Queensland Competition Authority

Draft Decision

Queensland Rail's 2013 Draft Access Undertaking

October 2014

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SUBMISSIONS

Closing date for submissions: 23 December 2014

Public involvement is an important element of the decision-making processes of the Queensland Competition Authority (QCA). Therefore submissions are invited from interested parties concerning its assessment of Queensland Rail's June 2013 draft access undertaking (DAU). The QCA will take account of all submissions received.

Submissions, comments or inquiries regarding this paper should be directed to:

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Confidentiality

In the interests of transparency and to promote informed discussion, the QCA would prefer submissions to be made publicly available wherever this is reasonable. However, if a person making a submission does not want that submission to be public, that person should claim confidentiality in respect of the document (or any part of the document). Claims for confidentiality should be clearly noted on the front page of the submission and the relevant sections of the submission should be marked as confidential, so that the remainder of the document can be made publicly available. It would also be appreciated if two copies of each version of these submissions (i.e. the complete version and another excising confidential information) could be provided. Where it is unclear why a submission has been marked 'confidential', the status of the submission will be discussed with the person making the submission.

While the QCA will endeavour to identify and protect material claimed as confidential as well as exempt information and information disclosure of which would be contrary to the public interest (within the meaning of the *Right to Information Act 2009* (RTI)), it cannot guarantee that submissions will not be made publicly available. As stated in s 187 of the Queensland Competition Authority Act 1997, the Authority must take all reasonable steps to ensure the information is not disclosed without the person's consent, provided the Authority believes that disclosure of the information would be likely to damage the person's commercial activities and that the disclosure of the information would not be in the public interest. Notwithstanding this, there is a possibility that the Authority may be required to reveal confidential information as a result of a RTI request.

Public access to submissions

Subject to any confidentiality constraints, submissions will be available for public inspection at the Brisbane office, or on the website at www.qca.org.au. If you experience any difficulty gaining access to documents please contact us on (07) 3222 0555.

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EXECUTIVE SUMMARY

Queensland Rail's business changed in 2010 when it was separated from Aurizon Holdings. Queensland Rail is seeking to replace an access undertaking it inherited with one that better reflects its business activities and competitive environment, including that it has a significant focus on passenger activities, it is not vertically integrated with freight activities and its non-bulk activities are subject to competition from roads.

There is, therefore, significant merit in a streamlined and simplified access undertaking. Accordingly, we are proposing to accept key elements of the 2013 draft access undertaking (DAU). However, as we are seeking to modify details of the 2013 DAU, we are not proposing to accept the 2013 DAU as submitted.

2013 DAU follows stakeholder consultations

Over the last three years, Queensland Rail has submitted three versions of a DAU. Queensland Rail withdrew the previous two DAUs to address stakeholders' concerns on a range of matters including the negotiation process, the investment framework, the process for amending documents not included in the undertaking and the dispute resolution mechanism. The 2013 DAU also included a proposed reference tariff for coal train services on the western system.

Despite this process of on-going consultation and amendment, stakeholders still object to detailed aspects of the 2013 DAU.

But Queensland Rail has shifted the balance of risks and responsibilities in its favour

The 2013 DAU proposes in some cases to shift risks and responsibilities onto access holders/seekers. The QCA believes that risks and responsibilities should be allocated to the party best placed to manage them. In this draft decision, the QCA proposes changes to ensure a more efficient and equitable approach than the 2013 DAU. The QCA believes that these changes will make the DAU more consistent with the objectives of a negotiate-arbitrate access regime. In the case of contracting, for example, the QCA proposes that Queensland Rail align its practices with those of Aurizon Network unless it can be demonstrated that differences in Queensland Rail's business and risk profile require a different approach.

In the same vein, Queensland Rail's proposed investment framework gives it excessive discretion when considering network extensions. The QCA has provided scope for a standard user funding arrangement to be developed in the future.

Pricing for commercial traffics

A key issue for Queensland Rail and stakeholders is the tariffs for commercial freight services on the western system and Mount Isa line.

Western system

Our Act requires, amongst other things, that the QCA ensures Queensland Rail's legitimate business interests are recognised, including its right to earn a reasonable return on its investments. Queensland Rail is seeking a substantial increase in its tariffs to cover its costs. For example, Queensland Rail is proposing an 82% increase in its maintenance costs.

