying with the Ring-fencing Guidelines to be audited on an annual basis: para 3.5(b).

QR stated in its supplementary submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* paper that its Ring-fencing Guidelines would be made available to access seekers as part of the preliminary information to be provided in accordance with para 4.3(c).

QR subsequently provided the QCA with a revised draft of Schedule B. QR advised the QCA it intended that a revised Schedule B would form a supplement to Part 3 of the Undertaking, in order to ensure a comprehensive statement of its ring-fencing principles was contained in the body of the Undertaking.

The revised Schedule B outlines QR's ring-fencing objective and its ring-fencing principles and processes, covering scheduling and train control, information management, compliance issues, and roles and responsibilities of its staff with respect to its Ring-fencing Guidelines. The provisions of the revised Schedule B are as follows:

**Ring-fencing objective** - QR's stated ring-fencing objective is to ensure it does not engage in conduct aimed at preventing or hindering a user's access to the declared service under an access agreement or a determination.

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<sup>30</sup> Schedule B outlined a set of ring-fencing principles and issues. The principles were as follows: assist in meeting QR's obligations under s104 of the QCA Act; ensure that QR's above-rail business groups are not placed at a competitive disadvantage in relation to the negotiation and provision of access; and retain the economic and other benefits which come from QR's vertical integration, subject to its obligations under the Undertaking and the QCA Act. The ring-fencing issues were as follows: provision of a framework for the movement of third-party operators' confidential information within QR; protection of QR's intellectual property and the intellectual property rights of third-party operators; requiring all QR staff and contractors involved in the provision of access to undergo training in relation to the Ring-fencing Guidelines; establishing staff transfer and secondment procedures to assist in protecting third-party operators' confidential information whilst not unreasonably limiting QR employees' career paths; establishing a register to identify ring-fencing issues and the actions taken to resolve them; establishing procedures to conduct investigations into potential breaches of the Ring-fencing Guidelines; and providing for audits of QR's compliance with the Ring-fencing Guidelines.

**Scheduling and Train Control** - Principles outlined by QR concerning network capacity management and the objectives of train control are discussed by the QCA in Chapter 6.

**Information management** - QR has outlined the following principles:

- Subject to the exceptions noted at para 4.2(c), Network Access will only use confidential information supplied to it by third-party operators for the purpose for which it was disclosed;
- Network Access staff who have access to confidential information will not disclose the information to any person outside of Network Access, unless one or more of the exceptions noted in para 4.2(c) apply, or it is necessary for Network Access to disclose the information to respond to an access inquiry in the manner provided in Part 4 of the Draft Undertaking;
- Network Access will not disclose confidential information to those segments of QR responsible for the commercial arrangements associated with QR operated train services without the approval of the owner/third-party operator who provided it;
- Network Access will not disclose confidential information to those segments of QR responsible for providing train control, scheduling and timetabling services on a day-to-day basis for the QR Network prior to the finalisation of access arrangements, after which necessary information will be given for the purpose of ensuring that the obligations of the respective QR parties established in internal service agreements are met;
- all QR employees external to Network Access, who have access to any confidential information obtained from Network Access, will comply with the same confidentiality principles as Network Access personnel; and
- where QR engages a consultant, contractor or agent external to QR and provides them with confidential information belonging to a third-party operator, they are not to use the information for a purpose other than that for which it was provided, or disclose the information to any other person(s).

QR proposes the following processes to support these principles:

- QR will develop a framework for managing the movement of information within QR to protect the confidentiality of information provided by railway operators, including both third-party operators and QR railway operators;
- QR will implement security measures to protect the integrity of the above electronic and paper-based confidential information;
- where QR engages a consultant, contractor or agent external to QR and provides them with confidential information supplied by a third-party operator, they will be required to provide a written undertaking that they will not use the information for a purpose other than that for which it was provided, or disclose the information to any other person(s); and
- QR will develop procedures for managing secondments and transfers between Network Access and QR railway operators to minimise the impact of such movement on the integrity of confidential information supplied by third-party operators and within Network Access' control.

**Compliance issues** - QR has outlined the following principles:

- QR will promote a culture of compliance in regard to ring-fencing;
- QR will monitor and enforce compliance with the Ring-fencing Guidelines as part of its governance and due diligence in regard to ring-fencing; and
- QR will periodically evaluate its Ring-fencing Guidelines to ensure their ongoing effectiveness and relevance, to identify and understand reasons for non-compliance and to identify and to facilitate continuous improvement.

QR proposes to develop a compliance system in accordance with AS 3806 (Compliance Programs)<sup>31</sup> that will comprise structural, operational and maintenance elements to facilitate compliance with the Ring-fencing Guidelines.

**Structural elements** - QR has made the following commitments:

- a Ring-fencing Compliance Policy endorsed by the QR Board and Senior Executive; and
- resources to ensure QR employees meet their obligations under the Ring-fencing Guidelines.

**Operational elements** - QR will develop a ring-fencing register to record:

- questions of interpretation;
- suggestions for improvement;
- changes to procedures or controls;
- action taken in response to audits; and
- notification of actual/potential breaches, complaints received and any resultant action taken.

QR also proposes to establish complaint-handling procedures to deal with complaints received from third parties that QR has breached its Ring-fencing Guidelines as well as alleged breaches reported by QR employees. These will specify the procedures and the responsibilities of relevant personnel in conducting investigations.

**Maintenance elements** - QR states that education and training will ensure all QR employees and contractors dealing with third-party access have an understanding of the Ring-fencing Guidelines and their responsibilities in relation to the guidelines.

QR also proposes to include audit and review processes to allow for both internal and external audits of QR's compliance with the Ring-fencing Guidelines.

The success of the compliance system will be measured against predetermined performance standards and reported to QR's Compliance Committee or equivalent.<sup>32</sup>

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<sup>31</sup> Australian Standard AS 3806: Compliance Programs was released by Standards Australia in 1998. It applies to legislation, regulation, industry codes and entity standards. It provides a guide for agencies in establishing, implementing and managing an effective legal compliance program.

**Roles and responsibilities** - QR proposes to develop a statement setting out the roles and responsibilities of relevant staff in regard to the Ring-fencing Guidelines and distribute these to all relevant employees. This is to ensure that all managers will understand, promote and be responsible for, compliance with the Ring-fencing Guidelines as they apply to activities within their day-to-day responsibilities.

### *Stakeholder Comment*

It should be noted that these stakeholder comments relate to the earlier version of the Ring-fencing Guidelines provided in QR's Draft Undertaking. As noted above, QR has since provided a revised draft of Schedule B.

Stakeholders generally expressed dissatisfaction with the Guidelines and as a result proposed amendments.

### **Table 6: QR's Ring-fencing Guidelines**

**AMC, Stanwell** - the parameters outlined in Schedule B fall well short of the types of ring-fencing guidelines necessary for an effective undertaking. Ring-fencing of capital investment decisions, senior management decision-making and the operation of the QR Board would need to be considered.

**QMC** - the principles and parameters are very broad. It is not possible to offer a sensible assessment in the absence of a draft of the Guidelines themselves.

**Toll** - the scope of the Ring-fencing Guidelines is entirely inadequate. The Guidelines need to contain much more detailed information, as found in the Ring-fencing Guidelines for the Gas Code, the National Electricity Market, and telecommunications provisions in Part XIc of the *Trade Practices Act 1974*. There should be an explicit requirement in the Undertaking - not the Ring-fencing Guidelines - that QR must not hinder or prevent access and must ensure that access to the declared service by the access provider is not on terms more favourable than those available to the access seeker.

**Queensland Government** - it may be necessary for external scrutiny of the Ring-fencing Guidelines to ensure the effectiveness of the ring-fencing arrangements over time. This may be especially the case regarding train control and access to stations and platforms and marshalling yards where information flows and decisions will involve QR's above-rail business groups.

Another important issue is whether the QCA has sufficient knowledge to determine whether s104 of the QCA Act is effectively being breached as a result of the breach or inadequacy of Ring-fencing Guidelines.

**Great Southern Railway** - the Undertaking should address clearly the procedures to gain access to other facilities controlled by QR as a part of its above-rail operations.

**National Rail** - there was a need for legally enforceable ring-fencing obligations, including legal remedies for parties suffering loss or damages. In other jurisdictions, ring-fencing measures typically include:

- statutory obligations relating to confidentiality carrying substantial penalties;<sup>33</sup>
- regulatory power to investigate reported breaches;
- separation of the contestable and monopoly portions of the integrated organisation;
- audit and review by a statutory regulator (eg. the QCA); and
- recourse to legal remedies in the event of apprehended or alleged actual breaches.

**FreightCorp, Queensland Government** - the parameters are a reasonable starting point from which to develop detailed guidelines. However, the crucial issue would be the final form of

<sup>32</sup> The performance standards are not specified.

<sup>33</sup> The QCA has no power to impose statutory penalties.

guidelines that are accepted by the regulator and parties reliant upon ring-fencing arrangements.

**FreightCorp** - the Guidelines should not be physically part of the Undertaking given their anticipated comprehensive nature. The Undertaking should incorporate the principles to be included in the Guidelines - as currently incorporated in Schedule B of the Undertaking - along with the machinery for their implementation and on-going management.

**RBTU** - Another view was that QR is subject to the same legal remedies as any client of any business that engages in unethical practices with information supplied in the normal course of business.

### ***QCA's Analysis***

The QCA concurs with the general stakeholder view that QR's Ring-fencing Guidelines contained in Schedule B of the Draft Undertaking provide insufficient detail to make an adequate assessment of QR's proposed ring-fencing arrangements.

QR's revised Schedule B has refined QR's ring-fencing objective and also provides some additional detail with respect to the processes QR proposes to implement to protect third-party operator's confidential information and to facilitate compliance with the Ring-fencing Guidelines. However, in terms of content, the revised Schedule B is broadly the same as the version contained in the Draft Undertaking.

The QCA believes that the principles and high level processes outlined by QR in its revised Schedule B generally reflect desirable arrangements for protecting third-party operator's confidential information and facilitating compliance with the Ring-fencing Guidelines.

Nevertheless, given the importance of ring-fencing arrangements to the effective operation of third-party access, reflected in the strength of stakeholder comment on the issue, the QCA is primarily concerned that the Ring-fencing Guidelines establish both enforceable obligations on, and rights of, QR and access seekers. Ring-fencing arrangements that are legally enforceable are essential to ensuring both parties' legitimate business interests are protected. Consequently, the QCA believes that there needs to be refinement of a number of the high-level processes QR has proposed in its revised Schedule B in order to establish enforceable obligations.

The QCA considers that the areas of greatest sensitivity regarding enforceable rights and obligations are:

- the protection of confidential information;
- investigation and reporting of alleged breaches of the Ring-fencing Guidelines; and
- compliance auditing.

The QCA's position on these matters is discussed in detail in the following sections of the chapter.

## **3.4 Protection of confidential information**

### ***QR's Position***

QR and a third-party operator will, at all times, keep confidential and not disclose to any other person, confidential information exchanged as part of access negotiations without the information provider's approval, except where disclosure is in accordance with para 4.2(c).

Confidential information is defined in the Undertaking as any information, data or other matter marked confidential by a party when disclosed to the other party or disclosed to the other party with an express requirement in writing that it be treated as confidential, where such information, data or other matter: (i) is not already in the public domain; (ii) does not become available to the public through means other than a breach of confidentiality; (iii) was not in the other party's possession prior to such disclosure; and (iv) is not received by the other party independently from a third-party free to disclose such information, data or other matter.

If required by either party, the parties shall enter into appropriate confidentiality arrangements to reflect this obligation: para 4.2(a).

Both parties will ensure that all confidential information is used only for the purpose for which it was provided: para 4.2(b).

QR makes an exception to the confidential information disclosure provisions in specific circumstances, including where disclosure is to a range of advisers, including the recipient's lawyers, financial institutions and consultants: para 4.2(c).<sup>34</sup>

The additional principles outlined in revised Schedule B concerning the flow of confidential information were outlined in the previous section. The most significant additions to Schedule B in the Draft Undertaking were that:

- the exceptions in para 4.2(c) are extended such that Network Access could disclose confidential information to other segments of QR in order to respond to an access inquiry;
- Network Access will not disclose confidential information to those segments of QR responsible for commercial arrangements associated with QR's train services;
- Network Access will not disclose confidential information to those segments of QR's above-rail business groups responsible for providing scheduling, train control and timetabling services on a daily basis prior to the finalisation of an access agreement. After finalisation, necessary information will be provided for the purpose of ensuring QR's obligations in internal service agreements are met;
- all QR employees external to Network Access who have access to confidential information obtained from Network Access will comply with the same confidentiality principles as Network Access personnel; and
- where QR provides a consultant/contractor/agent with a third-party operator's confidential information, the information must be used for the purpose for which it was provided and not be disclosed to another person.

QR stated in its initial submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* that the confidentiality arrangements are a structural issue and therefore beyond the QCA's power in considering whether or not to approve the Draft Undertaking. Nevertheless, it argued that the professional and ethical obligations of advisers are sufficient to guard against potential breaches of confidentiality. QR indicated that it already adopts a practice of allocating specific solicitors to particular business groups. However, it also noted that solicitors are a scarce resource and there may be a need to vary the role of solicitors within the organisation from time-to-time. QR also stated that both internal and external advisers

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<sup>34</sup> Under sub-cl 4.1.2(a), QR reserves itself the right to cease negotiations with access seekers who do not observe the relevant obligations and processes in the Undertaking. This would include para 4.2(c). However, the Draft Undertaking is silent on what happens if QR breaches this paragraph.

would be subject to the Ring-fencing Guidelines, which put into effect the confidentiality obligations in the Undertaking.

QR stated that common law consequences will flow from any breach of the confidentiality provisions in the Undertaking, either by QR or a third-party operator. As such, it did not believe that it is appropriate to include references to such remedies in the Undertaking.

### ***Stakeholder Comment***

Stakeholders have not had the opportunity to comment on the additional confidentiality principles outlined in QR's revised Schedule B. Nevertheless, stakeholders made a number of suggestions regarding appropriate arrangements to protect an access seeker/third party operator's confidential information.

#### **Table 7: Confidentiality**

**ARTC** - cl 4.2 of the Draft Undertaking should refer specifically to QR business units - including Network Access - rather than leave it to the Ring-fencing Guidelines to address this level of detail. The guidelines should only include measures and procedures for ensuring compliance with the confidentiality cl.

**AMC** - there is no reason why capacity, cost and pricing information supplied by Network Access would need to be confidential.

**QMC** - all access agreements should be registered with the QCA and made discoverable, however, the parties' confidentiality requirements during the negotiation phase should be respected.

**Queensland Government** - the Ring-fencing Guidelines could establish the parameters within which negotiations regarding confidentiality arrangements take place. While prospective third-party operators should guide the QCA on this issue, it would be reasonable that confidentiality arrangements be left up to the individual access seeker to negotiate with QR against a background of incontrovertible rights.

**Toll** - a third-party operator should be informed in advance if any confidential information is to be disclosed to enable it to take appropriate action.

**AMC** - information marked as confidential should not be released to anyone in QR, other than those involved in Network Access. Agreement of the third-party operator should be obtained before divulging information to another party.

**FreightCorp** - it is noteworthy that QR, like all monopolists, attempts to shroud its operations by requiring as much information as possible to be quarantined as confidential. Our experience has been similar with other monopoly infrastructure owners. It is FreightCorp's view that QR's requirement that access prices be treated as confidential is contrary to the public interest and serves no other purpose than to protect QR's privileged position. QR's access prices are not sensitive in the normal commercial sense – where is the competitor who can take advantage? Rather, it would appear that the only scrutiny that QR is seeking to avoid is that of the regulator.

The confidentiality of access prices appears to even contradict QR's own policy of publishing reference tariffs. Why would a deviation from a reference tariff be confidential if it is available to all parties for the same service?

**RTBU** - the confidentiality arrangements proposed by QR in the Draft Undertaking are reasonable.

A majority of stakeholders thought it was inappropriate for QR to use the same solicitors/advisers for above and below-rail activities, as this would be a clear conflict of interest. One stakeholder argued that this separation is one of the essential elements of the ring-fencing arrangements.

**Table 8: QR's Legal Advisers**

**National Rail** - the above and below rail portions of QR should engage legal and other advisers from different firms to remove any reasonable doubt about observance of probity in this area.

**Toll** - Network Access should have separate lawyers who can deal appropriately with confidential information and, further, this requirement should be expressly contained in the Ring-fencing Guidelines.

**Great Southern Railway, RTBU** - the disclosure of confidential information to legal and accounting advisers is reasonable given the codes of practice within these professions.

**Great South Railway** - given that consultants vary widely in size and competence, and in many circumstances operators will require much more certainty about the security of confidential information, permission to disclose information to a named consultant should be sought on an individual basis.

**Stanwell** - this separation is one of the essential elements of the ring-fencing arrangements.

**AMC** - this separation would be necessary to provide confidence in the ring-fencing arrangements.

**QMC** - this problem will not be confined to Network Access/QR's lawyers. It could also arise in regard to advisers of any kind, and highlights one of the basic, insoluble contradictions between vertical integration and non-discriminatory access.

**Queensland Government** - this is a commercial issue for QR to resolve with the QCA.

***QCA's analysis******Power of QCA to approve***

The confidentiality elements of the ring-fencing arrangements are a fundamental part of the Draft Undertaking. The QCA does not accept QR's view that this is a structural issue beyond the QCA's power in considering whether or not to approve the Draft Undertaking.

The protection of access seekers' confidential information is likely to be critical to the introduction of above-rail competition. For example, an access seeker may not want its interest in running services on a particular corridor to be brought to the attention of an incumbent QR above-rail business group.

***QR's definition of confidential information***

The QCA has some concerns with QR's proposed definition of confidential information. In particular, the definition defines confidential information as 'any information, data or other matter marked confidential by a party when disclosed'. This would exclude information of a confidential nature that was not marked so, and may therefore be too narrow. To remove doubt, where a third-party operator marks information as confidential or indicates its confidential nature as part of its disclosure then it should be deemed to be confidential.

The QCA believes that the inclusion of a more general definition of confidential information is appropriate. This would be consistent with practice in other jurisdictions. Confidential information is defined in the NSW rail access regime as that information which is 'not publicly available and the disclosure of which might reasonably be expected to affect materially the

commercial affairs of a person’.<sup>35</sup> The QCA believes this broader definition is more appropriate for QR’s Undertaking. This is because it is reasonable to expect that most matters about a negotiation will be confidential, including the fact of the negotiation itself.<sup>36</sup>

The QCA considers that the definition of confidential information should also include derived information, in other words, any notes, calculations, conclusions, summaries or other material derived or produced partly or wholly from any confidential information.

In addition, the word ‘lawful’ should be inserted before the word ‘possession’ in the definition of confidential information in Part 8 of the Draft Undertaking and cl 4.2 should refer not only to confidential information exchanged as part of the negotiation process but also exchanged throughout the duration of an access agreement.

Finally, the QCA considers that the Undertaking should specifically recognise that information reasonably necessary to be disclosed by a third-party operator to customers or potential customers in the course of and for the purpose of furthering its business is not confidential information.

#### *Enforceability of ring-fencing arrangements*

The QCA is primarily concerned that an approved undertaking gives rise to incontrovertible rights and obligations with respect to ring-fencing arrangements. This is particularly important with respect to QR’s handling of an access seekers’ confidential information prior to the signing of, and during the term of, an access agreement.

Accordingly, the QCA considers it desirable the Undertaking sets out the rights that either party can expect of the other in relation to the disclosure and treatment of confidential information. This way, the parties can engage in the information exchange that necessarily forms part of contract negotiations confident in the knowledge of the legally enforceable confidentiality obligations that attach to the information. It may also be desirable to supplement these basic obligations.

The QCA believes that enforceable rights regarding the protection of access seekers’ confidential information could be established within a three-tier framework specified in the Undertaking, as follows:

- all QR staff likely to be disclosed third-party operators’ confidential information execute confidentiality deeds which acknowledge the staff members’ confidentiality obligation to QR;
- an acknowledgment register to be established within QR for confidential information disclosed in the context of a particular access application; and
- an acknowledgment register to be established within QR for written information marked confidential which is supplied by a third-party operator in the context of a particular access application.

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<sup>35</sup> Similarly, the ACCC’s Code of Access to Telecommunications Transmission Towers, Sites of Towers and Underground Facilities defines confidential information as including all ‘information...commercial knowledge etc. of a confidential nature...relating to or developed in connection with or in support of the business of a carrier’.

<sup>36</sup> However, if either party is seeking capacity that is the subject of another current negotiation, both parties should be aware of the fact.

The purpose of the first tier is to establish an overarching responsibility on all QR staff likely to be disclosed an access seeker's confidential information, whether that is in an oral or written form, during an access negotiation or over the course of an access agreement. While the QCA does not envisage individual officers being potentially liable for breaching an access seeker's confidentiality, requiring a personal commitment through signing a confidentiality deed and acknowledgment registers would emphasise that it is ultimately individuals who breach confidentiality undertakings. In the QCA's view, the following QR staff are likely to be disclosed an access seeker's confidential information:

- all Network Access staff;
- Group General Manager Technical Services Group;
- all staff within the Rollingstock Engineering Unit within Technical Services Group;
- all staff within the Environmental Unit within Technical Services Group;
- all staff within the Safety Executive;
- Group General Manager Infrastructure Services Group;
- Corporate Counsel; and
- all other in-house legal advisers involved in advising Network Access.

The issue of disclosure of confidential information to QR's internal advisers is discussed in detail in the next section of the chapter.

The purpose of the establishment of an acknowledgment register under the second tier is to provide an ongoing record of those persons to whom confidential information is disclosed. It would buttress corporate responsibility and provide an audit trail regarding information disclosure within QR. At the same time, the QCA accepts that, given a broad definition of confidential information, as proposed in this Draft Decision, there could be practical difficulties in recording all information exchanged in what could be expected to be a series of access negotiations of a generally iterative nature. For example, should the register be signed for each piece of confidential information disclosed and/or each time a Network Access officer discusses with an officer from the Environmental or Rollingstock Engineering Units a particular aspect of a third-party operator's access application which incorporates confidential information?

To minimise such practical difficulties, the QCA believes that this acknowledgment register would only need to be signed once by each receiving QR officer outside of Network Access in the context of a particular access negotiation/application/agreement. The QCA recognises that different segments within Network Access may need to consult regularly regarding a particular access-negotiation. Requiring an acknowledgment register to be signed to reflect this consultation – oral or written – would place an unnecessary burden on Network Access staff.

The third-tier register is aimed at written confidential information that is marked confidential. In other words, the status of this confidential information is beyond doubt, and to recognise this the information has its own register. In the context of a particular access negotiation process, a third-party operator could ensure that all its confidential information disclosed to QR is in written form and has its status clearly marked on the documentation. Each piece of confidential information received by QR officers outside Network Access in this way would require a signature on an acknowledgment form and on the register.

The difference in purpose of the second and third tiers of the framework is that the second-tier register might include oral confidential information exchanged in a phone conversation whereas the third-tier register has only written confidential information clearly marked as such.

If the three-tier framework were specified in the Undertaking, a third-party operator would have legal recourse in the event of confidential information inappropriately flowing to one of the above-rail business groups. This would be dependent on the third-party operator establishing a breach of the provisions of an approved Undertaking.<sup>37</sup>

The QCA endorses the principle in para 4.2(a) which states that, if required by either party, appropriate confidentiality arrangements could be entered into to reflect the obligation that confidential information exchanged as part of the negotiation process would not be disclosed without the approval of the party who provided it. However, the Draft Undertaking does not define the arrangements that would apply in such a case. Consequently, it is possible that either party's desire to establish appropriate confidentiality arrangements could be thwarted through disagreements as to what those arrangements might be.

The QCA considers that, given the importance of protecting an access seeker's confidential information, it may be appropriate for the Authority to reserve the right to establish a deed that either party could enter into at their discretion. The QCA would review the need for such a confidentiality deed over time, reflecting upon the operation of the relevant confidentiality provisions of an approved undertaking.<sup>38</sup> This of course, would not impede QR access seekers agreeing upon their own specific arrangements.

The QCA recognises that reserving itself the right to develop a confidentiality deed could be seen as potentially imposing an onerous regulatory burden on QR. Nevertheless, the regulatory burden inherent in confidentiality deeds reflects the fact that Network Access exists within a vertically integrated organisation where above-rail business groups within that organisation face a potential competitive threat from third-party operators. Moreover, QR has established a functional allocation that necessitates Network Access seeking advice from other segments within the organisation in order to process access applications. These other segments also advise the above-rail business groups.<sup>39</sup>

#### *Disclosure of confidential information to internal advisers*

QR's revised Ring-fencing Guidelines contain similar principles to those contained in the National Gas Code<sup>40</sup> and the TAF Telecommunications Access Code<sup>41</sup>. In general, these

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<sup>37</sup> Section 150A of the QCA Act provides that 'a responsible person must comply with an approved access undertaking given by, or applicable to, the responsible person'.

<sup>38</sup> In practice, if a confidentiality deed was to be specified, the QCA envisages that an access seeker exercising its right would execute the deed with QR, the corporate entity, rather than Network Access or any other QR business group. This is because QR is a statutory government owned corporation with the powers of a natural person – subject to certain restrictions – whereas Network Access is merely a 'business group' of QR. As such, it lacks the capacity to be sued as an entity separate to QR.

<sup>39</sup> As discussed in section 3.1 of this chapter, under QR's functional allocation of responsibilities, Network Access will need to seek the advice of Technical Services Group and the Safety Executive to process a third-party operator's access application. Infrastructure Services Group may also need to be consulted.

<sup>40</sup> This code requires a service provider to establish arrangements that, at a minimum, ensure that: (a) confidential information provided by a user or prospective user is used only for the purposes for which it was provided and is not disclosed without their consent (except where such information is in the public domain or to comply with any law etc); and (b) confidential information which might reasonably be expected to materially affect the commercial interests of a user or prospective user is not disclosed to any other person without the permission of the user to whom the information pertains; and (c) marketing staff of a service provider are not also working for an Associate, and vice versa.

<sup>41</sup> The TAF Telecommunications Access Code (approved by the ACCC in January 1998 and applying to declared services) requires that confidential information of an access seeker (a) must only be used by an access provider to undertake planning, maintenance or re-configuration of its network for the purposes of the agreement or billing as required by the Australian

require that confidential information is only used for the purpose for which it was disclosed and that, where such information is disclosed to a third-party, it is only with the prior consent of the information provider.

The QCA believes that QR's Undertaking should provide that a third-party operator's confidential information must only be used for a permitted purpose, that is, to respond to an access application, develop an indicative access proposal or execute and administer an access agreement.

Network Access has to disclose confidential information to other segments within QR to progress the assessment of an access application. The expected flow of information within QR as it responds to an access application and subsequently negotiates an access agreement in accordance with the negotiation framework established in the Draft Undertaking was discussed in section 3.2 of this chapter.

The QCA believes that the Undertaking should define the segments of QR where disclosure can occur without a third-party operator's consent but have the acknowledgment process operating for officers receiving that information. The following persons and/or segments should be defined as the allowed segments of confidential information convergence:

- Chief Executive Officer and Board;
- Group General Manager Technical Services Group;
- Rollingstock Engineering Unit within Technical Services Group;
- Environmental Unit within Technical Services Group;
- Safety Executive;
- Group General Manager Infrastructure Services Group; and
- Corporate Counsel.

Given QR's organisational structure and associated functional allocation, officers in these positions or work groups could be expected to be disclosed confidential information belonging to an access seeker in the context of an access negotiation or during the term of an access agreement while at the same time advising the above-rail business groups on related matters. With the exception of the Chief Executive Officer and the Board, the officers in these positions should be required to sign an acknowledgment of receipt form upon being disclosed the confidential information and have that disclosure recognised in the relevant acknowledgment register.

The QCA believes that QR's Chief Executive and Board need not sign the acknowledgment register on the grounds that in a vertically integrated organisation there is an inevitable convergence of reporting responsibility within the organisation. Ultimately the Chief Executive and Board of a vertically integrated ring-fenced organisation will be exposed to all the information relevant to a particular issue. Nevertheless, QR's Chief Executive and Board would

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Communications Authority or the Commission; and (b) must only be disclosed to personnel directly involved in the above. There are a number of exceptions to this, including disclosure to directors, officers, employees, agents etc when the information is reasonably required to be disclosed for the purposes of the agreement; to any professional personal acting for the disclosing party; in connection with legal proceedings, arbitration, expert determination and other dispute resolution mechanisms; as required by law, provided the information provider is first notified; with the consent of the information provider; or if reasonably required to protect the safety of personnel or equipment.

be subject to the obligations established by the Undertaking regarding the protection of confidential information including that such information is only used for the purpose for which it was disclosed.

While a third-party operator's and above-rail business group's confidential information could be expected to converge in the hands of officers/work groups identified above given their respective functions within QR, the staff working for these officers may also be placed in a difficult situation. For example, staff working in the Safety Executive may be disclosed confidential information during the negotiation period between Network Access and a third-party operator. These officers may also be advising the above-rail business groups on a related matter, for example, safety arrangements for a particular haul that is the subject of a competitive tender. The QCA believes the Undertaking should establish an obligation that, in such situations, officers advising Network Access should not also advise the above-rail business group on the same or a related matter.

The QCA considers that an access seeker's approval for the release of confidential information to segments within QR not specified above cannot unreasonably be withheld in circumstances where:

- if Network Access intends passing the confidential information to an internal adviser to process an access application, it obtains the prior consent of the access seeker and agrees to execute a confidentiality deed in an agreed form – or, failing agreement, in a form approved by the Authority from time to time - with the access seeker; or
- the internal adviser being disclosed the confidential information has no direct or indirect involvement in advising an above-rail business group on that or related matters.

The QCA can envisage a situation where QR's in-house legal team could potentially be advising both Network Access and one of its above-rail business groups in a situation where the above-rail business group is competing with a third-party operator for the same traffic. It is conceivable that an in-house lawyer advising Network Access could be disclosed confidential information belonging to the third-party operator that may be commercially valuable to an above-rail business group if disclosed by that lawyer in the course of his/her advising that group. QR advised the QCA that, as a general rule, it appointed different in-house lawyers to different business groups to avoid such potential conflicts.

While supporting QR's intent regarding the assignment of its internal legal advisers, the QCA believes that it does not provide sufficient protection to a third-party operator's confidential information. Rather, Network Access should have its own legal team that does not work for any other QR business group. Members of this legal team would be subject to the general confidentiality obligations on QR staff involved in the third-party access process outlined above. In addition, a member of Network Access' legal team, if he/she subsequently moved on to work for a QR above-rail business group, would not be able to work for the next 12 months on a matter for that business group if it was directly or indirectly related to a matter involving a third-party operator that person dealt with whilst advising Network Access.

Given QR's vertically integrated structure, it could also be expected that a non-legal person working in Network Access for a period could subsequently transfer to other QR business groups, including the above-rail business groups. Such a transferee may have gained access to a third-party operator's confidential information while working in Network Access and clearly such information could be commercially significant if divulged to relevant persons in one of the above-rail business groups.

The QCA recognises the right of QR's management to freely move staff within the organisation according to business needs, as well as the right of QR staff to move within the integrated entity

to pursue career paths. Nevertheless, in recognising these rights, access seekers' rights with respect to the protection of their confidential information once it is passed to QR cannot be ignored.

In light of this, the QCA believes that there should be a debriefing process - exit interview - for all Network Access staff prior to their departure to another QR business group. The debriefing process would emphasise a departing staff member's confidentiality obligations established in the Undertaking. In addition, the staff member would be required to sign a separate acknowledgment that he/she had received third-party operators' confidential information, recognised the purpose for which the information had been disclosed and would not disclose it, whether directly or indirectly, in the course of their new duties.

#### *Disclosure of confidential information to external advisers*

The QCA considers that QR should engage different external advisers for its above and below-rail business groups in situations where there is a clear potential for a conflict of interest to occur. This is a key concern of several stakeholders.

QR's argument that the professional codes of practice will be sufficient to protect confidentiality is undermined by the fact that its external advisers face an obligation to QR as a whole, and not to particular groups within QR. As such, the QCA understands that an external adviser will only have an obligation to refrain from disclosing confidential information obtained from Network Access to the other QR business groups if this is specified in QR's contract with the adviser. Without this, there is no legal impediment to such advisers allowing confidential information to flow between QR's above and below-rail business groups, without breaching any ethical obligations to QR.

In order to address this situation, the QCA considers that the Undertaking should specify that QR's contracts with external advisers to Network Access will provide that the advisers will not disclose any information – confidential or otherwise - in respect of access seekers or users to other QR business groups. This would help ensure confidential information disclosed to Network Access is recognised when those external advisers act on behalf of above-rail business groups.

The QCA also considers that Network Access should be required to inform the access seeker before disclosing any information - confidential or otherwise - to its external advisers. The access seeker should be entitled to require such advisers execute a confidentiality undertaking in an agreed form before that disclosure occurs - or, failing agreement, in a form approved by the QCA from time to time.

Finally, the Undertaking should specify that Network Access will not disclose any of an access seeker's information - confidential or otherwise - in relation to a particular access negotiation process to an external adviser engaged by an above-rail business group.

The QCA is aware that the above proposed set of obligations on QR regarding its use of external advisers appears one sided. However, the Authority believes that QR's ring-fencing obligation to protect access seekers' confidential information must extend beyond the organisation to the extent that it appoints external advisers. This is because the aim of the obligation is to protect an access seekers' confidential information, regardless of whether the information flows within QR or beyond QR to its external advisers.

#### *Access to confidential information in an electronic format*

The revised Schedule B states that QR will implement security measures to protect the integrity of electronic and paper-based confidential information. The QCA believes that this

commitment fails to establish a meaningful obligation on QR with respect to implementing security measures or clear rights for an access seeker with respect to protecting the integrity of its confidential information.

One lesson from the UK electricity regulator (OFFER) drawn from its assessment of vertically-integrated public electricity suppliers is that the security of information for customers and competitors can only be achieved through the separation of data and the implementation of strict controls on the ability of internal businesses to access data.<sup>42</sup> OFFER argues that allowing a largely integrated form of information system gives no incentive to the integrated business to identify clearly where data is owned, who is responsible for maintaining it or even if it is necessary for the business.

The QCA considers that the handling of a third-party operator's confidential information in an electronic format should be consistent with the Authority's proposals for the handling of such information in a paper-based format, as outlined in the sections above. For example, QR would be obliged to ensure such information is only available to Network Access within electronic systems and not to any other segment of QR, except in certain defined circumstances, such as the processing of access applications. The obligations on officers to protect a third-party operator's confidential information would be the same regardless of it being in an electronic or paper-based format.

A particular area of sensitivity regarding QR's electronic systems is its freight-management system (FMS). The FMS is a mainframe-based information system that incorporates rollingstock control and train-operations data. Currently, QR above-rail business groups are able, amongst other things, to track train movements in real-time using the FMS. If a third-party operator started train services on QR's network, the above-rail business groups would be able to track that operator's train movements, however, the system would not allow the operator to do likewise for QR trains. From a competition perspective, this is clearly an unacceptable situation.

The QCA believes that determining the ownership of sensitive data produced by the FMS is the key to resolving the competition concerns. Determining ownership will allow access restrictions to be set in place such that rail operators would not be able to access each other's commercial-in-confidence information on the FMS. The Authority considers that an explicit commitment in the Undertaking that only Network Access should have access to the confidential information of a third-party operator on the FMS would address this matter.

#### ***QCA's Position***

**The QCA would favourably consider an Undertaking that:**

- **defined confidential information as that information which "is not publicly available and the disclosure of which might reasonably be expected to affect materially the commercial affairs of a person" and inserted the word "lawful" before the word "possession" in (iii) of the confidential information definition in Part 8;**
- **included 'derived information' in the definition of confidential information ie any notes, calculations, conclusions, summaries or other material derived or**

<sup>42</sup> Source: OFFER/OF GAS, Separation of Businesses: Proposals and Consultation, May 1999, p38.

**produced partly or wholly from any confidential information.**

- **amended para 4.2(a) of the Draft Undertaking to refer not only to confidential information exchanged as part of the negotiation process but also exchanged throughout the duration of an access agreement;**
- **recognised that information reasonably necessary to be disclosed by an access seeker to customers or potential customers in the course of and for the purpose of furthering its business is not confidential information.**
- **provided that an access seeker’s confidential information must only be used for a permitted purpose, that is, to respond to an access application, develop an indicative access proposal or execute and administer an access agreement.**
- **reserved the QCA’s right to develop a confidentiality deed which either QR or an access seeker could enter into at their discretion;**
- **required all QR staff likely to be an access seeker’s confidential information to sign an internal personal confidentiality deed;**
- **established an obligation on QR to establish an acknowledgment of receipt form and acknowledgment register for each access seeker and its associated access negotiation process to provide an ongoing record of those persons who are disclosed a third-party operator’s confidential information.**
- **specified the following persons and/or segments within QR as segments of ‘confidential information convergence’ ie. approval from an access seeker is not required prior to disclosure of its confidential information:**
  - **Chief Executive Officer and Board;**
  - **Group General Manager Technical Services Group;**
  - **Rollingstock Engineering Unit within Technical Services Group;**
  - **Environmental Unit within Technical Services Group;**
  - **Group General Manager Infrastructure Services Group; and**
  - **Corporate Counsel;**

- inserted a provision along the lines that an access seeker's approval for the release of its confidential information cannot unreasonably be withheld where:
  - if Network Access intends passing the confidential information to an internal adviser to process an access application, it obtains the prior consent of the access seeker and agrees to execute a confidentiality deed in an agreed form – or, failing agreement, in a form approved by the Authority from time to time - with the access seeker; or
  - the internal adviser being disclosed the confidential information has no direct or indirect involvement in advising an above-rail business group on that or related matters;
- required Network Access to appoint its own in-house legal team and precluded a member of that legal team, if he/she subsequently moved on to work for a QR above-rail business group, being able to work for the next 12 months on a matter for that business group if it was directly or indirectly related to a matter involving an access seeker that person dealt with whilst advising Network Access;
- required that QR employ different external solicitors/consultants/advisers for its above and below-rail business groups where there is a potential for a conflict of interest to occur, for example, where an access seeker and an above-rail business group are competing for business and an external adviser is acting for that QR business group;
- inserted a requirement to the effect that QR's contracts with external advisers to Network Access will provide that Network Access will inform the third-party operator before disclosing any information – confidential or otherwise - to the adviser and the adviser will not disclose confidential information in respect of access seekers or users to other QR business groups; and
- explicitly committed that only Network Access has access to the confidential information of a third-party operator in the FMS.

### 3.5 Breaches of Ring-fencing Guidelines

#### *QR's Position*

QR argued in its submissions to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* that documents associated with the Undertaking, such as the Ring-fencing Guidelines, must comply with and accurately reflect the relevant principles and high-level

processes specified in the Undertaking. If the documents fail to do this, QR will be exposed to the penalties and other consequences of non-compliance specified in the QCA Act.

QR argued that the Act does not confer any general investigative power upon the QCA in respect of alleged breaches of the Act or an approved Undertaking and QR did not believe that the Undertaking was the appropriate place to create such a power. QR considered that the appropriate role for the QCA, once an Undertaking had been approved, should be to safeguard the integrity of the constructed commercial environment in which access negotiations are to occur.

QR argued that the dispute resolution procedures provided in cl 4.9 trigger Division 5, Part 5 of the QCA Act, enabling an access seeker to refer the dispute to the QCA if it believes QR has failed to comply with its Undertaking, or has breached the provisions of the QCA Act. QR also argued that its obligations under the *Trade Practices Act 1974* are relevant (section 52 – misleading or deceptive conduct) and that the Undertaking enabled the QCA to require an annual audit of its compliance with the Ring-fencing Guidelines, which may extend to an independent external audit.

With respect to whether there should be a symmetry of consequences if QR and a third-party operator breach confidentiality provisions of the Undertaking, QR argued in its initial submission to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking* that it is difficult to see how this could be achieved given the obligations upon each party are very different. In particular, QR has a legal obligation to negotiate with third parties seeking access for the purpose of reaching an agreement, but third-party operators have no reciprocal obligation. As a result of this obligation, QR believes it is reasonable that a breach of the confidentiality provisions by a third-party operator form sufficient grounds for QR to cease negotiations. In turn, QR argued it is bound to negotiate in accordance with the provisions of the Undertaking, or face remedies under s158A of the QCA Act. QR reinforced this position in its supplementary submission to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking*.

### ***Stakeholder Comment***

There was general support in submissions for external reviews of alleged breaches of the Ring-fencing Guidelines.

#### **Table 9: External reviews of alleged breaches**

**National Rail** - there should be adequate provision for external review of alleged breaches and enforceable remedies available to parties suffering loss or damage.

**AMC, FreightCorp, National Rail, Stanwell, QMC, Toll** - the QCA should be the review body.

**Toll** - it may be appropriate for QR to conduct an internal investigation first.

**FreightCorp** - it may be appropriate for QR to conduct an internal investigation first. The Undertaking should contain a provision such that a party dissatisfied with any internal QR investigation could report the matter to the QCA. The QCA should also be able to conduct an investigation of its own volition where it has reasonable cause.

**Queensland Government** - external monitoring of compliance is supported. s104 of the QCA Act provides for external review of actions in instances where access is allegedly hindered or prevented.

**AMC, Queensland Government, Stanwell** - consideration may need to be given to including a provision in the Undertaking to allow the QCA to respond to individual complaints.

**RTBU** – If QR breaches its Ring-fencing Guidelines, a party has the right to refer the issue to the QCA or to a court. This is more redress than parties normally have in commercial relations and no more powers are required.

There was general support for the Undertaking to address the implications of the Ring-fencing Guidelines

**Table 10: Implications of a breach of the Ring-fencing Guidelines**

**Stanwell, Toll** - supported the Undertaking addressing the implications of a breach of the Ring-fencing Guidelines.

**Queensland Government** - supported the Undertaking addressing the implications of a breach of the Ring-fencing Guidelines provided the QCA did not consider that the only material breaches are those that relate to preventing or hindering access.

**ARTC** - appropriate penalties should exist to cater for any breach by QR.

**National Rail** - the Ring-fencing Guidelines need statutory backing, with sanctions and remedies available for third-party operators if breaches occur. The Undertaking could provide for assessment of compensation and for adjudication of complaints, with provision for penalties in the event of adverse findings against QR officers in breach of ring-fencing 'rules'.

**FreightCorp** - compliance can be enforced through the courts, provided the Undertaking incorporates the ring-fencing procedures.

**Toll** - the Undertaking should provide that if there is a finding of any breach of the ring-fencing requirements, the auditor must make an assessment of the benefit to QR of a breach of those provisions. QR should be required to make compensatory payments to the persons who have been affected.

There was broad agreement from stakeholders that there should be symmetry of consequences between QR and a third-party operator for a breach of the confidentiality provisions of the Undertaking.

**Table 11: Breach of confidentiality**

**AMC, Toll** - there should be a symmetry of consequences for breaches.

**QMC** - there should be a symmetry of consequences for breaches. This could only be achieved if there was a settlement in favour of the aggrieved party, with the QCA acting as arbiter.

**AMC, Stanwell** - it would be inappropriate for QR to insist that information is confidential when it should be in the public domain, and the Undertaking should include clear definitions of what is confidential.

**ARTC** - the Undertaking does not refer to the consequences of QR breaching confidentiality provisions.

**Queensland Government** - the consequences should be similar, regardless of which party breaches the confidentiality provision. This could be determined by commercial negotiations against a backdrop of standard rights.

**RTBU** - the Undertaking already contains symmetrical consequences as both parties have legal rights and the courts would allow for calculation of damages.

## *QCA's Analysis*

### *External reviews of breaches*

The QCA considers that provision for external review of alleged ring-fencing breaches has merit, on the grounds that access seekers are likely to have more confidence in an independent review process than one conducted by QR. Nevertheless, an initial step of internal review by QR is reasonable if appropriate levels of accountability are incorporated and a protracted process is avoided.

In the event of confidential information falling into the hands of a person within QR who did not reasonably require access to it, the QCA believes that the onus of proof should be on QR to demonstrate that this did not occur as a result of a breach of the confidentiality obligations.

In general terms, the QCA believes that the response to an alleged ring-fencing breach should follow three steps. First, the alleged breach has to be confirmed and, if relevant, compensatory action determined. Second, if a breach has occurred, QR's internal ring-fencing processes need to be reviewed and possibly changed to minimise the likelihood of the particular ring-fencing breach being repeated in the future. Finally, QR should advise the QCA of any alleged breach and the action taken by QR as this is an important aspect of the Authority's ongoing monitoring of the adequacy of the ring-fencing arrangements. Moreover, it is common practice that regulatory authorities require reporting of breaches.<sup>43</sup>

Allowing an internal review as a first step provides QR with a right to take any necessary actions internally in accordance with the second step. However, to the extent that a ring-fencing breach has occurred, it is in the interests of an access seeker to be able to seek recourse in a timely manner. Whilst the seriousness of ring-fencing breaches will likely vary, it is difficult to anticipate the pattern of such breaches in advance. Moreover, proving that breaches have occurred is likely to be a difficult matter.

The QCA believes that any internal review of an alleged ring-fencing breach should commit QR to complete the review and notify the access seeker in writing of the findings of the review within 28 days of the alleged breach being brought to QR's attention in writing. The findings should include the actions QR has taken in response to the breach including the measures QR intends to take to minimise the likelihood of the ring-fencing breach being repeated. The QCA should receive a copy of QR's findings at the same time as the access seeker or and subsequently be advised when the remedial action has been implemented.

It is possible that the complainant may be unhappy with QR's internal review. In such a situation, the QCA believes that the complainant should be able to refer the matter to the Authority, which should then investigate the potential breach. If the QCA or its external agent finds the breach proven, this would be evidence in any subsequent legal action taken against QR.<sup>44</sup>

The issue of liquidated damages is discussed in the next section.

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<sup>43</sup> The National Gas Code requires a service provider to report to the regulator at reasonable intervals (determined by the regulator) describing measures taken to ensure compliance with its ring-fencing obligations and an assessment of the effect of those measures. A service provider must also report any breach to the regulator immediately upon becoming aware that the breach has occurred. The QCA's draft Electricity Distribution: Ring-fencing Guidelines (December 1999) contains similar provisions regarding regular reporting of compliance and notification of breaches to the QCA. However, the QCA proposes to make publicly available the compliance report prepared by the service provider, along with the QCA's assessment of compliance. The QCA proposes that confidential information would be removed from the public report where the service provider can demonstrate that its public release would harm the commercial interests of the service provider.

<sup>44</sup> The QCA does not have the power to award compensation.

*Implications of a breach of the Ring-fencing Guidelines*

It is conceivable that the most frequent breaches of the Ring-fencing Guidelines will be in relation to inappropriate disclosure of confidential information by individuals. While submissions generally supported enforcement of ring-fencing breaches, there was no consensus on an appropriate approach.

The QCA believes that the confidentiality obligations established in the Undertaking should include a liquidated damages clause. This is on the grounds that those who suffer loss from a breach of the ring-fencing provisions of the Undertaking should be compensated, however, quantification of that loss will be difficult.

Reflecting this quantification problem, the QCA believes that there would be some benefit to both QR and access seekers in establishing a damages figure for relatively minor ring-fencing breaches in the Undertaking. Such a figure would provide a signal to both parties involved in the third-party access process that their obligation to protect each other's confidential information was a serious one.

The QCA believes that a reasonable pre-estimate of damages for a relatively minor ring-fencing breach would be \$10,000. An example of a relatively minor ring-fencing breach might be QR's Environmental Unit disclosing some aspect of a third-party operator's environmental management system for its proposed or actual train services to a QR above-rail business group. While such disclosure would likely breach the third-party operator's intellectual property rights, it would be unlikely to seriously affect the viability of its train services.

On the other hand, a new third-party operator entering the Queensland above-rail market could quite easily be required to make an investment in excess of \$100m - for rollingstock, re-fuelling facilities, office accommodation etc. Serious ring-fencing breaches, such as a Network Access officer advising an above-rail business group that an end-user was considering switching supply to a third-party operator, could result in plans for that operator's proposed train services being shelved. Damages of \$10,000 in such a situation would clearly be inappropriate. The QCA believes that for serious alleged ring-fencing breaches, a third-party operator should have recourse to the courts. A reasonable threshold for recourse to the courts would be potential damages in excess of \$100,000. In addition to any remedies available at law, the third-party operator should be able to seek injunctive relief against QR.

The QCA recognises that the amendments proposed above appear one-sided in that only QR's breach of an access seeker's confidential information is addressed and not vice versa. However, the reason for this is that it is the inappropriate disclosure of a third-party operator's confidential information within QR that is of particular concern to the Authority. There is no equivalent problem with respect to an access seeker handling QR's confidential information. Rather, the matter of an access seeker breaching QR's confidentiality can be adequately addressed through the usual legal and equitable avenues.<sup>45</sup>

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<sup>45</sup> The circumstances in which QR would be entitled not to negotiate including as a result of a breach of its confidentiality by an access seeker are discussed in section 4.4 of Chapter 4.

***QCA's Position***

The QCA would favourably consider an Undertaking that:

- provided for QR to report immediately to the QCA any actual or alleged breach of the Ring-fencing Guidelines and any response by QR;
- established an initial internal review process for alleged ring-fencing breaches such that:
  - the internal review is completed and the access seeker notified in writing of the findings of the review within 28 days of the alleged breach being brought to QR's attention in writing;
  - an access seeker and QCA could refer a dispute over the findings of the internal review to the QCA at the end of the 28 day period; and
  - the results of the subsequent QCA review provide a basis for compensation;
- included a liquidated damages clause of \$10,000 where confidential information is disclosed to an above-rail business group in breach of the Ring-fencing Guidelines; and
- allowed an access seeker to seek recourse through the courts if it could demonstrate that an alleged breach of the ring-fencing provisions of the Undertaking had caused damage in excess of \$100,000. In addition to any remedies available at law or in equity, the access seeker should also be able to seek injunctive relief against QR; and
- in the event of confidential information falling into the hands of a person within QR who did not reasonably require access to it, placed the onus of proof on QR to demonstrate that this did not occur as a result of a breach of the Undertaking's confidentiality obligations.

### 3.6 Auditing of QR's compliance with the Ring-fencing Guidelines

***QR's Position***

The QCA may require QR's performance in complying with the Ring-fencing Guidelines to be audited on an annual basis: para 3.5(b). Schedule B of the Draft Undertaking states that the Ring-fencing Guidelines will provide for audits of QR's compliance. Revised Schedule B raises the possibility of external compliance audits.

### *Stakeholder comment*

A majority of submissions supported annual audits, however alternative views were expressed.

#### **Table 12: Audits of QR's compliance with Ring-fencing Guidelines**

**AMC, ARTC, National Rail, Queensland Government, Stanwell, RTBU** - annual audits would be reasonable.

**FreightCorp** - annual auditing may be too restrictive, the QCA should have the option to conduct an audit of performance in this area as often or seldom as it thinks fit.

**Toll** - there should be an absolute requirement for six monthly audits and for QCA audits at any other time upon receipt of a bona fide complaint.

**AMC, FreightCorp, Stanwell, Toll** - the QCA should be able to appoint the auditor.

**Queensland Government** - the Undertaking should address the consequences of the Authority not accepting the identity of the person who is to conduct the audit.

**RTBU** - the appointment of an auditor to be a matter for QR with the QCA having no power to intervene.

**Toll** - the auditor must not have any other role in relation to QR, including audit of QR's other functions.

### *QCA's Analysis*

The QCA considers that regular auditing of QR's compliance with the Ring-fencing Guidelines is a potentially important means of demonstrating QR's commitment to meet its ring-fencing arrangements and provides accountability to its stakeholders. The QCA believes that QR's proposed processes are generally sound, however, they do not provide sufficient detail to establish enforceable obligations on QR.

The QCA believes that the key elements of QR's compliance auditing that need to be addressed in the Ring-fencing Guidelines are:

- appointment of an auditor;
- frequency of compliance audits;
- QR's commitment to provide information to the auditor within a required time frame; and
- reporting of audit reports.

The issue arises as to whether QR or an external party should conduct the audits. It is important to recognise that the confidence market participants have in the audit of QR's compliance will depend on the integrity of the internal reporting and investigation systems QR has in place. Its proposal to develop a compliance system in accordance with AS 3806 could be seen as a signal of QR's commitment to develop robust internal processes. However, at this stage, QR has not provided sufficient information to the QCA on its ring-fencing arrangements for the QCA to be able to make an assessment of the integrity of those internal processes.

Moreover, regardless of QR's internal processes, there is always likely to be a perception of potential bias if QR were to audit its own compliance with the ring-fencing arrangements. A lesson from other jurisdictions has been that where the regulated entity controls the appointment of the auditor the credibility of the outcomes is compromised.

In order to avoid the potential for a conflict to arise in this respect, the QCA believes it should reserve the right to appoint an external auditor to conduct the audit. The QCA will consult with QR about the identity of its proposed appointment and take account of any concerns QR raises. If the QCA chose to appoint an external auditor, QR would have to commit to provide all information requested by the auditor within specified time frames determined at the time of the auditor's appointment. QR also would be required to pay for the audit.

In terms of a regular audit process, the QCA considers that an annual compliance audit would be reasonable. An annual audit balances QR's legitimate business interest to not be subjected to an excessive regulatory burden and access seekers' interest to be informed in a timely manner regarding QR's compliance with its Ring-fencing Guidelines. Nevertheless, the QCA agrees with stakeholders that a capacity to respond to specific complaints regarding breaches of the Ring-fencing Guidelines would be preferable to annual auditing alone. The scope for access seekers to seek legal recourse in the event of a finding of a breach of the Ring-fencing Guidelines was discussed in the previous section.<sup>46</sup>

The completed compliance audit report would be provided to the QCA. In addition, the QCA is of the view that public reporting of the results of an audit would significantly enhance transparency and accountability, not only with current third-party operators, but also with intending access seekers, and hence promote confidence in the third-party access regime in Queensland.

The QCA is aware that IPART has proposed the appointment of a ring-fencing compliance officer in each NSW electricity distribution network service provider (DNSP) on the grounds that such an officer would be able to observe internal procedures far more closely than the Tribunal.<sup>47</sup> This would be in addition to a requirement to submit compliance reports to the Tribunal at specified intervals. The officer would be funded by the respective DNSPs and located at their business' headquarters. IPART would select the compliance officers who would be responsible to it. IPART argued that the concept of a compliance officer appointed by the regulator has received support in Tasmania and the United Kingdom.

The QCA recognises the grounds for IPART's proposal, however, at this stage has decided not to reserve a right to appoint a ring-fencing compliance officer within QR. The QCA has some concerns that such an officer would only pick up unintended, less serious ring-fencing breaches. It is the systemic breaches that the QCA is most concerned about. There is anecdotal evidence that even internally appointed compliance officers can do little to reveal surreptitious and persistent breaches of the very program they are appointed to enforce.<sup>48</sup>

Nevertheless, the Authority intends to closely monitor the efficacy of these arrangements in the jurisdictions in which they are applied and, if appropriate, adopt similar arrangements in conjunction with future reviews of QR's undertakings.

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<sup>46</sup> Auditing of cost allocations will be considered in conjunction with the Costing Manual and discussed in Chapter 5.

<sup>47</sup> 'Ring Fencing of New South Wales Electricity Distribution Network Service Providers', Discussion Paper and Draft Ring Fencing Guidelines, Independent Pricing and Regulatory Tribunal of New South Wales, September 2000.

<sup>48</sup> 'International Cartels: The Intersection between FCPA Violations and Antitrust Violations', Gary R. Spratling, US Department of Justice, December 1999.

***QCA's Position***

**The QCA could favourably consider an Undertaking that:**

- **provided for annual compliance audits of the Ring-fencing Guidelines;**
- **reserved the QCA's right to decide whether an internal or external compliance audit of the Ring-fencing Guidelines should be conducted and in the case of an external audit, to choose the identity of the auditor;**
- **committed QR, in the event of an external audit, to provide all information requested by the auditor within specified time frames determined at the time of the auditor's appointment and to pay for the audit;**
- **committed QR to provide compliance audit reports to the QCA; and**
- **allowed the QCA to publish, as appropriate, QR's compliance audit reports.**

### **3.7 Internal access agreements**

As QR is vertically integrated, the nature of the terms and conditions on which its below-rail services are provided to its above-rail business groups is a significant issue for new third-party entrants. There is arguably considerable scope for QR to favour its own operation at the expense of third-party operators in the contestable market. This has the potential to distort the development of the above-rail market, including raising barriers to entry for new third-party operators, with associated implications for price levels and the quality of services provided to end-users.

Consequently, the QCA considers that equivalence of the terms and conditions of internal and external access agreements should be a key objective of the framework established by the Undertaking. The equivalence of terms and conditions is relevant in the context of s104 and 125 of the QCA Act which prohibit an access provider supplying access to itself on more favourable terms than to a competitor, such conduct being deemed under these provisions to hinder access. However, these sections provide that an act done in accordance with an approved undertaking will not contravene these provisions. Consequently, internal access agreements developed in accordance with an approved undertaking cannot be challenged under these provisions of the QCA Act.

For existing QR traffics, there is an important transitional issue of what is the appropriate term of the access rights vested in these traffics through internal access agreements. This is because the QCA understands that many of QR's external contracts are short-term in nature.

In this context, the QCA believes that it is important to ensure that access rights are not 'grandfathered' in a non-contestable way through QR's Undertaking, effectively limiting customer choice and restricting available capacity. This is particularly important given that internal access agreements for existing traffics are not required to be consistent with the provisions of the Undertaking and cannot be challenged under the hindering access provisions

of the QCA Act. The issue is somewhat different for new traffics, given that internal access agreements relating to any new traffics are required to be consistent with the provisions of the Undertaking.

### **3.7.1 Proposed framework for establishing internal access agreements for existing QR train services**

#### ***QR's Position***

QR will develop internal access agreements between Network Access and the respective above-rail business groups for all its existing above-rail services: sub-cl 3.4.1. These internal access agreement will be developed according to the timetable set out in Schedule A: sub-cl 3.4.1(b). These internal access agreements, once developed, will be made available to the QCA for review if the QCA requires: sub-cl 3.4.1(c).

Nevertheless, QR does not intend to conduct all of the processes provided in the Draft Undertaking in developing these agreements. QR argued in its Explanatory Guide that many of the Undertaking's processes do not have any meaningful application to train services that have been operating on QR's network for some time. For example, all existing QR train services are covered by QR's safety management system so a safety risk assessment of these services is not necessary unless a significant change to these services is planned.

QR argued in its Explanatory Guide that, notwithstanding the Draft Undertaking does not require that internal access agreements for existing QR train services be consistent with the provisions of the Draft Undertaking, the internal agreements will be 'sufficiently' consistent' with the Draft Undertaking to ensure that QR is not in breach of s104 of the QCA Act.

QR indicated in its initial submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* that it had recently adopted an internal trading approach to its operations. Interim internal agreements were prepared for the 1998-99 year. Similar agreements for 1999-2000 have not been completed.

QR has subsequently provided the QCA with a *Principles for Determining Longevity and Rate Review of Internal Access Agreements for Existing Traffics* Discussion Paper.

#### ***Proposed timeframe for establishing internal access agreements (Schedule A)***

Schedule A of the Draft Undertaking contains a timetable for the completion of internal access agreements after the commencement of the Undertaking, ranging from:

- four months for coal and major industrial products;
- six months for unit trains of containers and primary industry products (eg grain, sugar), Brisbane urban and inter-urban passenger, long distance and country passenger; and
- nine months for other traffics, such as livestock and small freight.

#### ***Term of internal access agreements***

QR argued in its discussion paper that price and security/certainty of access were important factors in determining whether rail is used as a mode of transport. QR's role is to strike a balance that accommodates an operator's needs with respect to price and certainty, whilst not, particularly in capacity constrained areas, prohibiting traffics with a greater capacity to pay from gaining access.

In determining the longevity of internal access agreements, QR has distinguished between:

- existing traffics for which it has an agreement with customers that accurately reflects QR's - and the customers' - commitment; and
- traffics where there is either no external agreement or, if there is, its term does not reflect the commitment to train services QR has actually made.

QR argued that its above-rail business groups have developed goodwill with their customers over the years, including making assumptions about the anticipated demands of these customers. However, these assumptions have not been reflected in the existence of a contract or the longevity of such a contract, if in existence. The absence of competition for the provision of rail services has meant that QR's above-rail business groups have, in the past, not viewed contracts with these customers as essential.

For traffics where end contracts with customers have not been executed, QR argued that their purpose was primarily to set an agreed price. QR argued that the terms of these arrangements were not intended to reflect the length of time that the customer required QR to commit to provide the service or, consequently, the term for which QR above-rail business groups planned to provide the service. Accordingly, QR proposed that internal access agreements for existing traffics would – subject to a limited number of exceptions outlined below - accommodate a reasonable minimum term to take account of these issues.

On the other hand, QR argued that where the customer, such as coal and minerals developers, faced a large up-front capital investment in their business, they required the additional certainty of a contractual commitment from QR for the provision of train services for a defined term. In these cases, rail haulage agreements were created to give both customers and QR the contractual certainty each needed to make the necessary investments. Consequently, as QR considered that these agreements provided an accurate indication of the duration of QR's commitment to provide the relevant train services, it proposed to limit the longevity of internal access agreements for the relevant traffic to the term of the haulage agreement.

To reflect these considerations, QR proposed a minimum term of five years and a maximum term of ten years for internal access agreements for existing traffics. The exceptions to these terms apply to traffics:

- in respect of which a rail-haulage agreement exists, the duration of which accurately reflects the term of the commitment made by the customer to acquire the train services from QR and the commitment made by QR to provide the services in question. These traffics are likely to be predominantly coal and minerals traffics. The internal access agreements for these traffics will mirror the term of the haulage agreement which may be shorter than the minimum 5 year term or in excess of the maximum 10 year term;
- in respect of which the applicable QR above-rail business group requests a shorter-term access agreement than the minimum 5 years proposed; and
- that run over rail infrastructure funded by government through a below-rail government service agreement (GSA) where the agreement only provides a commitment to funding the provision of the infrastructure for less than five years. In such cases, including branch lines, the internal access agreement will not exceed the term for which the infrastructure is funded by Government, and therefore could be shorter than the five years proposed.

For all other internal traffics, QR has outlined the following principles which it considers to be relevant to determining where, within the five to ten year range, the term of the applicable internal access agreement should be set.

1. *End contracts for train services*

QR argued that the term of a contract between a freight forwarder and its customer may be a relevant factor in determining the term of certain internal access agreements. QR considered such contracts were relevant to the assumptions made by QR, as rail operator, in planning to provide particular train services.

2. *Lead Time*

Where the nature of the business dictates that there is a particular lead time to the performance of a train service, the longevity of access agreements in respect of those services would need to reflect, at a minimum, this lead time. For example, passenger services need significant lead time to accommodate scheduling, marketing of services and passenger bookings.

3. *Business plans*

QR argued that another relevant consideration is the decisions that have been or are planned to be taken, such as investment in rollingstock and/or marketing, in respect of the provision of certain train services, as indicated in business plans. QR noted that it would need to assess whether those decisions were based on a reasonable assumption as to the duration of their required commitment to provide those train services. In making this assessment, historical data on the provision of train services to be covered by access agreements, including the volume and spread of traffic, would be considered. Factors such as the expected life of the customer's business would also need to be considered as this may have affected the relevant above-rail business group's planning.

4. *Actual and potential competitors*

QR would take account of the access agreement term that a third-party operator required if it proposed to operate the same train services in question on a commercial basis. QR noted that experience in Queensland and New South Wales shows that many rail operators are seeking five to fifteen year access agreements, depending on the size of the operator, and generally with one or two options for longer terms, exercisable at the operator's discretion. In some cases, smaller operators would be seeking longer access agreements of up to 25 years.

5. *Anticipated demand for capacity*

Network Access would take account of the expected future demand for the relevant access rights.

In finalising an internal access agreement for an existing marginal traffic<sup>49</sup> wishing to operate in a capacity constrained area<sup>50</sup> of QR's network, whether or not there is actual demand for the capacity to be utilised by the marginal traffic, Network Access would limit the term of the access agreement for the marginal traffic to five years.

QR argued in its supplementary submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* that it did not agree that 'interruptible' capacity entitlements should be allotted to marginal traffics and/or in congested areas. However, QR recognised that in congested areas there is a benefit to be gained from limiting the term of

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<sup>49</sup> 'Marginal traffics' are defined by QR as traffics paying an access charge equivalent to a margin over long-run avoidable costs of less than 25 per cent of the fixed component of fully distributed costs.

<sup>50</sup> A 'capacity constrained area' is defined by QR as one in which less than 15 per cent of capacity is available for access.

agreements for marginal traffics to the maximum extent practicable, taking into account the genuine requirements of the traffics and the anticipated demand for capacity.

QR's proposed indicative access terms for internal access agreements are outlined in the table below.

**Table 13 Proposed term of internal access agreements for existing traffics**

Traffic type	Factors affecting term of access agreement	Indicative term
<b>Passenger</b> GSA funded - Traveltrain - Citytrain  Commercial - Kuranda	<ul style="list-style-type: none"> <li>• Business plans for service/s.</li> <li>• Government service agreement.</li> </ul> <ul style="list-style-type: none"> <li>• What commitment a third-party operator would need to make the provision of the same service/s viable commercially.</li> <li>• Nature of business – bookings 18 months ahead of travel, timetables 18 months ahead of application.</li> </ul>	5 years 7 years  10 years
<b>Primary Products</b>	<ul style="list-style-type: none"> <li>• Haulage contract.</li> <li>• Nature and history of business – seasonal.</li> <li>• Business plans for service – investment planned on basis of expected volumes etc.</li> <li>• Capacity constraints.</li> </ul>	5 years
<b>Coal &amp; Mineral products</b>	<ul style="list-style-type: none"> <li>• Haulage contract.</li> </ul>	Dependent on haulage contracts.
<b>Freight</b> - general freight - freight forwarding	<ul style="list-style-type: none"> <li>• Nature of business – on demand service.</li> <li>• Business plans for service – investment planned on basis of expected volumes etc.</li> <li>• Capacity constraints.</li> </ul>	North Coast Line – 5 years. Other – 7 years.
<b>Livestock</b>	<ul style="list-style-type: none"> <li>• Nature of business – on demand services.</li> <li>• Business plan for service – investment in livestock wagons on certain business assumptions.</li> <li>• Capacity constraints.</li> </ul>	5 years
<b>Ad hoc traffic</b>	<ul style="list-style-type: none"> <li>• Access agreements will be signed on one-off basis and subject to all other traffics.</li> </ul>	0

### *Stakeholder Comment*

A majority of stakeholders raised concerns about the proposed timetable for establishing internal access agreements.

**Table 14: Proposed timetable for establishing internal access agreements (Schedule A)**

**AMC, Stanwell** - the timetable appeared somewhat excessive given that some minor traffics were to be allowed up to nine months to be finalised.

**Toll** - the proposed timetable enabled self-preferment by establishing first what are likely to be QR's longest and most profitable contracts for coal and major industrial products.

**Queensland Government** - internal access agreements should already be under development and be completed as soon as possible. The timeframe may be critical if a third-party access seeker is confronted with capacity limitations.

**RTBU** - the timetable is reasonable.

**FreightCorp** – the timetable is reasonable given that the completion of internal access agreements is likely to be a time consuming task for the large number of traffics QR hauls and it is reasonable to expect that the approval process for the Undertaking will have some bearing on the content of the internal agreements.

It should be noted that stakeholders have not had the opportunity to comment on QR's discussion paper on internal access agreements. With respect to the appropriateness of the proposed framework for establishing internal access agreements, there was a general view among stakeholders that there should be competitively neutral treatment of QR's above-rail business groups and third-party operators

**Table 15: Term of internal access agreements**

**FreightCorp, Toll** - QR's indication in the Explanatory Guide that internal access agreements would be 'sufficiently consistent' with the terms of the Undertaking was too weak a commitment given that s104 of the QCA Act would not apply to an approved Undertaking.

**AMC, Stanwell** - there should be sufficiently detailed information available to third-party operators and the QCA in order for them to satisfy themselves that internal access agreements do not provide any benefit to QR's above-rail business groups. Sub-cl 3.4.1 does not provide sufficient detail in which to make an assessment as to whether this is the case.

**QMC** - the proposed framework is not acceptable. The Undertaking should commit QR to uncouple the access and haulage components of existing freight agreements, to be overseen by the QCA. The terms of operating agreements between Network Access and Coal and Mainline Freight should be reviewed in the event of contestability of coal and minerals haulage.

**MIM** - the fundamental terms/principles of internal access agreements should be made public, consistent with transparency requirements which are essential to both actual and perceived effectiveness of the ring-fencing arrangements. Existing longer term contracts, or at least those entered into in the past two years, should receive the benefit of the Undertaking approved by the QCA.

**Toll** - it is essential that there be a formal protocol and processes established for negotiating internal access agreements and that, save for pricing issues, those agreements are available for inspection by third-party operators. In addition, the obligations on QR regarding internal access agreements in the Undertaking should be detailed and specific and the Undertaking itself should include a provision that QR is not to hinder or prevent access.

**ARTC** - treatment of both internal and external parties under this Undertaking would instil greater confidence in neutrality in the marketplace than internal negotiations carried out under some different framework. There should also be guidelines regarding QCA reviews of internal access agreements.

**Queensland Government** - the soundness of the proposed framework for establishing internal access agreements is a matter for the QCA to determine.

**Table 16: The appropriate term of internal access agreements for existing train services**

**AMC, FreightCorp, Queensland Government, Stanwell** - internal access rights should be tied to the length of external contracts on the grounds that this would reduce the potential for QR to block third-party entry by holding access rights in excess of its reasonable requirements.

**Toll** - the critical issue is not so much the duration of the contract, but its flexibility.

**RTBU** - strictly limiting access rights to the duration of the end-customer's haulage agreement with QR is strongly opposed, because if it were to be adopted it would lead to uncertainty in the long-term relationships that now exist between rail and many industries.

### *QCA's Analysis*

The QCA believes that the finalisation of internal access agreements for existing train services is an important structural element in the above-rail market in Queensland because of the potential for such agreements to serve as a barrier to third-party entry. Internal access agreements for existing train services have important price and capacity implications:

- they will be relevant in comparison with the terms, including price, on which access is provided to access seekers in the event of potential breaches of ss104(2) and 125(2) of the QCA Act; and
- they could be the source of disputation if access seekers are faced with insufficient capacity.

#### *Proposed timetable for establishing internal access agreements (Schedule A)*

The QCA has decided not to endorse QR's proposed timetable because it forms part of an approach that could see below-rail capacity being locked-in by QR above-rail business groups for long periods.

The QCA has proposed an alternative approach for establishing internal access agreements for existing train services, including allowing transitional arrangements for QR and its customers where there are no existing external rail haulage contracts. The QCA's proposed approach is discussed in detail below.

#### *Term of internal access agreements*

Stakeholders clearly have concerns about the proposed framework for the development of internal access agreements for existing train services. There appears to be a high expectation that the QCA will play a role in ensuring the agreements are established on a competitively neutral basis in order to protect the integrity of the above-rail market.

However, in practice, this outcome is difficult to deliver in a pre-emptive sense given that most, if not all, of QR's internal access agreements should be negotiated before third-party operators have a meaningful opportunity to negotiate access agreements within the framework provided by the Undertaking. Moreover, the QCA understands that it does not have the power to approve QR's internal access agreements.

#### *Creation and/or extension of access rights for internal access agreements*

The QCA recognises that, in order to protect QR's legitimate business interests, existing commercial agreements should not be undermined or overturned as part of the establishment of internal access agreement terms. As such, the length of any external agreement with customers - private or government - should be the determining factor in setting such terms. QR broadly committed to this principle in its *Principles for Determining Longevity and Rate Review of Internal Access Agreements for Existing Traffics* Discussion Paper.

Nevertheless, the QCA recognises that QR's external contractual arrangements do not underpin all of its traffics. These traffics include general freight, freight forwarding and potentially additional tonnages of bulk commodities that are not covered by an existing contract. This complicates the establishment of internal access agreement terms. QR's proposal to create access rights where there are no existing external contracts and/or to extend access rights beyond the term of existing external contracts raises a number of concerns.

In the QCA's view, QR could use this creation and/or extension of access rights to lock up capacity for periods that extend well beyond existing fixed term contracts with its customers. This would neither be in the interests of those customers who are deprived of a choice of rail operator or access seekers who are faced with a barrier to entry to the above-rail market. Moreover, the effectiveness of an approved Undertaking would be undermined if this were allowed to occur.

In light of this, the QCA is concerned about QR's proposal that, in the absence of external agreements, the term of internal access agreements will be tied to the 'commercially realistic' agreement term. While the QCA considers that the reference to "commercially realistic" is reasonable, the Authority is concerned about the context in which QR uses it. 'Commercially realistic' implies a mutually agreed extension of the access right whereas, in reality, QR would appear to intend determining the length of the extension with little input from customers. Moreover, QR envisages extensions of access rights of between 5 and 10 years.

The QCA considers that QR's intention to create and/or extend access rights could have the effect of transferring the risk of past rollingstock investment decisions onto its customers. The fact that QR has chosen not to support these rollingstock investments with contractual arrangements with customers is a commercial decision on QR's part, albeit one taken in a different environment when there was not the prospect of third-party access applying. However, it can be contrasted with QR's decision to sign all its coal customers to long-term contracts. The QCA is not aware of any constraints on QR concluding commercial agreements with its customers if both parties wish to do so and QR is not disadvantaged in this regard compared to a third-party operator. Indeed, a sunk investment in rollingstock may result in QR enjoying a distinct commercial advantage relative to competitors.

It should also be remembered that QR has had a lengthy period in which to prepare for third-party entry on its network.<sup>51</sup> In April 1995, all Australian Governments signed the Competition Principles Agreement and QR's rail-transportation infrastructure was subsequently declared for third-party access purposes in March 1998.<sup>52</sup> Consequently, QR's past investment decisions and business plans should not be a major consideration in setting the term of internal access agreements.

The QCA does not accept QR's argument that cl 6.4 provides an adequate safeguard to prevent internal operators from tying up capacity for the purpose of preventing an actual or potential competitor from entering the market.<sup>53</sup> This clause allows Network Access to take back under-utilised capacity at its discretion and consequently raises concerns with equality of application between relevant parties. The QCA's proposed amendments to cl 6.4, discussed in Chapter 6, partially removes Network Access' discretion in this regard, however, in practice, resumption of capacity is likely to be a difficult process, characterised by delays and possibly disputes.

Irrespective of whether legal avenues exist to recover capacity from an existing operator, the QCA considers that it is preferable if the internal access agreement framework established in the Undertaking minimises the likelihood of such an issue arising in the first place. This is because it is in QR's legitimate business interests, the interests of access seekers and also in the public interest, for the negotiation framework in the Undertaking to minimise the need for recourse to dispute resolution.

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<sup>51</sup> Third-party access to essential infrastructure was foreshadowed in August 1993 with the publication of *National Competition Policy*, a Report by the Independent Committee of Inquiry (the Hilmer report).

<sup>52</sup> The declaration was extended in June 1998 with the removal of the exemption on access to coal infrastructure.

<sup>53</sup> Following discussions with the QCA, QR has proposed to replace this clause with an objective test for capacity resumption. Capacity resumption issues are discussed in Chapter 6.

*Principles to guide the setting of internal access agreement terms*

Given the QCA's concerns with QR's proposed approach, the Authority has proposed that the following set of principles should be used to guide the establishment of terms for internal access agreements for existing train services:

- for a service where an external contract with a customer exists, the internal access agreement should be linked to the term of that contract;
- for a service covered by a GSA, the internal access agreement should be linked to the term of that GSA;
- for new tonnages of bulk commodities not covered by an existing contract, the internal access agreement should be linked to the term of the new contract; and
- for general freight and freight-forwarding services, the maximum term for transitional internal access agreements should be two years.

The QCA believes that application of these principles would provide an appropriate balance between QR's legitimate business interests and the interests of access seekers. Nevertheless, the development of internal access agreements for existing services where QR has no existing external contracts with customers – private or government – poses the greatest difficulties in terms of drawing that balance.

The QCA supports constraining internal access agreements to the life of existing external haulage agreements because QR will not necessarily lose that business when the external agreement expires, but rather it will have to compete with potential new entrants for the business. It must be remembered that the central concept underpinning third-party rail access reform is that customers should be able to choose their rail provider, whilst the network owner's legitimate business interests are protected.

The QCA accepts QR's proposal that where a GSA funds a service, the term of the internal access agreement should be equivalent to the GSA term. There are currently three transport-service contracts between the Queensland Government and QR. These contracts relate to the provision of Citytrain urban passenger services, Traveltrain long-distance passenger services and below-rail infrastructure maintenance (for the CSO lines across QR's network). A transport service contract for general freight services is currently being negotiated.

Subject to these GSA agreements, the purpose of the transitional two year term for internal access agreements for existing general freight and freight forwarding services would be to recognise QR's past commitments, financial or otherwise, made on behalf of its customers. As discussed in the previous section, the QCA has doubts about some of QR's arguments regarding these commitments, however, the Authority recognises that there are practical difficulties in accurately estimating their size.

For long distance passenger services, it seems reasonable that the term of internal access agreements reflect the commitment QR has made to its customers in terms of lead times for bookings. As indicated by QR, this lead-time could be assumed to be 18 months at a maximum.

For freight and freight-forwarding services, QR's commitments to its customers, if any, are likely to be less tangible than, for example, forward passenger bookings. In the absence of external agreements with customers, it is difficult to determine an appropriate maximum term for internal access agreements for this type of services.

Nevertheless, the QCA believes that the likely time it would take for a third-party operator to develop a business case, gain finance, make the necessary investments – in rollingstock etc – and commence its train services should be an important consideration in establishing a transitional term for internal access agreements. This is because if the term of the internal access agreements extends beyond such a period, it effectively serves as a barrier to third-party entry. In light of this, the QCA believes that a period of two years for freight and freight forwarding services would provide a reasonable balance between QR's legitimate business interests and the interest of third-party operators.

It is important to note that during the proposed two year transitional period for the above services, QR's customer base would be free to negotiate with third-party operators regarding contracts that would commence after the two year provisional period ends. This freedom to negotiate within the framework provided by the Undertaking – including end-users buying capacity themselves - is aimed at preventing QR locking in capacity for long periods and effectively restricting third-party entry to the above-rail market. Nevertheless, QR's above-rail business groups would be free during this transitional period to negotiate with end-users for contracts to commence after the transitional internal access agreements expire.

The QCA recognises that the typical relationship between rail operators and customers in sectors such as freight and freight-forwarding is not one of long-term contracts. Rather, demand for these types of train services is generally of a short-term – including ad hoc - nature. This raises the issue of the approach that should apply at the end of the two year transitional period.

The QCA believes that the Undertaking should specify that for existing general freight and freight-forwarding services, once the two year transitional period ends, internal access agreements would be set for a 'commercially realistic term'. The Authority anticipates a commercially realistic term for a particular traffic as being one that reflects, amongst other things, the nature of the traffic, the size and age of the investment in the associated above-rail operation (including rollingstock) and the typical length of agreements in the rail industry for such traffic.

The QCA notes that both s104 of the QCA Act, regarding preferential self-dealing, and the capacity resumption clauses of the Undertaking would apply to such internal agreements. In other words, if Network Access negotiated an access agreement with an above-rail business group on more favourable terms - including price and the nature and quality of the service, including term – than provided to a third-party operator, s104 of the QCA Act would apply. In addition, if QR allocated a greater amount of capacity to its above-rail business groups than was required to deliver their train services, the proposed capacity resumption procedures in the Undertaking could be triggered by a third-party operator. Capacity resumption is discussed in section 6.6 of Chapter 6.

#### ***QCA's Position***

##### **The QCA would favourably consider an Undertaking that:**

- **inserted a clause to reflect that in developing internal access agreements for existing train services, the term of internal access agreements be the same as the term of the relevant external agreement between QR and its private and government customers;**
- **for general freight and freight forwarding services, applied a maximum transitional term of two years for internal access agreements unless there is a longer external agreement in place, and following this**

**transitional period provided that internal access agreements would be set for a commercially realistic term;**

- **for new tonnages of bulk commodities not covered by an existing contract, the internal access agreement should be linked to the term of the new contract.**

**The two year transitional period would start from the date of release of the QCA’s Final Decision on QR’s Undertaking.**

### **3.7.2 Rate review provisions in internal access agreements for existing marginal traffics**

#### ***QR’s Position***

In its discussion paper, QR addressed the following concerns about long-term internal access agreements for marginal traffics:

- capacity could be tied up which might subsequently be sought by third-party operators willing to make a greater contribution towards common costs;
- QR could commit to access charges covering only marginal costs for a significant period; and
- the inclusion of a rate review clause in internal access agreements for marginal traffics could enable QR, at a future time, to increase the applicable access charge in response to competition for the capacity from traffics willing to pay a higher access charge.

QR noted that the pricing principles in Part 5 of the Draft Undertaking recognise that, provided marginal traffics pay the incremental cost of their access and contribute towards fixed costs, they enhance the efficient utilisation of the network. However, this depended upon the opportunity costs such traffics impose on the system. The constrained market pricing approach QR proposed to adopt accommodates such traffic by enabling Network Access to charge them an access price at or near the floor price. In other words, Network Access has scope to price access, between the floor and ceiling constraints, at a level that reflects a traffic’s ability to pay.

QR argued it would generally be ineffective to charge a marginal traffic a premium to reflect the risk that another traffic, able to make a greater contribution towards common costs, would come along during the course of the access agreement and would not be able to get capacity. QR’s view was that Network Access risks forcing marginal traffics to use alternative means of transport, not simply by pricing access above what those traffics can afford to pay, but also by only committing to provide access for a short period of time or only with unacceptable rate review provisions.

QR considered that its proposal to limit the length of access agreements for existing marginal traffics in congested areas of the network to five years, would satisfactorily address this issue without creating uncertainty and disincentives for the traffic in question. It did not propose to include a pro-forma rate review provision in internal access agreements for existing marginal traffics. Its arguments in support of this position were:

- given that a marginal traffic’s access charge mirrors its ability to pay - according to QR’s proposed pricing principles - a rate review clause linked to a demand from traffic able to

pay a higher access charge would, in effect, equate to a termination of the access agreement for the marginal traffic. As a marginal traffic would be unlikely to be able to pay a higher charge, a rate review clause would constitute a disincentive for marginal traffics to use rail transport;

- if the relevant demand came from another marginal traffic wishing to directly compete with the existing traffic, it is unlikely the new traffic would be able to pay a higher access charge than the existing operator. If it could, Network Access could assume that the traffic in question or, more accurately, the market in which the traffic operates, has enhanced its ability to pay. Consequently, the existing traffic's access charge could legitimately be varied to reflect this improved ability to pay. QR considered that a clause incorporating such a rate review would not create the same disincentive that a rate review clause linked to demand from a traffic with a greater ability to pay would. However, QR noted that such a clause would likely be strongly resisted by any rail operator, as the review would mean that the applicable access charge could only ever go up;
- if the relevant demand came from another traffic wishing to directly compete with the existing traffic, but that new traffic could not pay a higher access charge than that being paid by the existing traffic, Network Access would gain nothing by replacing one rail operator with another. If the new traffic travelled over a greater distance than the existing traffic, and in this way, paid a higher total access charge, QR would need to balance the benefits of that additional revenue against the effects of greater capacity usage by the new traffic. QR considered that it is unlikely the new traffic would bring any noticeable benefits to the network as a whole, particularly if it was seeking to directly compete with, and potentially replace, the existing traffic; and
- QR considered the argument that users of rail infrastructure would be better off sharing the infrastructure with traffics that can pay a greater contribution towards common costs than a marginal traffic has flaws. In particular, it assumed that one type of traffic could be directly compared with another in terms of capacity impacts upon other users. For example, it was highly unlikely that two mutually exclusive traffics would have the same origins and destinations. Even assuming they did, in a non-commercial area of QR's network, if a traffic paying a higher contribution towards common costs came onto the infrastructure, in all likelihood the access charges paid by existing traffics would not decrease because the extra revenue earned by QR would go back to Queensland Transport in the form of decreased GSA funding. In a commercial area of QR's network, if a traffic paying a higher contribution came onto the infrastructure, the access charges paid by existing traffics would only go down if those traffics were paying access charges at the ceiling of the pricing limits. If QR were not in danger of exceeding its revenue cap, it would not necessarily decrease the access charges paid by existing traffics.