For their part, stakeholders are concerned that the western system network is not fit for the purpose of carrying heavy-haul coal services and claim that the proposed tariffs are excessive. These differences are most pronounced in disagreements over the asset valuation of the western system. A key sticking point is the costs associated with the assets that were already in place before coal services began in the mid-

1990s – the return on and of these assets represents around one-third of Queensland Rail's proposed tariff in the 2013 DAU.

Unfortunately, the previous regulatory round (in 2009) was cut short, with no agreement on aspects of the methodology for valuing the western system's regulated asset base. Earlier this year, the QCA proposed two tariff options in its consultation paper: a revised depreciated optimised replacement cost (DORC); and a historical cost roll-forward of investments since coal trains began operating on the western system. Both options relied on the same asset register adopted by QR Network (a predecessor company of Queensland Rail) in 2009.

The submissions on the consultation paper showed that the positions of Queensland Rail and other stakeholders on the western system tariff are far apart. Queensland Rail said that regulatory precedent was to use a DORC valuation but did not accept the QCA's DORC option. Other stakeholders restated their view that the maintenance costs proposed by Queensland Rail show that the network is not the 'modern engineering equivalent' assumed in Queensland Rail's DORC analysis and therefore it should have a lower valuation.

The QCA accepts that the western system is an old network that was not built to the standard required to support frequent heavy-haul coal services. The QCA recognises that using this network to provide coal services is unavoidably costly for Queensland Rail. Given this, the QCA proposes to accept nearly all of Queensland Rail's forecasts for maintenance and operating costs. This draft decision indicates in-principle agreement for a 67% increase in maintenance spending and a 34% increase in operating costs.

However, as a basic principle, access holders should only pay for assets once. Assets which are fully life expired should not generate returns as part of the regulated asset base. The QCA has in the past sought to avoid similar double counting of assets, including in its 2009 draft decision on the western system tariff and in its earlier decisions on gas distribution network pricing.

The QCA therefore proposes to assign a zero value to assets which are still in use beyond their expected useful life. Overall, the QCA is proposing changes which would provide Queensland Rail with a tariff of $14.29/'000 gtk for the western system for 2013–14 (about $7.16/net tonne).

Mount Isa line

There is also acknowledgement by parties that access charges for the Mount Isa line are most likely well below the ceiling price.

For some time, stakeholders have expressed concerns that Queensland Rail has substantial monopoly power at contract renewal as investments in mines and other businesses using the line are sunk. However, the 2013 DAU does not provide any mechanism to address these concerns, creating uncertainty.

The QCA accepts that sunk assets should not be stranded at contract renewal. But, at the same time, it is reasonable for Queensland Rail to cover at least the incremental costs of operating the line.

The QCA has therefore proposed a pricing rule at contract renewal for the Mount Isa line which provides for Queensland Rail to increase prices at a real rate of two per cent per annum while fully recovering the costs of any infrastructure specifically built for the access holder's service.

Parties are invited to provide an alternative mechanism that balances the rights of Queensland Rail and its customers if they have concerns with this approach.

Submissions invited

In reviewing Queensland Rail's 2013 DAU and stakeholder submissions and preparing this draft decision, the QCA had regard to its obligations under s. 138(2) of the *Queensland Competition Authority Act 1997* (the QCA Act).

However, it is important to be clear that this document is not a draft version of a final decision, and it has no force of itself. There should be no expectation that it presents views and recommendations as to how to amend the 2013 DAU which will prevail to the end of the decision making process unless the QCA is persuaded otherwise. This document represents the QCA's preliminary view and is intended to give stakeholders an insight into that view to encourage further contributions. The QCA's application of s. 138(2) and its thinking may change towards its final decision, which will be informed by submissions made in response to this document.

The QCA encourages stakeholders to comment on this draft decision. Submissions are invited by 5 pm, Tuesday 23 December 2014.

INTRODUCTION

Background

Queensland Rail is a statutory authority that owns and operates an 8,000 kilometre rail network, including the commuter lines in south east Queensland, as well as the western system, and the Mount Isa and north coast lines (see **Figure 1**). It also operates the state's suburban and long-distance passenger services.[1]

Declaration for third party access

The services provided by Queensland Rail's intra-state rail network were declared by regulation in 1997, making the services subject to the third party access provisions of the Queensland *Competition Authority Act 1997* (the QCA Act). As a result of that declaration, Queensland Rail, access seekers and access holders gained rights and obligations relating to the negotiation of the terms and conditions of access to Queensland Rail's rail transport infrastructure.

The below-rail (track) network is subject to the 2008 access undertaking (2008 undertaking) the QCA approved for the then QR Network, as amended in June 2010 to include new tariffs and tariff-setting rules.

The access regime established by Part 5 of the QCA Act is a negotiate/arbitrate model. That is, the primary responsibility is on the access provider and access seeker to negotiate on price and non-price terms, with the QCA becoming involved only under certain circumstances – for example, where agreement cannot be reached and either party has lodged a dispute notice with the QCA.

History of this draft decision

Following its creation, Queensland Rail commenced a process to transition from being subject to the 2008 undertaking to one that better reflected its assets and business structure. The history of this process is as follows:

(a) March 2012 – Queensland Rail submitted the 2012 DAU which sought to replace its 2008 undertaking with a set of requirements more suited to a network operator which is not vertically integrated with an above-rail freight business

(b) April 2012 – QCA released an Issues Paper on the 2012 DAU

(c) February 2013 – Queensland Rail withdrew its 2012 DAU and submitted the February 2013 DAU (the 2013 DAU). In doing so, Queensland Rail indicated that it had revised the 2012 DAU to reflect concerns raised by its stakeholders

(d) April and May 2013 – the QCA hosted a series of workshops on issues in the February 2013 DAU, including above-rail operational issues, western system pricing, standard access agreements (SAAs), Mount Isa pricing and investment framework matters

[1] Queensland Rail was created in 2010 when the Queensland Government split the former QR Ltd prior to privatising QR National Limited (now Aurizon Holdings Limited – which provides both above and below rail services). Queensland Rail owns most of the former QR Ltd rail network in Queensland, apart from the tracks in central Queensland owned by Aurizon Network Pty Ltd (formerly QR Network Pty Ltd). Another Aurizon Holdings subsidiary, Aurizon, operates the above-rail assets formerly owned by QR National Limited.

Figure 1 Queensland Rail's network

Source: Queensland Rail

(e) June 2013 – Queensland Rail resubmitted its 2013 DAU and included, for the first time, its proposed voluntary reference tariffs for the western system

(f) June 2014 – the QCA released its consultation paper on western system coal tariffs in the 2013 DAU along with a report on the western system prepared by its rail consultant, B&H Strategic Services (B&H)

(g) June 2014 – the QCA conducted a workshop with stakeholders on western system coal tariffs

(h) October 2014 – the QCA released this draft decision.

Submissions on Queensland Rail's DAU

The QCA received nine submissions in response to the February 2013 DAU – four on general matters, and a further five on matters discussed at the workshops hosted by the QCA in April and May 2013. The QCA has treated submissions on the February 2013 DAU as submissions on the June 2013 DAU, as the February and June 2103 DAUs were identical, apart from the inclusion of the western system tariff.

Submissions supported many aspects of Queensland Rail's 2013 DAU and noted that Queensland Rail had sought to address some stakeholder concerns as part of transitioning away from the provisions of the undertaking. Stakeholders said that some key matters, however, had not been addressed and those matters that had been revisited had not addressed all of their concerns.

As a result, stakeholders continued to raise material concerns that Queensland Rail's 2013 DAU was imbalanced and provided Queensland Rail with excessive discretion, in particular in relation to the proposals for:

(a) application and scope – including that the 2013 DAU does not apply to all of Queensland Rail's declared assets

(b) the negotiation process – including that Queensland Rail has provided itself with too much discretion over the nature of information exchanged, the time frames and the circumstances when it could cease negotiations

(c) pricing principles – namely that Queensland Rail's principles for how it will set and negotiate prices for access gave it too much discretion in setting access charges. Stakeholders were also concerned on a lack of clarity on Queensland Rail's pricing for its Mount Isa Line, particularly where the customers' assets were sunk and they had few alternative transport options

(d) principles and requirements for operating the network – including that Queensland Rail had provided itself with excessive discretions in how the network was to be managed and that there was a lack of information on how changes to the relevant requirements should occur

(e) reporting – including on the type and quality of information Queensland Rail was to report on a regular basis to demonstrate compliance with its obligations

(f) standard access agreements (SAA) – namely that as part of streamlining the SAA provisions, Queensland Rail has tilted the balance of obligations and responsibilities away from it and towards access holders

(g) investment framework – including that Queensland Rail had removed any obligation to extend the network.