The above arguments assume there is insufficient capacity for both a marginal and potentially higher paying traffic to obtain access rights. If there is sufficient capacity for both to operate and para 4.1.2(d) does not apply, Network Access would proceed to negotiate access in accordance with the Undertaking.

QR did not propose to include rate review clauses in internal access agreements for traffics subject to a reference tariff.

### ***Stakeholder Comment***

Stakeholders have not had the opportunity to comment on QR's discussion paper regarding internal access agreements. Nevertheless, stakeholders have previously commented on whether a new rail operator, who is prepared to make a greater contribution to common costs, should

gain priority over a current user who is given the opportunity to match a newcomer's contribution but declines to do so.

**Table 17: Payment of access charges by marginal traffics**

**AMC, Stanwell** - a newcomer who is prepared to make a greater contribution to the common costs should gain priority over a current user who does not wish to match the newcomers' contribution to common costs.

**FreightCorp** - the Undertaking needs to provide for two conflicting objectives in the best way possible: the need for certainty for existing operators; and the need to provide operators with a reasonable opportunity to enter or at least compete for a particular market. The most appropriate way of managing these conflicting objectives would be through a process whereby specific review periods made all capacity available. A capacity allocation procedure could then be implemented. If additional capacity was required outside that time, it should be provided by taking advantage of the flexibility in pathing that would be provided by allocating capacity rather than paths.

**QMC** - the access contracts covering less than fully costed traffic should be responsive and short-term, eg. one year, to guard against the locking up of capacity for extended periods.

**Queensland Government** - if QR has entered into an agreement for a specific slot, the contract should naturally be honoured. If the previous contract makes specific provision for such circumstances, and imposes commensurately lower access charges, adjustments of priority would be reasonable. However, as a general principle, where QR unilaterally seeks to reduce a user's rights - where no contractual agreement exists - adequate compensation must be provided for.

***QCA's analysis***

The QCA is concerned to ensure that QR does not tie up capacity for long periods with its marginal above-rail traffics, thereby preventing new entrants who could make a greater contribution to common costs from gaining access. However, it also recognises QR's concerns regarding contractual certainty for rail operators.

As discussed in section 3.6.1 of this chapter, the QCA considers that the term of an internal access agreement should be the same as the term of any corresponding external agreement with end-users, with the exception of freight forwarding traffic, long distance passenger services and services covered by a GSA. Under this approach, the problem of a marginal traffic tying up capacity would be reduced when it is a case of direct competition for the same traffic, as the end-user would choose its preferred operator if/when its contract with QR was due for renewal.

QR outlined a number of arguments against having a rate review clause in internal access agreements. The QCA has the following concerns:

- while QR argued that two traffics cannot be compared in terms of their capacity effects upon other users, this type of capacity assessment and allocation of priority is a core function of a network manager and, where priority in scheduling is linked to access charges, would reflect a more efficient utilisation of the network;
- QR argued that for a non-commercial area of its network, the addition of a traffic able to make a greater contribution to common costs may not result in lower access charges for other traffic, however, it may result in a reduction in the amount of government funding required. QR did not recognise that this in itself would be a public interest benefit in terms of the achievement of a more efficient allocation of resources;
- QR's argument that where a third-party operator's traffic wishes to directly compete with the existing marginal traffic and pay a higher access charge, Network Access could legitimately increase the access charge of the existing traffic, could be interpreted as QR

seeking to capture the third-party operator’s superior efficiency in the form of a higher access charge;

- QR’s argument that, where the third-party operator cannot pay a higher access charge, Network Access would gain nothing by replacing one rail operator with another, ignores the key issue that end-users should be able to choose which rail operator best meets their needs; and
- QR’s argument about the dangers of overriding existing access entitlements has validity, however, it would appear that QR’s existing integrated services only have implicit access rights attached and the argument is inconsistent with QR reserving the right to reschedule train operations.

In light of the above concerns, the QCA believes that the issue of marginal traffics tying up capacity for long periods would be better addressed by linking access charges to priority rather than through rate review clauses in internal access agreements. In other words, traffic willing to pay more for a higher priority path would gain precedence in scheduling over a marginal traffic.

This would be in both end-users’ and QR’s legitimate business interests as it would provide greater flexibility and choice to end-users and it would encourage more efficient utilisation of QR’s network through allocation of scarce capacity to those traffics willing to pay more. An existing rail operator would have an opportunity to match another operator’s higher proposed access charge in order to retain priority.<sup>54</sup>

***QCA’s Position***

**The QCA accepts that there should be not be a rate review clause in internal access agreements.**

### **3.7.3 Proposed framework for establishing internal access agreements for new or renewed train services**

***QR’s Position***

The access rights of internal access agreements for new or renewed services will be developed on a basis consistent with the principles outlined in Schedule E (Summary of Standard Access Agreement), Part 5 (Pricing Principles), Part 6 (Capacity Entitlements) and Part 7 (Interface Standards) of the Undertaking: sub-cl 3.4.2(a). However, QR argued in its Explanatory Guide that these obligations do not preclude QR taking advantage of any synergies that arise due to its vertically integrated status, provided this does not lead to a breach of s104 of the QCA Act.<sup>55</sup>

These internal access agreements will be made available to the QCA for review if required: sub-cl 3.4.2(b).

QR argued in its supplementary submission to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking* that as a matter of principle, it did not consider that it would be appropriate to have some, but not all, access agreements subject to mandatory

<sup>54</sup> The issue of linking access charges to priority is addressed in Chapters 5 and 9 and later in this chapter.

<sup>55</sup> The assignment of the benefits of QR’s vertical integration is discussed in section 5.4.2 of Chapter 5 and later in this Chapter.

disclosure arrangements. This was on the grounds that those rail operators - internal or otherwise - whose agreements were disclosed would be at a competitive disadvantage.

In addition, in QR's view, it would not be desirable to subject all access agreements to public disclosure requirements. The requirement for such disclosure would likely inhibit innovation in operational and/or technical matters, as rail operators would not be able to keep these details confidential. This could inhibit investment. In addition, disclosure of only select provisions of access agreements, such as price, would fail to provide access seekers with any meaningful information concerning the appropriateness of price levels.

QR argued in its supplementary submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*, that the QCA Act gives the QCA the power to review internal access arrangements to ensure that QR is not providing better terms and conditions to its own above-rail business groups than is offered to third-party operators. The Draft Undertaking supplements this by providing that these internal access agreements will be made available to the QCA for review if the QCA so requires. QR considered that this review mechanism should provide stakeholders with comfort that QR's above-rail business groups do not gain more favourable access terms and conditions.

The existence of reference tariffs and standard terms and conditions of access agreements, at the principle level, should also address any concerns of third-party operators.

### ***Stakeholder comment***

There was a range of views among stakeholders regarding QR's proposed framework for internal access agreements for new or renewed train services.

#### **Table 18: Internal access agreements for new train services**

**FreightCorp, QMC** - a QCA review of the internal access agreements should provide sufficient protection of access seekers' interests.

**Queensland Government** - the proposed framework appears reasonable.

**Stanwell** - there would appear no good reason why internal access agreements are not public. If the key elements of these agreements are not made public, allowing scrutiny only by the QCA may not provide the level of transparency which would be desirable in an effective Undertaking.

**AMC** - pricing is the key issue in the internal access agreements, secret internal arrangements provide an opportunity for an inappropriate allocation of common costs. This problem would be alleviated through greater transparency and by insisting that internal access agreements be on the public record and remain consistent with the Undertaking in all respects.

**Toll** - there should be an absolute requirement that internal access agreements are on substantially the same terms and conditions as corresponding external access agreements and that the terms contained in the internal access agreements are no more favourable than those offered to third-party operators. There should be a binding mechanism contained in the regime for a review/audit of internal access agreements. The QCA should have the power to require variations to such agreements insofar as the auditor finds them not to be substantially similar to corresponding external access agreements.

**Queensland Government** - the Undertaking should include formal arrangements in respect of the QCA's power to approve/disapprove any internal access agreements.

**Great Southern Railway** - arrangements need to be put in place for an effective review of internal access agreements given that the provisions of s104 of the QCA Act seem to render the ability of the QCA to review internal access agreements ineffective.

### *QCA's Analysis*

The QCA recognises that the confidence of access seekers in QR's access regime will depend to a considerable extent on the market's confidence that third-party operators obtain access on a non-discriminatory basis when compared to QR's above-rail business groups. As such, the nature and extent of disclosure of the internal access agreements for new train services requires a careful balancing of QR's legitimate business interests and the interests of access seekers.

The QCA believes that transparency in the nature of internal access agreements for new train services could be facilitated through one or a combination of the following mechanisms:

- exposure to legal action under s104 of the QCA Act;
- public disclosure;
- a QCA review process; or
- greater use of reference tariffs.

#### *Exposure to legal action under s104 of the QCA Act*

The Authority does not intend to approve sub-cl 3.4.2 because it would mean that internal access agreements negotiated in accordance with it would be brought within the 'safe harbour' of the Undertaking such that s104 of the QCA Act does not apply. As discussed in relation to internal access agreements for existing services, the risk of agreements negotiated in this way leading to breaches of s104 of the QCA Act is too high. Consequently, internal access agreements for new train services will be relevant to the terms on which access is provided to other access seekers/users in the context of potential future s104 actions.

#### *Public disclosure*

The QCA recognises QR's argument that it may not be desirable for all access agreements to be publicly disclosed and that in light of this, public disclosure of only QR's internal access agreements would likely be contrary to QR's legitimate business interests. This is because third-party operators would have access to potentially sensitive commercial information belonging to QR's above-rail business groups. The QCA is concerned that an approved Undertaking should not distort the development of competition in the above-rail market by establishing a framework that delivers an advantage to either QR's above-rail business groups or third-party operators.

Nevertheless, the QCA is aware that QMC, the representative body of one of QR's biggest customers, the Queensland coal mining sector, has argued that the below-rail component of all new access agreements – internal and external – in the coal sector should be publicly disclosed. In other words, the access charge and non-price terms and conditions negotiated between Network Access and the rail operator should be publicly disclosed. QMC has argued that such disclosure would enhance price transparency and preclude Network Access negotiating special 'deals' on non-price terms and conditions.

The QCA agrees with QMC's argument to the extent that it is just the below-rail component of access agreements that would be disclosed. The QCA accepts that such disclosure is not standard practice in the Australian rail sector, however, it believes that QR's legitimate interests would not be adversely affected by such disclosure. The publication of below-rail aspects of access agreements would provide information on negotiated departures from the reference tariff rates and negotiated non-price terms and conditions.

Nevertheless, the QCA recognises that this approach could lead to standardisation of, or rigidity in, access agreements for the coal sector, including Network Access feeling constrained in its negotiations with rail operators. The consequence of this would be that Network Access becomes unwilling to accommodate the particular concerns of individual rail operators. However, the coal mines would bear the inconvenience and cost of this inflexibility. In their view, the positive effects of complete transparency in access agreements – for example, enhanced competitiveness of the above-rail market – would outweigh the detrimental effect of Network Access’ reduced ability to tailor arrangements to individual rail operators.

Notwithstanding the above arguments, the QCA would not support above-rail aspects of agreements being disclosed, on the grounds that more efficient rail operators could be forced to disclose information that would reveal the source of their greater efficiency to other rail operators. The likely impact of disclosure over time would be to stymie innovation in above-rail operations.

In light of QMC’s strong representations on behalf of the Queensland mining sector, the QCA has proposed that Network Access should allow for the disclosure of all below-rail aspects of rail access agreements for the coal sector.

At this stage, the QCA does not believe that public disclosure of below-rail aspects of access agreements in other sectors is warranted. There has been no support from stakeholders for such a move.<sup>56</sup>

#### *A QCA review process*

The QCA accepts QR’s proposal to make its internal access agreements for train services in non-coal sectors available to the Authority for review. The QCA believes that this review mechanism should provide stakeholders with some comfort that QR’s above-rail business groups do not gain more favourable access terms and conditions. However, the QCA notes that it will not have the power to intervene with respect to QR’s internal arrangements. In addition, the QCA has little control over the way in which Network Access exercises discretionary rights under its contracts in a way that favours a particular operator.

The QCA understands that it does not have the power to approve internal access agreements or to require variations to internal access agreements. Consequently, these avenues have not been explored. Nevertheless, the Authority understands that QR’s internal access arrangements will be relevant as a comparison to the terms on which access is provided to other access seekers and users under ss104(2) and ss125(2) of the QCA Act.

#### *Greater use of reference tariffs*

The QCA believes that internal access agreements for new train services should be treated differently depending on whether they are developed in accordance with QCA-approved price

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<sup>56</sup> Toll has informally advised the QCA that it is strongly opposed to such public disclosure. It argued that each operator will, subject to the terms of the QCA Act and the Undertaking, be free to negotiate terms suitable to its own business, operations and customer requirements. Some flexibility is required to allow Network Access to negotiate appropriate terms. If access agreements are on public display, Network Access will naturally be very cautious about departing from the published terms for fear of criticism. This could stifle reasonable commercial requirements and innovation. In effect, the first access agreement will create the standard for all future agreements. National Rail informally advised the QCA that when access charges are publicly disclosed, provision needs to be made for at least some non-price terms and conditions to remain confidential, if this is desired by one or both parties. For example, an access agreement may include arrangements for new services, or other improvements, which an operator may not want revealed to its competitors.

and non-price terms and conditions. Specifically, internal access agreements for new train services developed in accordance with approved reference tariffs and a proposed standard access agreement applicable for coal haulage services, should be deemed to comply with s104 of the QCA Act.<sup>57</sup> This would provide an incentive for QR to negotiate agreements with its above-rail business groups in accordance with approved reference tariffs. Moreover, the development of reference tariffs, by increasing price transparency would, over time, constrain QR's ability to provide access to its own above-rail business groups on more favourable terms and conditions than third-party operators.

At this stage, QR has proposed that reference tariffs be developed only for its coal systems, however, the potential exists for reference tariffs to be developed for other parts of QR's network, such as the Mt Isa and North Coast Lines. The development of additional reference tariffs is discussed in Chapter 5.

Finally, the QCA notes QR's statement in the Explanatory Guide that it would take advantage of any synergies that arise due to its vertically integrated status, provided this does not lead to a breach of s104 of the QCA Act. QR's initial submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* did not deal with exactly how the benefits of integration - to the extent they exist - will be passed on to customers through cheaper prices and better service quality.

The QCA recognises the potential synergies from vertical integration in a theoretical sense, however, it is very difficult to quantify these synergies in practice. As part of its assessment of QR's reference tariffs, the QCA has undertaken a significant cost allocation exercise for QR's coal systems. As a result of this exercise, the QCA does not believe that the synergies are material. Indeed, one of the most significant benefits to QR from its current structure is the economy of scale arising from the reduced transaction costs of negotiating multiple access agreements at once. Consequently, the QCA proposes that QR's Undertaking does not need to address potential synergies from vertical integration.<sup>58</sup>

#### *QCA's Position*

**The QCA would favourably consider an Undertaking that:**

- **removed sub-clause 3.4.2 of the Draft Undertaking;**
- **following completion of the development of a standard access agreement for coal haulage services, provided for internal access agreements for new or renewed train services developed in accordance with that standard agreement and approved reference tariffs to not be subject to s104 of the QCA Act;**
- **allowed for the disclosure of all below-rail aspects of rail access agreements in the coal mining sector; and**
- **provided its internal access agreements for non-coal train services to the Authority for review.**

<sup>57</sup> QMC has advised the QCA that it intends negotiating a standard access agreement with QR to apply for coal haulage services.

<sup>58</sup> The cost allocation issue is discussed in Chapter 5 as part of the development of QR's Costing Manual.

## CHAPTER 4. NEGOTIATION FRAMEWORK

### KEY ASPECTS

**Vertical integration** - QR's vertical integration gives rise to a conflict of interest if access seekers are required to negotiate access with QR's above-rail business groups and then compete with them. An effective negotiation framework requires that Network Access alone must negotiate with access seekers regarding declared services.

**Rail infrastructure** - principles to guide the assignment of management responsibility for QR's rail infrastructure and associated line diagrams should be incorporated as a schedule to the Undertaking.

**Parties to access agreements** - both accredited and non-accredited organisations should be able to execute access agreements with QR, provided an appropriately accredited rail operator delivers the train services.

**Schedule D** - should include detailed cost information where no reference tariffs apply and where requested by access seekers. Schedule D does not limit QR's statutory obligation to provide information to access seekers - in particular, information associated with QR's capacity assessments.

**Dispute resolution** - the Undertaking should not limit the right of an access seeker to trigger dispute resolution with respect to indicative access proposals.

## 4.1 Introduction

Under the QCA Act, commercial negotiation is to play a central role in the securing of third-party access by an access seeker. Commercial negotiation is particularly important in the context of access to rail infrastructure due to the varying nature of the service required by a user, including frequency and timeliness. This requires an effective negotiation framework be established.

The QCA believes that if QR is to establish such a negotiation framework, a fundamental principle underpinning the assignment of management responsibility for QR's rail infrastructure is that Network Access alone must negotiate with access seekers. This is because, under QR's vertically integrated structure, an access seeker has to both negotiate access to declared services and, if successful, potentially compete with QR's above-rail business groups.

The QCA is strongly of the view that access seekers should not be expected to negotiate with potential competitors regarding any declared services. This is because the inherent conflict of interest would have the potential to seriously undermine the development of a contestable above-rail market in Queensland.

Key features of an effective negotiation framework include:

- provision of adequate information to access seekers in a timely manner;
- clearly defined negotiation procedures, including time frames for action by QR;
- clearly defined boundaries to negotiation;
- effective dispute-resolution procedures, including fair and timely resolution of disputes; and
- clarification of the respective responsibilities of QR and access seekers concerning the negotiation process.

A negotiation framework that omits or insufficiently develops any of the above features may become a barrier to entry to access seekers. On the other hand, QR is entitled to protect itself against becoming engaged in negotiations with non-genuine access seekers. Therefore, one of the key objectives of the negotiation framework must be to strike a balance between QR's legitimate business interests and the interests of access seekers.

## 4.2 Management responsibility for QR's infrastructure

The Draft Undertaking identifies the parties within QR who will be responsible for access negotiations. This will depend on whether Network Access or one of QR's other business groups is managing the facility providing the declared services. QR subsequently developed a 'common user' test that was designed to assign management responsibility for its rail infrastructure to each of its business groups in a complete and unambiguous manner. The business group assigned management responsibility for a facility would be responsible for negotiating access to its associated declared services, if any.

The QCA and QR's stakeholders had significant concerns about the practical effects of applying the common user test. Access seekers could potentially be required to negotiate access to declared services with QR's above-rail business groups. As a result, the QCA, in consultation with QR, developed principles to guide the assignment of management responsibility for QR's rail infrastructure. QR has subsequently prepared line diagrams for its infrastructure from Gladstone northwards reflecting the application of these principles. The QCA has proposed that

subject to stakeholder comment and the resolution of one unresolved assignment, these line diagrams be incorporated as a schedule to the Undertaking.

### ***QR's Position***

#### *Original position*

Negotiation for access with third-party operators will be undertaken by Network Access. The only exception to this is where access is required for below-rail services provided by a facility managed by a business group other than Network Access. In that case, Network Access will conduct access negotiations as an agent for the business group managing the facility: para 4.1.1(a).

The only exception to this arrangements is if the third-party operator's sole purpose of gaining access to a station, platform or marshalling yard is to utilise another above-rail facility managed by an above-rail business group, such as a workshop or terminal. In that case, negotiation will be directly between the third-party operator and that business group: para 4.1.1(b).

QR's proposed assignment of management responsibility for its rail transport infrastructure raises two key matters:

- the scope of the declaration of the rail transportation services provided by its infrastructure for third-party access purposes; and
- the appropriateness of a 'common user' test, foreshadowed in QR's supplementary submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*, as a means of assigning management responsibility for its infrastructure.

QR argued in its submission in response to the QCA's Request for Comments Paper *QR's Scheduling and Train Control Protocols and Proposed Assignment of Marshalling Yards* that there is a lack of clarity over precisely which of QR's assets fall into the definition of rail transport infrastructure in the *Transport Infrastructure Act 1994*. The most obvious example is the delineation of marshalling yards and items that are defined as other rail infrastructure, such as the railway track that is part of freight centres or depots, maintenance depots and workshops.

The declaration refers to the use of rail transport infrastructure for providing transportation by rail. However, neither the TI Act nor the declaration provides any definition of what activities are encompassed by the term *transportation by rail*. QR considered transportation by rail included the following functions:

- mainline running between the train's loading point and its unloading point, including the empty return trip if required;
- any queuing or staging that is reasonably required in the movement of the train from its loading point to its unloading point, including the empty return trip if required; and
- any train marshalling or shunting that is reasonably required in the movement of the train into/out of its loading or unloading point, including the empty return trip if required, where the relevant loading or unloading facility cannot accommodate such marshalling or shunting.

QR would provide a certain amount of 'bad order' or 'breakdown' sidings that may be utilised by all railway operators in emergency situations.

QR indicated the declaration did not oblige it to provide sufficient rail transport infrastructure to accommodate a railway operator's rollingstock at times when it is not being used for the purpose of providing transportation by rail. For example, whilst it is being maintained, or whilst it is being stored. In its view, this interpretation was supported by the definition of rail transport infrastructure that specifically excluded maintenance facilities and freight terminals.<sup>59</sup>

QR may permit railway operators to perform provisioning and running inspections whilst on track managed by Network Access subject to sufficient capacity being available for such activities. Where this occurs, it would be treated as a non-declared service provided by Network Access and the third-party operator's access charge would reflect this additional utilisation of QR's network capacity.

#### *Revised position*

In September 2000, QR wrote to the QCA advising of a change in its position. It argued that there needed to be a distinction drawn between the short and long-term rollingstock storage services provided by its rail infrastructure. QR proposed to use the term *stowage* for short-term storage, which formed part of the declared service and would be provided by Network Access. On the other hand, QR proposed to use the term *storage* for long-term storage, which did not form part of the declared service and would be the responsibility of above-rail operators.

QR defined stowage as the short-term storage of train consists on the rail transport infrastructure for the purpose of:

- enabling an operator to carry out scheduled above-rail services normally carried out during a scheduled operational cycle (such as crew changes, meal breaks, and provisioning) and/or;
- providing an operator with a place to temporarily store its trains;
- between scheduled train services in accordance with the terms of the relevant operator's capacity entitlement; or
- when the operator cannot operate its train service in accordance with the terms of its capacity entitlement as the result of a breakdown situation or temporary outage of the operator, the loading facility or the unloading facility, and/or unavailability of the rail transport infrastructure.

In addition to long-term storage of train consists, QR argued that storage referred to:

- short-term storage of train consists where a rail operator does not operate train services in accordance with its capacity entitlement; or
- storage of wagons for seasonal traffic in the 'off-season'; or
- storage of wagons destined for maintenance; or
- storage of rollingstock or train consists no longer in use.

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<sup>59</sup> 'Freight centres or depots' rather than 'freight terminals' are defined as 'other rail infrastructure' in the TI Act. 'Other rail infrastructure' is not covered by the declaration of QR's rail transport infrastructure.

QR argued that storage of train consists where a rail operator chose not to use its allocated train paths was included because in such circumstances the train consist storage was unplanned and at the discretion of the operator. Consequently, it was appropriate that the operator be required to find a location to store its train consist.

#### *Common user test*

In its supplementary submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*, QR foreshadowed a significant change to the treatment of marshalling yards. This amended approach was clarified in its submission to the QCA on the Definition of Common User Yards. Essentially, QR's revised approach involved an assessment of each of its marshalling yards (yards) with a view to identifying the areas within each yard that provide declared services and those that do not.

QR noted that there are areas within yards, which may involve one or two 'roads', that may be required by a number of operators in order to effectively utilise the mainline corridor or in circumstances where a number of above-rail facilities exist in the same vicinity. QR proposed that these yards be called common user yards and be assigned to Network Access. Network Access would directly negotiate with third-party operators for access to common user yards in accordance with QR's Draft Undertaking.

In contrast, QR argued that a single above-rail business group often exclusively uses particular areas within yards for the performance of above-rail functions, such as train storage, provisioning, maintenance or activities at freight terminals. This use is generally dictated by that operator's ownership of facilities - such as terminals or maintenance facilities - adjacent to those yard areas and the yard areas are currently solely used in conjunction with those facilities. QR argued that there is no legitimate need for these yards to be made available for access by other operators and therefore should be reserved for the exclusive use of that QR above-rail business group as opposed to being available for third-party access.<sup>60</sup> QR proposed that these yards be assigned to above-rail business groups and that the Undertaking **not** apply to them.<sup>61</sup>

QR completed a review of its entire rail infrastructure network, including marshalling yards, around mid 2000. The review was conducted in two stages – rail infrastructure from Gladstone northwards, and rail infrastructure south of Gladstone. QR prepared a series of line diagrams indicating its proposed assignment of management responsibility for its infrastructure. The line diagrams for infrastructure from Gladstone northwards were subject to consultation with stakeholders through the QCA's Request for Comments Paper *QR's Scheduling and Train Control Protocols and Proposed Assignment of Marshalling Yards*. QR has advised that the line diagrams for rail infrastructure south of Gladstone will be provided to the QCA during the consultation period for the Draft Decision.

QR's proposed assignment of management responsibility for its rail infrastructure is summarised in Table 1 below.

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<sup>60</sup> Third-party operators could seek access to such infrastructure via a commercial arrangement with the QR above-rail business group that manages that facility. For example, a third-party operator could enter a commercial service agreement with QR where QR maintains that operator's rollingstock in a QR maintenance facility, or loads and unloads its trains at a QR freight terminal.

<sup>61</sup> It is clear that declared services need not be subject to an undertaking although the QCA is empowered under the QCA Act to request an undertaking from an access provider in relation to the provision of declared services. If access is sought to declared services not covered by an undertaking, the arbitration machinery contained in the QCA Act would be available. This means that third-party access to the declared services provided by these facilities is still available irrespective of QR's assignment of management responsibility to its above-rail business groups.

**Table 1: Proposed Assignment of Management Responsibility**

Infrastructure/Facility Type	Management Responsibility
Mainlines and passing loops	Network Access
Container terminals and associated storage yards	Relevant QR above-rail business group/private owner (if private)
Major coal loading/unloading terminals	Network Access/private owner (if private)
Major mineral loading/unloading terminals	Network Access/private owner (if private)
All other loading/unloading terminals	Relevant QR above-rail business group/private owner (if private)
Private sidings	Private owner
Queuing facilities associated with a loading/unloading terminal/facility	Manager of the loading/unloading terminal/facility (for coal and minerals this will be Network Access)
Sections of yards used for access to private sidings (including any associated requirements for marshalling trains)	Network Access
Rollingstock maintenance depots and associated storage yards	Relevant QR above-rail business group
Infrastructure maintenance depots	QR Infrastructure Services Group
Workshops and associated storage yards	QR Workshops Group
Storage facilities/yards other than those associated with workshops, depots or terminals	Relevant QR above-rail business group

Source: QR Submission

#### *Application of common user test*

QR advised the QCA that the common user test has been applied as follows:

- all infrastructure used for the purpose of mainline running, including passing loops, is managed by Network Access and will be subject to access in accordance with the terms of the Undertaking;
- Network Access will manage infrastructure to provide for any queuing or staging reasonably required in the movement of the train from its loading point to its unloading point including the empty return trip if required. Consequently, for those yards close to major loading/unloading facilities and for which there is likely to be a requirement for queuing over and above what can occur in facilities owned by the relevant railway operator(s), extra holding roads for queuing and coordination of train movements are under the management of Network Access;<sup>62</sup>
- Network Access is to manage infrastructure to provide for any train marshalling or shunting reasonably required in the movement of the train into/out of its loading or

<sup>62</sup> These locations are at Callemondah, Jilalan and Mt Isa.

unloading point where the relevant facility cannot accommodate such marshalling or shunting; and

- Network Access will manage infrastructure necessary to provide access to all private sidings - including any necessary marshalling and shunting required to effectively utilise those sidings.

QR has generally not assigned infrastructure to Network Access for the purpose of train loading and unloading, maintenance and train storage, with the exception of major coal and minerals loading and unloading facilities.

QR advised the QCA during Working Group meetings in mid 2000 that the proposed assignment of marshalling yard assets between Network Access and its above-rail business groups reflected internal QR managerial purposes. QR argued that, while it would prefer to align its management of the rail infrastructure with the declared service, such that Network Access is responsible for managing all infrastructure providing declared services, an efficient internal management structure is its priority.

#### *Stakeholder concerns*

The QCA and QR's stakeholders shared concerns about QR's proposed assignment of management responsibility for its infrastructure reflected in the line diagrams referred to above, in particular, the potential for access seekers to be required to negotiate with QR's above-rail business groups for access to declared services.

As a result of these concerns, QR and the QCA engaged in a series of discussions in an attempt to find common ground. To this end, the QCA developed guiding principles for the assignment of management responsibility for QR's rail infrastructure. The principles are discussed in the QCA's analysis section of this chapter below.

QR subsequently agreed to amend its line diagrams using the guiding principles. A complete set of amended line diagrams is at the end of the chapter.

#### *Stakeholder Comment*

Submissions in response to the QCA's Request for Comments Paper *QR's Scheduling and Train Control Protocols and Proposed Assignment of Marshalling Yards* raised a number of concerns regarding the link between marshalling yards and the scope of the rail infrastructure declaration.

#### **Table 2: Scope of declaration**

**Queensland Transport** - the lack of a clear definition in the *Transport Infrastructure Act 1994* of marshalling yards, and in fact other rail infrastructure components such as stations and platforms, presents considerable complexity to the issue of allocation of responsibility for such infrastructure. Nevertheless, all of the functions identified by the QCA as within the scope of the declaration - ie. mainline running, train loading and unloading, marshalling and shunting, and short-term storage for repair and provisioning - are integral to the operation of trains. Accordingly, the view expressed by the QCA that the declaration of the services provided by QR's rail transport infrastructure extends to the use of that infrastructure is generally supported.

**FreightCorp** - the QCA's classification of below-rail functions, with the exception of its exclusion of long-term storage, is supported. To the extent it is a requirement to park trains at various times, part of the service provided by the network is to allow trains to be stabled. QR's intent is that third-party operators are required to build sufficient tracks such that all of their trains are able to completely exit from the QR network. Such a requirement is anti-competitive on the following grounds:

- it is unnecessary from a network management perspective for all of a third-party operator's trains to exit the network;
- it is an integral part of the network service to provide for the storage of trains within the network for bulk haulage trains that exhibit a cyclical unit train nature; and
- the existing infrastructure has been built to accommodate the current level of traffic and has been demonstrated to do so. It is therefore absurd to argue that the change of traffic from one operator to another would cause capacity to require augmentation.

While FreightCorp agrees with QR that some portions of (or potentially entire) facilities may be associated with above-rail activities and should therefore be excluded from declaration, this needs to be considered in context and with great care. In particular, the presence of a facility (eg a provisioning or fuelling facility) adjacent to the rail infrastructure does not necessarily mean that the infrastructure is purely related to above-rail activities. The former non-competitive nature of the rail industry has meant that infrastructure was often built without necessarily taking into account the distinction between above and below-rail activity so that it is quite probable that some facilities will include both.

It is also important to recognise that the separation of activities for the current usage of operations may change if a new operator seeks to undertake its operations in a different manner. QR's integrated structure may lead Network Access to judge all proposals by reference to current standards and operating practices. This predisposes decisions and pricing outcomes towards the status quo, with any innovation likely to be penalised.

**QMC** - QR's common-user approach does not relate to the scope of the Undertaking. Any amendment of the declaration, or limit on the QCA's interpretation of the declaration, to reflect the common-user approach would be opposed. The Undertaking should cover the declared services, including those current and potential rail transport services that the QCA has identified as being provided by QR's marshalling yards.

**ARTC** - the smooth operation of loading, unloading and maintenance aspects of a rail operation has a large influence on the efficiency and effectiveness of the line-haul portion of the service. Constraints in yards and terminals, where space is at a premium and often controlled by incumbent users, is often a greater limiting factor on a desired service than line-haul capacity constraints. Accordingly, the availability of suitable facilities for non-line-haul activities on the QR network will be vital to any access to the network by third-party operators.

Stakeholder submissions supported Network Access managing declared infrastructure. Concerns about the appropriateness of the common-user test were raised.

### **Table 3: Appropriateness of common user test**

**Queensland Transport** - any declared infrastructure should be managed by Network Access including handling all access negotiations with third parties. Management of infrastructure by an above-rail business group should desirably be restricted to infrastructure that is required solely by that group, in effect 'private sidings'.

**Toll** - the common user approach is not appropriate. All marshalling yards should be allocated to Network Access as it is impossible to judge at this stage which - if not all - of QR's marshalling yards might be needed by new operators to provide services to QR's existing customers or to new customers. The marshalling yards are being used by QR now and therefore must be of value in providing services to its current customer base. Therefore, all yards are potentially of value to a third-party operator who may want to offer services to QR customers. There did not appear to be any circumstances that justify the assignment of declared services to QR's above-rail business groups.

**QMC** - the obligation should be on Network Access to explain why the Undertaking should not cover a section of a marshalling yard and included in its sphere of management responsibility. This would involve a reversal of the onus of proof implicit in QR's proposal. A strict application of the declaration that involves assigning all, or almost all, of a marshalling yard to Network Access would not prevent QR's above-rail business groups from using them. It would merely place these business groups on the same footing as third parties needing to acquire access to the yard from Network Access. A failure to assign to Network Access those yard areas providing declared services could have serious deleterious effects on

the emergence of competition as QR's above-rail business group's would not be motivated to provide rival operators with access to these areas at reasonable cost, if at all.

**FreightCorp** - all declared infrastructure should be considered common use unless otherwise proven by QR to be specifically related solely to its above-rail business groups' operations and will always remain so.

We applaud QR's proposal to move all areas identified as common use yards under Network Access' management responsibility. However, it is manifestly strange that such a proposal leads to the outcome that the majority of the coal storage yards at Callemondah, Bluff and Jilalan are quarantined for Coal and Mainline Freight. We struggle to comprehend how any reasonable interpretation of the infrastructure needs of the coal rail haulage business does not lead to the conclusion that the tracks at those locations are required for the management of any and all coal trains using the system and are therefore common use in nature.

**ARTC** - QR appears to have assigned significant parts of many of the larger yards to its above-rail business groups, leaving third-party operator access, via Network Access, to through roads only. This leaves very little future opportunity and flexibility to third parties. Also, the designation within each yard may need to consider as best as possible future usage of the yard.

### ***QCA's Analysis***

#### *Scope of declaration*

The scope of the rail transport infrastructure declaration has been the subject of different interpretations by QR and its stakeholders.

In broad terms, QR narrowly interpreted the declaration, believing it to principally include services provided on an origin-to-destination basis, with the exception of loading and unloading facilities for coal and minerals traffic. In contrast, stakeholders argued the definition included a wide range of functions beyond origin-to-destination running.

The QCA's understanding is that the scope of the declaration extends to the use of QR's rail transport infrastructure for the following rail transport functions:

- mainline running, including the use of passing loops;
- train queuing and staging for the following activities so long as they are undertaken as part of the normal operational cycle:
- loading and unloading;
- transit;
- 'on track' maintenance, provisioning and crewing activities;
- train loading and unloading at facilities other than freight centres and depots, undertaken as part of the normal operational cycle;
- train marshalling and shunting:
- in preparation for transit;
- in preparation before or after train loading or unloading;
- in preparation before or after maintenance and provisioning;

- short-term train storage:
- in a breakdown situation;
- for short periods where product flow has been disrupted;
- for short periods where the timetable does not allow use.

The services provided by facilities that fall within the definition of ‘other rail infrastructure’ in the TI Act, such as freight centres or depots, maintenance facilities, workshops and track that is part of each these facilities, have not been declared. Nevertheless, the use of marshalling yards located near these facilities is subject to the declaration.

Accordingly, whilst the use of a maintenance facility is not subject to the declaration, the use of a marshalling yard that is adjacent to a maintenance facility to break up a train to enable faulty wagons to be separated and transported to another maintenance facility, falls within the range of services that have been declared under the QCA Act.

The QCA believes that the scope of declared services outlined above, which goes beyond the mere facilitation of point-to-point operation of trains to include services such as short-term storage, would be sufficient for a third-party operator to provide an effective train service. In this way, it balances the legitimate business interests of QR and the interests of third-party operators and provides for an efficacious rail access regime to be established.

#### *Appropriateness of common user test*

QR has developed the common user test to assign management responsibility for its entire rail infrastructure. However, it is in the context of marshalling yards that the test raises the greatest sensitivities from a third-party access perspective.

The QCA has a number of concerns with the specification and application of QR’s common user test. These are as follows:

- the existing use of QR’s infrastructure, rather than its potential future use in the context of the rail transport declaration, has dictated the assignment of management responsibility for the infrastructure;
- ease of access to end-user loading/unloading facilities adjoining QR’s rail infrastructure has not been adequately addressed; and
- the test operates at too high a level, which allows QR to exercise considerable discretion in its application. The exercise of this discretion results in a lack of certainty in the outcomes from QR’s assignment process.

As a result of these concerns, the QCA does not believe that the common user test provides sufficient protection of third-party operators’ interests. The QCA’s concerns are explained in more detail below.

**Performance of declared services within marshalling yards** - the QCA’s concern with the lack of an explicit link between the common user test and the rail transport declaration is that it results in areas within yards where above-rail functions are currently performed being reserved

for the *exclusive* use of the relevant above-rail business group.<sup>63</sup> For example, QR advised the QCA that predominantly above-rail activities take place in Callemondah yard - sited close to Gladstone port and the Gladstone Powerhouse Loop on the Blackwater system - and this is why an above-rail business group would manage the majority of the yard.

The QCA believes that marshalling yards, such as Callemondah, potentially provide both declared and non-declared services. The fact that an above-rail business group currently manages such a facility and is the only user of the associated declared services does not affect the fact that the services have been declared and *prima facie* should be assigned to Network Access.

In the future, third-party operators may potentially seek access to the declared services of the yards. Declared services that could potentially be provided by a yard and are likely to be required by third-party operators to deliver an effective rail service include queuing and staging, train marshalling and shunting, and short-term train storage.

For example, the QCA shares stakeholders' concerns that there is a lack of queuing roads for coal trains at Callemondah yard waiting to unload at Gladstone port. Similarly, at Pring yard – sited close to Abbott Point port on the Newlands system - two holding roads have been assigned to above-rail business groups. It is possible that these roads may be needed for queuing or short-term storage at the port, for example, if a cyclone disrupts shipments.

Under QR's common user test, a third-party operator would have to negotiate with an above-rail business group to carry out train inspections and/or train storage within a yard. Such negotiations would occur outside the scope of an approved undertaking. The QCA considers this to be an unacceptable situation because it represents a potential barrier to entry to a third-party operator gaining access to declared services. As discussed in the introduction of this chapter, a fundamental principle underpinning the assignment of management responsibility for QR's rail infrastructure should be that Network Access is the stand-alone provider of declared services.<sup>64</sup>

Furthermore, the QCA believes that the onus should be on QR to demonstrate strong grounds for departing from this fundamental principle. This is because the declaration of QR's services indicates an intention on the part of the Queensland Government that the majority of services provided by marshalling yards should be available for third-party access and be subject to the Undertaking.<sup>65</sup>

Moreover, evidence from other rail jurisdictions supports this position. The rail manager in NSW, RAC, is responsible for multi-user marshalling yards, for example, at Enfield and Chullora. In addition, ARTC owns a yard at Dry Creek in Adelaide that is licensed to Australian Southern Railway on a non-exclusive basis. The QCA believes that full utilisation of existing tracks would be to Network Access' commercial advantage.

**Third-party access to private adjoining infrastructure** - QR's proposed assignment of management responsibility for its rail infrastructure raises a sensitive competition issue associated with third-party access to adjoining infrastructure owned by end-users. For example,

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<sup>63</sup> The only way a third-party operator could gain access to the declared services provided by these facilities would be to negotiate with a QR above-rail business group without the protection offered by the Undertaking.

<sup>64</sup> Failure to take a forward-looking approach may also result in third-party operators being forced to duplicate QR's infrastructure in order to enter the above-rail market. Unnecessary duplication effectively serves as a barrier to entry to the above-rail market and inevitably increases rail haulage costs.

<sup>65</sup> The QCA recognises that there may be grounds for marshalling yards to be allocated to above-rail business groups, including where there is clearly demonstrated surplus marshalling yard capacity or where there is a rationalisation of infrastructure.

private sidings, sugar and grain handling terminals and livestock yards. A potential problem would arise if QR assigns a particular section of track or an area which adjoins other private facilities, such as a private siding, to one of its above-rail business groups. The end-user and/or the third-party operator hauling its product would have to negotiate with that above-rail business group for access to its facility outside of the Undertaking's negotiation framework.

It could be that the above-rail business groups was competing with the third-party operator to haul that end-user's product. Consequently, the above-rail business group would have little incentive to accommodate the third-party operator regarding access to the track it is managing. Assuming the above-rail business group was managing infrastructure that provided declared services, the third-party operator could use the arbitration machinery contained in the QCA Act. However, the time and expense involved in following this path would effectively serve as a barrier to entry to the third-party operator.

The QCA believes that such potential negotiation problems could be minimised if Network Access were to manage all track adjoining private sidings and other end-user facilities. Consequently, the QCA supports QR's commitment that Network Access will manage the infrastructure necessary to provide access to all private sidings, including any necessary marshalling and shunting required to effectively utilise those sidings.<sup>66</sup>

The situation regarding the assignment of management responsibility to track adjoining end-user or joint-use facilities is somewhat more complex. In some cases, because such infrastructure is sited off private sidings, ensuring Network Access manages track adjoining those sidings will mean that access to the end-user facilities is not a problem. However, in other cases, end-user facilities may be sited on QR's track, including that managed by an above-rail business group. Access to such facilities could potentially become a problem.

QR has generally not assigned such track to Network Access with the exception of major coal and minerals loading and unloading facilities. This has resulted in a number of end-user facilities being accessible only via track managed by an above-rail business group. For example, Mareeba Sugar Mill, the gypsum facility at Winton and all livestock yards.

Nevertheless, the QCA recognises that an end-user may have an arrangement with an above-rail business group which owns or leases its facility. Depending on the nature of that arrangement, exclusive use by the one rail operator may be appropriate for the term of the agreement and where such an arrangement does not affect other end-users. Alternatively, an above-rail business group may have a dedicated loading/unloading facility and associated track. In these cases, on operational grounds or because the facility could be easily duplicated, it may be appropriate for the above-rail groups rather than Network Access to manage access to the facilities.

The case of a facility where there is joint use by end-users is more straightforward. Network Access should be assigned management responsibility for such facilities unless they are privately owned. As the above-rail market in Queensland develops, different end-users are likely to have the choice of more than one rail operator. Assigning exclusive management responsibility for such facilities to just one of those rail operators could provide it with a competitive advantage over any other rail operators, for example, because it could manage the facility to suit its own operations.

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<sup>66</sup> The original set of line diagrams prepared by QR for its infrastructure from Gladstone northwards included some adjoining private infrastructure and facilities accessible only by track managed by QR's above-rail business groups. QR subsequently acknowledged such inconsistencies and prepared an amended set of line diagrams.

An example of such a facility would be a minerals or coal-unloading terminal at a port. The QCA supports QR's decision to assign management responsibility for such terminals to Network Access unless they are privately owned. Nevertheless, the QCA considers that a principle addressing access to end-user and joint use facilities is required to provide greater certainty to access seekers. The Authority proposes the principle should be that Network Access should provide access to any end-user's facility not owned or leased by a rail operator and a facility where there is joint use by end-users.

**Guiding principles** - given the limitations of the common user test, the QCA developed a set of principles in respect of QR's assignment of management responsibility for its infrastructure prior to the commencement and once an approved Undertaking is in place. The purpose of the principles is to provide a greater degree of certainty to third-party operators concerning the assignment process than that delivered by the common user test. However, the QCA did not wish to develop principles that hindered dynamic change in the utilisation of QR's rail network, either by QR or third-party operators. This is potentially an important benefit of third-party access.

The QCA recognises that it is very difficult to assign marshalling yards as part of the approval of an Undertaking without at least potentially inhibiting the future operations of third-party operators. This is because properly assigning marshalling yards requires knowledge of the particular operations of many potential third-party operators in relation to traffic tasks that are not yet known. For example, as more third-party operators have entered the above-rail market in NSW, sections of track previously thought to relate exclusively to a particular operator have in fact become integral to the operations of other above-rail operators. Operating patterns have changed and track has been abandoned or bypassed necessitating the reassignment and/or refinement of commercial lease arrangements. Anomalies in assignments have also surfaced.

Consequently, in developing a set of guiding principles for assignment, the QCA has attempted to balance the desirability of providing certainty to third-party operators at the commencement of an approved Undertaking against allowing flexibility in response to future changes in network utilisation. However, the QCA recognises that potential future reassignments could become a source of disputation between QR and third-party operators. Consequently, the QCA proposes to reserve the right to resolve disputes regarding the assignment of management responsibility for QR's infrastructure.<sup>67</sup>

The QCA proposes that the following assignment principles should form a schedule to an approved Undertaking:

- The overall objective of the assignment process is to ensure access seekers are not required to negotiate with QR's above-rail business groups for access to declared transportation services. This objective requires the following outcomes from the assignment process:
  - (a) Network Access should operate as a stand-alone provider of declared rail transport services. The onus of proof in justifying a departure from this principle rests with QR.
  - (b) Existing market shares of QR's above-rail business groups should not be a factor in the assignment of management responsibility for declared services.
  - (c) Network Access should provide access - using its own infrastructure - to any private siding.

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<sup>67</sup> The fact that the QCA has yet to receive QR's assignment for its infrastructure south of Gladstone impels the QCA to reserve such a right.

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- (d) Network Access should provide access to: any end-user's facility not owned or leased by a rail operator; a facility where there is joint use by end-users.
- (e) Network Access should provide access to declared rail transport services that assist normal mainline operations. These operations include the following rail transport functions:
- mainline running, including the use of passing loops;
  - loading and unloading at facilities other than freight centres and depots, undertaken as part of the normal operational cycle;
  - train queuing and staging for the following activities so long as they are undertaken as part of the normal operational cycle:
    - loading and unloading;
    - transit;
    - 'on track' maintenance, provisioning and crewing activities;
  - train marshalling and shunting:
    - in preparation for transit;
    - in preparation before or after train loading or unloading;
    - in preparation before or after maintenance and provisioning;
  - short-term train storage:
    - in a breakdown situation;
    - for short periods where product flow has been disrupted;
    - for short periods where the timetable does not allow use.
- (f) Disputes between an access seeker and QR with respect to a request for a reassignment of management responsibility for a part of QR's rail infrastructure from an above-rail business group to Network Access should be referred to the QCA for resolution. The QCA would adopt the following four step dispute-resolution process:
- the third-party operator would write to QR seeking a reassignment of management responsibility;
  - QR would be required to respond in writing within 30 days, providing an explanation of its decision;
  - if the access seeker did not accept QR's decision, the matter would be referred to the respective Chief Executive Officers of the two parties within 7 days for resolution. The Chief Executive Officers would have a further 14 days to resolve the dispute; and
  - if there were no resolution after 14 days, the access seeker or QR would give notice to the QCA about the dispute and the QCA would then resolve the matter.

In light of the concerns of QCA and stakeholders about QR's proposed assignment of management responsibility for its infrastructure, the QCA engaged in a series of discussions with QR. As a result, QR has amended the line diagrams for its infrastructure from Gladstone northwards using the above guiding principles. A complete set of amended line diagrams is at the end of the chapter.

The QCA believes the amended line diagrams represent an appropriate assignment of management responsibility for QR's infrastructure between Network Access and its above-rail business groups.<sup>68</sup> Subject to stakeholder comment on the proposed assignment, the QCA proposes that the amended line diagrams be included as a schedule to an approved Undertaking.

The QCA has yet to receive a draft of QR's line diagrams for its infrastructure south of Gladstone. The QCA expects QR to assign management responsibility for this infrastructure in accordance with the guiding principles. Once completed, the line diagrams will be subject to consultation with stakeholders. The QCA anticipates that a set of line diagrams for QR's infrastructure south of Gladstone will be finalised in time to be incorporated as a schedule to an approved Undertaking.

#### ***QCA's Position***

**The QCA would favourably consider an Undertaking that:**

- **subject to stakeholder comment, assigned management responsibility for QR's infrastructure in accordance with the attached line diagrams; and**
- **incorporated the following principles for the assignment of management responsibility for QR's rail infrastructure, as a schedule to the Undertaking:**
- **the overall objective of the assignment process is to ensure access seekers are not forced to negotiate with QR's above-rail business groups for access to declared rail transport services. This objective requires the following outcomes from the assignment process:**
  - (a) **Network Access should operate as a stand-alone provider of declared rail transportation services. The onus of proof in justifying a departure from this principle rests with QR.**
  - (b) **Existing market shares of QR's above-rail business groups should not be a factor in the assignment of management responsibility for declared services.**
  - (c) **Network Access should provide access - using its own infrastructure - to any private siding.**
  - (d) **Network Access should provide access to: any end-user's**

<sup>68</sup> The assignment of management responsibility for the MIM Balloon Loop at Mt Isa is the one remaining outstanding matter between QR and the QCA. QR advised the QCA on 1 September 2000 that the balloon loop will be managed by Coal and Mainline Freight which has an agreement with MIM Group to this end. The QCA intends to resolve this matter after the release of the Draft Decision.

**facility not owned or leased by a rail operator; a facility where there is joint use by end-users.**

**(e) Network Access should provide access to declared rail transport services that assist normal mainline operations. These operations include the following rail transport functions:**

- **mainline running, including the use of passing loops;**
- **loading and unloading at facilities other than freight centres and depots, undertaken as part of the normal operational cycle;**
- **train queuing and staging for the following activities so long as they are undertaken as part of the normal operational cycle:**
  - **loading and unloading;**
  - **transit;**
  - **‘on track’ maintenance, provisioning and crewing activities;**
- **train marshalling and shunting:**
  - **in preparation for transit;**
  - **in preparation before or after train loading or unloading;**
  - **in preparation before or after maintenance and provisioning.**
- **short-term train storage**
  - **in a breakdown situation;**
  - **for short periods where product flow has been disrupted;**
  - **for short periods where the timetable does not allow use.**

**(f) Disputes between an access seeker and QR with respect to a request for a reassignment of management responsibility for a part of QR’s rail infrastructure from an above-rail business group to Network Access should be referred to the QCA for resolution. The QCA would adopt the following four step dispute resolution process:**

- **the access seeker would write to QR seeking a**

**reassignment of management responsibility;**

- **QR would be required to respond in writing within 30 days, providing an explanation of its decision;**
- **if the access seeker did not accept QR's decision, the matter would be referred to the respective Chief Executive Officers of the two parties within 7 days for resolution. The Chief Executive Officers would have a further 14 days to resolve the dispute; and**
- **if there were no resolution after 14 days, the access seeker or QR would give notice to the QCA about the dispute and the QCA would then resolve the matter.**

### 4.3 Assignment of management responsibility for stations and platforms

#### *QR's Position*

Negotiation for access with third-party operators will be undertaken by Network Access. Where access is required for below-rail services provided by a facility managed by a business group other than Network Access, the latter will conduct access negotiations as an agent for the business group managing the facility: para 4.1.1(a).

The only exception to this arrangement is if the third-party operator's sole purpose of gaining access to a station, platform or marshalling yard is to utilise an above-rail facility managed by an above-rail business group, such as a workshop or terminal. In that case, negotiation will be directly between the third-party operator and that business group: para 4.1.1(b).

QR's initial submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* stated that the cost of transferring management of stations and platforms from its above-rail business groups would adversely impact on the cost of providing access. QR argued that because the management of stations is critical to managing the desirability of passenger rail transport, it should be the responsibility of the QR business group upon which it has the greatest impact, that is, an above-rail business group. If stations were to be managed by Network Access, they would be one step further removed from the direct business environment. This would increase the potential for management of such infrastructure to become less responsive to business needs directly related to customer service quality.

QR, in its supplementary submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*, noted that the NSW rail access regime excludes stations and platforms completely, whereas the South Australian and Northern Territory access regime provides that stations and platforms should be subject to third-party access.

#### *Stakeholder Comments*

A majority of submissions supported Network Access taking responsibility for managing stations and platforms.

**Table 4: Management of stations and platforms**

**FreightCorp** - placing such facilities in the hands of train operators will, more than likely, lead to difficulties in arriving at suitable commercial outcomes.

**Queensland Government** - this should be a matter for the QR Board to determine in the first instance. Nevertheless, it is preferable that responsibility for management of all infrastructure that is the subject of a declared service should be with one part of an organisation.

**Stanwell** - if QR's above-rail business groups control access to infrastructure such as marshalling yards, stations and platforms, it will be a barrier to entry by increasing operational difficulties and costs of third-party operators.

**Great Southern Railway** - Cl 4.1 has no reference to facilities for passenger trains where operators will require access not only to platforms and stations but also stabling sidings, and maintenance and cleaning facilities. It is not clear what happens in the event of a dispute between a third-party operator and a QR above-rail business group. Unless there can be some clear way of ensuring that disagreements will be dealt with equitably, control over all declared services should be dealt with by Network Access.

**AMC** - above-rail business groups should not control the access points to the rail infrastructure such as marshalling yards and stations and platforms. To avoid this unnecessary barrier to entry, Network Access should control and provide access to these facilities.

**Toll** - all infrastructure subject to the declaration should be subject to the Undertaking and within the control of Network Access.

**RTBU** - operational control of marshalling yards, platforms and stations is integral to the daily operations of the freight and passenger business groups in QR, and management by these groups is important for safety and for network efficiencies.

***QCA's Analysis***

Stations and platforms are covered by the declaration of rail transport services provided by QR's rail transport infrastructure for the purposes of the third-party access provisions of the QCA Act.

QR argued in its initial submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* that stations and platforms would be managed by its above-rail business groups because these facilities provide mainly above-rail services. However, the line diagrams QR provided to the QCA for its infrastructure from Gladstone northwards, reflecting the application of the common user test, indicated that Network Access would be responsible for the mainline track running through Gladstone, Townsville and Rockhampton stations.

The QCA believes the principles for the assignment of management responsibility for QR's infrastructure discussed in the previous section should be applied with respect to stations and platforms. In applying the principles, it is useful to view access to stations and platforms in two stages:

- trains arrive into, dwell at and then depart from the station/platform; and
- passengers/staff utilise facilities/structures sited at the station or platform.

The QCA supports the assignment of management responsibility for the track adjoining stations/platforms across QR's network to Network Access, on the grounds that train movements in and out of these facilities is a fundamental part of managing traffic on the

network.<sup>69</sup> In practice, this means that third-party operators would negotiate with Network Access for arrival/departure times for its trains at the station/platform within the framework provided by an approved Undertaking.

The use of facilities and structures at the station or platform potentially raises a more complex set of issues. The QCA considers that stations and platforms are likely to be most important to a third-party operator considering entering the passenger services market.

In order to deliver an effective passenger service, a third-party operator will likely want to deliver support services within the station to facilitate the processing of passengers. For example, establishing a ticketing office and/or ticket machine, providing information on train arrival/departure times, and facilities for baggage handling. In order to deliver these support services, the third-party operator is more likely to want to lease space within the station or on the platform.<sup>70</sup> The QCA believes that these services are covered by the declaration, as well as other basic infrastructure that facilitates the movement of passengers – and freight – through and around the station or platform. Third-party operators' access to such services should therefore be negotiated with Network Access.

The main concern is that a third-party operator planning to run passenger services should not have to negotiate with an above-rail business group for access to declared services within the station. An above-rail business group in direct competition with the third-party operator would have little incentive to negotiate commercial terms and conditions for such services. Notwithstanding that the conflict of interest would be less strong if the two parties were not in direct competition, the QCA's assignment principles provide that any negotiations concerning declared services should be conducted with Network Access within the framework of an approved Undertaking.

The QCA recognises that there are many services performed within stations that are not declared. Consequently, the case for Network Access managing the whole of such facilities is not strong. Moreover, at the majority of QR's stations – Roma Street in Brisbane being the main exception – QR's above-rail business groups are the only user and are likely to remain so under current Queensland Government policies. As a result of both of these factors, the QCA accepts QR's above-rail business groups being assigned operational management responsibility for stations and platforms, subject to Network Access being responsible for access negotiations regarding declared services. Such negotiations should occur within the terms and conditions established by the Undertaking.

Finally, the QCA considers that if there is significant third-party entry into the passenger services market and stations take on the character of multi-user facilities, it may need to revisit the situation where operational control of such facilities is assigned to QR's above-rail business groups. However, the QCA expects that this is likely to be a more significant issue for subsequent terms of QR's Undertaking rather than for the initial one.

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<sup>69</sup> This assumes that the stations and platforms are situated on the mainline of QR's network.

<sup>70</sup> It is also possible that the relevant above-rail business group and the third-party operator could reach an agreement for the operator to use QR's existing systems. Unless it was found that the service in question was declared under the QCA Act, the Authority would have no role in the resolution of disputes on these matters.

***QCA's Position***

**The QCA would favourably consider an Undertaking that:**

- **assigned management responsibility, including access negotiations, for track adjacent to all platforms/stations to Network Access; and**
- **assigned responsibility for access negotiations regarding declared services within stations and platforms to Network Access. Such negotiations should occur within the framework of the Undertaking.**

#### **4.4 Access seekers' rights to sign access agreements with QR**

In broad terms, an access agreement for below-rail services has two key components: an access right and a haulage arrangement. The access right is the specification of the access seeker's entitlement to use a 'slot' or 'path' of the network capacity (on a non-exclusive basis). The haulage arrangement addresses the technical issues associated with the access seeker's rollingstock and its interface with the rail infrastructure and other rail operators.

The access right and haulage arrangement can be 'bundled' such that a rail operator must come to an agreement with the rail manager on both the capacity and haulage aspects of the access agreement. Under a bundled arrangement, the rail operator and the rail manager are the only parties to the agreement.

Alternatively, the access right and haulage arrangements could be 'unbundled' such that the rail manager and end-user, for example a coal mine, negotiate a separate agreement concerning access rights. The customer then contracts with an accredited rail operator to provide train services on its behalf in line with the access right. The rail operator and the rail manager have a separate agreement concerning operational and technical matters, for example, interface arrangements.<sup>71</sup>

***QR's Position***

Notwithstanding that an end-user may participate in the negotiation for access rights, only a party who is, or will become, an accredited railway operator may enter into an access agreement with QR: sub-cl 4.1.1.

The Explanatory Guide outlines the following scenario concerning how an access negotiation consistent with sub-cl 4.1.1 might proceed. Representatives from a coal mine lodge an access application with QR. QR provides an indicative access proposal to the mine that then calls for tenders for the operation of the relevant train services, consistent with the train service information in their access application. Competing railway operators submit tenders to the mine based on the indicative access proposal. The mine then selects its preferred customer and nominates that party to finalise an access agreement with QR. The coal mine can continue to be

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<sup>71</sup> This is just one example of unbundling. It is possible to envisage alternative unbundled arrangements. For example, a customer may negotiate and sign an access agreement with the access provider for capacity and sub-contract the use of that capacity to a freight forwarder. The freight forwarder, in turn, sub-contracts the provision of the rail haulage service to a rail operator (that provides the locomotives, rollingstock, train drivers etc).

involved in negotiations with QR, however, QR and the railway operator will sign the access agreement.

The Draft Undertaking currently reflects what QR believes to be the optimal approach to dealing with access entitlements to its infrastructure. The access agreement envisaged by the Undertaking exists between QR and an accredited railway operator and encompasses all access issues, including technical and operational interface issues as well as commercial issues. QR acknowledges that other state rail access regimes appear to have accepted the right of end-users to have access entitlements in some form. QR does not believe that its proposed approach precludes an end-user, such as a mine, obtaining an access entitlement, it simply requires such an end-user to be an accredited railway operator.<sup>72</sup>

QR argued in its supplementary submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* that having access agreements encompassing both commercial (capacity) and operational/technical parameters ensures that access is achieved in the safest and most efficient manner. QR believed that network efficiency and safety may be compromised through an indirect relationship between Network Access, the infrastructure manager, and the applicable railway operator. In addition, in its view, linking access rights to operational parameters provided the simplest and most effective way of ensuring against misuse of capacity entitlements.

According to QR, practical and legal problems with parallel agreements included:

- while the end-user would have an obligation to make payments to QR for the capacity purchased, there would not be any consideration given to QR by the railway operator in the operations agreement. The operations agreement would not therefore constitute a binding contract but would need to take the form of a deed. As QR would be required to hold the mine accountable for the actions of its operator, additional complexity would be injected into contractual arrangements through indemnities and insurances;
- there would be difficulty in guaranteeing the compatibility of the capacity and operational agreements, with the likely considerable overlap between the two creating potential confusion in their implementation;
- it is difficult to apply a performance regime with respect to the use of capacity by operators and the way in which capacity is provided; and
- the 'parallel agreement' approach has no real precedent in the rail industry and would take considerable time and debate to effect.

From a commercial perspective, QR argued that unbundling would result in mines avoiding the liability for operational interface issues associated with access.

### ***Stakeholder Comments***

A majority of stakeholder submissions strongly supported the unbundling of access agreements.

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<sup>72</sup> The QCA understands that the NSW access regime allows both accredited rail operators and end-users to sign access agreements with the track manager, RAC.

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**Table 5: Unbundling of access agreements**

**National Rail** - allowing customers to hold access rights would remove some of QR's discretion to refuse to negotiate in relation to an existing QR customer who is considering competing alternatives.

**MIM Group** - a customer access right for bulk commodity traffic would facilitate competition for the rail haulage service and consequently is an essential component of a competitive transport system.

**AMC** - allowing customers to hold access rights would allow genuine competition between third-party operators and allow customers to use multiple rail operators where desired.

**MIM Group, QMC** - safety, environmental, and interface conditions could all be incorporated in an 'operator's agreement' existing alongside an access agreement with an end-user.

**Queensland Government** - the undertaking should provide sufficient flexibility to allow both accredited and non-accredited organisations to enter access agreements provided that an appropriately accredited operator undertakes the operation of the train services. It is reasonable that shippers of bulk commodities be able to negotiate access on their own behalf, with details to be finalised upon the selection of a railway operator. The question of who will transport customer's commodities is a commercial one for the customer to decide.

**FreightCorp** – supports the right of end-users to hold access agreements, although we do believe that in practice this does have the potential to create contractual difficulties. While we agree with QR that an indirect relationship with the infrastructure owner can lead to inefficiencies, we strongly disagree that such relationships necessarily compromise safety.

The right of end-users of rail services to seek access agreements, in theory, allows for them to seek alternative train operators to provide haulage services, and might provide customers with large haulage contracts additional opportunities to seek efficiencies in the overall cost of transporting their products. Nevertheless, the task of transporting goods is complex, and is often seen by producers as not part of their core skills. The task of negotiating an access agreement is not a trivial one and requires substantial knowledge of railway operations and engineering. A specialist train operator is able to add value to the transport task by negotiating and managing an access agreement with the infrastructure provider.

The NSW Rail Access Regime provides for end-users of rail services to hold access contracts. To date, no end-user has decided to use this option, preferring to leave the complexity of managing infrastructure access to train operators. Thus while end-users have the potential to arrange any part of their transport themselves, they have seen the value added by genuine competition between train operators and have availed themselves of that opportunity. It is our expectation that a similar outcome will occur in Queensland if there is a genuine opportunity for train operators to compete.

**ARTC** – QR's argument is that a tripartite arrangement is likely to be more complicated than the 'traditional' access arrangement and is without precedent, and separates the commercial aspects of the arrangement from the technical/operational aspects. Whilst such an arrangement is yet to occur in the rail industry (although we are currently finalising access wholesale arrangements), there are many precedents in other industries, for example, gas, where more flexible arrangements than the standard operator/owner agreement exists.

For example, the QR approach effectively blocks a major miner from contracting a path, on condition that it is operated by an accredited operator, and calling for bids from train operators to undertake the task. If anything, this provides QR with additional security as it provides two parties from which to seek remedies.

Our view in this matter is that the market should be left to decide what is the most appropriate arrangement for access. If the more complicated arrangement is inefficient (costs/risks v benefits) then the market will avoid such an arrangement, but it should not be precluded by regulation. We are not expecting to preclude such arrangements by way of our undertaking.

**RTBU** – is strongly opposed to unbundling on the grounds that it would have an adverse impact on network integrity, safety and jobs.

### *QCA's Analysis*

In considering the issue of unbundling, it is important to distinguish between existing and future rail haulage contracts. The issue of whether it is appropriate to depart or provide relief from existing contracts is an issue for QR, its customers and the Queensland Government. The QCA has no legislative mandate to revisit existing contracts as part of its review of QR's Draft Undertaking.

The QCA supports QR's customers having the option of exercising direct control over transportation of their commodities, subject to QR's legitimate business interests being protected. Unbundling the access and haulage elements of access agreements negotiated under an approved Undertaking is potentially an important means of achieving this objective.

It is difficult to predict how the Queensland above-rail market will evolve, especially if there is strong growth in demand. Consequently, it is important not to impose constraints on the evolution of that market through the operation of an approved Undertaking. For example, integrated access agreements could become a barrier to customers switching rail operators by increasing the associated transaction costs.

It is possible to envisage that, as the number of credible rail operators servicing the Queensland market increases, the risks associated with engaging one of these operators will fall. Customers may place a premium on choice in rail operators and enter short-term haulage agreements, which in turn could be expected to enhance above-rail performance. Providing an unbundling option would have the desirable attribute of allowing a greater role for market-based allocation of access rights.

The QCA's view that unbundling is likely to be in QR's customers' - and access seekers' - interests is consistent with stakeholders support for unbundling, in particular, QMC, which represents some of QR's largest customers. This is very important for the Authority's consideration of the issue. The QCA does not wish to impose a requirement on QR that would be of minor benefit to QR's customers and potential access seekers. In addition, the QCA understands that the NSW Rail Access Regime allows both end-users and rail operators to enter into access agreements with RAC.

QR's Draft Undertaking does not state that access agreements will only be entered into with third-party operators, however, it provides a framework for access arrangements which is restricted to third-party operators. The practical effect of this would be that, while an end-user could participate in access negotiations, only an accredited rail operator would be able to enter into any resulting access agreements with QR. In other words, all of the protections contained in the Undertaking would not apply to end-users seeking to negotiate access agreements in their own right.

Moreover, the QCA understands that, if QR refused to sign an access agreement with an end-user with respect to declared services, the Undertaking would not constrain a determination by the QCA of an access dispute instigated by that end-user. In effect, QR cannot use the Undertaking to restrict certain parties from negotiating and signing access agreements with respect to declared services.

The QCA is keen to avoid approving an Undertaking incorporating provisions that appear likely to generate a disproportionate number of access disputes. Given stakeholder views on this issue, the current wording of para 4.1.1(c) clearly presents a risk of such an outcome.

Nevertheless, the QCA recognises that not all end-users or potential access seekers will be interested in negotiating an unbundled access agreement with QR and that, in certain

circumstances, third-party operators may be better placed to negotiate and manage all aspects of an access agreement than customers.

The Authority accepts that the task of negotiating an access agreement requires substantial knowledge of technical issues associated with railway operation and, as such, a rail operator may be able to add value by negotiating and managing an access agreement with the infrastructure provider. Moreover, above-rail operators have the capacity to add considerable value in relation to the day-to-day issues associated with the practical operation of access arrangements.

The QCA believes that, if third-party operators can add value in these ways, end-users may choose integrated access agreements. However, the key issue remains that end-users should have the discretion to choose between an unbundled or integrated access agreement. This way, the market is able to determine the most desirable contractual structure for the holding of access rights.

In order to achieve this objective, the QCA believes that an approved Undertaking should provide sufficient flexibility to allow both accredited and non-accredited organisations to enter access agreements with QR, provided that an appropriately accredited rail operator performs the train services. The interface between QR and an accredited railway operator in an environment of unbundled access agreements is discussed in more detail in a section below. In practical terms, if an access seeker chose the unbundled option, QR would have to split its standard access agreement into separate capacity and haulage agreements. This would be undertaken on a case-by-case basis.<sup>73</sup>

As noted above, the QCA's support for unbundling is subject to QR's legitimate business interests being protected. However, the QCA considers that the arguments put forward by QR in its supplementary submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* opposing unbundling are not persuasive. Clearly, all QR's valid operational concerns must be addressed before haulage services commence. However, this is not a relevant concern for contractual structure so long as these requirements are established.

#### *New contractual arrangements*

In an environment where customers are free to negotiate access agreements with QR, the key contractual arrangements would likely be between:

- QR and the end-user;
- the end-user and an accredited third-party operator; and
- the accredited third-party operator and QR.

The QCA believes that the additional complexity asserted by QR is unlikely to be material - indemnities have already been included in QR's draft standard access agreement. Indeed, far more complex commercial agreements are commonplace for less significant commercial transactions. The allocation of risk amongst QR, third-party operators and end-users would be resolved through contractual arrangements.

The QCA is not aware why QR would suffer from an absence of commercial leverage over the third-party operator as QR has suggested. It would be normal commercial practice for the

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<sup>73</sup> Although a 'benchmark' separation could be effected as part of the process of establishing a standard access agreement for the coal sector.

contract between QR and the end-user to specify that the end-user is responsible for any damage its employees, contractors or agents cause to QR. QR would still retain a contractual arrangement with the rail operator dealing with, for example, safety, environmental and interface conditions.

Moreover, the QCA expects that the rail haulage contract between the end-user and the third-party operator would mirror the obligations established in the contract between the end-user and QR as far as the interface between the third-party operator and QR's network is concerned. In establishing such 'back-to-back' contracts, QR would establish the same rights as dealing with the third-party operator directly. With such back-to-back contracts in place, there is no reason why there would be any difference in the application of a performance regime for unbundled agreements compared to integrated ones, nor that there would be a decline in network integrity.

### *Interface issues*

QR argued that those not familiar with the rail industry have underestimated interface issues. However, the QCA believes that QR would be able to address both commercial issues, such as costs associated with the quality of rollingstock, and safety interface issues through its contract with the end-user. Broader safety issues would be addressed through the rail safety accreditation framework administered by Queensland Transport.<sup>74</sup>

The QCA considers that the requirements imposed on third-party operators through the provisions of Part 7 of the Draft Undertaking, once approved, would be incorporated in the contract between the end-user and third-party operator. Consequently, the third-party operator would need to agree with QR on rollingstock interface standards and environmental requirements, and address interface safety issues in consultation with QR. Failure to meet its obligations in any of these areas would result in the third-party operator being prevented from using the network and hence delivering a service to its end-user.

The argument by QR and a stakeholder that network safety may be compromised through an indirect relationship between Network Access and the third-party operator also ignores the role of the Queensland rail safety regulator. This independent rail safety process should provide reassurance to QR that unsafe third-party operators are not running train services on its network. Moreover, the QCA considers that end-users have a strong incentive to employ a safe, efficient third-party operator to carry their products, on the grounds that the customers bear the risk if its product is not delivered, for example, if the third-party operator loses its accreditation.

### *Capacity issues*

QR argued that tying the operational and commercial aspects of an access agreement is the simplest way of ensuring capacity entitlements are not misused. However, the QCA believes that allowing the unbundling of access agreements could provide scope for more flexible management of rail capacity from the perspective both of QR and end-users.

For example, the unbundling approach could also assist in allocating capacity where more than one rail operator is competing to haul the same traffic. By negotiating directly with the end-user, QR would avoid requiring third-party operators to demonstrate that the end-user was agreeable to the execution of an access agreement and that the rail operator had or would gain the right to haul the product in question.<sup>75</sup>

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<sup>74</sup> Chapter 7 discusses interface issues at length, including Queensland's legislative rail safety framework.

<sup>75</sup> Capacity issues are discussed in Chapter 6.

***QCA's Position***

**The QCA would favourably consider an Undertaking that provided that both accredited and non-accredited organisations could execute access agreements with QR, provided that an appropriately accredited rail operator performs the train services.**

**4.5 Discretion to refuse to negotiate – prudential requirements*****QR's Position***

QR reserves the right to negotiate only with third-party operators who comply with the relevant obligations and applicable processes set out in the Undertaking. The circumstances that would justify QR refusing to negotiate with a third-party QR operator are:

- the material failure to comply with relevant obligations and processes set out in the Undertaking: para 4.1.2(a); and
- an inability to meet specified prudential requirements including:
- a requirement that the third-party operator be solvent: sub-para 4.1.2(b)(i); and
- that it not have been in material default<sup>76</sup> of any agreement with QR or with another rail manager providing access to rail infrastructure, in the previous two years: sub-para 4.1.2(c)(ii).

QR argued in its initial submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* that faced with a legislative obligation to negotiate access, it could potentially be exposed to resource-intensive negotiations with parties who may leave the process at any time. In QR's view, the conditions it has outlined, including in regard to prudential requirements and material default provisions, are no more than is reasonably necessary to protect its legitimate business interests.

QR went on to argue that although the Undertaking does not expressly state it, QR intends to provide written reasons for any refusal to negotiate at the same time that it advises a third-party operator on the matter.

QR will prepare an indicative access proposal where a third-party operator:

- seeks access to already committed capacity; and/or
- seeks access that is required for carrying bulk consignments of commodities, when it is of the reasonable belief that these commodities will be otherwise carried by services under an existing access agreement: sub-paras 4.1.2(d)(i) and (ii).

However, QR will not be obligated to enter into further negotiations for access rights unless and until it is apparent there is an arrangement in place to make the committed capacity available, or to ensure QR only has one access agreement for services carrying the relevant bulk

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<sup>76</sup> 'Material Default', as defined in the Draft Undertaking, means: (a) repeated failure to comply with the terms and/or conditions of any of the agreements specified in Paragraph 4.1.2(c); or (b) any breach of a fundamental term and/or condition of any of the agreements specified in Paragraph 4.1.2(c).

consignments. QR also notes that it will give priority to the preparation of indicative access proposals for applications that relate to available capacity: sub-para 4.1.2(d)(iv).

QR argued in its Explanatory Guide that para 4.1.2(d) is not intended to allow QR to make an assessment of whether or not there is sufficient market demand to justify the entrance of an additional operator, but rather to ensure QR does not ‘over-commit’ its capacity. In its submissions, QR stated it does not believe the Undertaking should be concerned with contestability of traffics for which QR currently has integrated rail haulage agreements, as it believes the QCA Act does not allow for the opening up of existing contracts. QR considered its self-imposed obligation to provide an indicative access proposal in these circumstances is more than adequate to meet the legitimate interests of access seekers.

If QR refuses to negotiate access with a third-party operator, it undertakes to provide written reasons to the third-party operator for its refusal. If the third-party operator considers this refusal is unreasonable, it may refer the matter to the QCA. Where the QCA determines QR has unreasonably refused to commence or subsequently unreasonably ceased negotiations, QR will recommence negotiations immediately: para 4.1.2(e).

### ***Stakeholder Comments***

There was no agreement in stakeholder submissions as to whether prudential requirements are overly strict or whether the term ‘material default’ is sufficiently clear.

#### **Table 6: Prudential requirements: solvency**

**AMC, RTBU, Stanwell** - the prudential requirements are reasonable.

**Great Southern Railway, QMC, Toll** - the prudential requirements are overly strict and give QR too much scope to refuse to negotiate.

**FreightCorp** - it is inappropriate that QR should judge the solvency of a party by reference to ‘material default’ of another access agreement.

**Stanwell** - the dispute resolution process should allow an access seeker to dispute QR’s findings regarding prudential requirements.

**Queensland Government** - solvency is a reasonable requirement.

#### **Table 7: Prudential requirements: Material default**

**AMC, FreightCorp, Stanwell** - the proposed definition of ‘material default’ is appropriate.

**Queensland Government, QMC, Toll** - the definition is not sufficiently clear and requires clarification.

**Toll** - QR’s examples of material default are minor in most cases. It is entirely inappropriate for QR to refuse to negotiate with an access seeker in default of an agreement with any rail manager anywhere, as an access seeker may have a legitimate dispute with such a manager. Material default should be defined as a fundamental breach of the relevant access agreement with QR.

**AMC, National Rail, Queensland Government, QMC, Stanwell, Toll** - events of default should be defined in the Undertaking.

**RTBU** - events of default should not be defined in the Undertaking.

There was general concern that para 4.1.2(d) could legitimise anti-competitive behaviour notwithstanding recognition that QR could not sell committed capacity.

**Table 8: Discretion to refuse to negotiate**

**AMC, MIM, Stanwell, Toll** - this provision is a significant barrier to entry.

**MIM** - there is potential for this approach to entrench the position of QR's Coal and Mainline Freight Group as the provider of coal haulage services. Further, it would defeat meaningful determination of market rates by limiting our ability to obtain competitive prices.

**AMC, Stanwell** - this clause would make it difficult for a new operator to gain access on competitively neutral terms with QR's existing traffic, particularly if the haulage contract has a different termination date to the access agreement.

**Toll** - QR should be required to progress negotiations to the point of signing, as the proposed approach works contrary to an open and contestable market.

**FreightCorp** – we have sought access prices for a number of operations within Queensland. In almost all cases, QRNAG has questioned us with regard to the status of the tonnages for which we are seeking prices. Further, despite our assurances to the contrary, they appear unwilling to concede that tonnages might genuinely be available for haulage. FreightCorp regards this as intolerable and can find no use for Section 4.1.2(d)(ii) of the Undertaking other than to frustrate genuine access enquiries. Having said this, we note that QR has not, to date, refused to provide access charges for these hauls. However, this is continually held over our heads.

It would be simple to make the granting of access rights contingent on the winning of a particular contract.

**Queensland Government** - para 4.1.2(d) could be used to protect existing QR above-rail business and appears inappropriate for that reason. The clause should be removed, and reliance be placed on the QCA to determine whether negotiation or arbitration should continue. The current wording of para 4.1.2(d) unfairly enables QR to block entrants into the market.

**QMC** - the clause was acceptable subject to a number of conditions including:

- negotiations between Network Access and access seekers being allowed to commence and extend beyond the indicative access proposal stage well in advance of the expiry of access agreements defining committed capacity; and
- indicative access proposals are provided in a reasonable time.

**RTBU** - the clause is acceptable (and consistent with the requirements of the Competition Principles Agreement).

There was general agreement that a time frame for notification of a refusal to negotiate should be given, however, there was no agreement on the time frame.

**Table 9: Time frames for refusal to negotiate**

**AMC, National Rail, QMC, Toll** - a time frame should be included, with proposals varying from 7 to 21 days.

**Queensland Government** - a 'reasonable' period would need to be provided to allow time for investigation.

**FreightCorp, Stanwell** - this issue need not be addressed in the Undertaking.

***QCA's Analysis******Discretion to refuse to negotiate***

In assessing the reasonableness of QR establishing prudential requirements and a material default of any access agreement with QR or any other track manager in the previous two years

as grounds upon which it can refuse to negotiate with an access seeker, the QCA had regard to the following considerations:

- s99-s101 and Division 5, including s122, of the QCA Act;
- the areas of greatest concern expressed by stakeholders, including QR; and
- the negotiation conditions applied in other access regimes.

S99 provides that an access provider of a declared service must, if required by an access seeker, negotiate with the access seeker for making an access agreement relating to the service. Therefore, by virtue of this section, QR is under a general statutory obligation to negotiate with an access seeker. In addition, s100 requires the parties to negotiate in good faith. However, the Act does not provide that the obligations contained in s99 and s100 are subject to the provisions of an approved undertaking.<sup>77</sup>

Consequently, irrespective of whether the Undertaking sets out conditions on which QR may refuse to negotiate with an access seeker, QR has a general statutory obligation to negotiate. Should QR refuse to negotiate - whether or not this refusal was on the grounds set out in the Undertaking - it would be open to an access seeker to give notice to the Authority under Division 5 that an access dispute existed.

The QCA does not believe that it can approve an Undertaking that contains restrictions on QR's obligation to negotiate with an access seeker because it would be inconsistent with s99 of the QCA Act. Nevertheless, the QCA recognises that there may be circumstances in which QR would be entitled to refuse to enter into an access agreement in order to protect its legitimate business interests. These circumstances could include the failure of an access seeker to meet specified prudential requirements or a consistent failure to comply with the terms of another relevant agreement with QR.

Consequently, the QCA would not object to an Undertaking that provided for QR to establish the circumstances in which it could refuse to enter into an access agreement. Such an approach would be consistent with QR's obligations under s101, which provides that, in negotiations towards an access agreement, an access provider must make all reasonable efforts to satisfy the reasonable requirements of an access seeker.

This would mean that QR would be required to enter into negotiations with an access seeker in order that it could establish whether the circumstances for a refusal to enter into an access agreement were met. If QR established that the circumstances applied, then QR could give notice that it did not intend to enter into an access agreement with the access seeker and therefore, would not be required to continue negotiations on this basis.

The QCA believes that this approach would protect QR's legitimate business interests in that it would not be required to enter into extensive negotiations with all access seekers. Further, provided that QR applied these conditions in good faith, it would arguably protect itself from claims by access seekers that it was in breach of s99 or s100 of the QCA Act. However, should an access seeker consider that QR had incorrectly decided not to enter into an access agreement or that QR had not conducted these negotiations in good faith, then it would be open to the access seeker to give notice to the Authority under Division 5 that an access dispute existed.

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<sup>77</sup> In contrast, s104 and s125 of the QCA Act, regarding preventing or hindering access, do not apply to negotiations towards access agreements as they are only relevant once an access agreement or access determination is in place. For that reason, s104(6)(a) and 125(6)(a), which protect access providers from complaints in respect to acts done under an approved undertaking, would not apply in these circumstances.

S122 allows the Authority to decide not to begin an arbitration or to end an arbitration at any time, if it considers that the dispute notice was vexatious, the subject matter of the dispute is trivial, misconceived or lacking in substance, or the party who gave the access dispute notice had not engaged in negotiations for an access agreement in good faith. As a result, the Authority could refuse to arbitrate if it did not consider that the access seeker's claims were genuine or of substance.

Further, in arbitrating access disputes, the Authority is not required under s119(5) of the QCA Act to make an access determination unless it is satisfied that the legitimate business interests of the owner of the facility are protected. Therefore, if the Authority considered that the access seeker was not financially competent or that it was in material breach of a relevant agreement, it could refuse to make an access determination on these grounds.

As discussed above, the QCA would not object to an Undertaking that established the circumstances in which QR could refuse to enter into an access agreement. However, the QCA is aware that if the threshold for such a refusal was to be set too low by QR, the evolution of the above-rail market could be distorted. Establishing a low threshold would be a very effective means of keeping potential competitors out of the above-rail market and this would potentially deny customers choice in their rail haulage provider.

On these grounds, the QCA believes that the onus should be on QR to justify a refusal to enter into an access agreement. In this regard, an appropriate test would be for QR to demonstrate that the access seeker is not capable of meeting the terms and conditions specified in its proposed access agreement.

The QCA believes that there will be a range of factors relevant to such a demonstration by QR. These factors are likely to be both forward and backward-looking, on the grounds that QR's assessment of an access seeker's ability to meet the terms and conditions of a proposed access agreement will be partly influenced by the track record of the access seeker.

The QCA has assessed the prudential requirements in the Draft Undertaking in the context of the factors relevant to QR demonstrating that an access seeker is not capable of meeting the terms and conditions specified in its proposed access agreement.

#### *Prudential requirements: Solvency*

The QCA recognises that QR could potentially become drawn into an ongoing series of discrete negotiation processes with an insolvent access seeker unless it establishes a set of prudential requirements at the preliminary stage of the access negotiation process. Provisions allowing access providers the discretion to refuse to negotiate on prudential grounds can be found in other access regimes (discussed below), however, a statutory obligation to negotiate does not apply to the access providers in these cases.

ARTC's prudential requirements entail the access seeker delivering to ARTC security for the rail operator's obligations under the agreement in the form of an unconditional bank guarantee or similar security. Under the proposed Western Australia rail access regime,<sup>78</sup> Westrail is entitled to require a proponent to show it has the necessary financial resources to carry on the proposed rail operations. This includes its ability to meet its financial obligations under an access agreement to Westrail (having regard to any credit arrangements with Westrail) and to other persons (including excesses under policies of insurance). RAC's standard access agreement also contains an obligation on the rail operator to grant security for the operator's

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<sup>78</sup> Government Railways Access Code (Draft), Western Australia, 10 September 1999.

obligations under the agreement in the form of an unconditional and irrevocable bank guarantee or a letter of credit.

The QCA's support for solvency to be a factor relevant to QR demonstrating an access seeker's lack of financial competence would be conditional on such a factor not being set at too high a level that financially sound access seekers would be precluded from entering into an access agreement with QR. Moreover, the QCA believes that where an access seeker provides some form of prudential contribution or security deposit as part of a proposed access arrangement, solvency may not be a relevant factor.

QR's proposed definition of solvency in the Draft Undertaking is similar to those found in other non-rail access regimes.<sup>79</sup> However, the QCA has some concerns that the definition of solvency could have the effect of QR claiming that an access seeker was insolvent in circumstances where it was not warranted. Consequently, the QCA has proposed a number of minor amendments to the proposed definition.

The QCA would raise no objection to QR establishing failure to meet the solvency requirement defined below as a factor to be considered in demonstrating an access seeker is not capable of meeting the terms and conditions specified in its proposed access agreement. The QCA considers that QR's existing definition is acceptable, subject to minor amendment. The Authority's proposed definition is as follows:

**“Solvent”** means none of the following events have happened in relation to the third-party operator:

- (a) the third-party operator is unable to pay all its debts as and when they become due and payable or it has failed to comply with a statutory demand as provided in Section 459F(1) of the Corporations Law;
- (b) a meeting is convened to pass a resolution to place it in voluntary liquidation or to appoint an administrator, unless the resolution is withdrawn within 14 days or the resolution fails to pass;
- (c) an application is made to a court for it to be wound up and the application is not dismissed within one month;
- (d) the appointment of a controller (as defined in the Corporations Law) of any of its assets, if that appointment is not revoked within 14 days after it is made; or

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<sup>79</sup> The TAF (Telecommunications Access Forum) Telecommunications Access Code allows an access provider to refuse to accept an application when there are reasonable grounds to believe the access seeker would fail, to a material extent, to comply with the terms and conditions on which the provider complies with relevant Standard Access Obligations (contained in the Trade Practices Act, section 152AR). Evidence of grounds for believing this include evidence the access seeker is not creditworthy. Where the refusal to provide access is on prudential grounds, the access provider should include specific evidence as to why it believes the access seeker would not be able to meet its financial obligations with respect to access and any independent supporting evidence of that position. In the event of a dispute, the Code provides for a number of resolution mechanisms, including inter-party working groups, mediation, expert committee and arbitration under Division 8 of Part XIC of the *Trade Practices Act*.

The National Electricity Code (NEC) states that a connection applicant must provide, in addition to other information, commercial information to enable the service provider to make an assessment of the ability of the applicant to satisfy the prudential requirements for network service. These requirements are a matter for negotiation between the parties and may take the form of, but need not be limited to, capital contributions, pre-payments or financial guarantees. In any case, Market Participants (persons registered with NEMMCO as a Market Generator or a Market Customer under the NEC) have to meet certain prudential requirements. These include a condition that they must not be under external administration under any laws applicable to it in any jurisdiction, they must be resident in or have a permanent establishment in Australia, they must not be immune from suit in respect of obligations under the Code and they must be capable of being sued in its own name in a court of Australia.

- (e) the third-party operator resolves to enter into or enters into any form of arrangement (formal or informal) with its creditors or any of them, including a deed of company arrangement.

*Prudential requirements: material default*

The QCA recognises QR's concern about entering into an access agreement with an access seeker who may have a track record of defaulting on access agreements with QR on non-trivial matters. However, the QCA believes that QR's proposed discretion to refuse to negotiate on the grounds of material default could become a major barrier to entry. For example, a third-party operator would be precluded from expanding its market share whilst QR considered it was in material default of another access agreement with QR or another access provider.

The QCA has a particular concern with the proposal that QR could refuse to negotiate with an access seeker in the event of default under an agreement with any rail manager, even in another jurisdiction, in the last two years. It is arguable that, where default is with another service provider, it is not strictly relevant to any potential agreement between the access seeker and QR, unless it goes to matters that are considered by Queensland Transport as part of the rail safety accreditation process.<sup>80</sup> Furthermore, it seems inappropriate for QR to be in a position to judge the merits of any dispute with another service provider.

Similar provisions for refusal to negotiate access are not common in other access regimes. ARTC grants access on the basis that a potential rail operator is capable of meeting the terms and conditions specified in its access agreement. Although access will not be granted until all specifications have been met, the onus is on the access seeker to meet these requirements, such as safety accreditation. Failure to meet requirements may result in access being denied. Once the rail operator's compliance with these requirements is evidenced, ARTC will continue negotiations. QR's proposed provisions are not commonly found in non-rail access regimes either, with neither the Gas Access Code or the National Electricity Code containing any such provision. The exception to this is the TAF Telecommunications Access Code.<sup>81</sup>

The QCA believes that defaults of access agreements should be brought within the list of factors relevant to QR demonstrating that an access seeker is not capable, to a material extent, of meeting the terms and conditions specified in its proposed access agreement. The key issue is to balance the need to protect QR's legitimate business interests through specifying key risks, against the potential for this specification to prevent third-party operators from entering the above-rail market in Queensland.

QR's proposed material default definition encompasses repeated failure to comply with the terms and/or conditions of any of the agreements specified in cl 4.1.2(c) of the Draft Undertaking or any breach of a fundamental term and/or condition in these agreements.

The QCA believes that the first part of this definition relating to repeated breaches is reasonable provided QR recognises that the breaches are 'non-trivial' and assuming that either party is free to refer the matter to the QCA for dispute resolution. The distinction between a breach and a 'non-trivial' breach of an access agreement is important. It is possible that an agreement may be breached inadvertently and in a manner that has no material effect on QR. The 'breach' could be the subject of a dispute relating to an existing access agreement. Moreover, the non-

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<sup>80</sup> The rail safety accreditation process is discussed in Chapter 7.

<sup>81</sup> This Code allows as a condition to refuse to negotiate evidence of repeated failure by the access seeker to comply with the terms and conditions on which the same or similar access has been provided, whether or not by the access provider. Such a refusal must contain evidence of any previous failure by the access seeker, its owners or directors, to comply with terms and conditions of which the access provider is aware.

compliance may be rectified as soon as it becomes apparent. In these circumstances, it is difficult to sustain the argument that this would be sufficient ground for QR not to enter into future access agreements.

The second part of QR's definition of material default, which refers to 'any breach of a fundamental term', lacks objectivity, in particular, the term 'fundamental' raises too much potential for confusion.

As discussed above, the QCA has proposed that defaults of access agreements should be brought within a list of factors relevant to QR demonstrating that an access seeker is not capable of meeting the terms and conditions specified in its proposed access agreement. The main benefit of such an approach would be that QR clearly states what it considers to be significant events of default so the scope for disagreement/misunderstandings with access seekers is reduced. Greater certainty in the negotiation framework reduces the scope for disputes to arise. A majority of submissions in response to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* supported a list of material events of default being defined in QR's Undertaking.

Nevertheless, following discussions between QR and its stakeholders in the first half of 2000 regarding the development of principles for a standard access agreement, it was proposed that material events of default should be agreed during the access negotiation process rather than specified in QR's Undertaking. It could be expected that the material events of default would reflect the risks each party faced in the context of the particular access seeker's proposed train services, nevertheless, some events of default would likely become standard across all access agreements.

The following is a non-exhaustive list of factors that could be used by QR to demonstrate an access seeker's inability to comply, to a material extent, with the terms of its proposed access agreement:

- the suspension of a rail operator's safety accreditation,
- the safety accreditation of a rail operator or a contractor being cancelled;
- the rail operator failing to maintain insurances required under the access agreement;
- the rail operator failing to comply with a suspension;
- repeated non-trivial breaches in the last two years of existing access agreements with QR; and
- insolvency, in the absence of alternative arrangements, such as security deposits, which protect QR's financial exposure.

#### *Discretion to refuse to negotiate*

An indicative access proposal sets out the non-binding indicative arrangements in relation to factors such as available capacity. In QR stating that it will not negotiate beyond the provision of such a proposal in instances where there is already existing traffic, it seems that the document could be commercially ineffective. The indicative access proposal is intended to be prepared to progress negotiations towards an access agreement, whereas QR's specific statement will preclude this in these circumstances.

The QCA Act (s.100), states that both the access provider and the access seeker must negotiate in good faith for reaching an access agreement. If a dispute arises, under s122, the QCA can

end arbitration without making a determination if it considers that the subject matter of the dispute was vexatious or frivolous.

Network Access will not have possession of all information relating to the existing haulage contracts between a third-party operator and an end-user and thus will not be aware of potential contractual issues such as breaches, renegotiations or preferences for changes of operators. Accordingly, the fact that an access application relates to a traffic that Network Access believes is contracted capacity is not itself grounds to believe the application has not been made in good faith.

Accordingly, the QCA considers that para 4.1.2(d) has the potential to stifle competition by entrenching the position of any incumbent operator in the above-rail market. This is clearly contrary to access seekers' interests and, in turn, the long-term interests of end-users. Moreover, it could potentially inhibit the evolution of the above-rail market. Forcing third-party operators to instigate formal dispute resolution in response to QR's refusal to negotiate beyond the provision of an indicative access proposal is inappropriate.

However, there are alternative approaches that would avoid QR being drawn into access negotiations that have no reasonable prospect of success, whilst not undermining the integrity of the above-rail market. QR proposes that para 4.1.2(d) apply only in respect of bulk commodities. A feature of such traffics is that there are identifiable end-users. Consequently it is possible to make access negotiations, and any rights that emerge, subject to the approval of the end-user.<sup>82</sup> This is a better option than outright refusal by QR to negotiate so long as QR's legitimate business interests are protected. It is proposed that the protection of QR's legitimate business interests be achieved by QR being entitled to insist that as a condition of preparing an indicative access proposal and negotiating in good faith, it be allowed to recover its costs if subsequently QR can demonstrate that an access application was frivolous or vexatious. Consequently, when an access seeker makes the decision to negotiate, it bears these risks rather than QR. However, it must also be remembered that access seekers also incur considerable costs in negotiating, which makes frivolous and vexatious access applications unlikely.<sup>83</sup>

#### *Time frames for refusal to negotiate*

The QCA has previously expressed its concerns regarding QR's Undertaking referring to a refusal to negotiate with an access seeker.

Nevertheless, the QCA believes that it is reasonable for the Undertaking to expressly state that QR intends to provide written reasons at the same time that it advises an access seeker of its refusal to enter into an access agreement. A time frame would provide third-party operators with some certainty as to the preliminary negotiation process and would enable referral to the QCA as soon as possible. In terms of what is required in other jurisdictions, the proposed

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<sup>82</sup> This approach to capacity allocation is discussed further in regard to mutually exclusive traffics in section 6.5 of Chapter 6.

<sup>83</sup> ARTC considers that it is difficult to imagine all capacity being committed. While acknowledging that it may not be able to meet the preferred path of the access seeker, ARTC would offer a range of alternatives, for example, offering a different time or different length path. ARTC acknowledges that in some instances, this may be a long and iterative process. In contrast, the approach contained in the proposed Western Australian rail regime is to require the access seeker to show that its proposed operations are within the capacity of the route. If Westrail is not satisfied with this evidence and the access seeker disputes this finding, it must notify Westrail that there is a dispute between them. Disputes may then be referred to arbitration. While the onus of proof of available capacity is different, this resort to arbitration is similar to what is proposed by QR. In terms of non-rail access regimes, the TAF Telecommunications Access Code allows an access provider to refuse to accept an access application if the supply of the relevant service to the access seeker would prevent the provider or another operator already being provided with the service from meeting their reasonably anticipated requirements. A written refusal on these grounds should include the time horizon over which reasonably anticipated requirements are measured, how these have been identified and assessed by the access provider and the level of commitment or certainty with regard to these requirements.

Western Australian rail access regime specifies a period of seven days for Westrail to notify a proponent of its dissatisfaction with the information it has received in regard to the access seeker's managerial/financial ability and available capacity.<sup>84</sup>

QR's stakeholders proposed time frames for QR notifying a refusal to negotiate varying from 7 to 21 days. The QCA considers that a period of 14 days for QR to notify an access seeker of its refusal to enter into an access agreement would protect QR's legitimate business interests and the interests of access seekers.

***QCA's Position***

**The QCA would favourably consider an Undertaking that:**

- **required QR to enter into negotiations with an access seeker in order that it could establish whether the circumstances for a refusal to enter into an access agreement are met;**
- **placed the onus on QR to justify its refusal to enter into an access agreement by demonstrating that the access seeker was not capable of meeting the terms and conditions specified in its proposed access agreement in a material way;**
- **required where QR established the circumstances for a refusal to enter into an access agreement to provide written reasons for its refusal to the access seeker within 14 days; and**
- **adopted the following definition of solvency;**

**“Solvent” means none of the following events have happened in relation to the access seeker:**

- (a) **the access seeker operator is unable to pay all its debts as and when they become due and payable or it has failed to comply with a statutory demand as provided in Section 459F(1) of the Corporations Law;**
- (b) **a meeting is convened to pass a resolution to place it in voluntary liquidation or to appoint an administrator, unless the resolution is withdrawn within 14 days or the resolution fails to pass;**
- (c) **an application is made to a court for it to be wound up and the application is not dismissed within one month;**
- (d) **the appointment of a controller (as defined in the Corporations Law) of any of its assets, if that appointment is not revoked within 14 days after it is**

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<sup>84</sup> The TAF Telecommunications Access Code states that the access provider should exercise its rights in 'a timely manner'. Further, the access provider must cooperate reasonably with an access seeker who wishes to discuss reasons for refusal.

**made; or**

**(e) the access seeker resolves to enter into or enters into any form of arrangement (formal or informal) with its creditors or any of them, including a deed of company arrangement;**

- **removed clause 4.1.2(d) included the following principle for negotiating in respect of committed capacity:**
- **if QR can establish that an application is frivolous or vexatious, it is entitled to recover its costs. QR may seek acknowledgment of an access seeker's liability for costs in such a negotiation.**

## **4.6 Access application process**

Requests for access are to be submitted in the form of an access application: cl 4.3.

### **4.6.1 Information required by QR**

#### ***QR's Position***

To assess an access application, QR will require the third-party operator to provide detailed train service description information concerning its planned operations as set out in Schedule C: para 4.3(b). Prior to submitting the access application, the third-party operator may seek initial meetings with QR to discuss the Schedule C requirements and other relevant matters concerning the access application process.

QR requires train service description information for freight services as follows:

- route of operation;
- required term of agreement;
- method of transporting freight;
- description of freight;
- net tonnes per annum for years 1 to 4 and onwards from year 4 (including seasonal peak tonnages if relevant);
- access to stations and any storage/load/unload facilities;
- storage/serving locations, repositioning requirements;
- required frequency of the proposed train services, including specific daily/weekly requirements, seasonal variations and any trends over the agreement term;
- general train details (that is, proposed number of locomotives and wagons per train; type, class and mass of locomotives and nominal gross mass of wagons; tare mass of each wagon and per container; average number of containers per wagon; average proposed

load per wagons; maximum proposed gross tonnes per wagon; axle load/spacing; wheel size; gross tonnes per train service, forward and return; and

- maximum operational speed of loaded and empty train.

QR requires train service description information for passenger services as follows:

- route of operation;
- required term of agreement;
- type of passenger traffic, for example, long distance, commuter, tourist;
- embarking and disembarking stations en route, facilities required at stations and estimated dwell time;
- stabling/servicing locations, empty returning/repositioning requirements;
- required frequency of train services, including specific daily requirements, weekly requirements, seasonality variations and any trends over the agreement term;
- general train details (that is, total number of locomotives and carriages per train; total number of passenger multiple units (PMUs) per train; type class and mass of locomotives; type, class and nominal gross mass of carriages; tare mass per carriage; type, class and nominal gross mass of PMU, axle load/spacing; wheel size; gross tonnes per train service, forward and return); and
- maximum operation speed of loaded and empty train.

QR argued in its initial submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* that the information specified in Schedule C is no more than is reasonably necessary for the purposes of QR preparing an indicative access proposal. It argued that any operator serious about gaining access would be able to provide this information, or at least make reasonable assumptions and that the proposed process allows for fine-tuning at a later date.

QR's supplementary submission to *Queensland Rail Draft Undertaking* proposed to extend the information in Schedule C to detail more specifically the commodity to be carried so that QR could better inform itself of situations where competing operators seek to carry the same product for an end-user.

#### **Table 10: Schedule C information requirements**

**FreightCorp, RTBU, Stanwell** - the information set out in Schedule C is reasonable, although some details would not be known at the early stage of an access negotiation process.

**FreightCorp** - Schedule C needs to be sufficiently flexible to accommodate differences between services.

**AMC** - the details required by QR seem reasonable for an Undertaking that only allows third-party operators to hold access rights (an approach which is seriously flawed).

**National Rail, QMC, Toll** - the information requirement is excessive.

**National Rail** - the access seeker should provide what it thinks is sufficient, with QR having the opportunity to request supplementary information.

**QMC** - many details requested may not be determined at the stage a prospective train operator would want to obtain indicative access information.

**Toll** - there should be an express provision that information can only be required to the extent reasonably necessary to enable QR to provide detailed rates and availability. In addition, much of the information which QR seeks will depend on the contracts which the train operator succeeds in obtaining.

**Queensland Government** - the QCA should be guided by QR and prospective access seekers on this matter.

### *QCA's Analysis*

The QCA recognises that it is in QR's legitimate business interests to specify information requirements from potential access seekers in order for it to make a sound assessment of its ability to meet their access requirements. Access seekers' interests are also served to the extent QR can prepare a better indicative access proposal as a result of the information requirements. However, the QCA recognises that the potential exists for QR to seek more information from access seekers, with its associated cost, than is necessary to prepare a sound indicative access proposal. Also, an important issue is the timing of information exchange, including whether QR provides information to access seekers first.

The QCA has clarified with QR that paragraphs 4.3(c) and (d) envisage a process whereby the access seeker can seek Schedule D preliminary information from QR before it is required to provide the Schedule C information. The Authority considers this sequencing is necessary to facilitate the access negotiation process and that the Undertaking should provide an explicit right for an access seeker to receive Schedule D information before providing Schedule C information.

The operational and service description information requested by QR from the access seeker appears to be broadly similar to that requested by other rail access providers, although it appears to be more prescriptive.

The draft Western Australian Railways Access Code requires a third-party operator's access proposal to specify the route, including infrastructure, to which access is sought, indicate the times when access is required and set out the nature of the proposed operations. ARTC requires from an operator an operational plan (planned movements including origin destination shunts if possible, preferred speed/train type), locomotive type and specification and wagon type. ARTC does not require any commercial information from access seekers.

The NSW rail access regime requires RAC to commence negotiations once it has received from the access seeker operational specifications, which comply with available capacity of facilities. These operational specifications include time of entry to and exit from the route, duration of use, maximum speeds, maximum axle loads, commodities to be carried, technical specifications of rollingstock and rail infrastructure facilities, and operational and safety standards.<sup>85</sup>

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<sup>85</sup> The access application processes followed in access regimes for the telecommunications and gas industries in Australia are broadly similar to that proposed by QR, such that the access provider is required to have an information package available for each declared service to all potential access seekers who request it. These information packages include a description of the access application process to be followed, any relevant access arrangements/access Undertakings and technical and capacity information for the relevant service. The TAF Telecommunications Access Code also specifies that security requirements and any confidentiality agreements be outlined in the information package. In addition, the Telecommunications Access Code also provides for the information package to include, if requested by the access seeker, a reasonable degree of information relevant to how the access provider proposes to take steps to ensure technical and operational quality and timing of the interconnection will be equivalent to that which it provides itself.

It is important to recognise that a prescriptive information requirement will reduce the potential for disputes, provided the requirements are not excessive. However, some stakeholders have raised concerns that some of the detail required by QR may not be known at the preliminary stage of the access negotiation process. The QCA considers that in order not to unduly inhibit the progress of negotiations, it is important that the information exchange process is flexible to accommodate unknown factors or differences between products. In this regard, QR indicates that it is not seeking definitive positions from access seekers, but rather reasonable assumptions about the proposed operations. Given this, it is important that access seekers are able to revisit the Schedule C information they provide during the course of negotiations.

Indeed an iterative process is likely to form a critical part of any negotiation process. For example, where a potential third-party operator's arrangements depart from QR's, there will need to be an assessment of the capacity implications of the departure. Clearly, it is necessary for information to be exchanged as part of the negotiation process. However, it is impossible to foreshadow all possible information requests that may arise in the future.

Finally, the QCA notes that the development of reference tariffs should substantially alleviate the concerns expressed by stakeholders for the services that those tariffs apply to. Initially, this will be limited to the coal carrying services on the Blackwater, Goonyella, Moura and Newlands systems. However, section 5.3 of Chapter 5 foreshadows that reference tariffs may also be developed for other services including West Moreton coal, and the Mt Isa and North Coast lines.

#### ***QCA's Position***

**The QCA would favourably consider an Undertaking that:**

- **allows access seekers the opportunity to revisit the Schedule C information that they provide as the negotiation process proceeds; and**
- **imposes an obligation on QR to provide Schedule D preliminary information before it requires Schedule C information, provided the costs of provision are met.**

#### **4.6.2 Information provided by QR**

##### ***QR's Position***

If requested by the third-party operator, QR will provide information regarding the corridor of interest to assist in the formulation of the access application. This information will be in the form of preliminary information and will include the information outlined in Part One of Schedule D (or such items in this schedule as are required by the third-party operator): para 4.3(c).

QR will use reasonable efforts to make the preliminary information available to the third-party operator, either within 14 days, if the preliminary information has been previously compiled, or otherwise within 30 days of QR receiving the request: para 4.3(d).

If the application progresses to the negotiation phase, QR undertakes to provide additional information regarding the corridor of interest, including any information outlined in Part One of Schedule D not provided as part of the preliminary information and the information outlined in Part Two of Schedule D, to the extent such information is required by either the third-party

operator or as part of the access agreement: para 4.7.2(a). QR argued in its initial submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* that Schedule D sets out all the operational information a third-party operator should require.

Part One of Schedule D (preliminary information) is as follows:

1.1 Introduction

1.2 Technical information

- Civil infrastructure (description of track, operational constraints).
- Signals and operational systems (description of safeworking systems).
- Telecommunications (description of communications system used).
- Electric traction (general system description).
- Rollingstock interface requirements (track gauge, axle load, train speed, minimum structure gauge, noise limits).
- Locality information (terrain information, environmental conditions).
- Committed and/or potential corridor upgrades.
- Relevant maps and drawings (corridor maps, working plan and section drawings).
- Level crossings (number of level crossings, type of protection used).

1.3 Operational information

- Capacity (indication of capacity utilisation for the nominated network, general description of known capacity constraints, committed capacity upgrades).
- Train operation (sectional running times, maximum train length).
- Description of systems (operational, safeworking).

1.4 Commercial information

- Reference tariffs.
- Cost allocation manual.

1.5 Policies

- QR's standard access agreement<sup>86</sup>

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<sup>86</sup> The Draft Undertaking currently contains the principles relating to QR's standard access agreement. Acceptance by the QCA of Schedule E, or variant of, as part of the Undertaking does not imply the QCA endorses any particular agreement devised by QR. However, such an agreement, outlining proposed terms and conditions of access, should be provided to access seekers as part of Schedule D information.

- Undertaking.
- Ring-Fencing Guidelines.
- Processes for authorisation of rollingstock.
- Process for authorisation of rollingstock configurations.
- Scheduling and train control protocols.

Schedule D (additional information) comprises the rollingstock interface standards and train standards applicable for the system(s) on which the third-party operator's train services will run.

QR will be entitled to levy an appropriate charge commensurate with the cost of preparation and supply of preliminary information: para 4.3(f). The issue of charging for information provision by QR is addressed in section 4.5.4 of this chapter.

In subsequent discussions with the QCA, QR advised its intention to prepare an Information Pack for each of the fourteen systems on its network:

- Brisbane Metropolitan/Suburban;
- North Coast Line;
- Mt Isa Line;
- Goonyella;
- Blackwater;
- Moura;
- Newlands;
- Tablelands;
- Central West;
- South West;
- Western;
- Mainline;
- Maryborough; and
- Standard/dual gauge.

The information packs for the coal systems (Blackwater, Goonyella, Moura, Newlands) are being prepared first, with the remainder to be completed on a rolling basis.<sup>87</sup> QR advised the

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<sup>87</sup> QR has produced final versions of the Newlands, Goonyella and Moura information packs. Drafts of the Blackwater & Mt Isa packs are expected to be finalised by December 2000.

QCA that the packs will be reviewed annually, however, any safety critical changes will be advised to existing operators through QR's other information systems.

QR's intention is that the information packs will fulfil its Schedule D (preliminary information) obligations concerning the provision of technical/operational information and it will be made available on request at any point in time.

QR proposes that its information packs will contain the following information:

- General information;
  - general description of the system, including map.
- Business environment;
  - brief description of customers/businesses on system, for example, mines and processing plants; and
  - statement as to whether the line receives any operating subsidy from Government.
- General climate.
- Description of the railway;
  - description of line, including facilities (any marshalling yards, passing loops), sleeper construction, curvature of track and maximum axle load and speed, for particular segments of line; and
  - brief description of terrain for particular segments of line.
- Integrity of permanent way corridor;
  - description of fencing.
- Description of the track;
  - description of track, speed through curves, management of wheel/rail interaction.
- Operational constraints – rollingstock;
  - diagram showing design, in accordance with which rollingstock can operate in an unrestricted manner.
- Operational constraints – infrastructure;
  - maximum grade encountered by a loaded/empty train on the system;
  - minimum horizontal curve radius for new or upgrade works;
  - existing minimum horizontal curve radii for segments of line; and
  - speed restrictions.
- Trackside detection equipment.

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- Weighbridges.
  - Operational systems and train control.
  - Information systems.
  - System capacity;
    - defined in terms of standard train paths/day, between stations (average usage and percentage committed capacity).
  - Sectional running times.
  - Communications;
    - description of channels used.
  - Incident recovery time and management;
    - including description of latitude and longitude of passing loops.
  - Rail/road interfaces.
  - Rail operations and the environment;
    - noise levels.
  - Crossing loop lengths.
  - Rollingstock braking rate.
  - Future planned infrastructure improvements (subject to funding availability).
  - Infrastructure management and access;
    - schematic layout indicating which QR business group is responsible for managing the different elements of QR's declared and non-declared infrastructure and assets; and
    - initial point of contact.
  - Appendices;
    - definitions;
    - rail/road interface details;
    - Speed Boards; and
    - Working plan and sections (curve and gradient diagrams where available).

QR stated in its initial submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* it would object to an obligation to provide any other operational information, irrespective of any ability to charge an appropriate amount for that information. QR believes Schedule D sets out all the information a third-party operator should reasonably require and any

further obligation would allow a potential for abuse. QR claims such an obligation might enable a third-party operator to seek information that might be the intellectual property of QR or might otherwise undermine the competitive position of QR. Alternatively, QR may be asked to provide information in a non-standard format, or provide interpretation or analysis of the information provided. QR claims, even in regard to below-rail information, it needs to protect commercially sensitive information that could be used by potential competitors for the operation and construction of new railways.

In its supplementary submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*, QR indicated a preference to deal with any perceived deficiencies in Schedule D now.

### ***Stakeholder Comment***

While views diverged, a majority of stakeholders believed that the information in Schedule D (in the form that it was then in) was insufficient.

#### **Table 11: Schedule D information provision by QR**

**AMC, FreightCorp, QMC, Stanwell, Toll** - the information is not sufficient for the access seeker to proceed with an application.

**AMC, Stanwell** - it should include an indicative tariff, which could be used in conjunction with a 'bulletin board' of all access prices, including reference tariffs;

**FreightCorp, QMC** - an operator will not be able to provide Schedule C information without knowing at least part of Schedule D information.

**FreightCorp** - Schedule D should include full copies of the working timetable plus any supplements and the general appendix to the working timetable and relevant train diagrams, to the extent these provide information not otherwise contained in Schedule D.

**Toll** - an access seeker will need much of the Schedule D material for the preparation of Schedule C. QR should provide detailed costing information.

**Queensland Government** - the preliminary and additional information (Schedule D) which QR provides to prospective third-party operators has little information on costs. While the physical/technical description of the rail system is an important component of information, meaningful information on costs (ie. operating costs to maintain a line, train control costs, capital costs, etc) are crucial to the third-party operator in the context of negotiations for access.

**National Rail, RTBU** – the information provided by QR is sufficient. National Rail stated that QR should provide information about quality of service and how it will be measured.

A majority of submissions considered it was reasonable for QR to provide additional information reasonably required by a third-party operator. However, there was a divergence of views regarding payment for that information.

#### **Table 12: Additional information provision by QR**

**QMC** - the provision of information to enable access seekers to evaluate and respond to the proposed service is a basic obligation of Network Access. The preliminary information provided must be sufficient to ensure the access seeker is not disadvantaged compared to any incumbent.

**FreightCorp** - QR should be willing to provide additional information where an access seeker is willing to pay for it. However, QR should not have to provide commercially sensitive information regarding its internal train operators that it would otherwise not disclose.

**AMC, Stanwell** - no charges should apply for reasonable information requests as this is part of Network Access' normal business. Only if a request is considered unreasonable, after reference to the QCA, should it attract a cost, or Network Access may be allowed not to respond.

**Toll** - access seekers should not have to pay QR's costs to obtain basic access information and Network Access should have sufficient transparency to enable access charge information to be obtained easily.

**Queensland Government** - the Undertaking should not constrain the information to be provided to the third-party operator. However, it may be appropriate for the third-party operator to pay a reasonable cost for information given which is above the standard information provided.

**ARTC** - it is reasonable for Network Access to charge for information beyond any threshold requirement. This information should be proprietary to Network Access and should not be ordinarily available to QR's business groups. The pricing methodology should be included in the Undertaking. However, if such an arrangement is not possible, third-party operators should not be charged as it cannot be done on an equitable basis.

**RTBU** - QR should not be under an obligation to provide more information as this is a matter for commercial negotiation.

### ***QCA's Analysis***

It is in an access seeker's interests to receive enough information from QR to make a meaningful assessment of its ability to run commercial train services on QR's network. Similarly, if QR is genuine about selling access to its network, the QCA would expect it to provide sufficient information to access seekers to enable them to make a sound assessment of above-rail business opportunities.

S101 of the QCA Act states that an access provider must make all reasonable efforts to try to satisfy the reasonable requirements of an access seeker. This requirement is mirrored in cl 6(4)(3) of the Competition Principles Agreement. In addition, the QCA considers it is important the information exchange process be sufficiently flexible to allow both parties to obtain the reasonable information necessary to proceed with the application process. However, the QCA also recognises, in practice, the gathering and dissemination of information is not a costless exercise for QR and the potential exists for QR to be asked to provide commercially sensitive information. It is in QR's legitimate business interests to have some constraint on information provision. The key issue for the QCA is where the line is drawn.

The QCA, with the assistance of Rail Management Services Pty Ltd, has assessed the content of QR's information pack for the Newlands system. In general, the Authority considers that the Newlands Information Pack (the Newlands pack) describes the technical and operational characteristics of that system in a concise and well-structured manner. In addition, the information contained in the Newlands pack is consistent with sections 1.2 (technical information) and 1.3 (operational information) of Schedule D (preliminary information).

While the Newlands pack provides a generally thorough outline of the system's existing operational and technical characteristics, the QCA considers it is important that the pack does not give a misleading impression of the potential operational capabilities of the system. For example, the line is approved for 20 tonne axle loads but is constructed of components that are used elsewhere on the QR system in a 22 tonne axle load configuration. In some parts of QR's coal network, 26 tonne axle load wagons are running on exactly the same configuration. In addition, the supplied envelope for rollingstock represents a minimum position for all non-electric rollingstock over QR's entire system. Nevertheless, QR already has rollingstock operating outside the supplied envelope elsewhere on its coal systems. Consequently, it is important that the information packs do not convey existing QR configurations as binding technical/operational limits where this is not the case.

In this regard, the QCA recognises the Newlands pack notes that rollingstock not conforming with the supplied envelope may be accepted via the rollingstock authorisation process and may be operated subject to constraints imposed as a result of that process. In principle, QR should be prepared to negotiate with third-party operators regarding operational differences where this is feasible.

To further assess the reasonableness of the information QR is proposing to provide, the QCA has reviewed the information provided by rail access providers in other Australian jurisdictions.

Under the proposed Western Australian rail access regime, Westrail is required to prepare and make available for purchase as soon as practicable after the commencement of the rail access code, a publication containing the form of its standard access agreement, a map of the routes to which the code applies and, for each route section, details of: length, ruling grades, operating gauge, track design characteristics, indicative running times, maximum axle loads and speed restrictions that apply and indicative maximum train lengths. It must also include permissible gauge outlines that enable the required dimensions of rollingstock to be determined.

Following a request from an access seeker, Westrail is also to provide an initial indication of available capacity, price, terms and conditions and obligations it would want included in an agreement, gross tonnes carried on the relevant route section in the preceding three years and curve and gradient diagrams. In addition, it must provide working timetables, information on the origin and destination of any train path proposed by it for that route and any technical information relevant to the design of rollingstock.

Under the Northern Territory/South Australia Rail Access regime,<sup>88</sup> the access provider must, on the application of any person, provide information reasonably requested about the extent to which the access provider's railway infrastructure facilities are currently being used, technical details and requirements of the access provider (such as axle load data, clearance and running speeds) and whether the access provider would be prepared to provide a railway infrastructure service of a specified description.

ARTC's defined network and pricing and standard access agreement is publicly available on its web site. Information on capacity and any other technical information (eg track dimensions) are provided to access seekers on request. It does not provide any commercial information relating to ARTC. In general, ARTC provides as much information as an access seeker requires on an 'as needs' basis, reflecting that it is trying to encourage users, and users need certain information in order to progress access.

In assessing the effectiveness of the NSW rail access regime, the NCC required the NSW Government to impose upon the provider of below-rail services (RAC) very prescriptive provisions regarding the information it should provide access seekers. It included an obligation to provide detailed information on: network configuration, recurrent costs, capital costs, system usage, operational and other information, unutilised capacity, and arbitration information.<sup>89</sup> However, the NSW regime allows RAC to exclude the provision of information which could lead to material harm to any access seeker if disclosed, or to re-categorise or aggregate the information to the extent necessary to ensure the disclosure of information does not or is not likely to lead to material harm to the interests of RAC or access seekers.

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<sup>88</sup> The AustralAsia Railway (Third-party Access) Code 1999 is embodied in a schedule to the AustralAsia Railway (Third-party Access) Bill (NT) 1999 and in the AustralAsia Railway (Third-party Access) Bill (SA) 1999. In February 2000, the NCC recommended that the regime be certified.

<sup>89</sup> However, it should be noted that RAC does not provide reference tariffs. In the absence of reference tariffs, more detailed costing information would seem appropriate.

*Additional information*

The QCA considers a willingness to provide additional information to access seekers, that is, more than that foreshadowed in Schedule D, is not an unreasonable position for QR to adopt if it has a genuine commitment to sell access. Further, as noted earlier, the process of gaining access will be enhanced if the information exchange process is flexible. ARTC acknowledges that the process is iterative, requiring communication between the parties rather than a definitive ‘yes/no’ process.<sup>90</sup>

Moreover, s101 of the QCA Act imposes an obligation on an access provider to make all reasonable efforts to satisfy the reasonable requirements of the access seeker. Ss101(2) lists the information that an access provider must give the access seeker, including information about the access price (and the pricing methodology), costs (including capital, operations and maintenance), asset values (and the asset valuation methodology) and spare capacity (including the way in which it is calculated).

However, ss101(3) provides some protection to the access provider with respect to this information disclosure. If the QCA reasonably considers that disclosure may damage the commercial activities of the access provider, the Authority may either categorise or aggregate the information so disclosure is not unduly damaging or alternatively authorise that the access provider not give the access seeker the potentially damaging information.

The QCA considers that ss101(3) addresses QR’s concern that access seekers could obtain commercially sensitive information from it. In practice, the QCA would have to identify when information is confidential and whether, in appropriate cases, other mechanisms could protect QR’s legitimate business interests, for example, confidentiality agreements between QR and third-party operators or the normal legal protection of intellectual property. In addition, a majority of stakeholders accepted they should pay for any additional information required from QR.

The QCA notes stakeholder concerns about the lack of information in Schedule D relating to price and cost information. The QCA considers QR’s commitment to provide reference tariffs as part of Schedule D would meet its commitment under ss101(2) regarding price information for its coal corridors. The development of reference tariffs for corridors beyond those foreshadowed in the Draft Undertaking is also a possibility in the future (for example, North Coast Line). This issue is discussed in Chapter 5.

Nevertheless, the issue of what sort of price information should be provided with respect to corridors where reference tariffs are not proposed in the Draft Undertaking arises. The QCA believes QR should comply with the requirements of ss101(2) and ss101(3) of the QCA Act. This would entail QR providing its access price and associated methodology, which would assist an access seeker to assess the commercial viability of its planned train services. However, to meet its legislative commitments, supplementary capital, operation and maintenance cost information for the relevant rail corridor would also need to be provided. The QCA Act provides that this information is to be made available unless the QCA authorises QR to do otherwise. No request for the Authority’s advice or directions about these matters has been received from QR.

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<sup>90</sup> The TAF Telecommunications Access Code supports this approach, stating that an access provider should use reasonable endeavours to cooperate with potential access seekers’ reasonable requests from time to time for additional information to enable the formation of a request for supply. The Code specifies that access providers and access seekers acknowledge the exchange of information during the application phase is an iterative process, whereby each party assesses the requirements and capabilities of the other over a period of time and after several exchanges of information. An access provider’s application process should recognise this and should facilitate this process rather than hinder it.

The QCA also considers that as part of Schedule D, QR should disclose sufficient capacity information to allow access seekers to conduct their own capacity analysis. This is discussed as part of capacity management matters in section 6.4 of Chapter 6.

***QCA's Position***

**The QCA would favourably consider an Undertaking that for rail corridors where no reference tariffs apply, incorporates in the Schedule D preliminary information, price and costing information consistent with ss101(2) and ss101(3) of the QCA Act.**

### 4.6.3 QR's obligation to provide accurate and up-to-date information

***QR's Position***

QR will use reasonable efforts to ensure any information provided will reflect the most current information available to QR. Further, QR will identify the currency of the information provided: para 4.3(e).

QR argued, in its initial submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*, that a 'reasonable efforts' obligation to provide up-to-date and accurate information is appropriate as the information to be provided is not always available from a single source or regularly updated given the size of QR's network. However, QR noted the accuracy of information would be unlikely to have an impact on an access seeker's proposal at the access application stage.

QR also noted it has legal obligations with respect to misleading or deceptive conduct and, further, it is establishing systems to collate and make relevant information available to access seekers. However, given the size of QR's network and the ongoing changes that occur, QR argued it would be impractical to guarantee that the information provided is the most up-to-date at any point in time. The cost of providing systems to ensure constantly up-to-date information, including insurance against liability, would be prohibitive and ultimately borne by end-users.

QR advised the QCA that its intentions to review the information packs annually would mean that the information provided to access seekers would be one year out of date at the most. However, any changes affecting safety would immediately be made known to current operators using the network.

Stakeholder submissions were split roughly equally between those that thought a 'reasonable efforts' obligation was appropriate and those that thought such an obligation was too weak.

**Table 13: Currency of information of information provided by QR**

**AMC, FreightCorp, QMC, Stanwell** - a 'reasonable efforts' obligation is appropriate.

**FreightCorp** - the clause should also require the information to be accurate, again with reasonable efforts.

**Toll** - such an obligation is not sufficient. The obligation on QR should be absolute and damages should be recoverable if loss is suffered as a consequence of inaccurate information.

**Great Southern Railway** - QR should be responsible if it provided information that is incorrect.

**Queensland Government** - QR should be required to ensure information it provides to third-party operators is accurate and is as current as possible given the currency of information that QR has available itself. During the negotiation process it is crucial that QR provides accurate and current information, and descriptions like ‘reasonable endeavours’ and ‘reasonable efforts’ may be insufficient. QR is the only source of essential information and has a responsibility to provide accurate information or be prepared to face the consequences of incorrect information. In circumstances where it is not possible to provide definitive information, that fact should be clearly stated and a reason provided.

**RTBU** - QR’s legal liability, if found to negligently provide incorrect information, should provide sufficient incentive.

### *QCA’s Analysis*

From a theoretical perspective, the risk associated with not providing accurate or up-to-date information should be assigned to QR because, as railway manager, it has a greater knowledge of the network than any other party.<sup>91</sup> The QCA understands that, if QR provides information to access seekers, it has statutory, common law and equitable obligations to ensure the accuracy of that information. Further, it is unlikely that the existence of an approved Undertaking will have any effect on QR’s general law obligation to provide an access seeker with accurate information.

Consequently, the QCA does not consider it is necessary for QR to include a guarantee of accuracy in the Draft Undertaking, as QR’s legal obligations will provide adequate protection to access seekers’ interests. A ‘reasonable efforts’ obligation is appropriate having regard to the stage of the negotiation process, the importance of the information to an access seeker, and the general law. QR’s legitimate business interests are protected by provision of such an obligation in an approved Undertaking.

In terms of other rail access regimes, the proposed Northern Territory/South Australia rail access regime, RAC and ARTC<sup>92</sup> do not provide any legal warranty as to the accuracy of information they provide to access seekers. The Western Australian Rail Access Code requires Westrail to review, and amend or replace, its published information package as often as is necessary to ensure the details in it remain reasonably current at all times.

#### *QCA’s Position*

**The QCA accepts QR committing to provide a ‘reasonable efforts’ obligation to ensure the information it provides access seekers is up-to-date and accurate.**

### **4.6.4 Appropriateness and basis of fees for information provision by QR**

#### *QR’s Position*

For the provision of preliminary information (Part One, Schedule D) under cl 4.3 (access application) and the provision of additional information (Part Two, Schedule D) under sub-cl 4.7.2 (Issues to be addressed during negotiation), QR reserves itself the right to levy an

<sup>91</sup> The nature and currency of the network information at QR’s disposal will be a function of the trade-off between the quality of QR’s internal management system and the cost of establishing and maintaining it.

<sup>92</sup> While ARTC’s access agreement currently contains a clause providing a warranty as to accuracy of information, discussions with ARTC indicate that current negotiations with operators are likely to result in such a warranty by either party being dropped. This is because indemnity clauses are likely to move to a cause-based arrangement.

appropriate charge commensurate with the cost of preparation and supply of that information: para 4.3(f). QR has also indirectly addressed this issue in the context of Schedule D (refer sub-section 4.5.2 of this chapter), rejecting the provision of additional information to access seekers regardless of payment for that information.

QR has subsequently advised the QCA that it will charge a fee of approximately \$500 for the information packs. Where an access proposal is more complex and requires more detailed analysis, including perhaps design work, QR intends to charge the access seeker an amount commensurate with the cost of preparation.

A small majority of the stakeholders thought it is reasonable for QR to charge fees, however, there was some variance in views on the basis of the fee.

#### **Table 14: Fees for information provision**

**Great Southern Railway** - the basis of the fee should be established as part of the Undertaking.

**RTBU** - the fee should be negotiated in the course of the access application.

**ARTC** - it is reasonable for Network Access to charge for information that is beyond any threshold requirement of the pricing methodology included in the Undertaking.

**Queensland Government** - it appears reasonable for QR to impose a charge for the provision of preliminary information, and this is consistent with the current user-pays philosophy. It would be reasonable that the basis for the charge (and perhaps an indication of the likely level of the charge) should be included within the Undertaking and therefore be subject to QCA consideration.

**FreightCorp** - the fee should discourage frivolous requests and allow QR to cover the costs of information gathering and dissemination.

**Toll** - charges should not be on an individual request basis, but included as part of Network Access' overheads.

**AMC** - costs associated with provision of information to access seekers should be included in 'common costs' and recovered from access charges. This approach would ensure charging for information did not become a barrier to entry.

**National Rail** - information provision is in the nature of a price quotation and should therefore be free.

#### ***QCA's Analysis***

The QCA considers that QR should be able to reserve itself the right to charge fees to recover the costs of information gathering and dissemination. In the normal course of events, the QCA would not expect the level of these fees to be significant. QR's proposed fee of \$500 for the information packs is consistent with the Authority's expectations.

The precedent of charging a basic fee for information provision appears to be established in other access regimes. The NSW rail access regime states that RAC may require the payment of a reasonable fee for copying its information package. The Northern Territory/South Australia Rail Access regime allows the access provider to make a reasonable charge, to be determined on a basis approved by the regulator, for providing information to access seekers. The WA rail access regime allows Westrail to make a reasonable charge for supplying a copy of its information package. ARTC does not currently charge for information, however, it would not

rule it out in future in the event it had to consider a more complex and costly access application requiring, for example, a feasibility study.<sup>93</sup>

The QCA agrees that payment of a fee by access seekers should prevent frivolous access requests, while allowing QR to recoup the costs of gathering and disseminating information. In this way, QR's legitimate business interests would be protected and entry by genuine access seekers facilitated.

Nevertheless, the QCA considers that the basis of the fee(s) should be contained in the Undertaking for greater transparency and to constrain Network Access exploiting its information advantage. A number of stakeholders supported this position. In discussions with the QCA, QR indicated a preference to develop a set of principles to guide fee setting rather than, for example, a schedule of hourly rates paid to staff. The key principle would be that the level of fees for information should be tied to the costs of provision. The QCA supports the development of principles along these lines, considering that it would be a useful guide in the event of any disputes emerging over the level of the fee.

The QCA does not consider it appropriate that QR be entitled to charge fees for the processing of access applications, for example, responding to requests for access charges. Allowing Network Access to charge fees for the processing of applications could adversely affect the evolution of the above-rail market.

#### *QCA's Position*

**The QCA accepts QR establishing a right to charge fees for information provision, provided such fees reflect the costs of provision, and guiding principles regarding the setting of fees are established in the Undertaking. A fee of \$500 for an Information Pack is acceptable to the QCA.**

#### 4.6.5 Time frames for action

##### *QR's Position*

QR will provide a number of commitments upon receiving an access application including:

- providing a written acknowledgment within seven days of receipt; or
- seeking additional information or clarifying existing information within seven days of receipt and acknowledging receipt of such information within a further seven days: paras 4.4(a) & (b).

QR will provide an indicative access proposal within 30 days of acknowledgment of an access application, unless extenuating circumstances exist: para 4.4(c). In these cases, QR undertakes

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<sup>93</sup> The TAF Telecommunications Access Code states that an access provider should not charge a prohibitive fee for the provision of its information package. Similarly, to gain access to the electricity network, a connection applicant must pay a fee when lodging its application to connect, with the amount not being more than is necessary to cover the reasonable costs of all work anticipated to arise from investigating the application and preparing the offer to connect. However, the Access Code for Natural Gas Pipeline Systems states that the service provider may require payment of a reasonable fee (determined in a manner approved by the regulator) for copying the Access Arrangement information, but must not charge a fee for any other item in the information package. (The Access Arrangement is a statement of the policies and basic terms and conditions that apply to third-party access to a covered pipeline.)

to notify the applicant of the expected delivery of the indicative access proposal within seven days of acknowledgment and use reasonable efforts to meet this time frame. QR provides some examples of such circumstances, including major impediments to the provision of the necessary capacity, fundamental changes in technical or operational parameters and abnormal work commitments within Network Access.

If after 30 days following QR's acknowledgment of the access application, the third-party operator believes that QR is not making reasonable progress in the preparation of the proposal, then it may refer the matter to the QCA for a determination in accordance with sub-cl 4.9.4 of the Draft Undertaking: para 4.5(c).

A third-party operator wishing to proceed to the access negotiation phase must notify QR of its intention in writing within 90 days of receiving an indicative access proposal (unless otherwise agreed). If QR receives a notification of intent after this limit, it reserves the right to revise the indicative access proposal. However, QR does not propose to provide the access seeker with written advice outlining the reasons for any revisions: para 4.6(a).

A prospective third-party operator concerned that an indicative access proposal has not been prepared in accordance with the Undertaking will need to notify QR within 30 days of its receipt: para 4.6(b).

QR will respond to these concerns, including revising the indicative access proposal, within a reasonable time frame. If the third-party operator is satisfied with the response received from QR, including any revision to an indicative access proposal, it must notify QR of its intention to proceed with negotiations within 30 days of receiving QR's response. In the event that the third-party operator is not satisfied with QR's response, including any revision to the indicative access proposal, there is a limit of 30 days for a prospective third-party operator to trigger the dispute resolution process: para 4.6(c).

Finally, the prospective operator must notify QR in writing within 14 days of the dispute being resolved if it wishes to proceed with an access application: para 4.6(d).

QR did not address the issue of whether the Undertaking should restrict a access seekers' recourse to dispute resolution, or the issues to be resolved in that dispute resolution, in either of its submissions to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*.

### ***Stakeholder Comment***

There was general agreement that the time frames allowed are acceptable. However, a concern was expressed regarding the time frame within which a third-party operator would have to respond to QR if it had a problem with an indicative access proposal. Also, the lack of a time frame within which QR would have to respond to the third-party operator's concerns was queried.

#### **Table 15: QR's acknowledgment of receipt of access application**

**AMC, FreightCorp, Queensland Government, QMC, Stanwell, Toll** - the time frames are reasonable.

**Queensland Government** - if QR felt it necessary to provide a response beyond the standard 30 days, it should be required to justify that time frame.

**Table 16: Access seekers' notification of intent to progress access application**

**AMC, QMC, Stanwell** - the proposed time frames are reasonable.

**Queensland Government** - third-party operators would be in the best position to determine the reasonableness of the proposed time limits.

**Toll** - the time limits proposed in 4.6(b), (c) and (d) are unreasonable. The limit in (b) should be 90 days as it will require some detailed consideration to determine whether an indicative access proposal is not in accordance with the Undertaking. There is currently no time limit imposed upon QR to respond to a third-party operator's concern that the indicative access proposal is not in accordance with the Undertaking, and such a limit should be imposed. 60 days would be appropriate. The remaining time periods in paragraphs (c) and (d) should be 30 days.

**FreightCorp** - the provisions for notification are appropriate. However, in respect of 4.6(c), the Undertaking does not provide for the situation in which QR fails to respond in 'a reasonable time frame'. In this instance, it is not apparent whether there is any time limit on the operator triggering the dispute resolution process. The Undertaking should provide for an operator to trigger the dispute resolution process at any time where it considers that Network Access has failed to respond within a reasonable time.

**Table 17: Restrictions on access seekers' recourse to dispute resolution**

**FreightCorp, QMC, RTBU, Stanwell** - the provisions for notification are appropriate.

**RTBU** - the access process should encourage commercial negotiation and not recourse to the QCA or the courts.

**FreightCorp** - an operator should be able to trigger the dispute resolution process at any time where it considers that Network Access has failed to respond within a reasonable time.

**AMC** - the conditions are reasonable for a descriptive rather than prescriptive process in the Undertaking.

**Queensland Government** - it is reasonable for there to be some constraints in the Undertaking for triggering dispute resolution proceedings. The complete lack of constraints would likely hinder progress rather than expedite it.

**QMC** - 4.5(c) is reasonable provided it does not preclude the access seeker giving notice of a dispute to the QCA earlier in the negotiation and on other grounds, as already provided for in the QCA Act.

***QCA's Analysis***

Given the general support of stakeholders, the QCA accepts the time frames for action proposed in cl 4.4 (acknowledgment) and cl 4.5 (indicative access proposal). However, the Authority has proposed extensions to the time frames in para 4.6(b) and (c) regarding the notification of intent to progress access applications. Subject to stakeholder comment, the QCA considers that the proposed extensions would provide access seekers with greater protection during an access negotiation, while not harming QR's legitimate business interests.

The time frame in para 4.6(b) of 30 days for a third-party operator to inform QR in writing that it considers the indicative access proposal has not been prepared in accordance with the Undertaking is too short and should be extended to 60 days. It is reasonable to expect that to make such an assessment, the access seeker will need to give detailed consideration to the indicative access proposal. In discussions with the QCA, QR has indicated it is prepared to extend the time limit in para 4.6(b) to 60 days.

The QCA also has concerns about the lack of a specific time frame imposed on QR in para 4.6(c), with QR committing to respond to a third-party operator's concerns about the preparation of the indicative access proposal within a 'reasonable time frame'. This open-ended commitment is inconsistent with the strict time frames for action that apply to third-party operators in cl 4.6. In discussions with the QCA, QR has indicated it will insert a time limit in cl 4.6(c) of 30 days, in normal circumstances, however, where the work required is more complex, it proposes to inform the access seeker of when it expects to respond. This would be consistent with para 4.4(c).

The time frame in para 4.6(c), which sets the period in which a third-party operator must notify QR of its intent to proceed with negotiations after receipt of QR's response to previous concerns about the indicative access proposal, should be extended from 30 to 60 days. An access seeker will need sufficient time to consider any revisions to the original indicative access proposal and clear any decisions through the appropriate internal channels.

Para 4.6(c) also limits a third-party operator instigating dispute resolution processes to 30 days following receipt of an indicative access proposal. It is the QCA's view that, in principle, there should not be any time restrictions on the triggering of the QCA Act's dispute resolution processes. Such restrictions are generally likely to be contrary to access seekers' interests.

QR has advised the QCA that the rationale for the time frame of 30 days for the triggering of dispute resolution in relation to indicative access proposals is to provide certainty to QR. It does not want to provide open-ended indicative access proposals given the uncertainty whether the access seeker will pursue the proposal or not. Imposing a time limit on the triggering of dispute resolution is a part of this strategy.

The QCA acknowledges QR's preference not to prepare open-ended indicative access proposals. Nevertheless, the Authority considers that there should be no limit on the triggering of dispute resolution. In practice, access negotiations are likely to be a lengthy, iterative process. Limiting recourse to dispute resolution in such an environment may actually result in more disputes than if there was no limit because access seekers may choose to avoid permanently losing such a right for a particular access negotiation by triggering the dispute resolution process.

Moreover, the QCA considers that QR's proposed three-tiered dispute resolution process (cl 4.9) would provide a reasonable balance between the imposition of reasonable constraints upon dispute resolution and the subsequent relatively quick access to dispute resolution if required by either QR or the access seeker. Cl 4.9 is discussed in section 4.7 below.

#### ***QCA's Position***

**The QCA would favourably consider an Undertaking that:**

- **extends the time frame in paragraph 4.6(b) to 60 days;**
- **amends paragraph 4.6(c) to reflect that QR will respond to concerns including, where appropriate, the making of revisions to the indicative access proposal, within a period of 30 days, under normal circumstances. If the required response is more complex, QR will advise the access seeker within 7 days of receipt of its written concerns regarding the time required to respond, consistent with the indicative access proposal process in paragraph**

**4.4(c);**

- **amends paragraph 4.6(c) to state, if an access seeker is satisfied with the response received from QR, including any revisions to the indicative access proposal, it must notify QR of its intent to proceed with negotiations within 60 days of receiving QR’s response; and**
- **removes the time frame in paragraph 4.6(c) for the triggering of dispute resolution.**

## 4.7 Dispute resolution

### *QR’s Position*

A three-tiered approach to disputes arising under the Undertaking is established: cl 4.9. Initially disputes are to be referred to the chief executive of the respective parties or their nominees within seven days of the dispute notice. Failing resolution of the dispute by the chief executives within 14 days, the dispute may be referred to an expert if both parties agree. Failing such agreement, either party may refer the dispute to the QCA.

In the absence of manifest error, the decision of the expert shall be final and binding upon the parties: para 4.9.3(h). If a party believes there has been a manifest error, it may refer the matter to the QCA for a determination. If the QCA finds that a manifest error has occurred, the parties may agree to refer the dispute to another expert or, failing agreement, either party may refer the dispute to the QCA. If a third-party operator does not comply with a decision of the expert, it will not be entitled to refer the dispute to the QCA and QR will no longer be obligated to continue access negotiations with the operator.

With respect to the proposed three-tiered approach to dispute resolution, in its initial submission to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking*, QR stated that the dispute resolution process is aimed at avoiding delays in the negotiation process. It is for this reason that disputes are referred to the Chief Executives of QR and the relevant third-party operator in the first instance. QR asserted this does not involve unnecessary delay as there is no obligation on parties to come to a resolution in this forum and it is only 14 days before parties may resort to alternative dispute resolution forums.

On the issue of whether QR should be exposed to penalties if it does not comply with an expert’s decision, QR stated in its initial submission to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking* that the statement in the Undertaking that, in the absence of manifest error, the decision of the expert is final and binding, is unambiguous. Neither QR nor a third-party operator can act contrary to an expert’s decision, in the absence of error. QR’s position is that it is inappropriate for the Undertaking to specify penalties for a breach of the Undertaking as the QCA Act provides an avenue for redress.

### *Stakeholder Comment*

Submissions expressed strong views about the proposed three-tiered approach to dispute resolution, however, there was no agreement:

**Table 18: Dispute resolution process**

**AMC, FreightCorp, Stanwell, RTBU** - it is appropriate to have chief executive resolution in the first instance.

**AMC, Stanwell** - provided QR's Chief Executive understands his various roles, this should not be insurmountable.

**Stanwell** - QR and third-party operators should be required to adhere to the expert's finding, and this should be stated in the Undertaking.

**AMC** - a conference of chief executives would seem appropriate as a first step.

**FreightCorp** - should the access seeker believe the QR Chief Executive is not willing or capable of entering into a bona fide process to resolve the dispute, the access seeker has recourse to the QCA.

**QMC** - disputes should be referred to Network Access' General Manager, in keeping with QR's vertically integrated structure.

**Toll** - a separate subsidiary should be established, in which case the dispute resolution could be referred to the Chief Executive Officer of the subsidiary (who reports to the board of the subsidiary and in turn to the QR Board).

**ARTC** - the proposal to have chief executive resolution of disputes is inconsistent with the intent of ring-fencing QR's above and below-rail activities and could serve to undermine industry confidence. Any disputes between Network Access and a third-party operator should be referred to the QCA, with the QCA controlling the expert process if necessary. If this results in too much involvement by the QCA, then the appropriate response is to make the Undertaking more prescriptive. There is no mention of what happens in the event of a dispute between Network Access and another QR business unit.

**AMC, Toll** - the Undertaking should not limit reasons for triggering a dispute.

**AMC** - the grounds for triggering a dispute should be left open as it is not possible to envisage all possible grounds for a dispute at such an early stage of an access negotiation.

With respect to the issue of whether QR should be exposed to penalties for not complying with an expert's decision, no consensus emerged:

**Table 19: Penalties for non-compliance with Undertaking**

**QMC** - penalties for non-compliance should be incorporated in the Undertaking.

**Great Southern Railway** - penalties for failure to comply with an expert's decision should apply to both parties.

**Toll** - the decision of an expert should be enforceable by court action.

**AMC** - in the same way third-party operators are required to adhere to the expert's findings, so too should QR, and this should be stated in the Undertaking.

**FreightCorp, Toll** - the QCA Act provides for courts to order compliance, and this should be sufficient.

**ARTC** - there is no mention of how the parties may jointly select and appoint an expert – a process which may also result in dispute. The Undertaking addresses a third-party operator's failure to comply with a QCA direction, but not QR's failure to do so. The practice in many other jurisdictions is to have a final right of appeal to a determination by the regulator (as required by the Competition Principles Agreement).

### *QCA's Analysis*

While recognising the legitimate concerns expressed by stakeholders regarding conflict of interest for QR's Chief Executive, the QCA considers that QR's proposed three-tiered approach to dispute resolution is acceptable given that either party can refer the dispute to the QCA after 14 days. This effectively 'short circuits' the dispute resolution process by missing out the expert resolution stage. The QCA considers the proposed time frame for Chief Executive resolution is short enough to protect the interests of access seekers and QR.

The Draft Undertaking specifies resolution by the respective Chief Executives or their 'nominees'. In the case of QR, the QCA considers it appropriate that, where QR utilises a 'nominee', it should be the person occupying the position of General Manager of Network Access.

The QCA considers it is unlikely that it has the power to insist upon QR including as part of its Undertaking a provision for penalties. Rather, it concurs with the view that the QCA Act provides for enforcement of determinations as well as remedies for breaches of access obligations under Division 8 of Part 5.

#### ***QCA's Position***

**The QCA accepts the proposed three-tiered approach to dispute resolution subject to QR specifying that, where it utilises a 'nominee' in the Chief Executive resolution process, that nominee be the General Manager of Network Access.**

**APPENDICES**

Sheet 1	Moura and Blackwater Systems
Sheet 2	Gladstone and Auckland Point
Sheet 3	Blackwater System
Sheet 4	North Coast Line System
Sheet 5	Rockhampton yard
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Sheet 15	Central Line – Burngrove to Winton
Sheet 16	Central West System

## CHAPTER 5. PRICING PRINCIPLES

### KEY ASPECTS

**Price objectives** - the Undertaking should allow QR to generate sufficient revenue to maintain its incentive to invest in its infrastructure while not distorting competition in the above-rail market by allowing discrimination between QR's above-rail groups and third-party operators on other than cost and risk grounds.

**Price differentiation** - a market test may be applied to all third-party operators within defined markets to ensure they are subject to price differentiation on cost and risk differences only.

**Efficient costs** - the pricing limits, based on stand alone and incremental costs, should only reflect those costs efficiently incurred.

**Rate review** - access agreements should contain a rate review provision for instances when third-party operators can demonstrate that QR has sold a 'like' train path to another operator for a lower price than its own.

**Costing Manual** - should provide confidence in the integrity of the separation of costs between above and below-rail activities and be a reliable source for the evaluation of access charges. A strong audit procedure is required to improve confidence in the cost allocation process.

**Reporting** - for the Undertaking to be effective, it is necessary there be a regime of transparent financial and performance reporting in relation to the provision of below-rail services.

## 5.1 Introduction

In any market, prices play a central role in co-ordinating commercial activity. The market involving the provision of rail infrastructure by QR is no different. The pricing principles discussed in this chapter will underpin the development of access charges which in turn will substantially influence the evolution of the above-rail market.

The pricing principles adopted are critical to protecting QR's legitimate business interests. For example, if the pricing principles prevented QR from generating sufficient revenue, QR might not have sufficient incentive to undertake new investment in, and maintenance of, its rail infrastructure. Under-investment in or insufficient maintenance of rail infrastructure could ultimately impose costs on the economy as great as those from an environment where an excessive profit is allowed to be earned by a monopoly provider. It is also important that the pricing principles provide QR with an incentive to innovate to better meet customer needs in the services it provides.

The pricing principles are also important to protecting the legitimate business interests of above-rail operators and end customers. QR's pricing principles should not enable an excessive return to be realised by QR's below-rail business. It is also critical that access charges not distort competition in the above-rail market, by discriminating, on other than cost grounds, between QR's above-rail groups and third-party operators or between different third-party operators.

The pricing principles will also influence the evolution of the above-rail market and the efficient utilisation and expansion of the network. In a competitive market, above-rail operators will develop rail transport solutions which take into account the access charges they will be levied. Access charges must therefore be consistent with efficient utilisation and expansion of the rail infrastructure.

## 5.2 Pricing Objectives

The Draft Undertaking establishes the following pricing objectives to underpin the development of access charges:

- the overriding objective is, over time, to achieve revenue adequacy;
- by maximising the commercially viable utilisation of the rail infrastructure;
- subject to constraints on price differentiation (which allows QR to price differentiate subject to defined limits): cl 5.1.

These objectives are considered in turn.

### 5.2.1 *Appropriateness of revenue adequacy objective*

#### ***QR's Position***

QR will be entitled to earn sufficient revenue from the provision of access, including both access charges and infrastructure payments, to achieve full recovery of reasonable costs, including a commercial rate of return on the value of assets reasonably required for the long-term sustainable provision of rail infrastructure: para 5.1.1(a).

QR's proposal is that the application of the revenue adequacy objective should enable it to earn a revenue stream that recovers:

- all recurrent costs provided that such costs reflect ‘reasonably expected improvements in efficiency that QR should achieve’: sub-para 5.1.1(b)(i); and
- a risk-adjusted commercial rate of return on the value of all ‘assets reasonably required for the provision of access’ taking account of the investments required for rail infrastructure enhancements and asset replacement: sub-para 5.1.1(b)(ii).

In its initial submission to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking*, QR expressed wariness about the specification of ‘efficient’ costs in the formulation of access prices. It argued that based on its past experience in investigations to specify ‘efficient costs’ for its operations, there is always the potential to review the costs borne by other rail organisations and assess what is ‘efficient’ without paying appropriate regard to the environment in which QR operates.

As a result, QR proposed a ‘reasonable’ cost approach, determined within the context of the environment in which QR is operating and providing for improvements in efficiency that might reasonably be expected in that environment. Relevant factors to be taken into account include railway construction, geographical characteristics, environmental characteristics, cost of inputs, and award conditions.

QR stated in its initial submission to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking* that it does not believe there is any conflict in its pricing objectives. QR’s overriding objective is to achieve revenue adequacy, however, its actions in achieving that objective will be constrained by its obligations with respect to pricing.

### ***Stakeholder Comments***

There was general agreement in stakeholder submissions with the overall objective of revenue adequacy in the setting of access charges. However, some respondents expressed concern with the capacity of the Draft Undertaking’s pricing principles to achieve the overall objective without undue price discrimination and cross-subsidisation between above-rail operators and end-users.

#### **Table 1: Reasonableness of revenue adequacy objective**

**Toll** - the pricing objectives and proposed pricing structure operate to provide a significant disincentive to entry by third-party operators contemplating the movement of general freight. This is especially the case when considering the different cost structures which an operator faces when using rail compared to road. In addition the performance benchmark should not be solely or principally revenue adequacy, the objective should rather be one of recovery of incremental costs and efficient track utilisation.

**FreightCorp** - the principle that QR should seek sufficient revenue, over time, such that it is able to achieve its weighted average cost of capital is accepted. However, the source of QR’s revenue adequacy should come not only from train operators, but also from Government, recognising the social and economic benefits provided to the community at large from a railway system.

**Queensland Government** - in general, the objectives appear reasonable, although there is some scope for debate in relation to the various terms in the objective.

**ARTC** – we adopt a more open pricing approach than that proposed by QR, where reference prices are posted and open to all parties. Our customers have readily accepted this approach because it is transparent, openly equitable, provides certainty to the operator and is simple. The main weakness of QR’s approach is that the access provider is not in the best position to know that the prices being set represent the market’s assessment of the value of a given path (even if prices can be set so that revenue adequacy is achievable).

**AMC, FreightCorp, Queensland Government, QMC, Stanwell, Toll** - an inappropriate level of price discrimination could potentially result from the proposed pricing principles.

There appeared to be general agreement that QR should only recover efficient costs as determined by reference to external infrastructure management standards. Several stakeholders believed that mechanisms need to be introduced to ensure QR achieves ongoing efficiency improvements, which are passed on to customers.

**Table 2: Appropriateness of reasonableness tests for operational and capital efficiency**

**FreightCorp** - prices should reflect the infrastructure required, which is not necessarily the infrastructure available. For example, the majority of the track in the Brisbane metropolitan area is provided to cater for the peak urban passenger services. Freight may not require this level of infrastructure and should not be required to fund it through high access charges.

**QMC** - the utilisation of existing network assets and investment in new assets needs to be cost effective. This requirement encompasses technical efficiency, but goes further in requiring any new or expanded asset to generate sufficient revenue to avoid increasing the cost of access to existing users.

**AMC, Stanwell** - ‘reasonably required’ offers too much scope for allowing certain inefficiencies under certain conditions.

**AMC, Great Southern Railway, Queensland Government, QMC, Stanwell** - non-commercial requirements imposed on QR by government should form part of explicit CSO payments. This is necessary so that users of the network are not required to pay for non-commercial objectives that the Government may choose to ask QR to provide for the benefit of the community.

### *QCA’s Analysis*

There are three distinct issues that arise in the context of QR’s revenue adequacy objective:

- the reasonableness of it;
- whether the revenue stream that QR proposes it should be allowed to earn is consistent with the objective; and
- how conflicts between QR’s pricing objectives should be resolved.

#### *Reasonableness of revenue adequacy objective*

The issue of revenue adequacy arises because a rail network exhibits significant economies of scale and density. Pricing the use of the network on the basis of the cost that use imposes leads to the network provider not being able to generate sufficient revenue to justify its investment in the network (or to carry out new investment). In other words, for QR to recover its total costs, it must set access charges for use of the network for some traffics above the additional costs that their use of the network imposes on QR.

The QCA recognises that QR’s legitimate business interests require it to be able to pursue its revenue adequacy objective. Consequently, the QCA accepts revenue adequacy as a legitimate pricing objective for QR to adopt, so long as its application is pursued in a manner that minimises distortions to commercial activity in the above-rail market.

This raises the question of the approach the Authority should take in the future if it is required to arbitrate where QR sets an access charge for a traffic that is above the cost it imposes on the network (including capacity) but results in that traffic being priced away from the network. It is arguable that the public interest would be advanced by ensuring that the rail network retains the

traffic to avoid the adverse effects of it moving to road (congestion, pollution etc).<sup>94</sup> However, there is also a significant regulatory risk involved in intervening in QR's commercial decision making where:

- there is no prospect of the service, or any combination of services, being required to pay more than their stand-alone cost; and
- QR's above-rail business groups are not involved in the particular market.

Where QR operates in such a market, the limits on price differentiation discussed in section 5.1.2 below will address these concerns. However, in the rare cases where QR's above-rail business groups do not compete in the market that is being served, the Authority would be most reluctant to intervene - potentially undermining QR's pursuit of its revenue adequacy objective - unless it could be demonstrated that QR was acting in a way that compromised the integrity of the above-rail market. Such a case could arise for example where it is clear that QR is quoting access charges that could not sustain the traffic relative to its rival modes, and QR can provide no justification for such an outcome.

The Authority would thus be reluctant to interfere where QR is able to provide an appropriate justification because of the regulatory risks such an approach would create for QR's below-rail business. In particular, whilst the Authority notes that QR does not have complete information about the capacity of users to pay for access, it will normally be the case that a regulatory body, such as the QCA, will be in an even worse position to make such a judgement. This emphasises the concerns that the QCA has in becoming involved in such a dispute.

The practical application of the revenue adequacy objective is considered in the Authority's assessment of QR's proposed reference tariffs in Chapters 9 to 16.

#### *Appropriateness of reasonableness tests for operational and capital efficiency*

Competitive pressures normally impel participants in an industry to operate as efficiently as possible because:

- competitive pressures prevent prices including a margin to accommodate inefficiency; and
- market participants that operate more efficiently than their rivals are able to correspondingly increase their profit.

Competitive pressures in the provision of access to QR's network are not as strong as they might be if it were a competitive activity. Therefore, the concept of efficiency in service provision, both in terms of operating costs and investment in the rail infrastructure, is important in the regulatory process. In practice, the application of any efficiency benchmark requires account be taken of the subject organisation's particular circumstances and operational environment.<sup>95</sup>

QR's position is ambiguous. Whilst it could be interpreted to be consistent with QR being assessed against efficient benchmarks for the purposes of revenue adequacy, the precise

<sup>94</sup> Whilst the Authority acknowledges these public benefits, it does not consider it appropriate that access charges increase on account of them. This is because the access charges for most of QR's traffic will be driven by the price of road transport.

<sup>95</sup> Moreover, to the extent that there is an identified gap between QR's operations and those of benchmark organisations, there remains the issue of the transitional path over which it is appropriate to expect the gap to be closed. This issue is addressed in more detail in the context of the Authority's assessment of QR's proposed reference tariffs.

meaning of ‘reasonably expected improvements in efficiency’ is unclear. The Authority considers it desirable that there be as little ambiguity in the Undertaking as possible. Consequently, the Authority believes it is important that the emphasis be placed on the efficiency of operations and the assets required to efficiently provide the relevant service.

In relation to government directions to QR, the Authority considers explicit government infrastructure payments should be made for any formal government directives that impose non-commercial objectives on QR.

#### *Conflicts between pricing objectives*

The QCA is concerned that the characterisation of revenue adequacy as QR’s ‘overriding objective’ could justify inappropriate price discrimination. It is therefore necessary to clarify how conflicts between the pricing objectives should be resolved.

The pursuit of revenue adequacy at the expense of other objectives could seriously distort the evolution of the above-rail market. For example, it could allow Network Access to charge a more efficient above-rail operator a higher access charge than a less efficient operator.

Consequently, whilst the importance of revenue as a key corporate objective is recognised, it needs to be subject to the overriding requirement that QR does not engage in inappropriate price differentiation (considered in more detail below) unless QR can justify the price difference. It is difficult to envisage a situation where price differentiation in a particular market could be justified over other available avenues of achieving revenue adequacy.

#### ***QCA’s Position***

**The Authority would favourably consider an Undertaking that:**

- **considered revenue adequacy in the context of efficient operations and the efficient level of assets actually required to provide the service; and**
- **provided in the event there is a conflict between QR pursuing revenue adequacy and non-discriminatory pricing in a particular market, then the latter will prevail unless QR can justify the price difference to the QCA.**

### **5.2.2 Limits on Price Differentiation**

#### ***QR’s Position***

##### *Limits on price differentiation*

The limits to price differentiation incorporated by QR in achieving its revenue adequacy objective, provide that, where access negotiations occur at a similar time:

- railway operators which are competing directly to provide a specified commodity between a specified origin and destination will be offered consistent access charges. For the purpose of this paragraph, access charges are considered to be consistent when differences between them only reflect differences in the costs or risks to QR of providing access as a result of, for example, the standard type of train service, the rollingstock used or conditions of access: para 5.1.2(a); and

- railway operators which are not competing directly with each other, but providing train services for a specified commodity within the same geographic system, will have access charges determined on a consistent approach: para 5.1.2(b). However, QR does not explain what would qualify as a ‘consistent approach’.

QR argued in its initial submission to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking*, that sub-clause 5.12 creates an obligation on QR to price consistently for competing traffics with respect to access charges negotiated at a similar time.

#### *Rate reviews*

Access charges may vary over time. Paras 5.1.2(a) & (b) relate to access negotiations that occur at a similar time and do not require QR to develop access charges in a current negotiation with regard to access charges incorporated in existing access agreements. Rather, QR will give railway operators the opportunity to incorporate rate review provisions in access agreements to reflect, for example, changes in reference tariffs: para 5.1.2(c).

QR argued in its initial submission to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking*, that its willingness to allow rate review provisions in access agreements will allow access charges negotiated at different times to remain comparable. However, QR does not believe that it should specify a generic rate review provision.

#### *Stakeholder Comments*

All submissions expressed concern that an inappropriate level of price discrimination could result from the proposed pricing principles. However, there was no agreement on the best way to resolve this conflict.

#### **Table 3: Limits on price differentiation**

**QMC** - the Draft Undertaking provides QR with too much pricing latitude. The following pricing principles are proposed:

- transparent fully-costed CSOs for user groups incapable of paying average costs;
- no price differentiation among users within the same class, for example, mines, whether or not they are located on the same rail system;
- price differentiation between different classes of users should be confined to groups using the same assets ie user groups on the same system;
- the admission of a new user should not result in an increase in a reference tariff applying to established users;
- QR should be required to identify which traffic groups on each system are deemed unable to pay full average costs, and the access agreements relating to those services should be discoverable; and
- those agreements should only be short-term (for example, one year) to require for the regular review of the nature and pricing of incrementally-costed traffics and to ensure that the level of system utilisation has not changed to the disadvantage of full fare paying users.

**Great Southern Railway** - the only difference in QR’s charges between competing operators should reflect the differences in costs to QR in providing access to them.

**AMC, Stanwell** - greater transparency and the provision of more detailed cost and revenue information (that is, on a system or line section basis) may reduce QR’s ability to unfairly price differentiate.

**Queensland Government** - customer differentiation is necessary to provide sufficient flexibility to encourage maximum use of infrastructure. However, it may be useful to incorporate a mechanism to ensure sufficient transparency for agents to assess whether an equitable approach is taken to pricing.

**AMC, Queensland Government, Stanwell, Toll** - the QR pricing model is no worse than others that are in place in NSW and Western Australia.

There was no consensus on the appropriateness of the limits on price differentiation and specifically concerning similar traffics at different points in time.

**Table 4: Consistent pricing at different times**

**Queensland Government** - it would be appropriate for different prices to be levied at different points in time. This is because costs to QR could well vary over time, as could market conditions generally. It should be up to the access seeker and the marketer of the specific commodity to ensure that overall timing of entry to the market is favourable (in terms of transport and access costs as well as overall market conditions).

**AMC** - it is not appropriate for different prices to be charged for the same services at different times. To avoid this outcome it is necessary to provide for regular pricing reviews. Findings from these reviews should be reflected in all access prices.

**Stanwell** - an annual review of revenues could ensure that revenue limits for each of the various segments of infrastructure are not exceeded. Where revenue is above its limit for a particular segment, users could perhaps be provided with a rebate based on the share each meets of the 'common costs'.

**Toll** - the price should be the same except for differences related to verifiable cost differentials.

Stakeholder submissions generally supported rate review provisions in access agreements. There was some support for the Undertaking including details on the nature of the rate reviews.

**Table 5: Rate reviews**

**Toll, National Rail** - the circumstances of any rate review should be identified clearly, as should the way in which the rate review is to be conducted.

**FreightCorp** - the review provisions in the Draft Undertaking are appropriate.

**Queensland Government, AMC** - the inclusion of rate review principles within the Draft Undertaking would add to the transparency of the regime and reduce the monopoly power that QR possesses. The Draft Undertaking should specify the factors that will trigger reviews.

**AMC** - the effects of the rate reviews should be reflected in all relevant access charges.

***QCA's Analysis***

*Limits on price differentiation*

QR proposes two limitations on its ability to set differential prices:

- consistent charges for directly competing services (same specified commodity between a specified origin and destination at a similar time); and
- a consistent approach to charges for the same commodity type in the same geographic system.

QR proposes that consistent access charges will vary between operators only according to the cost (or risk) differences. For example, cost differences may arise because trains travelling at different speeds may consume more capacity, or because different trains could impart differing levels of wear and tear on the track. The QCA accepts this approach.

However, QR's constraint on differential prices for directly competing services is limited to negotiations involving a specified transport service occurring at a similar time. QR does not provide clear guidance about the intended meaning of 'similar time'. One interpretation is that a similar time would be confined to a circumstance where third-party operators were competing to perform an end user's freight task (that is, in an open tender situation).

QR's commitment to levying consistent access charges may therefore apply only in relation to a narrow range of potentially competing services. For example, QR's current proposal would legitimise QR levying an inconsistent access charge where two railway operators seek access at different times, that is, one operator is a potential entrant while one is an incumbent for the same end user). Clearly, such an outcome risks distorting the evolution of a competitive above-rail market.

The limitation on differing access charges for railway operators that are not competing directly (according to QR's test) assumes particular significance in this context. QR's proposal provides extensive latitude to pursue price differentiation between similar traffic types. For example, if the 'consistent approach' involved achieving revenue adequacy (that is, maximum possible access charges), QR could set higher access charges for a third-party operator than applied to its own traffic, simply because of the third-party operator's more efficient practices and QR's assessment of its capacity to pay.<sup>96</sup> This could be so despite the two services having identical train operational, technical and risk characteristics and serving end-users in the same market. Such an outcome could seriously distort competition in the above-rail market.

Moreover, if QR's Undertaking was approved in its current form, the conduct would not transgress the hindering access provisions of the QCA Act because it would be authorised under the approved Undertaking.<sup>97</sup>

The QCA notes that QR's approach is markedly different to that of ARTC who has posted prices applying for traffic on its network regardless of the commodity carried. However, ARTC's approach is a result of commercial decisions it has made. As a regulator, the QCA's concerns are more narrow, focusing on ensuring that QR does not impose access charges that exceed stand-alone cost (described below) and that it does not levy access charges that distort competition in the above-rail market.<sup>98</sup>

In order to avoid distorting competition in the above-rail market, the QCA believes QR's capacity to price differentiate should be constrained by a market test. Under such a test, prices in the same market (that is, limited by commodity, geography etc) should differ only on the basis of identifiable costs or risks. This would extend to agreements negotiated at different times, subject again to where QR is able to demonstrate the existence of a verifiable cost or risk differential.

Under this approach, the Undertaking would restrict price differentiation so that all third-party operators that serve the same markets are only subject to price differentiation because of cost or risk differences irrespective of whether or not they are competing head-to-head for a particular haul. This allows QR to price differentiate in access charges between markets but requires within markets an approach where price differentials are limited to those that QR can justify on

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<sup>96</sup> This is especially a concern given QR's overriding objective is revenue adequacy. QR's Explanatory Guide indicates that QR will not differentiate between train services on grounds such as "the perceived ability of one end user to pay more than another end user for reasons such as market incumbency, financial liquidity or product quality characteristics". However, there is no mention of whether or not superior efficiency could justify a higher access charge being levied on the more efficient operator.

<sup>97</sup> Refer to s104 and s125 of the QCA Act.

<sup>98</sup> There may be other concerns, such as to ensure that the negotiation process is not unnecessarily impeded by the range of access charges that fall within the floor and ceiling limits.

a causal basis. Examples of causally based departures could include a higher (lower) access charge to reflect:

- greater (less) maintenance being required for the track because of a particular third-party operator's operational configuration;
- greater (less) capacity being consumed. This could be due to many factors, including the interaction of the requirements train's speed, acceleration or priority with those currently on the network;
- a higher risk being associated with a particular third-party operator; or
- differences in the cost in the provision of rail infrastructure emerging over time.

The QCA considers that QR should bear the onus of justifying any causally based departure for access charges in the same market.

Pricing arrangements for third-party access in telecommunications markets have been simplified by the assumption of a limited number of defined markets. The benefit of this approach is that it reduces the risk of disputes emerging about market definition, although it does potentially limit QR's capacity to price differentiate. The Authority is attracted to an approach which expressly limits the number of markets for the purpose of establishing access charges with the onus on QR to justify the inclusion of additional markets. Examples of these markets are likely to include:<sup>99</sup>

- coal traffic;
- minerals traffics;
- grain traffics;
- other bulk products;
- long distance passenger traffics; and
- intermodal traffics.

The application of this approach would not prevent pricing distinctions within a market on account of service differences. For example, a livestock train which received priority would be required to pay a higher access charge than an intermodal train with a lower level of priority.

However, where numerous above-rail operators, with identical characteristics, are seeking access to mutually exclusive paths (as opposed to mutually exclusive traffic) then pricing objectives should allow for prices to vary to ensure that the capacity entitlement is allocated in accordance with maximum value.<sup>100</sup>

The cost and revenue information to be provided to market participants during the negotiation process is addressed in Chapter 4. The disaggregation of financial reports for users is discussed in section 5.4 of this chapter. The allocation of costs (including overhead) to users in the coal system is discussed in Chapter 12.

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<sup>99</sup> The Authority intends reviewing these markets with QR after the release of the Draft Decision.

<sup>100</sup> This matter is discussed in Chapter 6.

### *Rate review*

The duration of access agreements will often exceed a five year period. Given the long time horizon, issues arise concerning the allocation of risk between the parties for changes in cost or market conditions that emerge during the term of the agreement.

For example, one means of reflecting the allocation of risk for the supplier is to pass on changes in certain costs to the customer. This can be achieved either automatically, for specified costs, or by means of a rate review, for costs or other factors that might not be known with clarity at the time the contract commences. A significant risk for above-rail operators is that a competitor serving the same end market could gain access to QR's network for a lower access charge than applies to its own services, where there is no causal basis for the discount.