In addition to these broad ranging concerns, stakeholders had very particular and detailed concerns on Queensland Rail's proposed western system tariff.

The QCA received five submissions on Queensland Rail's June 2013 DAU all of which focused on the proposed western system tariff. The QCA received a further five submissions after the release of the QCA's consultation paper on this matter.

Queensland Rail had proposed a tariff of $22.22/'000 gross tonne kilometres (gtk) which was 20% higher than the 2013–14 tariff ($18.56/'000 gtk) applying at the time. Queensland Rail considered that this tariff reflected an appropriate return on the assets needed to deliver capacity for coal trains as well as higher maintenance costs and investment to maintain the operating capability of the line.

In contrast, stakeholders considered this tariff was excessive, in particular in comparison to other coal networks where tariffs were lower and performance standards were superior. They argued that the QCA should revisit the asset valuation, in particular given the step increase (82%) in maintenance costs.

The QCA sought to address stakeholders' concerns by providing two tariff options in its consultation paper ($13.59/'000 gtk and $17.21/'000 gtk) that illustrated different approaches to valuing the western system assets.

Stakeholders' positions on the consultation paper reflected polarised views. On the one hand, Queensland Rail argued that its original proposal was reasonable and that both of the QCA's tariff options were too low. In contrast, all other stakeholders (i.e. the train operator and coal companies) argued that the QCA needed to revisit its asset valuation as the $13.59/'000 gtk option in the QCA's consultation paper was still too high given the service characteristics of the western system.

The QCA's considerations

The QCA has considered Queensland Rail's 2013 DAU and stakeholder submissions in accordance with the assessment criteria in s. 138(2) of the QCA Act. This states that the QCA may approve a DAU only if it considers it appropriate having regard to:

(a) the object of Part 5 of the QCA Act, which is:

> *... to promote the economically efficient operation of, use of and investment in, significant infrastructure by which services are provided, with the effect of promoting effective competition in upstream and downstream markets (s. 69E).*

(b) the legitimate business interests of the owner or operator of the service

(c) if the owner and operator of the service are different entities – the legitimate business interests of the operator of the service are protected

(d) the public interest, including the public interest in having competition in markets (whether or not in Australia)

(e) the interests of persons who may seek access to the service, including whether adequate provision has been made for compensation if the rights of users of the service are adversely affected

(f) the effect of excluding existing assets for pricing purposes

(g) the pricing principles in s. 168A of the QCA Act, which in relation to the price of access to a service are that the price should:

  (i) generate expected revenue for the service that is at least enough to meet the efficient costs of providing access to the service and include a return on investment commensurate with the regulatory and commercial risks involved

  (ii) allow for multi-part pricing and price discrimination where it aids efficiency

(iii) not allow a related access provider to set terms and conditions that discriminate in favour of the downstream operations of the access provider or a related body corporate of the access provider, except to the extent the cost of providing access to other operators is higher

(iv) provide incentives to reduce costs or otherwise improve productivity

(h) any other issues the Authority considers relevant (the interests of access holders and their customers).

It is not open to the QCA to approve an access undertaking that does not include the matters required by s. 137. These are:

(a) an expiry date

(b) provisions for identifying, preventing and remedying conduct by an access provider that provides, or proposes to provide, access to itself or a related body corporate that unfairly differentiates in a material way between access seekers (in negotiations) and access holders (in providing the service)

(c) provisions preventing an access provider that provides, or proposes to provide, access to itself or a related body corporate recovering, through the price of access, costs that are not reasonably attributable to the provision of the service.

Sections 137(2) and 138A set out matters which may be included in an access undertaking.

Nature of this document

Queensland Rail has submitted the 2013 DAU under s. 136(1) of the QCA Act. Under s. 136(4), the QCA must consider the DAU and either approve, or refuse to approve, it. If it refuses to approve the DAU, under s. 136(5), the QCA must give reasons and state the way in which it considers it is appropriate to amend it.

The QCA Act does not provide for the making of a draft decision. However it is common practice for regulators generally, and for the QCA, to publish a 'draft decision' to provide stakeholders with an indication of its views at a reasonably advanced point in time to allow stakeholders an opportunity to make submissions on them. In keeping with that practice, the QCA has styled this document as a draft decision.

However, it is important to be clear that this document is not a draft version of a final decision, and it has no force of itself. There should be no expectation that it presents views and recommendations as to how to amend the 2013 DAU which will prevail to the end of the decision making process unless the QCA is persuaded otherwise. Rather, this document represents the QCA's preliminary view and is intended to give stakeholders an insight into that view to encourage further contributions. The QCA's application of s. 138(2) and its thinking may develop further or differently towards its final decision, which will be informed by submissions made in response to this document.

Structure

This draft decision follows the structure of the 2013 DAU, including:

(a) Chapter 1: Application and scope – considers the extent to which the 2013 DAU applies to the entirety of Queensland Rail's declared service

(b) Chapter 2: Negotiation and capacity management – considers Queensland Rail's process for negotiating with access seekers and its discretion to allocate capacity between competing access seekers

(c) Chapter 3: Pricing principles – considers the principles for setting access charges. The chapter also proposes a pricing rule at contract renewal for the Mount Isa line

(d) Chapter 4: Network management principles (NMP) and the operating requirements manual (ORM) – considers the appropriateness of the rules in the NMP for how Queensland Rail will demonstrate capacity, coordinate maintenance and schedule and operate trains. The chapter also considers the technical matters in the ORM that Queensland Rail proposes be removed from the SAAs and placed on the web

(e) Chapter 5: Reporting – considers Queensland Rail's proposed approach to reporting and audit of costs, performance and compliance with the undertaking

(f) Chapter 6: Administrative provisions – considers Queensland Rail's structural changes to streamline the operation of administrative provisions, including for dispute resolution and tariff reporting

(g) Chapter 7: SAAs – considers Queensland Rail's access agreement principles and the coal SAA

(h) Chapter 8: Western system tariff – considers the best approach to the reference tariffs for the western system

(i) Chapter 9: Investment framework, planning and coordination – considers Queensland Rail's treatment of its obligation to extend the network.

Consultation on the draft decision

The QCA invites submissions from interested parties on this draft decision. In particular the QCA seeks submissions on:

(a) the QCA's preliminary views on the various aspects of the DAU, as set out in this document

(b) the QCA's proposed treatment for the western system (Chapter 8).

The QCA seeks submissions in relation to this draft decision no later than 5 pm on Tuesday, 23 December 2014.

The QCA will weigh the arguments and information put forward by Queensland Rail supporting its 2013 DAU, stakeholders' comments and submissions, as well as the QCA's own analysis.

The QCA will be assisted if submissions are made in the context of the assessment criteria in s. 138(2) of the QCA Act, including the relative importance of matters where the application of the assessment criteria leads to conflicting or inconsistent conclusions.

LEGISLATIVE FRAMEWORK

In assessing the 2013 DAU, the QCA has had regard to all the matters specified in s. 138(2) of the QCA Act. In particular, the QCA has considered:

(a) whether the DAU provides for an appropriate balance between the interests of stakeholders

(b) the economically efficient operation of, use of and investment in Queensland Rail's below-rail network and the effect on competition in upstream and downstream markets including those for above rail freight market and for domestic and export coal markets

(c) the legitimate business interests of Queensland Rail on a range of matters, particularly that it should be able to earn a return on investment commensurate with the regulatory and commercial risks involved in providing the below-rail service

(d) the interests of access seekers and access holders on a range of matters, particularly that they pay a price that reflects efficient costs

(e) the public interest, noting that it can include a wide variety of matters

(f) pricing principles, including providing reasonable certainty for developing access charges.

Section 138(2) – general observations

The matters to which the QCA must have regard are set out in s. 138(2) of the QCA Act. This chapter discusses in a general sense how the QCA proposes to have regard to those matters in making its draft decision.