QR's Draft Undertaking proposes that third-party operators be given an opportunity to incorporate rate review provisions in access agreements, but does not specify how this might be done other than to provide, as an example, a change in reference tariff, as being a basis for the rate review applying. Therefore, the Draft Undertaking provides no right for a third-party operator to require a rate review as part of its access agreement.

The QCA agrees with QR that rate reviews should be available to those that seek it on account of changes in reference tariffs, and that QR should be entitled to insist that any such review must be symmetrical, that is, rate increases being passed on as well as rate decreases. The Authority considers that the Undertaking should provide greater clarity as to the circumstances in which third-party operators should be able to insist upon rate review arrangements being contained in access agreements.

In considering the circumstances in which it is reasonable that third-party operators should be able to insist on a review of their access charges, the limits on price differentiation discussed above are relevant – QR should not increase access charges to operators in the same market without a cost or risk justification. Conversely, if QR reduces access charges in a market without a cost or risk justification it could distort above-rail competition.

Another rail manager (ARTC) has addressed this concern in its standard access agreement which provides operators with a right to have access charges reviewed if they are able to demonstrate that ARTC has sold a 'like train path' to another operator for a lower price than applies to the operator. Such a provision could usefully be applied in the Queensland context.

ARTC's approach to rate reviews is based on matters such as location, duration, quality of train paths, nature of the train consist etc, but does not extend to the market being served by the operators.<sup>101</sup> The QCA recognises that QR distinguishes between markets served for pricing purposes in its Draft Undertaking (even if this may be limited in the future to defined markets). From a regulatory perspective, the QCA considers it inappropriate that QR's ability to price differentiate between markets be undermined by an inconsistent approach to rate reviews. Accordingly, any consideration of like train paths in rate reviews would have to have regard to the end market being served.

Clearly, it is possible that access charges for two operators serving in the same market could change over time where there exists a causal basis for the departure. Nevertheless, the QCA considers access seekers should be entitled to require a rate review mechanism be incorporated in access agreements for access charges in the same market where reference tariffs do not apply. Under such a mechanism, which, subject to negotiation between the parties, might involve referral of the issue to an expert for resolution, the third-party operator would bear the onus of

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<sup>101</sup> This is because ARTC does not distinguish end-user markets for the purpose of setting access charges.

establishing a different access charge applied to a like train path and, once established, QR would bear the onus of justifying the difference.

The rate review mechanism would preclude QR charging a different access charge for a different operator in the same end market unless it could demonstrate an underlying cost or risk rationale for the difference. Examples of such a justification could be a difference in the cost in the provision of the rail infrastructure has emerged or because of the cost or risk factors specific to an operator. The rate review provision would allow recourse to dispute resolution as provided in the access agreement.

The other issues associated with rate reviews for material changes in cost are addressed in the discussion of Schedule E in Chapter 8.

#### ***QCA's Position***

**The Authority would favourably consider an Undertaking that:**

- **made price differentiation subject to a market test in which all third-party operators within defined markets would be subject to price differentiation on cost and risk differences only (whether or not they are competing head-to-head) with QR bearing the onus of justifying price differences; and**
- **gave third-party operators the option of rate review provisions in access agreements if an operator is able to demonstrate that QR has sold a like train path to another operator for a lower price than applies to that operator.**

### ***5.2.3 Rail Infrastructure Utilisation***

#### ***QR's Position***

QR will be entitled to establish access charges with different levels of contribution to common costs for railway operators serving different markets to maximise the commercially viable use of capacity, while meeting, in aggregate, the common costs of providing the rail infrastructure: para 5.1.3(a).

Capacity will be allocated in accordance with cl 6.3. Capacity will be augmented where QR reasonably considers that the achievable access revenues are sufficient to commercially justify the required expenditure: para 5.1.3(b).

Where multiple access seekers are competing for capacity on a capacity constrained part of its network, QR reserves the right to nominate the highest access charge it is likely to achieve from potential access seekers. That is, the charge which incorporates the highest contribution to common costs: para 5.1.3(c).

In this context, QR reserves the right to assign infrastructure payments in accordance with the terms of the contract under which they are provided. For example, where infrastructure payments or CSOs are paid by the Government, conditional upon the benefit of those payments being available only for train services serving a specified market, the access charge assessable in respect of these train services should take into account the proportion of the payments directly related to those train services: para 5.1.3(d).

## Stakeholder Comments

A range of views emerged in the submissions in response to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*.

### Table 6: CSO's and utilisation of rail infrastructure

**Queensland Government** - the contract between the Government and QR regarding infrastructure payments will specify that payments will not be directly available for train services.

**National Rail** - CSO payments should only be made to the access provider and not to above-rail operators, so that subsidies are available to meet the cost of infrastructure provision regardless of what operator is providing the train service.

**QMC** - the Draft Undertaking correctly intends to attribute CSOs to the below-rail provider.

**Stanwell, AMC** - QR should comply with the principle of competitive neutrality in attributing infrastructure payments to train services, particularly where there is excess capacity.

**FreightCorp** - it is the government's prerogative to allocate payments in a manner it believes appropriate, which may not necessarily be consistent with the achievement of competitive neutrality.

**RTBU** - the QCA is misusing the concept of competitive neutrality by suggesting that it can be applied to the attribution of infrastructure payments.

## QCA's Analysis

QR's commitment to expand the capacity of the network is subject to where QR reasonably considers that access revenues are sufficient to commercially justify the required expenditure. This will occur in the context of its past investment in the network being largely sunk. Consequently, the commercial justification for the expansion of the network should focus on the net additional revenue expected to be earned. In other words, the recovery of historic investment should not be a relevant consideration in the context of QR's decision regarding whether or not to expand the network. It would be desirable if this could be clarified in the Undertaking.

The allocation of capacity in capacity constrained parts of the network is considered in Chapter 6.

Under the *Government Owned Corporations Act 1993*, the Government may require QR to perform certain activities that would not be undertaken on a commercial basis through community service obligation (CSO) payments. Infrastructure payments for the maintenance of low volume infrastructure is an example of a CSO.<sup>102</sup>

The QCA notes the Queensland Government's advice that the contract between the Government and QR regarding infrastructure payments will specify that payments will not be directly available for train services. Although it would appear that some of the concerns raised by stakeholders will not arise in practice, the method of achieving the intended social objectives is a matter for the Government, not the QCA.

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<sup>102</sup> CSOs paid to QR for the provision of above-rail services are not relevant to the Authority's consideration of the Draft Undertaking, although they could be the subject of a competitive neutrality complaint.

***QCA's Position***

**The Authority would favourably consider an Undertaking that clarified the basis upon which QR would expand the network such that the assessment of the commercial justification for expansions of the network should focus on the net additional revenue expected to be earned.**

**5.3 Pricing Limits*****QR's Position***

Pricing limits will be applied in respect of the following elements for every individual train service (and combination of train services) and will ensure that cross-subsidisation is avoided:

- a lower bound defined by its (their) incremental costs – which should include both the physical costs imposed (that is, maintenance) and the opportunity cost of the capacity utilised by that user; and
- an upper bound defined as its (their) expected stand-alone cost, being the cost QR would incur if the train service (combination of train services) was the only train service (combination of train services) provided with access: sub-paras 5.2.2(a) and 5.2.3(a).

Where it is necessary to assess whether access charges are consistent with the upper limit, a revenue limit will be established for both the individual train service and for identified train service groups (this is discussed below): sub-paras 5.2.2(b) and 5.2.3(b).

The constrained market pricing method allows QR to establish access charges that vary significantly between the bounds established by the floor and ceiling prices. However, QR has argued that sufficient constraint exists on its ability to inappropriately price discrimination, as the Draft Undertaking requires that different railway operators competing to provide the same specified transport service be offered 'consistent access charges' that is, charges that differ from each other (for a comparable service) only on the basis of cost or risk differences.<sup>103</sup>

QR is strongly of the view that the constrained market pricing approach will provide the most efficient pricing outcomes. QR also contends the provision of different service levels to competing operators should be reflected in their respective access charges (for example, different levels of priority). The general level of cost recovery from a particular market segment will be driven by the ability of operators competing in that market segment to contribute to common costs, but within a given market segment, access charges will vary in relation to the service level provided.

***Stakeholder Comments***

The majority of submissions in response to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*, argued that the proposed pricing objectives provide QR with excessive pricing latitude.

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<sup>103</sup> The limitations of this proposal have been discussed above.

**Table 7: Appropriateness of upper and lower pricing limits**

**Stanwell, AMC** - the Draft Undertaking does not provide any indication as to the methodology and factors to be used by QR in determining an access charge and gives it a discretion that is too wide. In addition, the pricing methodology fails to adequately address the downstream market conditions in which third-party operators will compete.

**Stanwell** - the Draft Undertaking provides QR with a very broad range in which to negotiate prices varying from incremental or marginal cost to the full stand-alone cost. While this approach is intended to allow economically efficient pricing, QR's ability to assess capacity to pay for each user within each group of train services is doubted.

**FreightCorp** - under the proposed pricing principles, a situation may arise where improvements in train operating efficiencies may not lead to a lower access charge. Further, in effect, the Draft Undertaking puts in place a 'mezzanine' level, such that revenue from all operators over a group of line sections must cover the costs of those line sections. The purpose of the mezzanine mechanism is to transfer the revenue and volume risk from the infrastructure owner to the train operator(s) using the network. If traffic disappears from the network, QR would appear to be entitled to increase access charges for the remaining traffics. This is inappropriate, the volume risk most appropriately belongs to the infrastructure owner.

**Queensland Government** - there is scope for further detail to be provided in the Draft Undertaking regarding the manner by which QR will determine prices.

**RTBU** - the Draft Undertaking does not provide QR with excessive pricing latitude. The QCA should allow QR to implement a commercial mechanism as set out in the Competition Principles Agreement, rather than attempting to dictate an administered process to QR.

**FreightCorp** - the Undertaking allows for both individual and combinations of train service price limits. For both, the stand-alone cost of providing the infrastructure service is the test. A similar pricing policy in NSW has shown that the individual pricing limit can be used, in certain circumstances, to grossly skew the charges to a particular traffic while still meeting the group limits. Prices should be limited to paying:

- the genuine incremental costs from usage of the railway, assuming the railway as it exists is in place in perpetuity;
- a premium for priority (and other service quality elements) and;
- an average share of fixed (common) costs.

Where traffics are unable to pay this level of access price, government should provide below-rail CSOs to support the difference.

**Table 8: Cross-subsidisation**

**AMC, Stanwell** - a situation where one individual train service was meeting all the common costs and several other train services using the same infrastructure were simply meeting their incremental costs, would be an undesirable outcome even though no cross-subsidies as defined by QR are involved.

**QMC** - the Draft Undertaking should:

- espouse the principle of user-pays access pricing;
- contain sufficiently precise definitions of costs, and sufficient information on the attribution of those costs to different categories of users, to demonstrate compliance with the user-pays principle; and
- provide for disclosure of CSO payments for the provision of access to traffic that is unable to fully cover its costs, as well as the basis on which the amounts were calculated.

**Queensland Government** - it may be possible for a cross-subsidy to exist if the network is not sufficiently disaggregated for costing and charging purposes. Both avoidable and fixed

costs may be misallocated and cross subsidies could occur between train services on separate sections of track.

**ARTC** - whilst the approach proposed by QR to the pricing of rail access is appropriate, it need not be applied to each and every section that makes up a route, so long as no other service is affected adversely.

#### **Table 9: Attribution of common costs for identifying cross subsidies**

**Queensland Government, Toll, AMC, Stanwell** - common costs should be related as specifically as possible, that is, to individual sections of rail infrastructure, in determining the ceiling level for access charges.

**Stanwell** - common costs should incorporate head office costs allocated to the relevant sections of infrastructure involved.

**QMC** - QR's overheads should not be excluded from the meaning of common costs. To the extent that they may be, as a result of the potential effect of restricting the definition of common costs to 'transport infrastructure', then that nexus should be broken. Also, common costs should be allocated on a genuine user-pays basis, that is, in accordance with users' relative demands wherever possible, and resort to crude measures like tonne or passenger kilometres should be minimised.

**RTBU** - QR's aggregated annual accounts are a sufficient basis on which to achieve a commercial outcome with respect to access negotiations.

There was a preference amongst stakeholders that the Draft Undertaking should set out the methodology that is to be used in determining access charges.

#### **Table 10: Requirement for a more prescriptive pricing approach**

**FreightCorp** - there is too much scope for QR to make subjective assessments of the prices it can extract from end users of rail infrastructure via third-party operators. It is possible to arrive at a reasonable price for infrastructure services under estimates of future usage from a reasonably prescriptive approach. However those prices should not be allowed to adjust upwards in the case that traffic reduces (either through loss of business or efficiency).

**Queensland Government** - a more prescriptive pricing methodology could prove advantageous to the acceptance of the regime. However, there is a risk that such a methodology could introduce undesirable rigidities and loss of efficiency in pricing and infrastructure use. Overall, clearly defined pricing principles and key parameters support a flexible application of those principles.

**AMC** - a more prescriptive pricing methodology is necessary because the gains in economic efficiency from the proposed discriminatory pricing would not materialise because of QR's inability to determine the price elasticities (that is, capacity to pay of operators and or end-users).

**Stanwell** - if the pricing methodology proposed in the Draft Undertaking is retained, in order that pricing decisions are not ad hoc and to provide a suitable negotiating environment, it is critical that the Draft Undertaking define the methodologies to be used in determining capacity to pay.

**Toll** - the publication of reference tariffs is not sufficient and the Draft Undertaking should set out, together with reference tariffs, the methodology which is to be used in determining access charges.

**QMC** - supports a prescriptive pricing approach for coal and mineral access.

**Table 11: Charging on the basis of opportunity cost as part of incremental cost**

**FreightCorp** - to the extent that a train service imposes costs on other users of the system, either directly or through indirect means by denying another train the opportunity of using that capacity, the train should, at least, be charged those costs.

**Stanwell** - in economic terms, opportunity costs are included in incremental cost.

**ARTC** - such an inclusion will add further complexity to the process, reducing transparency, and it may also result in new entrants paying a higher charge than incumbents, thereby discouraging entry.

### *QCA's Analysis*

#### *Definition of cross-subsidies*

For a cross-subsidy to arise, it is necessary to demonstrate that a user or cluster of users contributes less than their incremental cost and that another user or cluster of users pays more than their stand-alone cost. The prospect of users being required to pay more than the stand-alone cost that they impose on the system is most likely to arise on the coal systems, where protection will be provided by the reference tariffs. The Authority's assessment of incremental cost and stand-alone cost (including cost allocation issues) is discussed below and applied in the context of its assessment of the Authority's assessment of QR's proposed reference tariff for the coal systems.

Whilst the QCA accepts QR's proposed prohibition on cross-subsidisation, the key issue relates to the price limits that underpin this test and the circumstances in which QR is able to price differentially.

#### *The appropriateness of pricing limits*

Rail infrastructure and its associated below-rail services exhibit economies of scale and density arising from the large fixed (and sunk) costs associated with investment in rail infrastructure. In this environment, and in the absence of congestion, additional users impose few additional costs on the network. Consequently, increasing traffic volumes enable costs to be spread over the greater volume of traffic, reducing average costs. In this situation, setting access charges on the basis of recovering the cost of providing an additional service would prevent QR from breaking even, as fixed costs would not be recovered.

In order to recover total costs, it is therefore necessary that the network provider set charges for at least some traffics above their incremental cost. The challenge is then to achieve such an outcome without pricing away traffic that at least meets its incremental cost. In order to address this problem, QR is proposing to adopt what is known as a constrained market pricing or a 'floor/ceiling' approach to the setting of access prices.

The pricing ceiling would be set so as to avoid QR earning excessive returns while the minimum (floor) price would ensure traffics recover at least their incremental cost. The main restriction on pricing within these bands involves the limitations on price differentiation, discussed above. This pricing freedom is intended to facilitate QR achieving revenue adequacy by charging different consumers and different products (such as grain and coal) different access charges based on QR's assessment of their capacity to pay. The appropriateness of the proposed ceiling (stand-alone cost) and floor (incremental cost) bounds will be considered in turn.

**Stand-alone cost** - QR defines stand-alone cost (SAC) as those costs that QR would incur if the relevant train service or combination of train services (as appropriate) was the only train service or group of train services provided access by QR. In practice, the below-rail services provided by QR most likely to be subjected to the SAC test are those comprising the four major coal

systems (Newlands, Goonyella, Blackwater and Moura). The QCA is concerned that the QR definition involves theoretical and practical limitations.

In theory, an access charge calculated according to the SAC methodology represents the maximum amount an efficient entrant access provider could charge a user (or any combination of users) without diversion of traffic to a hypothetical competing service that was configured to accommodate that traffic as efficiently as possible. That is, SACs are those costs that the hypothetical efficient network provider would incur if it were to enter the market by recreating infrastructure and assets to provide the services delivered by QR.<sup>104</sup>

However, the Draft Undertaking refers to the costs that QR would incur if the relevant train service (or combination of train services) was the service(s) provided access by QR in isolation. QR's definition refers to the costs incurred by QR itself rather than an efficient entrant. The application of this test is considered as part of the Authority's assessment of QR's reference tariffs.

The most significant practical concern arises from the application of the SAC test in networks that carry a range of different traffics. For example, in the Blackwater system, complexities arise because track standard is dictated by traffics other than coal (complicating the assessment of stand alone maintenance costs). In addition, different train services consume differing amounts of capacity. Accordingly, on a system where there is a significant mix of traffics, the assessment of SAC is complex. A detailed assessment of SAC in the context of the reference tariffs for these services is contained in Chapter 12.

As an additional protection to users, QR proposes access revenue would fall below a specific limit on designated systems, calculated pursuant to a formula outlined in the Undertaking. QR proposes this limit apply for train services operating on the Central Queensland coal systems (individually and collectively) and the Mt Isa system.<sup>105</sup> The QCA accepts that the QR's other systems are unlikely to recover revenue in excess of their stand-alone cost, but considers such a revenue limit should apply to each system and to the system as a whole.

**Incremental cost** - the definition and measurement of incremental cost for a rail network is complex. For example, on lightly trafficked lines, a significant cost is incurred in simply keeping the track in operation. In addition, the incremental cost for a range of services would normally exceed the sum of incremental costs of the individual services comprising that range.

The QCA's analysis suggests that rail infrastructure costs generally can be attributed to a system reasonably effectively. In other words, the 'jointness' that exists in the provision of rail infrastructure manifests itself principally at the system level. Within a system, it is not feasible to unambiguously assign costs to particular traffics or train services, other than:

- incremental maintenance and capacity costs associated with changes in volume and the level of service and the costs associated with train control; and

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<sup>104</sup> In the United Kingdom and the United States of America, the stand-alone cost concept is used in rate assessment processes. While the Surface Transportation Board in the US recognises that a stand-alone facility would, in reality, seldom be constructed, they contend that by identifying the costs that would be incurred if it were, an appropriate rate cap can be determined. "In this way, railroads functioning in a non-competitive market will be required to price as if alternatives to their services were available. That is, their rates will be judged against simulated competitive prices". However, the 'bypass' approach is rarely used to estimate stand-alone costs, because of the practical difficulties involved in estimating the costs of alternative routes, track type etc. Consequently, an allocation approach has been adopted in New South Wales and Western Australia for the quantification of stand-alone costs.

<sup>105</sup> These services are listed in Schedule F.

- the asset-related costs that could be avoided if particular sections of track were not required.

Therefore, common costs are generally only able to be identified at the system level.

QR's definition of incremental costs comprises two elements:

- maintenance and operational costs that would not be incurred if the relevant train service or group of train services did not operate. The QCA's preliminary assessment of these costs is contained in working paper 2; and
- capital costs associated with the cost of providing paths. The number of paths consumed by a particular train service or group of train services depends on the interaction between the operational parameters of the affected services (for example, priority, sectional running time, etc). The QCA's preliminary assessment of the approach to quantify these costs (including quantification for the major coal systems) is contained in working paper 3.<sup>106</sup>

QR's definition excludes some of the costs a train service imposes on the network such as:<sup>107</sup>

- disruption costs – an additional train service is likely to increase transit times for existing train services operating on a system;<sup>108</sup>
- opportunity costs – where the train services prevent other revenue being earned by the network provider.

In addition, QR's definition recognises only those costs QR would actually avoid if a train service did not operate but overlooks any additional cost that would be avoided by an efficient rail provider.<sup>109</sup>

Moreover, as incremental cost is a function of the services being assessed, the incremental cost of a group of train services could generally be expected to exceed the sum of the incremental

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<sup>106</sup> It is possible to apply a short-term or a long-term approach to the assessment of the cost of an additional train path. Short-run marginal capacity costs are less if capacity is not constrained. However, if capacity is constrained, the short-run marginal cost of a path is the compensation an existing user requires in order to forego its entitlement. Where this amount is lower than the cost of creating additional paths (as may be the case for traffics the subject of vigorous intermodal competition) then it is appropriate to assess this incremental cost on a short-run basis. In practice, where the short-run is used for assessing incremental capacity costs, secondary trading as defined in Chapter 6 will be important to producing an outcome where capacity is efficiently allocated.

<sup>107</sup> In theory, a network provider could derive a benefit from the use of its network beyond the monetary payment it receives for the service. For the purposes of assessing these benefits, the Authority does not consider it appropriate for Network Access to consider the revenue its above-rail business groups receive from the use of its rollingstock because doing so would distort the above-rail market. The non-financial benefits of traffics that do not cover incremental cost and have little future prospect of doing so are unlikely to be significant even allowing for CSO funding.

<sup>108</sup> The inclusion of congestion costs in access charges would mean that the costs of disruption would be borne by those users imposing the costs. With several operators on a route, delays caused by one third-party operator, for example from broken down trains or simply from increased capacity utilisation impacting upon cycle-times, can affect other operators' services. Within an efficient system of access charges, congestion charges should therefore reflect the cost of delays caused to other operator's services, that is, train operators should face the full cost they impose on the network including the costs imposed on other above-rail operators. However, the QCA recognises the unanimous view of stakeholders expressed at the working group meeting that it would be premature to implement congestion pricing in the current environment.

<sup>109</sup> This tendency is exacerbated as the number of train services under consideration increases, so does common costs that are able to be attributed to that group, especially when the group includes all train services operating on a system. An efficient organisation would be able to lower its costs more than an inefficient organisation as the number of train services avoided increases and in theory, incremental cost should focus on the former rather than the latter.

costs of the individual services comprising that group. Consequently, the withdrawal of a train service may adversely affect the recovery of incremental cost for a group of train services.

In general, the incremental cost of an individual train service will consist mainly of avoidable maintenance charges and possibly incremental capacity charges. For relatively low tonnage levels, these avoided costs will be small (unless that train service prevents others operating that are willing to pay higher access charges or otherwise imposes capacity-related costs on other users).

The Authority notes the Queensland Government's policy that QR's unprofitable lines remain open and that indeed the Government has ensured this outcome through CSO arrangements with QR. In such a case, the cost relationships are such that there is a level of traffic that will not require maintenance beyond that which is necessary to keep the line open, so that the incremental maintenance cost of additional traffic will be zero. At slightly higher tonnage levels, the maintenance costs tend towards a linear function (in that they tend to vary directly with incremental traffic). Traffic on lightly trafficked lines is unlikely to cause additional cost in terms of capacity, disruption etc.

Accordingly, where Government has required that such lines remain in operation, and the common costs associated with the system would largely be incurred irrespective of traffic levels, an approach which requires individual traffics cover incremental costs provides a reasonable working basis against which to assess cross subsidisation. In other words, where Government policy requires that lines remain open, the Authority considers there would be little difference between the sum of the incremental costs of train services operating on a line and the incremental cost of the line itself.

In practice therefore the QCA proposes that the appropriateness of access charges should not focus on incremental cost but rather on the relativities with other charges pertaining to the relevant market so long as no traffic or combination of traffics is required to pay more than its stand-alone cost. This means that the pricing limits should be considered in the context of the limits on price differentiation discussed in section 5.1.2 above.

The QCA accepts that it would be inappropriate for access charges to depart from the limits on price differentiation because of non-recovery of incremental cost for a group of train services. In other words, it would be inappropriate for QR to increase access charges to a 'mezzanine' level on account of the withdrawal of train services on a system where the Government contracts with QR to keep that rail line in operation.<sup>110</sup>

In such an environment, individual train services that cover their incremental cost are very unlikely to result in QR not recovering the incremental cost caused by a group of train services. An exception may arise where substantial damage is caused to the track by natural causes, for example, flood, where it may be unreasonable to insist on QR meeting a substantial capital cost where no other party is prepared to remedy the situation.

The practical importance of this issue arises in the context of conduct in accordance with an approved Undertaking being deemed to comply with the hindering access prohibitions contained in the QCA Act. The QCA considers that in order to gain protection from a breach of this provision:

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<sup>110</sup> Indeed, the prospect of an additional charge being levied could itself inhibit above-rail competition.

- QR should observe the limits on price differentiation described in section 5.1.2 above irrespective of whether the resulting access charges cover the incremental cost of the individual train service; and
- QR must not allocate capacity in a way that could hinder access.

*Requirement for a more prescriptive pricing approach*

As QR's proposed approach only establishes floor and ceiling limits, it creates uncertainty for access seekers in access negotiations, which could undermine the integrity of the emerging above-rail market. The additional constraints on QR's capacity to differentially price for access do not of themselves satisfy these concerns as QR's access charges will not be publicly available (except in relation to access for coal transportation).

The QCA is concerned that attempting at this stage to prescribe a methodology for the determination of access charges could prove to be counterproductive. The issue in the affected markets will normally involve an assessment of access charges in an environment where intermodal competition exists. In such a case, subject to the stand-alone cost ceiling, the QCA is attracted to the approach adopted for the AustralAsia Railway Project which proposes to use a Competitive Imputation Pricing Rule (which is an application of the Efficient Component Pricing Rule) in establishing access charges. The concept underpinning this approach is that access charges are effectively capped by competing transport modes (for example, road, sea and air). Consequently, the price charged is limited by the price of these competitors, in much the same way as a conventional market operates.

This pricing approach is given by:

$$AP = CRLP_{AB} - IC_{AR}$$

where:

- AP is the competitive imputation access price;
- $CRLP_{AB}$  is the competitive rail line-haul price, defined as the maximum competitive price (above and below-rail) that the access provider could charge for the transport of a commodity between two points; and
- $IC_{AR}$  is the incremental cost of the above-rail service provided by the current operator.

In assessing the incremental cost of the above-rail service provided by the current operator, regard would need to be had to the duration of the service and the capital cost associated with the provision of rollingstock.

However, this rule is clearly difficult to apply in practice because a prospective third-party operator will have no ability to question an access charge based on this rule except by pursuing arbitration. This is because the incremental cost of QR's above-rail operations for a particular traffic will be confidential to QR. Further complicating the assessment of incremental cost of QR's above-rail operator is that the final price for the service is likely to involve a complex amalgam of products (warehousing, logistics etc). Moreover, it is difficult to assess the 'cost' of establishing a commercial relationship with a customer.

The cost and delay associated with this option may be sufficient to discourage potential third-party operators seeking access in the first place. Such an outcome would clearly be inimical to the emergence of the above-rail market. The QCA is therefore conscious of the desirability of developing reference tariffs for those traffics that are likely to attract significant levels of

interest from third-party operators. These reference tariffs would however be heavily influenced by the application of the Competitive Imputation Pricing Rule.

In summary, the QCA is mindful that the key considerations in the setting of access charges for traffics other than the major coal systems are likely to focus on:

- incremental maintenance and capacity costs (providing the floor); and
- the difference between QR's current haulage rates and its avoidable above-rail costs as this difference will be critical to assessing QR's internal access charges, which in turn will be relevant for third-party operators serving the same market. This will be important because the limitations on price differentiation require that there be no differentiation on access charges for the same market, subject to cost and risk considerations. The concerns associated with the practical and efficacious implementation of the Competitive Imputation Pricing Rule suggest that there may be merit in the Authority setting access charges for relatively homogenous traffics via the reference tariff mechanism. This is considered below.

#### *QCA's Position*

**The Authority would favourably consider an Undertaking that:**

- **amended the stand-alone cost definition, and accordingly the method for calculating stand-alone costs, to those costs which would be incurred by an efficient network provider;**
- **obliged QR to observe the limits on price differentiation irrespective of whether the resulting access charges cover the incremental cost of the individual train service; and**
- **amended the incremental cost definition to reflect the costs that would be avoided by an efficient network provider.**

## 5.4 Reference tariffs

To address the large range between the price floor and price ceiling under the constrained market pricing approach, QR proposed to develop and have approved by the QCA, reference tariffs for certain types of train services. Reference tariffs are aimed at promoting access price transparency and providing confidence to above-rail operators that access charges are being set at a reasonable level.

This section of the chapter has only addressed the issue of reference tariffs further to those QR has proposed for its Central Queensland coal systems in Schedule G of the Draft Undertaking. Chapters 9 to 16 of the Draft Decision discuss matters raised by Schedule G.

#### *QR's Position*

Reference tariffs for other types of train services will be developed as and when QR and the QCA agree them to be necessary, taking into account the level of demand for access for that type of train service by third-party operators. QR will submit a draft amending undertaking

varying Schedule G to identify the manner in which reference tariffs will apply to these train services within one month of agreeing to develop the additional reference tariffs: para 5.1.3(f).

Where Schedule E is varied in accordance with para 5.1.3(f), QR will submit to the QCA reference tariffs for the types of train services added to Schedule E within 3 months of the QCA accepting the draft amending undertaking. In considering whether to endorse a reference tariff the QCA must be satisfied that the reference tariff is consistent with the principles established in Part 5 of the Undertaking: para 5.1.3(g).

### ***Stakeholder Comments***

A range of views was expressed as to whether reference tariffs ought to be developed for services beyond those specified in the Draft Undertaking.

#### **Table 12: Further reference tariffs**

**Great Southern Railway** - a passenger reference tariff is unlikely to be useful.

**AMC, QMC, FreightCorp** - reference tariffs could be developed for various parts of the North Coast line and/or Mt Isa line.

**Stanwell** - the same arrangements should apply for reference tariffs for domestic and export coal.

**Toll** - reference tariffs should not become a method of entrenching commodity surcharges in relation to the transport of particular products or commodities. There is no economic or practical reason for setting commodity specific reference tariffs in the way proposed. We have encountered significant difficulties because QR has sought to impose a surcharge on the movement of certain commodities. This generally corresponded with significant contracts held by QR's above-rail business units.

**Queensland Government** - prospective third-party operators will identify other services warranting reference tariffs.

### ***QCA Analysis***

The QCA envisages that reference tariffs for coal traffic will provide increased pricing transparency that will facilitate negotiation by providing a benchmark against which third-party operators can assess the reasonableness of QR's proposed access charges.

There remains however the issue as to whether additional reference tariffs should be developed for other train services. In this regard, the establishment of further reference tariffs represents a form of price regulation of QR's below-rail business that could arise even though it produces access charges that do not exceed the stand-alone cost test in respect of the subject services.

The Authority considers that the key consideration in the development of further reference tariffs is whether the benefit to the competitiveness of the above-rail market from increased pricing transparency for a relatively homogenous set of train services justifies the intrusion into QR's operational autonomy.

The potential benefits of this increased price transparency include the time and effort required to negotiate access to relevant services being substantially reduced through the availability of reference tariffs. It is conceivable that, in the absence of reference tariffs, the transaction costs associated with negotiating access charges (including costs arising from delay) could be so high that a distortion is introduced into the above-rail market.

Another benefit is that if QR levies access charges for its above-rail operator in accordance with an approved reference tariff, it is very unlikely to be in breach of the hindering access provisions of the QCA Act.

The QCA considers that reference tariffs ought to be established for the services most likely to attract interest from third-party operators. It is expected that these services could include:<sup>111</sup>

- traffic on the Mt Isa line; and
- intermodal traffic on the North Coast line.

To ensure that the integrity of the above-rail market is not compromised, the Authority considers it should reserve the right to require QR to submit additional reference tariffs (that is for services other than those contained in Schedule G) for defined below-rail services. The QCA should be able to request the submission of reference tariffs during the course of the regulatory period (that is whilst an approved undertaking remains in place). QR should submit reference tariffs within 3 months of a request from the QCA. QR should also be obliged to provide any information the QCA requires in order to assess the reference tariffs QR submits. If QR does not submit reference tariffs within the time requested by QR, then the QCA should be able to determine the relevant charges to apply.

#### *QCA's Position*

**The Authority would favourably consider an Undertaking that required QR to submit reference tariffs for other services within three months of being required to do so by the QCA and obliged QR to comply with any request from the QCA for information to enable the QCA to assess those reference tariffs.**

## 5.5 Cost allocation

The Draft Undertaking proposed that QR would submit a Cost Allocation Manual (Manual) to the QCA following finalisation of the Undertaking: para 5.5(a). However, on the request of the QCA, QR submitted a Manual for consideration in December 1999. The QCA released a Request for Comments Paper *QR's Draft Undertaking – Costing Manual*, discussing the draft Manual and seeking responses from interested stakeholders. In addition, cost allocation was the subject of a working group meeting. The following discussion draws on the responses to that request for comments paper and the discussions at the working group meeting.

An inappropriate assignment of costs will have several adverse effects. For example, a cost allocation approach that assigns too great a proportion of costs to below-rail services (as opposed to above-rail services) will result in:

- third-party operators being placed at a competitive disadvantage relative to QR's above-rail business groups which could undermine the integrity of the above-rail market; and
- customers paying too much for their rail haulage services where there is an absence of intermodal transportation alternatives. Assigning a greater than appropriate portion of

<sup>111</sup> The QCA is continuing to assess reference tariffs for the coal traffic on the West Moreton line. This assessment is continuing at the time of release of this Draft Decision.

costs to below-rail services will tend to raise access charges which could be passed on to customers in the form of higher rates for rail haulage services.

An inappropriate assignment of costs to various levels within the organisation could have similar consequences. Accordingly, the adoption of the Manual by QR plays an important role in providing confidence to customers and above-rail operators that QR is not gaining an inappropriate commercial advantage over competitors through its vertical integration. It also should provide confidence that customers are not being required to pay excessive access charges (and in doing so cross subsidising other traffics).

### **5.5.1 Timing of finalisation of the Manual**

Under the QCA Act, the Authority may finalise a cost allocation manual approval independently of its assessment of a Draft Undertaking. Accordingly, the assessment of QR's Manual included whether it was appropriate to attempt to finalise the Manual in conjunction with the Authority's assessment of QR's Draft Undertaking or subsequent to it. The Authority suggested it may be appropriate to defer finalisation of the Manual until after the reference tariff process had been completed.

#### ***QR's Position***

QR accepted that it may be appropriate to defer finalisation of the Manual until after the completion of the Authority's assessment of the Draft Undertaking. However, QR emphasised that it does not support any approach where it would be required to redevelop and resubmit a Costing Manual in the absence of any formal feedback on the Manual already submitted.

#### ***Stakeholder Comments***

Stakeholder submissions expressed a range of views on the best time to finalise the Manual.

#### **Table 13: Finalisation of Manual**

**Queensland Treasury** – this is a matter for the QCA having regard to the views put by stakeholders.

**FreightCorp, Stanwell** - it would be appropriate for the QCA to delay approval of the Manual until after the final determination of the Undertaking.

**ARTC** - the Manual should be finalised with the benefit of the experience gained from the assessment of reference tariffs but before the draft and final decision on the basis that this approach would provide a longer term competitive benefit.

#### ***QCA's Analysis***

Finalisation of the Manual as part of the Authority's assessment of the Draft Undertaking could be expected to delay the Authority's release of a Draft and Final Decision by up to 6 months.

The key issue is therefore the extent to which the regulatory environment might be compromised if finalisation of the Manual were deferred until after completion of the Authority's assessment of the Draft Undertaking. This depends on the extent to which the QCA has the power to establish a cost allocation manual independently of the undertaking process.

The QCA's powers to ensure that appropriate cost allocation arrangements are in place will not be compromised if the QCA's assessment of the Draft Understanding is finalised before the Manual has been settled. The QCA Act makes it clear that acceptance of the Undertaking will not affect the QCA's ability to, if necessary, impose cost allocation arrangements upon QR.

Under the QCA Act, the QCA may request the owner of a declared service or its agent to prepare a cost allocation manual. If the Authority is not satisfied with the manual, then the Authority may prepare a cost allocation manual and the owner or its agent must comply with it. Under the QCA Act, the QCA may revise the manual from time to time.

Once a manual is in place, the owner of the declared service (or its agent) has a 6 month period of grace (up to 1 year if the QCA allows) after which it must keep its accounting records in accordance with the manual. Accordingly, the Authority is empowered, if necessary, to establish cost allocation arrangements independently of the Undertaking assessment process.

The QCA considers that QR's Manual should perform two critical functions, which are to:

- assist in providing confidence in the integrity of the above-rail market; and
- provide information relevant to the determination and evaluation of access charges.

The QCA is concerned to ensure that the regulatory environment provided by the Undertaking protects the integrity of the above-rail market and provides market participants with sufficient confidence in this outcome so that investment in the industry is not discouraged by QR's vertical integration. This primarily requires that the costs and assets associated with the provision of above-rail services are not inappropriately assigned to below-rail services. This in turn involves potentially assigning the benefits of vertical integration between QR (and, in turn, its shareholders) and its customers.

The Manual also provides the basis for the assembly of information to inform the quantification of access charges, including future reviews of reference tariffs by:

- setting out the appropriate level within the organisation to which below-rail costs should be assigned – such as to a line section, to a geographic region or to the network as a whole; and
- enabling costs to be assigned to particular traffics for the setting of access charges.

In addition, third-party operators and end users will seek to ensure that the Manual provides a framework that ensures that particular traffics are not assigned costs that cannot reasonably be attributed to those traffics. These parties will also want to ensure that the Manual provides a framework within which they are able to monitor QR's financial performance in respect of the provision of below-rail services in order to assess the appropriateness of access charges, especially reference tariffs.

To assess the integrity of QR's apportionment of costs and assets between its above and below-rail businesses, the QCA appointed Mr Dick Bullock to review QR's management accounts. His report is contained in working paper 6. Mr Bullock's assessment was that the separation of costs and assets between QR's above and below-rail operations was extremely robust.<sup>112</sup> On this basis, the Authority does not consider that deferring finalisation on the Manual will jeopardise the development of the above-rail market.

The concern that stakeholders be capable of monitoring QR's financial performance with a view to, for example, assessing the appropriateness of reference tariffs remains. However, even if the Manual was finalised as part of the assessment of QR's Undertaking, it is unlikely that financial reports for the previous financial year would be subject to it. Accordingly, there appears to be

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<sup>112</sup> Mr Bullock's suggested improvements to QR's management accounts are discussed below.

little disadvantage in deferring consideration of the Manual until after finalisation of the Undertaking so long as the process is completed before the end of the current financial year.

Accordingly, the Authority does not consider it appropriate to attempt to complete its assessment of QR's Manual in conjunction with its assessment of QR's Draft Undertaking. In this regard, the Authority notes that on balance, stakeholders preferred the approach of deferring finalisation of the Manual at least until the Draft and Final Decision on QR's Undertaking has been released. However, in recognising the concerns expressed by various stakeholders, including QR, the Authority's Draft Decision contains a detailed analysis of the major issues that the Authority considers relevant to the finalisation of the Manual. The Authority is keen to gain the benefit of stakeholder views on the appropriateness of these proposals in conjunction with the finalisation of its assessment of QR's Draft Undertaking.

The consultation associated with the Draft Decision will thus provide all interested parties with an opportunity to participate in the finalisation of the process. On balance, the Authority considers this is the most expeditious means of moving forward. The Authority's detailed views on the Manual are set out below.

***QCA's Position***

**The QCA accepts the proposal to finalise the Costing Manual following the conclusion of its assessment of the Undertaking.**

### **5.5.2 Transparency**

#### ***QR's Position***

##### *Level of prescription*

QR argued in its submission to the QCA's Request for Comments Paper *QR's Draft Undertaking – Costing Manual*, that the primary role of the Manual is to provide a statement of costing principles. The Manual sets out how QR performs cost identification, attribution and allocation, and the Manual is quite specific about the process by which QR conducts cost and asset allocations.

QR argued the role of the Manual is not to provide detailed technical analysis and data on cost allocators. For example, it requires that each of QR's facilities be individually assessed to identify the above/below-rail split, however, it does not necessarily identify the specific allocator to be used in all circumstances. In QR's view, good costing practice will recognise that circumstances and hence allocators, will vary in quantum and nature.

QR is, however, prepared to include in the Manual a 'default' allocator, where applicable, for allocating costs. The default allocator generally would reflect accepted railway costing practices. However, alternate allocators may be used on a case by case basis if they would not result in a materially different allocation of costs, or in the event that better information is available, the alternate allocator would provide a better allocation of costs.

In relation to the choice of regions, QR's view is that the fundamental principle of the hierarchy of below-rail costs is to minimise the extent to which costs need to be attributed or allocated to a level that is arbitrary and potentially misleading. QR maintains it has chosen its specific geographic regions according to the best 'natural' delineation of costs. That is, it has tried to minimise the extent to which allocations are used across regions.

Were regions to be reduced to a level below that of the ‘natural’ delineation of costs, the use of allocation to identify regional costs would increase. The provision of these smaller regions on a stand alone basis would be likely to incur costs ‘attributed’ to other regions. As a result, QR would not be able to guarantee the exclusion of costs incurred in other regions from costs of the region in which a given train service operates.

QR offered to enhance the manual by providing that an allocation of these costs to a region and, within a region, to a system, will form the starting point for an assessment of stand-alone cost. However, in order to finalise the estimate of stand-alone cost, QR noted it may adjust the amount of costs associated with these activities to reflect the effect of economies of scale associated with the provision of these services to a smaller group of traffics.

QR noted the materiality of the issues the QCA has raised relating to cost identification, attribution and allocation depends on the proportion of QR's costs identified as above or below-rail and (for below-rail costs) identified to line sections, regions or network wide.

The table below, provided by QR in its submission in response to the issues paper, provides an indicative disaggregation of these proportions, for 1998-99. With reference to the figures provided in that table, QR suggests a misallocation of those operating costs not identified directly as relating to particular line sections (9.8 per cent of total costs) is not likely to affect significantly the distribution of costs. An example provided by QR notes a 50 per cent misallocation of costs between uses would cause a difference from a correct allocation of less than 5 per cent (that is  $9.8\% \times 0.5 = 4.9\%$ ), a proportion which is less than that usually regarded as material by auditors.

#### **Indicative disaggregation of QR's costs, 1998-99 figures**

**Panel 1. Proportion of QR above and below-rail operating costs relative to total operating costs (%)**

	Above-rail	Below-rail	Other Activities	Total
Percentage of total QR operating costs accounted for	55. 0	29. 5	15. 5	100. 0

**Panel 2. Proportion of QR below-rail operating costs identified, attributed and allocated as below-rail operating costs (%)**

	Identified	Attributed	Allocated	Total
Line Section Specific	62. 8	5. 6	0. 0	68. 4
Regional Specific	7. 7	8. 2	0. 8	16. 7
System Wide	3. 9	1. 9	9. 1	14. 8
<i>Total Below-rail Operating Costs</i>	<i>74. 4</i>	<i>15. 7</i>	<i>9. 8</i>	<i>100. 0</i>

**Panel 3. Proportion of QR below-rail assets identified, attributed and allocated as below-rail assets (%)**

	Identified	Attributed	Allocated	Total
Line Section Specific	76. 1	6. 0	0. 0	82. 1
Regional Specific	4. 9	3. 4	0. 0	8. 3
System Wide	4. 6	4. 4	0. 6	9. 6
<i>Total Below-rail Assets</i>	<i>85. 6</i>	<i>13. 7</i>	<i>0. 6</i>	<i>100. 0</i>

QR argued that the purpose of the use of terms such as ‘small proportion’ and ‘significant proportion’ are intended to give stakeholders some better understanding of how stand-alone costs and incremental costs will be assessed. QR regards the interpretation of such terms to be primarily a matter of experience and judgment. Interpretations may vary in different contexts.

As such QR believes that the judgement of materiality should be made on a case-by-case basis. If an operator disagrees with QR’s assessment of materiality (‘small’, or ‘significant’), there is the ability for this matter to be referred for expert resolution.

#### *Assignment of benefits of vertical integration*

QR considers that the pricing approach it has adopted (constrained market pricing - see Section 5.2) allows it to establish access charges within bounds set by incremental and stand-alone costs. QR suggests that a requirement by the QCA to pass on selected cost savings would be inconsistent with the economic theory underlying this pricing approach. QR also noted the costs of complying with regulatory requirements are higher because of vertical integration, so that passing on just the benefits to below-rail operators would disadvantage QR.<sup>113</sup>

#### *Stakeholders Comments*

Stakeholder submissions in response to the QCA’s Request for Comments Paper *QR’s Draft Undertaking – Costing Manual*, agreed there was insufficient information in the Manual to provide confidence that it would perform its intended role and that this was the major problem. Submissions addressed the parameters that QR proposed to underpin the attribution or allocation of assets/costs and the level of disaggregation in cost allocation.

#### **Table 14: Costing Manual deficiencies**

**Stanwell** - the assumptions and cost drivers underlying cost allocations should be made explicit and public, particularly in the case of so-called ‘common’ and ‘joint’ costs. It is of little assistance for users to know that costs will be allocated on a ‘usage’ basis, on a ‘reasonable’ basis, or in a ‘balanced’ manner.

**Queensland Treasury** - it is essential that the identification, attribution and allocation of costs and assets is accurately undertaken to ensure that the relevant users are charged according to their corresponding access to the rail network.

**ARTC** - it would add transparency if ‘small proportion’ was defined. Reporting, whether public or to the regulator, should include a more disaggregated set of segmented costs to either region or even line section.

With regard to the system of work orders and account coding proposed in the Manual, cost control and data integrity (accidental or deliberate) is not always a high priority and this will need to be monitored very closely by the regulator through the audit process.

**FreightCorp** - for most of the issues that could be raised, a user of the Manual would be satisfied that an appropriate level of detail regarding the allocation was provided if (s)he had guidance as to the relative importance of such issues.

There should not be significant problems with the regions as identified, but there is insufficient detail regarding the allocation of costs in order to be able to make a specific judgement on this issue.

#### *Assignment of the benefit from vertical integration*

Stakeholders considered whether the Manual should specify how cost savings from vertical integration would be passed on to above-rail operators.

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<sup>113</sup> QR has argued that the additional costs involved in meeting the additional regulatory requirements arising from its vertical integration should form part of its cost base. This is addressed in Chapter 12.

**Table 15: Cost savings from QR’s vertical integration**

**FreightCorp** - this is appropriate as QR has deliberately chosen to provide infrastructure services as an integrated entity (although acknowledging the difficulty of allocating the cost benefits).

**Stanwell** - to make allowance separately for cost efficiencies from vertical integration, in addition to taking account of efficiency gains generally, would be to risk ‘double counting’ the cost saving.

**Queensland Treasury** - an appropriate portion of the benefits of vertical integration (generally encapsulated in overhead costs) should be passed on through the below-rail access pricing.

A majority of stakeholder submissions in response to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking*, expressed concern about QR’s intent as far as retaining the benefits of its vertical integration is concerned.

**Table 16: Benefits of QR’s vertical integration**

**ARTC, National Rail, Toll** - more information is required on the nature of the synergies.

**ARTC** - if such synergies are financially identifiable they should be recognised in the Manual and appropriately apportioned to above and below-rail activities.

**QMC** - the cost savings from vertical integration should be attributed to Network Access and be reflected in lower access charges. No element of the savings should be allowed to be retained by QR above-rail business groups or Network Access. Nonetheless, the benefits of QR’s vertical integration had yet to be demonstrated.

**AMC, Stanwell** - there would not appear to be any sound grounds why QR should retain all the benefits of synergies from vertical integration. In a competitive situation, such synergies would in general be passed on to customers in order for the business to maintain these customers or to win new customers from competitors. If vertical integration reduces the infrastructure provider’s costs, then these lower costs should be reflected in the revenue requirement of that provider and in turn be reflected in access charges for the infrastructure. In this way, end-users benefit.

**Queensland Government** - the benefits from vertical integration include: lower transaction costs, especially contracting costs; benefits both in terms of coordination of day-to-day operations and investment planning; and general economies of scope. These benefits - by way of lower costs - of vertical integration should be available to third-party operators under the pricing principles contained in the Undertaking. If it is possible to identify future cost savings flowing from vertical integration or alternatively, additional costs resulting from a separation of QR, aside from those already inherent in the existing cost structure, there may be a need to ensure that there is a process for pass-through of these cost savings to users.

**RTBU** - QR should retain the benefits of its vertical integration. Would the QCA suggest a coal exporter that starts to operate a coal train service on the QR network should not benefit from the linkages it has between mine, train and port? Nevertheless, QR’s customers are already benefiting from its vertical integration through QR’s enhanced reliability, safety and commercial orientation.

***QCA’s Analysis***

The appropriate level of prescription for the Manual turns on its intended purpose. At times, regulatory authorities in various jurisdictions have prescribed highly complex regulatory accounting arrangements that may have materially departed from financial accounting

arrangements applicable to the regulated organisations.<sup>114</sup> Highly prescriptive cost allocation arrangements continue to apply to sectors of the rail industry around the world.

In contrast, QR's proposed Manual represents what could be described as a procedural guide to its cost allocation processes. A key issue is therefore assessing the level of prescription that is appropriate given the intended role of the Manual. As discussed above, the Authority considers the purpose of the Manual is to provide interested parties with confidence in the integrity of the above-rail market and to provide information relevant to the determination and evaluation of access charges.

Broadly, there appear to be three options concerning the level of prescription that is appropriate for the Manual:

- QR's current approach, which could be described as high level;
- highly prescriptive approaches, such as the Uniform Rail Accounts that apply in the United States; and
- a middle ground which is more detailed than QR's proposed Manual but less prescriptive than alternative models.

Whilst prescriptive processes provide a high level of certainty and relative confidence that appropriate processes are in place, they are invasive and inflexible and can impose high compliance costs. There is also the risk that they will impose requirements that force inappropriate allocations to be made.

QR's current approach might be described as a 'high level'. This is because the Manual espouses high level principles. These high level principles could in practice provide an inappropriate degree of latitude to the assignment of costs and assets as any number of possible allocations could be effected in accordance with the principles.

The issue therefore arises as to whether adjustments can be made to QR's current Manual to achieve an outcome that reflects an appropriate allocation of costs and instils confidence in this outcome without being more invasive than is necessary.

A critical consideration of this assessment is the role the Manual is intended to perform. The regulatory costing systems that were developed in North America were designed to assist in detailed assessments of total freight charges, which required costs be assigned to individual traffics and to branch lines proposed for abandonment. The purpose of QR's Manual is different in that its key purpose is to achieve an apportionment of cost between above and below-rail operations, where a substantial proportion of below-rail costs can be unequivocally ascribed to particular line sections.

Accordingly, in an environment where an independent expert has endorsed QR's assignment of costs and assets between its above and below-rail businesses, the Authority considers that it is reasonable to accept a less prescriptive approach be applied than might otherwise be the case (at least initially), subject to the amendments proposed below. However, the Authority is particularly concerned with stakeholder views on the adequacy or otherwise of these arrangements. In this respect, the Authority is mindful of its capacity to revise the Manual over time should it become necessary.

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<sup>114</sup> Similarly, tax legislation may impose a different set of accounting rules to those applied for financial accounting purposes. This is another example of different sets of rules being designed to perform different functions and inform different audiences and processes.

The issues relevant to the assessment of the Manual arise at two different levels. The first level concerns the assignment of costs and assets between QR's above and below-rail operations. The second level concerns the cost allocation underpinning the determination of stand-alone cost, which is critical to the Authority's assessment of QR's proposed and future reference tariffs. The concerns in relation to this second level are considered in chapter 12.

Therefore, an important starting point in establishing confidence in QR's cost allocation process is to identify the proportion of QR's costs accounted for by above and below-rail and, for the below-rail component, proportions of operating costs and assets identified, attributed or allocated to line sections.

Mr Bullock's report extensively examines QR's practice in the assignment of costs and assets between QR's above and below-rail operations. This report, which forms working paper 6, provides the QCA with confidence that QR's current procedures provide a good estimate of the division of costs between above and below-rail activities.

Mr Bullock pointed out that most costs can be unambiguously estimated and identified to either specific line sections (in the case of maintenance costs) or systems (in the case of train control). Consequently, apart from a limited number of identifiable cost categories, such as corporate overhead, QR's scope for discretion in the allocation of costs is relatively limited. This is an important finding. From a regulatory perspective, it means that attention can be focused on the functions in QR's operations that straddle above and below-rail components of the business.

Whilst Mr Bullock's approval of QR's cost allocation practice is significant, and provides the Authority with confidence in QR's actual allocation of above and below-rail costs and assets (which in turn is relevant to the setting of reference tariffs), his report contained several recommendations to enhance QR's Manual.

Mr Bullock found that the reliability of the estimates relies heavily on the knowledge and diligence of the staff undertaking the work and measures should be implemented to enable much of the work to be done automatically through the accounting system.

Moreover, the Manual in its current form could justify a significantly different and inappropriate allocation of costs and assets. Accordingly, the transparency of the cost allocation arrangements requires greater attention. Accordingly, the Authority considers the following enhancements should be made to the Manual:

- all costs and assets directly associated with declared services be specifically identified and distinguished from:
  - costs and assets that do not relate to below-rail services; and
  - costs and assets that indirectly relate to below-rail services;
- the work order system that is central to detailed cost identification under the current QR SAP accounting system be enhanced;
- clearer allocation rules be adopted, including in some cases, default allocators;
- that the four systems that comprise the Central Queensland coal region be designated geographic regions in their own right;
- distribution of cost to lower levels within the organisation; and
- greater clarity for assessing materiality.

### *Specification of declared services*

The component of QR's business of critical concern is the provision of declared services which requires a clear distinction be made between costs and assets involved in the delivery of below-rail services and the remainder of the business (which is comprised mainly of QR's above-rail operations). However, even the provision of below-rail services can be separated into two components:

- the costs and assets directly associated with the provision of declared services (for example track, train control); and
- the costs and assets indirectly associated with the provision of declared services (for example, maintenance of assets).

Categorising the costs and assets comprising QR's business in this way facilitates the isolation of functions which involve more than one of these components, which, in turn, identifies areas of interest to the cost allocation process. In other words, the categorisation minimises the intrusion into QR's operations because it facilitates focusing on those functions which currently involve both above and below-rail operations.

This could be done, for example, by using a specific code in the customer area of the work order in the following areas:

- yards, with those parts of line sections that are subject to the declaration being coded differently to those that are not. This avoids the risk of costs associated with above-rail yards and sidings being inappropriately attributed to below-rail operations;
- groups involved in both above and below-rail activities (for example, train control which currently also involves train management) having separate sub-pay centres so that above and below-rail costs can be clearly separated to the maximum extent possible;
- ISG facilities, which are below-rail in nature but are not declared, being separated from infrastructure providing declared services (so that declared and undeclared below-rail services are separated); and
- the cost of residences should be identified to the businesses whose employees use them and should be netted off with employee contributions towards their upkeep.

The effect of this recommendation should enable QR's below-rail role as infrastructure manager to be clearly separated from its other role as maintenance contractor. The costs associated with the latter should be removed from the direct above/below-rail split and instead be transferred to a separate group whose costs would flow to the above or below-rail groups depending on the maintenance activities undertaken.

If such a distinction is made, it would then be possible for QR's general ledger to clearly distinguish between two discrete below-rail functions, being:

- the asset manager, train scheduling and train control functions (performed by Network Access); and
- the contract maintenance functions (performed by ISG).

For example, in the case of facilities maintenance, some assets are below-rail and declared (for example maintenance of a CTC hut) while others are below-rail but not declared (for example residences for ISG staff). Distinguishing between these classes of cost and asset would provide

a more accurate distribution of cost between above and below-rail, and in turn, to the provision of declared services.

Without such a distinction being made in the accounts, it is very difficult to properly assess the efficiency with which QR's internal maintenance provider performs relative to external maintenance contractors. Although the costs associated with the maintenance function represent the major share of below-rail operating expenditure, they are generally not subject to competitive tender. Nevertheless, ISG's potential competitors can provide benchmarks for the QCA to assess the appropriateness of QR's proposed infrastructure maintenance charges. Unless below-rail costs are appropriately assigned to Network Access and ISG respectively, it is difficult to protect QR's legitimate business interests or the interests of those that seek access to QR's network.

#### *Work orders*

The Authority considers that greater use ought to be made of work orders.<sup>115</sup> Under QR's proposed accounting arrangements, work orders play a pivotal role in the cost allocation process as they are the vehicle through which the incurring of cost is recognised and through which the allocation of cost is effected.

Consequently, the integrity of QR's cost allocation process turns on the faithful completion of work orders and it is expected future audit processes will monitor this aspect closely. However, an audit of work orders for the 1998-99 year revealed a marked variation between regions in the way in which costs were recorded.

An area requiring greater accountability arises in respect of the Technical Services Group, which incurs significant costs on behalf of Network Access. The QCA considers that all substantial projects, including any series of related projects which in aggregate involve expenditure of greater than \$100,000, should be the subject of a separate work order.

Similarly, station costs should be charged to ISG through work orders. This would assist in the better identification of below-rail costs.

#### *Clearer allocation rules*

In its submission QR has offered to provide a 'default allocator' in the Manual, where applicable, which would reflect generally accepted costing practices. QR has not yet provided any indication on the proposed default allocators, nor provided any guide as to what proportion of costs would be covered in this way. However, such default allocations will substantially enhance the transparency of the cost allocation process.

The Manual should contain a default allocator to facilitate the allocation of overheads according to defined rules. Corporate overheads can be separated into two categories:

- those of a general corporate management nature where there are considerable difficulties in identifying individual costs that are either specifically above or below-rail; and
- those of a more direct nature which are able to be allocated (for example, payroll according to staff number).

In relation to the first category, the QCA considers that overhead be allocated between above and below-rail groups on the basis of total working expenses, after an allowance has been made

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<sup>115</sup> The Authority recognises that QR is currently increasing its use of work orders.

at the corporate management level for corporate overhead credits for the corporate management effort applied to capital projects (at present, there is no such allowance). However, in other respects, this corresponds with QR's current practice.

The other significant function covering both above and below-rail areas relates to work trains. Work trains involve the use of rollingstock (above-rail) for the maintenance function (for example, hauling ballast and rail-mounted inspection equipment). The costs associated with work trains include capital (use of the locomotives and wagons), crew, fuel, maintenance station costs and overhead. These costs contribute approximately 3% of total maintenance costs. The resources used for providing these services are not dedicated to ISG tasks. Accordingly, the costs of performing this function must be assigned to ISG on the basis of work orders.

The Authority considers that greater transparency is required for the assignment of costs from the provision of work trains. An acceptable level of transparency would be accomplished by simply providing the basis for charging these services (that is ¢/ntk of haulage and \$/train hour for time spent on site). It is understood this accords with current internal practice. Similarly, station costs should be charged to ISG as part of the work order process. This will permit better identification of maintenance costs.

The other significant function that provides services to both above and below components of QR's business is telecommunications. QR's backbone infrastructure is increasingly being supplied by third parties and consequently it would appear that the most realistic approach to cost allocation would be to adopt a commercial pricing approach. The QCA considers that QR's use of its telecommunications network for purposes other than to support core below-rail functions should be priced on a commercial basis, that is, on the cost of using a third-party network. This approach is most likely to set a price that is consistent with the price that QR would be indifferent to selling the service to a competitor.

#### *Creation of additional geographic regions*

Once costs have been assessed as above or below-rail, it is necessary to assign those costs to various levels in the organisation. QR has suggested that costs and assets be assigned to three levels within the organisation – to a line section, to a geographic region (of which there are 9) or to the network as a whole.

However, the Authority considers the Blackwater, Goonyella, Newlands and Moura systems should each constitute a separate geographic region as cost can be assigned to these systems in a way that is not arbitrary. The most significant regional cost involves the provision of train control services, which can be relatively easily assigned to a system (or even to a particular traffic) on a per train path kilometre basis.

QR has objected to this approach on the basis that a potentially misleading assignment of costs could occur with a greater level of disaggregation. Notwithstanding this view, the QCA understands a significant proportion of costs presently assigned by QR on a regional basis can be readily associated with particular coal systems. The basis for this view is that the appropriate allocator for many below-rail costs, as discussed above, is capable of being applied at the system level. QR's assertion of a misleading outcome is inconsistent with the fact that such an allocation of cost is required as part of the development of reference tariffs.

The QCA therefore considers a greater degree of disaggregation of the coal system for the purposes of assigning below-rail costs is warranted with the Central Queensland coal system being disaggregated into four regions, based on the Blackwater, Goonyella, Newlands, Goonyella and Moura systems.

### *Transfers*

The QCA would prefer if the current practice of transferring employee related costs was changed to distribute these costs directly as labour and materials on-costs to the lower level cost centres rather than to the top level of branch administration, and thus reduce the administrative overhead. Moreover, the costs of the ISG facilities manager should be removed from administration and included in the direct costs of facilities maintenance (after allowance for an allocation of this manager's time on other activities, such as graphic services etc).

### *Accounting adjustments*

The Authority considers that QR should 'net off' costs at least partially against corresponding revenues, with only the net amount being charged to either above-rail or below-rail activities. Examples include property, capital projects expensed and residences. This might require a reconciliation between published financial statements and those produced pursuant to the Manual.

### *Materiality*

In its submission, QR provided an example that shows a misallocation of 50 per cent of regional and system-wide costs would result in a difference of less than 5 per cent of total costs. However, 5 per cent of total costs is such a level of discrepancy that would overwhelm the profit margin in many industries.

With regard to the use by QR of terms such as 'small proportion' and 'significant proportion', the QCA is concerned that QR proposes to leave these terms to its own interpretation. Recourse to dispute resolution procedures is unlikely to provide an adequate solution to disputes on the meaning of these terms because of the inherent subjectivity involved.

However, the other amendments proposed to the Manual substantially alleviate the QCA's concerns on this issue. This is because Mr Bullock recommended separate cost codes be developed for costs or assets that currently involve a declared and undeclared component, for example, land and signals in yards and train control. This is the context in which terms such as small proportion are most commonly used in the Manual.

The other area of the Manual that refers extensively to these terms relates to the calculation of the incremental cost of traffic on lines. This issue is significant in the calculation of the stand-alone cost of the coal network and is considered in Chapter 12.

### *Assessment of benefits of vertical integration*

The split between above and below-rail is reasonably straight forward. It is unlikely that there are substantial synergies from vertical integration for the purposes of the cost allocation process. Indeed, the most significant benefit from QR's vertical integration is related to the reduced transaction costs in negotiating and administering access agreements. For example, where a disagreement between a third-party operator and QR might require an expensive arbitration, internal QR disputes could normally be expected to be quickly resolved by QR's Chief Executive. In addition, the limited number of QR's internal access agreements means that they are relatively inexpensive to negotiate relative to third-party operators.

Beyond these transactional savings, the most significant source of benefit from QR's vertical integration is possible overhead scale economics. However, overheads only represent approximately 5% of total working expenditure, and therefore a small saving in these overheads will not be significant in overall terms. The QCA's assessment of QR's proposed cost allocation concluded that allocating QR's existing overheads resulted in expenditure that was at

the upper bound of a reasonable range for an efficient stand alone provider and consequently, scale economies, even if present, do not result in allocated costs that are below those estimated for a hypothetical efficient stand alone provider. The estimation of these costs is discussed in Chapter 12.

Accordingly, the Authority does not consider it necessary to make recommendations in relation to the assignment of the benefits of vertical integration.

***QCA's Position***

**The Authority would favourably consider a Costing Manual that provides for:**

- **default allocators for corporate overheads;**
- **the creation of additional account codes to more accurately reflect the split of costs and assets relating to declared and undeclared services;**
- **telecommunications costs to be assigned to QR's business groups, than below-rail groups, on the basis of the market price of the services consumed by those business groups;**
- **QR's four Central Queensland coal systems to be treated as geographic regions in their own right;**
- **the more structured use of work orders;**
- **the netting off of 'like for like' cost recovery type revenue items against the relevant cost items; and**
- **the assignment of corporate service costs to levels appropriate to where the costs are incurred rather than the Group General Manager level.**

### ***5.5.3 Approaches to Cost Allocation – Internal Trading or General Ledger***

***QR's Position***

QR argued in its submission to the QCA's Request for Comments Paper *QR's Draft Undertaking – Costing Manual*, that costing based on the general ledger is compatible with existing management accounting processes within QR. The approach also permits comparability with historic information, although there is some complexity in the number of allocation interactions.

QR accepted that an internal trading basis reflecting market prices for access has some benefits and that it is moving towards this for service delivery between business groups. However, QR does not regard its current internal trading system as mature enough to form a base for accurate estimation of vertically and geographically separate costs and hence the Manual. QR's internal trading is essentially a mechanism to encourage commercial behaviour in the relationships between its business groups.

However, QR noted the driving force behind the further development of QR's internal trading arrangement will be QR's business requirements and, from a commercial perspective, the

cost/benefit trade-off of moving to this arrangement. QR pointed out the provisions of the QCA Act which state that, in so far as it considers practicable, the Authority must take account of the existing accounting system of the operator of the declared service.

Regarding additional information, QR stated the purpose of transparency is to ensure that stakeholders can have comfort that QR's cost base is reasonable. There can be a number of ways in which this comfort can be provided, and requirements for disclosure of specific information must be considered in the context of the package of arrangements that is being proposed. Most notably these considerations include QR's commercial confidentiality requirements and matters of business efficiency.

QR stated that it considers that the package of arrangements offered in the Draft Undertaking and in subsequent submissions should provide comfort to stakeholders that QR's prices are appropriate, and that there is no requirement for additional information to be provided through the Manual. These arrangements comprise:

- public reporting of a statement of assets and statement of earnings before interest and tax for below-rail services;
- public reporting of costs and assets for the Central Queensland coal region separate to the rest of QR's rail network;
- an independent audit to ensure that QR develops its costs for the purpose of public reporting in accordance with the provisions of the Manual; and
- published reference tariffs for coal carrying services that have been reviewed and endorsed by the QCA as complying with the principles of the Undertaking, including:
  - not exceeding stand-alone cost (measured on a combinatorial basis);
  - reflecting a transition to efficient cost service delivery; and
  - reflecting a commercial return on an optimised asset valuation.

### ***Stakeholder Comments***

Stakeholders commented on the internal trading approach and additional information QR might be required to produce.

#### **Table 17: Cost allocation approach**

**FreightCorp** - an internal trading approach would be likely to provide a much clearer understanding of what costs are applied and how they are arrived at. Under such an arrangement it would be much easier for a regulator to judge the appropriateness of the charge. This would be one mechanism that would facilitate the use of efficient costs (using external benchmarks) and would obviate the problem of disentangling costs that are associated with other functions, such as maintaining work practices, that are related to reasons other than commercial behaviour.

However, the use of internal trading does provide the opportunity for misbehaviour in the loading of costs if the trading regime is not subject to external scrutiny. For this reason, we would expect any adoption of internal trading to be subject to review by the QCA.

**Stanwell** - where QR provides Network Access with internal services that could readily be sourced outside of QR, internal trading arrangements are appropriate. Where the internal service is not available outside of QR, a general ledger approach is appropriate.

**FreightCorp** - under either approach QR should publish the statistics (in total, for each line section) for the various cost drivers used in allocating costs to line sections, along with the total costs. However, if the general ledger approach were adopted, there would be an even greater need for explicit reporting of activity to allow users and the QCA to observe the actual performance of QR.

The industry would gain an overall advantage from the publishing of access contracts such that all parties can identify the access charges that are being paid for each haul.

**Stanwell** - if the general ledger approach is adopted, QR ought to provide the internal 'purchasing' business unit with reasonably accurate costings for those services that it purchases.

**QMC** - cost effective decision making requires adequate knowledge of, and control of, costs. However, Network Access does not have its own separate accounting system. Rather, QR's accounting is centralised and costs are collected on a functional rather than responsibility basis. Network Access should develop its own accounts within a reasonable period and costs should be recorded on a train service group (system) basis as it is at this level that major assets, and costs, are shared. This requirement should be stated in the Undertaking and reflected in the proposed Manual.

### ***QCA's Analysis***

The Manual is based on the general ledger approach as distinct from an internal trading arrangement. Costs are allocated through the management accounts process rather than on the basis of available market benchmarks.

A Manual based on internal trading would assign costs consistent with the prices that had been determined for internal trading arrangements. For example, under such an approach, the need to extract the cost for below-rail departmental trains (work trains) from the general ledger on a component by component basis (maintenance, fuel etc) would not exist. Instead, Network Access would simply pay a market based rate for the use of above-rail trains on the same basis as if the product was transported by an external road haulage contractor.

The general ledger approach has the advantage of compatibility with QR's current general ledger and associated accounting protocols, which is important given the QCA's obligation to have regard to QR's existing accounting system. Minor changes to QR's internal structure can be more easily accommodated under this approach.

However, it suffers the disadvantage of reducing the level of transparency about the costs of services delivered by QR Network Access to rail operators (for example, departmental or work trains) and to Network Access by QR's above-rail business groups and ISG. The lack of transparency arises because of the number of cost manipulations that are necessary in this environment. For example, payroll costs for maintenance employees would go through several steps before reaching below-rail costs.

In contrast, the cost of such services would be included in the contract-based charge in an internal trading environment, providing a basis for the charges to be compared to market rates. Therefore, the internal trading approach is likely to facilitate transparency for the purposes of attributing the cost of internally provided service cost by allowing the regulator (and, if appropriate, other parties) to clearly see the basis of internal contracting arrangements.

The key issue is whether sufficient clarity and transparency can be achieved using QR's existing accounting system. The QCA considers that it is possible to address the concerns raised above through the suggestions that were made in relation to the improved transparency of the cost allocation arrangements. For example, in the case of departmental trains, which if the Authority's recommendations were adopted would be the most significant service provided to below-rail groups by above-rail groups, sufficient transparency may be achieved through

disclosure of relevant rates. The concerns with the provision of services by ISG can be addressed by separating the costs and assets for below-rail functions into those that are directly and indirectly related to declared services.

The QCA notes the suggestion of one stakeholder that Network Access should independently maintain its own accounting system. However, the Authority does not consider it necessary as the creation of such a system would not avoid the cost allocation issues that must be addressed through the Manual. This is because Network Access would still remain part of an integrated organisation. Accordingly, it is not considered realistic or desirable to insist that Network Access establish its own accounting system.

***QCA's Position***

**The QCA will accept the Manual being based on QR's existing general ledger approach.**

#### **5.5.4 Actual or efficient costs**

##### ***QR's Position***

QR stated in its submission to the QCA's Request for Comments Paper *QR's Draft Undertaking – Costing Manual*, the question of whether QR's costs are efficient is one that the QCA will separately examine in the context of assessing the maximum revenue that QR may earn from providing the declared service. Where QR's actual costs differ from the efficient costs of providing the service, QR may not achieve its target rate of return on the rail infrastructure assets.

QR stated historic costs are essential inputs to determining appropriate future costs, and are used as a matter of good practice to benchmark forecast costs. For planning purposes future costs take account of factors that are expected to change and efficiency improvements that QR expects to achieve over the forecast period. QR's costings that input into its access pricing limits therefore take into account the efficiencies that QR is expected to achieve.

##### ***Stakeholder Comments***

**Table 18: Incorporation of actual or efficient costs in Manual**

**FreightCorp** - forward looking efficient costs should be used in the determination of the floor, mezzanine and ceiling access charges. The use of actual costs will fail to achieve the correct pricing that would otherwise prevail in a genuine competitive market.

**Stanwell** - an allocation regime should ensure users pay only efficient costs.

##### ***QCA Analysis***

The QCA accepts that costs should be able to be reconciled with QR's audited financial accounts, to ensure the integrity of the cost data used to assess the cost of providing the declared service. In practice, it would become unworkable for QR to base its cost allocation processes on efficient costs as an audit trail does not exist for these costs in QR's existing accounting system. QR's cost allocation already involves a complex process, but has the desirable attribute of being reconcilable to source documentation. This would not be possible in a cost allocation environment based on QR's assessment of efficient costs.

The cost data provided via the application of the Manual will provide a basis for estimating stand-alone costs. The key point for the Authority’s assessment of efficient stand-alone costs is to ensure that QR’s accounting system generates information appropriate to the estimation of QR’s existing stand-alone costs. This information will then facilitate subsequent assessment of how those costs might depart from those that would be incurred if it were operating efficiently, to the extent that an efficiency gap can be identified.

***QCA Position***

**The QCA accepts that the base data for allocations under the Manual should be historic cost data.**

### 5.5.5 *Financial Reporting*

Two issues are relevant to the level of financial reporting:

- the extent to which QR should be obliged to report to a greater level of disaggregation than its below-rail business as a whole; and
- the publication of discrepancies between asset values and depreciation/amortisation amounts used for public reporting and for pricing.

#### ***QR’s position***

##### *Level of disaggregation*

QR will establish and maintain a separate set of financial accounts (a profit and loss statement and balance sheet) in respect of below-rail services provided by Network Access: para 3.3(a). These would be published in the Annual Report: para 3.3(c). QR will allocate any costs associated with staff or assets that provide functions jointly for both below-rail services provided by Network Access and for any other services in accordance with the method set out in the Costing Manual: para 3.3(b).

QR argued in its initial submission to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking*, that in developing the accounting arrangements, Network Access’ status as a QR business group without a separate legal identity or financial accounting system was a key consideration.

QR’s also indicated that rather than a balance sheet for below-rail services, it now intended preparing a statement of assets, on the grounds that the only additional information that the liabilities and equity information provides is the mix of financing assets. On a similar basis, it proposed that the profit and loss statement prepared for below-rail services provided by Network Access take the form of a statement of earnings before interest and tax.

In addition, QR confirmed that it did not intend to provide a statement of cash flows, as the main purpose of such a statement is to provide an indication of an organisation’s liquidity. Liquidity is not relevant from a business group perspective, as claims by creditors will be on the cash flows of the organisation as a whole.

QR argued in its supplementary submission to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking*, that it is not prepared to provide detailed financial information on a system basis. In support of its position, QR outlined some concerns with publishing detailed disaggregated below-rail financial information. These concerns are:

- Network Access will potentially compete with other railway managers in gaining the right to develop/manage extensions to the rail infrastructure. Consequently, QR's cost of infrastructure provision has commercial value to potential infrastructure providers;
- the current trend towards outsourcing means there is commercial value in below-rail cost information that could undermine QR's competitiveness in future competitive tendering in Queensland and interstate; and
- the provision of detailed cost information provides an incentive for operators to focus on how QR is managing the infrastructure rather than overall output.

In QR's view, the development of reference tariffs is a better means than published disaggregated financial information of addressing the information asymmetry between the access provider and access seeker concerning the setting of access prices. This is because:

- reference tariffs provide a reasonable compromise between QR's legitimate business interests and those of third-party operators, as it provides the latter with an indicative access price developed in accordance with the pricing principles set out in the Undertaking, while maintaining the confidentiality of QR's detailed below-rail costs;
- cost transparency in itself will not clearly identify what is an appropriate access charge;
- reference tariffs will promote understanding of what is a reasonable access charge and be the subject of regulatory scrutiny;
- regulatory scrutiny will minimise the occurrence of price related disputes;
- QR has committed to price consistently with the reference tariff; and
- the QCA is the only body that reviews QR's detailed cost components which provides for administrative simplicity.

#### *Disclosure of asset values*

In its submission in response to the QCA's Request for Comments Paper *QR Draft Undertaking - Costing Manual*, QR undertook to include, in the Undertaking, a package of measures to enhance the transparency of its cost allocations. These measures included:

- the public reporting of a statement of assets and a statement of earnings before interest and tax for below-rail services;
- the public reporting of costs and assets for the Central Queensland coal region separate to the rest of QR's rail network;
- an independent audit to ensure that QR develops its costs for the purpose of public reporting in accordance with the provisions of the Costing Manual; and
- the publishing of reference tariffs for coal carrying services, that have been reviewed and endorsed by the QCA as complying with the principles of the Undertaking, including:
  - not exceeding stand-alone cost (measured on a combinatorial basis);
  - reflecting a transition to efficient cost service delivery; and
  - reflecting a commercial return on an optimised asset valuation.

### **Stakeholder Comment**

Generally, stakeholders were concerned as to the level of proposed financial disclosure and supported separate reporting of elements of QR's below-rail operations.

#### **Table 19: Level of disaggregation**

**Queensland Government** - the financial disclosure proposed by QR appears likely to be inadequate in providing the desired level of transparency. More disaggregation of financial data, particularly in respect of components of the network, would be desirable. Providing profit and loss statements and balance sheets at an appropriately disaggregated level of the network would facilitate assessments of the appropriateness of specific access pricing. The publication of asset value discrepancies would ensure a more transparent process.

**AMC** - an overall profit and loss statement and balance sheet for QR's network will not allow effective scrutiny of network pricing by individual rail users.

**FreightCorp, National Rail** - the Undertaking should incorporate line section based cost information (see NSW Rail Access Regime and the (Western Australian) Government Railways Access Code 1999).

**FreightCorp** - the publication of discrepancies between asset values and depreciation/amortisation amounts used for public reporting and pricing is necessary, in keeping with a requirement for reconciliation between detailed cost categories and the published partial financial statements.

**National Rail** - CSO payments to QR's above and below-rail operations should be reported.

**QMC** - the Undertaking should identify the separate train service groups and state the major expense/revenue accounts that will be published for these areas.

**Toll** - QR's maintenance and remedial program, capital works (including any proposed upgrade and new track works) and track restrictions should be separately reported on.

**Stanwell** - the accounts need to be provided on a more disaggregated basis so that the important elements of infrastructure can be clearly identified in terms of their capital value, operating costs and revenues.

**ARTC** - we recognise QR's concern that open disclosure of detailed cost information will have an adverse effect on QR's business interests as described, and accepts the approach of reference tariffs endorsed by the QCA as a reasonable compromise in providing price transparency in the market.

There was unanimous support for the preparation of a cash flow statement for below-rail services. In addition, a number of submissions considered that the cash flow statement should be presented on a disaggregated basis.

#### **Table 20: Cash flow statements**

**Queensland Government** - information contained in the cash flow statement is a valuable source of information for the QCA and should be prepared.

**Stanwell** - a cash flow statement should be prepared for each of the major elements of the infrastructure (for example Goonyella system, Moura system, Mt Isa line, North Coast line).

**FreightCorp** - Australian Accounting Standard AS 28 'Statement of Cash Flows' requires a cash flow statement to be included with all general purpose financial statements - QR must comply with Australian Accounting Statements.

**AMC** - the cash flow statement should be on a line section basis.

## ***QCA Analysis***

### *Level of disaggregation*

The reporting of appropriately aggregated financial information forms an important component of a performance monitoring system. It allows stakeholders to assess how a regulated entity is operating given the pricing constraints imposed by the regulatory regime.

The QCA shares some of the concerns of stakeholders about the proposed level of financial disclosure. In particular, the Authority recognises the desirability of balance sheet and profit and loss type information for the coal systems being disclosed to enhance the level of transparency. This enhanced transparency would allow users and potential access seekers to carry out their own assessments as to the appropriateness of access charges, including reference tariffs.

However, the Authority recognises that it is impractical to attempt to attribute liabilities such as debt and expense items such as tax and interest to individual business units in the organisation. Consequently, rather than a balance sheet and profit and loss statement, the Authority considers that QR should publish:

- a statement of assets; and
- a statement of earnings before interest and tax;

aggregated for:

- the declared services; and
- the four coal systems

on an annual basis, 6 months after the end of the financial year.

A number of submissions have indicated that stakeholders require a detailed decomposition of costs on a line section by line section basis to make transparent QR's allocation of costs. However, the QCA agrees with QR that this level of disaggregation has the potential to compromise QR's legitimate business interests and, in any event, is not necessary in order for stakeholders to have confidence in the access regime.

Cost data is unlikely to be relevant for systems where there is strong intermodal competition (that is road and/or sea transport are substitutes for rail). For these systems, transparency of pricing, especially between QR and third-party operators, is likely to be a more significant issue than cost transparency. This is because access charges for these traffics are unlikely to be cost based. Consequently, a detailed analysis of costs has little relevance for traffics which compete with intermodal providers, such as on the North Coast line.<sup>116</sup>

For the coal systems, the publication of detailed cost data is unnecessary for price assessment purposes given the transparency that will arise from the publication of reference tariffs for specified train services. In this manner, the focus of credibility and accountability in decision making will shift to the QCA. However, the Authority believes that publication of asset and profit and loss information, adjusted to reflect the fact that it pertains only to part of the organisation, provides a sufficient level of transparency to ensure the QCA is accountable for the reference tariffs it approves without compromising QR's legitimate business interests. In

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<sup>116</sup> The discussion on information to be provided to access seekers is addressed in Chapter 4.

preparing these statements, the QCA considers QR should apply the allocators set out in Chapter 12.

The Authority considers that a cash flow statement (adjusted to reflect the fact that interest, tax and dividends cannot be ascribed to a part of QR's business) at the below-rail and coal system levels, is important because it is pursuant to these cash flows that QR's overall valuation will be realised. In addition, QR appears to overlook the role that such a statement could play as far as transparency of the financial flows (costs and revenues) of its below-rail services is concerned. The cash flow information provides important additional information for assessing QR's position relative to that adopted in the valuation process for its below-rail assets. The QCA's financial model for the assessment of reference tariffs is based on cash flows. Therefore, the QCA considers that QR should provide a cash flow statement aggregated for:

- the declared services; and
- the 4 coal systems, on an annual basis,

6 months after the end of the financial year.

#### *Disclosure of asset values*

The QCA's final concern with the transparency of QR's proposed cost allocation arrangements arises where QR's asset values and depreciation rates differ between published accounts and those used for pricing purposes.

The values of assets comprising QR's rail network are unlikely to constitute a significant pricing input for the majority of below-rail services. However, asset values will be significant for any service priced with reference to stand-alone cost. The clearest example of access charges based on stand-alone cost relates to the provision of access for the transportation of coal.

In these instances, the published accounts will provide information of limited relevance to interested parties. This is because interested parties will not be able to gain assurance that access charges provide for an appropriate return on those assets without information concerning the value of the assets (and depreciation) for pricing purposes.

Accordingly, the Authority considers that for those services for which access charges are based on the stand-alone cost ceiling, asset values and depreciation should be published for relevant assets where values for pricing purposes depart from those published in financial statements.

#### ***QCA's Position***

**The QCA would favourably consider an Undertaking that:**

- **commits QR to report to the QCA within the first half of each financial year, in respect of its previous financial year:**
  - **a statement of assets, a statement of earnings before interest and tax and a cash flow statement, excluding interest, tax and dividends, aggregated for the declared services, prepared using generally accepted accounting principles and in accordance with QR's normal external reporting format; and**

- **a statement of assets, a statement of earnings before interest and tax and a cash flow statement, excluding interest, tax and dividends, aggregated for operations on the Blackwater, Goonyella, Newlands and Moura coal systems, prepared using generally accepted accounting principles and in accordance with QR's normal external reporting format; and**
- **undertakes to publish asset values and depreciation for those services for which access charges are based on the ceiling of stand-alone cost, in the instances where relevant asset values for pricing purposes depart from those published in financial statements.**

### 5.5.6 *Accountability*

#### *QR's Position*

QR argued in its submission to the QCA's Request for Comments Paper *QR's Draft Undertaking – Costing Manual*, that the role of the auditor is critical to ensuring that the principles described in the Manual are adhered to. QR has proposed that the Manual is sufficiently detailed for the purpose for which it is intended, that is, as a statement of costing principles that can be applied by an experienced professional.

QR noted that the QCA has discussed the possibility of greater provision of information to allow for such comfort and that QR is willing to provide some additional information on default allocators as part of the Manual. However, QR also considers that the provision of this comfort is one of the intrinsic purposes of the audit.