The discussion in this chapter presents overarching observations that form the foundation of the analysis in later chapters. Those chapters consider issues by reference to this discussion and to a specific discussion of the matters in s. 138(2) as relevant.

In reaching its draft decision the QCA has had regard to all the paragraphs of s. 138(2). However, in the interests of readability the discussion in later chapters often considers the issues not by express reference to each paragraph of s. 138(2), but rather by reference to the substance of the matters contained in those paragraphs.

The QCA notes that the issues that arise in its consideration of the 2013 DAU are often in the nature of a tension between the legitimate business interests of Queensland Rail and the interests of access seekers and access holders. In very broad terms this is a tension between Queensland Rail recovering its efficient costs and earning a normal return on investment and access seekers and access holders paying a reasonable price.

This tension can be seen in the light of the potentially conflicting considerations of s. 138(2). The QCA Act leaves the weight to be given to these matters and the balancing of them at the discretion of the QCA. Overall, the QCA is of the view that the 2013 DAU should provide an appropriate balance between the interests of Queensland Rail and the interests of access seekers and access holders. The correct balance between these interests will contribute to the economically efficient operation of, use of and investment in Queensland Rail's below-rail network and the promotion of effective competition in upstream and downstream markets.

It is possible that these interests can align. For example, efficient expenditure can encompass a range of investment and operating activities. In general terms Queensland Rail has an interest in having the ability and incentive to invest in and operate the network to provide the service in a manner which meets its

legal obligations (on a range of matters) and its customers' requirements, both present and future, whilst earning a normal return. The interests of access seekers, access holders (and the public) are that Queensland Rail is able to invest in and operate the network to meet those same ends at a price that reflects efficient costs. Where these conditions are achieved the interests of Queensland Rail, access seekers, access holders and the public are aligned. Effective competition in markets upstream and downstream of the network will be promoted.

The object of Part 5

Section 138(2)(a) requires the QCA to have regard to the object of Part 5 of the QCA Act. The object of Part 5 is in s. 69E. It is to promote the economically efficient operation of, use of and investment in significant infrastructure by which services are provided, with the effect of promoting effective competition in upstream and downstream markets.

These explicit references in s. 69E to three aspects of efficiency in the operation of, use of and investment in the Queensland Rail rail network correspond, respectively, to the productive, allocative and dynamic dimensions of efficiency as used and understood by economists.

While the QCA has not conducted a market definition analysis, and has therefore not reached a conclusive view on what constitutes a particular upstream or downstream market, the QCA notes that access to the Queensland Rail rail network may have significance for competition in, *inter alia*, the market for freight services, including through the operation of contracting and operating requirements embodied in Queensland Rail's proposal. Moreover, while the QCA accepts the passenger services and freight markets are distinct, the QCA has had regard to concerns that Queensland Rail may favour its above-rail passenger business to the detriment of above-rail freight business.

The legitimate business interests of Queensland Rail

Section 138(2)(b) requires the QCA to have regard to the legitimate business interests of the owner or operator of the service, in this case Queensland Rail.

Queensland Rail will have a legitimate business interest as a below-rail operator in a range of issues that arise for consideration. By way of example it will have a legitimate business interest in earning a return on its investments commensurate with the regulatory and commercial risks involved, an effective negotiation framework, earning revenue it expects from access holders' contracted train service entitlements (TSEs) through reasonable take-or-pay arrangements and a fair and balanced capacity and investment framework.

Queensland Rail has made a number of submissions in support of the 2013 DAU which outline its view of its legitimate business interests and to which the QCA has had regard in making this draft decision. The QCA refers to aspects of these submissions in later chapters.

The public interest

Section 138(2)(d) requires the QCA to have regard to the public interest, including the public interest in having competition in markets (whether or not in Australia). The public interest may include a wide variety of matters and is a concept which imports a discretionary value judgement.

As such, there is a public interest in the promotion of competition in upstream and downstream markets, employment opportunities in Queensland, a fair and balanced capacity and investment framework and the long-term growth of mining and other industries and the future economic prosperity of the communities that rely on and service Queensland Rail’s below-rail network.

The interests of access seekers

Section 138(2)(e) requires the QCA to have regard to the interests of persons who may seek access to the service, including whether adequate provision has been made for compensation if the rights of users of the services are adversely affected.