Therefore, provided that the auditor considers that the processes used by QR are effective, QR's view is that this in itself should provide sufficient reassurance to stakeholders. Likewise, should the audit be qualified, QR stated it will accept that its processes in these areas may need review.

QR also indicated that if stakeholders have concerns regarding the clarity of the auditor's role or powers, or the process for the audit, it will consider providing greater detail in the Manual.

QR noted that the QCA has raised the issue of disagreement over the choice of auditor and whether the QCA or QR should be responsible for the appointment of the auditor. QR stated it believes that the auditor should be someone reasonably acceptable to both QR and the QCA. Provided that this is the case, QR would not be overly concerned about who should appoint the auditor.

Nonetheless, QR indicated it would expect that typical practice would be for QR to arrange for the audit to be provided (including appointment of the auditor). Where agreement cannot be reached, QR would expect that the choice of the auditor would be determined by the QCA, provided that the QCA took reasonable account of QR's concerns in the appointment of the auditor.

QR indicated that the Manual already contained strong accountability measures including accounts being signed off by management, independent audit and the serious consequences of non-compliance. Therefore QR did not consider that a requirement for sign off by directors would act to further promote QR's accountability in complying with the Manual.

### ***Stakeholder Comments***

There was unanimity of view among stakeholders that QR's accountability for the Manual was inadequate.

#### **Table 21: Audit process for Manual**

**ARTC** - the audit process (meant to assess the integrity of financial systems and reporting) has not been clearly defined and would struggle to make a valid assessment of the allocative processes. Without further prescription, there would be no point in auditing compliance with the Manual.

**Stanwell** - if the audit is simply a check of QR's compliance with the costing process set down in the Manual, then this would add little value, since the costing estimates derived are likely to be very imprecise.

It is unclear from the Manual whether the auditor would simply be certifying compliance with the processes in the Manual (themselves very widely drafted), or be certifying as true and correct the values ascribed to the various cost items in the partial financial statements proposed by QR.

The QCA, as the independent regulator, should appoint the auditor, together with an independent rail expert who could assist in the audit function.

**Queensland Treasury** - the Manual may benefit from greater specificity and needs to identify the components of the audit process in order to allow for an assessment of the auditor's performance and to reduce, as far as possible, the scope for variable interpretations of the appropriate allocation or attribution of costs.

**FreightCorp** - the auditor should have a role that encompasses a review of the processes that QR uses to carry out its revenue limit and pricing functions.

The QCA should appoint the auditor and be empowered to conduct an audit at any time, rather than annually. This would facilitate the appearance of independence as well as clarify the reporting relationship for the auditor.

**Queensland Treasury** - in the event that the QCA does not agree with the auditor selected by QR, there must be a mechanism in the Undertaking for resolving such a dispute.

Submissions also commented on whether QR's Directors should certify that accounts have been prepared in accordance with the Manual.

#### **Table 22: Certification of accounts**

**Stanwell** - if the Manual was considerably more detailed, such a Directors' certification may be valuable for users.

**FreightCorp** - certification by the QR Directors would not be sufficient to replace the provision of the level of detail to stakeholders we seek.

**Queensland Treasury** - public certification would provide an accountable framework.

### ***QCA's Analysis***

The QCA accepts that the audit has a major role in establishing confidence in QR's cost allocation processes. However, to justify that confidence, the QCA considers the following matters should be considered in the context of the proposed audit arrangements:

- the scope of the audit;
- the timing of accounts prepared in accordance with the Manual;

- the certification by directors that accounts have been prepared in accordance with the Manual;
- the appointment of the auditor;
- QR's obligations in relation to the audit;
- the process in the event that the auditor issues a qualified report; and
- the frequency of audits.

#### *The scope of the audit*

Essentially, QR is suggesting the audit process carry the main burden of establishing whether QR's allocation of costs and assets is appropriate. This is in contrast to the view expressed by some stakeholders that any audit would be of limited benefit because the lack of detail contained in the Manual would mean that an unqualified report would provide interested parties with little confidence in the integrity of the allocation process.

The QCA's views on the transparency of QR's proposed arrangements are set out above – in general the Authority considers a more detailed approach to cost allocation is warranted but at this stage is reluctant to impose on QR a highly prescriptive cost allocation model. Whilst stakeholders expressed the view that an audit process could be pointless in the absence of a detailed cost allocation process, the Authority considers that to some extent they are substitutable. In other words, the Authority considers adopting a less than highly prescriptive approach to the Manual in turn requires that an auditor have an extremely wide brief to conduct a detailed investigation of the appropriateness of QR's cost allocation processes and report on its findings. Consequently, the Authority sees merit in the scope of the audit being defined in greater detail in the Undertaking itself.

Broadly, the scope of the audits could include:

- ensuring that the processes contained in the Manual have been followed;
- attesting to the fact that QR's allocation of costs and assets (as reflected in financial statements) are consistent with the Manual; and
- attesting to the reasonableness of the values contained in those statements, that is attesting to the appropriateness of the actual allocators adopted by QR.

Consequently, the scope of the audit proposed by the QCA extends well beyond that traditionally undertaken as part of audit processes. In particular, the auditor will be obliged to investigate and form its view on the appropriateness of the allocation processes undertaken by QR, and indeed, to the appropriateness of the allocators themselves. The QCA considers that this very broad role is justified in order to provide interested parties with confidence in the outcome of the process.

Accordingly, the auditor's role should extend beyond an assessment of whether the processes underpinning the allocation process have been conducted in accordance with the Manual to assess the accuracy, completeness and valuation aspects of the accounts that are thereby produced. The auditor's report should extend, if necessary, to comment on whether QR's management information systems are appropriate for the task at hand. Aspects of the process related phase of the audit process would include, for example, assessing the veracity of the surveys.

Another aspect of QR's cost allocation practices that the Authority considers should be addressed through the audit process relates to ensuring the satisfactory completion of work orders. This would extend to assessing the appropriateness of the actual values placed on the provision of services through work orders, that is, QR's determination of standard costs, such as the reasonableness of the charge for the use of work trains. In addition, it may be appropriate for the auditor to assess the standard costs used under SAP, and, where appropriate, assess such costs against available external benchmarks. In practice, the assessment of costs for the provision of services, including the standard costs applied under SAP, is likely to represent one of the auditor's most important tasks.

#### *Timing of accounts*

The QCA accepts that QR accounting process involves observing relatively strict deadlines in the months following the end of the financial year in order to meet statutory requirements. The QCA recognises that it would be inappropriate to seek to impose additional requirements on QR during this busy period. Accordingly, the QCA considers it is reasonable that QR be allowed six months following the end of the financial year to prepare its financial statements in accordance with the Manual. This period provides QR with an opportunity to ensure that its existing statutory reporting obligations are completed prior to preparing its accounts in accordance with the Manual.

#### *Certification by Directors*

Whilst QR has argued that management approval is sufficient to provide an appropriate level of endorsement, the financial statements prepared in accordance with the Manual will assume considerable significance in QR's regulatory environment.

In other jurisdictions, directors are involved in attesting to the accuracy of regulatory accounting information. For example, in NSW, at least two Directors of each electricity distribution business are required to sign a Director's Responsibility Statement. This document is attached to the regulatory accounts and affirms that the regulatory accounts and supporting schedules are fairly presented in accordance with the accounting separation code and associated regulatory information requirements (the equivalent of the Manual). Similar arrangements apply to the electricity industry in Victoria (although only a single Director is required to sign the corresponding statement).

One benefit from this process is that it compels senior management to take responsibility for ensuring that the organisation meets its reporting obligations. It highlights the importance of the information contained in the financial statements and their status amongst market participants.

The Authority notes the importance market participants will attach to having confidence in accounts being prepared in accordance with the Manual. Consequently, the Authority considers that the Chair and one Director, or the Chair and the Chief Executive, should attest to the fact that financial statements have been prepared in accordance with the Manual.

#### *The appointment of the auditor*

The QCA considers that the integrity of the audit process would be irretrievably compromised if QR were to appoint the auditor. Moreover, the auditor should be in no doubt that its client-related obligations are to the QCA. Accordingly, the Authority considers that it must appoint the auditor so that it is accountable for the competence and independence of the appointee. Nevertheless, the QCA accepts that it would be consistent with QR's legitimate business

interests that the Authority consults QR before it appoints an auditor and take account of the any views QR expresses in relation to that person's proposed appointment. As the need for the audit arises from QR's vertical integration, it is proposed that QR be required to meet this cost.<sup>117</sup>

#### *Assistance to be provided*

QR should be obliged to provide any assistance the auditor requires, particularly relating to the provision of information in a timely manner. In particular, it is important that the auditor have complete access to QR's financial and information systems.

It is important that QR commit to provide this assistance in its Undertaking within any reasonable time frame nominated by the auditor. The QCA would expect that the auditor's view on level of assistance provided by QR would form part of the audit report.

#### *Implications of a qualified audit report*

The QCA Act requires the organisation's books of account be maintained in accordance with the Manual. Non-compliance with this requirement carries significant penalties.

In the event of a qualified audit report, it is proposed that the auditor offer its view on the significance of the discrepancy, and if necessary, require that allocations be performed in accordance with the auditor's requirements. In an extreme case, it may be necessary for the auditor to provide detailed advice on how the accounts need to be amended in order for them to comply with the Manual. Indeed, it is conceivable that the auditor could form the view that action be instigated under the QCA Act in the event of serious non-compliance with the Manual.

The issue of a qualified audit report may raise serious questions concerning the integrity of QR's cost allocation. Consequently, it will be important to ensure errors are corrected quickly so that the market is informed of any discrepancy. The QCA therefore considers that QR should undertake to amend its accounts prepared under the Manual to take account of any QCA requirements that arise from a qualified audit report, in accordance with the time frames required by the Authority.

The auditor's report should be published via the QCA (although it may be appropriate to keep some aspects of the auditor's report confidential).

#### *Frequency of audit*

QR's cost allocation processes are undertaken on quarterly and annual cycles. However, the annual allocation process is significantly more thorough than those undertaken each quarter.

Some stakeholders expressed the concern an annual audit provides QR with scope to deter entry by cost shifting during the course of a year. However, the frequency of the audit process is unlikely to significantly increase QR's opportunity to engage in cost shifting activity. Indeed, the annual cycle of work within the relevant areas of QR means that audits at particular times of the year could seriously interfere with the management accounting process.

It would therefore appear highly unlikely that conducting comprehensive audits of allocations more frequently than on an annual audit would yield net benefit.

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<sup>117</sup> The QCA has acknowledged there will be a small increase in QR's compliance costs as a consequence of the regulatory arrangements.

However, there may be considerable benefit in an audit being undertaken on specific aspects of QR's cost allocation process during the course of the year. For example, as a consequence of Mr Bullock's report, the QCA may be concerned with the treatment of work orders as part of the implementation of SAP. In future years, there may be a mid year review to assess whether QR was implementing the recommendations of a previous year's audit. Such a process could avoid the adverse consequences of a qualified audit report.

Accordingly, the QCA considers it appropriate that it reserve the right to engage in an audit on other than an annual basis, although instigation of audits outside of an annual review may be rare in practice.

Finally, the Authority notes that there is a risk that the auditing arrangements will not be effective unless they are included as part of the Undertaking.

#### ***QCA's Position***

**The QCA would favourably consider an Undertaking that:**

- **defines the scope of the audit, such that the auditor examines whether:**
  - **the processes contained in the Manual have been followed; and**
  - **the financial statements represent a reasonable allocation of costs and are consistent with the Manual;**
- **contains an obligation on QR to present financial statements prepared in accordance with the Manual within 6 months of the end of the financial year;**
- **provides that these accounts would be certified by the Chair and the Chief Executive or the Chair and a Director;**
- **provides for the QCA to select the auditor to audit QR's compliance with its Manual;**
- **confirms the auditor would be provided full access to QR's information systems, with the degree of access forming part of the auditor's report to the QCA;**
- **obliges QR to provide any information the auditor requires within any reasonable timeframe nominated by the auditor;**
- **acknowledges that QR must comply with the Authority's requirements in response to a qualified audit report in accordance with the Authority's time frames; and**
- **acknowledges that an audit may be conducted at any time.**

## 5.6 Performance regime

Performance against contractual obligations will be a feature of access agreements. However, performance has wider implications because of the effect of poor performance on other users of the system and the effect of performance on the possible level of use.

### *QR's Position*

QR proposed in its submission to the QCA's Issues Paper *Queensland Rail's Draft Access Undertaking – Reference Tariffs, Reference Train Services and Rate Regulation*, that any performance regime for coal carrying services in Queensland be phased in over a reasonable period of time and be sufficiently flexible to take account of national developments with respect to performance measurement.

QR further proposed that the performance regime should ensure that operators are informed with regard to what constitutes a reasonable level of service associated with the required access and, once the access agreement has been formalised, the agreed service standard should be maintained.

QR noted that the service standard for a coal carrying service would be defined in the reference train service. Operators would thus need to be aware of the standard of service applicable to the reference tariff being charged. With respect to maintenance of service standards, QR argued that the access agreement will incorporate performance standards related to the train service and will identify the consequences for both parties of not meeting those standards. That is, they will contain a system of key performance indicators (KPIs) and associated incentives/disincentives with a view to maintaining service quality at the agreed level. Disputes during the term of the agreement will be dealt with in accordance with the dispute resolution provisions of the particular access agreement. QR concluded that the proposed contractual arrangements provide the most appropriate performance regime for the provision of rail access.

The KPIs to be included in the access agreements will focus on:

- delays in excess of those planned in the definition of the capacity entitlement due to the above and/or below-rail operator;
- availability of train paths provided for in the capacity entitlement; and
- utilisation of train paths provided for in the capacity entitlement.

QR advised that they are currently finalising the definitions of the KPI to measure these factors. It then intends to record its own performance for a reasonable period of time in order to develop benchmarks prior to the specification of the relevant performance standards. QR advised that it then intends to measure its performance for 12 months in order to assess the cost impact of varying service standards. The number of KPIs may be expanded where a need is determined.

QR expressed the view that it is not necessary to incorporate public performance reporting as part of the regulatory regime in order to provide an incentive to maintain service quality. QR believed its above-rail customers will be sufficiently well informed of performance via the chain of agreements that such information is unnecessary.

QR argued that the emphasis should be on meeting rather than exceeding agreed service standards and reiterated that a system of incentives and disincentives will be included in the access agreement to encourage the achievement of such standards. However, QR stated that these financial disincentives should at least initially not reflect the fully liquidated damages to either party of under-performance but be adequate to discourage under-performance. QR

argued that over-emphasis on a limited set of performance indicators might result in distortions as both operators and QR concentrate on achieving satisfactory levels of these performance indicators at the expense of others. QR therefore concluded that it is not appropriate to apply regulator-enforced penalties for under-performance outside of those provided for in individual access agreements to avoid inefficient behaviour on the part of QR.

In terms of whether the expected level of compensation payments by QR to operators due to QR's under-performance should be included in revenue limits and hence reference tariffs, QR proposed that reasonable costs should include an allowance for the impact of unique risk factors on its performance including the risk of it not being able to meet its contracted service standards.

### **Stakeholder Comments**

Stakeholder submissions in response to the QCA's Issue Paper *Queensland Rail's Draft Access Undertaking – Reference Tariffs, Reference Train Services and Rate Regulation*, supported the development of performance measures and identified potential service quality indicators.

#### **Table 23: Performance monitoring**

**Stanwell** - higher levels of public reporting are necessary to overcome the effects of information asymmetry in the market for below-rail infrastructure. To this end, QR should provide a detailed list of service quality indicators to assist decision making by interested parties and to facilitate the negotiation of access agreements. The range of indicators include network reliability, ease of access, accident frequency and cost, billing accuracy, response times, customer satisfaction indicators, etc. This information should be compiled by system on a monthly and year to date basis. It is also important that QR informs the QCA and all market participants of progress in managing the below-rail assets and provides the QCA with an implementation plan, including strategies, milestones and performance criteria.

**FreightCorp** - the service quality elements that could be incorporated in the regime, and publicly reported by the QCA on a monthly basis, should include length of running time for a given service, variability of running time and variability in running to scheduled time.

**ARTC** - a number of service quality elements can be identified that impact on the overall outcome of the network owner/user interface. These include service reliability, service transit times, service availability, safety, rollingstock standard and track standard.

**QMC** - reference tariffs should be predicated on minimum performance standards for QR and third-party operators to ensure that tariffs are not maintained at agreed levels while service standards are allowed to fall. Performance standards should be contained in access agreements and be supported by periodic reporting of performance outcomes and a cooperative process to ensure the efficient operation of the network.

**Queensland Government** - performance monitoring as a necessary component of incentive regulation and supports an independent audit oversighted by QCA. Public reporting of QR's performance is supported, provided that the confidentiality of individual operators is maintained. As a minimum, the service quality elements of timeliness and reliability should be measured and reported.

There was no consensus on the use of penalties to enforce compliance with performance measures.

#### **Table 24: Performance compliance**

**FreightCorp** - the performance regime should have financial incentives and penalties in order to provide the correct price signals to market participants. However, these incentives/penalties are not equivalent to compensation in magnitude or intent. In addition, increased infrastructure costs resulting from the imposition of penalties for poor performance should not be included in the cost base for pricing purposes.

**Stanwell** - penalties for service breaches along the lines being developed for the electricity industry should be introduced.

**Queensland Government** - it is not clear that poor performance should result in an indirect penalty to the disaffected party by way of subsequent price increases to cover additional risk. The passthrough of performance risk by QR to its customers would be counterproductive.

**ARTC** - appropriate incentives need to be employed to ensure poor performance against these commitments is minimised. However, such a system runs the risk of a focus on the resource-intensive allocation of blame instead of towards the improvement of service quality and superior investment decisions. Hence, performance should be measured over a period of time adequate to enable a reasonable assessment of performance against the agreed criteria before any commitment to financial arrangements are made.

### ***QCA's Analysis***

Service performance indicators allow users and potential access seekers to evaluate the cost effectiveness of the service currently being delivered and increase the accountability of QR in terms of that service delivery. The QCA believes that QR, as network manager, should be accountable for the provision of its below-rail services.

The development of a performance regime is a complex process because of the interaction between the individual delays caused by faults on the part of the network manager (Network Access) and the individual operators. It would be desirable to develop a performance regime that:

- is consistent with benchmarks developed elsewhere in Australia;
- identifies the correct (market driven) KPIs;
- is capable of use with a reporting information system QR would be able to develop; and
- pays due attention to the role of incentives of individuals responsible for reporting against performance measures, to avoid subjective data.

The QCA recognises the evolutionary nature of the performance regime and the complexity of arriving at meaningful KPIs. While there is a need to have measures in place as soon as possible, they will need to be subject to revision.

The QCA also recognises the key role played in a performance regime by access agreements and that these will reflect a negotiated outcome between QR and third-party operators. However, there is a role for a centrally determined performance regime, because of:

- the monopoly position of QR;
- the possibility of the costs of poor performance being borne by end-users not the contracting parties;
- the lack of a performance regime in the internal QR access agreements; and
- the role of public information in a performance regime.

QR has argued there is no role for public disclosure of performance against benchmarks as above-rail operators would be aware of necessary information through the working of the access agreements. However, the QCA considers there are considerable benefits to public disclosure, in terms of public confidence in the performance arrangements, particularly given the vertical integration of QR. This point was made very strongly by other stakeholders, who stated the

view that any disadvantage to themselves of public disclosure of contract details would be outweighed by the benefits.

In a Working Group meeting between QR and industry stakeholders held in April 2000, the QCA tabled a list of potential service quality indicators with a view to formulating a preliminary performance regime. This list comprised six categories as follows:

- the reliability of the service;
  - the number, and percentage, of trains that enter the network healthy,<sup>118</sup> but depart unhealthy;
  - the number, and percentage, of unhealthy trains that do not deteriorate further whilst on the network;
  - the number, and percentage, of healthy trains that leave the network early;
  - the number, and percentage, of unhealthy trains that leave the network early;
  - the average deterioration time of unhealthy trains;
  - the number, and average duration, of delays by cause such as track repairs, track construction, terminals, equipment failure, network scheduling, above-rail operator, weather and accidents; and
  - the number of complaints relating to system reliability and delays;
- the transit time of the service;
  - the number of kilometres under temporary speed restrictions, expressed as a percentage of total track kilometres;
- the availability of the service;
  - the number, and percentage, of instances in which trains have not achieved their allocated timetable or path, or a path is allocated outside the tolerance of the capacity entitlement, due to the unavailability of the allocated path;
  - the number of instances of track possession time overruns, and the percentage of total track possessions in which such possessions have been of a greater duration than foreshadowed in the daily train plan; and
  - the number of instances in which an operator has failed to be contacted about a departure from its capacity entitlements;
- a measure of track quality;
  - track quality measured by a quality index with component measures such as rail surface level, alignment, twist/cross level and gauge variation;

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<sup>118</sup> A healthy train is one that has experienced no deviation - in excess of an agreed tolerance - from the path in the daily train plan that could be attributed to QR in its role as rail manager.

- a measure of safety;
  - the number of reportable incidents, specific to each operator; and
- a measure of the accuracy of billing systems;
  - the number of complaints regarding billing accuracy.

For indicators in the categories of service reliability, transit time and availability, the QCA considered it appropriate from a regulatory perspective to separate data from coal and non-coal operations and, where applicable, disaggregate each into QR above-rail and other third-party operators. The QCA believed that the appropriate reporting frequency was monthly.

Generally, there was a favourable response from industry participants to the proposed suite of indicators. QR advised the Working Group that they would consider the list and distribute a proposal to participants shortly thereafter. The QCA emphasised the importance of this process being completed before the release of the Draft Decision. QR has since indicated that it will put its preferred position on this issue in response to the Draft Decision.

Penalties are an important feature of a performance regime. Without financial penalties, QR and third-party operators would have reduced incentives to carry out their obligations under agreements. However, the developmental nature of the KPIs makes difficult any meaningful penalty regime at the moment.

Notwithstanding the opportunity for access agreements to take any position that might be negotiated between parties, the QCA does not consider it appropriate at this stage to nominate penalties to apply to KPIs. In the QCA's view, it would be better to begin collecting appropriate data now, in order to assist the development of meaningful KPIs in the future. The QCA will revisit this issue at the end of this regulatory period.

#### *QCA's Position*

**The QCA would favourably consider an Undertaking that provides for the following key performance indicators to be disclosed publicly on a monthly basis:**

- **the number, and percentage, of trains that enter the network healthy, but depart unhealthy;**
- **the number, and percentage, of unhealthy trains that do not deteriorate further whilst on the network;**
- **the number, and percentage, of healthy trains that leave the network early;**
- **the number, and percentage, of unhealthy trains that leave the network early;**
- **the average deterioration time of unhealthy trains;**
- **the number, and average duration, of delays by source such as track repairs, track construction, terminals, equipment failure, network scheduling, above-rail operator, weather and accidents;**

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- **the number of complaints relating to system reliability and delays;**
  - **the number of kilometres under temporary speed restrictions, expressed as a percentage of total track kilometres;**
  - **the number, and percentage, of instances in which trains have not achieved their allocated timetable or path, or a path is allocated outside the tolerance of the capacity entitlement, due to the unavailability of the allocated path;**
  - **the number of instances of track possession time overruns, and the percentage of total track possessions in which such possessions have been of a greater duration than foreshadowed in the daily train plan;**
  - **the number of instances in which an operator has failed to be contacted about a departure from its capacity entitlements;**
  - **track quality measured by a quality index with component measures such as rail surface level, alignment, twist/cross level and gauge variation;**
  - **the number of reportable incidents, specific to each operator; and**
  - **the number of complaints regarding billing accuracy.**

## CHAPTER 6. CAPACITY MANAGEMENT

### KEY ASPECTS

**Transparent procedures** - QR's vertical integration raises a potential conflict in that it must allocate train paths for its own train services and those of third-party operators. To protect the integrity of the above-rail market, transparent capacity management procedures and clarification of the rights and obligations of QR and third-party operators are necessary.

**Scheduling & train control** - principles to guide the performance of the scheduling and train control functions should replace the Protocols and be incorporated as a schedule to the Undertaking.

**Capacity information** - the Undertaking should commit QR to make information available to facilitate independent capacity assessments.

**Capacity allocation** - the Undertaking should establish transparent capacity allocation procedures, in particular, for situations where two or more access seekers are either competing concurrently for the same capacity, or alternatively competing for the traffic of a particular end-user.

**Resumption** - QR's right to resume capacity should be subject to an objective test established in the Undertaking, with disputes subject to resolution by expert determination in accordance with a process to be established in the Undertaking.

**Relinquishment** - the Undertaking should allow an access seeker carrying non-coal freight and passenger traffics to relinquish its access rights, subject to QR's legitimate business interests being protected.

**Secondary trading** - the Undertaking should permit full and partial transfer of unwanted capacity rights between participants operating in the same market, subject to the establishment of adequate notification procedures between QR and capacity holders.

## 6.1 Introduction

The allocation of a rail network's capacity is achieved through the development of train schedules/timetables. A train schedule for a particular section of the rail network can be considered as a series of train paths with a time and distance dimension. Each train path has a departure, transit and arrival time between origin and destination points. The train paths reflect the priorities established in the schedule for different types of traffic. In theory, decisions with respect to priority should reflect an estimation and comparison of the flow-on effects on the train schedule of delaying each train, and the respective costs incurred as a result of the delay. The efficient allocation of capacity also requires account be taken of the railway operator's willingness to pay for priority.

The constraints on the capacity (and hence available train paths) of a rail network reflect a range of factors including:

- the condition of the track and the associated infrastructure. For example, the size and spacing of sleepers and depth of ballast under the track affect axle load and train speeds, the length of passing loops affects train length;
- the type of train services operating on the network. For example, passenger trains generally travel faster than freight trains; and
- the need to observe safeworking procedures on and around the track. For example, trains must travel at safe distances from each other.

Available capacity could be expected to vary quite significantly across different parts of QR's network. Demand for train paths on certain parts of QR's network may be relatively uniform throughout each day, for example, Goonyella and Blackwater coal systems. In contrast other parts of the network are characterised by significant variations in train path demand depending on the time of day, for example, peak and off-peak demands on the Brisbane metropolitan system. During peak times, the existing capacity of a particular system may be fully utilised.

## 6.2 Scheduling and train control framework

### *QR's Position*

QR proposes to perform the scheduling and train control functions within a framework established by four documents:

- Draft Undertaking – the overarching document that establishes the respective roles of the Protocols and the Interface Plan.
- the Protocols - QR proposes that the Protocols have two roles:
  - to allocate below-rail capacity and manage on-track traffic; and
  - to address the conflict of interest arising from its above-rail business groups performing scheduling and train control functions.
- Interface Plan - a schedule to the standard access agreement that provides information on how QR intends to manage certain aspects of the scheduling and train control functions. It will address issues such as operational procedures, emergency procedures, incident management, track possession procedures, train control contacts, train-schedule variation procedures and service recovery procedures.

- Access Plan – this is proposed to contain all the information that scheduling and train control officers need to be aware of for them to perform the scheduling, train control and associated incident management services they are contracted to supply to Network Access. An Access Plan would be prepared for each third-party operator. It assembles the following documentation:
  - the operator’s capacity entitlements;
  - a description of the nominated network;
  - the rollingstock specification and rollingstock standards;
  - safeworking procedures, safety standards, emergency procedures and environmental standards;
  - the Interface Plan; and
  - the operating plan.

The Protocols did not make it clear whether the Access Plan would be made available to third-party operators. However, QR has subsequently advised the QCA that this will be the case.

### ***Stakeholder Comments***<sup>119</sup>

Stakeholders identified concerns about the multi-document structure of the scheduling and train control framework.

#### **Table 1: Scheduling and train control framework**

**FreightCorp, Toll** - the Protocols should provide a comprehensive guide to all parties as to their rights and responsibilities, with information being in a single document.

**Toll** - the links between the Draft Undertaking, the Protocols including the Access Plan, and the Interface Plan, are not sufficiently clear, and this lack of clarity is a potentially serious safety issue. It is not clear what will be incorporated in the Access Plan that would not be in the Protocols and the Interface Plan. However, it is essential that all access protocols be set out in the Protocols and that any other secondary plans be entirely consistent with the Protocols. The proposed system, which relies on three layers of plans, appears unnecessary, bureaucratic and is likely to cause confusion.

**FreightCorp** - anything that is common to all parties should be included in the Protocols and any issues specific to a particular operator or group of operators should be contained in the Interface Plan. This would ensure a common approach is used and would reduce the time required to negotiate the arrangements between Network Access and each rail operator. In addition, some of the issues contained within the Interface Plan should also be canvassed in the Protocols.

**FreightCorp, QMC** - the general references to consultation, for instance in the allocation of capacity and the sharing of information, need to be developed into clear procedures.

**QMC** - the Protocols are inadequate, and fail to ensure the transparency and accountability essential for effective, dispute-free train control. The scheduling and train control function provides several opportunities for discriminatory treatment of train operators. The Protocols will need to impose clear obligations on Network Access as to the even-handed treatment of operators

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<sup>119</sup> The QCA released a Requests for Comments Paper *QR’s Scheduling and Train Control Protocols and Proposed Assignment of Marshalling Yards* in February 2000 inviting submissions from interested parties concerning the appropriateness of the Protocols. The following stakeholder comments are in response to that paper.

and to describe in reasonable detail the procedures through which these obligations will be discharged.

Procedures should be formulated to resolve disputes in relation to:

- train priority (in real time); and
- train path disruptions and operator complaints.

**FreightCorp** - the language of QR's Interface Plan is typical of the language of QR's other access documents in that it is:

- highly prescriptive of the third-party operator's obligations;
- vague or silent about QR's obligations;
- designed to favour the incumbent; and
- generally anti-competitive in approach.

The term 'Access Plan' does not appear in the Undertaking at all. Concerns with the document include:

- it is an internal QR document, with no expectation of any consultation with the third-party operator or review of the final document;
- the restatement of the Protocols in a separate document can lead to variation from the agreed Protocols resulting from mistranslation and misinterpretation;
- QR does not intend to provide the Access Plan to third-party operators. The fact that QR train controllers will have the Access Plan but not the third-party operator also has the potential to make communication between the two parties difficult; and
- conflicts may arise between the documents. The Undertaking is silent on any conflict between the Access Plan, the Protocols and the Interface Plan.

### *QCA's Analysis*

The scheduling and train control framework is critical in establishing a consistent basis upon which to manage traffic and subsequently is a significant influence on the daily performance and efficiency of rail operators. The integrity of its processes are therefore essential in maintaining third-party operators' confidence in the above-rail market which has been historically dominated by an integrated rail service provider.

The performance of scheduling and train control functions is a continuous process in the sense that high-level capacity entitlements must be translated and interpreted into scheduled train paths able to be acted upon instantaneously by train controllers. It is essential, therefore, that the decision-making process is consistent, both in formulation and application. Transparency is also critical to providing all rail operators with confidence in the scheduling and train control procedures.

In principle, the consistency of application at the planning and implementation stages would be enhanced by these functions being performed in one single organisational unit. While QR has proposed that short-term scheduling and train control activity will be undertaken by various above-rail business groups, the QCA considers that the scheduling and train control functions should be performed at the below-rail level only, that is by Network Access.<sup>120</sup> This arrangement alleviates the perception of potential conflicts of interest that would face QR above-rail business groups if they were to deliver train control services to third-party operators. Nonetheless, there still remains a crucial need to increase the degree of transparency in QR's scheduling and train control framework.

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<sup>120</sup> This issue was discussed in Chapter 3.

At the operational level, QR's proposed scheduling and train control framework lacks clarity. As the overarching document, the Draft Undertaking should establish the roles of the Protocols and the Interface Plan. However, no direct relationship between the two is established, notwithstanding some apparent overlap in the matters each is proposed to address. Moreover, the Access Plan is not referred to in the Draft Undertaking.

While QR has advised the QCA that the Access Plan will not contain anything that is not already in the Interface Plan or the Protocols, stakeholders have expressed concern that the content of the document lacks transparency. The QCA supports QR's decision to make the Access Plan available to third-party operators and believes that this would provide confidence in the integrity of the access regime and ensure that train controllers and operators have a common operational frame of reference. The QCA considers that such confidence in transparency would be consolidated if QR, as part of its Undertaking, agreed to provide third-party operators with any document that train controllers are given to assist in the performance of their duties.

It appears that the only guidance that train schedulers will be given in making the allocation of paths is that specified in each rail operator's Access Plan. However, the definition of this plan does not clarify the obligations of these officers, nor does it provide a means of assessing their performance and conduct. This situation is unlikely to provide reassurance to third-party operators that train path allocations are being made in a competitively neutral manner.

The QCA believes that a streamlined scheduling and train control framework would likely allay many stakeholder concerns. Currently, the Protocols outline the general framework of the scheduling and control functions specifying, at a high level, primarily procedural matters. The Interface Plan compliments the Protocols by providing a greater level of detail as to the implementation of these processes.

A superior approach would be to specify principles for the scheduling and train control functions in the Undertaking. The separation of principles from procedural matters in the framework documentation should alleviate stakeholder concerns by providing increased transparency and greater certainty in respect of scheduling and train control outcomes.

Consequently, the QCA considers that the Protocols should be replaced by a set of broad Network Management Principles for each phase in the scheduling and train control process. These principles are discussed in sections 6.2 and 6.3 of this chapter.

#### ***QCA's Position***

**The QCA would favourably consider an Undertaking that:**

- **included a clause that required QR to provide a third-party operator with any document that train controllers are supplied with to assist in the performance of their duties; and**
- **removed references to the Protocols.**

### **6.3 Train scheduling practice**

QR's intentions regarding the performance of the scheduling function have evolved since lodgement of its Draft Undertaking, which provided that QR would develop the Protocols within three months of the commencement of an approved Undertaking. However, following

discussions with the QCA, QR provided a draft of the Protocols to the Authority in December 1999.

### ***QR's Position***

#### *The Draft Undertaking*

The capacity entitlements of a third-party operator are to be defined in terms of the number of train services that can be operated in a given time period subject to constraints agreed with the third-party operator. These constraints may include:

- a specified origin and/or destination time;
- minimum and maximum time periods between train services;
- average travel time and acceptable variations to travel time;
- regularity of timetable reviews and the applicable review process; and
- allowable modifications of timetable, such as service cancellations or deferrals: para 6.1(a).

As part of the negotiation process, QR will develop an initial specification of the third-party operator's capacity entitlement. This will be subsequently refined by both parties during the negotiation process and be incorporated into the access agreement: para 6.1(b). The capacity entitlement will be then used to develop an initial timetable, which QR and the third-party operator will be required to adhere to unless and/or until such time as the timetable is varied in accordance with the operator's capacity entitlement and the Protocols: para 6.1(c).

QR will manage the development of the timetables to optimise the use of rail infrastructure as circumstances change, subject to third-party operators' capacity entitlements and the Protocols: para 6.1(d).

#### *Scheduling and Train Control Protocols*

The key elements of the Protocols were as follows.

Network Access would prepare a series of master train plans for each of the fourteen systems on QR's network, to be updated as required, detailing:

- the maximum capacity of the network, based on a train service with the characteristics of the predominant train service operating on the relevant infrastructure;
- the contracted capacity entitlements of operators using or planning to use the relevant infrastructure from week to week, including train service paths, pathing determination and railway operator-specific requirements;
- maintenance windows/possessions; and
- the available capacity of the network.<sup>121</sup>

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<sup>121</sup> The difference between maximum capacity and capacity entitlements.

The Group General Manager, Network Access, would allocate train paths in the master train plan in accordance with the capacity entitlements of all railway operators on the network and could accommodate new and/or additional traffic on the network or agreed variations to capacity entitlements of existing railway operators, provided the contracted capacity entitlements of other existing railway operators were preserved. In allocating train paths, the Group General Manager would seek outcomes that:

- address the requirements of railway operators and the infrastructure maintenance provider;
- achieve the efficient utilisation of network capacity; and
- optimise the sharing of capacity on the network and encourage co-operation between railway operators, and between railway operators and Network Access, to improve overall service, and provide overall service patterns and connections that meet the needs of users.

The master train plan could be translated into the daily train plan in accordance with:

- variations in the day-to-day business requirements of railway operators in accordance with the terms of their Access Plans;
- infrastructure maintenance and enhancement works on the network; and
- any other planned or unplanned events, such as industrial action, force majeure events or incidents, that may lead to a need to deviate from the master train plan.

The scheduling and train control officers from the relevant above-rail business groups will implement the requirements of the master train plan through the daily train plan on a day-to-day basis in accordance with the relevant Access Plans, QR's safety management system and other pre-determined procedures.

#### *Changes in scheduling practice since lodgement of Draft Undertaking*

In its submission in response to QCA's Requests for Comments Paper *QR's Scheduling and Train Control Protocols and Proposed Assignment of Marshalling Yards*, QR foreshadowed two significant changes to the performance of the scheduling function:

- the establishment of a Network Planning Centre; and
- the formation of a master train plan working group.

The Network Planning Centre would be the vehicle through which Network Access could assess its ability to provide capacity in response to access requests, and schedule train services and infrastructure possessions onto the master train plan. The Network Planning Centre is envisaged to fulfil the following responsibilities:

- capacity determination and capacity management of the network managed by Network Access;
- development of the master train plan in accordance with operator requirements expressed in access agreements;
- planning track closures and possessions in accordance with the requirements of QR's network maintenance plan and network development plan;

- assessment of capacity and operational requirements for the processing of access requests;
- in conjunction with operators, development and maintenance of operating plans;
- development and implementation of measures to assess the performance of the master train plan; and
- management of legislative and contractual compliance.

Changes to the master train plan will be developed through the establishment of a master train plan working group. This group is to be comprised of representatives from Network Access, railway operators and infrastructure service providers. The purpose of the forum is to ensure that, so far as possible, all parties interacting on QR's below-rail infrastructure are aware of the dynamics of their interactions so that the system as a whole can be managed in the most efficient way.

### **Stakeholder Comments<sup>122</sup>**

Stakeholders considered the guiding principles for the allocation of train paths and sharing of capacity on QR's network were not sufficiently transparent.

#### **Table 2: Allocation of train paths by QR**

**FreightCorp** - QR has not apparently specified any mechanism for the allocation of capacity entitlements to train operators. There is a problem in accommodating 'capacity entitlements' on the one hand and specific train paths on the other. Mineral trains will, over time, be discriminated against in favour of passenger and general freight trains. The lack of a consultative framework for the allocation of paths is inappropriate. Relying on a definition of capacity entitlement within the access agreement is likely to lead to an inflexible outcome that may work against the efficient utilisation of the network.

The use of a master timetable has limited relevance to the majority of QR's trains, that is, the coal and grain trains. Such trains cannot be specifically nominated in the same way that passenger or freight services can. Unfortunately, QR does not seem to address this fundamental fact in its discussion of the allocation of paths.

**Stanwell** - the Access Plan does not clarify the obligations of the rail controller to ensure that train path allocations are determined in a competitively neutral manner. While granting access rights on a 'first come, first served basis' has the appeal of administrative simplicity, it may result in a major barrier to entry. For the objectives of efficient utilisation and optimisation of capacity to be meaningful, it must be in reference to international rail industry best-practice standards.

**Toll** - the Protocols lack sufficient clarity as to how the objectives of efficient utilisation and optimisation of capacity will be achieved.

**FreightCorp, Toll** - defining the capacity of the network in terms of the predominant train service operating favours the incumbent's train services, stifles innovation and ignores the fact that the predominant service may change over time, leading to a need to reassess capacity.

Stakeholder submissions proposed ways of improving the visibility of the process QR uses to allocate capacity.

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<sup>122</sup> The following comments are in response to the QCA's Requests for Comments Paper *QR's Scheduling and Train Control Protocols and Proposed Assignment of Marshalling Yards*.

**Table 3: Train path allocation process**

**FreightCorp** - a minimum detailed process should be articulated within the Protocols that specifies how network capacity is to be measured and allocated. This would include the re-allocation of capacity over time and ensuring that operators and potential operators are not constrained from competing by 'grandfather rights' allocated to other operators. The capacity transfer mechanism in cl 6.4 of the Draft Undertaking is inadequate. Given the complexity of calculating capacity, a more practical approach is to provide a series of criteria by which trains are to be allocated as a framework within which the group of all operators and infrastructure maintainers can articulate their requirements.

**Toll** - it would be difficult to state the guiding principles definitively as Network Access will have to remain flexible to the changing needs of the marketplace. However, in determining capacity, Network Access should act impartially as between all operators, having regard to contracted capacity, and the process should be entirely transparent to all operators. The train plans should be available to all operators as this is essential for proper and efficient management of trains by operators.

Stakeholders expressed concerns with respect to the lack of consultation in the development of, and changes to, the master and daily train plans.

**Table 4: Master and daily train plans**

**FreightCorp** - QR provides no reasons as to why the master and daily train plans should not be made available to operators and access seekers and there also appears to be no process for the recognition of variations in the requirements of downstream customers. In addition, there appears to be no requirement for QR to consult regarding both master and daily train plan modifications. A requirement for QR to consult regarding both the master and daily train plans needs to be included in the Protocols as a third-party operator would expect to have significant input into these processes.

**ARTC** - there does not appear to be anything specifically detailed in the Protocols which prevent or give any assurance to third parties that, in making deviations to the master train plan contemplated by the daily train plan, reflecting unplanned maintenance and other events, scheduling and train control officers will not put the needs of QR business groups ahead of those of third-party operators.

In developing and amending our master train plan, operators are generally involved to the extent that we can obtain and incorporate their specific requirements. We then decide how to best optimise the performance of the network. To maintain confidentiality, operators generally do not play a role in the development or amendment of the master train plan. Similarly, if Network Access is responsible for the development of the master train plan, then it should have sufficient expertise available to it to be able to optimise the performance of the railway network with only limited input from the operators and without giving rise to any situation where confidentiality is questionable. Therefore the consultation process needs to be specified in greater detail, specifically with regard to any confidentiality requirements.

**Stanwell** - a pragmatic rather than a legalistic approach should be adopted. The full working timetable, including a timetable protocol and master timetable, should be available to all above-rail operators. The provision of the maximum possible amount of information equally to all rail operators will facilitate the achievement of the principles of fairness, transparency and accountability. There are no aspects of the master and daily train plans that are confidential.

***QCA's Analysis******Capacity entitlements and train paths***

The QCA believes that the process of converting a capacity entitlement into a specific train path on a timetable was not adequately addressed in the Draft Undertaking or the Protocols. This lack of clarity provides QR with significant discretion in allocating train paths. The QCA recognises that QR, as network manager, should have the final say in the allocation of train paths. However, there is a need to recognise and protect the rights of third-party operators in this allocation process. The possibility of arbitrary changes to agreed schedules can have a

considerable impact on the quality of service that a third-party operator can offer its customers. The greater the perception of arbitrary changes to schedules, the less confidence third-party operators will have to enter the above-rail market.

The QCA envisages the process of allocating train paths would commence with details of scheduling and train control being initially quantified in the capacity entitlements negotiated between a rail operator and Network Access. The entitlements will reflect the importance placed on the train service by the operator. In some instances, the operator would be seeking definitive departure and arrival times according to a published timetable. In other cases, the operator would be concerned with the order in which its train arrives at the destination and the total cycle time from origin to destination, back to origin and the allowable gap before the next cycle.

The master train plan should convert all capacity entitlements, as well as the requirements of Network Access, into a format that could be interpreted by all rail operators so that they could understand how their service fits into the overall system. The master train plan would take the form of charts that show diagrammatically how the train services fit into the available capacity of the system. Explanatory notes would supplement the charts, for example, explaining tolerances around capacity entitlements. The master train plan would indicate all of the train services to be operated for a lengthy period, say 6 months to a year into the future.

The daily train plan would be formulated weekly, showing diagrammatically how the permanent trains on the master train plan would actually operate on a given day. The daily train plan would therefore be a detailed subset of the master train plan with the addition of any other trains run on an ad-hoc basis.

The actual train control decision-making would be made on the basis of the daily train plan, any conditions associated with an operator's capacity entitlement, as well as in response to the instantaneous events occurring on the day of operation.

Finally, in order for rail operators to understand whether the system was operating according to contractual obligations, the actual performance of the trains would be monitored and subsequently reported to all rail operators using relevant parts of the network. Refinements could then be made to the plans to ensure the system is predictable.

### *Scheduling principles*

A strong theme to emerge in stakeholder comments regarding the Protocols was its failure to establish a satisfactory consultative framework with respect to the allocation of train paths, including the development of, and changes to, the master train plan and the daily train plan. QR has subsequently improved the consultation arrangements by proposing the establishment of a Network Planning Centre and a master train plan working group. The QCA supports these developments.

Nevertheless the QCA believes that to fully protect third-party operators' legitimate business interests, the Draft Undertaking should incorporate Scheduling Principles to guide the conversion of a third-party operator's capacity entitlement into specific train paths on a daily train plan. These Scheduling Principles, along with the associated train control principles discussed in section 6.3 of this chapter, would form a set of Network Management Principles and replace the Protocols.

The Scheduling Principles would guide the performance of the scheduling function by QR and comprise principles for each of capacity entitlements, the master train plan and the daily train plan.

As the capacity entitlement must represent, for contractual purposes, the entitlement to the service being provided by Network Access to the operator, it is in effect the specification of the entitlement to the infrastructure. The QCA endorses QR's flexible definition of a capacity entitlement, provided in the Draft Undertaking, allowing the differing requirements of various railway operators to be met. However the Authority considers that it should be augmented by the following capacity entitlement principles:

- (a) All railway operators' capacity entitlements will use consistent terminology incorporated in a single glossary.
- (b) Capacity entitlements will be expressed in terms that can be interpreted for the development of a master train plan and a daily train plan.
- (c) Where objectives of either party cannot be met, the parties could, in accepting the capacity entitlements, document the areas where the objectives are not being met with a view to modifying the capacity entitlements at another opportunity.

The master train plan expresses the objectives sought by the railway operator and Network Access in the capacity entitlements and access agreement. It is a document common to all railway operators, expressing the train services over a longer term planning horizon. The master train plan principles, which outline its characteristics and means of formulation, comprise the following:

- (a) The master train plan will need to define all of the railway operators' capacity entitlements and Network Access' requirements in a form that indicates the time/distance (location) relationship of the train services.
- (b) The master train plan will consist of a graphical representation as well as any explanatory notes to indicate any relevant conditions of service, for example, explanations of underlying capacity entitlements.

The master train plan may be modified:

- (a) from time to time according to new capacity entitlements, changes to existing capacity entitlements, or their underlying objectives, and any actual train data;
- (b) at any time following a request by an railway operator to make such a change on terms established by their capacity entitlements;
- (c) where actual train running indicates a consistent variation to that planned of greater than 10%; and
- (d) following a review by railway operators at least every 3 months.
- (e) Network Access will invite all railway operators to contribute to the modification of the master train plan. Each operator will be provided with a copy of any proposed changes 48 hours prior to a meeting between all parties. An operator will have the power of veto over changes to the master train plan if their capacity entitlements can no longer be satisfied.
- (f) The master train plan will be in a form that is readily convertible to a daily train plan, which is the principal reference document to be used by the train controllers in carrying out their duties.

The daily train plan will express the daily train operation requirements in accordance with the capacity entitlements and master train plan taking into account the daily requirements of railway

operators and Network Access. It is a document common to all the affected operators, expressing the train services over a short-term planning horizon. The daily train plan principles, which outline its characteristics and means of formulation, comprise the following:

- (a) The daily train plan will express the relevant railway operator's capacity entitlements and Network Access' requirements in a form that indicates the time/distance (location) relationship of the train services. It will reflect the information contained in the master train plan.
- (b) The daily train plan will consist of a graphical representation as well as any explanatory notes to indicate any relevant conditions of service.
- (c) Network Access will invite all railway operators to contribute to the formulation of the daily train plan. This will normally occur each week, for the coming week or fortnight. Unless otherwise agreed by all parties, Network Access will make available a draft on its understanding of operators' requirements 24 hours before a weekly meeting of all parties to finalise the plan.
- (d) The daily train plan may be modified:
  - (i) periodically during the course of its currency, in accordance with the railway operators' capacity entitlements or Network Access' needs;
  - (ii) at any time following a request by a railway operator to make such a change on terms established by their capacity entitlements; and
  - (iii) where actual train running indicates a consistent variation to that established in the access agreement and formulated in the daily train plan.
- (e) Network Access will invite all railway operators to contribute to the modification of the daily train plan. Each operator will be provided with a copy of any proposed changes.
- (f) The daily train plan will be the principal reference document from which train controllers will carry out their normal duties of train routing and dispatch, as well as incident management where trains run differently from their expected paths.
- (g) The daily train plan will express the expected train operation performance target over its period and will be used as the base information for the means of performance monitoring in reference to the underlying capacity entitlements.
- (h) Modifications to the daily train plan may occur during the course of its duration in the event of out-of-course running. Those modifications will occur according to the train control principles.

The QCA believes that the key benefit of the Scheduling Principles compared to the Protocols is that they establish an overarching scheduling framework that clarifies the roles and responsibilities of Network Access and third-party operators. In addition, they define transparent processes for the development of, and the making of changes to, the master train plan and the daily train plan.

***QCA's Position***

The QCA would favourably consider an Undertaking that:

- amended clause 6.1 of the Draft Undertaking to commit QR to perform the scheduling function in accordance with the Scheduling Principles; and
- incorporated the following Scheduling Principles as a schedule to the Undertaking:

**Capacity Entitlement Principles**

- (a) All railway operators' capacity entitlements will use consistent terminology incorporated in a single glossary.
- (b) Capacity entitlements will be expressed in terms that can be interpreted for the development of a master train plan and a daily train plan.
- (c) Where objectives of either party cannot be met, the parties could, in accepting the capacity entitlement, document the areas where the objectives are not being met with a view to modifying the capacity entitlement at another opportunity.

**Master Train Plan Principles**

- (a) The master train plan will need to define all of the railway operators' capacity entitlements and Network Access' requirements in a form that indicates the time/distance (location) relationship of the train services.
- (b) The master train plan will consist of a graphical representation as well as any explanatory notes to indicate any relevant conditions of service (eg. explanations of underlying capacity entitlements).
- (c) The master train plan may be modified:
  - (i) From time to time according to new capacity entitlements, changes to existing capacity entitlements, or their underlying objectives, and any actual train data. In any event, stakeholders will review the master train plan at least every 3 months.
  - (ii) At any time following a request by an railway operator to make such a change on terms established by their capacity entitlement.
  - (iii) Where actual train running indicates a consistent variation of greater than 10%.

- (iv) Following a review by railway operators at least every 3 months.**
- (d) Network Access will invite all railway operators to contribute to the modification of the master train plan. Each operator will be provided with a copy of any proposed changes 48 hours prior to a meeting between all parties. An operator will have the power of veto over changes to the master train plan if its capacity entitlement can no longer be satisfied.**
- (e) The master train plan will be in a form that is readily convertible to a daily train plan, which is the principal reference document to be used by the train controllers in carrying out their duties.**

#### **Daily Train Plan Principles**

- (a) The daily train plan will express the relevant railway operator's capacity entitlement and Network Access' requirements in a form that indicates the time/distance (location) relationship of the train services. It will reflect the information contained in the master train plan.**
- (b) The daily train plan will consist of a graphical representation as well as any explanatory notes to indicate any relevant conditions of service.**
- (c) Network Access will invite all railway operators to contribute to the formulation of the daily train plan. This will normally occur each week, for the coming week or fortnight. Unless otherwise agreed by all parties, Network Access will make available a draft of its understanding of operators' requirements 24 hours before a weekly meeting of all parties to finalise the plan.**
- (d) The daily train plan may be modified:**
  - (i) Periodically during the course of its currency, in accordance with the railway operators' capacity entitlements or Network Access' needs.**
  - (ii) At any time following a request by a railway operator to make such a change on terms established by its capacity entitlement.**
  - (iii) Where actual train running indicates a consistent variation to that established in the access agreement and formulated in the daily train plan.**
- (e) Network Access will invite all railway operators to contribute to the modification of the daily train plan. Each operator will be provided with a copy of any proposed changes.**

- (f) **The daily train plan will be the principal reference document from which train controllers will carry out their normal duties of train routing and dispatch, as well as incident management where trains run differently from their expected paths.**
- (g) **The daily train plan will express the expected train operation performance target over its period and will be used as the base information for the performance monitoring in reference to the underlying capacity entitlement.**
- (h) **Modifications to the daily train plan may occur during the course of its duration in the event of out-of-course running. Those modifications will occur according to the train control principles.**

#### 6.4 Train priority

QR's intentions regarding the performance of the train control function have also evolved since lodgement of its Draft Undertaking. Following the development of the Protocols, and the receipt of submissions to the QCA's Requests for Comments Paper *QR's Scheduling and Train Control Protocols and Proposed Assignment of Marshalling Yards* in February 2000, QR prepared a document Principles for the Performance of Train Control (Train Control Principles). This document outlined a set of over-riding management principles to guide the train control function.

QR revised the Train Control Principles following discussions with the QCA and stakeholders. It was agreed that they would replace the train control clauses in the Protocols and form a schedule to the Undertaking.

##### ***QR's Position***

##### *Scheduling and Train Control Protocols*

Section 4.2 of the Protocols states that the fundamental objective of train control will be to achieve on-time running for all trains and on-time commencement and closure of track possessions. This objective will be considered in the context of different types of traffic on the network as follows:

<b>Traffic</b>	<b>Critical objective</b>
Passenger.	To arrive and depart from all stops in accordance with a published timetable.
Freight and livestock.	To achieve scheduled network entry and exit times, and to arrive and depart from any other service delivery locations as scheduled.
Coal and bulk commodities, including coal, sugar, minerals, fuel, grain, sugar, acid and fertiliser.	To achieve their contracted capacity entitlements in terms of an overall number of scheduled trains within a nominated period.
Construction and infrastructure.	To perform planned tasks as scheduled.

QR has made assumptions about the critical objectives held by the various forms of traffic types. These critical objectives will be considered in the context of the overall fundamental objective in ascertaining priority on the network in the event of out-of-course running.

The decision-making process for resolving conflicts in the event of out-of-course running will be managed in accordance with the following Traffic Management Decision-Making Matrix (the Matrix).

		Train A – Current Status			
		Train A Objective	Train Running “On Time”	Train Running “Ahead”	Train Running “Late”
Train B – Current Status	Train B Objective	On Time Exit	Scheduled Cross	A or B Rule 2	B Rule 3
	Train Running “On Time”	On Time Exit	A or B Rule 2	A or B Rule 2	B Rule 3
	Train Running “Ahead”	Lose no more time Make up time Hold the gain	A Rule 1	A Rule 1	A or B Rule 4

- Rule 1. Train B may be given priority on condition Train A will still meet its ‘On Time’ objective or as otherwise provided for in Note 5.
- Rule 2. Both trains must meet their ‘On Time’ objective.
- Rule 3. Train A may be given priority on condition Train B will still meet its ‘On Time’ objective or as otherwise provided for in Note 5 (see below).
- Rule 4. Give priority to the train where performance indicates it will lose least or no more time and even make up time and hold the gain.

The Matrix is to be used in accordance with the following series of notes:

- (a) Train A and Train B are competing for the right to go first in relation to a traffic management decision by the train control, for example, network entry, a cross or pass with another train in single line territory;
- (b) The controller compares the current “status” or performance of both trains in terms of running ‘on time’ ‘ahead’ or ‘late’;
- (c) The decision is given to the train and the rule that has been applied indicated at the point of intersection;

- (d) Passengers may be given priority over other trains in contravention of the Matrix rules if specified in the relevant Access Plans; and
- (e) A train running ‘on time’ may be delayed and preference given to the train running ‘late’ if it is reasonably expected that the consequences of such action will be less aggregated consequential delays to other trains than otherwise would be the case, provided the second train is running “late” due to no fault of that train operator.

QR stated that the identity of a railway operator will, of itself, play no part in a decision to alter that railway operator’s train schedule.

If an incident occurs, the scheduling and train control officers will implement the incident management practices provided in each railway operator’s Access Plan. In addition, the Protocols provide that the scheduling and train control officers may deviate from a railway operator’s capacity entitlement in the event of an incident. In such circumstances, the following procedures will apply:

- the identity of a railway operator will, of itself, play no part in a decision to deviate from a railway operator’s contracted capacity entitlement in the event of an incident;
- the General Manager of each of QR’s above-rail business groups - Coal and Mainline Freight, Metropolitan & Regional Services, Citytrain - may authorise the departure from, or suspension of, the Protocols relating to the resolution of conflicts arising from out-of-course running for the purpose of restoring normal operations after the occurrence of an incident. Such an authorisation may be granted on a case-by-case basis after consideration of all relevant facts and, where possible, consultation with affected railway operators; and
- train services should return to normal and the relevant Protocols for resolving conflicts that arise from out-of-course running should apply as soon as reasonably possible after an incident.

Network Access must be informed of every instance where a departure or suspension of the Protocols occurs.

#### *Train Control Principles*

QR has subsequently proposed the following principles as a schedule to its Undertaking.

The fundamental objective of train control will be to facilitate the running of train services and the commencement and closures of track possessions as scheduled in the daily train plan.

The following general principles apply to train operations and train control:

- (a) all parties will ensure that operational safety is maintained through compliance with safeworking rules, safety management systems, applicable safety risk management and rollingstock interface requirements and environmental management systems;
- (b) railway operators will ensure operating integrity, including train crewing, locomotives, wagons and loading so that the daily train plan can be met;
- (c) QR will manage the network on behalf of railway operators based on agreed entry/exit times as specified in the daily train plan with the objectives of managing trains according to their schedule for on-time exit, not contributing to late running and, if a train is running late, making up time and holding the gain where reasonably possible; and

- (d) all things being equal, the primary objective is to keep trains healthy.

Out-of-course running is dependent on the particular circumstances of a rail corridor, including the traffic-type using the corridor. In the event of out-of-course running:

- (a) except as provided in a railway operator’s access agreement, train control will adhere to the contracted capacity entitlement of each railway operator, expressed in terms of the daily train plan;
- (b) where train control fails to adhere to a railway operator’s contracted capacity entitlement, the terms of that operator’s access agreement will govern the consequences;
- (c) the identity of a railway operator will, of itself, play no part in a decision by train control to alter that operator’s scheduled train service; and
- (d) train control will resolve conflicts that arise with reference to the following critical objectives of the different traffic types operating on the network:
- passenger – to arrive and depart from all stops in accordance with a published timetable;
  - livestock and freight – to achieve scheduled network entry and exit times and to arrive and depart from any other service delivery locations as scheduled; and
  - coal and bulk commodities – to achieve cycle times (incorporating in-line running to key, common destinations) that enable them to run a specified number of train services within a nominated period of time as provided in their capacity entitlement, having regard to external factors affecting throughput such as loading and unloading limitations.
- (e) The Matrix will be provided to train control to assist train controllers in the resolution of disputes in accordance with the above principles.
- (f) QR will provide operators with real time train control information and copies of train control diagrams to assist operators understand how train control decisions are made.

### ***Stakeholder Comments***<sup>123</sup>

Stakeholders generally felt that rail operators should be given the opportunity to influence the level of service priority.

#### **Table 5: Train service priority**

**FreightCorp** - while according priority to passengers and livestock is normal, the access charging mechanism needs to take into account the cost of providing priority.

**Stanwell, QT** - rail operators should have the ability to negotiate differing levels of train priority on QR’s network. It would be normal to expect that higher levels of priority would come at a higher cost and vice versa. Third-party operators should have the flexibility to negotiate with QR for both short and long-term arrangements for different priority levels, enabling third-party operators to offer rail customers tailored services, which could include one-off high priority services to better meet customer requirements.

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<sup>123</sup> The following comments are in response to the QCA’s Requests for Comments Paper *QR’s Scheduling and Train Control Protocols and Proposed Assignment of Marshalling Yards*.

**Toll** - the system adopted by ARTC for managing train priority is appropriate. Allowing passenger traffic priority is the norm, even though this traffic is not expected to pay for the privilege.

There was little support for the Matrix as a process of managing the resolution of conflicts in the event of out-of-course running.

#### **Table 6: The Matrix**

**FreightCorp** - the Matrix fails to provide a definitive guide to matters such as priority. For example, it gives priority to passenger trains if this is included in a railway operator's Access Plan. The Matrix should acknowledge additional factors, in that it currently fails to provide for the requirements and complexities of entry/exit point infrastructure such as loading and unloading equipment. The Protocols should be extended to incorporate the rules for the presentation of trains to such facilities, and to allow for downstream customer preferences to be taken into consideration.

**ARTC** - the nature of the industry is such that QR's stated aim of 'achieving on-time running for all trains and on-time commencement and closure of track possessions' is unachievable. Delays occur to trains resulting from the failure (or less than optimal performance) of above-rail assets, as well as the condition (and failure) of below-rail assets. The issue is how does the access provider best balance the needs of all market participants. Given the competitive nature of the industry, it is important to a rail operator that, if it has not contributed to any late running of its service, then the service should achieve on-time exit, regardless of the impact on other operators' services where those operators have contributed to late running. In other words, there is an expectation that the access provider would not cause any interference to the running of the former service, unless the exit objectives were still achieved. Consequently, the objective of train control must focus on its obligations to respective operators, and consider only performance over which train control has control.

**Toll** - the rules governing priority of passenger trains must be transparent and available to all operators, not buried in individual Access Plans. The only ground for delaying a train running 'on-time' should be genuine safety issues. On-time running is the deliverable by a track owner, and is what the operator pays for through its track access agreement. The Matrix gives train control complete discretion over network performance based on its perception of 'aggregated consequential delays'. This concept is a throwback to superseded practices and is not in tune with the requirements of today's marketplace or the practice of other track owners. It does nothing to encourage rail operators to maintain on-time performance. The concept of 'aggregated consequential delays' is so vague that rail operators adversely affected by a judgement based on this principle are unlikely to be able to challenge it.

A number of stakeholders believed that Protocols should never be suspended. Other stakeholders considered that there needed to be clear circumstances in which the Protocols would be suspended and a transparent procedure for the restoration of normal operations. There was no agreement about the appropriateness of an officer from one of QR's above-rail business groups having the authority to suspend the Protocols.

#### **Table 7: The Protocols**

**Toll** - the Protocols should include and govern the process for dealing with incidents to provide certainty and consistency to all rail operators and train controllers. The proposition that a QR above-rail business group has the power to suspend the Protocols is dangerous, considering that the safety and integrity of the network demands a centralised, consistent and coordinated approach managed by the track owner. QR's proposal has the real potential to produce a chaotic and unsafe system. Only Network Access should have the power to suspend the Protocols.

**ARTC** - the Protocols define the terms 'incident' and 'out-of-course running' separately and contemplate two different resultant courses of action. The Matrix could handle any out-of-course running situation regardless of the cause.

**FreightCorp** – suspension of the Protocols should not be done on a trivial basis and the Protocols should identify the circumstances and any remedies required to ensure fair outcomes. Procedures for restoring normal operations should be incorporated, including:

- consideration of safety and environmental issues;
- consultation with network users affected;
- consideration of the competing commercial imperatives; and
- consideration of the most expedient method of restoring normal operations.

QR has nominated the General Manager Operations of the relevant QR above-rail business group as having the authority to suspend the Protocols. In practice, this is likely to be delegated, which is appropriate, provided that the responsibility to provide the contracted service via the Protocols is clearly understood by the delegate.

**Stanwell** - the Protocols should be developed with a view to providing maximum possible certainty to third-party operators, such as the circumstances in which the Protocols may be suspended and roles and responsibilities of QR operational staff and other stakeholders in this instance. In addition, they should seek to maintain the confidence of rail users in the integrity of the third-party access regime by ensuring that procedures are fair and equitable and provide the most expedient method of restoring normal operations.

### *QCA's Analysis*

The crucial role of the train control function in a rail network is to undertake the traffic coordination task. Poor quality traffic management has the potential to cause excessive delays and increases in cycle times, which affect a rail operator's utilisation of locomotive and rollingstock assets and the quality of service it is able to offer its customers. Furthermore, with third-party entry on the network, there is a need to establish transparent processes to ensure that the train control function is performed in a competitively neutral manner.

The QCA had a number of concerns about QR's proposed framework for the performance of the train control function established in the Protocols, in particular, the significant discretion QR reserved for itself and the resulting potential lack of transparency in train control decisions. Subject to a change regarding priority in train running, the QCA supports QR's train control principles, believing that their outcome-based focus is more likely to protect third-party operators' interests than the Protocols.

#### *Priority in train running*

Section 3(d) of the proposed Train Control Principles sets out what QR deems to be the critical operating objectives of the different traffic types using its network and, from these objectives, it establishes priorities across different traffic types for train control purposes. Implicit in this assessment is an assumption that a rail operator's capacity entitlements should reflect required outputs and critical operating objectives, such as transit-time requirements.

The QCA considers it unclear whether the critical objectives QR has determined for different traffics will be consistent with the likely requirements of third-party operators. Pre-determining priority levels would constrain third-party operators' choices. For instance, freight operators may wish to obtain the level of priority afforded to passenger services, and be prepared to pay a premium for this privilege.

A majority of stakeholders have supported more sophisticated priority arrangements than those proposed by QR. The QCA believes that a more flexible approach is required whereby objectives would not be related to specific traffics, but rather to the levels of priority that third-party operators require and for which they are actually prepared to pay. This would be incorporated into the access charge negotiated between Network Access and the third-party

operator. Capacity entitlements should therefore reflect a particular level of priority for the contracted train service.<sup>124</sup>

The issue of linking access charges to priority is discussed in Chapters 5 and 10.

#### *Departures from train schedules*

Under QR's proposed Train Control Principles, the primary objective is to keep trains 'healthy'. A healthy train is one that has experienced no deviation - in excess of an agreed tolerance - from the path in the daily train plan that could be attributed to QR in its role as rail manager. The QCA expects that a third-party operator and QR would negotiate particular tolerances around contracted train paths as part of an access agreement.<sup>125</sup>

Where the agreed tolerance is exceeded, the service is 'unhealthy' and involved in out-of-course running. Out-of-course running can be defined as the circumstances where the actual running of a train service differs, by more than an agreed tolerance, from the path provided in the daily train plan.

The QCA believes that the healthy/unhealthy concept and its link to out-of-course running can be consistently applied across all traffic types using the network. It should also provide a third-party operator with reasonable confidence that any potential conflict in train running will be dealt with in a consistent and non-discriminatory manner. Definitions of 'healthy' trains and out-of-course running should be included in the Train Control Principles.

The QCA agrees with ARTC that the objective of train control should be to focus on QR's obligations to respective rail operators, and to consider only performance over which the train control centres have control. To this end, it is important to a rail operator that, if it has not contributed to any late running of its service, then the service should achieve on-time exit, regardless of the impact on other rail operators' services where those operators have contributed to late running.

It is important to appreciate this point in the context of the definition of a healthy train. QR performs the role of train controller and thereby its actions can influence the performance of operators on the system. Potentially, it can create system delays by allowing an operator to secure paths that are inconsistent with other operators adhering to their scheduled paths. For example, by allowing a train that is running late to proceed, QR could cause a healthy train to be delayed because the unhealthy train occupies its path. Consequently, where a train presents on time and continues to operate within the agreed tolerances, but is outside its scheduled path on the daily train plan due to system delays (that is, through the action of QR's train control), it should be characterised as being a healthy train.

Section 4 of the Train Control Principles states that a Matrix will be provided to train controllers to assist decision-making in the event of out-of-course running. This procedural document facilitates the minute-by-minute decision-making necessary for the safe and effective provision of traffic coordination services. The QCA believes that the Matrix and any associated explanatory notes should be provided to third-party operators to assist their understanding of

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<sup>124</sup> On the ARTC network, operators are able to purchase capacity according to four levels of service – 'premium', 'high', 'standard' and 'low' – each reflecting different levels of priority. The four priority levels are reflected in the flagfall access price. For example, the access price for premium priority is generally around 50 per cent higher than for 'low' priority.

<sup>125</sup> Indicative tolerances for the various traffic types, which may also be dependent upon traffic density, could be: passenger (metropolitan) – 3 minutes; passenger (long distance) – 10 minutes; livestock and freight – 15 minutes; and coal and bulk commodities – 15 minutes.

train controllers' decision-making in the event of out-of-course running. To provide greater reassurance to third-party operators, the QCA has proposed that it approves the Matrix.

The issue of providing information to third-party operators to facilitate their understanding of train control decisions is described in more detail in the next section.

#### *Implications of departures from train schedules*

QR has not proposed to include any traffic management decision-making rules as part of its Undertaking. Stakeholders expressed concern about possible inconsistency in train control decision-making, in particular, one rail operator being favoured over another. The disruption of train path entitlements is also a potential source of dispute between QR and third-party operators.

The QCA believes that the inclusion of the Train Control Principles in an approved Undertaking, plus the dissemination of all planning tools used by QR to perform the train control function, would both increase QR's accountability and provide third-party operators with a sound understanding of QR's train control decision-making processes.

Inclusion of the Train Control Principles in an approved Undertaking is important because it establishes an enforceable obligation on QR to comply with them. Moreover, the Train Control Principles clearly outline the broad objectives or outcomes that third-party operators could expect from the performance of the train control function. This is an alternative to developing prescriptive rules for the resolution of conflicts over train control decisions.

The QCA supports QR's commitment to make available real-time train control information and copies of train control diagrams to assist rail operators gain an understanding of train control decisions. These information flows should eventually generate a level of predictability in the behaviour of train controllers, and, in particular, serve to improve transparency with respect to out-of-course running procedures such that many of the concerns of potential third-party operators would be allayed.

Where a third-party operator believed that the principle of competitive neutrality and/or its contractual entitlements had been breached, it would have the opportunity to initiate dispute resolution proceedings. It could be expected that potential remedies for such a breach would be reflected in the access agreement.

While the Protocols identified procedures that would result in a departure from, or suspension of, the Protocols, the Train Control Principles are silent in regards to these matters. The QCA believes that the Train Control Principles are robust enough to encompass a diverse range of incidents<sup>126</sup> that may lead to out-of-course running, and as such, the decision-making processes for resolving these conflicts should be clear to all rail operators. Consequently, there would be no requirement to divert from train control operations performed in accordance with the Train Control Principles. Once more, procedural transparency should be adequately facilitated by QR's disclosure of train control information to third-party operators.

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<sup>126</sup> An incident refers to any rollingstock derailment, rollingstock disablement or breakdown, accident, collision or any other unplanned occurrence on the infrastructure that causes or could cause: injury to any person; damage to property; environmental harm; or a loss to process including a cancellation by QR of any train movement.

***QCA's Position***

The QCA would favourably consider an Undertaking that:

- amended cl 6.1 of the Draft Undertaking to commit QR to perform the train control function in accordance with the Train Control Principles;
- incorporated the following Train Control Principles as a schedule to the Undertaking:
  - (a) The fundamental objective of train control will be to facilitate the running of train services and the commencement and closures of track possessions as scheduled in the daily train plan.
  - (b) The following general principles apply to train operations and train control:
    - (i) all parties will ensure that operational safety is maintained through compliance with safeworking rules, safety management systems, applicable safety risk management and rollingstock interface requirements and environmental management systems;
    - (ii) railway operators will ensure operating integrity, including train crewing, locomotives, wagons and loading so that the daily train plan can be met;
    - (iii) QR will manage the network on behalf of railway operators based on agreed entry/exit times as specified in the daily train plan with the objectives of managing trains according to their schedule for on time exit, not contributing to late running and, if a train is running late, making up time and holding the gain where reasonably possible; and
    - (iv) the primary objective is to keep healthy trains healthy.
  - (c) Out-of-course running is dependent on the particular circumstances of a rail corridor, including the traffic type using the corridor. In the event of out-of-course running:
    - (i) except as provided in a railway operator's access agreement, train control will adhere to the contracted capacity entitlement of each railway operator, expressed in terms of the daily train plan. The capacity entitlement will reflect a level of priority on the network;
    - (ii) where train control fails to adhere to a railway operator's contracted capacity entitlement, the

<p><b>terms of that operator’s access agreement will govern the consequences;</b></p> <p><b>(iii) the identity of a railway operator will, of itself, play no part in a decision by train control to alter that operator’s scheduled train service; and</b></p> <p><b>(iv) train control will resolve conflicts in accordance with the primary goal of keeping trains healthy.</b></p> <p><b>(d) The Matrix, approved by the QCA, will be provided to assist train controllers in the resolution of disputes in accordance with the above principles.</b></p> <p><b>(e) For the purposes of the Matrix, a ‘healthy’ train is defined as one that has experienced no deviation - in excess of an agreed tolerance - from the path in the daily train plan that is attributable to QR as the rail manager. Out-of-course running refers to the circumstances in which the actual running of a train service differs, by more than an agreed tolerance, from the path provided in the daily train plan.</b></p> <p><b>(f) QR will provide railway operators with the current version of the Matrix, real time train control information and copies of train control diagrams to assist operators understand how train control decisions are made.</b></p>
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## 6.5 Public availability of capacity information

### *QR’s Position*

QR proposes that it will undertake an initial capacity assessment as part of the preparation of an indicative access proposal. The initial capacity assessment will identify the amount of capacity that is not required to preserve existing capacity entitlements. The initial capacity assessment is designed to determine whether there is sufficient capacity to meet a third-party operator’s requirements and, if not, the extent to which additional capacity is required: para 6.2(a). A more comprehensive capacity analysis will be undertaken as part of the negotiation process between QR and the third-party operator: para 6.2(b).

QR argued in its supplementary submission to the QCA’s Request for Comments Paper *Queensland Rail’s Draft Undertaking* that the capacity information provided to access seekers is meant to be indicative and to provide a framework within which to consider QR’s overall assessment. QR indicated that the ‘operational information’ in Schedule D would include where applicable:

- the average number of trains travelling over a corridor on a daily and weekly basis; and
- the maximum number of trains travelling over a corridor on a daily and weekly basis.

QR has subsequently indicated its intention to prepare an Information Pack for each of the fourteen systems on its network, to be provided to potential access seekers on request for a \$500 fee. The QCA has been provided with copies of the Newlands, Blackwater, Goonyella and

Moura Information Packs. They define system capacity in terms of standard train paths per day and provides estimates of:

- average usage; and
- percentage of capacity committed.<sup>127</sup>

QR also argued in its supplementary submission that it would provide all rail operators with a copy of the master and daily train plans. However, in its view, there were practical problems in the provision of such information including:

- train plans are large documents that cannot easily be reproduced in their entirety in paper form;
- only seeing part of the plan(s) applicable to a (proposed) path may be misleading because it may not always be possible to consider available capacity in some regions in isolation from other regions in the network; and
- the master train plan is unlikely to reveal all information regarding the entitlements of individual operators in terms of capacity, for example, rescheduling options and priority, or whether capacity is currently under negotiation.

QR refined its position regarding the release of the master and daily train plans in its submission to the QCA's Request for Comments Paper *QR's Scheduling and Train Control Protocols and Proposed Assignment of Marshalling Yards*. In that submission, QR proposed that it would provide rail operators with copies of the part of the master and daily train plans that is directly relevant to their actual area of operation. However, QR would place the following caveats upon these plans:

- the identity of the rail operator for the scheduled train services would not be revealed;
- the train plans would not disclose the terms and conditions of each operator's capacity entitlement. For this reason, these plans may not provide a definitive basis for an assessment of available capacity; and
- as they would not show all parts of the network, they may not include all train services that could impact upon the capacity of a particular train service.

QR indicated that it was concerned some rail operators would not want other operators to be able to derive sectional running times from the plans. In any event, QR was only prepared to provide the master and daily train plans to rail operators and not to the public at large.

Finally, QR noted that Network Access has been trialing electronic versions of train plan details. If an electronic system is implemented within QR, it will provide operators with the train plan data in an electronic form.

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<sup>127</sup> The Information Packs are intended to fulfil QR's Schedule D (preliminary information) obligations and were discussed in Chapter 4.

## Stakeholder Comments

The majority of stakeholders considered it essential that QR be required to provide adequate information from which potential third-party operators could make their own capacity assessment.

### Table 8: Independent capacity assessments

**Great Southern Railway** - it will never be acceptable to access seekers to have to accept QR's analysis without the opportunity to check it.

**QMC** - access seekers should be able to argue QR's assessment of available capacity and have recourse to the QCA.

**Queensland Government** - in the event of access being denied because of capacity problems, the access seeker should be able to obtain, from QR, details of the capacity of the track, including the basis of capacity determination, and details of current and future access entitlements.

**AMC, Stanwell** - assessment of capacity is not a simple process and third-party operators should be on the same footing with QR in terms of conducting negotiations over access rights.

**Toll** - in the event that the initial capacity assessment indicates major impediments to the provision of sufficient capacity, a third-party operator should be provided with sufficient information to enable it to carry out its own assessment and be required to pay a reasonable fee for the provision of that information.

**FreightCorp** - it would be reasonable for QR to provide copies of train diagrams on which was printed the train timetable current for the applicable period. However, it would not be essential for an access seeker to have the train diagrams if the full working timetable was made available.

**ARTC** – operators are not likely to have sufficient expertise, nor knowledge of the wider operational issues beyond their access requirements in order to carry out their own capacity analyses.

A better way to create an equitable arrangement with regard to the capacity planning for all competitors would be for Network Access to be directly responsible for day-to-day capacity analysis. A consultative approach is preferable for this activity.

All stakeholder submissions in response to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*, favoured the release of master and daily train plans to potential rail operators on request.

### Table 9: Release of master and daily train plans

**FreightCorp** – With regard to capacity information, our experience is at odds with QR's assertion that it is prepared to provide master train plan and 48/24 hour train plan information on request. Our experience has been that QR is reluctant to provide this information on grounds that it infringes other operator's confidential information. We look forward to QR conforming with its stated position. We would also expect to be able to access this information in electronic format.

The full working timetable (tabular form of the master train plan with notes pertaining to all transit conditions) should be made available to operators

**Queensland Government** - third-party operators should have access to all information about train movements, including a timetable protocol and publicly available master timetable, to facilitate transparency and fairness

**AMC, Stanwell** - it is critical that information about train movements are made available publicly, because without this public knowledge it is unlikely that third-party operators or customers would have any confidence in the access arrangements

**Great Southern Railway** - information about train movements should be publicly available, however, the 24/48 hour train scheduling arrangements should remain confidential to those operators who have a current access agreement.

**QMC** - the information should be available on request.

### ***QCA's Analysis***

There is a significant information disparity between QR and third-party operators concerning available capacity on the network. Given QR's commercial incentive as a vertically integrated rail service provider to protect the revenues of its above-rail operations, the transparency of the capacity analysis process is crucial to protecting the interests of third-party operators and providing confidence to the marketplace.

The Draft Undertaking provides no right for a prospective third-party operator to be provided with the information it needs to test QR's capacity assessment. However, QR has since indicated a preparedness to provide operators with copies of the parts of the master and daily train plans relevant to their operations.

The QCA considers that the provision of adequate capacity information is necessary to provide confidence in the market about QR's capacity assessments. This is especially pertinent given the perception that QR could distort capacity outcomes in favour of its own train services. The key principle is that information relating to usage of the network should be publicly available and not be considered commercial-in-confidence to be 'owned' by Network Access.

The very nature of rail operations is that it is possible for anyone to identify train movements by strategically positioning a sufficient number of observers on the network. Clearly therefore, the nature of rail operations per se is not confidential – the data is merely expensive to collect for potential third-party operators. Hence, the QCA considers it desirable to avoid the need for third-party operators to collect this information by requiring QR to disclose it. As such, sufficient information should be made available to third-party operators to allow them to conduct their own capacity analysis. The following data would assist operators in their assessment of capacity, should they require it:

- master train plan;
- relevant daily train plans;
- train control diagrams;
- maintenance requirements; and
- historical delay and system disruption data.

QR's reasonable costs of complying with such a request should be met by the access seeker.

The QCA recognises the potential commercial sensitivity of some information that could be contained in the documents listed above. For example, it is not considered appropriate that QR provides details of capacity under negotiation, unless to inform an access seeker that the capacity it is seeking is currently under negotiation. However, third-party operators have indicated to the QCA that they view the benefit from public disclosure of information as outweighing the cost to them of that disclosure. This is an important point. QR is not suggesting public disclosure of capacity information would expose commercial-in-confidence information relating to its below-rail operations. Rather, QR has expressed concern about the potential harm that this may cause rail operators.

QR has identified practical problems in providing specific items of capacity-related information. However, train plans, while large and difficult to be reproduced in graphical format, can be expressed as schedule data. In addition, while recognising the limitations of these plans as only providing a partial view of the entire system, the data does at least provide potential rail operators with a guide with which to further progress negotiations with Network Access.

***QCA's Position***

**The QCA would favourably consider an Undertaking that:**

- **provided for the release of sufficient information to allow access seekers operators to conduct their own capacity analysis. Such information would include:**
  - **master train plan;**
  - **relevant daily train plans;**
  - **train control diagrams;**
  - **maintenance requirements; and**
  - **historical delay and system disruption data.**
- **required access seekers to pay QR's reasonable costs in providing such information.**

## 6.6 Capacity allocation process

***QR's Position***

Access rights will be allocated to the first railway operator with whom QR can negotiate and execute an acceptable access agreement: para 6.3.2(a). However, if at any time two or more railway operators are seeking access with respect to mutually exclusive access rights, QR is entitled to seek to finalise an access agreement with the railway operator with whom QR can agree to terms and conditions, which is most favourable in terms of the commercial performance of below-rail services: para 6.3.2(b).

QR's Explanatory Guide provides an indication of the factors QR will take into account in making such an assessment including:

- the length of the access agreement;
- the access charge and resultant contribution to common costs of the particular train service;
- terms and conditions relating to interface issues; and
- an approach to the capacity entitlement definition that is conducive to the optimisation of the utilisation of the rail infrastructure.

Access rights will be characterised in terms of train paths and frequency. Train paths will be established as part of the negotiation process and where they are not, and a frequency is

specified instead, they will be subsequently allocated by QR in accordance with the capacity entitlement of an operator through the Protocols: para 6.1(a).

In situations where two or more operators seek access to mutually exclusive access rights, once QR has signed an agreement with one operator it will cease to negotiate with the other operator(s): para 4.7.1(c)(iii). In its initial submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*, QR acknowledged that, in such circumstances, it may not be appropriate to discard information exchanged up to that point, however, it would inevitably be necessary to revisit the access proposal.

In its supplementary submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*, QR indicated that it would draft additional provisions to supplement para 4.7.1(c)(iii). These would reflect its intent that the negotiation process would not be recommenced from step one but rather revisited to reflect the impact of the changed circumstances. QR anticipated such provisions to involve it reviewing and revising the indicative access proposal and continuing the process from there. QR argued that while shorter timeframes will, in many circumstances, be possible, it did not consider it appropriate to further modify the process as the reconsideration of capacity impacts is often one of the most time consuming aspects of preparing access proposals.

In response to the argument that it could use para 4.7.1(c)(iii) to grant access to a marginal QR traffic over a more commercial third-party operator's proposition, QR argued that the Undertaking provided a commitment on its part to evaluate each access proposition in terms of the commercial performance of QR's below-rail services: para 6.3.2(b). In QR's view, this will preclude any favouritism to internal operators.<sup>128</sup>

### ***Stakeholder Comment***

Stakeholders viewed competitive neutrality as an important principle in the allocation of train paths.

#### **Table 10: Allocation of train paths**

**Great Southern Railway, National Rail, QMC, Toll** - protocols should be established in the Draft Undertaking to ensure competitive neutrality in capacity allocation.

**Toll** - it is necessary for there to be a transparent decision-making process in relation to the allocation of train paths and all rights of recourse should be available to any third-party operator who believes that the principles of competitive neutrality have not been fairly applied. The QCA should be the appropriate dispute resolution body in relation to competitive neutrality complaints. Public reporting in relation to these issues is probably not appropriate. However, reporting to the QCA should be required.

**Queensland Government** - there should not be separate protocols for this matter. The principle of competitive neutrality should be inherent in the allocation of train paths and train control protocols. The QCA could step in if a complaint is lodged under the QCA Act.