Submissions made during consultation are particularly relevant in having regard to s. 138(2)(e). The QCA has had regard to these submissions and refers to them in later chapters as they relate to particular issues.

In this instance, access seekers' interests include: an effective negotiation framework; transparent and public information about access to and use of the network; adequate reporting; effective transitional arrangements as one undertaking replaces another; access principles that are effective for a balanced negotiation or renewal of an access agreement; standard access agreements that represent a fair risk allocation; effective obligations to maintain the network; and a workable and effective extension and expansion framework.

The effect of excluding existing assets for pricing purposes

Section 138(2)(f) requires the QCA to have regard to the effect of excluding existing assets for pricing purposes.

This issue has been considered by the QCA in some detail as part of proposing a tariff for the western system (see Chapter 8).

The pricing principles in section 168A

Section 138(2)(g) requires the QCA to have regard to the pricing principles in s. 168A.

The pricing principles in relation to the price of access to a service are that the price should:

> *(a) generate expected revenue for the service that is at least enough to meet the efficient costs of providing access to the service and include a return on investment commensurate with the regulatory and commercial risks involved; and*
>
> *(b) allow for multi-part pricing and price discrimination when it aids efficiency; and*
>
> *(c) not allow a related access provider to set terms and conditions that discriminate in favour of the downstream operations of the access provider or a related body corporate of the access provider, except to the extent the cost of providing access to other operators is higher; and*
>
> *(d) provide incentives to reduce costs or otherwise improve productivity.*

The intent of the pricing principles is to provide a transparent framework for determining price limits, the structure of access charges and associated pricing matters. This framework should afford Queensland Rail, access seekers, access holders and the public reasonable certainty surrounding the processes for developing access charges for Queensland Rail's below-rail network.

Any other matters the QCA thinks are relevant

Section 138(2)(h) requires the QCA to have regard to any other issues it considers relevant.

This paragraph is expressed in broad terms and gives the QCA considerable latitude. However, a consideration of other relevant issues has not arisen in this draft decision other than in relation to the interests of access holders and end-users which the QCA considers relevant under this paragraph. The interests of these stakeholders broadly coincide with the interests of access seekers; however, specific issues for access holders and end-users are discussed in later chapters as relevant.

1 APPLICATION AND SCOPE (PART 1)

Part 1 of Queensland Rail's 2013 DAU contains provisions on the scope of access, provisions for non-discriminatory treatment of its above rail operations, ring-fencing and on the term of the undertaking.

Stakeholders said Queensland Rail had removed many of the controls contained in the 2008 undertaking that were necessary for access to be provided equitably and efficiently. Stakeholders said that greater clarity and controls were needed to ensure that Queensland Rail did not act in a manner that favoured its above-rail passenger services. Stakeholders also said that the term of the undertaking be no more than four years.

The QCA accepts that Queensland Rail's above-rail passenger services do not compete in the same markets as its other access holders and seekers and that Queensland Rail also has passenger priority obligations under the Transport Infrastructure Act 1994. Nevertheless, these passenger priority obligations need to be balanced against the rights of access seekers and holders to gain effective access to the declared service. The QCA has proposed amendments to achieve this.

The QCA accepts Queensland Rail's proposal that the undertaking expire on 30 June 2017. This expiry date is consistent with the period over which the western system reference tariffs have been assessed and provides an early opportunity to further refine the operation of a new regulatory approach for Queensland Rail.

1.1 Introduction

Part 1 of Queensland Rail's 2013 DAU sets out the core principles – scope of the undertaking and non-discriminatory treatment, that the rest of the undertaking has regard for and is constructed around.

This chapter is organised to consider the following matters:

(a) scope of access in the undertaking (Section 1.2)

(b) provisions for non-discriminatory treatment (Section 1.3)

(c) ring-fencing arrangements (Section 1.4)

(d) duration of the 2013 DAU (Section 1.5).

1.2 Scope of access in the undertaking

The QCA Act declares for access 'rail transport infrastructure' for which Queensland Rail, or its successor, assign or subsidiary is the 'railway manager' (s. 250(1)(b)).