**Stanwell** - it is inappropriate for QR to decide between two operators competing for mutually exclusive business. However, if the QCA decided that QR should have the power to do this, then the process suggested by QR in the Draft Undertaking effectively would establish a protocol to sell to the highest bidder. The allocation of access rights to rail users would alleviate the problem of competitive neutrality between train operators.

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<sup>128</sup> It should be noted, however, that para 6.3.2(b) states that QR is 'entitled to', rather than 'required to', seek to finalise an access agreement with the operator whom QR can agree to terms and conditions most favourable in terms of the commercial performance of below-rail services.

**AMC** - a protocol is a second best solution, as it does not provide rail users with any guarantees, especially if applied internally in secret.

**FreightCorp** – The issue of capacity allocation is, no doubt, complex. However, whatever the outcome, FreightCorp believes that the process must have the following principles:

- open to scrutiny of all parties; and
- provide for genuine consultation between the parties (that is, multi-lateral participation not a series of bi-lateral consultations between Network Access and each operator).

The process should not be one which leaves Network Access as the only decision maker.

The Draft Undertaking should provide for the allocation of all capacity, not just QR's spare capacity. Unless this is done, QR will be in a position to allocate whatever capacity it sees fit to its own internal train operators.

Opinion was divided on the possible role of auction markets as an alternative means of allocating capacity.

#### **Table 11: Capacity auctions**

**Stanwell** - capacity auctions for allocation of mutually exclusive asset demands would be appropriate provided QR's revenue limit was not exceeded for the infrastructure involved.

**QMC, Toll** - capacity should not be auctioned.

**AMC** - capacity auctions are effectively what will take place under para 6.3.2 (b), although the details of the bids would not appear to be a public process and this could have some undesirable outcomes. The extension of the idea of auctions to allow resale of access rights amongst access holders would seem quite straightforward.

**ARTC** - an auction approach should be used to allocate mutually exclusive access rights. The approach proposed by QR could be open to abuse by QR (giving favouritism to its own business groups).

ARTC is considering auctioning (in conjunction with a secondary market in paths) to get around the problem of the access provider making an assessment of a train path to a rail operator. This approach is efficient from a track owner's perspective, allows the value of a path to be assessed by the party in the best position to make such an assessment (operator), and retains many of the benefits of a good pricing regime such as transparency and flexibility. It would require prudent management on the part of the track owner to ensure revenue adequacy and could co-exist with posted reference pricing where appropriate. This pricing approach does, however, require all bidders to be competitively neutral, a situation that does not yet exist on the interstate mainline.

**FreightCorp** - QR's suggestion that the process of access allocation could involve auctions is a no-lose proposition for a vertically integrated operator and a no-win proposition for rail-freight customers. If QR and a third party operator were seeking the same path and it was priced in an auction process QR could bid high knowing that it would win the auction, pay the high price to QRNAG and have the money ultimately accounted for in QR's annual report as a revenue and an expenditure of equal size and be of no net impact. Alternatively if QR bid high and the third party operator bid higher then QR would have been successful in increasing its revenue from access fees. Neither outcome fosters competition and both outcomes lead to higher prices for rail-freight customers.

A majority of submissions expressed concerns about QR's proposal to terminate an access negotiation with an operator due to a reduction in available capacity caused by another operator finalising an access agreement with QR.

**Table 12: Reductions in available capacity**

**AMC, National Rail, QMC, Stanwell** - it is inappropriate for QR to end negotiations with an operator on the grounds of reduced capacity adversely affecting the access rights sought.

**QMC** - the access seeker should be able to continue the negotiations on the basis of the revised amount of available capacity.

**National Rail** - QR should be required to notify the QCA for a possible validation of available capacity.

**MIM** - the proposed trigger for termination of access agreements is highly likely to prevent access and will favour incumbent QR businesses. One means of preventing this is to require access negotiations to continue if the ultimate customer notifies Network Access that it has not committed to a rail haulage agreement for the relevant capacity.

**Great Southern Railway** - there is considerable scope for QR to fail to find the maximum capacity available without following the rigorous process that is required.

**Stanwell** - it would be inappropriate if two third-party operators were competing for the one business and Network Access allocated track capacity or finalised an access agreement with one that excluded the other even though the customer may have chosen the losing party as their preferred operator. In the case where two third-party operators are seeking rail capacity for two different customer loads and there is only capacity to meet one of the customer needs, this may result in an inappropriate outcome if scarce capacity is allocated at lower prices by Network Access which deemed the customers of the successful third-party operator had a lesser capacity to pay. Further, the completion of an agreement with the first third-party operator should not allow Network Access to end negotiations with the second, as Network Access should be required to review its proposal rather than terminate negotiations.

**AMC** - this situation could be overcome by customers holding access rights.

**FreightCorp, Toll** - this issue needed to be considered as part of a comprehensive capacity allocation policy.

**Queensland Government** - reductions in available capacity may alter the direction of negotiations, but it does not appear reasonable that negotiations should automatically cease. A reduction in capacity could be addressed by increasing capacity, and it is likely that serious negotiation in respect of increasing capacity would not have occurred. The requirement should be that QR advise of changed circumstances and seek the response of the applicant.

**RTBU** - QR's proposal is appropriate as it is consistent with the Competition Principles Agreement.

***QCA's Analysis***

Allocating capacity on QR's rail infrastructure in an efficient manner is complicated by a number of factors, including:

- the monopoly characteristics of rail infrastructure, so that QR's ability to charge monopoly prices for use of its assets needs to be restrained;
- the role of capacity as a barrier to entry. With a vertically integrated organisational structure, attention needs to be paid to QR's incentive to favour its above-rail business groups over third-party operators;
- the role of congestion charging in rationing capacity and providing signals for new investment; and
- the different capacity requirements of various traffic types, such as non time-sensitive bulk train services and highly time-sensitive passenger train services.

In considering the various methods by which QR could allocate capacity, the QCA is mindful of the different characteristics of the haulage markets that third-party operators seeking access will be operating on. There is an important distinction to be drawn between two types of mutual exclusivity in the allocation of capacity:

- mutually exclusive traffics; and
- mutually exclusive paths.

Mutually exclusive traffics occur where several operators are competing for the traffic of a single end user, for example, where a coal mine calls for tenders. This is distinguished from a situation where operators will seek access on behalf of different end-users (mutually exclusive paths).<sup>129</sup> In the early stages of competition on QR's network, the former is more likely to prevail. The latter may well become more prevalent as the above-rail market in Queensland matures and more third-party operators establish a presence. The procedure for providing access must recognise both of these models.

QR is essentially proposing a 'first-come, first-served' process for allocating capacity. Where there is a constraint and multiple operators are seeking access to mutually exclusive access rights, QR proposes to make an agreement with the access seeker that results in the most favourable commercial outcome for Network Access.

Stakeholders have indicated that competitive neutrality issues are important in the allocation of train paths. Accordingly, the QCA is concerned that the 'most favourable' proposition provides inadequate transparency. It is a difficult test to apply and could potentially allow Network Access to favour one rail operator over another. Although the Explanatory Guide has indicated relevant criteria on which the 'most favourable' commercial outcome test will be based, it is still uncertain whether all operators will be treated equally, given the limited breadth of the explanation. However, adequate ring-fencing measures and QR's need to comply with s104 of the QCA Act, which relates to the prevention or hindering of access, should allay stakeholder concerns in relation to this matter.

In the case of mutually exclusive traffics, the principal requirement is that QR should treat the same traffic equally. It is imperative that Network Access is not afforded an inappropriate degree of influence in the assignment of that traffic at this point in the evolution of the above-rail market, given QR's vertically integrated structure. Under QR's proposal, there is potential for access to be used as a barrier to entry for above-rail operators. The first above-rail operator to complete an agreement with Network Access could effectively lock out any other operator for the same business, even though they have no formal contract with the end-user. In this instance, QR's approach is inappropriate.

Alternatively, if Network Access became aware of a situation with mutually exclusive traffics, it could execute contingent access contracts that would permit QR to deal with multiple operators on a contingent basis initially. These contingent access contracts would consist of prices and conditions for the operators' particular train and operating configurations.

Once a rail operator had been chosen by the single end-user as the preferred bidder, that operator's access right would become unconditional and the others would forfeit their conditional right. The other operators could not show that they would utilise the capacity QR had granted them conditionally, whereas the preferred bidder would be able to demonstrate its contingent rights should mature to an unconditional contractual entitlement.

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<sup>129</sup> This is the predominant type of access sought on the ARTC network.

Consequently, in these circumstances, QR would not find it necessary to apply the ‘most favourable outcome’ test. QR has indicated in its supplementary submission to the QCA’s Requests for Comments Paper *Queensland Rail Draft Undertaking* that it intends to add a provision to cl 4.8 to facilitate this.<sup>130</sup>

In the case of mutually exclusive paths, different businesses are competing for the same capacity in respect of the number and timing of paths. This problem may well be rare in practice, at least in the early stages of third-party access to QR’s network, especially as a commercial entity such as Network Access should have an incentive to accommodate the requirements of both operators. Where mutual agreement cannot be reached, then QR is required to make a commercial judgement. It must however be mindful of s.104 of the QCA Act in the event that it favours its own above-rail business groups over a third-party operator.

With respect to the rail operators who were unable to finalise an access agreement with QR, the QCA favours an approach whereby negotiations would not be terminated, but continue on the basis of a revised access proposal by Network Access taking into account the reduction in the available capacity. This is similar to the approach followed by ARTC, which tries to find an alternative path rather than end negotiations if the requested path is unavailable. ARTC’s approach is to maintain an open dialogue with any organisation wishing to pursue access as it is trying to encourage additional business on the network. Consequently, the QCA considers that para 4.7.1(c)(iii) should be removed.

If one rail operator’s requirements are such that it precludes another operator gaining access, for example, through inflexibility or time sensitivity, then it should be forced to pay a premium as it is likely to consume more than one path. This premium paid should assist in the funding of capacity augmentation, if it becomes commercial to accommodate the second user.<sup>131</sup>

Auctions, as an alternative means of allocating capacity, offer some advantages, including:

- they are useful when the value of an item or service is not well known;
- properly structured auctions (for example, with rules to prevent favouritism) are fair because all bidders have an equal opportunity to buy the item being sold and sellers have an equal opportunity to sell;
- they limit price discrimination; and
- they help allocate goods and services to the highest value consumers and production to the lowest cost suppliers.

However, in the context of Network Access’ business, auctions may have some disadvantages:

- fairness may be difficult to achieve given QR’s vertically integrated structure;<sup>132</sup>
- an unconstrained auction in a capacity-constrained part of the network could discourage QR from investing in the network;

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<sup>130</sup> An alternative approach involves an end-user appointing a preferred tenderer to commence negotiations with QR. However, such an approach may not be effective if there are expected to be substantial differences in access charges emerging from differing operational configurations which are difficult to predict.

<sup>131</sup> The circumstances in which QR will expand capacity are discussed in Chapter 5.

<sup>132</sup> There is an important difference between QR’s bids in an auction and that of third-party operators. QR’s solvency is not affected by bids from above-rail business groups in the way that a third-party operator’s solvency is potentially affected as no ‘cash’ changes hands.

- to operate effectively as an allocation mechanism, auctions require liquidity in the market; and
- there may be a lack of homogeneity in the definition of capacity entitlements.

While auctions may not be optimal for the initial allocation of capacity, at least at this stage, they may be a viable option where several third-party operators are seeking access to mutually exclusive capacity. QR's current proposal to seek the most favourable outcome in allocating capacity may resemble an auction market, however, the process is not transparent to the parties involved. If auctioning were introduced, each third-party operator would be able to bid in an open market. This could result in capacity being allocated to the highest value user.

Auctions have not been widely supported in submissions to the QCA. QR has recognised that capacity auctions may be a desirable way of allocating capacity, however, they may not be appropriate in all circumstances. Accordingly, QR has stated that the Draft Undertaking should be flexible enough to allow, but not require, an auction to occur.

The QCA notes that a significant evolution in capacity assignment will be likely in the future, as capacity becomes increasingly harder to obtain. Capacity auctions, while having never been successfully proven in the rail transport industry in the past, remain a possible means of allocating capacity.<sup>133</sup> Accordingly, whether or not to adopt auctions as a means of allocating capacity should be a commercial decision for QR. However, the QCA remains concerned about the safeguards that should be included as part of an auction mechanism to address potential regulatory issues. The following safeguards would be appropriate:

- lodgement of bids are to be made before a specified closing date;
- bids are to be made on a closed basis, with rivals unaware of the extent of each other's offer;
- the winning bid must be made transparent and communicated to all participating parties; and
- the process should be overseen by an independent person (ie. a probity auditor).

#### ***QCA's Position***

**The QCA would favourably consider an Undertaking that:**

- **included access rights being contingent on the winning of a contract with an end-user by a specified date. In this instance, reference to 'the most favourable commercial outcome for the below-rail service provider' should be deleted;**
- **removed paragraph 4.7.1(c)(iii); and**
- **included the following procedures if capacity auctions are to be conducted:**

<sup>133</sup> For instance, see Brewer P.J. and Plott C.R. (1996), 'A Binary Conflict Ascending Price (BICAP) Mechanism for the Decentralized Allocation of the Right to Use Railroad Tracks', *International Journal of Industrial Organisation*, vol. 14, pp. 857-86.

- **lodgement of bids made before a specified date;**
- **closed bids, with rivals unaware of competitors' offers;**
- **winning bid made transparent and communicated to all participants; and**
- **process overseen by an independent person.**

## 6.7 Resumption of capacity rights

### *QR's Position*

QR's intentions regarding capacity resumption have evolved since the lodgement of its Draft Undertaking. QR's initial capacity resumption policy was revised in its supplementary submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*. In July 2000, following discussions with the QCA, QR further amended its position. It formulated a set of objective criteria to assess under-utilised capacity under the capacity resumption test.

### *The Draft Undertaking*

QR reserves the right to reduce a third-party operator's access rights where the operator has consistently under-utilised its rights under its access agreement for a six month period and cannot reasonably demonstrate to QR a future requirement for those access rights: para 6.4(a).

A third-party operator has a right to trigger the dispute resolution procedure provided in its access agreement if QR reduces access rights in accordance with para 6.4(a) and the operator believes that QR's decision is not justified in the circumstances specified in that paragraph: para 6.4(b).

The Explanatory Guide notes that a third-party operator could meet the 'reasonably demonstrate' test if it provides evidence of a contract it has with another party which will require it to utilise the relevant access rights, or evidence of short-term extenuating circumstances affecting demand for its train services. Nevertheless, if the operator does not demonstrate that it will increase the use of its access rights to their full extent, QR may reduce those rights to a level that QR considers will meet the operator's anticipated level of demand.

### *Supplementary submission to the QCA's Request for Comments Paper Queensland Rail Draft Undertaking*

QR argued that in order to be more consistent with the approach taken by other Australian rail access providers and to better meet the concerns of stakeholders with respect to capacity, the time frame within which third-party operators had to use contracted capacity or lose it should be reduced from six months to three.

### *Objective criteria to assess the test for capacity resumption*

Following discussions with the QCA about the need to provide objective criteria so that the capacity resumption test could be transparently applied and assessed, QR has proposed to replace paragraphs 6.4 (a) and (b) with the following.

Where a railway operator, for any reason other than the occurrence of a force majeure event or the failure of QR to make the railway operator's access rights available, does not operate:

- a train service on a scheduled train path<sup>134</sup> seven (7) or more (not necessarily consecutive) times out of any twelve (12) consecutive occasions on which that particular scheduled train path exists; or
- all of its nominated weekly train services<sup>135</sup> for seven (7) or more (not necessarily consecutive) weeks out of any twelve (12) consecutive weeks;

and the railway operator cannot demonstrate, to QR's reasonable satisfaction, a sustained requirement for the access rights that have not been utilised, the terms of the access agreement will provide that QR may, by notice in writing, reduce the railway operator's access rights by:

- deleting the scheduled train path referred to above from the railway operator's access agreement; or
- reducing the railway operator's nominated weekly train services referred to above, provided that the number of remaining nominated weekly train services is no less than the railway operator's average weekly usage during the relevant twelve (12) week period.

Where QR reduces a railway operator's access rights in accordance with these provisions, the access charge payable by the railway operator will be varied in accordance with the terms of its access agreement.

Where QR makes a decision to reduce a railway operator's access rights in accordance with these provisions, and the railway operator believes that QR's decision is not justified in the circumstances after having regard to the factors specified in these provisions, the railway operator may challenge the decision through the dispute resolution procedure provided in its access agreement. QR will not implement the reduction, unless and until the dispute resolution procedure has been exhausted in favour of its decision, provided it is not otherwise required to do so by law.

### *Stakeholder Comments*

There was no agreement amongst stakeholders on the issue of capacity resumption.

#### **Table 13: Capacity resumption**

**National Rail, Stanwell, ARTC** - the resumption of rights by QR is inimical to competition and is a significant barrier to market development.

**Stanwell** - capacity reassignment is a central issue, but the Draft Undertaking is seriously flawed as it does not allow trading in rail capacity which is an essential element in efficiently allocating and pricing capacity. It is inappropriate that QR be given the power to withdraw access rights from any access holder or to transfer access rights from a third-party operator to its above-rail business groups.

<sup>134</sup> Scheduled train path means an entitlement of a railway operator to use a specified portion of the rail infrastructure at the times and between the locations specified in its access agreement, as amended or varied from time to time, so as to allow the passage of one train.

<sup>135</sup> Nominated weekly train services means the number of train services that a railway operator has an entitlement to operate during any one week period, as specified in its access agreement, as amended or varied from time to time.

**National Rail** - the ‘trigger’ period of six months is too short. Many long-term rail businesses would barely have started in such a short period, or may not have started at all, due to problems associated with equipment supply, mine commissioning and the like.

**ARTC** - QR should only be able to act as proposed if there is another bona-fide call on the path. The instigation of a flexible take-or-pay arrangement with the operator may better protect QR’s interests without threat to the operator’s certainty. It is, however, important that QR acts to prevent the taking of paths as a blocking ploy (whether or not QR business groups are involved).

**Toll** - whether capacity reassignment is operated as a barrier will depend upon how well the capacity allocation policy works. The critical issue is the ability of a third-party operator to relinquish access rights. This can either be by way of agreement with QR or trading rights.

**Queensland Government** - a capacity transfer protocol could be developed which has the objective of optimising the efficient utilisation of QR’s network while protecting the legitimate business rights of third-party users. Issues that could be addressed in the protocol include access fees for non-utilisation and capacity reassignment procedures. It may be preferable for the Draft Undertaking to assign the role of arbiter in this situation to the QCA.

**FreightCorp** - the Draft Undertaking should allow for the compulsory resumption and reassignment of rights under circumstances where another operator has won the business that was served by those rights. This would avoid the potential for the frustration of access to be used as a threat to an end-user.

**QMC** - the Draft Undertaking’s proposed capacity transfer procedures are not relevant if an alternative capacity allocation approach is adopted. In that context, limited transferability of access capacity during the term of the initial Draft Undertaking is recommended.

### *QCA’s Analysis*

The QCA recognises the significance and sensitivity of capacity resumption in QR’s capacity management policy. Capacity resumption has important competition and public interest dimensions. The QCA believes that QR needs to retain a resumption right to prevent capacity becoming a barrier to entry in the above-rail market. On the other hand, QR could apply its capacity resumption right to frustrate a third-party operator’s attempts to develop its business. If permitted, this also could become a significant barrier to entry. Consequently, the specification and application of any resumption test will involve a difficult balancing of interests.

#### *The interests to be balanced*

In many of the markets served by rail, third-party operators will require a reasonable period over which they can build and develop their businesses to the point that capacity rights are being utilised. In this regard it is not evident that three months provides a train operator with a reasonable opportunity to achieve this objective. That is, the QCA considers that QR’s proposed resumption provisions may act as a barrier to entry through the prevention of adequate time to develop a viable business.

This concern may be partially ameliorated by encouraging the rail operator and QR to explicitly note the probability of a ‘ramp-up’ in operations in their access agreement. In this manner, ramping up arrangements could become part of a normal commercial access negotiation. However, the securing of access to the network is just one of a number of factors creating uncertainty for a new rail business. Other factors include building a customer base and the finalisation of a myriad of requirements to enable operations to commence. Consequently, the inclusion of ramping up arrangements will not of itself overcome the difficulties associated with application of a rigid resumption test for a new operation.

The commercial interests of QR require that where access rights are not being utilised by rail operators and demand exists for these rights, then QR should be entitled to resume them. However, the necessity for QR to retain a resumption right on commercial grounds hinges partly

upon the nature and requirement for payment of access charges. For example, QR's cash flows are less vulnerable if the relevant contract contains a 'take-or-pay' element, as opposed to one that is based exclusively on 'pay-by-use' arrangements.

In addition to these competitive conduct concerns, the Authority considers that resumption rights are consistent with the public interest. This is particularly so given the considerable amount of public resources invested in QR's network, and the public interest in having available rail capacity utilised as fully as possible to reduce road congestion and greenhouse gas emissions.

It is in this context that the Authority has assessed QR's proposed threshold test for the resumption of capacity.

*Objective criteria to assess 'consistently underutilised' capacity – the 'triggers'*

The QCA was concerned that the Draft Undertaking contained a 'consistently under-utilised' test but no objective criteria against which a transparent assessment could be made as to whether the threshold for the resumption process had been triggered for a railway operator's capacity. The uncertainty surrounding the application of this test could have deterred third-party entry into the above-rail market.

QR's latest proposal addresses this concern through the identification of a trigger, formulated as a particular usage condition. These resumption triggers are expressed in terms of scheduled train paths and nominated weekly train services, which reflect the operation of various traffic types and nature of the respective capacity entitlements.

Once a trigger for resumption is activated, the incumbent operator could be required to show cause as to why its access rights should not be reduced to meet the current level of demand for its haulage services. Where access rights are revoked, QR has stated that a rail operator can challenge the decision through the dispute-resolution procedure in its access agreement

Similar approaches have been adopted by rail managers in other jurisdictions. RAC has a capacity resumption policy such that if an operator does not use a train path in accordance with the train specification:

- on at least 3 consecutive occasions; or
- for an average of at least 50% of the time measured over a rolling 3 month period; or
- for a continuous period of 30 days;

and another rail operator requests access to some or all of the relevant train path, the incumbent operator will be asked to show cause why its access rights should not be revoked. If it fails to do so, RAC may remove the train path from the access agreement.

ARTC retains the right to delete any scheduled train path if the service using that path is not operated 7 or more times, whether consecutively or not, out of any 12 such services which are consecutively scheduled. The ARTC test does not require there be another rail operator requesting access to some or all of the relevant train paths.

The first limb of QR's proposed approach is similar to the ARTC test. However, QR's test is more stringent because of the presence of a second trigger, which requires that an operator should use all of its nominated weekly train services for 7 or more weeks out of 12 consecutive weeks.

These triggers, by their very nature, are backward looking. In practice, there is no alternative but to adopt such an approach. However, it is important that the ultimate test applied is forward looking, in the sense that the focus of the assessment is whether or not the rail operator can demonstrate a sustained requirement for the access rights. This is because the satisfaction of the trigger would not guarantee the absence of a sustained future requirement for the capacity. For example, there are a number of potential factors such as seasonal fluctuations, a cyclone, or a prolonged problem at a port or mine, that may result in a trigger being satisfied. In many of these cases, it would be inappropriate that an operator's capacity entitlements were jeopardised. In recognising that these conditions are only a trigger, the QCA is of the view that QR should not revoke paths from an operator unless regard is had to end-user requirements.

In this respect, the QCA is satisfied with the resumption triggers QR has proposed. However, the activation of a trigger could result in capacity being resumed without alternative demand being demonstrated.

#### *Alternative demand for capacity*

QR's proposed resumption test does not include a requirement that alternative demand exists for the service that is potentially the subject of the resumption process.

In general, it might be expected that QR will have limited incentive to resume paths in the absence of alternative demand where the incumbent rail operator pays an access charge. However, the QCA considers that the sensitivity of a resumption of capacity makes it reasonable that there be a demonstration of a reasonable expectation of the existence of alternative demand for the capacity before resumption occurs. In addition, it is desirable that steps be taken to minimise the risk of 'phantom' access applications being made merely to facilitate the resumption of capacity.

Accordingly, the QCA considers the test should make reference to the reasonably expected existence of alternative demand for the capacity that is the subject of the resumption process. Where QR acts to reduce an rail operator's capacity entitlement the onus should be on QR to demonstrate that there is a reasonable expectation of alternative demand for the disputed capacity in the event the incumbent instigates the dispute-resolution processes.

A further issue concerns the threshold for the reasonable expectation of alternative demand. In this respect, a key concern to the QCA is the likely delay in the completion of the dispute-resolution process (discussed below). The longer the dispute-resolution process takes to finalise, the greater the justification for a lower threshold for alternative demand.

If lengthy delays were expected in the resumption process, the legitimate business interests of QR, as network manager, and access seekers could be frustrated by an incumbent that draws out the resumption process for as long as possible. In such a case, QR could argue that resumption is necessary in the absence of an access application because it would not be feasible to resume capacity within a reasonable period following its receipt of an access application.

However, the Authority understands that a properly constructed dispute resolution process via expert determination should normally reach a conclusion within one month or six weeks. Consequently, there does not appear to be a strong case for a low threshold to be set for the demonstration of alternative demand on account of possible delays in the resumption process.

The availability of capacity-related information such as the master train plan, relevant daily train plans and train control diagrams will make transparent the allocation of paths and path usage. In particular, this means that those seeking to gain access to already committed capacity will become aware of its potential availability through resumption. Should a potential third-party operator identify a need for particular allocated but unused paths, the QCA considers that

this operator should be able to require QR to consider resumption of those existing access rights by contracting to purchase the available paths once they become available. Such a commitment would clearly demonstrate alternative demand and, in appropriate circumstances, facilitate a more decentralised capacity-resumption process.

Accordingly, there should be two ways in which the resumption process for unused capacity may be instigated:

- where Network Access seeks to resume capacity (perhaps because of the receipt of a conditional commitment from an access seeker to acquire the disputed capacity or some part of it); and
- where an access seeker seeks to resume capacity so that it can acquire that capacity, or some part of it.

#### *The resolution of disputes*

Access agreements will normally define dispute resolution procedures. For example, QR's Schedule E provides that the parties may refer a dispute for resolution by an expert or arbitration. However, in the context of a possible resumption of capacity, the Authority considers it desirable that the dispute-resolution process be quick and clear to all parties, including those access seekers who wish to invoke it. Consequently, the Authority considers it important that the Undertaking define the dispute resolution process.

The QCA has proposed a process that would involve a party (either QR or an access seeker) giving notice to the Authority and the other relevant parties indicating the capacity sought and detail the circumstances which have led to the satisfaction of the trigger. The QCA would then substantiate the information and appoint an expert to hear the matter. Once the expert had been appointed, the process would begin with the parties being allowed 10 business days to make submissions to the expert, with:

- the incumbent rail operator bearing the onus of demonstrating it satisfies the test for a sustained requirement for the access right; and
- QR, as the network manager, bearing the onus of demonstrating the test of a reasonable expectation of alternative demand is met. In the event that the access seeker makes the application directly, then an issue may arise concerning the access seeker's compliance with QR's requirements in its Draft Undertaking (eg interface issues).

The dispute resolution process would then allow the expert 10 business days in which to deliver a decision. This should allow the dispute resolution process to be finalised normally within one month of the expert being appointed. The expert's decision would be final and become effective at its discretion.

#### *Life of the trigger*

The next issue concerns the period of time over which the trigger event remains 'live', in the sense that it remains available to QR or access seekers to instigate the resumption process. In this respect, it is relevant that:

- the threshold trigger proposed by QR involves a relatively low threshold, for example failure to operate all scheduled services in 7 weeks out of 12. Moreover, this threshold is a rolling threshold – the fact that a failure to operate contributes to one threshold does not preclude that same failure subsequently triggering the resumption process at a later point in time; and

- the resumption test - once the trigger has been satisfied - is essentially forward looking, both in terms of the incumbent showing cause and the access seeker or Network Access demonstrating alternative demand.

The QCA considers that the trigger should only be available for one month. This is because the forward-looking resumption test means that a trigger's relevance to resumption, if activated as a result of an isolated event, should not have long-term implications. If an incumbent third-party operator's use of the network consistently triggers the test then the access seeker and QR would not be unduly inconvenienced – the passing of one 'live' period would be followed by another. However, a consistent pattern of under-usage would, over time, build the case for a resumption.

#### *End user's change of rail operator*

Finally, the QCA believes that an end-user should have the right to notify QR that it wishes to change its haulage operator irrespective of whether or not access agreements are unbundled. Where a rail operator can demonstrate that it has an unconditional contractual entitlement with an end-user for paths in preference to an incumbent rail operator and the end-user nominated in the access agreement serves notice on Network Access indicating its commitment to change operator from a given date, then the incumbent's capacity entitlement should be reassigned from that date. This would be subject to the satisfaction of the capacity transfer conditions. This process will ensure that capacity need not be a barrier to switching operator. It would leave contractual disputes to be resolved between the end-user giving the notice and its former rail operator.

#### ***QCA's Position***

**The QCA would favourably consider an Undertaking that:**

- **establishes a threshold trigger for resumption of access rights where a railway operator, for any reason other than the occurrence of a force majeure event or the failure of QR to make the railway operator's access rights available, does not operate:**
  - **a train service on a scheduled train path seven (7) or more (not necessarily consecutive) times out of any twelve (12) consecutive occasions on which that particular scheduled train path exists; or**
  - **all of its nominated weekly train services for seven (7) or more (not necessarily consecutive) weeks out of any twelve (12) consecutive weeks;**
- **allows QR to issue a notice in writing which reduces the railway operator's access rights, either by:**
  - **deleting the relevant scheduled train path from the railway operator's access agreement; or**
  - **reducing the railway operator's relevant nominated weekly train services, provided that the number of remaining nominated weekly train services is no less than the railway operator's average weekly usage during the relevant twelve (12) week period;**

**once the threshold trigger has been satisfied and provided:**

- the railway operator is not able to demonstrate, to QR’s reasonable satisfaction, a sustained requirement for the access rights; and
  - QR is satisfied that it can demonstrate that it has a reasonable expectation of alternative demand to justify a resumption of capacity;
- provides that where QR reduces a railway operator’s access rights, the access charge payable by the railway operator will be varied in accordance with the terms of its access agreement;
- provides that where QR makes a decision to reduce a railway operator’s access rights in accordance with the stated procedure, and the railway operator believes that QR’s decision is not justified in the circumstances, the railway operator may challenge the decision through the dispute resolution procedure for capacity resumption disputes;
- provides that QR will not implement the reduction, unless and until the dispute resolution procedure has been exhausted in favour of its decision, provided it is not otherwise required to do so by law;
- incorporates the following procedure to apply with respect to capacity resumption disputes. A party (either QR, a railway operator or an access seeker) instigates the process by giving notice to the QCA and the other relevant parties indicating the capacity sought and detailing the circumstances which have led to the satisfaction of the trigger. The QCA would then substantiate the information and appoint an expert to hear the matter. Once an expert has been appointed, parties would be allowed 10 business days to make submissions with:
  - the incumbent railway operator bearing the onus of demonstrating that it satisfies the test for a sustained requirement for the access right; and
  - QR, as network manager, bearing the onus of demonstrating that the test of a reasonable expectation of alternative demand is met.

The expert would be allowed 10 business days in which to deliver a decision, which would become effective at the expert’s discretion;

- establishes the life of a particular transgression of the capacity resumption trigger as one month;

- **permits an end user to change its rail operator subject to the satisfaction of capacity transfer conditions;**
- **provides that all of the above matters also be included in access agreements; and**
- **establishes a right for access seekers to apply for a resumption of an incumbent’s capacity.**

## 6.8 Capacity transfer procedures

### *QR’s Position*

Should an operator wish to reduce its entitlements allocated under an access agreement, it must seek to surrender those unwanted access rights to QR who will then use all reasonable endeavours to reassign them. These unwanted rights, and the attached liabilities, will only be reduced if QR is able to allocate them to another accredited rail operator: para 6.4(c).

Access rights may only be transferred by an operator assigning the whole of its respective rights and obligations under an access agreement in accordance with the assignment provisions of that access agreement: para 6.4(f). In this process, operators are not permitted to on-sell their rights directly to other accredited rail operators but must do so through QR who acts as a broker.

QR argues transferability of access rights directly between rail operators raises a number of practical difficulties:

- access rights are not homogenous. Access rights will be granted to a particular rail operator under a set of terms and conditions appropriate to the specific operation including a definition of capacity entitlement, an agreed operating plan and agreed rollingstock interface standards. For access rights to be directly transferable to another railway operator, there would need to be a requirement for the new operator to satisfy the same terms and conditions outlined in the access agreement, for example, the same rollingstock and operating plan. Given that the requirements for different train services can be highly variable, particularly given the wide range of end-user markets that are serviced by rail and the variety of rollingstock and operational solutions available, it is difficult to define access rights which can be confidently traded without creating inflexibilities which potentially reduce the attractiveness of access to rail operators and/or the capacity and efficiency of the overall system;
- access rights are likely to be most homogenous within the same end-user markets. However, even in these circumstances, homogeneity cannot be assumed. In the export coal market, for example, access rights are defined in terms of a movement from mine to port. Selling those access rights to another user, such as the operator for another mine, would require a change in the definition of the access rights. System integrity concerns would require such a change to be approved by the access provider;
- QR is proposing a market-pricing philosophy for determining access charges, as this will assist in maximising economic efficiency whilst allowing QR to recover its reasonable costs in providing access. The ability to promote economic efficiency through differential pricing becomes limited once access rights are directly tradeable – rail operators paying lower access charges have the ability to cannibalise the market by on-selling to those paying higher access charges; and

- government payments support much of QR's rail infrastructure. The direct transferability of access rights could allow 'profits' to leak from the rail system because of the information advantage of operators and speculators (allowing arbitrage) which may increase the cost to Government of supporting this rail infrastructure. Further, any reduction in the efficiency of the system resulting from the reduced flexibility in tailoring capacity entitlements to specific user requirements could increase the cost to Government of making such infrastructure available to rail operators.

In the context of discussions between QR and its stakeholders in mid-2000 regarding the development of revised Schedule E principles, FreightCorp proposed the inclusion in QR's Undertaking of a provision allowing access holders to relinquish access rights.

In correspondence to the QCA, QR opposed a relinquishment right, arguing that a rail operator would be free to walk away from a long-term access agreement, to the extent of the capacity which it wished to relinquish, in circumstances where it no longer required all of the contracted capacity. In contrast, QR would be obliged to provide the contracted capacity during the term of the access agreement - and incur penalties for failing to do so. The mismatch in the obligations of the parties was obvious and unacceptable to QR.

QR argued that the obligation on the part of QR to apply capital to provide the contracted capacity must be matched by an obligation on the part of the rail operator to pay for that capacity during the full term of the access agreement.

### *Stakeholder Comments*

There was some support for end-users and third-party operators being able to reassign access rights. There was also support for QR's legitimate business interests being protected in such an environment.

#### **Table 14: Reassigning capacity**

**AMC, Stanwell** - access rights should be available to customers and they should be able to freely trade, that is reassign, their access rights. A market in access rights would not affect QR's ability to meet its revenue limit or safety obligations. Arbitrage is normal in markets and should be allowed in the market for access rights.

**AMC** - the Draft Undertaking should allow for free capacity transfer between parties.

**Queensland Government** - reassignment by a third-party operator, rather than resale, appears a reasonable option. However, it would be crucial that procedures are established that ensure that QR's legitimate business interests are adequately protected.

**FreightCorp** - Network Access has an important role in network management and therefore in the assignment and reassignment of access rights. It would therefore be most appropriate for all assignments of access rights to be handled through Network Access. Moreover, QR should have the right to veto transfer of access between operators.

**ARTC** - in our undertaking, we are allowing an operator to sell/trade any scheduled train path to another person who proposes to operate a train using the path, without significant ARTC involvement when certain circumstances apply, primarily where the terms and conditions of the original access agreement are retained but apply to the proposed operator.

In June 2000, FreightCorp provided correspondence to the QCA arguing that a rail operator should have the right to voluntarily surrender capacity which it has contracted for under a long-term access agreement in circumstances where it no longer requires all of the contracted capacity. These circumstances could include loss of business from a mine or a change in technology leading to the use of more efficient trains.

FreightCorp argued that, under a long-term contract, it is possible that an operator's circumstances change significantly such that it requires less - or different - capacity than that originally contracted for. Without the ability to modify that contracted capacity, the operator would have an obligation to pay the fixed component on any excess capacity until the end of the contract.

### *QCA's Analysis*

In broad terms, the QCA believes that there are potentially two forms of capacity transfer. First, a holder of access rights may choose to surrender some or all its capacity entitlement to the access provider. The access provider could subsequently attempt to reassign that capacity entitlement to a different access seeker. Second, a holder of access rights could attempt to reassign some or all of its capacity entitlement directly to another access seeker. This would require a formal secondary market in access rights. In such a market, the role of the access provider could vary from 'hands off' – requiring notification of such a transfer – to 'hands on' – reserving a right to approve the transfer. The QCA considers that the establishment of a secondary market in access rights is important to facilitate entry into the above-rail market because it enables an access seeker's potential future liability to be reduced.

#### *Surrendering access rights to Network Access*

The Draft Undertaking imposes significant restrictions on the reassignment of capacity, while providing a key role for QR in the process. Where a third-party operator wishes to reduce its access rights, it may seek to surrender the unwanted access rights to QR. QR will subsequently use reasonable endeavours to reassign them to another operator. These access rights will only be reduced if and to the extent that QR reallocates them, or as otherwise agreed between QR and the operator. This implies that:

- unwanted access rights cannot be transferred to another operator (only Network Access); and
- the incumbent holder of the access rights is liable for payment of the entitlement until otherwise reassigned.

Under these arrangements, QR may have little incentive to reassign a third-party operator's access rights before it sells a fresh capacity entitlement to another third-party operator.<sup>136</sup>

The QCA believes that a right to surrender access rights should form an important part of the capacity transfer framework established by an approved Undertaking. Such a right would complement the establishment of a secondary market in access rights.<sup>137</sup> Hence, if a rail operator found itself in a situation where it no longer required some of its contracted capacity, the QCA would expect, in the first instance, that it would attempt to transfer the capacity to another rail operator using a secondary market in access rights. However, given this market may take some time to develop, and could remain 'thin' for a long period, the rail operator would be able to choose to surrender capacity if it could not find an alternative user.

In terms of the Draft Undertaking's right to surrender capacity: para 6.4(c), the QCA has proposed amendments to provide greater protection of the interests of access seekers, particularly with respect to payment for surrendered and reassigned capacity.

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<sup>136</sup> The Draft Undertaking allows only accredited railway operators to hold access rights.

<sup>137</sup> The QCA has proposed a number of amendments to the Draft Undertaking to facilitate the development of a secondary market in access rights, which are discussed in the next section of this chapter.

In proposing these amendments, the QCA recognises that the nature of a right to surrender capacity could adversely affect the dynamics of negotiations regarding capacity. For example, it could create an incentive for rail operators to seek longer terms for access agreements than they otherwise might. It is also likely to affect the frequency with which services are sought – the easier that relinquishment can be secured the more likely access seekers will apply for more paths per week than they are likely to require. This is because the relinquishment right would effectively serve as an ‘option’ to hand back capacity. The rail operator would be able to exercise the option during the term of the agreement. A right to surrender capacity along such lines would fail to protect QR’s legitimate business interests.

FreightCorp identified the closure of a mine or introduction of more efficient trains as events potentially justifying relinquishment of an access right. The QCA believes that the appropriate party to manage the risk associated with the occurrence of either of these two circumstances is very different. The introduction of more efficient trains is predominantly an above-rail risk that should be managed by the rail operator and its customer(s). In contrast, the closure of a mine is a risk appropriately managed by the network manager, rail operator and customer. This illustrates the difficulty in developing a right to surrender capacity that protects the interests of both QR and access seekers.

The Authority has distinguished between two broad customer classes utilising QR’s network. One such customer class comprises those traffics paying access charges that reflect the full cost of providing the service, for example, coal. The other customer class comprises those traffics that make only a moderate, if any, contribution beyond the incremental costs of their usage, for example, non-coal freight and passenger. The relinquishment of access rights in QR’s coal system is discussed as part of the development of reference tariffs in Chapters 10 and 16, which deal with the annual commitment to purchase train paths and the review of reference tariffs respectively. The QCA believes that the nature of the relinquishment right for the non-coal freight and passenger customer classes should reflect their small contribution to capital costs.

Consequently, for non-coal freight and passenger traffics, the QCA has proposed that, after surrendering access rights, an access seeker would continue to pay the difference between its total access charge and the maintenance costs saved by the service not operating for the remainder of the contract term, or until QR re-sold the capacity. The difference between the access seeker’s total access charge and the maintenance costs saved by the service not operating would effectively reflect the opportunity costs of QR providing capacity under the haulage contract. In this way, QR’s legitimate business interests would not be adversely affected.

Nevertheless, if QR could demonstrate that its maintenance costs would not reasonably be affected by the reduced traffic for a period of time, then the access seeker would be obliged to pay the full access charge for that time. QR would, however, bear the onus of establishing this fact. If QR reassigned the incumbent access seeker’s access rights before its contract expired, the access seeker’s obligation to continue paying access charges would be terminated.

In this respect, the Authority notes that commercial negotiation will normally resolve these matters. However, the establishment of the proposed benchmark will assist these negotiations to progress. It is expected that the parties may negotiate relinquishment rights that varied substantially from the arrangement outlined above. For example, Network Access and a third-party operator may agree that the operator pay a premium in order to be able to relinquish its access rights without penalty.

It is possible that QR could accept relinquished access rights from an access seeker and then sell another set of access rights for essentially the same capacity to a different access seeker. This would effectively enable QR to recover its costs twice for the same capacity. To protect the access seekers’ interests, the Authority considers that QR should be obliged to assign

surrendered capacity to the next access seeker that seeks rights consistent with those that have been surrendered.

The QCA accepts that determining such consistency is difficult and can only be undertaken on a case-by-case basis. Nevertheless, a reasonable test of consistency would appear to be that, if QR could not have supplied a train path to the next access seeker without using some part of the relinquished capacity, then the obligations associated with the relinquished capacity should be treated as if the capacity had been resumed.

It is recognised there is a risk that this mechanism could result in QR reassigning capacity for a long haul to another railway operator that requires only a small part of that capacity to operate and that such an outcome would effectively end the relinquishing party's obligations to QR. Under certain circumstances, this could leave QR worse off and reduce its incentive to encourage the resale of relinquished capacity. However, in practice, it is highly unlikely and the arrangements proposed by the QCA are consistent with QR's proposal in relation to the capacity resumption processes.

### *Secondary market in access rights*

Where a rail operator wants to transfer access rights to another non-related body corporate (or operator), the Draft Undertaking constrains transfer to the whole of its respective rights and obligations, as detailed in the access arrangement, and only with the prior written consent of QR, which shall not be unreasonably withheld. However, the Draft Undertaking provides no basis to assess when consent might be reasonably withheld. Consequently, QR is both an intermediary through whom unwanted capacity can be transferred and also an arbitrator on the transfer of capacity.

The QCA accepts the difficulties that QR has raised in relation to capacity transfer. However, the promotion of secondary trading of capacity entitlements should have beneficial implications for the efficient allocation of capacity.<sup>138</sup> It could complement the proposed 'unbundling' of new access agreements into access right and haulage components where an end-user chooses, which also provides scope for more flexible management of rail capacity from the perspective both of QR and its customers.<sup>139</sup>

Transferability of access rights could be accommodated through the development of a formal secondary trading market or informally through adequate allowances in QR's Undertaking which empower holders of access rights to transfer the rights through bilateral agreements.<sup>140</sup> The QCA believes that, while effective secondary trading mechanisms are likely to increase the efficiency of allocation, the cost of establishing a formal secondary market is likely to outweigh the benefits at this stage of the development of a contestable above-rail market in Queensland.<sup>141</sup>

QR has proposed that full transfer include all of the respective rights and obligations under the access agreement. Consequently, an accredited operator purchasing the rights from another operator must adhere to the full obligations of the access agreement that comes with the rights.

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<sup>138</sup> Klein, M and Gray, Philip (1997) "Competition in Network Industries – Where and How to Introduce It", in *Public Policy for The Private Sector*, argue that if rights to use railway tracks are defined and allocated to multiple parties, secondary trading should yield the optimal set of paths through the network (the set that maximises welfare given producers and consumers valuations of the service).

<sup>139</sup> 'Unbundling' is discussed in Chapter 4.

<sup>140</sup> Capacity release programs are a central element to the regulation of gas transportation in the USA and have allowed for increased flexibility and efficiency of gas markets.

<sup>141</sup> However, it should be noted that a form of secondary market already exists as part of the Blackwater User Group on the Blackwater system – mines indicate preferences and paths are assigned accordingly. This is a form of organised secondary market for train paths.

Heterogeneity of product imposes a significant hurdle in the transfer of access rights. While many of the clauses in the access agreements may be generic, others will be specific to the nature of the traffic, such as product hauled and train specification. Accordingly, the transfer of rights between access seekers needs to have regard to the implications of contracts.

The QCA believes that QR's consent should be sought for transfer of access rights and that this consent should not be unreasonably withheld. Relevant factors that need to be considered include:

- QR should be compensated for additional maintenance or capacity costs according to reference tariff criteria, or on a similar basis for other traffics;
- interface arrangements need to be satisfied;
- adjustments need to be made to pricing on the basis of the end-market being served, so as to discourage arbitrage; and
- subject to a commerciality test, the assignor's liability should be reduced under the contract once the assignment has been effected. QR's consent to an assignment could be reasonably withheld where QR is exposed to an unacceptable financial risk from the transfer. However, in other circumstances, the assignor's liability to QR should cease with the assignment.

Subsequently, where consent is given, the QCA considers that QR should not be able to require that it oversee the arrangement in a brokering capacity, except as is necessary to protect its legitimate business interests. Transfer could be facilitated through an adequate notification procedure, although a contract between the new rail operator and QR would need to be signed. Furthermore, partial transfer of capacity should be permitted in this manner.

#### *QCA's Position*

**The QCA would favourably consider an Undertaking that:**

- **allowed an access seeker carrying non-coal freight and passenger traffics to surrender its access rights subject to the access seeker continuing to pay the difference between its contracted access charge and the maintenance costs saved for the relevant line/corridor for the remainder of the contract term, or until QR re-sells the capacity;**
- **obliged QR to assign surrendered access rights to the next access seeker that seeks rights consistent with those that have been surrendered;**
- **recognised that if QR could not have supplied a train path to the next access seeker without using some part of the surrendered capacity, then the access rights should be considered consistent and the surrendered party's obligation to QR would then be terminated;**
- **allowed the transfer of unwanted capacity rights between participants, including partial transfer, by bilateral negotiation, subject to the establishment of adequate notification procedures between QR and capacity**

**holders;**

- **allowed access agreements to make appropriate adjustments to access rights so that transferability could be accommodated; and**
- **subject to a commerciality test, did not allow QR to unreasonably withhold consent for the transfer of capacity.**

## CHAPTER 7. INTERFACE CONSIDERATIONS

### KEY ASPECTS

**Interface requirements** - QR's vertical integration gives rise to a conflict of interest because of its ability to use rolling stock, safety and environmental requirements in the Undertaking to hinder access to its below-rail services, thereby protecting its above-rail business groups.

**Joint safety risk assessment** - all rolling stock interface, safety risk and additional training matters should be agreed between QR and a third-party operator during the joint safety risk assessment.

**Suspension** - QR should not be able to exercise a contractual right to suspend a third-party operator's staff or its rolling stock in any way contrary to s104 and s125 of the QCA Act and should bear the onus of demonstrating the reasonableness of any suspension action.

**Mediation** - the Rail Safety Accreditation Unit (RSAU) of Queensland Transport should provide non-binding advice to the parties regarding safety-related interface disputes.

**Environmental management** - to ensure consistency with Queensland's environmental regulatory framework, a third-party operator's environmental management system should be based on a risk assessment of its proposed train services and the identification of appropriate control measures to manage those risks. Accreditation under international standards is not necessary under the framework.

**Environmental audits** - QR and a third-party operator should provide each other with copies of the relevant parts of their respective internal audit reports.

**Non-compliance** - a third-party operator should be obliged to inform QR of non-compliance with its environmental management system and to take the necessary steps to address the non-compliance.

**Adjoining infrastructure** - the Undertaking should establish the scope of the interface to clarify the rights of QR and third-party operators regarding the design and construction of adjoining infrastructure.

## 7.1 Introduction

### *Rail Safety, rollingstock and operational requirements*

The strong interdependency between the rail infrastructure and delivery of above-rail services raises a range of interface issues associated with the interaction between QR, as network manager, and third-party operators. Key interface issues include the establishment of safety, technical, operational and environmental standards.

QR's proposed interface standards are important because they establish key non-price parameters within which Network Access will allow third-party operators to access QR's below-rail services. The QCA agrees with QR that in order to retain the integrity of the rail infrastructure, QR has an interest in ensuring that the interface is closely managed on a consistent basis. Nevertheless, the QCA is mindful that QR, as a vertically integrated provider, faces a conflict of interest in its ability to use the interface standards to hinder access to its below-rail services, thereby protecting the revenues of its above-rail operations. Consequently, in considering the interface provisions of QR's Draft Undertaking, the QCA has carefully balanced these competing interests.

The first part of this chapter discusses rail safety, rollingstock and operational interface requirements. Environmental requirements are discussed in the second part of the chapter.

### *Australian rail safety regulatory framework*

The Australian rail safety framework is based on the principle of co-regulation, with rail safety being managed jointly by government and industry.

Individual State and Territory Governments have autonomy in rail safety regulation, administered in accordance with relevant legislation in each jurisdiction. In 1996, Australian governments<sup>142</sup> signed an Inter-Governmental Agreement (IGA) which provided that legislation would be passed making AS 4292, representing a uniform rail safety standard, the basis for rail safety accreditation.<sup>143</sup> The IGA also provided that the parties would make provision under existing or new legislation for accreditation by an accreditation authority and for mutual recognition.<sup>144</sup>

The accreditation authorities that were subsequently established - generally within State Transport Departments - have developed Draft National Guidelines for Rail Safety Accreditation, which are aimed at achieving consistency in processing applications and simplifying mutual recognition requirements. In light of the efforts to achieve a nationally consistent approach to rail safety, the QCA's assessment of the rail safety and rollingstock provisions of QR's Draft Undertaking has recognised national developments in rail safety policy and its administration.

Under the co-regulatory framework, the performance of the accreditation function is separated from the performance of above-rail operations and below-rail infrastructure management. Track owners and rail operators, not the regulator, are responsible for the safety of their activities. The

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<sup>142</sup> Excluding the ACT.

<sup>143</sup> After the publication of Part 1 of AS 4292 in 1995, the following parts were published in 1997: Part 2, Track, civil and electric traction infrastructure; Part 3, Rollingstock; Part 4, Signalling and telecommunications systems and equipment; Part 5, Operational systems; and Part 6, Railway interface with other infrastructure.

<sup>144</sup> Mutual recognition is based on the premise that safety accreditation of a rail operator or rail owner in one jurisdiction should be acceptable in other jurisdictions.

regulator must be satisfied that track owners and rail operators have in place, and can demonstrate, an appropriate safety management system.

This separation of regulatory and commercial functions is consistent with the Competition Principles Agreement.<sup>145</sup> If a track manager and/or rail operator played a dual role of safety regulator and commercial train service provider, it would face a potential conflict of interest between advancing its commercial interests and advancing the wider public interest in rail safety through the exercise of its regulatory powers. This would present an opportunity for it to misuse control over regulatory standards to frustrate the actions of actual or potential competitors or to advantage its own operations.

### ***Queensland rail safety regulatory framework***

The Queensland rail safety framework is established in the *Transport Infrastructure Act 1994* (the TI Act), as amended by the *Transport Infrastructure Amendment (Rail) Act 1995*. The Chief Executive of Queensland Transport (QT) is responsible for administering the rail safety provisions of the Act. Rail safety policy, accreditation and performance monitoring have been delegated to the Rail Safety Accreditation Unit (RSAU) within QT.

Under the provisions of Part 4 of the TI Act, QT is required to accredit an applicant as a ‘railway operator’ to operate rollingstock on a railway if satisfied as to the following criteria:

- the applicant is accredited in another State to operate rollingstock on a railway for a similar type of service or has the competency and capacity to operate rollingstock on the railway safely;
- the applicant has an agreement with the railway’s manager to operate particular rollingstock on the railway, and the agreement includes appropriate arrangements for the safe operation of the rollingstock, unless the applicant is applying for accreditation as a railway manager and operator;
- the applicant has an appropriate safety management system; and
- the applicant has the financial capacity or public risk insurance arrangements to meet reasonable potential accident liabilities for the railway.

The establishment of an appropriate safety management system is also a requirement for accreditation of a railway manager (to manage rail transport infrastructure).

In considering a safety management system, QT is required to consider:

- the applicant’s rail transport proposal;
- the appropriateness of the safety management system for the proposal;
- the safety levels achievable, consistent with the nature of the proposal, at a reasonable cost;
- the need for efficient and competitive rail transport services;

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<sup>145</sup> Cl 4(3) of the Competition Principles Agreement states that before a party introduces competition to a sector traditionally supplied by a public monopoly, it will remove from the public monopoly any responsibilities for industry regulation. The party will re-locate industry regulation functions so as to prevent the former monopolist enjoying a regulatory advantage over its (existing and potential) rivals.

- consistency with generally accepted risk management principles; and
- the levels of safety proposed relative to the levels of safety of competing transport modes.

The TI Act allows QT to consider other matters at its discretion.

Finally, the Act establishes a range of procedures once accreditations are granted including, the imposition of conditions or amendments, the grounds for suspension or cancellation and provision of an opportunity for surrender.

### *QT's administration of legislative provisions*

In addition to the provisions of the TI Act, applicants seeking accreditation must develop their rail safety management systems in a manner consistent with the Australian Standard for rail safety management, AS 4292, and QT's 'Rail Safety Management within Queensland' manual, to RSAU's satisfaction.

The manual aims to assist railway managers and railway operators to develop safety accreditation applications in accordance with the TI Act. The manual translates the requirements of the TI Act and the AS 4292.1 standard into accreditation acceptance requirements, and provides guidance notes where necessary.

The manual states that accreditation applications must cover three main areas:

- the activities being undertaken;
- the risks associated with those activities; and
- the means applied to control the risks.

RSAU requires that applicants must be able to demonstrate they fully understand the safety risks of their operation and how the risks are managed through:

- an effective safety management system;
- clear assignment of safety responsibilities;
- competent staff undertaking safety activities;
- effective control of interfaces; and
- arrangements for monitoring and reporting safety performance.

In the context of third-party entry on QR's network, in order to satisfy itself of the effective control of interfaces, QT would require a third-party operator to provide a copy of a joint risk assessment it has undertaken in conjunction with the railway manager and the controls which are to be put in place to manage the identified risks.<sup>146</sup>

RSAU's manual states that a railway manager/railway operator's safety management system is the key component of accreditation. RSAU expects railway managers/operators to demonstrate they have the will, resources, competence and commitment to control risks and manage safety

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<sup>146</sup> As part of the accreditation requirements, applicants must demonstrate that they have addressed all interface issues, including those associated with level crossings, terminals, yards and stations.

processes. For each control mechanism within the safety management system (for example, document control, emergency planning) RSAU is looking for the railway manager/railway operators’:

- policy - for each given subject in the safety system;
- organisation – the person(s) responsible to discharge the policy and the training/competencies this person(s) requires;
- plan – as to how the policy will be achieved;
- monitoring – of what and how to ensure the plan is being enacted; and
- review – how and when the effectiveness of the policy, results and control mechanisms will be reviewed.

Implementation of the safety management principles requires compliance with a range of operational, infrastructure and rollingstock aspects, and recognition of the responsibilities of interfacing parties in respect of other transport modes.

Applicants also need to demonstrate that access rights to the rail network have been obtained before accreditation will be granted, and stipulate to the RSAU any requirements that need to be met as part of the access right, although in practice the two procedures proceed in parallel.

## 7.2 Establishment of rollingstock interface standards

### *QR’s Position*

QR will develop rollingstock interface standards (RIS) concerning rollingstock design and performance and the configuration of rollingstock to form a train. These standards will incorporate both safety and commercial constraints: sub-cl 7.1.1.

In order to ensure the integrity of its rail infrastructure, only rollingstock and rollingstock configurations complying with the RIS may operate on the rail infrastructure: para 7.1.1(a). QR argued in its Explanatory Guide that the RIS are not intended to specify detailed implementation methods, unless such methods or processes are critical to the effective management of risks, such as incidents involving the rail infrastructure/rollingstock interface. Rather the RIS are intended to specify the outcome that must be achieved to maintain compatibility with the rail infrastructure.

The preliminary information - refer Schedule D - that may be provided by QR to third-party operators will include preliminary information on applicable RIS for the purpose of assisting a third-party operator to make an initial assessment of its rollingstock requirements: para 7.1.1(d). QR has subsequently advised the QCA that it will be preparing information packs for each of its systems that, amongst other things, includes headline rollingstock parameters.<sup>147</sup> QR believes that the parameters should be sufficient to enable a potential third-party operator to assess business prospects and exposure to risks.

QR may consider variations to the RIS in response to the particular requirements of the third-party operator with respect to either its proposed rollingstock requirements or operating plan: para 7.1.1(e). A particular rollingstock configuration chosen by a third-party operator may

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<sup>147</sup> See section 4.5.2 of Chapter 4 for a discussion on the information packs.

impose additional costs on QR, such as greater wear and tear on the track. QR reserves the right to recover such additional costs from the operator: para 7.1.1(g).

Alternatively, where a third-party operator exclusively funds the additional costs of an agreed variation in RIS, QR reserves the right to restrict the benefits of the variation flowing to other rail operators until they make an appropriate contribution to the costs thereof: para 7.1.1(h). QR argued in its initial submission to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking* that it envisaged the nature of any operator’s contribution to upgrades being defined during the negotiation period and spelt out, along with any future entitlement to compensation from other future usage, in the operator’s access agreement. This would be a matter for commercial negotiation.

QR has proposed the following Schedule E principle to address situations where it may want to change the rollingstock interface standards:

- “QR may, acting reasonably, vary the rollingstock interface standards at any time and where this necessitates modification of the third-party’s rollingstock, the costs of such modifications are to be borne in the manner agreed by the parties or, failing agreement, as determined by an expert.”

### ***Stakeholder Comment***

There was a general concern that the RIS could potentially stifle innovation and/or act as a barrier to entry.

#### **Table 1: Nature of rollingstock interface standards**

**QMC** - the standards might constitute a barrier to entry and not permit arrangements that the rail safety regulator would permit. Network Access’ decisions on these matters must be able to be challenged. The standards should be divided into two parts:

- specifications that are unable to be altered or negotiated and are included in the Undertaking; and
- variable factors that are noted in the Undertaking as being negotiable.

**FreightCorp** - it is essential for the Undertaking to provide a mechanism for the RIS to be modified, over time, to incorporate new ideas. It would compromise the ability of Network Access to manage the infrastructure on an impartial basis if responsibility for the rollingstock interface - and other - standards is held by another group within QR.

There is a suite of standard tests accepted by industry bodies in Australia which should be sufficient to meet Network Access’ needs with regard to the performance of the rollingstock and which should be expressly incorporated in the Undertaking rather than the more generalised certification requirements that are currently presented. In addition, the Undertaking should not require each individual piece of rollingstock to be authorised.

**Stanwell** - the RIS should not be predefined, rather, it would be desirable if accreditation of rollingstock was based on the report of an independent expert other than one chosen by QR. If QR and/or the third-party operator disagreed with the expert’s findings then it could be referred to the QCA for resolution. RIS should not be a barrier to entry or stifle innovation and should be based on sound engineering practice and achieve appropriate performance and economic outcomes.

**AMC** - rather than have a predefined RIS which has the potential to stifle innovation, the Undertaking could provide for an independent expert to adjudicate on any disagreements.

**Toll** - the RIS should be consistent with ARTC standards as far as practicable.

### *QCA's Analysis*

The QCA recognises the importance of establishing minimum rollingstock standards for QR's rail network. Such minimum standards are the means by which QR ensures that a third-party operator's rollingstock is compatible with the rail infrastructure. This compatibility has both safety and commercial implications for QR. On the one hand, a rail operator's rollingstock must be able to operate in accordance with QR's safeworking procedures and safety standards. On the other hand, the rollingstock will impart wear and tear on QR's track.

The Draft Undertaking provides that only rollingstock and rollingstock configurations complying with the RIS may operate on the rail infrastructure. However, QR reserves the right to relax the rollingstock requirements in response to the particular requirements of a third-party operator. Nevertheless, under QR's proposal, the RIS will be the starting point for negotiations between QR and a third-party operator regarding the operator's proposed rollingstock for its train services.

The QCA notes stakeholder concerns that the RIS could act as a barrier to third-party entry and stifle innovation in the performance of train services by third-party operators. In assessing whether these outcomes are likely to eventuate, the QCA considers that the key test is the level of prescriptiveness of the RIS and the extent to which they address matters beyond the wheel-track interface. The wheel-track interface is important to QR in the context of third-party operators' rollingstock running on its network because of the safety and commercial interests referred to above. However, if the standards address matters beyond this interface, QR is essentially imposing an additional layer of regulation on third-party operators through prescribing the rollingstock characteristics a third-party operator must use on its network.

The RIS are composed of 30 standards, 5 of which are in draft form.<sup>148</sup> QR has advised the QCA that the RIS have been developed for QR's above-rail business groups rather than third-party operators. QR has indicated to the QCA that some of its existing rollingstock would not meet the proposed RIS, however, this is not required, as any rollingstock operating on the network prior to 1 March 1999 is considered registered.<sup>149</sup> In contrast, any new or modified rollingstock brought onto the network by either QR or a third-party operator since 1 March 1999 has to meet the RIS.

The QCA sought the views of Rail Management Services Pty Ltd and the RSAU concerning the nature of the proposed RIS. The preliminary view of these organisations was that, in general, the standards were very detailed and prescriptive and went beyond purely interface issues. For example, the matters addressed by the RIS include 'rollingstock interior environment', 'rollingstock cab layout' and 'requirements for hygiene on rollingstock'. It is not apparent to the QCA what safety or legitimate commercial interest QR is attempting to protect if such standards were to be imposed on third-party operators. This suggests that there is a clear potential for the RIS to both stifle innovation in third-party operators' train services and serve as a barrier to entry to the above-rail market.

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<sup>148</sup> (1) Rollingstock dynamic performance; (2) rollingstock/signalling interaction; (3) event recorders; (4) rollingstock visibility and audibility; (5) hazardous materials used on the rollingstock; (6) emergency equipment carried on rollingstock; (7) rollingstock interior environment; (8) requirements for hygiene on rollingstock; (9) electrical equipment for rollingstock; (10) rollingstock cab layout; (11) rail tank cars; (12) rollingstock structural requirements; (13) axle bearings for rollingstock; (14) passenger vehicle interior crashworthiness; (15) rollingstock drawgear; (16) rollingstock brake system requirements; (17) rollingstock brake system maintenance requirements; (18) structural requirements for railway bogies; (19) wheelset for rollingstock; (20) train safety systems; (21) rural fire management; (22) wheel defect identification and rectification; (23) wheels for rollingstock; (24) wheel set for assembly (25) axles for rollingstock; (26) kinematic and rollingstock outlines (draft); (27) steam locomotive technical requirements (draft); (28) pantagraph technical requirements (draft); (29) passenger vehicle access (draft); (30) fire requirements (draft).

<sup>149</sup> This issue is discussed in more detail in section 7.2.

In response to these concerns, QR has indicated to the QCA that while some aspects of the RIS might appear overly prescriptive, interface issues go beyond merely wheel-on-track issues and have to be considered in light of public and staff safety. QR further argued that the proposed RIS are a set of minimum as opposed to best practice standards.

It is apparent from the above discussion that third-party operators have a legitimate business interest in being consulted on the development of the RIS for QR's network and subsequently on an ongoing basis if variations are made to the standards. The QCA understands that QR has only conducted limited consultation with third-party operators regarding the development of the RIS.

Given that the Draft Undertaking provides that only rollingstock and rollingstock configurations complying with the RIS may operate on the rail infrastructure, the QCA is not prepared to endorse the RIS as part of the Draft Undertaking in the absence of a full public consultation process. It would be open to QR to submit a draft amending undertaking in the future that would provide the opportunity for such a consultation process to occur.<sup>150</sup>

Nevertheless, the QCA recognises that the nature of a third-party operator's rollingstock and rollingstock configurations for its proposed train services will always be a key interface issue to be resolved in any access negotiation process. Consequently, there needs to be a mechanism to allow for consideration of rollingstock interface matters. The QCA considers that the joint safety risk assessment that QR and the third-party operator must conduct as part of the safety accreditation process is the best mechanism to address rollingstock interface matters. The joint safety risk assessment is discussed in detail in section 7.5 below.

In the context of the joint safety risk assessment, the QCA sees merit in establishing some parameters for negotiations concerning rollingstock interface standards. The aim of these parameters would be to focus the negotiations on the critical rollingstock interface standards associated with the wheel-track interface. By doing so, it would constrain QR's ability to impose an additional layer of regulation on third-party operators through prescribing their rollingstock characteristics.

One way of establishing such parameters would be to prescribe - in place of the RIS - true minimum rollingstock interface standards for the network as part of the approval of QR's Draft Undertaking. However, the QCA believes that the development of minimum rollingstock interface standards prior to third-party entry on QR's network could result in an inappropriate set of prescriptive standards being established. This is particularly the case when the above-rail market in Queensland is at an early stage in its development. The development of prescriptive rollingstock interface standards would not be in the interests of either QR or access seekers. Alternatively, the completion of a number of joint safety risk assessments over the course of the first term of an approved undertaking would assist in the development of minimum rollingstock standards that could apply during future undertaking terms. The QCA would expect the arguments for and against the development of such minimum standards to receive particular attention at that time.

Nevertheless, in order to guide negotiations regarding minimum rollingstock interface standards, the QCA proposes the incorporation of a schedule to an approved Undertaking, which would provide a non-exhaustive list of relevant items. The proposed schedule would play a similar role to Schedule I in the Draft Undertaking, which provides a list of minimum requirements to be addressed in the assessment of environmental risks prior to the commencement of a third-party operator's train services.

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<sup>150</sup> QR has subsequently advised the QCA that if the RIS are not to be mandated, but rather would be subject to negotiation with third-party operators, then a consultation process is not necessary.

The QCA believes that the draft National Code of Practice for railway rollingstock provides a list of suitable minimum interface requirements that would form a schedule to an approved Undertaking. This draft National Code of Practice states that minimum interface requirements are those necessary for a vehicle to obtain access to a rail network and to ensure that the vehicle can safely complete transit over its intended route of operation. In simple terms this requires the vehicle to:

- remain on the track up to the permissible speed limit;
- negotiate the varied track elements and configuration without interference or fouling;
- clear track-side structures and infrastructure;
- activate the signalling system;
- stop from track speed within the required distances;
- retain its loading; and
- comply with environmental requirements.

By proposing the incorporation of the above list of requirements as a schedule to an approved Undertaking, the QCA does not intend to constrain the freedom of third-party operators to innovate with respect to rollingstock interface standards. In addition, the QCA recognises that negotiations between QR and third-party operators could extend beyond this list of items.

Finally, the QCA recognises that once a third-party operator is running its train services, Network Access may need to change the agreed rollingstock interface standards. For example, this may result from a serious accident on the network involving the third-party operator, or one involving another operator but with system-wide implications. However, the third-party operator is entitled to some protection regarding the process by which QR initiates changes in such interface standards.

To this end, the QCA believes that QR should be able to vary the agreed rollingstock interface standards at any time on safety grounds, however, the third-party operator should be consulted regarding the change(s). On the other hand, changes to the standards on any other grounds should be negotiated with the third-party operator.

The QCA believes that the following proposed change to QR’s revised Schedule E principle would provide additional protection to third parties with respect to changes in rollingstock interface standards agreed during the joint safety risk assessment:

- “QR may, acting reasonably, vary the agreed rollingstock interface standards at any time on safety grounds, after consultation with the third-party. Otherwise, QR may, acting reasonably, negotiate any other changes with the third-party. Where any changes in the standards necessitate modification of the third-party’s rollingstock, the costs of such modifications are to be borne in the manner agreed by the parties or, failing agreement, as determined by an expert.”

***QCA’s Position***

**The QCA would favourably consider an Undertaking that:**

- **removed the reference to the development of RIS for the rail infrastructure and the requirement that only**

**rollingstock and rollingstock configurations complying with the RIS may operate on that infrastructure; and**

- **incorporated a schedule to the Undertaking that provided the following non-exhaustive list of minimum interface requirements to guide negotiations regarding minimum rollingstock interface standards during the safety risk assessment so that any vehicle a third-party operator proposes to run on QR’s network should be able to:**
  - (a) **remain on the track up to the permissible speed limit;**
  - (b) **negotiate the varied track elements and configuration without interference or fouling;**
  - (c) **clear track-side structures and infrastructure;**
  - (d) **activate the signalling system;**
  - (e) **stop from track speed within the required distances;**
  - (f) **retain its loading; and**
  - (g) **comply with environmental requirements; and**
- **incorporated the following Schedule E principle:**
  - **“QR may, acting reasonably, vary the agreed rollingstock interface standards at any time on safety grounds, after consultation with the third-party. Otherwise, QR may, acting reasonably, negotiate any other changes with the third-party. Where any changes in the standards necessitate modification of the third-party’s rollingstock, the costs of such modifications are to be borne in the manner agreed by the parties or, failing agreement, as determined by an expert.”**

### 7.3 Appropriateness of QR’s role in authorising rollingstock

#### *QR’s Position*

To ensure that only rollingstock and rollingstock configurations complying with the RIS operate on the rail infrastructure, all rollingstock and rollingstock configurations must be authorised by QR: para 7.1.2(a). This requires a certificate of compliance be prepared by someone QR accepts as being competent to give certification, which may require commissioning tests be undertaken: para 7.1.2(b).

QR argued in its supplementary submission to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking* that the RSAU is required to accredit an applicant as a railway operator if it is satisfied, amongst other things, that:

- the applicant has an agreement with the railway’s manager to operate particular rollingstock on the railway, and
- the agreement includes appropriate arrangements for the safe operation of that rollingstock.

Consequently, QR argues that its RIS need to be complied with for an operator to gain and maintain accreditation.

### ***Stakeholder Comment***

A majority of stakeholders favoured an independent body authorising third-party operators’ rollingstock.

#### **Table 2: Authorisation of third-party operators’ rollingstock**

**AMC, QMC** - it should be the rail safety regulator - ie RSAU - not QR.

**FreightCorp** - safety regulation of the network is the sole responsibility of RSAU.

**QMC** - QR does not currently require certificates of compliance for rollingstock operating on the interstate part of its network.

**Queensland Government** - QR should provide its interface standards in the Undertaking and Queensland Transport should ensure operators comply and carry out commissioning tests.

**Stanwell** - if the recommendation of the independent expert is that a third-party operator’s rollingstock and its configuration meets the standards, then QR should be obliged to authorise the rollingstock and configurations.

### ***QCA’s Analysis***

QR has developed an internal mandatory standard ‘Rollingstock Acceptance, Validation and Registration’ (STD/0068/TEC) (known within QR as ‘Standard 68’) within its safety management system, effective from 1 March 1999. QR states that the purpose of Standard 68 is to provide:

- a means of assuring that new or modified rollingstock complies with the requirements of QR’s technical standards and specifications in its safety management system prior to operation of that rollingstock on QR’s track; and
- that all rollingstock which is permitted to operate on QR’s track is registered with its capabilities.<sup>151</sup>

Standard 68 provides a means of validating an alternative method for controlling a rollingstock related hazard to an acceptable level of risk if technologies equivalent to those dictated by a rollingstock-related standard or specification are proposed.

It is important to note that Standard 68 does not apply to rollingstock running on QR’s network prior to 1 March 1999. In other words, the detailed validation procedures established in Standard 68 have not been applied to the majority of QR’s rollingstock.

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<sup>151</sup> Standard 68 requires the completion of the following: a validation and compliance plan; a certificate of design conformance; a certificate of construction conformance; a certificate of conformance – acceptance testing; and supply of registration details.

QT has advised the QCA that it does not authorise individual items of rollingstock as part of the accreditation process for a rail operator. It regards this task as the responsibility of the rail operator. However, the operator will not gain accreditation until it has demonstrated that it has appropriate processes in place for all rollingstock safety issues, including design, testing, commissioning and compatibility. Standard 68 should be seen as QR, in its role as a rail operator, fulfilling part of QT's requirements in this regard. However, the QCA does not believe that QR should impose this standard on a third-party operator as that party may choose to meet QT's requirements in a different way and, moreover, as noted in section 7.1, the majority of QR's own rollingstock does not meet the standard.

QT believes that its requirements - which are in accordance with the AS 4292 standard – make it unnecessary for independent authorisation by RSAU or any other body, unless the rail operator itself determines that it does not have internal expertise. The operator's decision whether it had such expertise or not would be subject to RSAU's satisfaction. Consistent with this approach, QT has advised the QCA that it does not require QR's above-rail business groups to have independent authorisation of their rollingstock. QT has also indicated that QR does not place any requirement on its own above-rail business groups to have independent approval of rollingstock and has argued strongly against this in the past.<sup>152</sup> Standard 68 does not require independent authorisation.

The QCA agrees with QT's argument that as part of gaining accreditation a third-party operator would have to demonstrate that it has qualified and competent staff who are able, amongst other things, to select a party competent to provide certification for its rollingstock. In the current rail safety regulatory environment, QR reserving itself the right both to approve the party that provides a certificate of compliance to the third-party operator and reserving an open ended right to require a commissioning test be undertaken, could clearly be seen as unnecessarily intrusive.

Consequently, the QCA believes that QR and a third-party operator should agree on a party competent to provide certification for the operator's rollingstock. This would likely occur prior to or during the joint safety risk assessment process. However, the QCA does not accept that QR should also have the right to require a commissioning test be undertaken. Such an open ended right has the potential to unreasonably extend the time required to complete the authorisation process, at no cost to QR and significant cost to the third-party operator.

QR would be entitled to view the third-party operator's certificate that its rollingstock and rollingstock configurations meet the standards agreed as part of the safety risk management plan in order to protect its legitimate business interests.<sup>153</sup> Where particular rollingstock configurations chosen by a third-party operator impose additional costs on QR (eg greater wear and tear on the track), QR may impose a correspondingly higher access charge. In addition, registration of a third-party operator's rollingstock provides the basis for QR to enforce compliance with the rollingstock standards established in an access agreement.

The QCA believes that scope clearly exists for commercial disputes over a third-party operator's rollingstock characteristics, given that measuring rollingstock performance is not an unambiguous task. The dispute resolution procedures established in the Draft Undertaking - or the QCA Act's arbitration process in the absence of an approved Undertaking - provide an independent forum for resolution of such disputes. Disputes over rollingstock interface safety issues are discussed in section 7.4 below.

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<sup>152</sup> Refer to QT's submission in QR's *Submission of Draft Undertaking* (December 1998) document.

<sup>153</sup> The safety risk management plan agreed between QR and a third-party operator concerning interface matters is the outcome of a joint safety risk assessment by the two parties. This issue is discussed in detail in the next section of this chapter.

Under the authorisation approach proposed above, the QCA believes that QR's legitimate business interests would be protected. This is because any concerns it may have with the standard of a third-party operator's rollingstock are resolved through its right to agree to the authorisation party, view the operator's relevant certificates and negotiate the price of access. A third-party operator's interests would be protected because it would have prime responsibility for authorising its rollingstock, which is consistent with the current rail safety regulatory environment in Queensland. Moreover, QR would not play a role as a rollingstock regulator.

***QCA's Position***

**The QCA would favourably consider an Undertaking that:**

- **provides that QR and a third-party operator should agree on a party competent to provide certification for the operator's rollingstock and reserves QR's right to seek documentation – eg certificates of compliance - from a third-party operator in order to confirm that the rollingstock/rollingstock configurations for its proposed train services are as agreed by the two parties in the safety risk management plan.**

#### **7.4 Appropriateness of QR's right to suspend the use of a third-party operator's rollingstock**

***QR's Position***

QR's revised Schedule E principles proposed the following:

- the third-party is responsible for the safe operation of its rollingstock on the nominated network and must ensure that at all times its rollingstock and rollingstock configurations comply with all applicable laws, the rollingstock specification and the rollingstock interface standards specified in the agreement. The operation of rollingstock and trains may be suspended by QR, acting reasonably, for non-compliance until such non-compliance is rectified.

QR argued that because of the implications for the safety of all operators on the network, it must be in a position to suspend an operator's rollingstock if it does not comply with the rollingstock specification or rollingstock interface standards, which are primarily directed at the safety of operations on the network. Any departure from this approach compromises the safety of operations on the network.

Furthermore, the proposed Schedule E principle already stipulates that QR must act reasonably in exercising any right of suspension.

***Stakeholder Comment***

A paper prepared by stakeholders<sup>154</sup> in April 2000 outlining the principles they considered should be included in a revised Schedule E, included the following principle regarding QR's proposed right to suspend a third-party operator's rollingstock:

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<sup>154</sup> FreightCorp, National Rail, Toll, QMC, AMC, Stanwell and Ensham Resources.

- the third-party operator must ensure all loadings of rollingstock are secure and comply with the requirements of the rollingstock interface standards and rollingstock specification in the access agreement. QR must be allowed to suspend access rights where it becomes aware that there is non-conformance, and such non-conformance has a materially negative impact on the operation of the network, not where it merely suspects non-conformance.

Also, in the context of QR's revised Schedule E, FreightCorp advised the QCA it accepted Network Access must have the right to suspend rollingstock if non-compliance with an access agreement creates a 'genuine' safety issue. If the non-compliance does not have safety implications, the operator should be required to rectify the issue within a reasonable period of time, but not be suspended. Moreover, in order to prevent QR using issues regarding a third-party operator's accreditation as a mechanism to frustrate access, access holders should have a direct contractual right against QR under these circumstances.

### *QCA's Analysis*

The QCA recognises QR's view that it should have a right to suspend a third-party operator's train services and that the exercise of this right would be subject to a reasonableness test. This potentially provides some protection to third-party operator's interests. Nevertheless, the Authority believes that stakeholders have legitimate concerns that QR, as a vertically integrated service provider, could exercise its suspension power such that it frustrates third-party access. Moreover, suspension of a third-party operator's rollingstock could have very serious adverse commercial implications for it.

The QCA believes that, in practice, QR's response to rollingstock non-compliance should depend on whether there are safety implications or not. If the source of non-compliance does not have safety implications, the third-party operator should be required to rectify the non-compliance within a reasonable period of time, but not be suspended. This is because the continued operation of the rollingstock would not cause an unacceptable safety risk. Clearly, the length of the reasonable period to address the non-compliance would depend on the nature of that non-compliance, including the extent to which QR's infrastructure was being adversely affected. A reasonable period may well be immediately. For example, an operator could be required to cut an over-loaded wagon out of the train consist before it commenced its service.

Regardless, a third-party operator that did not subsequently rectify demonstrated non-compliance of its rollingstock and trains would not be protected. The QCA would expect agreed contractual penalty arrangements to apply in such a situation. This could include liquidated damages, for example, for overloading or coal contamination.

In contrast, the QCA accepts that situations could arise where it is prudent for QR to suspend a third-party operator's train services on safety grounds, notwithstanding that the evidence may be ambiguous. However, the Authority also recognises it will only be after QR has initiated a suspension that the reasonableness of its actions could be assessed. The QCA does not support suspensions being made on 'genuine' safety considerations, because of the practical difficulty in differentiating between a 'genuine' and 'non-genuine' safety consideration.

The QCA understands that if an approved undertaking were to allow QR to oversee matters of rail safety accreditation or regulation, such as suspension of rollingstock, QR could potentially use this power to restrict or hinder access and then argue that it was an act done in accordance with the Undertaking. This would be possible because s104 and s125 provide that an act done in accordance with an approved undertaking does not amount to a hindering or restriction of access.

Consequently, in order to constrain QR's ability to use its suspension power in an anti-competitive manner, the following obligation should be imposed on QR. Wherever QR establishes an oversight power in the undertaking with respect to matters of rail safety accreditation or regulation, it would not be able to exercise the power to hinder or restrict access to the service in any way contrary to s104 and s125 of the QCA Act. The QCA proposes that this obligation would apply in relation to QR's rollingstock suspension power. This would mean that a third-party operator believing that the suspension power had been used against it in an anti-competitive manner could take legal action against QR under the Act and request that the Court exercise its discretion to order an injunction, compensation or make any other order that it considers appropriate.

The suspension of a third-party operator's rollingstock could be a source of dispute. In such an event, in the absence of an alternative dispute resolution process agreed between the parties, the dispute resolution processes outlined in clause 4.9 of the Draft Undertaking could be triggered. The QCA believes the option provided under sub-clause 4.9.3 for the parties to agree to refer a dispute to an independent expert for resolution in the form of a binding decision, would be a good one. In such a case, the QCA would expect the decision to address the appropriateness of the suspension of the rollingstock and what action, if any, would be required to lift the suspension. The QCA understands that the Institution of Engineers has a standing committee that could hear such matters. The benefit of such an option would be to facilitate a quicker resolution of the matter than the QCA Act's formal dispute resolution procedures would allow.

To provide additional legal protection to third-party operators, the QCA proposes a contractual right to prevent QR suspending their rollingstock in order to frustrate access. The QCA believes that this would better protect the interests of third-party operators, as a breach of such a term would give third-party operators a right to claim damages for breach of contract, rather than being limited to rely on the Court to exercise its discretion to award compensation in an action under the QCA Act. The QCA does not believe that this would harm QR's legitimate business interests, but would rather increase the onus of responsibility on QR to demonstrate that its actions had a reasonable foundation. The third-party operator's right would be that if its rollingstock was suspended without reasonable justification, then QR would be liable for the loss thereby caused.

Finally, the QCA believes that its proposal for QR to reassign management responsibility for train control from QR's above-rail business groups to Network Access at four of QR's five train control centres should lessen the possibility that QR's rollingstock suspension power would be used in an anti-competitive manner.<sup>155</sup>

#### ***QCA's Position***

**The QCA would favourably consider an Undertaking that incorporated the following Schedule E principles:**

- **“The third-party is responsible for the safe operation of its rollingstock on the nominated network and must ensure that at all times its rollingstock and rollingstock configurations comply with all applicable laws, the rollingstock specification and the rollingstock interface standards specified in the Agreement.**

<sup>155</sup> The assignment of management responsibility for train control is discussed in Section 3.2 of Chapter 3.

- **QR may suspend the operation of rollingstock and trains for demonstrated non-compliance that has safety implications until such non-compliance is rectified. If the source of non-compliance does not have safety implications, the third-party should be required to rectify the non-compliance within a reasonable period of time, but not be suspended. If the non-compliance is not rectified within a reasonable period, QR may suspend the operation of the affected rollingstock and trains.**
- **QR will not exercise its suspension power in relation to a third-party’s rollingstock and trains in such a manner as to hinder or restrict access to the declared service in any way contrary to s104 and s125 of the QCA Act.**
- **If the suspension of a third-party operator’s rollingstock and trains becomes a source of disputation, in the absence of an alternative dispute resolution process agreed between the parties, the Undertaking’s dispute resolution procedures could be triggered.**
- **A third-party operator could reserve the right that if its rollingstock is suspended without reasonable justification, then QR would be liable for the loss thereby caused.”**

## 7.5 Preparation of joint safety risk assessment by QR and a third-party operator

### *QR’s Position*

A third-party operator shall, jointly with QR, conduct a safety risk assessment of its operations insofar as they interface with the rail infrastructure: para 7.3(a). The safety risk assessment should identify all reasonably foreseeable hazards relating to the interface between the third-party operator, QR and other railway operators arising out of the proposed operation of train services and the risks and implications of such hazards occurring: para 7.3.1(d).

Only a preliminary assessment need be conducted prior to execution of an access agreement, but a final safety risk assessment, conducted by a suitably qualified person reasonably acceptable to both parties, must be completed prior to the operation of train services on the rail infrastructure: para 7.3.1(b).

To address the results of the safety risk assessment, a safety risk management plan is to be developed and agreed between the third-party operator and QR prior to the operation of train services: para 7.3.2(a).

Prior to the operation of the third-party operator’s train services, QR and the third-party operator shall ensure that their respective safety management systems incorporate the elements of the safety risk management plan that each is responsible for implementing. The third-party operator shall also incorporate necessary processes for ensuring that its rollingstock and train services at all times comply with the safety requirements of the access agreement, including the safeworking procedures and other applicable safety standards: para 7.3.2(b).

The implementation of the safety risk management plan may necessitate changes in the terms and conditions of the access agreement, including variations to the access charge and the RIS.

QR’s revised Schedule E requires that:

- “the third-party is responsible for demonstrating through the safety risk assessment process the competence of all of its staff involved in safety-related work. Also, QR reserves the right to temporarily suspend the right of the third-party’s staff to operate on the nominated network in the event of breach or likely breach of any laws, QR train control directions, safeworking procedures or safety standards.”

### **Stakeholder Comment**

The main theme to emerge in stakeholder comments was that RSAU is the appropriate body to deal with rail safety issues in Queensland.

#### **Table 3: Safety roles of QR and RSAU**

**National Rail, Toll** - the Undertaking needs to more clearly delineate the roles of QR and RSAU as far as rail safety is concerned.

**National Rail** - while it is acceptable for QR to require preparation of a safety risk management plan and to be consulted in its preparation, two provisos must apply: Network Access must be responsible for all QR input; and where there is disagreement between QR and the third-party operator, QT must be empowered to provide a final decision on the adequacy of the safety risk management plan.

**FreightCorp** - it is sufficient for Network Access to require an operator to be accredited prior to commencing train services for QR to have fulfilled its obligations.

**Queensland Government** - the Undertaking should address the situation where if QR and the operators agree on interface risk assessments only, the RSAU will ensure the safety issues for QR and the operator are addressed.

**QMC** - the Undertaking’s focus on managing the interface risks should not cut across broader rail safety obligations under AS 4292 and cause confusion.

**ARTC** – we require operators to meet their responsibility under the rail safety regime in the relevant state to become safety accredited and adhere to all operating requirements of the relevant rail safety legislation. Beyond this, we require through our agreements that the operator has responsibility for ensuring any rollingstock is in ‘fit for use’ condition, as per the Railways of Australia (ROA) Manual of Engineering Standards and Practices (the Rollingstock Manual).

Stakeholder comments were received regarding QR’s requirements in relation to third-party operators’ staff in response to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking*.

#### **Table 4: Third-party operators’ staff**

**Queensland Government** - QR should put in place safety requirements, however, the QCA should ensure that these requirements are not onerous or unduly restrict access. The requirement for the third-party operator to be ‘responsible for the health and safety of its staff and their property’ should be qualified to relate strictly to health and safety as it relates to their employment. In addition, the reference to QR having the right to temporarily suspend a third-party operator’s staff if they breach ‘any law’ should be restricted to laws relating to the operation of a safe railway.

**National Rail** - the third-party operator should not be required to demonstrate the competence of all staff, provided they are covered by the operator’s accreditation under the *Transport Infrastructure Act 1994*.

**AMC**- if a third-party operator is accredited by the Department of Transport under the *Transport Infrastructure Act 1994*, then it would be inappropriate for QR to have such

powers. If QR has concerns regarding staffing, then these could be referred to the Department of Transport for consideration.

**QMC** - Australian rail standards and safety law will stipulate minimum staffing and skill requirements, and these will be implicit in an operator's accreditation. It should not be up to QR Network Access to require additional demonstration of staff competence or to intervene to suspend staff in the event of a perceived breach of its procedures.

**Toll** - the requirements are excessive.

**FreightCorp** - it is reasonable that all staff associated with train operations be appropriately qualified. We would not have difficulty with the requirements in the standard agreement regarding this matter.

**RTBU** - QR's requirements can hardly be called excessive. This is required of QR itself, for over-riding employee and public safety reasons. The QCA is required to address and uphold public interest issues and their cost cutting approach to training must be rejected. The need for all rail employees, regardless of employer, to have competencies as specified in the Transport and Distribution Training Board Packages is strongly endorsed. QR is doing this, as should all other operators on competitive neutrality grounds.

**AMC, Ensham Resources, FreightCorp, National Rail, Toll, QMC, Stanwell** - all staff should be appropriately accredited. The obligation should be reciprocal. QR should not have the right to require additional training obligations over and above the accreditation requirements. This is a cost issue for an access holder, which must be clearly identified and dealt with prior to entering into an access agreement.<sup>156</sup>

### *QCA's Analysis*

The QCA considers that clarification of the allocation of responsibilities between QR, in its role as track manager, third-party operators and RSAU is the key to determining a set of safety provisions in the Draft Undertaking that balance QR's legitimate business interests and the interests of access seekers.

#### *Scope of rail interface*

As previously noted, under the Australian co-regulatory rail safety framework, the performance of the accreditation function is separated from the performance of rail operations and infrastructure management. Under this framework, the safety role of the track manager is confined to addressing interface issues.

In broad terms, for railway operations there are a wide range of interfaces between the engineering and operational functions. The interfaces include:

- track gauge and tolerances;
- curve and gradient data;
- electrical system parameters;
- vehicle and load dimension, including tolerances, limits and clearances;
- axle load capacity;
- location and configuration of track, including points and crossings;

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<sup>156</sup> This comment was made in a paper prepared by stakeholders in April 2000 outlining the principles they considered should be included in a revised Schedule E.

- safeworking system procedures;
- emergency procedures; and
- train control arrangements and procedures.

The RSAU has advised the QCA that it does not consider that it is possible to provide a definitive list of interface issues because they will vary depending on the nature of the train services.

In the context of a third-party operator seeking to run its train services on QR's network, the interface covers all areas where the respective parties' rail operations interact. As part of the accreditation process, the RSAU would require that a third-party operator provide a copy of a risk assessment it has undertaken in conjunction with QR identifying the risks associated with the interface between their respective operations and the controls which are to be put in place to manage the identified risks. The document that will emerge from the conduct of a safety risk assessment and development of a safety risk management plan in accordance with sub-clauses 7.3.1 and 7.3.2 will be equivalent to the joint risk assessment document required by RSAU.

RSAU has advised the QCA that it does not believe that QR should prescribe set standards for interface issues. Rather, QR may wish to put forward the standards it currently uses in the joint risk assessment process in an effort to determine their suitability for the third-party operator's proposed train services. The QCA supports such an approach, subject to the standards put forward by QR being solely interface standards, considering that it reduces the potential for third-party operators to be faced with an unnecessary additional layer of regulation.

#### *Disputes over interface issues*

Nevertheless, the QCA considers that, in practice, there may be some difficulty in clearly defining the scope of the interface between QR and a third-party operator. This creates the potential for the joint risk assessment to be a source of disagreement between the two parties. For example, QR may believe that a third-party operator is not appropriately identifying an interface issue. Alternatively, a third-party operator may believe that QR is attempting to impose an inappropriate standard or is interfering in non-interface issues. The RSAU does not have any legislative power to arbitrate in such a dispute. Moreover, until an outstanding interface issue is resolved, a third-party operator would not be granted accreditation.

The QCA, RSAU and QR have engaged in a series of discussions in an attempt to address this potential problem. All parties accepted that recourse to formal arbitration under the QCA Act, with its associated adverse time and cost implications for QR and third-party operators, would not be the best means of resolving disputes over what might or might not be a safety-related interface issue. In contrast, all parties agreed that a dispute resolution process outside the formal procedures outlined in Part 4 of the Draft Undertaking or the QCA Act's arbitration procedures could be of benefit to both QR and third-party operators. This alternative process would only deal with safety related interface issues, as opposed to commercial interface issues.

The alternative dispute resolution approach favoured by the QCA, RSAU and QR is similar to the one QR has proposed in Part 4 of the Draft Undertaking. In the event of a dispute over a safety related interface matter, the Chief Executive Officers (CEOs) of the two organisations would meet to try and resolve the issue. If the CEOs could not reach a resolution after 14 days,

the matter would be referred to the RSAU, which would provide non-binding advice to the two parties.<sup>157</sup>

The potential exists under this alternative dispute resolution model for trivial disagreements to be brought to the RSAU for resolution. Such an outcome would undermine the intent of the model and likely place an unnecessarily heavy burden on RSAU in terms of the demand on its time and resources. However, the QCA believes that, in practice, it would not be in the long-term interests of either QR or third-party operators to abuse the dispute resolution process by referring trivial matters to the RSAU.

#### *Third-party operator's staff*

QR's revised Schedule E proposal regarding third-party operators' staff is best broken down and considered as two discrete matters. First, the party who should be responsible for assessing the competence of such staff and second, QR's right to suspend such staff for actual or likely safety breaches.

In discussions between the QCA, QR and RSAU, QR supported its requirements regarding the competence of third-party operators' staff by arguing that RSAU's safety accreditation process is undertaken at too high a level for it to have full confidence in the safety credentials of third-party operators. In particular, while local conditions on QR's network will impinge on the ability of third-party operators' staff to safely undertake their activities, the nature of RSAU's process is such that these would not be addressed. For example, QR argued that RSAU does not check a train driver's route knowledge, which it considers to be a critical safety issue.

RSAU considers that it is a requirement of the accreditation process that railway operators and managers demonstrate that procedures are in place for worker competence. The QCA understands that a railway operator could choose to demonstrate its workers' competencies by reference to the national rail competencies developed by the Transport and Distribution Industry Training Advisory Board. The joint safety risk assessment would identify any additional training requirements necessary to address interface issues. Driver route knowledge could be considered to be such a requirement. However, RSAU considers that it is not QR's role to check a third-party operator's staff competency levels or qualifications. Once an operator is accredited, QR should be satisfied that the operator's staff are trained and competent. Similarly, given QR is an accredited organisation, an operator should accept that QR's staff are trained and competent.

The QCA accepts QR's arguments about the importance of driver route knowledge. However, the Authority considers that QR's revised Schedule E proposal concerning third-party operator's staff competence is too broadly defined and, as a result, fails to satisfactorily differentiate between QR legitimately collaborating with operators on interface safety issues and duplicating the work of the RSAU. Moreover, it creates the potential for QR to interfere in the internal safety management decisions of third-party operators.

In order to reduce the scope for duplication and provide additional certainty to third-party operators, the QCA proposes that an approved Undertaking should provide that QR and a third-party operator would agree upon any additional training requirements for the latter's staff during the safety risk assessment process. Beyond driver route knowledge, QR has not been able to identify any additional training requirements it would expect third-party operators to meet.

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<sup>157</sup> There would be nothing to stop QR and a third-party operator reaching agreement on an alternative dispute resolution process. For example, the parties might prefer to refer the safety interface matter to a mediator prior to it being referred to the CEOs of the respective organisations.

Nevertheless, any disagreements over such requirements should trigger the informal safety dispute resolution process.

In addition, the QCA proposes that QR should specifically make a ‘reasonable endeavours’ commitment to assist a third-party operator meet any additional training requirements agreed during the joint safety risk assessment. This matter is discussed in more detail in section 7.6 below.

QR reserving itself the right to temporarily suspend a third-party operator’s staff as a result of actual or likely safety breaches raises a number of sensitive matters regarding the respective safety responsibilities of QR and RSAU.<sup>158</sup> In addition, its application would have similar potential effects as QR’s proposed right to suspend a third-party operator’s rollingstock, discussed in section 7.4.

The QCA recognises that there will be situations where it is prudent for QR to act to prevent a safety breach occurring rather than wait for the breach to occur and then take action. Similarly, QR, as network manager and having responsibility for train control, may be better placed than RSAU to respond to, or prevent, the occurrence of a safety breach in a timely manner. For example, QR’s train control could refuse to allow a scheduled train to commence its train services because its driver was seen consuming alcohol shortly before the train’s departure time.

As with QR’s proposed right to suspend a third-party operator’s rollingstock, the QCA recognises that QR could exercise its proposed suspension right regarding third-party operator’s staff such that it frustrates third-party access. Nevertheless, it would only be after QR has initiated a suspension that the reasonableness of its actions could be assessed. For example, QR’s suspicion that a third-party operator’s train driver was drunk could be subsequently proven to be without foundation and/or false.

However, as discussed with respect to the suspension of rollingstock, the QCA understands that if an approved Undertaking were to allow QR to oversee matters of rail safety accreditation or regulation, QR could potentially use such a power to restrict or hinder access and then argue that it was an act done in accordance with the Undertaking.

Consequently, the QCA believes that in order to protect access seekers’ interests, QR should commit that it would not exercise its proposed suspension right for third-party operators’ staff to hinder or restrict access to the declared service in any way contrary to s104 and s125 of the QCA Act. This would mean that a third-party operator believing that the suspension power had been used against it in an anti-competitive manner could take legal action against QR to seek financial recompense.

Finally, the QCA believes that third-party operators should have additional protection through access to a contractual right to prevent QR from exercising its suspension right with respect to that operator’s train services in order to frustrate access. The third-party operator’s right would be that if a member of its staff was suspended without reasonable justification, then QR would be liable for the loss thereby caused. This proposed contractual right would be identical to the one discussed in section 7.4 aimed at preventing QR suspend a third-party operator’s rollingstock in order to frustrate access.

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<sup>158</sup> In practice, QR would not strictly be suspending the third-party operator’s staff, but rather suspending that operator’s train services associated with the staff member who is the subject of QR’s safety concerns. For example, a particular train driver employed by the third-party operator.

***QCA's Position***

The QCA would favourably consider an Undertaking that:

- recognised that QR's role in the preparation of a third-party operator's safety risk assessments should not extend beyond preparation of the joint safety risk assessment;
- provided for the following dispute resolution process for safety-related interface matters:
  - following receipt of written notice from either party notifying the other party of a safety-related interface matter, the Chief Executive Officers (CEOs) of the two organisations would meet to try and resolve the matter;
  - if the CEOs could not reach a resolution after 14 days of receipt of the written notice, the matter would be referred to the RSAU which would provide non-binding advice to the two parties;
  - if the RSAU's advice did not facilitate resolution of the dispute, the matter would be referred to the QCA for arbitration under the QCA Act;
- provided that QR and a third-party operator would agree any additional training requirements for the third-party operator's staff during the safety risk assessment process; and
- incorporated the following Schedule E principles:
  - “QR reserves the right to temporarily suspend the right of the third-party's staff to operate on the nominated network in the event of breach or likely breach of any laws relating to rail safety, QR train control directions, safeworking procedures or safety standards. QR will not exercise this suspension power in such a manner as to hinder or restrict access to the declared service in any way contrary to s104 and s125 of the QCA Act.
  - A third-party operator could reserve the right that if its staff are suspended without reasonable justification, then QR would be liable for the loss thereby caused.”

## 7.6 Appropriateness of QR providing assistance to prospective third-party operators to fulfil the Draft Undertaking’s rollingstock and safety requirements

### *QR’s Position*

QR has not addressed this issue in the Draft Undertaking or its submissions in response to the QCA’s Request for Comments Paper *Queensland Rail Draft Undertaking*.

### *Stakeholder Comment*

There was support for QR to provide assistance to third-party operators, however, alternative views were expressed.

#### **Table 5: Assistance for third-party operators**

**FreightCorp** - QR could assist operators by providing information as to the systems that QR has in place, and with which an operator would need to conform, in order to meet the accreditation requirements.

**Toll** - there should be a positive obligation on QR to supply any information that is reasonably necessary for third-party operators in relation to rollingstock, safety management and interface standards.

**QMC** - if Network Access is to go beyond describing rollingstock standards, then Network Access should explain how it arrives at those requirements and assist the operator to satisfy them and other conditions.

**Stanwell** - provided the safety management and interface standards for rollingstock are clearly defined in the Undertaking then third-party operators should not require QR’s assistance.

**AMC** - a third-party operator possessing the necessary bona fides should not require QR’s assistance in fulfilling these requirements.

**Queensland Government** - it is not appropriate for QR or the RSAU to provide assistance over and above the provision of sufficient guidance and information to facilitate the meeting of these standards.

### *QCA’s Analysis*

The QCA considers that QR’s obligations to provide assistance to third-party operators concerning fulfilment of the Draft Undertaking’s requirements on rollingstock and safety management can be addressed through providing information:

- in response to access inquiries; and
- during the joint safety risk assessment;

and through a ‘reasonable assistance’ commitment to meet additional training requirements identified during the joint safety risk assessment.

Schedule D (preliminary information) foreshadows the provision of technical and operational information regarding, amongst other things, rollingstock interface requirements, to access seekers. As discussed in Chapter 4, QR has advised the QCA that in order to meet part of its Schedule D commitment, it intends to prepare Information Packs for each rail system on its network incorporating the relevant technical and operational information. These Information Packs would include information of a nature suitable for access seekers not already running train services on the particular rail system.

The QCA argued in Chapter 4 that it is important an Information Pack does not give a misleading impression of the potential operational capabilities of a particular system such that it conveys existing QR configurations as binding technical/operational limits where this is not the case. QR should be prepared to negotiate with third-party operators regarding operational differences where this is feasible.

Once an access seeker has moved beyond the initial access application stage, it will require rollingstock and rail safety information of a more detailed nature. Schedule D (additional information) commits QR to provide the rollingstock standards and train standards applicable for the system(s) on which the third-party operator's train services will run. As noted earlier in this chapter, the QCA is not prepared to endorse the RIS without a full public consultation process. Nevertheless, there is no reason why QR cannot provide a copy of its rollingstock interface standards to a third-party operator in order for that operator to assess their relevance to its proposed train services as part of the joint safety risk assessment process. Indeed, provision of such standards would be obligatory if QR sought to impose any of them on a third-party operator.

The QCA also believes that an obligation on QR to provide all relevant information as part of the joint safety risk assessment is necessary to protect a third-party operator's interests. Under the negotiation framework proposed in Part 4, a third-party operator who has received an indicative access proposal and indicated an intention to progress its access application enters the formal negotiation process with QR.<sup>159</sup> In the negotiation period, the third-party operator will be required to provide additional information to QR in order for it to develop an access charge and terms and conditions for acceptance.<sup>160</sup> This additional information includes preparation of a safety risk assessment by the third-party operator jointly with QR.<sup>161</sup>

In order for the third-party operator to conduct the safety risk assessment, it will need to understand all relevant aspects of QR's safety management system, including the safeworking standard and rules applying on the corridor(s) of interest. This is because it will have to demonstrate to RSAU as part of gaining accreditation that it fully understands the safety risks of its operation and that the identified risks are adequately managed. Consequently, an obligation on QR to provide information to a third-party operator on all relevant aspects of its safety management system would protect the interests of that operator.

As discussed in section 7.5, the QCA has proposed that the Undertaking should provide that QR and a third-party operator would agree upon any additional training requirements for the third-party operator's staff during the safety risk assessment process. The QCA believes that QR, in its role as network manager, would likely initiate discussions regarding the need for such additional requirements. Consequently, it is reasonable for QR to accept some level of responsibility to assist a third-party operator meet them. Moreover, QR is in the best position to provide assistance.

The level of required assistance would clearly depend on the nature of the requirement. For example, if it was agreed that a third-party operator's drivers must have route knowledge and a suitable demonstration of this was that the driver, accompanied by a tutor, actually took control of a train over the route, then QR should supply the tutor. Alternatively, if it was agreed that driving a car and walking alongside the track along the designated route was sufficient to gain route knowledge, then the extent of the assistance required would be to ensure the third-party operator could access the rail corridor for inspection purposes. Consequently, the QCA believes

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<sup>159</sup> Clause 4.7.

<sup>160</sup> Sub-paragraph 4.5(a)(vii).

<sup>161</sup> Sub-clause 4.7.2.

that QR should provide a ‘reasonable endeavours’ obligation to third-party operators regarding additional training requirements.

***QCA’s Position***

The QCA would favourably consider an Undertaking that:

- inserted a provision with respect to sub-clause 4.7.2 committing QR to provide to a third-party operator, on a timely basis, all information relevant to the joint safety risk assessment during the negotiation period; and
- inserted a provision committing QR to provide a ‘reasonable endeavours’ commitment to assist a third-party operator meet any additional training requirements for its staff identified during the safety risk assessment process.

**7.7 Annual audits of third-party operators’ compliance with the RIS and safety management systems**

***QR’s Position***

A third-party operator will be required to have its rail operations audited on an annual basis in order to demonstrate to QR’s reasonable satisfaction that the operator is complying with:

- the RIS; and
- the safety risk management plan: para 7.5(a).

QR reserves the right, at any time, to require a third-party operator to have specific elements of its operations audited where QR has reasonable grounds for believing that these interface requirements have not been complied with and appropriate measures to rectify such non-compliance have not been undertaken: para 7.5(b).

Subject to QR’s reasonable satisfaction, audits concerning RIS and safety risk management plans may be undertaken in conjunction with an audit required by the safety regulator: para 7.5(c).

***Stakeholder Comment***

All stakeholder submissions expressed concern that QR was proposing to duplicate the role of the RSAU.

**Table 6: Audit rights**

**Toll** - the requirement for an annual audit should be removed. In the absence of any indication of non-compliance, it is an unnecessary expense with no relevant benefit to require an annual audit by any organisation or authority.

**FreightCorp** - where QR considers that a breach of an operator’s accreditation has occurred, or the operator has failed to comply with its rail safety system, the matter should be referred to the RSAU. For our current Queensland operations, the RSAU has not imposed any requirement for an annual external audit. If an operator is failing to conform with the RIS, then a review of that performance should not be delayed until an annual audit and can be

accommodated through the requirement for an audit at any time when there is evidence of non-conformance.

**Queensland Government** - QR must accept that the granting of rail safety accreditation to an access seeker will ensure that an appropriate safety management system is in place and will provide for a system of monitoring/auditing. However, there may be scope for either QR or an access user to arrange 'audits' to ensure compliance with the interface plan where the party has a legitimate business interest to protect.

**AMC, Stanwell** - independent auditors appointed by QT after discussion with the parties should undertake audits.

**QMC** - joint audits of the interface elements of third-party operators' safety management systems without RSAU involvement would be appropriate under AS 4292. However, for other aspects of operators' safety management systems, Network Access should rely on the RSAU for auditing purposes.

Stakeholders provided a range of views regarding who should pay for audits required by QR.

**Table 7: Payment for cost of audits**

**Stanwell** - QR should pay for the cost of any audits it requires.

**FreightCorp, Toll** – QR should pay for the cost of any audit it requires, however, should QR find any defects, it would be entitled to recover the cost of the audit.

**AMC** - payment should be by those requesting the audit, whether it is QR or a third-party operator, regardless of the outcome.

**Queensland Government** - potentially QR should pay, depending upon the circumstances.

**QMC** - if QR were required to pay for audits, this would motivate Network Access to find minor deficiencies to both justify requiring audits and avoid paying for them.

***QCA's Analysis***

The QCA considers that QR's proposed auditing of third-party operators' safety risk management plans raises somewhat different issues to its auditing of those operators' compliance with agreed rollingstock standards and as a result is better addressed separately.

Safety risk assessments are an integral part of a railway manager/operator's safety management system, which must be approved by the RSAU as part of the safety accreditation process. The RSAU has advised the QCA that it audits accredited organisations within the first six months of commencement of their accreditation, and subsequently on an annual basis. This does not mean that it cannot conduct audits on a more regular basis if it sees a need to do so and/or pursue alternative enforcement options, such as suspension of accreditation. In addition to the periodic audits, audits may be conducted as a result of an incident or accident or following an identification of a decline in safety performance as a result of on-going monitoring, such as incident-trend analysis.

As noted above, the Draft Undertaking provides that QR's auditing requirements for safety risk management plans may be undertaken in conjunction with RSAU's requirements, subject to QR's reasonable satisfaction. While in one sense this can be seen as an attempt by QR to minimise the auditing burden on third-party operators, the QCA nevertheless considers that QR is unnecessarily encroaching on RSAU's responsibilities.

RSAU has clear legislative responsibilities with respect to approving and ensuring compliance with safety management systems both for QR and third-party operators. The RSAU has advised the QCA that if QR has reasonable grounds for suspicion that a third-party operator is not

complying with network safety standards, it should inform the RSAU of its concerns and the safety regulator would then take the appropriate action.

Nevertheless, the QCA recognises that there may be instances where QR believes that the safety risk management plan has been breached and safety compromised such that the situation needs addressing urgently. For example, QR may feel that an urgent suspension of the third-party operator's train services is required because of a risk of a major incident due to that operator's conduct. As discussed in sections 7.4 and 7.5 of this chapter, in order to address such situations, QR has proposed to reserve itself the right to suspend a third-party operator's rollingstock and/or its staff. In light of this, the QCA does not believe that QR should also reserve itself an audit power that appears ill-suited to deal with such situations.

The key point for the QCA is that while the contractual implications of a suspension of train services initiated by QR would have to be resolved between QR and the third-party operator, the broader accreditation implications of such a suspension, if any, would be a matter for the RSAU. Consequently, the QCA would expect the RSAU to be informed of such a suspension as a matter of course.

In contrast to QR's position on safety audits, the QCA believes that there may be scope for either QR or a third-party operator to arrange audits where the party has a legitimate business interest to protect. This appears to be the case with respect to QR auditing a third-party operator's compliance with the rollingstock standards agreed as part of the joint safety risk assessment. This is because a third-party operator using rollingstock and/or rollingstock configurations that impart greater wear and tear on the track than negotiated in an access agreement would affect QR's commercial interests. Such a situation, however, would not be of concern to the RSAU unless there were associated safety implications. The issue arises then as to whether QR is entitled to require both annual and 'spot' audits of a third-party operator's compliance with the agreed rollingstock standards.

The QCA is concerned that the Draft Undertaking's requirement for an annual audit of the RIS will substantially duplicate RSAU audits. As noted earlier in this chapter, the QCA is not prepared to endorse QR's proposed RIS. Nevertheless, there will be an agreed set of rollingstock standards following completion of the joint safety risk assessment. Once the joint safety risk assessment has been approved by RSAU, a third-party operator will need to demonstrate to RSAU as part of its own safety management system that it has in place internal processes to comply with the agreed rollingstock interface standards. The QCA considers that QR's proposal that its own auditing requirement might be undertaken in conjunction with that of the safety regulator is too weak because it still allows QR to exercise its discretion and impose an audit on top of the RSAU audit.

Nevertheless, for cases where rail safety is not at risk but QR's legitimate business interests are threatened, the QCA sees merit in QR being able to carry out 'spot' audits of rollingstock if it can demonstrate grounds for non-compliance, as proposed in the Draft Undertaking. The QCA agrees that if a third-party operator is using rollingstock that is damaging the track infrastructure, QR will need to take immediate action. A 'spot' rather than annual audit is clearly best suited to this task.

The issue that then arises is the scope of QR's power to undertake 'spot' audits ie whether this should be an open-ended right, or a right whereby the matters that are potentially auditable are specified in the Draft Undertaking or standard access agreement.

ARTC's draft standard access agreement reserves the right to audit - subject to specified limitations - a rail operator's compliance with the terms and conditions of the access agreement such that:

- the train manifest is correct;
- the capacity of any one or more of the individual wagons has been exceeded; and
- unsafe or potentially unsafe loading of any one or more of the individual wagons has occurred.

RAC's standard access agreement provides it with a right to inspect trains and rollingstock for the purpose of checking compliance with the train manifest and the provisions of the access agreement. RAC also reserves the right to require any train or part of a train to be weighed at a weighbridge provided by RAC.

The QCA supports QR adopting an auditing right with respect to a third-party operator's rollingstock but would require QR to demonstrate the reasons why the audit is required prior to QR actually exercising the right. The Draft Undertaking provides that if QR has 'reasonable grounds' for believing the RIS have not been complied with and the third-party operator has not taken appropriate measures to rectify the non-compliance, then QR can require an audit be conducted. The QCA believes that a basis of 'reasonable grounds' lacks specificity and provides too much scope for QR to exercise its discretion, potentially at the expense of a third-party operator.

Consequently, the QCA believes that QR's audit right should be exercised within the following defined framework established in an approved Undertaking:

- QR would be obliged to provide all relevant information on above-rail rollingstock incidents – eg. incidences of dragging equipment and 'hot box' detection, over-loading and inaccurate train manifests - to a third-party operator concerning its train services.<sup>162</sup> The access agreement between QR and a third-party operator would establish rollingstock standards and agreed tolerances; and
- the ongoing monitoring of data on above-rail rollingstock incidents would allow QR to discern any adverse pattern of performance of the third-party operator's rollingstock, including whether or not this was outside agreed tolerances. QR could use evidence gathered in this way as grounds for requiring an audit of a third-party operator.

The benefits of such an approach would be that QR is able to identify prior to the commencement of an operator's train services what it considers to be its key concerns, while third-party operators have certainty about what aspects of their operations are potentially auditable. QR's scope to arbitrarily use its audit power is reduced by requiring a demonstration of the grounds for audit.

Finally, the QCA supports the principle of a third-party operator paying for any audits of its rollingstock required by QR if the reasonable grounds for audit established in the access agreement are satisfied. This would protect QR's legitimate business interests by deterring a third-party operator allowing a series of above-rail incidents to build up without taking appropriate action.

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<sup>162</sup> QR should provide this sort of information to a third-party operator as a matter of course.

**QCA's Position**

The QCA would favourably consider an Undertaking that:

- removed QR's right to require an annual or 'spot' audit of a third-party operator's safety risk management plan;
- removed QR's right to an open-ended audit power concerning a third-party operator's compliance with the agreed rollingstock standards but rather provided an entitlement to audit within the following framework:
  - QR must be obliged to provide all relevant information on above-rail rollingstock incidents - eg. incidences of dragging equipment and 'hot box' detection, over-loading and inaccurate train manifests - to a third-party operator concerning its train services;
  - it should be specified in the access agreement with a third-party operator what aspects of that operator's compliance with the agreed rollingstock standards QR can audit; and
  - QR must provide reasonable grounds, as established in the access agreement, for the need for an audit prior to exercising its audit right; and
  - provided that a third-party operator must pay for audits of its rollingstock required by QR if the reasonable grounds for audit established in the access agreement are satisfied.

## 7.8 Appropriate allocation of QR's and third-party operators' responsibilities under the EPA Act

The Draft Undertaking imposes a number of environmental requirements upon third-party operators, including investigations, risk management plans and audits. These requirements raise a range of sensitive issues including:

- the interaction of the environmental responsibilities of QR and third-party operators under the *Environmental Protection Act 1994* (the EPA Act), as administered by the Queensland Environmental Protection Agency (the EPA);
- the potential restriction of access to QR's network on environmental grounds, either prior to the execution of an agreement or as a result of premature termination of an agreement; and
- if such a restriction were to eventuate, whether this would be in the public interest, having regard to the QCA's requirement under the QCA Act to consider the public interest,

including legislation and government policies relating to ecologically sustainable development.<sup>163</sup>

The QCA's key concern is that QR's approach could be interpreted as reserving itself a de-facto regulatory role regarding environmental protection. This regulatory role could mean that QR effectively imposes environmental requirements in addition to those currently imposed under Queensland's environmental regulatory framework.

### ***QR's Position***

QR argued in December 1998<sup>164</sup> that the requirements it proposes to impose on third-party operators concerning environmental risk management flow from its obligations, as manager of its rail network, under the EPA Act. QR argued that environmental risks will be created through the interface between the rail infrastructure and rollingstock and that management of these risks is the responsibility of both QR and third-party operators. In QR's view, the environmental provisions of the Draft Undertaking are aimed at protecting its legitimate business interests from these environmental risks.

### ***Stakeholder Comment***

A majority of stakeholders considered that the allocation of environmental responsibilities was inappropriate or unclear.

#### **Table 8: Allocation of environmental responsibilities**

**AMC** - to avoid any misunderstandings, the EPA's role needed to be incorporated in the Undertaking.

**Toll** - there should be a mechanism whereby if QR has concerns about the way in which a third-party operator is conducting its operations, it can raise the issue with the EPA.

**National Rail** - an environmental management plan should be required of all third-party operators, however, these plans must be prepared, authorised and enforced in conformity with the requirements of Queensland's environmental protection law. Any other arrangement will provide a basis for non-price restrictions on competition.

**Queensland Government** - the allocation of responsibilities and the standards that QR is considering are of concern. The QCA and, where necessary, the EPA should discuss this matter further before finalisation of the Undertaking.

**QMC** - it should be the responsibility of the relevant regulatory agency to determine, sanction or stop environmentally unacceptable operations. Network Access' responsibility should be restricted to a reporting role and the operator should be advised by Network Access of a possible or pending incident report being made to the EPA.

**RTBU** - the allocation of responsibilities proposed in the Draft Undertaking are reasonable.

<sup>163</sup> This matter was also discussed in Chapter 1.

<sup>164</sup> *Submission of Draft Undertaking* paper released in December 1998. This paper provided supporting material to a preliminary version of QR's Draft Undertaking distributed to the QCA and a number of interested rail and non-rail parties. This process, initiated by QR, occurred prior to the formal lodgement of the Draft Undertaking with the QCA. Apart from the explanatory material in the 1998 paper, QR has not publicly provided an explanation of its position on the environmental provisions of the Draft Undertaking.

### *QCA's Analysis*

The QCA considers that QR's environmental obligations under the EPA Act, in the context of it effectively being required by statute to allow others to use its network,<sup>165</sup> require clarification in order to assess the reasonableness of the relevant provisions of the Draft Undertaking.

#### *Operation of the EPA Act*

The EPA Act places an overarching obligation in the form of a general environmental duty on all persons and enterprises conducting activities in Queensland. The duty is that a person must not carry out any activity that causes, or is likely to cause, environmental harm unless the person takes all reasonable and practicable measures to prevent or minimise the harm.<sup>166</sup> In addition to the general environmental duty, the EPA Act imposes a general duty to notify the EPA (or other relevant agency) concerning actual or threatened environmental harm.<sup>167</sup> Consequently, both QR and third-party operators have a general environmental duty under the EPA Act and hence each has a legitimate business interest to take responsibility for the potential environmental impact of their operations.

The EPA Act is designed to facilitate the development of environmental management processes at a number of levels, from the general to the specific, and for activities with low risk to high-risk environmental implications. It does not set prescriptive standards which persons and enterprises must meet. Rather, the Act places the onus on these groups to take responsibility for pursuing sound environmental practices, including establishing environmental processes and monitoring environmental performance. The EPA is the primary body responsible for administering the provisions of the EPA Act.

According to EPA guidelines, the observance of due diligence, including the development of environmental management systems, is a key mechanism by which enterprises can show proof of compliance with the general environmental duty. Appropriate due diligence is likely to require demonstration that an organisation understands the environmental risks posed by its operations and has implemented processes to manage those risks. However, only if an activity is high-risk, as defined under the EPA Act as 'environmentally relevant', does the EPA approve the processes to manage the risks created by the particular activity.

The EPA notes in its enforcement guidelines that in assessing corporate liability for breaches of the EPA Act, it will consider the existence and effective implementation of environmental compliance programs by the affected enterprise. The guidelines go on to state that the only substantial defence for companies is if they have undertaken their activities with due diligence. There is a range of enforcement measures available to the EPA including infringement notices, injunctions to cease an activity and prosecution.

For activities with high environmental risks, the EPA Act requires accountability for their management through a licensing system. In terms of railway operations, both of an above and below-rail nature, the primary defined 'environmentally relevant activity' is a 'railway facility'. This is defined as any railway facility for refuelling and maintaining or repairing rollingstock.

In addition, there are a number of other defined environmentally-related activities that could take place as part of an above or below-rail operation including petroleum product storage and stockpiling, and loading or unloading of bulk goods. There are also environmentally-relevant activities concerning metal products activities and boiler making or engineering, which cover

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<sup>165</sup> Queensland Competition Authority Regulation 1997.

<sup>166</sup> S36(1).

<sup>167</sup> S37(1).

the operations of a rail workshop and the manufacture of rollingstock and rail track infrastructure.<sup>168</sup> Running passenger or freight trains between origin and destination points is not defined to be an environmentally-relevant activity.<sup>169</sup>

The EPA Act provides for the proclamation of subordinate legislation in the form of legally binding environmental protection policies for specific issues. The *Environmental Protection (Noise) Policy 1997* (the EPP Noise) is of most relevance to rail operations nominating long-term noise planning levels. In working towards these long-term levels, QR has developed the Queensland Rail Code of Practice for Railway Noise Management.<sup>170</sup> The Code sets out how QR will progressively reduce noise emissions from its operations and thereby meet the general environmental duty placed on all persons by the Act. The Code will apply to third-party operators running train services on QR's network.

#### *QR's responsibilities under the EPA Act and its legitimate business interests*

The QCA has been advised that if QR satisfies its general environmental duty in relation to its own activities and those of its executive officers, employees and agents, it will have a defence to the offence of causing environmental harm quite independent of the question of liability on the part of a third-party operator. In other words, QR is only responsible for its own acts.

QR's general environmental duty does not allow it to ignore its own activities because even if QR takes steps to try to ensure a third-party operator conducts its business in an environmentally responsible way, this will be no defence to QR having caused environmental harm if it failed to maintain its own infrastructure or systems in an appropriate state.

In order to protect itself against environmental liability, QR could provide infrastructure that is fit for an agreed purpose, for example, hauling coal with defined axle loads at defined speeds. QR could also require third-party operators to run trains within limits that are outlined in access agreements, so that QR imposes a contractual obligation upon these operators to run trains within those limits.

Failure to comply with the general environmental duty does not give rise to direct criminal or civil liability but may prompt other enforcement action such as environment protection orders.<sup>171</sup> However, the general environmental duty only provides a defence to offences concerning the 'causing of environmental harm'.<sup>172</sup>

With respect to the negotiation process prior to the signing of an access agreement, QR can legitimately seek information from third-party operators that will allow QR to assess the impact

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<sup>168</sup> QR's 1998-99 Annual Report indicated that it held 27 environmental authorities issued by the EPA for environmentally relevant activities. QR also indicated that it had identified 15 additional authorities that were required under the EPA Act and these had been applied for and were being negotiated with the EPA.

<sup>169</sup> Schedule 1 of the *Environmental Protection Regulation 1998* outlines a list of level 1 and level 2 environmentally relevant activities.

<sup>170</sup> Approved by the Minister for Environment and Heritage and Minister for Natural Resources under Section 219 of the EPA Act on 3 December 1999. Section 219(1) provides that the Minister may, by gazette notice, approve codes of practice stating ways of achieving compliance with the general environmental duty for any activity that causes, or is likely to cause, environmental harm.

<sup>171</sup> An environmental protection order can take two forms – requiring a person or corporation to cease an action or to undertake an action.

<sup>172</sup> There are five main areas of potential liability for QR under the EPA: (a) causing environmental harm; (b) contravening an environmental protection policy; (c) causing or allowing the placing of a contaminant where it could be reasonably expected to cause environmental harm; (d) as holder of an environmental authority contravening a condition of the authority or a condition of a development approval; (e) a requirement to notify the EPA where serious or material environmental harm is caused or threatened by the access party's act or omission in carrying out another activity being carried out in association with QR's activities.

of the proposed train services and hence any additional environmental risks they pose. As a result of this assessment, QR might need to upgrade old, or implement new, elements of its own environmental management system, to make sure that it cannot be responsible for causing a state of affairs which might ultimately give rise to environmental harm.

This is likely to be of greatest importance where a third-party operator's proposed train services are significantly different from those QR has had practical experience of and poses material environmental risks. For example, the third-party operator could be planning to carry a hazardous product that QR has never previously carried.

In order to fulfil its own general environmental duty, a third-party operator will need to inform itself of all relevant environmental risks associated with its use of QR's network in order to develop an environmental management system for its Queensland operations. If the third-party operator already runs train services in the State, this process may entail an upgrading of its existing environmental management system.

It is apparent that the existence of the general environmental duty places an emphasis on QR and third-party operators to disclose all relevant environmental information to each other in order for each to conduct an environmental risk assessment and develop an environmental management system. The EPA, however, does not have a legislative role to conduct or approve such environmental risk assessments and/or environmental management systems of activities if they are not defined as 'environmentally relevant' under the EPA Act.

#### ***QCA's Position***

**The QCA considers that:**

- **QR can legitimately seek information of the kind set out in Schedule I of the Draft Undertaking from a third-party operator that will allow QR to assess the impact of that operator's proposed train services and hence any additional environmental risks posed, in order to assess the need to upgrade QR's own environmental management system; and**
- **a third-party operator can legitimately seek information from QR that will allow that operator to assess the environmental risks of its proposed train services given the particular features of QR's network, in order to develop an environmental management system for its Queensland operations.**

There are timing issues associated with the exchange of relevant environmental information by QR and third-party operators. This is discussed in section 7.10 below.

## **7.9 Reasonableness of QR's environmental requirements**

### ***QR's Position***

The Draft Undertaking imposes a set of environmental requirements on third-party operators in addition to those applying under the EPA Act. Since lodgement of its Draft Undertaking and following a series of discussions with the QCA, QR has made a number of refinements to these requirements. The original requirements are as follows:

- prior to the commencement of its train services, the third-party operator, in collaboration with QR, must procure an environmental investigation of its operations as far as they interface with QR and other rail operators including risks related to the issues identified in Schedule I of the Draft Undertaking. The environmental investigation must be conducted by a suitably qualified party reasonably acceptable to both parties: para 7.4.1(a);
- at QR’s discretion, the environmental investigation may take the form of an impact assessment study: para 7.4.1(a);<sup>173</sup>
- QR and a prospective third-party operator must develop and agree on an environmental risk management plan and QR will need to be reasonably satisfied that the plan is appropriate and compatible with the existing management systems for the rail infrastructure: para 7.4.2(a);
- a third-party operator’s environmental management system must incorporate: all legislative requirements, including any requirements in respect of QR’s environmental authorities/licences; the agreed elements of the environmental risk management plan for which the operator is responsible; and necessary processes to ensure compliance with the environmental requirements of the access agreement: sub-paras 7.4.2(b)(i), (ii) & (iii);
- the third-party operator must receive ISO 14,000 accreditation for its environmental management system prior to commencing its train services: para 7.4.2(b);
- the third-party operator must undertake annual environmental audits: para 7.5(a); and
- the third-party operator is subject to periodic audits at QR’s discretion where QR has reasonable grounds for believing that the third-party operator is not complying with its environmental management system and has not taken appropriate measures to rectify the non-compliance: para 7.5(b).

QR also proposed the following Schedule E principles:

- QR reserves itself the right to terminate an access agreement if it believes, to its reasonable satisfaction, that it would be placed at an unacceptable risk of environmental liability, regardless of whether environmental harm has occurred or not. Before termination of the agreement, QR must first have the material on which it has based its risk assessment subjected to an independent review by an expert;
- if carrying dangerous goods, the third-party operator must comply with the Dangerous Goods Code - including obtaining necessary authorisations and providing details to QR prior to commencement of each train service - and must include procedures for the handling of any incident in its emergency response plan;
- the third-party operator must comply with the noise guidelines specified in the agreement and any other documents prepared by QR in accordance with the relevant environmental protection policy. Where the train services of the third-party operator exceed permitted noise levels the third-party operator, at its cost, may be required to participate in noise abatement measures and further monitoring of noise levels;

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<sup>173</sup> Defined by QR as a detailed study of the short-term and long-term beneficial and detrimental effects on the environment of the third-party operator’s operations insofar as they interact with the rail infrastructure and which includes an assessment of all relevant environmental factors, including social, economic and biophysical factors related to such operations.

- the third-party operator is responsible for taking measures to prevent contamination and to deal with any spillage or leakage which could result in contamination; and
- the third-party operator indemnify QR for any loss it suffers arising through that operator's non-compliance with environmental obligations.

The key refinements to QR's proposed environmental requirements since its lodgement of the Draft Undertaking are:

- the independent suitably qualified party will prepare an environmental investigation and risk management report incorporating both a risk assessment and risk management component rather than just an environmental risk assessment;
- QR reserves the right to cease negotiations if an access agreement has not been entered into, or if it has, to terminate the access agreement if, in its reasonable opinion, the independent report does not adequately identify or address all environmental risks. QR may require the operator to submit a further written proposal demonstrating how it proposes to manage those risks. If the operator fails to submit a proposal or QR rejects the proposal, QR may refer the issue to an independent expert. If the expert's determination supports QR's assessment as being reasonable the agreement may be terminated, otherwise the operator's environmental investigation and risk management report can be finalised;
- QR no longer reserves the right to require an impact assessment study where the proposed train services are substantially different from existing operations or will result in a significant increase in traffic levels;
- the requirement that a third-party operator's environmental management system should be accredited under the ISO 14,000 standard prior to commencing its train services has been weakened, such that its environmental management system must be consistent with ISO 14,000;
- the third-party operator is subject to periodic independent audits at QR's discretion if QR becomes aware of any circumstances which may give rise to material or serious environmental harm associated with the operator's activities, or non-compliance by the operator with the environmental investigation and risk management report; and
- except where the environmental audits of the third-party operator's train services are conducted by an independent person, pursuant to an accredited environmental management system, audits must be conducted by a suitably qualified person reasonably acceptable to both parties.

### ***Stakeholder Comment***

Stakeholders have only had the opportunity to comment on QR's position on environmental matters proposed in the Draft Undertaking. Their comments were made in response to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking*.

#### **Table 9: Appropriateness of QR's environmental requirements**

**AMC, Stanwell, Queensland Government, QMC** – the Undertaking's environmental requirements should be consistent with the relevant legislation.

**Queensland Government** - as currently drafted, the requirements are not clear as to the benchmark against which compliance is to be taken and that environmental requirements

should be applied consistently to all rail users. QR and the QCA should consult with the EPA on this matter.

**Environmental Protection Agency** - the generality of the provisions in the Draft Undertaking will enable QR to nominate any environmental issue for consideration.

**QMC** - where there is an environmental risk, Network Access should also review its own plans for appropriateness.

**Toll** - the environmental requirements are excessive.

**ARTC** - it is understood that QR's environmental requirements are significantly greater than those required by legislation, and whilst QR may be seeking to further protect its own interests, this could be perceived as representing a significant barrier to entry for new entrants.

Stakeholder submissions raised a number of concerns about the requirement for accreditation under ISO 14,000.

**Table 10: ISO 14,000 accreditation**

**AMC, Stanwell** - the only circumstances in which requiring compliance with ISO 14,000 is reasonable is if it is not in excess of Queensland's environmental legislation.

**Queensland Government** - there is no legislative requirement to gain accreditation under ISO 14,000 - in cases of non-compliance with ISO 14,000, it may be appropriate for QR to obtain an indemnity from the operator.

**FreightCorp** - there are a number of operators of heritage trains with minimal funds who would not be in a position to conduct an onerous environmental risk assessment or seek accreditation under the ISO 14,000 standard. We have chosen not, at this time, to seek accreditation under ISO 14,000, however, we believe our environmental management system is fully compliant with that standard.

**Great Southern Railway** - will it be possible for an access seeker to have accreditation under ISO 14,000 if it does not operate any services elsewhere?

All stakeholder submissions expressed concerns about QR's right to require audits. A majority of submissions supported QR having to pay the cost of an environmental audit it requires if it finds no deficiencies.

**Table 11: Audit rights**

**FreightCorp, Stanwell, Toll** - the auditing of third-party operators' environmental management performance should be the responsibility of the EPA, not QR.

**QMC** - auditing by QR was an unreasonable requirement.

**AMC, Queensland Government, Stanwell** - if QR believes on reasonable grounds that there has been, or is likely to be, a breach of environmental requirements, it may be preferable for QR to refer the situation to the EPA.

**FreightCorp, Toll** - should QR find any defects, it would be entitled to recover the cost of the audit.

**AMC, Stanwell** - the party requesting the audit should make payment, whether it is QR or a third-party operator, regardless of the outcome.

**QMC** - requiring QR to pay for audits would motivate Network Access to find minor deficiencies, to both justify requiring audits and to avoid paying for them.

All stakeholder submissions regarded the principle in Schedule E allowing QR to terminate an access agreement on the grounds of unacceptable risk as being unreasonable.<sup>174</sup> All argued that the EPA was the appropriate body to make judgements about unacceptable risks of environmental liability.

### *QCA's Analysis*

The QCA considers that the Draft Undertaking should establish environmental requirements that protect QR's legitimate business interests through their consistency with Queensland's environmental regulatory framework, including policies relating to ecologically sustainable development. In doing so, the Draft Undertaking should not hinder the development of competition in the above-rail market through the imposition of more onerous requirements on third-party operators than necessary under that regulatory framework. Consistency with the requirements of Queensland's environmental regulatory framework and compliance with the principles of ecologically sustainable development ensure that the public interest in environmental protection is adequately addressed.

In broad terms, QR's environmental requirements are applied at two stages in the third-party access process. First, prior to the commencement of the third-party operator's train services. Second, once the operator has commenced its train services.

The key requirements in the first stage of the process are the procuring of an environmental risk investigation and risk management report and the development of an environmental management system in accordance with the ISO 14,000 standard. In addition, a major sensitivity is QR reserving itself the right to terminate an access agreement on the grounds of environmental risks not being identified and/or adequately addressed in the Report.

#### *Environmental risk investigation and risk management report*

The requirement that a third-party operator initiate the preparation of an environmental investigation and risk management report should be assessed in the context of the operator working within the same environmental regulatory framework as QR. This includes third-party operators being subject to the general environmental duty.

As part of its general environmental duty, a third-party operator planning to run train services on QR's network would need to conduct an environmental risk assessment of its operations. In order to protect itself against environmental liability and conform with EPA due diligence guidelines, it would then develop an environmental management system for its operations. The nature of the environmental management system would depend directly on the nature of its planned train services including their associated environmental risks.

If a third-party operator intended to set up a maintenance depot (including re-fuelling facility) or workshop, then it would need to seek licences from the EPA because these are environmentally relevant activities. However, the QCA considers that this should not be a condition of access as it is a matter to be resolved between the operator and the EPA. As noted in section 7.8 of this chapter, QR indicated in its 1998-99 Annual Report that it was negotiating with the EPA concerning a number of additional authorities required under the EPA Act, however, this has not stopped QR continuing to run its train services.

As discussed in section 7.8, in order to protect itself against environmental liability, QR must inform itself of the nature of the risks associated with the third-party operator's proposed train services so it can then make any necessary changes to its internal management processes. The

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<sup>174</sup> AMC, FreightCorp, National Rail, QMC, Queensland Government, Stanwell, Toll.

key point is that QR and third-party operators have a mutual interest in sharing relevant environmental information.

The QCA supports QR's proposal for an environmental investigation and risk management report provided:

- both QR and the third-party operator provide adequate background material and full details of existing and proposed operations;<sup>175</sup> and
- the scope of the investigation and report are appropriately structured to identify the relevant risks and proposed management processes.

If these two conditions are met, the preparation of the environmental risk investigation and risk management report would provide a reasonable balance between QR's legitimate business interests and the interests of third-party operators, while protecting the public interest in environmental protection. This would be achieved as:

- the independent party preparing such a report reduces the potential for QR to play a de-facto regulatory role regarding environmental protection, including imposing requirements in excess of environmental legislation and/or potentially restricting access to its network on environmental grounds. As a result, a third-party operator's interests are protected;
- QR protects itself against environmental liability by ensuring that an independent report is prepared identifying all relevant environmental risks posed by the third-party operator's proposed train services and processes to manage those risks, allowing QR to make any changes to its own risk management processes; and
- the public interest in environmental protection is adequately addressed through an independent suitably qualified party preparing the environmental investigation and risk management report.

Nevertheless, the QCA can envisage a situation where a third-party operator may already be running train services in Queensland and as a result has developed an environmental management system for its operations. It is likely that such an operator will need to upgrade and/or develop new elements of its existing management system rather than develop a risk management system from scratch. For such an operator, the environmental investigation and risk management report may be an unnecessary requirement, with associated adverse cost and time effects.

To address such a situation, the QCA believes that an approved Undertaking should provide for a third-party operator to be able to present a copy of its environmental management system for its Queensland operations to QR to provide a basis for negotiation. QR could then assess the risks posed by the proposed train services and the operator's intended management of those risks, as well as the compatibility of the operator's environmental management system with QR's own system. Such an approach does not hinder QR's legitimate business interests and potentially provides greater flexibility and timeliness in the consideration of environmental risks of a third-party operator's proposed train services than the preparation of an environmental investigation and risk management report. This approach is consistent with the QCA's belief that the handling of environmental interface issues by track managers and rail operators in the

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<sup>175</sup> Environmental information disclosure is discussed in more detail in section 7.10 of this chapter.

Australian rail sector has not presented insurmountable problems in recent years, including in the context of third-party access arrangements.

The QCA therefore considers that an approved undertaking should provide two options for a third-party operator. Option 1 is as currently proposed by QR, whereby an environmental risk investigation and risk management report by an appropriately qualified independent party is procured by the third-party operator. Option 2 would provide for the third-party operator to present a copy of its existing environmental management system to QR for its consideration and as a basis for negotiation.

Under its current proposal, QR reserves the right to terminate an access agreement on the grounds of the environmental investigation and risk management report failing to identify or propose adequate management processes for environmental risks.

Given that a suitably qualified independent party acceptable to QR will prepare the report, the QCA considers that QR should then need strong grounds to require a third-party operator to submit a further written proposal about how it intends to manage environmental risks. For example, the QCA would be very concerned if, after the completion of the report, QR identified environmental risks that could have been brought to the attention of the independent party - via the third-party operator - during its preparation.<sup>176</sup>

Consequently, the QCA considers that QR should commit to provide a statement of reasons to the third-party operator outlining the environmental risks it believes are not identified or inadequately dealt with in the report. The statement of reasons should be limited to the declared service element of the third-party operator's proposed train services, on the grounds that other aspects of a third-party operator's train service, for example, re-fuelling and maintenance facilities, will require environmental authorities/licences granted by the EPA. The third-party operator should then have a right of reply. QR should follow the same process under the QCA's Option 2 if it rejects the third-party operator's environmental management system. The QCA notes that QR's revised environmental requirements provide that QR will provide reasons for rejection and may make recommendations for amendment.

If the operator does not submit a written proposal or QR rejects the proposal, QR reserves the right to refer the issue to an independent expert for a determination which if supportive of QR's position will allow QR to terminate the access agreement. The QCA does not believe this 'second opinion' process sufficiently protects a third-party operator's interests.

If a third-party operator disagrees with QR's concerns about the environmental risk investigation and risk management report, there is no guarantee that the operator will be satisfied with the determination of the second independent expert. Consequently, a second report could be prepared without resolving any of the outstanding issues between QR and the third-party operator. A formal dispute is the likely outcome, however, the third-party operator's access agreement could have already been terminated before the dispute is resolved. The third-party operator's business reputation is potentially exposed to serious damage, particularly if it is unable to deliver in accordance with its commitment to customers.

To avoid such a situation arising, the QCA believes that the third-party operator and QR should have the right to trigger the QCA Act's dispute resolution provisions immediately after QR responds to the operator's reply to QR's statement of reasons for its rejection of the environmental investigation and risk management report or the operator's environmental

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<sup>176</sup> The QCA considers it is important that QR provides all relevant information to the independent party preparing the Report to minimise the potential for 'overlooked' problems to emerge after completion of the Report. Information provision is discussed in more detail in section 7.10 below.

management system. The scope of the dispute resolution process would be to identify and propose adequate management processes of environmental risk, and as a consequence facilitate progress in the negotiation over access.

Such formal recourse to dispute resolution provides a third-party operator with greater protection than QR's proposal, while not adversely affecting QR's legitimate business interests. A third-party operator that QR considers poses unacceptable environmental risks will not be running train services while the dispute is heard, while the dispute resolution process provides an independent adjudication of the environmental risks of the operator's proposed train services. In addition, by short circuiting the 'second opinion' process, time could be saved in the negotiation period.

#### *Accreditation of environmental management systems under ISO 14,000*

The QCA is opposed to the proposed requirement in the Draft Undertaking that a third-party operator's environmental management system be accredited under the ISO 14,000 international standard prior to the operation of its train services. QR's revised environmental requirements are somewhat weaker, proposing that a third-party operator's environmental management system should be consistent with ISO 14,000. Nevertheless, the QCA remains opposed to such a requirement.

First, any requirements for compliance with environmental standards should be imposed on a non-discriminatory basis. Network Access has confirmed to the QCA that QR is not currently accredited under the standard and is highly unlikely to be until at least 2001. The QCA is not aware of any Australian rail track manager or rail operator that is accredited under the ISO 14,000 standard.

As previously noted, the EPA Act requires persons and organisations to develop an environmental management system to suit their operations and meet their due diligence obligations. The EPA Act does not impose any requirement on how the environmental management system is developed and implemented or whether the finished environmental management system should be accredited under, or be consistent with, a particular domestic or international standard.

A requirement for compliance with a particular standard could be justified under the public interest test by reference to generally accepted industry practice or to government policies relating to ecologically sustainable development. However, QR has failed to demonstrate in any of its documentation provided to the QCA why a proposed requirement that a third-party operator's environmental management system be accredited under ISO 14,000 is necessary to protect QR's legitimate business interests or is in the public interest.

On the basis of the evidence available to it, the QCA considers that while a third-party operator may have problems meeting the costs of developing an environmental management system to the ISO 14,000 standard, it could still develop processes that satisfactorily manage the environmental risks posed by its train services and hence be consistent with Queensland's legislative requirements.<sup>177</sup> Indeed, the lack of accreditation under ISO 14,000 would not mean that QR was unreasonably exposed to environmental liability compared to the situation where the operator's environmental management system properly reflected the outcome of the initial environmental risk investigation and risk management report.

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<sup>177</sup> The Queensland EPA has indicated to the QCA that it is difficult to gain accreditation under ISO 14,000. The QCA's own research has found literature indicating that the development of an environmental management system to ISO 14,000 standard could take in excess of 18 months.

In the QCA's view, QR's proposed ISO 14,000 requirement has not been justified on the basis of legislative requirements or the public interest. Over time, if ISO 14,000 became recognised within Queensland's evolving environmental regulatory framework, including policies relating to ecologically sustainable development, as the appropriate standard for environmental management systems and/or that ISO 14,000 became a generally accepted benchmark within the Australian rail sector, then it would be open to QR to submit an amending undertaking incorporating its ISO 14,000 requirement for consideration at that time.

The QCA's concerns about QR's revised requirement that a third-party operator's environmental management system be consistent with the ISO 14,000 standard stem from the fact that it remains in excess of Queensland's environmental legislative requirements. Moreover, such a requirement would introduce an unnecessary additional element of uncertainty for third-party operators regarding the 'consistency' threshold QR would establish for their environmental management systems.

#### *Third-party operator's environmental management system*

The Draft Undertaking provides that a third-party operator's environmental management system incorporate all legislative requirements including any requirements in respect of environmental authorities held by QR from time-to-time as appropriate.

The QCA considers that the link between the requirements in respect of environmental authorities and the impact of access on QR should be made more specific. This is because some of QR's licence requirements may not in any way be relevant to the third-party operator's train services and its associated activities. An amendment to the Draft Undertaking along the lines of 'relevant' requirements in respect of QR's environmental authorities would satisfy the QCA's concerns. The QCA notes that QR's revised environmental requirements are consistent with this position.

#### *Noise management*

The impact of a third-party operator's proposed train services on QR's noise management policy arise as an issue both prior to and after the commencement of those train services. In broad terms, QR's approach to noise management has an environmental protection dimension, which is manifested in a track capacity dimension.

The environmental protection dimension stems from QR's obligations under the Environmental Protection (Noise) Policy 1997 (the EPP Noise) that nominates long-term noise 'planning levels' (long-term levels) and establishes the criteria for determining unreasonable noise.<sup>178</sup> The EPP Noise recognises that some 'beneficial assets', such as railways, have noise levels higher than the long-term levels identified in the EPP Noise and that these long-term levels are not immediately achievable in respect of such assets.

In working towards the long-term levels, QR has developed its own Code of Practice for Railway Noise Management which was approved by the Minister for Environment and Heritage and Minister for Natural Resources under section 219 of the EPA Act on 3 December 1999. The Code sets out 'interim levels' that QR must meet and establishes a process – the Network Noise Management Plan – which aims to prioritise areas of the network in which action for noise attenuation is necessary in order for QR to meet the long-term levels over time.<sup>179</sup> The

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<sup>178</sup> The noise planning levels are: 65dB(A) assessed as the 24 hour average equivalent continuous A-weighted sound pressure level; and 87dB(A) assessed as a single event maximum sound pressure level.

<sup>179</sup> The interim noise planning levels are: 70dB(A), assessed as the 24 hour average equivalent continuous A-weighted sound pressure level; and 95dB(A) assessed as a single event maximum sound pressure level.

Code of Practice effectively states the way in which QR will comply with the general environmental duty.<sup>180</sup>

QR has indicated to the QCA that when a third-party operator makes an application for access to a particular part of QR's network, QR must ensure that the third-party operator's train services will not affect a prioritisation program for noise attenuation. A third-party operator will be required to participate in a noise-attenuation program if:

- the relevant part of the network is at or close to the applicable noise planning level - whether that is a long-term or interim level - constraining the operation of train services on that infrastructure at the time of the application for access, and
- the third-party operator's train services will exceed the applicable noise planning level.

The QCA is aware that the application of rail noise-abatement measures could effectively place a cap on QR's track capacity. For example, in the absence of noise-abatement measures, the maximum capacity of a particular corridor on QR's network could be 12 train paths a day. However, the noise generated by the incumbent train services on that corridor utilising only 9 train paths a day is equivalent to the noise planning levels for that corridor. In the absence of noise abatement measures, the noise management policy effectively constrains capacity to 9 train paths a day.

Existing train services will provide the base noise level for a corridor, with a new third-party operator's train service causing an incremental addition to that base. To the extent that existing train services are generating noise below noise planning levels then capacity will not be constrained by QR's noise management policy. However, if existing train services are generating noise close to or in excess of the noise planning levels, then sensitivities arise as a result of third-party entry. Indeed, QR has indicated in its Code Of Practice that with its existing rollingstock, interim planning levels on some parts of the network cannot be met.

Sensitivities include:

- the calculation of the cost of abatement measures when the incremental units of noise push aggregate noise over the planning level;
- the sharing of abatement costs, for example, a rail operator could be required to pay either the full cost of noise abatement given its train services push noise over the applicable planning level, or rather a proportion of the cost in relation to its contribution to the total level of noise; and
- the approach to third-party entry on parts of QR's network where existing train services are generating noise above interim planning levels.

In the past, in its role as network manager and as the dominant provider of above-rail services on the network, QR has been able to internalise the handling of noise abatement issues, including the associated costs. The QCA recognises that third-party entry on QR's network has the potential to complicate the calculation and assignment of abatement costs. Moreover, there is the potential for QR's management of noise abatement issues to become a barrier to third-party entry. For example, a third-party operator could be required to pay the full cost of noise abatement measures given its train services pushed noise levels over the applicable planning

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<sup>180</sup> Noise management is likely to be a significant issue principally in the Brisbane metropolitan area and possibly at some regional centres.

level for a particular corridor, notwithstanding that the majority of train services on the corridor were provided by QR trains.

This raises the issue of whether specific provisions in the Draft Undertaking, or Schedule E, should address noise management issues, in particular, the framework for determining noise-abatement cost measures. Given the early stage of development of the above-rail market, and recognising that noise abatement concerns are likely to be principally focussed on the Brisbane metropolitan system, the QCA does not consider it appropriate to prescribe a methodology for calculating noise abatement costs in the Undertaking. Such matters are best negotiated between QR, in its role as network manager, and the affected rail operator(s) on a case-by-case basis.

Nevertheless, in principle, the QCA believes that each rail operator should pay for the cost of the incremental units of noise its train services generate, reflected in the cost of noise abatement measures. This would not mean that a new rail operator would pay the whole of the incremental cost of any noise abatement measures, but rather that it would pay a proportion of the cost in proportion to its contribution to the total units of noise on the corridor. This would provide incentives for rail operators to minimise the total noise abatement cost on a particular corridor. In practice, for a rail corridor with a binding noise planning level, the cost of noise-abatement measures would be seen as an additional cost for all rail operators running their train services on that corridor. If no abatement measures were required on a particular corridor, then rail operators would not face this additional cost of running their train services. This incremental cost approach to noise abatement would be consistent with the QCA's proposed incremental cost of capacity concept discussed in relation to the calculation of reference tariffs in Chapter 12.

While the QCA does not believe that a methodology for calculating noise abatement costs should be established in the Undertaking, the Authority recognises the importance of full disclosure by QR, in its role as network manager, of noise information that would impact on a third-party operator's performance. The QCA believes that the Undertaking should establish obligations on QR to provide relevant environmental information to third-party operators and discusses this matter in detail in section 7.10 below.

Once the environmental risk assessment and environmental management system associated with the third-party operator's proposed train services have been completed to QR's satisfaction, the operator can commence its services. This triggers a requirement with respect to audits of a third-party operator's environmental management system. In addition, a major sensitivity is the possibility of QR establishing environmental harm caused or contributed by a third-party operator's train services as a material event of default, providing grounds for QR to terminate the access agreement.

#### *Environmental audits*

QR's proposed auditing requirements in the Draft Undertaking need to be considered in the context of QR's obligations under QR's environmental regulatory framework, including protecting itself against potential environmental liability. A third-party operator's own environmental obligations under that framework cannot be ignored. In this context, the QCA has a number of concerns with the Draft Undertaking's proposed annual and 'spot' auditing requirements.

First, the requirements establish no link to the environmental risks posed by the third-party operator's train services. For example, a third-party operator running a number of services per day carrying a list of dangerous goods (oil, acid etc) could be subject to the same auditing requirements as a third-party operator running a daily service on its heritage train.

An alternative would be for the third-party operator's audit requirements to be established in its environmental management system. These requirements could be addressed in the environmental risk investigation and management report if prepared, or during the exchange of information associated with the upgrading of the two parties respective environmental management systems. In this way, the audit requirements could be clarified from the outset and tailored to the precise circumstances of the access arrangement. The QCA notes that QR's revised environmental requirements provide that the environmental investigation and risk management report will identify the audit regime associated with the operator's proposed train services.

Second, the auditing requirements fail to recognise that for each environmentally relevant activity performed by a third-party operator, such as a re-fuelling facility and/or maintenance depot supporting its train services, an EPA environmental authority/licence will be required. These licences will require annual environmental reports to be performed. Monitoring of the operator's compliance with the requirements of its licences will be a matter for the EPA not QR. It is difficult to envisage any situation or any activities by the third-party operator in such a facility that could result in any potential for environmental liability on the part of QR. As a result, QR's interest in the auditing of a third-party operator's train services should be confined to the element of the service regarding train running between origin and destination points.

Third, the auditing requirements fail to recognise that a third-party operator is likely to be conducting and preparing audit reports on the element of its operation concerning train running between origin and destination points as part of its own environmental management system. Consequently, QR's proposed annual audits would likely only serve to duplicate the third-party operator's internal audits. The QCA considers that it would be reasonable for QR to require the operator to provide copies of the relevant parts of such audit reports to QR.

In this way, QR could check that the operator is complying with the processes set out in its environmental management system. QR protects itself from environmental liability by checking that the audits are being completed and gains an understanding of the management processes the operator has adopted. The regularity of reporting should be dependent on the risks posed by the train services of the third-party operator. Clearly, QR would not be protected if the third-party operator failed to produce its own audits and QR did not follow this up. Similarly, in order to protect itself against environmental liability, an operator should have the right to see the relevant parts of QR's internal environmental audits.

The QCA also has concerns about QR conducting 'spot' audits of a third-party operator's compliance with its environmental management system. An operator's non-compliance with its environmental management system potentially has implications for the operator, QR and the EPA. It is not clear that in all cases it will be QR's responsibility to investigate or take action regarding the non-compliance. It may well be a matter best resolved between the EPA and the third-party operator.

In light of this uncertainty, the QCA considers that the onus should be on the third-party operator to inform QR that it has breached its environmental management system and include details regarding how it intends to rectify that breach, rather than QR requiring 'spot' audits to be conducted of the operator's activities. The operator could be required to rectify the breach as soon as practicable, having regard to the nature of the breach and any action required by the EPA, and comply with any reasonable directions from QR. This protects the interests of third-party operators by removing scope for potentially invasive audits. QR, by placing a contractual obligation on an operator that it be informed and that the operator take the necessary steps to address the non-compliance, protects its own legitimate business interests. The QCA has developed an additional Schedule E principle to address this matter.

*Material event of default*

As discussed in Chapter 8, Schedule E of QR's Draft Undertaking incorporated a summary of a standard access agreement. The summary was in the form of detailed principles. Schedule E has been the subject of considerable discussions between the QCA, QR and its stakeholders. As a result of these discussions, a number of versions of Schedule E were prepared. The QCA had significant concern with a version of QR's Schedule E of March 2000 that provided that QR's 'reasonable opinion' regarding the adverse environmental impacts of a third-party operator's train services could result in a material event of default. This would be sufficient ground for QR to terminate an access agreement.

As a result of agreement between QR and its stakeholders that events of default would be agreed during the access negotiation process rather than specified in the Draft Undertaking or a standard access agreement, the environmental material event of default has not been incorporated in the Schedule E principles proposed in this Draft Decision. Nevertheless, the QCA remains concerned that QR may negotiate to incorporate such an event of default into its access agreements.

QR has indicated to the QCA that it needs such a default principle to protect itself from environmental liability once a third-party operator is running train services on its network. QR believes that situations may arise where it has to force a third-party operator off its tracks because of the environmental risks its services are posing. QR believes that its environmental obligations as rail network manager under Queensland's environmental regulatory framework require that it takes such action, otherwise it will leave itself open to enforcement measures by the EPA.

The QCA considers that the proposed termination right goes considerably beyond what is necessary for QR to meet its environmental obligations under the environmental regulatory framework and, moreover, goes beyond the EPA's powers to suspend or stop environmentally damaging activities.

Using the hypothetical situation of an organisation performing an activity that was causing serious environmental harm, the EPA has a number of enforcement measures available to it to respond to such a situation. For example, the EPA could seek an injunction to stop the particular activity causing the harm. This would not mean, however, that the organisation would have to stop any other activities it was performing which had no relation to the activity causing the harm. The injunction would only apply to the relevant activity. Similarly, the EPA could issue an environmental protection order requiring the offending organisation to cease an action or to undertake an action in relation to the activity causing the harm. The thrust of any EPA action would be to stop the activity causing the environmental harm until a means could be found, if any, for it to recommence without causing that harm. This is clearly a more narrowly focussed approach than closing down the whole of the affected organisation's operations, which could be the practical effect of QR's proposed material environmental default right.

Under QR's proposal, the Authority can envisage a possible scenario where a third-party operator is forced off QR's tracks and its access agreement terminated without a breach of environmental legislation actually having occurred. While a third-party operator could subsequently be able to claim damages against QR under such a scenario, this may be little consolation if its business reputation has been ruined in the Queensland market for the long-term. Given this significant asymmetry in consequences faced by QR and third-party operators concerning termination of access agreements, the QCA believes that any termination right QR reserves for itself in access agreements should be associated with a process entailing significant checks and balances before the right can be exercised.

The QCA considers that the key principles underpinning the development of a balanced process culminating in an environmental termination right for QR should be that:

- the relevant provisions of the EPA Act, including the role of the EPA, are recognised; and
- the exercise of an environmental termination right is directly linked to serious and/or material environmental risks and/or environmental harm caused or threatened by the third-party operator’s train services.

In assessing whether a material event of default has occurred with respect to environmental matters, QR proposes to adopt the definition of ‘environmental harm’ in the EPA Act. Environmental harm is defined as any adverse effect, or potential adverse effect – whether temporary or permanent and of whatever magnitude, duration or frequency - on an environmental value and includes environmental nuisance.<sup>181</sup> QR has chosen to use the broadest definition of environmental harm in the EPA Act, notwithstanding that ‘material’ and ‘serious’ environmental harm are also defined. The QCA considers that as a minimum, any right to terminate an access agreement on environmental grounds should be linked to the definition of serious environmental harm in the EPA Act.<sup>182</sup>

The QCA believes that QR reserving itself the right to terminate an access agreement on environmental grounds must be viewed in the context of s37 of the EPA Act (Duty to notify environmental harm). S37 of the EPA Act places an obligation on a person who, while carrying out an activity (the primary activity) becomes aware that serious or material environmental harm is caused or threatened by the person’s or someone else’s act or omission in carrying out the primary activity or another activity being carried out in association with the primary activity.<sup>183</sup>

Ss37(3) and ss37(4) establish the process by which the EPA is informed of the environmental harm. In QR’s case, as soon as it becomes aware of the environmental harm – whether caused by itself or by a third-party operator - it must immediately give written notice to the EPA of the event, its nature and the circumstances in which it happened. A person must not, without reasonable excuse, fail to comply with ss37(3) or s37(4).

It is apparent that if a third-party operator’s train services cause or threaten environmental harm and QR notifies the EPA as required under the EPA Act, the EPA must investigate the matter in order to assess whether a breach of the Act has occurred. The EPA has a range of enforcement measures at its disposal to cater for varying degrees of seriousness of environmental incidents including:

- infringement notices;
- orders to carry out specified works or clean up damage;
- injunctions to cease activity;

<sup>181</sup> Environmental nuisance is defined as unreasonable interference or likely interference with an environmental value caused by (a) noise, dust, odour, light; or (b) an unhealthy, offensive or unsightly condition because of contamination; or (c) another way prescribed by regulation.

<sup>182</sup> Serious environmental harm is environmental harm (other than environmental nuisance) – (a) that causes actual or potential harm to environmental values that is irreversible, of a high impact or widespread; or (b) that causes actual or potential harm to environmental values of an area of high conservation value or special significance; or (c) that causes actual or potential loss or damage to property of an amount of, or amounts totalling, more than the threshold amount; or (d) that results in costs of more than the threshold amount being incurred in taking appropriate action to – (i) prevent or minimise the harm; and (ii) rehabilitate or restore the environment to its condition before the harm. The threshold amount is \$50,000.

<sup>183</sup> S37(2) provides a number of exceptions where environmental harm can be authorised.

- prosecution; and
- cancellation or suspension of a licence.

The QCA believes that the EPA's enforcement role has to be reflected in any process that QR establishes culminating in an environmental termination right. When QR has reason to believe that environmental harm is caused or threatened by a third-party operator's train services, the EPA Act requires that QR should draw the EPA's attention to the matter in writing as soon as reasonably practicable. The third-party operator should be copied the written advice to the EPA. The EPA has informed the QCA that having received QR's written advice, the EPA would conduct an investigation of the matter and determine the appropriate course of action. This may entail use of one of the enforcement measures stated above. Alternatively, it may not if the EPA finds QR's concerns to be misplaced.

The QCA understands that if QR fulfils its duty to notify environmental harm caused by a third-party operator's train services, then it is likely to protect itself against any subsequent enforcement action the EPA may decide to take.

If the third-party operator chooses not to take any action following QR's notice to the EPA, this could become a trigger for further action by QR concerning its access agreement with that operator. However, any decision concerning the third-party operator's train services should await the outcome of the EPA's investigation, including the outcome of any review applications or appeals against any relevant enforcement mechanism imposed by the EPA.

This is because QR's concerns have to be proven valid and, if this is the case, environmental harm could vary from relatively trivial (for example, emitting black smoke) to very serious (for example, acid spill into waterway). For relatively trivial potential or actual environmental incidents, the EPA could serve an infringement notice on the operator requiring action be taken to address the problem, but allowing train services to continue. Alternatively, the EPA could find that potential or actual serious environmental harm justified the issuing of an environment protection order and suspension of the operator's train services until the incident was addressed.

The key point for the QCA is that the outcome of an EPA investigation determines the nature of QR's action concerning the status of the third-party operator's access agreement. The EPA's enforcement guidelines state that the use of environmental protection orders allows a fast and effective response to environmental harm in order to ensure an environmental solution to a problem rather than a legal one.

Moreover, the QCA considers that the key driver of any QR action on environmental issues is to avoid environmental liability. Linking QR's action regarding a third-party operator's train services to EPA action meets this objective. The QCA believes that QR's standard access agreement could require that a third-party operator comply with its obligations under the EPA Act, including any notices or directions it received from the EPA. Failure to comply with such an obligation and for that failure to cause or threaten serious environmental harm establishes grounds for a material event of default. The linking of a failure to comply with the outcome of an EPA investigation to a requirement that such a failure causes or threatens serious or material environmental harm is important. This is because a failure to comply with the outcome of the EPA investigation may not have serious environmental consequences or expose QR to any additional liability.

Notwithstanding that it may notify actual or threatened environmental harm to the EPA pursuant to s37, QR has indicated to the QCA that it remains potentially liable under s126 of the EPA Act (Offence to place contaminant where environmental harm or nuisance may be caused) if it allowed a third-party operator who caused or threatened environmental harm to continue running its train services.

S126 states that a person must not cause or allow a contaminant to be placed in a position where it could reasonably be expected to cause serious or material environmental harm or environmental nuisance.

QR's concern about liability arising from actions by the third-party operator means that QR cannot itself be liable for 'causing a contaminant to be placed' merely because of some action by the operator. Only if QR caused some relevant link in the causal chain, such as not maintaining a piece of its infrastructure to an appropriate standard, would QR be potentially liable for 'causing a contaminant to be placed'. The issue of QR protecting itself against environmental liability through maintaining its infrastructure to an appropriate standard was discussed in section 7.8 above.

This means that the main potential area for concern is where QR itself has allowed a contaminant to be placed in a relevant position. It is the 'placing' of the contaminant - in a particular place or position - that QR must 'allow' in order to commit the offence. The explanatory memorandum to the EPA Act indicated that the aim of s126 was to encourage prevention rather than wait for damage to occur. The courts have considered the meaning of 'allow' in other contexts. There must be some direct or indirect sanction of a thing to allow it to be done. A person cannot be said to allow something of which they are unaware or which is something that they cannot prevent.

It seems reasonable to conclude that the relevant offence is allowing the placing of the contaminant. The offence is not a failure to remove a contaminant placed in such a position when a person becomes aware of it. This provides a sensible tie-in between s126 and s37 of the EPA Act in that a person who did not authorise the placing of a contaminant and who was unaware of it but then became aware of it, is not obliged to remove it but to notify the EPA if s37 applies. Therefore, where QR is unaware of a third-party operator placing contaminants in a relevant position, the potential risk for liability under s126 appears to be quite small.

The QCA recognises that the key objective of the environmental provisions of the Draft Undertaking should be that QR is not unreasonably exposed to environmental liability. The QCA believes that the process for establishing a material event of default on environmental grounds outlined above would meet that objective.

#### *Environmental Indemnities*

QR's legitimate business interests include trying to avoid:

- criminal liability and penalties; and
- clean-up and rehabilitation costs, compensation and the cost of complying with other enforcement action

arising out of the environmental impacts of the train services of a third-party operator.

Similarly, it is in the legitimate business interests of a third-party operator to take the necessary steps to avoid exposure to environmental penalties arising from its use of QR's network.

Schedule E in the Draft Undertaking requires the third-party operator to indemnify QR for any loss it suffers arising from that operator's non-compliance with environmental obligations, although the indemnity reduces proportionately by the extent of QR's default or negligence. However, the Schedule E principles proposed in this Draft Decision have replaced this

environmental indemnity with a general reciprocal indemnity with respect to claims caused or contributed by wilful default or negligent act or omission of either party or its staff.<sup>184</sup>

The QCA is comfortable with the use of reciprocal indemnities for wilful or negligent behaviour by either party in an access agreement including for the causing of, or contributing to, environmental harm. Nevertheless, the QCA recognises that in the context of the obligations of QR and third-party operators under Queensland’s environmental regulatory framework, such indemnities should complement the development of their respective environmental management systems rather than act as a substitute for them.

#### ***QCA’s Position***

**The QCA would favourably consider an Undertaking that:**

- **provided an option under sub-clause 7.4.1 for a third-party operator to present its existing environmental management system to QR for its consideration and as a basis for negotiation, as an alternative to the procurement of an environmental investigation and risk management report;**
- **did not reserve QR’s right to terminate access agreements on the grounds of unacceptable environmental risks but rather instituted a process whereby QR must provide a statement of reasons why it does not accept the environmental investigation and risk management report or the third-party operator’s environmental management system. The third-party operator should have a right of reply, and if the two parties still cannot reach agreement on the contentious environmental matters, each should have the right to trigger dispute resolution procedures;**
- **did not require that a third-party operator’s environmental management system be consistent with the ISO 14,000 environmental standard;**
- **imposed requirements in respect of QR’s environmental authorities/licences on third-party operators to the extent that these licence requirements are relevant to the third-party operator’s train services;**
- **linked QR’s auditing requirement to the risks posed by a third-party operator’s train services and what is established in that operator’s environmental management system. Auditing requirements should be specifically addressed in the environmental risk investigation and management report, if prepared, or during the exchange of information associated with the upgrading of the two parties respective environmental management systems. Each party should be required to provide the other with**

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<sup>184</sup> The QCA has concerns with the wording of the revised general reciprocal indemnity. These concerns are discussed in Chapter 8.

<p><b>copies of the relevant parts of its internal audit reports;</b></p> <ul style="list-style-type: none"> <li>• <b>could require that a third-party operator comply with its obligations under the EPA Act, including any notices or directions it receives from the EPA. Failure to comply with such an obligation <u>and</u> for that failure to cause or threaten serious environmental harm would establish grounds for a material event of default; and</b></li> <li>• <b>incorporated the following Schedule E principles:</b></li> <li>• <b>“Environmental management must be approached on a risk identification and risk management basis with respect to operations on the nominated network and auditing requirements should be linked to the environmental risks posed by a third-party’s train services and be established in that third-party’s environmental management system.</b></li> <li>• <b>The third-party is required to inform QR of non-compliance with its environmental management system and provide details of how it intends to address the non-compliance. The third-party is required to rectify the breach as soon as practicable having regard to the nature of the breach and any action required by the EPA.”</b></li> </ul>
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#### 7.10 QR’s assistance to prospective third-party operators concerning the Draft Undertaking’s environmental requirements

##### *QR’s Position*

QR has not addressed this issue in the Draft Undertaking nor in its explanatory material.

##### *Stakeholder Comment*

A majority of stakeholder submissions supported QR providing information to enable third-party operator’s to fulfil the Draft Undertaking’s environmental requirements.

##### **Table 12: Assistance to third-party operators**

**FreightCorp, Toll** - QR should be required to provide its own environmental risk management plan and any relevant documentation and data (including that relating to noise and any other measures that would impact on a third-party operators’ performance).

**Queensland Government** - much of the base data required to adequately assess the impact of third-party operations would only be available from QR.

**QMC** - third-party operators should fulfil the environmental requirements without assistance or interference from QR.

**FreightCorp** - QR had not always been in a position to provide appropriate assistance in the preparation of the environmental management plan for our Queensland operations. In addition, QR had been unable, or unwilling, to provide baseline noise data upon which we could measure our performance.

### ***QCA's Analysis***

As noted in section 7.8, in order to protect itself against environmental liability, a third-party operator can legitimately seek information from QR that will allow the operator to assess the environmental risks of its proposed train services, given the particular features of QR's network. This will assist the operator to develop an environmental management system for its Queensland operations.

In this regard, the QCA considers that there needs to be full disclosure by QR of all relevant environmental information that will impact on a third-party operator's proposed or actual train services. This information is likely to include environmental reports, relevant licence conditions, baseline noise data, particulars of noise complaints, any enforcement actions, and the Queensland Rail Code of Practice for Railway Noise Management.

There are timing issues associated with QR's provision of such environmental information. Clearly, a potential access seeker making a preliminary inquiry to Network Access would not require baseline noise data or particulars of noise complaints. However, an access seeker who has gone beyond the initial inquiry stage and has lodged an access application and received an indicative access proposal from Network Access would require detailed noise information.

The QCA considers that QR's proposed Information Packs (Schedule D preliminary information) should include 'planning levels' for railway noise, including any 'interim' planning levels, and the extent to which such levels are binding. This should be sufficient information for initial inquiries from access seekers.

Under the negotiation framework proposed in the Draft Undertaking, a third-party operator who has received an indicative access proposal and indicated an intention to progress its access application enters the formal negotiation process with QR.<sup>185</sup> In the negotiation period, the third-party operator will be required to provide additional information to QR in order for it to develop an access charge and terms and conditions for acceptance.<sup>186</sup> This additional information includes preparation of the environmental investigation and environmental risk management report.<sup>187</sup> It is during the preparation of this report or - as proposed by the QCA - the negotiations concerning the upgrading of the two parties respective environmental management systems, that QR should provide, for example, the detailed noise data to the third-party operator.

#### ***QCA's position***

**The QCA would favourably consider an Undertaking that:**

- **included in the preliminary information provided to access seekers (Schedule D - Information Packs), noise planning levels, including 'interim' planning levels, and an indication as to whether the planning levels are binding; and**
- **committed QR to provide on a timely basis all environmental reports, relevant licence conditions, baseline noise data, particulars of noise complaints, any enforcement action and a copy of the Queensland Rail**

<sup>185</sup> Clause 4.7.

<sup>186</sup> Sub-paragraph 4.5(a)(vii).

<sup>187</sup> Sub-clause 4.7.2.

**Code of Practice for Railway Noise Management, to a third-party operator during the negotiation period.**

## 7.11 Treatment of issues relating to adjoining infrastructure

### *QR's Position*

QR provides that it shall either design, or approve the design of, and supervise the construction of any connecting infrastructure of a third-party operator and other elements of the adjoining infrastructure essential to the operation of safeworking systems on the rail infrastructure, including the connection itself: para 7.7(a). QR proposes that the third-party operator will pay the design, supervision and all construction costs associated with the adjoining infrastructure and connection: para 7.7(b).

QR argued in its submission to the QCA's Request for Comments Paper *Queensland Rail Draft Undertaking* that it was within its legitimate business interests to manage any enhancements to the rail infrastructure.

### *Stakeholder Comment*

A majority of submissions agreed that QR had a legitimate interest in ensuring that there are safe and proper connections with its existing infrastructure.

#### **Table 13: QR's role regarding adjoining infrastructure**

**FreightCorp, Stanwell** - there is no indication in the Draft Undertaking that QR would not prevent an access seeker designing and constructing any infrastructure up to the point of interface with the QR network.

**FreightCorp** - it is likely that in any given situation there will be more than one solution available and the Draft Undertaking fails to recognise the legitimate interests of the operator in this regard.

**QMC** - connecting infrastructure requires an interface management plan to ensure all round safety is managed. QR should be obliged to recognise other managers' responsibilities and both parties have to agree on the plan. The default condition that Network Access does not pay unless otherwise agreed with the third-party operator should be removed.

**Toll** - there should be no express or implicit pressure on the part of a third-party operator to use QR to prepare any design.

**Queensland Government** - with respect to design, QR's role should be limited to approval only, with design being undertaken by the third-party operator.

**Stanwell, Toll** - QR's role in approving any design should be limited to the interconnection point.

All submissions expressed concern that QR's adjoining infrastructure proposal potentially enables it to require that adjoining infrastructure be constructed to a higher standard than QR's current infrastructure.

**Table 14: Standard of adjoining infrastructure**

**FreightCorp** - the proposal allows QR to mandate any standard of construction it wishes. The reasonable interests of the operator need to be accommodated. While it is expected that QR would, in practice, make every effort to minimise the costs of the interface, the Draft Undertaking did not reflect this.

**Stanwell** - the Undertaking should make clear that the standard of interconnecting infrastructure will be similar to that of the existing infrastructure.

**QMC** - a provision for independent challenge should be noted in the Undertaking.

**Queensland Government** - there should be no possibility that QR could require higher standards for adjoining infrastructure. The standards adopted should allow scope for innovative design. The QCA needed to investigate this matter further.

**Toll** - beyond the direct interconnection issues, QR should not have any role in, or specify the standard to which, any adjoining infrastructure should be constructed.

***QCA's Analysis***

The QCA considers that the key issue with respect to adjoining infrastructure is what QR should be able to reasonably require to protect its legitimate business interests. This issue has three dimensions:

- the scope of the interface, which establishes the boundary for QR's interest in the adjoining infrastructure;
- QR's role in the design and construction of any adjoining infrastructure, including the recovery of its costs thereof; and
- the appropriate standard of the adjoining infrastructure.

In principle, QR's involvement in the development of any adjoining infrastructure should be limited to the interface with the existing network, on the grounds that the characteristics of the adjoining infrastructure beyond the interface have no effect on QR's management of its network. Consequently, QR has no legitimate business interest in determining or influencing the nature of those characteristics.

The QCA considers there are three elements to the interface between adjoining infrastructure and QR's network:

- the connection point or turnout;
- the safeworking system, including signalling; and
- the electrical overhead system, where relevant.

The connection point is where the adjoining track interconnects with the track of the existing network.

The elements of adjoining infrastructure essential to the network's safeworking systems are infrastructure and procedural-based, including the track work and signalling. In practice, QR's interest will extend beyond the point of connection.

For example, the 100m or more section of track up to and including the point of connection could be essential to the safeworking system because this could be the safe stopping distance for trains entering the network from the adjoining infrastructure. The grade and curvature of

adjoining track also could be relevant. The track may have in-built protection devices to prevent uncontrolled rolling stock entering the existing network. This too would be relevant for the network's safeworking system.

The signalling system on the adjoining infrastructure is essential to the network's safeworking system because it controls the movement of trains onto the network. While it need not be identical to QR's signalling system, the two systems would have to communicate with each other so that QR, as network manager, could control the movement of trains from the adjoining track onto the network and coordinate these movements with mainline traffic movements. This communication could be electronic or procedural in nature.

QR has legitimate business interests to protect in relation to the network's electrical overhead power system, in particular, the supply of electrical power and the physical link between the network's electrical infrastructure and the electrical infrastructure on the adjoining track. If the adjoining track is electrified and without a stand-alone generator, the respective electrical overhead systems of that track and QR's network would need to be physically linked up. In this case, trains entering the network from the adjoining infrastructure would need to draw on electricity from QR's network.

The QCA considers that the current wording of the Draft Undertaking lacks clarity with respect to QR's intentions regarding the design and construction of the above elements of the adjoining infrastructure essential to the interface with its network. One interpretation could be that QR is reserving itself the right to choose whether to design or approve the design of the relevant adjoining infrastructure, as well as supervise the construction.

The QCA considers that if QR reserves itself the right to approve the design of the relevant adjoining infrastructure and check the construction (after completion) against the design, QR would be protecting its legitimate business interests. QR would be entitled to recover its reasonable costs associated with the approval of the design and construction. Under this approach, the third party operator would be entitled to take responsibility for managing the development of its adjoining infrastructure, including choosing and funding a design that best meets its needs and supervising construction.

Nevertheless, QR's role in approving the design of adjoining infrastructure could become a source of disagreement with third party operators. Disagreement is likely to stem from a lack of clarity in the engineering and safeworking standards it is appropriate for the adjoining infrastructure to meet.

The QCA considers that physical compatibility of existing and adjoining track is very important at the connection point alone. For the adjoining track beyond the connection point, physical compatibility is not important because it has no effect on QR's network and is therefore not an interface matter.

If QR had the right to intervene in the engineering standards of track beyond the connection point, the potential would exist for the track to be built to a higher standard than the existing infrastructure, or to a higher standard than necessary to ensure that train operations are consistent with the network's safeworking systems. For example, QR should not be able to insist that the adjoining track have concrete sleepers to ensure compatibility with the mainline, when from a safeworking perspective wooden sleepers would be satisfactory because gross tonnage and train speeds over the adjoining track are significantly lower than the mainline.

Consequently, the QCA considers that the connection point (or turnout) between the existing track and the adjoining track should be designed and constructed to QR's existing or committed engineering standards, whichever is relevant. However, this should not prevent a third party designing and contracting infrastructure to a higher standard at its own volition.

It is not possible to specify in detail the safeworking standards that are appropriate for adjoining infrastructure. In broad terms, the QCA considers the appropriate safeworking arrangements would be tailored to the level of risks generated by the particular physical characteristics of the adjoining infrastructure and the mainline, as well as the train services using the mainline and the adjoining infrastructure. QR's current safeworking arrangements vary across its network for these sorts of reasons.

For example, adjoining track interconnecting with a mainline with heavy traffic flow would require a more sophisticated safeworking system than adjoining track interconnecting with a mainline with minimal traffic flow. However, adjoining track interconnecting with a mainline with minimal traffic flow would not need a safeworking system commensurate with a mainline with heavy traffic flow.

The QCA considers that safeworking systems adopted by QR on other parts of its network would establish precedents for the safeworking arrangements required for any adjoining infrastructure. The nature of the safeworking arrangements would need to be negotiated between QR and the third party operator and approved by RSAU.

The appropriate standards for the electrical infrastructure of adjoining track will vary depending on whether it is the supply of electrical power or the electrical infrastructure that is concerned.

Even if a third party operator decides to supply its own power, an interface will need to exist between both power sources because where multiple locomotives are used the two systems interact electrically, one locomotive on one system and one on the other. Therefore the actual power supply system on the adjoining infrastructure would need to be completely in accord with QR's current design (or committed design in appropriate circumstances).

In contrast, the standards of the third party operator's electrical infrastructure could be varied in accord with its own risk factors. For instance, the speed of trains on the third party operator's infrastructure could be lower than the mainline resulting in lower 'train loading' and a need for smaller component designs. Since the frequency of train services on the adjoining track is likely to be lower than on the mainline, the contact wire-wear design factors could also be optimised. Finally, it may be possible for the design life of the adjoining electrical infrastructure to be lower than the mainline design life, including because of a short expectation of the life of the activity serviced by the adjoining track. Consequently, the QCA considers that the physical link between the electrical infrastructure on the mainline and adjoining track, must be constructed to QR's current design (or committed design in appropriate circumstances). However, beyond that physical link, the design of the electrical infrastructure is a matter for the third party operator alone.

Finally, it should be noted that if a third party operator decided to build adjoining infrastructure to QR's network, it would need to become accredited as a railway manager under the TI Act.

#### ***QCA's Position***

**The QCA would favourably consider an Undertaking that:**

- **limited QR's interest in the development of any adjoining infrastructure to the following interface elements:**
  - **the connection point or turn-out;**
  - **the safeworking system, including signalling; and**

– the electrical overhead system, where relevant.

- reserved QR's right to approve the design of adjoining infrastructure and check its construction (after completion) against the design for the above interface elements and recover its reasonable costs thereof;
- required that the connection point (or turn-out) between the existing infrastructure and the adjoining infrastructure should be designed and constructed to QR's existing or committed engineering standards, whichever is relevant;
- recognised that safeworking arrangements for the adjoining infrastructure would be tailored to the level of risks generated by the particular physical characteristics of the adjoining infrastructure and the mainline, as well as the train services using the mainline and the adjoining infrastructure; and
- recognised the electrical power supply systems of QR and a third-party operator would need to be completely in accord with QR's current design (or committed design in appropriate circumstances), as would the physical link between the electrical infrastructure on the mainline and adjoining track.

**CHAPTER 8. SCHEDULE E – SUMMARY OF STANDARD ACCESS AGREEMENT****KEY ASPECTS**

**Guidance** – the Undertaking should have a schedule incorporating broad principles relating to access agreements upon which the parties can rely in the event of the QCA being called to arbitrate in a dispute.

**Disputes** - if a dispute arises during an access negotiation and is referred to the QCA, the Authority may appoint an external mediator so as not to jeopardise possible future arbitration.

**Network blockages** - Network Access should coordinate the clearance of network blockages, including retaining a right to direct any rail operator to assist in the clearance of a blockage.

**Material change events** – as specified in access agreements are triggers only and should be assessed on a case-by-case basis, not automatically flowed on.

**Confidentiality** - an access seeker should be able to bind QR contractually to comply with the confidentiality arrangements established in an approved Undertaking.

## 8.1 Introduction

Schedule E of QR's Draft Undertaking incorporated a summary of a standard access agreement. The summary was in the form of detailed principles. QR argued that it outlined all the major issues likely to be addressed in an access agreement. The Draft Undertaking provided that unless otherwise agreed between QR and a third-party operator, an access agreement must be consistent with the principles.

There was generally strong support from stakeholders for a flexible standard access agreement, however, there was a concern that the Schedule E principles were not commercially balanced.<sup>188</sup> The QCA shared stakeholders' concerns. QR's view was that the Schedule E principles protected QR's legitimate business interests and did not impose unreasonable restrictions upon third-party operators. Following discussions with the QCA, QR made a number of revisions to Schedule E.

In an effort to find areas of common ground between QR and stakeholders, the QCA hosted a Working Group meeting on 5 April 2000 to discuss the revised version of Schedule E prepared by QR. Several stakeholders expressed the view that many of the points in the revised Schedule E were too detailed for a summary document. Given that the same level of detail was not present in other points in the summary, the document was unbalanced. Further, stakeholders expressed the view that, while more detail would be required in Schedule E to address this problem, this could preclude necessary flexibility in commercial negotiations.

At the Working Group meeting, it was agreed that QR's Undertaking should have a schedule incorporating a set of broad principles relating to access agreements upon which parties could rely in the event of the QCA being called upon to arbitrate in a dispute. This schedule would leave many of the issues covered by QR's revised Schedule E to commercial negotiation. It would also need to be broad enough to cover the different requirements of a heterogeneous set of rail operators and end-users.

FreightCorp, on behalf of a number of rail operators and end-users,<sup>189</sup> subsequently prepared a paper outlining the principles that it considered should be included in a Schedule E to the Undertaking. This paper provided the basis for further discussions between QR and the various parties, the outcome of which was further revisions to QR's Schedule E.

Following more discussions between QR and the above stakeholders, the QCA was provided a version of Schedule E reflecting agreement on a large number of issues. Nevertheless, there remained a number of outstanding issues that have required the QCA to exercise its judgement in developing this Draft Decision.

## 8.2 QR's proposed Schedule E principles

QR advised the QCA that after consideration of the views of third-party operators, end-users and the QCA, it had prepared the following summary of high level principles that it proposed would replace Schedule E in the Draft Undertaking:

### 1. Access Rights

- The Agreement will provide for non-exclusive train service entitlements for the operation of train services in terms of agreed service levels over the nominated network. Long-term train service entitlements can be varied only in accordance with agreed scheduling procedures specified in the agreement or as otherwise agreed between the parties.

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<sup>188</sup> Submissions received by the QCA in response to its Request for Comments Paper *Queensland Rail Draft Undertaking*.

<sup>189</sup> National Rail, Toll, QMC, AMC, Stanwell and Ensham Resources.

- It is the responsibility of the third-party entering into an access agreement with QR to ensure that the operator of train services utilising the access rights is accredited.
- Access agreements will be for a specified term and include a good-faith negotiation process for renewal.

## **2. Access Charges**

- Access charges are to be agreed between the parties and payable in accordance with the agreement. Late payments or credits by either party will bear interest at an agreed default rate.
- The agreement will provide for a fair and reasonable mechanism for dealing with bona fide disputed invoices.
- The agreement may provide for periodic review of access charges.
- Unless otherwise stated, all amounts payable under the agreement are exclusive of GST.
- In appropriate cases QR may require lodgement of a security deposit to secure performance by the third-party of its obligations under the agreement having regard to QR's reasonable assessment of the creditworthiness of the third-party.

## **3. Train Service Entitlements**

- The third-party shall not be entitled to commence train services unless and until all provisions of the agreement required to be completed or complied with prior to the commencement of train services have been completed or complied with by the due date specified in the agreement. QR will cooperate with the third-party to the extent reasonably necessary to facilitate the third-party's completion or compliance with such requirements.
- The third-party must only operate trains of the nominated specification for the transport of the nominated product type over the nominated network.
- Train service entitlements can be reduced by QR upon reasonable notice to prevent the hoarding of capacity and appropriate adjustments will be made to the access charges payable.

## **4. Day-to-Day Train Movements**

- QR is to have responsibility for train control and shall exercise train control having regard to the safe conduct of rail operations on the nominated network. Operations protocols will as far as practicable be consistent for all railway operators on the nominated network.
- The parties shall use all reasonable endeavours to ensure that the operation of train services is in accordance with the timetable developed in accordance with the train service entitlements or applicable under the train service entitlements and the agreed scheduling procedures. Timetables applicable to the day to day operation of the train services may be varied in the circumstances specified in the agreement (which normally include safety considerations, force majeure, incidents or emergencies, track possessions in accordance with the agreement or as otherwise agreed between the parties, such agreement not to be unreasonably withheld).
- The third-party is required to comply with all QR train control directions and ensure all trains and rollingstock are equipped with appropriate communication systems to comply with the rollingstock interface standards.

## 5. Train Operations

- The agreement will specify all reasonable operational, communication and procedural requirements for train services.
- The third-party is to comply with all laws, safeworking procedures and safety standards and all other train operations requirements in the Agreement. QR will comply with its safeworking procedures and safety standards and may, acting reasonably, vary the safeworking procedures and safety standards at any time following consultation with, and reasonable notice to, the third-party. Subject to such variations being on safety grounds, each party is responsible for its costs (including the costs of additional or modified equipment) in complying with the safeworking procedures and safety standards. Safeworking procedures and safety standards will as far as practicable be consistent for all railway operators on the nominated network.
- The parties may agree specific performance levels and measurement criteria as a basis for creating effective performance management and incentives. This may involve financially based incentives and sanctions. The performance levels may also be reviewed periodically.
- The agreement will specify relevant rollingstock interface standards. The third-party must obtain certification from an appropriately qualified person (both certification and person to be subject to the reasonable satisfaction of QR) that its rollingstock and rollingstock configurations comply with such rollingstock interface standards. Rollingstock and rollingstock configurations which are so certified will be included in the rollingstock specification as being authorised to operate on the nominated network subject to continuing compliance with the rollingstock interface standards and rollingstock specification.
- The third-party is responsible for the safe operation of its rollingstock on the nominated network and must ensure that at all times its rollingstock and rollingstock configurations comply with all applicable laws, the rollingstock specification and the rollingstock interface standards specified in the agreement. The operation of rollingstock and trains may be suspended by QR, acting reasonably, for non-compliance until such non-compliance is rectified.
- The third-party must ensure all loadings of rollingstock are secure.
- QR may, acting reasonably, vary the rollingstock interface standards at any time and where this necessitates modification of the third-party's rollingstock, the costs of such modifications are to be borne in the manner agreed by the parties or, failing agreement, as determined by an expert.

## 6. Infrastructure Management

- QR is responsible for the management and control of the nominated network.
- QR will carry out maintenance work on the nominated network such that, subject to applicable operational constraints and any other agreed criteria, the infrastructure is consistent with the rollingstock interface standards and the third-party can operate train services in accordance with its train service entitlements.
- QR may impose operational constraints (such as speed or load restrictions) for the protection of persons or property or to facilitate maintenance work or enhancements and has reasonable entitlements to take possession of the track for the purpose of maintenance work, emergency repairs and enhancements. In carrying out such work QR will use its reasonable endeavours to minimise disruption to train services so that the third-party can operate train services substantially in accordance with its train service entitlements.

- The agreement will contain principles for consultation with the third-party regarding maintenance that will impact on the third-party's schedule.
- The agreement will contain provisions requiring the parties to provide advice to each other in relation to factors that could affect the third-party's operation of train services or the integrity of the nominated network.
- The third-party may inspect the nominated network for the purposes of assessing the operational, environmental and safety risks with respect to the infrastructure as well as the standard of the infrastructure comprising the nominated network including, but not limited to, fencing and at grade crossing protection. QR will not be liable for claims in relation to, or arising out of, the standard of the infrastructure except where QR fails to maintain the infrastructure such that, subject to applicable operational constraints and any other agreed criteria, it is consistent with the rollingstock interface standards and the third-party can operate train services in accordance with its train service entitlements.
- The agreement will specify the reasonable terms and conditions on which the third-party will have access to the nominated network for the purpose of inspecting the standard of the infrastructure comprising the nominated network.

## **7. Incident Management**

- Prior to the commencement of train services the third-party is required to develop an emergency response plan containing procedures for dealing with incidents which must be consistent with QR's emergency procedures.
- In the event of an incident, QR is responsible for the overall coordination and management of incident responses and may, subject to using reasonable efforts to consult with the third-party, take any action it considers reasonably necessary to recommence services as soon as possible. The third-party is responsible for recovery of rollingstock and to cooperate and assist with the restoration of train movements.
- Investigations into incidents are to be commenced as soon as practicable after an incident and carried out in accordance with the process specified in the agreement. The parties must cooperate in any investigation and consult in good faith in relation to the implementation of any recommendations.

## **8. Environmental Protection and Other Issues**

- All environmental laws, regulations and relevant guidelines must be complied with.
- Environmental management must be approached on a risk identification and risk management basis with respect to operations on the nominated network and independent audits of a third-party's compliance with its environmental management system will be required in the absence of certification of the third-party's environmental management system in accordance with Standard ISO14001.

## **9. Accreditation**

- QR must have and maintain accreditation as a railway manager under the *Transport Infrastructure Act 1994* to the extent required to perform its obligations under the Agreement.
- Train services must be operated by an operator accredited as a railway operator under the *Transport Infrastructure Act 1994* and the operator must maintain such accreditation to the extent required to perform its obligations under the agreement.

**10. Third-party's Staff**

- The third-party is responsible for demonstrating through the safety risk assessment process the competence of all of its staff performing safety related work. QR may temporarily suspend the right of the third-party's staff to operate on the nominated network in the event of breach or likely breach of any laws, QR train control directions, safeworking procedures or safety standards.

**11. Safety Risk Management**

- Safety risk management must be addressed by risk identification through a joint safety risk assessment process and the formulation of a safety risk management plan. The parties will be required to comply with the safety risk management plan.

**12. Inspection and Audit Rights**

- Rights of inspection and audit in relation to the third-party's compliance with the agreement and inspection of trains and rollingstock shall be included in the agreement. The agreement will specify the terms and conditions on which QR can carry out such inspections and audits. Except in emergencies QR will, in carrying out any inspection or audit, give the third-party reasonable notice and use reasonable endeavours to minimise disruption to the third-party's train services.

**13. Insurance**

- The agreement will provide for insurances to be effected by the parties to appropriately provide for the relevant insurance risks.

**14. Indemnities and Liabilities**

- Each party is liable for and is required to release and indemnify each other for all claims in respect of personal injury, death or property damage caused or contributed to (to the extent of the contribution) by the wilful default or negligent act or omission of that party or its staff.
- The third-party is solely liable for and is required to release and indemnify QR for any damage to property or personal injury or death of any person being transported on train services.

**15. Limitation of Liability**

- The liabilities of the parties for default shall be limited as specified in the Agreement.
- Neither party has any liability for consequential loss or damage or loss of profits in any circumstances.
- Claims by either party must be lodged within twelve months of the occurrence of the event or circumstance giving rise to the claim.

**16. Material Change**

- Access charges will be adjusted to reflect the net impact of any material change where such material change results in a variation to the net cost to QR of performing its obligations under the Agreement.
- A material change shall be limited to changes in taxes, laws or reduction in available funding from QR's government infrastructure payments (ie a reduction in the amount of funding

available from such payments in respect to the nominated network shall be considered as an increase in the net cost to QR of performing its obligations under this Agreement).

- Any dispute regarding the impact on access charges as a result of a material change will be determined by an independent expert.

#### **17. Disputes**

- Any dispute between the parties is to be firstly referred in writing to the respective chief executives for resolution. If the dispute is not resolved then the parties may agree to refer the dispute for resolution by an expert or arbitration. If there is no agreement to resolve the dispute in this manner then the dispute is to be determined by a court.

#### **18. Default, Suspension and Termination**

- The agreement will specify events of default and rights of suspension and termination.

#### **19. Force Majeure Event**

- The obligations of either party (other than an obligation to pay monies due) will be suspended where by reason of a force majeure event that party is delayed in or prevented from carrying out its obligations under the agreement. The agreement will provide for relief in respect of the payment of access charges to the extent that QR is unable to provide access rights because of a force majeure event affecting QR.
- In the event that infrastructure on specified lightly trafficked corridors of the nominated network is damaged by a force majeure event and in QR's reasonable opinion the cost of repairing the damage is not economic, QR may elect not to proceed with repairs or replacement unless the parties agree as to the funding of the cost of that work.
- The access agreement will provide for a process which might result in termination of the agreement in the event that circumstances of prolonged force majeure prevents the performance by a party of its obligations.

#### **20. Assignment**

- The third-party may assign the whole of its rights and obligations under the agreement to a related body corporate provided that the assignor remains liable for the performance of obligations under the agreement or to a non-related body corporate with the prior written consent of QR (such consent not to be unreasonably withheld).
- A change in control of a third-party not a publicly listed corporation will be deemed to be an assignment of the agreement.

#### **21. QR's Access Undertaking**

- QR will comply with all applicable laws and the terms of QR's Access Undertaking in effect from time-to-time.

FreightCorp and Toll have subsequently raised concerns about particular aspects of the above schedule, including omissions from it. These concerns are discussed in the next section along with QR's responses to the concerns.

### 8.3 Area of disagreement between stakeholders and QR

At the Working Group meeting of 5 April 2000, stakeholders generally supported the development of a set of broad principles that would be included in a revised Schedule E. This was on the grounds that time constraints precluded QR and stakeholders agreeing the terms and conditions of a standard form access agreement prior to the release of the QCA's Draft Decision.

The paper prepared by stakeholders outlining their proposed broad principles is broadly consistent with QR's version of Schedule E outlined in the previous section.<sup>190</sup> However, there remained areas of disagreement.

#### 8.3.1 *Dispute resolution process*

There was general support amongst stakeholders for a dispute resolution process (ruling mechanism), to be administered by the QCA, that would complement the revised Schedule E. The ruling mechanism would allow parties to seek a non-binding ruling or position from the QCA - or an appropriate expert - as to the position that the QCA would likely take if an issue was subject to the arbitration procedures under the QCA Act.

QR responded that in the absence of specific legislative authority for a ruling mechanism, it perceived that there may be some difficulties associated with the QCA or its nominee making a preliminary ruling in respect of a matter that might ultimately become the subject of a formal arbitration before the QCA. QR was prepared to consider and respond to any proposal by the QCA in relation to a ruling mechanism.

#### 8.3.2 *Obligations on the access holder*

Stakeholders argued that all obligations of the access holder need to be clearly stated and agreed at the outset of the access agreement so that the access holder can accurately determine the total cost of the performance of its obligations under the access agreement. There should be clear mechanisms and principles to indicate the basis upon which QR can require changes to those requirements. As an overriding factor, QR should not be able to change the access holder's obligations without agreement, unless there is a genuine safety issue which requires QR to have the power to direct the access holder.

QR responded that it intends that each access agreement will be a complete statement of the respective rights and obligations of QR and the third-party. The mechanisms for variation of the provisions of the access agreement will be clearly specified in the access agreement, without the reservation to QR of any discretionary right to change the access agreement.

QR considered that this approach is clearly reflected in Schedule E and in this respect it referred to the following provisions of Schedule E which specifically reference the basis of variation of an access agreement:

- principle 1 - long-term service entitlements varied in accordance with scheduling procedures or as otherwise agreed between the parties;
- principle 4 - day-to-day train movements varied in accordance with specified circumstances including safety considerations, force majeure and incidents, or as otherwise agreed between the parties; and

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<sup>190</sup> A copy of the paper is available on the QCA website at [www.qca.org.au](http://www.qca.org.au).

- principle 5 - safeworking procedures and safety standards varied by QR at any time following consultation with, and reasonable notice to the third party. Rollingstock standards varied by QR at any time, acting reasonably.

### **8.3.3 *Obligation to act in good faith and in a non discriminatory manner***

Stakeholders argued that while the QCA Act provides that QR must not act in a discriminatory fashion, there should be an obligation in the access agreement to act in good faith and treat each rail operator on a non-discriminatory basis. There should also be a ‘most favoured nation’ provision which ensures that if any other rail operator - which should include QR above-rail business groups - is given a better access deal than another rail operator, then all operators should be provided with those arrangements.

In addition, the principle of non-discrimination should be included in relation to scheduling and capacity allocation. Network Access should be required to treat each operator equally, and in this context must consider QR’s above-rail business groups as a separate rail operator. Underpinning these obligations, the parties will need to ensure that Network Access maintains appropriate records of communications between all rail operators and that the operators are entitled to have access to those records for the purposes of determining compliance with the access agreement.

QR responded that the QCA Act and the Undertaking impose obligations that require QR to act in good faith and in a non-discriminatory manner. In this respect, QR did not see the need to replicate the detail of the legislation or the Undertaking in its access agreements.

### **8.3.4 *Accreditation agencies and regulatory bodies – oversight role of QR***

Stakeholders argued that Network Access should not have an exhaustive role in ‘second guessing’ the terms and conditions of an access holder’s accreditation. Once an access holder is accredited, Network Access should only be able to require and review details that go to the root of that accreditation for genuine safety and operational efficiency reasons. In principle, Network Access should rely on the accreditation of a rail operator as sufficient qualification for that operator to perform on the network.

It must be recognised that the access agreement should not provide the opportunity for an uncooperative Network Access to use issues that go to the accreditation of an operator - ie rollingstock accreditation, staff accreditation etc, - as a mechanism to frustrate access. FreightCorp understands that Network Access considers that an access holder would have rights against QR pursuant to the QCA Act (for hindering access) if this were to occur. FreightCorp considers that an access holder should have a direct contractual right against QR under these circumstances.

Stakeholders argued that all staff should be appropriately accredited. The obligation should be reciprocal. QR should not have the right to require additional training obligations over and above the accreditation requirements. This is a cost issue for an access holder, which must be clearly identified and dealt with prior to entering into an access agreement.

QR responded that the relationship between the requirements of accreditation and regulatory bodies and the requirements of QR under access agreements in relation to similar issues has been the subject of discussion between QR and the QCA.

### **8.3.5 Access charges<sup>191</sup>**

Stakeholders stated that payment terms that are commercially reasonable should be included. The mechanism should not inhibit the raising of genuine disputes.

In addition, the security required by QR - if any - should be commensurate with the creditworthiness of the access holder. In this regard, objective criteria in relation to creditworthiness, such as S&P or Moody's credit rating, should be applied. The amount of any such security should also be determined in relation to the revenue risk which Network Access is in fact taking. That is, if the access agreement provides for Network Access to suspend access rights within 30 days for non-payment of access charges, the amount of any security should be limited to the equivalent amount of that month's access charges.

### **8.3.6 Train service entitlements**

FreightCorp stated that QR should provide a 'reasonable endeavours' commitment to facilitate a third-party's compliance with the requirements that are prerequisites to the commencement of its train services.

QR responded that it is the third-party's responsibility to satisfy such requirements. QR's responsibility is to facilitate compliance and not to use all reasonable endeavours to achieve compliance.

### **8.3.7 Day to day train movements**

FreightCorp proposed a change in QR's wording such that timetables for train services may be varied for 'genuine' safety, rather than merely safety considerations. FreightCorp's proposed change reflected its concern about the potential for the scheduling and train control functions to be performed in a non-discriminatory manner.

QR responded that FreightCorp's use of the word 'genuine' before safety considerations implied that there might be 'genuine' and 'non-genuine' safety considerations. QR considered that a particular circumstance could be objectively assessed to be a safety consideration or not, and the use of the word genuine was neither helpful nor appropriate. QR also argued that the QCA Act and the Undertaking impose obligations that require QR to act in good faith and in a non-discriminatory manner.

### **8.3.8 Train operations**

Stakeholders argued that QR should be able to vary the rollingstock interface standards at any time - after consultation - for a 'genuine' safety reason. Any other reason for changes needs to be agreed and negotiated with a rail operator. An operator should be compensated by Network Access when it is required to modify its rollingstock due to changes in the standards.

FreightCorp accepted that there is a requirement for a suitably qualified person to certify that rollingstock complies with the relevant standards and does so in accordance with an auditable process. However, it did not accept that Network Access should have the right to review the certification that is given as a result of that process from the suitably qualified person. This involves duplication, which is unnecessary, time-consuming and costly. The audit of the process used by the qualified person should be carried out by an independent person, agreed by the parties.

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<sup>191</sup> Stakeholders stated that generally, access charges must reflect the efficient costs of providing access, any costs imposed on other users, plus a reasonable rate of return.

FreightCorp accepted that Network Access must have the right to suspend rollingstock if non-compliance with an access agreement creates a ‘genuine’ safety issue. If the non-compliance does not have safety implications, the operator should be required to rectify the issue within a reasonable period of time, but not be suspended.

QR considered it unnecessary to make variations in the rollingstock interface standards conditional on consultation with rail operators, on the grounds that QR’s obligation to ‘act reasonably’ in making such variations would necessarily imply consultation with operators.

### **8.3.9 Infrastructure management**

Stakeholders argued that QR should be obliged to maintain the network to a standard that meets its obligations under access agreements, not to the minimum standard required under its accreditation, which would be insufficient.

FreightCorp argued that QR’s commitment to maintain its infrastructure to a standard consistent with rollingstock interface standards and such that third parties could operate train services in accordance with train service entitlements conditional on ‘applicable operational constraints’, was too weak. Rather, Network Access should commit to providing the train service entitlement – except in the event of force majeure – and any failure to provide the contracted level of service as a result of operational constraints should be covered by the key performance indicator regime or through compensation to the rail operator.<sup>192</sup> Similarly, the reference in Schedule E to a third-party operating train services ‘substantially’ in accordance with its train service entitlements was too weak and the word ‘substantially’ should be removed.

In addition, the access agreement should contain principles for consultation with operators regarding maintenance. Most maintenance will be planned and capable of discussion with rail operators before it impacts on their schedules.

The access holder should have the right to inspect the infrastructure comprising the declared network in order to satisfy itself as to the standard of the infrastructure and to assess the operational, environmental and safety risks associated with operation of train services on the infrastructure.

QR responded that Schedule E specifies QR’s obligation to maintain the infrastructure such that it is consistent with the rollingstock interface standards and such that the third-party can operate substantially in accordance with its train service entitlements. QR argued that it is unreasonable to suggest that it should have no right to impose operational constraints. Moreover, the imposition of operational constraints necessarily implies that there may be some disruption to train service entitlements and for that reason the caveat of ‘substantially’ meeting its commitments must be retained.

QR argued that it had undertaken to use its reasonable endeavours to minimise any disruption to train service entitlements and that its failure to meet the required performance levels may result in the imposition of financial sanctions.

### **8.3.10 Incident management**

FreightCorp proposed that the third-party should be required to develop an emergency response plan which must ‘not be inconsistent’ rather than ‘be consistent’ with QR’s emergency procedures.

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<sup>192</sup> Toll shared FreightCorp’s views.

QR responded that as it had responsibility for safety on the network, it considered that a third-party's emergency response plan must be consistent with QR's emergency procedures. Consequently, QR did not accept FreightCorp's proposed wording change.

Stakeholders recognised that in some instances Network Access needs to be able to require an access holder to utilise its assets for the benefit of removing any temporary network restrictions, which may arise as a result of, for example, an incident. Nevertheless, Network Access should be required to compensate an access holder for diverting its assets to assist in any such situations.

In this context, the access holder should be able to claim as a minimum, cost plus a fixed percentage for its requirement to assist in such circumstances. Network Access should be responsible for payment of those costs, with it seeking recompense from the parties whose actions gave rise to the incident.

QR was strongly of the view that the provision of rescue and recovery services for rail operators on the network does not comprise part of the service which has been declared for the purposes of the QCA Act and which is the subject of QR's Draft Undertaking. It is the responsibility of rail operators to put in place arrangements to effect rescue and recovery services in respect of their rollingstock that is operating on the network.

QR did not accept that, in its capacity as manager of the network, it should be responsible for brokering arrangements between rail operators.

#### **8.3.11 Environment protection and other issues**

Stakeholders argued that all rail operators must comply with environmental health and safety laws and have an appropriate environmental health and safety system. QR should not be able to require a higher level of compliance than is required at law, nor should it be able to act as a regulator in these matters.

#### **8.3.12 Third-party's staff**

FreightCorp proposed that QR's suspension right regarding a third-party's staff should apply in the event of breach, but not, as QR proposed, 'likely' breach of any laws, QR train control directions, safeworking procedures or safety standards.

QR responded that it would address this matter with the QCA.

#### **8.3.13 Inspection and audit rights**

Stakeholders argued that generally, subject to confidentiality, either party should have a right to inspect and audit to ensure compliance by the other party with the agreement - at its own cost. Such audits should not cause unwarranted disruption to the other party, for example, due to unreasonable frequency. FreightCorp proposed a number of wording changes to QR's Schedule E to reflect reciprocity in audit and inspection rights.

QR responded that at a superficial level, a reciprocal approach in relation to inspection and auditing appears reasonable. The difficulty is that the adoption of this approach would require QR to submit to a contractual right of audit by all rail operators on the network. The potential for substantial disruption, additional cost to QR and variance in outcome because of different audit standards and procedures was a significant concern to QR if all operators are to have contractually conferred audit rights.

QR argued that it is common practice for railway managers/owners in other States to have rights of inspection and audit with respect to records, procedures and compliance with the access agreement

generally including inspection of trains and rollingstock. QR does provide the third-party with a right of inspection of its rail infrastructure.

Furthermore, QR's obligation to report publicly on compliance with the Undertaking together with QCA's overview of the Undertaking should be sufficient for QR to deliver the required performance outcomes.

#### **8.3.14 Indemnities and liabilities**

Stakeholders argued that the parties need to consider whether indemnities are in fact appropriate and if so, they should be reciprocal. FreightCorp proposed that a third-party's liability should be reduced to the extent that any loss or injury is caused by QR.

QR responded that the purpose of the indemnity provision of Schedule E is to ensure that the third-party assumes the responsibility for damage to property or injury to persons being transported on train services operated by that third-party. The rationale for this requirement is that the risk in relation to such damage or injury is best managed by that third-party for the reason that:

- the third-party knows, or ought to know, the detail of the property being carried and the risks associated with the carriage of that property. This information will not be known by QR; and
- the third-party can manage that risk by, as is usually the case, limiting the extent of its liability under the terms of carriage of the relevant property or person and thereby transferring the insurance risk to the consignor of the property or the person being carried.

#### **8.3.15 Limitation of liability**

Freight Corp proposed that the liabilities of the parties for default should be limited as 'agreed', not as 'specified', in the Agreement.

#### **8.3.16 Material change**

Stakeholders argued that QR should not have the capacity to pass through material changes in its cost base without consultation with the access holder. FreightCorp proposed that reference to 'laws' as a material change should be removed and that 'increases' as well as 'decreases' in government infrastructure payments should be recognised.

QR responded it is fundamental that, if it is to enter into long-term access agreements with fixed access charges, then it must have the ability to pass on increases in costs arising from any change in law which impacts on the net cost to QR of performing its obligations under the relevant access agreement. Such an increase in net costs would be outside QR's control and it is usual to manage the exposure to the risk of additional costs arising from a change in law in this way.

QR did not accept that an increase in government funding must flow through to the third-party in the form of a reduction in the agreed access charges. QR is not aware of any circumstances where it would be appropriate for access charges payable by a third-party to be automatically reduced. Should that be the intent of the change in funding, then it would be expected that Government would specify the desired outcome and require QR's compliance.

Principle 16 otherwise provides for a pass-through to the third-party of the net impact of a change in law which results in a reduction in the net cost to QR of performing its obligations under the access agreement.

### **8.3.17 Default, suspension and termination**

Stakeholders argued that access rights should not be suspended for financial default, only where such default is likely to cause disruption to train movements or create risks to the safety of any person or property. Train services should be suspended if the third-party operator's accreditation is suspended or cancelled. However, QR may approve the operation of train services by another accredited operator.

QR responded that it remained strongly of the view that it should have the right to suspend access rights if the operator fails to pay access charges, and in other circumstances that may impact on the integrity of the network and safety operations on the network.

Stakeholders argued that in addition to specific rights of termination in the agreement, the parties will have the right to terminate the agreement for material events of default. These events of default must be clearly stated. A right to terminate for material event of default should not be a 'hair trigger' provision, but should provide for the relevant party with an opportunity to attempt to cure the event first. FreightCorp proposed that Schedule E should reflect that the agreement will specify 'agreed' events of default.

### **8.3.18 QR's Access Undertaking - confidentiality and ring-fencing**

Stakeholders argued that the access agreement should reflect the spirit and intent of the Ring-fencing Guidelines by containing appropriate confidentiality provisions that give the access holder sufficient comfort that:

- information which may be required by Network Access for the purposes of the access agreement will only relate to the implementation of the agreement – for example safety and capacity issues – but only to the extent absolutely necessary;
- the information so provided will only be used by Network Access for the purposes of the access agreement and will not be provided to the above-rail sections of QR without the consent of the access holder;
- Network Access will implement systems and procedures to protect the integrity and separation of that information; and
- information gained by QR through the provision of services such as train scheduling and train control will not be available to any QR officer that is involved in the preparation for, or conduct of, any commercial negotiations or customer interface beyond that directly required to carry out the scheduling and train control functions.

QR responded that ring-fencing will be dealt with in the Undertaking, which is itself enforceable under the QCA Act. Furthermore, Principle 21 contains a commitment by QR to comply with all applicable laws and the terms of the Undertaking in effect from time-to-time. QR did not accept the need to further entrench the ring-fencing provisions in each access agreement. In particular, QR did not believe that it should be bound by the Undertaking if it ceases to be of effect.

## **8.4 QCA's assessment of outstanding matters**

### **8.4.1 Dispute resolution process**

The QCA understands that it does not have the power to perform the proposed ruling mechanism, on the grounds that it effectively entails a party seeking a pre-judgement from the QCA on a matter that

may become subject to future arbitration under the QCA Act. This would imperil the outcome of a future arbitration on the matter on the grounds that there was a breach of the rules of natural justice.<sup>193</sup>

Nevertheless, s115A of the QCA Act allows the Authority to refer access disputes to mediation. As with the proposed ruling mechanism, the QCA understands that its performance of a mediation role in a dispute which it later arbitrates under the QCA Act may jeopardise the efficacy of the QCA's determination. Consequently, if the QCA believed that a mediated resolution of an access dispute during an access negotiation could be achieved, it would refer the dispute to an independent mediator.

In practice, the performance of this mediation role could potentially deliver a similar outcome to the proposed ruling mechanism, including a shortening of the period between the commencement of an access negotiation and the signing of an access agreement. The QCA is aware that such negotiations in the rail sector can extend up to 12 months. A mechanism that facilitates a reduction in the average duration of the access negotiation process would appear to be consistent with protecting QR's legitimate business interests and the interests of access seekers.

In the event of failure of mediation, an access seeker would have recourse to the formal arbitration procedures established by the QCA Act. In arbitrating a dispute over the standard terms and conditions of an access agreement, the QCA would take into consideration the approaches adopted by access providers in other Australian rail jurisdictions. The Authority recognises that the characteristics of rail networks, the associated traffics and commercial imperatives of access providers vary across jurisdictions and may justify different approaches to the setting of access terms and conditions. However, the QCA is conscious of the complaints of rail operators regarding the costs associated with dealing with the multiplicity of access regimes across Australia and considers there is merit in there being consistency in QR's approach compared with other access providers where QR's legitimate business interests are not threatened.

#### **8.4.2 Obligations on the access holder**

The QCA believes that, in practice, the establishment of clear contractual rights and obligations with respect to QR and access seekers will come down to the actual drafting of the access agreement between the parties. Nevertheless, the most sensitive issue is likely to be QR's basis for variation of the provisions of an access agreement, in particular, variations in the access seeker's train service entitlement.

QR has advised the QCA that it has differentiated between long-term and short-term train service entitlements in the revised Schedule E principles. Principle 1 addresses the long-term, providing that entitlements can only be varied in accordance with agreed scheduling procedures specified in the access agreement or as otherwise agreed between the parties. Principle 4 addresses the short-term, providing that day-to-day train schedules may be varied in the circumstances specified in the agreement, including safety considerations, force majeure, incidents or emergencies, track possessions or as otherwise agreed between the parties, such agreement not to be unreasonably withheld.

The QCA believes that Principles 1 and 4 of the revised Schedule E establish reasonable parameters within which QR and an access seeker would negotiate and agree on the circumstances where QR could vary the access seeker's train service entitlements.

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<sup>193</sup> Section 20(2)(a) of *Judicial Review Act 1991* (Qld).

### 8.4.3 *Obligation to act in good faith and in a non-discriminatory manner*

The QCA Act provides that an access provider and access seeker must negotiate in good faith for reaching an access agreement. S104 and s125 of the QCA Act are directed at preventing an access provider engaging in conduct for the purpose of preventing or hindering access.

The QCA believes that inserting a general obligation to act in good faith in access agreements would have potentially complex commercial implications. It would be difficult to prescribe a fair result in advance except by way of specific rules. As with QR's right to suspend a third-party operator's train services and/or staff, it is only after the event that an assessment can be made of the nature of QR's decision.<sup>194</sup>

Nevertheless, the QCA's Draft Decision has proposed specific measures to be incorporated in the Undertaking to facilitate non-discriminatory treatment of third-party operators compared to QR's above-rail business groups. These measures include:

- a right for a third-party operator to seek a rate review where it can demonstrate that Network Access has sold a like train path to another rail operator for a lower price than applies to the third-party operator;<sup>195</sup> and
- the development of Network Management Principles, to be incorporated as a schedule to an approved Undertaking, that include a commitment by QR that the identity of a rail operator will, of itself, play no part in a decision by QR's train control to alter the rail operator's scheduled train services. This is complemented by QR's commitment to report train control information in real time and after the event to all rail operators using QR's network.<sup>196</sup>

The QCA recognises that identification of a list of specific cases where good faith arrangements could be appropriate would be one means of providing greater certainty to QR and at the same time protecting third-party operators' interests. Such a list could be incorporated in the Schedule E principles. Nevertheless, the QCA believes that the onus should be on stakeholders to identify cases where good faith arrangements could be appropriate. The QCA is prepared to consider the merits of including any such cases in the Schedule E principles.

### 8.4.4 *Accreditation agencies and regulatory bodies – oversight role for QR*

The QCA recognises stakeholders' concerns regarding the potential overlap in regulatory responsibilities of QR and bodies such as the Rail Safety Accreditation Unit of Queensland Transport and the Environmental Protection Agency. This matter was discussed in Chapter 7.

### 8.4.5 *Access charges*

The QCA has some concerns about QR's proposed principles for payment of access charges, on the grounds that the potential exists for Network Access to exert significant commercial leverage as the provider of a monopoly service.

The QCA has proposed the following italicised change to the first dot point of principle 2 to provide greater protection to third parties' interests:

- “Access charges are to be agreed between the parties and payable in accordance with *reasonable payment terms* set out in the agreement”.

<sup>194</sup> The matter of QR suspending a third-party's train services or staff was discussed in Chapter 7.

<sup>195</sup> Pricing matters are discussed in Chapter 5 of the Draft Decision.

<sup>196</sup> Scheduling and train control processes are discussed in Chapter 6.

The QCA does not believe that the proposed change adversely affects QR's legitimate business interests, but rather provides a counter-weight to Network Access' commercial leverage.

Finally, the QCA recognises stakeholders' concerns that QR's reference to a 'reasonable assessment' of the creditworthiness of a rail operator provides Network Access with significant scope to use its discretion. Nevertheless, the QCA recognises that QR faces a risk that a third-party using its network will default on paying its access charges and it has legitimate commercial reasons to manage that risk. The difficult matter is finding a way to manage that risk which balances QR's legitimate business interests and the interests of access seekers.

The usual way of managing such a risk is for the access provider to require a prudential contribution or security deposit. Such contributions can, however, serve as a barrier to entry if they:

- involve a high administrative burden on users;
- are imposed - or are perceived to be imposed - on an arbitrary or subjective basis; or
- are set at an amount disproportionate to the risk involved.

In principle, the QCA believes that QR's requirement for security from an access seeker should be linked to its potential exposure. In this way, QR protects its legitimate business interests. In practice, however, assessing the potential exposure is difficult.

It would appear unreasonable to impose security arrangements on an access seeker who is a substantive entity and has a track record of timely payment of similar obligations. Nevertheless, where QR negotiates long-term access agreements, that is, in excess of five years, which would likely have an access charge with fixed and usage-based components, it is likely to face a significant financial exposure regardless of the track record of the access holder.

The QCA believes that it would be unreasonable for QR to require an access seeker to pay the fixed charge component of the full term of a long-term access agreement as a security deposit. This would likely serve as a barrier to third-party entry. Moreover, the QCA expects that in terminating or suspending an access agreement, QR would have taken additional steps to protect its financial exposure by reserving itself the right to recover damages or pursue other remedies under the agreement. However, the approach will depend upon the circumstances. For example, in a situation where it is agreed that QR undertakes an investment for a customer on the basis of that customer entering a long-term contract, then it could be reasonable for QR to seek to protect its exposure via a security arrangement.

Some users will not be able to demonstrate a track record of timely payment of similar obligations, as they may be new corporate entities or special-purpose vehicles without guarantees. For such users, the QCA believes that any security should reflect the revenue risk that QR has taken on. The QCA supports stakeholders' argument that if the access agreement provides for QR to suspend access rights within 30 days for non-payment of access charges, subject to the raising of genuine disputes, the amount of any security should be limited to the equivalent of that month's access charges. By linking any required security to QR's revenue risk, the QCA believes that QR's scope to use its discretion regarding a 'reasonable' assessment of a third-party's creditworthiness is constrained.<sup>197</sup>

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<sup>197</sup> The QCA recognises that a third-party's inability to meet a solvency test prior to entering into an access agreement would be a relevant factor in QR's assessment of required security. Solvency was discussed in Chapter 4.

Where there are no security arrangements in place and a user defaults on its payments, QR should be entitled to require some form of security equivalent to QR's financial exposure, where the default was not attributable to a legitimate dispute.

Where the security deposit is by way of up-front payment of access charges in advance, the access seeker paying the security deposit should be credited interest on the security at a market-based rate.

As a result of the above arguments, the QCA has proposed the following italicised changes to principle 2, fifth dot point:

- “In appropriate cases, QR may require lodgement of a security to secure performance by the third-party of its obligations under the agreement having regard to QR's reasonable assessment of the creditworthiness of the third-party. *An established rail entity's ability to demonstrate a track record of timely payment of similar obligations in other rail jurisdictions should be a relevant factor in assessing creditworthiness. Any required security should reflect the revenue risk that QR has taken on.*”

The QCA has proposed the following additional text to be incorporated in principle 2 of Schedule E:

- “Where there are no security arrangements in place and a user defaults on its payments, QR is entitled to require some form of security equivalent to its financial exposure, where the default was not attributable to a legitimate dispute.”
- “A third-party paying a security deposit should be credited with interest on the security at a market based rate for as long as it is held by QR.”

#### 8.4.6 *Train service entitlements*

The QCA believes that a ‘reasonable endeavours’ commitment by QR to assist a third-party complete or comply with those provisions of an access agreement that are a pre-condition to the third-party commencing its train services establishes a clearer obligation than the wording proposed by QR. In addition, the QCA does not believe that such an obligation would impose an onerous burden on QR. This is likely to be important in terms of obligations QR may seek to require of a third-party, for example, through the joint safety risk assessment, or Railway Noise Management Code of Practice. It would require the following deletion and italicised change to principle 3, first dot point:

- “QR will *use all reasonable endeavours to* co-operate with the third-party ~~to the extent reasonably necessary~~ to facilitate the third-party's completion or compliance with such requirements.”

#### 8.4.7 *Day-to-day train movements*

The QCA believes that QR's obligation to use ‘all reasonable endeavours’ to ensure that train services operate in accordance with train service entitlements and agreed scheduling procedures is too weak and provides insufficient certainty to third parties that QR will deliver on its contractual commitments.

The QCA discussed the link between train service entitlements and the development of train schedules, in particular, the master and daily train plans, in Chapter 6. In negotiating train service entitlements, QR should be aware of what capacity - train paths - is available on its network. Consequently, once QR has negotiated a train service entitlement with a third-party, it should be obliged to deliver that entitlement, subject to force majeure events and any other agreed criteria. If QR fails to deliver a third-party's entitlement, there should be a contractual penalty. Under a ‘reasonable endeavours’ commitment, QR would be able to depart from a contractual commitment regarding train service entitlements without penalty.

The QCA also has concerns that QR refers to day-to-day train movements in the context of ‘timetables’ rather than the ‘daily train plan’. The daily train plans are the key short-term scheduling documents used by QR. Timetables are only relevant for passenger travel. The QCA believes it would be useful for the terminology in Schedule E to be consistent with that used in the rest of the Draft Undertaking.

Consequently, the QCA has proposed the following deletion and italicised change to principle 4, second dot point:

- ~~“The parties QR shall use all reasonable endeavours to ensure that the operation of train services is in accordance with the timetable developed in accordance with the train service entitlements or applicable under the train service entitlements and the agreed scheduling procedures relevant daily train plan Timetables applicable to the day to day operation of the train services Daily train plans, which may be varied in the circumstances specified in the agreement (which normally include safety considerations, force majeure, incidents or emergencies, track possessions in accordance with the agreement or as otherwise agreed between the parties, such agreement not to be unreasonably withheld).”~~

The QCA does not support the inclusion of the word ‘genuine’ before ‘safety consideration’ as proposed by FreightCorp, recognising the practical difficulty in differentiating between a ‘genuine’ and ‘non-genuine’ safety consideration. Nevertheless, the QCA recognises that the exercise of QR’s right to change a third-party’s scheduled train services as a result of safety considerations could be a source of dispute.

Consequently, the QCA believes that QR should be able to change a train schedule due to safety considerations. However, if QR is subsequently unable to provide a reasonable justification for the change within the context of the contractual relationship, the third-party should be compensated for the disruption to its train services.

The QCA has decided not to approve QR’s proposed rollingstock interface standards in their current form.<sup>198</sup> Consequently, the QCA has proposed the following italicised change to principle 4, third dot point:

- “The third-party is required to comply with all QR train control directions and ensure all trains and rollingstock are equipped with appropriate communication systems to comply with the *agreed* rollingstock interface standards.”

#### 8.4.8 Train operations

A central aspect of any access agreement is likely to concern the adherence of both parties to specific performance levels and management criteria. Indeed, it is expected that failure to agree on such issues could become a major source of dispute. This emphasises the commercial imperative that such matters be reflected in access agreements and, in turn, Schedule E.

Consequently, the QCA has proposed the following italicised change to principle 5, third dot point:

- “The parties ~~may~~ *should* agree specific performance levels and measurement criteria as a basis for creating effective performance management and incentives. This may involve financially-based incentives and sanctions.”

The rights and obligations of QR and third-party operators regarding changes to rollingstock standards and suspension of a third-party operator’s rollingstock were discussed in Chapter 7. In

<sup>198</sup> This matter was discussed in Chapter 7.

order to provide greater protection to third-party operator’s interests, the QCA proposed the following deletion and italicised changes to principle 5, fifth and seventh dot points:

- “The third-party is responsible for the safe operation of its rollingstock on the nominated network and must ensure that at all times its rollingstock and rollingstock configurations comply with all applicable laws, the rollingstock specification and the rollingstock interface standards specified in the agreement. *QR may suspend the operation of rollingstock and trains for demonstrated non-compliance that has safety implications*—~~The operation of rollingstock and trains may be suspended by QR, acting reasonably, for non-compliance until such non-compliance is rectified. If the source of non-compliance does not have safety implications, the third-party should be required to rectify the non-compliance within a reasonable period of time, but not be suspended. If the non-compliance is not rectified within a reasonable period, QR may suspend the operation of the affected rollingstock and trains.~~”
- “QR may, acting reasonably, vary the *agreed* rollingstock interface standards at any time *on safety grounds, after consultation with the third-party*. *Otherwise, QR may, acting reasonably, negotiate any other changes with the third-party*. Where any changes in the standards necessitate modification of the third-party’s rollingstock, the costs of such modifications are to be borne in the manner agreed by the parties or, failing agreement, as determined by an expert.”

The QCA has proposed the incorporation of three additional points under principle 5:

- “QR will not exercise its suspension power in relation to a third-party’s rollingstock and trains in such a manner as to hinder or restrict access to the declared service in any way contrary to s104 and s125 of the QCA Act.”
- “If the suspension of a third-party operator’s rollingstock becomes a source of disputation, in the absence of an alternative dispute resolution process agreed between the parties, the Undertaking’s dispute resolution procedures could be triggered.”
- “A third-party operator could reserve the right that if its rollingstock is suspended without reasonable justification, then QR would be liable for the loss thereby caused.”

#### **8.4.9 Infrastructure management**

The proposed Schedule E principles provide caveats to QR’s commitment to deliver a third-party’s train service entitlements in the face of maintenance work on its network. Specifically, there is reference to train service entitlements being delivered subject to ‘applicable operational constraints’ and a third-party operating train services ‘substantially’ in accordance with its train service entitlements.

The QCA believes that such caveats would weaken QR’s obligation to deliver a third-party’s contracted train service entitlement, by providing QR with a reasonably wide discretion to depart from such an entitlement on the grounds of it carrying out maintenance work. Moreover, this discretion could allow QR to maintain its track to a lower standard than contracted - and paid for - without facing a penalty. The QCA believes that QR, as network manager, should bear the risk of maintaining its rail infrastructure to an agreed standard.

The QCA recognises that train service entitlements cannot be delivered if a force majeure event occurs. However, beyond that, any failure on QR’s part to deliver train service entitlements should be addressed through the performance regime – reflected in key performance indicators - negotiated with the third-party.

Consequently, the QCA has proposed the following deletions and italicised changes to the second, third and sixth dot points of principle 6:

- “QR will carry out maintenance work on the nominated network such that, subject to ~~applicable operational constraints and any other~~ agreed criteria, the infrastructure is consistent with the *agreed* rollingstock interface standards .....
- “In carrying out such [maintenance] work, QR will use its reasonable endeavours to minimise disruption to train services so that the third-party can operate train services ~~substantially~~ in accordance with its train service entitlements.”
- QR will not be liable for claims in relation to, or arising out of, the standard of the infrastructure except where QR fails to maintain the infrastructure such that, subject to ~~applicable operational constraints and any other~~ agreed criteria, it is consistent with the *agreed* rollingstock interface standards.....”

#### 8.4.10 Incident management

The QCA has accepted FreightCorp’s proposal that a third-party’s emergency response plan should ‘not be inconsistent’ with QR’s emergency procedures. The key objective for such plans is that they are compatible and that there is a co-ordinated response to an emergency. The QCA believes that a plan not being inconsistent is a more straightforward test for a third-party to meet than the consistency test proposed by QR, however, the key objective of preparing such plans would not be jeopardised.

Consequently, the QCA has proposed the following italicised change to principle 7, first dot point:

- “Prior to the commencement of train services, the third-party is required to develop an emergency response plan containing procedures for dealing with incidents which must *not* be *inconsistent* with QR’s emergency procedures.”

Disagreement between QR and stakeholders has arisen regarding the respective roles and responsibilities of Network Access and rail operators in relation to the rescue and recovery of broken-down rollingstock on QR’s network. In understanding this issue, the QCA believes that it is important to differentiate between two types of rollingstock rescue and recovery service. First, rescue and recovery of rollingstock that is causing a network blockage. The key objective of such rescue is the short-term imperative of moving the broken-down rollingstock off the mainline to a breakdown siding in order to allow other trains to utilise the network. Second, recovery of rollingstock from a breakdown siding. Once a train has been moved off the mainline and is no longer causing a blockage, the affected operator needs to make arrangements to move its broken-down rollingstock to a maintenance facility within a reasonable period (assuming the maintenance cannot be undertaken at the breakdown siding). The key difference between the two types of rescue service is that the removal of the rollingstock is less time-critical for the second case.

The QCA believes that there are sound operational and safety reasons for Network Access to coordinate the clearance of network blockages, for example, as a result of an incident. To this end, Network Access may need to utilise the rollingstock of a third-party operator or a QR above-rail business group to assist it in the recovery task. It would be open for QR to require that access agreements contain a requirement that access seekers make rollingstock available for the purposes of clearing blockages.

The QCA accepts QR’s argument that it is the responsibility of rail operators to put in place arrangements to effect the second type of rescue and recovery service. However, the QCA believes that this would not automatically imply that a third-party operator would need to retain spare locomotives for recovery purposes. The QCA accepts that it is reasonable for QR to expect a rail operator to have a recovery plan for its rollingstock including effecting the recovery within a reasonable period. However, the provision of spare locomotives is not the only way that rollingstock can be recovered from a breakdown siding. For example, a train consist could be split in two and moved by one locomotive in two separate runs. The QCA believes that if QR were to insist that a

third-party operator’s recovery arrangements incorporated the provision of spare locomotives when that operator could demonstrate satisfactory alternative means of recovering rollingstock, then it would become a barrier to entry for third-party operators.

Accordingly, the QCA considers it appropriate that Network Access retain the right to direct any rail operator to assist in the clearance of a blockage. Moreover, third parties are entitled to expect that all rail operators using QR’s network be subject to the same obligation. However, this obligation should be subject to the rail operator that performs the clearance task being compensated if its assets, human and capital, are required for recovery purposes. The derivation of the charge should be specified in the access agreement. QR should be responsible for those costs, with it seeking recompense from the party whose actions gave rise to the blockage. The QCA does not believe that the charge should reflect consequential damages, on the grounds stakeholders are unanimous the imposition of consequential liabilities is premature for the rail industry at this time. Rather, the charge should reflect both the cost of labour - relevant hourly wage rate - and rollingstock - including fuel and a rate of return on capital - for the period the operator’s rollingstock was used for recovery purposes.

Consequently, the QCA has proposed the following deletion and italicised changes to principle 7, second dot point, and the incorporation of an additional point:

- “The third-party is ~~responsible for recovery of rollingstock and~~ to cooperate and assist with the restoration of train movements *in accordance with directions from train controllers seeking to coordinate the clearance of network blockages. Any third-party so directed should be adequately compensated for doing so and is entitled to expect that all rail operators are subject to the same obligation.*”
- “*Once a third-party’s train has been moved off the mainline and is no longer causing a blockage, it is responsible for implementing its recovery plan for the broken-down rollingstock, including effecting the recovery within a reasonable period.*”

#### **8.4.11 Environmental protection and other issues**

The QCA discussed the environmental provisions of the Draft Undertaking in Chapter 7.

In that chapter, the QCA argued that QR’s auditing requirements should be linked to the environmental risks posed by a third-party operator’s train services. However, QR’s requirement for an annual external audit goes beyond what a third-party operator must do in order to meet its obligations under the EPA Act. Consequently, the QCA has proposed the following deletion and italicised change to principle 8, second dot point:

- “Environmental management must be approached on a risk identification and risk management basis with respect to operations on the nominated network. ~~and independent audits of a third party’s compliance with its environmental management system will be required in the absence of certification of the third party’s environmental management system in accordance with Standard ISO14001.~~ *Auditing requirements should be linked to the environmental risks posed by a third-party’s train services and be established in that third-party’s environmental management system.*”

The QCA has proposed an additional point regarding a third party’s obligation to inform QR of non-compliance with its environmental management system:

- “The third party is required to inform QR of non-compliance with its environmental management system and provide details of how it intends to address the non-compliance. The operator is required to rectify the breach as soon as practicable, having regard to the nature of the breach and any action required by EPA.”

#### 8.4.12 *Third-party’s staff*

The QCA has rejected FreightCorp’s proposal that QR’s right to suspend a third-party’s staff should only apply to actual rather than likely breaches of laws, train control directions, safeworking procedures or safety standards. This is because it is possible to envisage situations where it is prudent for QR to act to prevent a breach occurring rather than waiting for the breach to occur and then take action. Nevertheless, the QCA has proposed that a third-party should have a right to seek damages if QR takes action in response to a likely breach but is subsequently proven to have acted in error. The onus would be on QR to demonstrate that its action was reasonable.<sup>199</sup>

The QCA has proposed the following deletion and italicised changes to principle 10, first dot point, and three additional points:

- “The third-party is responsible for demonstrating *to the Rail Safety Accreditation Unit* through the joint safety-risk assessment process, the competence of its staff performing safety-related work. QR may ~~temporarily~~ suspend the right of the third-party’s staff to operate on the nominated network in the event of breach, or likely breach, of any laws, QR train control directions, safeworking procedures or safety standards, *until such non-compliance is rectified.*
- *QR will not exercise its suspension power in relation to a third-party’s staff in such a manner as to hinder or restrict access to the declared service in any way contrary to s104 and s125 of the QCA Act.*
- *If the suspension of a third-party operator’s staff becomes a source of disputation, in the absence of an alternative dispute-resolution process agreed between the parties, the Undertaking’s dispute-resolution procedures could be triggered.*
- *A third-party operator could reserve the right that if its staff are suspended without reasonable justification, then QR would be liable for the loss thereby caused.”*

#### 8.4.13 *Inspection and audit rights*

The QCA believes that, in principle, and subject to the protection of confidential information, either party to an access agreement should have a right to inspect and audit to ensure compliance by the other party with the agreement.

Principle 12 establishes the broad framework within which QR would conduct inspections and audits. The QCA believes that the proposed framework is reasonable. However, the QCA has concerns about QR’s auditing rights with respect to safety and environmental issues established in the Draft Undertaking.<sup>200</sup>

The auditing rights of access holders are not addressed under principle 12. However, access holders’ auditing rights with respect to the standard of QR’s infrastructure are recognised under principle 6. The QCA supports this right. Beyond information on QR’s infrastructure standards, a third-party would be interested in receiving information regarding services that QR has contracted to supply to it as part of an access agreement, such as train control, in order to assess QR’s compliance with the agreement.

In this regard, the QCA has proposed ongoing public reporting by QR on its compliance with the Undertaking.<sup>201</sup> The QCA believes that this type of public reporting is potentially less burdensome

<sup>199</sup> This issue was discussed in Chapter 7.

<sup>200</sup> These concerns were discussed in Chapter 7.

<sup>201</sup> Public reporting is discussed in Chapters 2 and 5.

on QR than the creation of a broad-based audit right available to all rail operators using its network. Public reporting will promote QR's accountability and should provide confidence to access seekers and third-party operators that the Undertaking is operating effectively, or if this is not the case, provide a basis for action against QR for breach of contract. The QCA's proposals envisage public reporting by QR on its financial performance, general undertaking compliance and service performance.

#### **8.4.14 Indemnities and liabilities**

The QCA believes that a third-party should assume responsibility for damage to property or injury to persons being transported by its train services and QR should be indemnified against such outcomes by the third-party accordingly. However, in the QCA's view, standard commercial practice is that the indemnity should not cover a situation where an act or omission by QR caused or contributed to the damage or harm.

Consequently, the QCA has proposed the following italicised change to principle 14, second dot point:

- “The third-party is solely liable for and is required to release and indemnify QR for any damage to property or personal injury or death of any person being transported on train services, *except to the extent that an act or omission by QR, its servants or agents, caused or contributed to the damage or harm.*”

#### **8.4.15 Limitation of liability**

The QCA considers that the liabilities of the parties for default should be limited as ‘agreed’ rather than as ‘specified’ in the access agreement. Consequently, the QCA has proposed the following deletion and italicised change to principle 15, first dot point:

“The liabilities of the parties for default shall be limited as ~~specified~~ *agreed* in the agreement.”

#### **8.4.16 Material change**

In terms of the development of Schedule E, material changes could be defined in very specific terms to provide certainty to all parties, or alternatively, defined in very broad terms to allow the specific nature of material changes to be determined by the parties during an access negotiation.

It is clear that once a material change has been defined in broad terms, in practice, its effect on QR could be adverse or positive. However, QR's revised Schedule E principle proposes that, amongst other things, a reduction in government infrastructure payments should be considered as an increase in the net cost to QR of performing its obligations under an access agreement and should automatically lead to an increase in a third-party's access charges.

The QCA believes that it would only be possible to assess the actual effect of material changes on a case-by-case basis. The key point is that the material changes are triggers only and hence there should be no assumption of automatic flow-on effects. For example, there would be little justification for passing on reductions in government infrastructure payments to a third-party who is already paying charges on the basis of stand-alone costs. Nevertheless, the QCA recognises that if QR cannot automatically flow through the effect of a reduction in government infrastructure payments to access charges, then there may be circumstances in which QR would wish to limit the term of access agreements for the affected rail lines to the term of the relevant government service agreement.

The QCA has proposed the following deletion and italicised change to principle 16, second dot point:

- “A material change shall be limited to changes in taxes, laws or ~~reduction in available~~ funding from QR’s government infrastructure payments. *The effect of material changes should be assessed on a case-by-case basis and in consultation with the third-party. There should be no assumption of automatic flow-on effects of material changes.*”

This would leave the parties to assign the risk for these changes during contractual negotiations.

Under the broad definition, the triggering of a material change could be a source of disputation. The QCA accepts QR’s principle that disputes regarding the impact on access charges of material changes will be determined by an independent expert.

#### **8.4.17 Default, suspension and termination**

The QCA believes this revised Schedule E principle could be expressed to provide greater protection to third parties’ interests. Consequently, the QCA has proposed the following italicised change to principle 18:

- “The agreement will specify *reasonable* events of default and *mutual* rights of suspension and termination *having regard to the commercial interests of both parties.*”

#### **8.4.18 QR’s Access Undertaking - confidentiality and ring fencing**

The QCA believes that it is reasonable for QR to be bound contractually to comply with the confidentiality arrangements established in its Draft Undertaking. This is likely to be particularly important for a third-party operator if there is to be any period in the future when an undertaking is not in force, such as between the expiry of an approved undertaking and its replacement by another approved undertaking.

Given QR’s vertically integrated structure, the QCA argued in Chapter 3 that protection of a third-party operator’s confidential information, both during an access negotiation and once an access agreement has been signed, is a key element of the ring-fencing arrangements established in the Draft Undertaking. Consequently, the QCA believes that such protection is of sufficient importance to be recognised in the Schedule E principles.

The QCA has not proposed that QR’s ring-fencing provisions in their entirety should be entrenched in access agreements. However, the establishment of provisions to protect a third-party operator’s confidential information could be seen as being consistent with standard commercial practice.

In light of the above arguments, the QCA has proposed that the following additional text be added to principle 21:

- “The agreement will contain provisions which require information provided to Network Access by third-party operators to only be used for the purposes of the agreement and to be kept confidential in that it not be provided to any other person (including other employees or agents of QR) without the consent of the third-party operator. Consent need not be sought where the transfer of a third-party’s confidential information is for the purpose of processing an access application and QCA-approved procedures concerning the protection of such information are in place.”
- The obligation to keep such information confidential will continue to bind the parties for a reasonable period of time following the expiry of the agreement.”

**QCA's position**

The QCA would favourably consider an Undertaking that incorporated the following principles regarding the development of a standard access agreement in lieu of the Draft Undertaking's Schedule E:

**1. Access Rights**

- The agreement will provide for non-exclusive train service entitlements for the operation of train services in terms of agreed service levels over the nominated network. Train service entitlements can be varied only in accordance with agreed scheduling procedures specified in the agreement or as otherwise agreed between the parties.
- It is the responsibility of the third-party entering into an access agreement with QR to ensure that the operator of train services utilising the access rights is accredited.
- Access agreements will be for a specified term and include a good faith negotiation process for renewal.

**2. Access Charges**

- Access charges are to be agreed between the parties and payable in accordance with reasonable payment terms set out in the agreement. Late payments or credits by either party will bear interest at an agreed default rate.
- The Agreement will provide for a fair and reasonable mechanism for dealing with bona fide disputed invoices.
- The agreement may provide for periodic review of access charges.
- Unless otherwise stated, all amounts payable under the agreement are exclusive of GST.
- In appropriate cases, QR may require lodgement of a security to secure performance by the third-party of its obligations under the agreement having regard to QR's reasonable assessment of the creditworthiness of the third-party. An established rail entity's ability to demonstrate a track record of timely payment of similar obligations in other rail jurisdictions should be a relevant factor in assessing creditworthiness. Any required security should reflect the revenue risk that QR has taken on.
- Where there are no security arrangements in place and a user defaults on its payments, QR is entitled to require some form of security equivalent to its financial exposure, where the default was not attributable to a legitimate

dispute.

- A third-party paying a security deposit should be credited with interest on the security at a market-based rate for as long as it is held by QR.

### 3. Train Service Entitlements

- The third-party shall not be entitled to commence train services unless and until all provisions of the agreement required to be completed or complied with prior to the commencement of train services have been completed or complied with by the due date specified in the agreement. QR will use all reasonable endeavours to cooperate with the third-party to facilitate the third-party's completion or compliance with such requirements.
- The third-party must only operate trains of the nominated specification for the transport of the nominated product type over the nominated network.
- Train service entitlements can be reduced by QR upon reasonable notice to prevent the hoarding of capacity and appropriate adjustments will be made to the access charges payable.

### 4. Day-to-Day Train Movements

- QR is to have responsibility for train control and shall exercise train control having regard to the safe conduct of rail operations on the nominated network.
- QR shall ensure that the operation of train services is in accordance with the relevant daily train plan, which may be varied in the circumstances specified in the agreement (which normally include safety considerations, force majeure, incidents or emergencies, track possessions in accordance with the agreement or as otherwise agreed between the parties, such agreement not to be unreasonably withheld).
- The third-party is required to comply with all QR train control directions and ensure all trains and rollingstock are equipped with appropriate communication systems to comply with the agreed rollingstock interface standards.

### 5. Train Operations

- The agreement will specify all reasonable operational, communication and procedural requirements for train services.
- The third-party is to comply with all laws, safeworking procedures and safety standards and all other train operations requirements in the agreement. QR will comply with its safeworking procedures and safety

standards and may, acting reasonably, vary the safeworking procedures and safety standards at any time following consultation with, and reasonable notice to, the third-party. Subject to such variations being on safety grounds, each party is responsible for its costs - including the costs of additional or modified equipment - in complying with the safeworking procedures and safety standards. Safeworking procedures and safety standards will as far as practicable be consistent for all railway operators on the nominated network.

- The parties should agree specific performance levels and measurement criteria as a basis for creating effective performance management and incentives. This may involve financially-based incentives and sanctions. The performance levels may also be reviewed periodically.
- The agreement will specify relevant rollingstock interface standards. The third-party must obtain certification from an appropriately qualified person - both certification and person to be subject to the reasonable satisfaction of QR - that its rollingstock and rollingstock configurations comply with such rollingstock interface standards. Rollingstock and rollingstock configurations that are so certified will be included in the rollingstock specification as being authorised to operate on the nominated network subject to continuing compliance with the rollingstock interface standards and rollingstock specification.
- The third-party is responsible for the safe operation of its rollingstock on the nominated network and must ensure that at all times its rollingstock and rollingstock configurations comply with all applicable laws, the rollingstock specification and the rollingstock interface standards specified in the agreement. QR may suspend the operation of rollingstock and trains for demonstrated non-compliance that has safety implications until such non-compliance is rectified. If the source of non-compliance does not have safety implications, the third-party should be required to rectify the non-compliance within a reasonable period of time, but not be suspended. If the non-compliance is not rectified within a reasonable period, QR may suspend the operation of the affected rollingstock and trains.
- The third-party must ensure all loadings of rollingstock are secure.
- QR may, acting reasonably, vary the agreed rollingstock interface standards at any time on safety grounds, after consultation with the third-party. Otherwise, QR may, acting reasonably, negotiate any other changes with the third-party. Where any changes in the standards necessitate modification of the third-party's rollingstock,

the costs of such modifications are to be borne in the manner agreed by the parties or, failing agreement, as determined by an expert.

- QR will not exercise its suspension power in relation to a third-party's rollingstock and trains in such a manner as to hinder or restrict access to the declared service in any way contrary to s104 and s125 of the QCA Act.
- If the suspension of a third-party operator's rollingstock becomes a source of disputation, in the absence of an alternative dispute resolution process agreed between the parties, the Undertaking's dispute-resolution procedures could be triggered.
- A third-party operator could reserve the right that if its rollingstock is suspended without reasonable justification, then QR would be liable for the loss thereby caused.

#### 6. Infrastructure Management

- QR is responsible for the management and control of the nominated network.
- QR will carry out maintenance work on the nominated network such that, subject to any agreed criteria, the infrastructure is consistent with the agreed rollingstock interface standards and the third-party can operate train services in accordance with its train service entitlements.
- QR may impose operational constraints - such as speed or load restrictions - for the protection of persons or property or to facilitate maintenance work or enhancements and has reasonable entitlements to take possession of the track for the purpose of maintenance work, emergency repairs and enhancements. In carrying out such work, QR will use its reasonable endeavours to minimise disruption to train services so that the third-party can operate train services in accordance with its train service entitlements.
- The agreement will contain principles for consultation with the third-party regarding maintenance that will impact on the third-party's schedule.
- The agreement will contain provisions requiring the parties to provide advice to each other in relation to factors that could affect the third-party's operation of train services or the integrity of the nominated network.
- The third-party may inspect the nominated network for the purposes of assessing the operational, environmental and safety risks with respect to the infrastructure, as well as the standard of the infrastructure comprising the nominated network including, but not limited to, fencing

and at-grade crossing protection. QR will not be liable for claims in relation to, or arising out of, the standard of the infrastructure except where QR fails to maintain the infrastructure such that, subject to any agreed criteria, it is consistent with the agreed rollingstock interface standards and the third-party can operate train services in accordance with its train service entitlements.

- The agreement will specify the reasonable terms and conditions on which the third-party will have access to the nominated network for the purpose of inspecting the standard of the infrastructure comprising the nominated network.

#### **7. Incident Management**

- Prior to the commencement of train services the third-party is required to develop an emergency response plan containing procedures for dealing with incidents which must not be inconsistent with QR's emergency procedures.
- In the event of an incident, QR is responsible for the overall coordination and management of incident responses and may, subject to using reasonable efforts to consult with the third-party, take any action it considers reasonably necessary to recommence services as soon as possible. The third-party is to cooperate and assist with the restoration of train movements in accordance with directions from train controllers seeking to coordinate the clearance of network blockages. Any third-party so directed should be adequately compensated for doing so and is entitled to expect that all rail operators are subject to the same obligation.
- Once a third-party's train has been moved off the mainline and is no longer causing a blockage, it is responsible for implementing its recovery plan for the broken-down rollingstock, including effecting the recovery within a reasonable period.
- Investigations into incidents are to be commenced as soon as practicable after an incident and carried out in accordance with the process specified in the agreement. The parties must cooperate in any investigation and consult in good faith in relation to the implementation of any recommendations.

#### **8. Environmental Protection and Other Issues**

- All environmental laws, regulations and relevant guidelines must be complied with.
- Environmental management must be approached on a risk identification and management basis with respect to operations on the nominated network. Auditing

requirements should be linked to the environmental risks posed by a third-party's train services and be established in that third-party's environmental management system.

- The third party is required to inform QR of non-compliance with its environmental management system and provide details of how it intends to address the non-compliance. The operator is required to rectify the breach as soon as practicable, having regard to the nature of the breach and any action required by EPA.

#### **9. Accreditation**

- QR must have and maintain accreditation as a railway manager under the *Transport Infrastructure Act 1994* to the extent required to perform its obligations under the Agreement.
- An operator accredited as a railway operator under the *Transport Infrastructure Act 1994* must operate train services and the operator must maintain such accreditation to the extent required to perform its obligations under the Agreement.

#### **10. Third-party's Staff**

- The third-party is responsible for demonstrating to the Rail Safety Accreditation Unit through the joint safety risk assessment process, the competence of its staff performing safety-related work. QR may suspend the right of the third-party's staff to operate on the nominated network in the event of breach, or likely breach, of any laws, QR train control directions, safeworking procedures or safety standards, until such non-compliance is rectified.
- QR will not exercise its suspension power in relation to a third-party's staff in such a manner as to hinder or restrict access to the declared service in any way contrary to s104 and s125 of the QCA Act.
- If the suspension of a third-party operator's staff becomes a source of disputation, in the absence of an alternative dispute resolution process agreed between the parties, the Undertaking's dispute resolution procedures could be triggered.
- A third-party operator could reserve the right that if its staff are suspended without reasonable justification, then QR would be liable for the loss thereby caused.

#### **11. Safety Risk Management**

- Safety risk management must be addressed by risk identification through a joint safety risk assessment process and the formulation of a safety risk management

plan. The parties will be required to comply with the safety risk management plan.

**12. Inspection and Audit Rights**

- **Rights of inspection and audit in relation to the third-party's compliance with the agreement and inspection of trains and rollingstock shall be included in the agreement. The agreement will specify the terms and conditions on which QR can carry out such inspections and audits. Except in emergencies, QR will, in carrying out any inspection or audit, give the third-party reasonable notice and use reasonable endeavours to minimise disruption to the third-party's train services.**

**13. Insurance**

- **The agreement will provide for insurances to be effected by the parties to appropriately provide for the relevant insurance risks.**

**14. Indemnities and Liabilities**

- **Each party is liable for, and is required to release and indemnify each other for, all claims in respect of personal injury, death or property damage caused or contributed to - to the extent of the contribution - by the wilful default or negligent act or omission of that party or its staff.**
- **The third-party is solely liable for, and is required to release and indemnify QR for, any damage to property or personal injury or death of any person being transported on train services, except to the extent that an act or omission by QR, its servants or agents, caused or contributed to the damage or harm.**

**15. Limitation of Liability**

- **The liabilities of the parties for default shall be limited as agreed in the agreement.**
- **Neither party has any liability for consequential loss or damage or loss of profits in any circumstances.**
- **Claims by either party must be lodged within twelve months of the occurrence of the event or circumstance giving rise to the claim.**

**16. Material Change**

- **Access charges will be adjusted to reflect the net impact of any material change where such material change results in a variation to the net cost to QR of performing its obligations under the agreement.**
- **A material change shall be limited to changes in taxes,**

laws or funding from QR's government infrastructure payments. The effect of material changes should be assessed on a case-by-case basis and in consultation with the third-party. There should be no assumption of automatic flow-on effects of material changes.

- Any dispute regarding the impact on access charges as a result of a material change will be determined by an independent expert.

**17. Disputes**

- Any dispute between the parties is to be firstly referred in writing to the respective chief executives for resolution. If the dispute is not resolved, then the parties may agree to refer the dispute for resolution by an expert or arbitration. If there is no agreement to resolve the dispute in this manner then the dispute is to be determined by a court.

**18. Default, Suspension and Termination**

- The agreement will specify reasonable events of default and mutual rights of suspension and termination having regard to the commercial interests of both parties.

**19. Force Majeure Event**

- The obligations of either party - other than an obligation to pay monies due - will be suspended where by reason of a force majeure event, that party is delayed in, or prevented from, carrying out its obligations under the agreement. The agreement will provide for relief in respect of the payment of access charges to the extent that QR is unable to provide access rights because of a force majeure event affecting QR.
- In the event that infrastructure on specified lightly trafficked corridors of the nominated network is damaged by a force majeure event and in QR's reasonable opinion the cost of repairing the damage is not economic, QR may elect not to proceed with repairs or replacement unless the parties agree as to the funding of the cost of that work.
- The access agreement will provide for a process that might result in termination of the agreement in the event that circumstances of prolonged force majeure prevent the performance by a party of its obligations.

**20. Assignment**

- The third-party may assign the whole of its rights and obligations under the Agreement to a related body corporate, provided that the assignor remains liable for the performance of obligations under the agreement or to

a non-related body corporate, with the prior written consent of QR, such consent not to be unreasonably withheld.

- A change in control of a third-party not a publicly listed corporation will be deemed to be an assignment of the agreement.

**21. QR's Undertaking**

- QR will comply with all applicable laws and the terms of QR's Access Undertaking in effect from time-to-time.
- The agreement will contain provisions which require information provided to Network Access by third-party operators to only be used for the purposes of the Agreement and to be kept confidential, in that it not be provided to any other person - including other employees or agents of QR - without the consent of the third-party operator. Consent need not be sought where the transfer of a third-party's confidential information is for the purpose of processing an access application and QCA-approved procedures governing the flow of that information are in place.
- The obligation to keep such information confidential will continue to bind the parties for a reasonable period of time following the expiry of the agreement.