The *Transport Infrastructure Act 1994* (the TI Act) defines 'rail transport infrastructure' as 'facilities necessary for operating a railway' such as railway track and other infrastructure associated with a railway's operation (e.g. bridges, stations and platforms). The TI Act definition of rail transport infrastructure does not include maintenance depots, office buildings and rolling stock that operate on a railway (TI Act, Schedule 6: 628–633).

The 2008 undertaking mirrors the TI Act's definition of rail transport infrastructure.

Queensland Rail's 2013 DAU

In the 2013 DAU (like the 2012 DAU), Queensland Rail proposed narrowing the scope of the access undertaking by excluding:

(a) access by freight train services to those parts of the rail network provided for the benefit of passengers or passenger train services (*passenger infrastructure)*

(b) rail transport infrastructure (as defined in the TI Act) for which Queensland Rail was the railway manager but not the owner, leasee or sub-leasee (*ownership test*) (cl. 1.2.1(b)(i)).

Passenger infrastructure

Queensland Rail argued that the QCA Act did not require a voluntary access undertaking to apply to all of a declared service. It said that an access seeker could seek access to the excluded part of the declared service through the QCA Act (Queensland Rail, sub. no. 2: 26-27).

Accordingly, Queensland Rail proposed to exclude from the scope of the 2013 DAU access by non-passenger train services to those parts of the network provided for the benefit of passengers or passenger train services including:

(a) stations and platforms used predominantly for passengers or passenger train services

(b) yards and associated facilities used to stage, maintain or store rolling stock used for passenger train services (Queensland Rail, sub. no. 18: 46).

Queensland Rail added that yards and associated facilities used for rolling-stock maintenance were not part of the declared service and the 2013 DAU excluded them to provide clarity about their treatment (Queensland Rail, sub. no. 2: 27).

Queensland Rail said the 2013 DAU aimed to be 'fit for purpose', applying to those assets most likely to attract access seekers. It said that freight train services had already established operational facilities such as crew change points, marshalling areas and designated areas to attach and detach wagons. Therefore, it was unlikely that freight train services would require access to the excluded passenger infrastructure (Queensland Rail, sub. no. 2: 26-27).

Queensland Rail said if it were to expand the scope of the undertaking to include access to passenger assets, then that would require detailed provisions, and said:

> *This could potentially result in detailed and complex provisions being unnecessarily included in AU1 – as those provisions would need to be able to address all potential access requests and circumstances relating to various types of freight train services and stations, platforms and other passenger rail infrastructure. Provisions of that nature may also potentially result in either a risk of gaps or the need for general catch-all provisions (Queensland Rail, sub. no. 2: 28).*

Queensland Rail also proposed to publish line diagrams on its website showing its rail network and existing private infrastructure connection points to the network. Queensland Rail also proposed to provide a description of amendments to the line diagrams and review and notify the QCA about any amendments to those line diagrams at least every six months (cl. 1.2.3).

Ownership Test

Queensland Rail said it was not in a position to provide access rights to rail transport infrastructure for which it was the railway manager but did not own or lease the infrastructure or land on which it sits. Queensland Rail chose to exclude rail infrastructure which it did not own or lease from the scope of the 2013 DAU. Queensland Rail said that access to privately owned rail infrastructure would be governed by the QCA Act rather than the 2013 DAU (Queensland Rail, sub. no. 19: 10).

Stakeholders' comments

Stakeholders argued that the scope of access in the 2013 DAU (like the 2012 DAU) was narrow, particularly compared with the 2008 undertaking that includes a range of below-rail facilities and services necessary to operate a train service.

Passenger infrastructure

Aurizon was concerned Queensland Rail's definition of rail transport infrastructure created ambiguity around the services it would provide as part of access rights, and the services it would treat as ancillary services, and therefore price separately to access charges. Aurizon also raised an issue with Queensland Rail's proposal to exclude access to stations, platforms, yards and depots used predominantly for passenger services (Aurizon, sub. no. 27: 10).

On line diagrams, Peabody said that any material changes should be communicated with affected customers and end users (Peabody sub. no. 34: 3). To provide certainty to the access holder, Aurizon and Glencore[2] proposed the inclusion of a dispute resolution mechanism to prevent Queensland Rail from making inappropriate changes, such as removing parts of the rail network which are in used in existing freight operations (Aurizon, sub. no. 27: 10; Glencore, sub. no. 34: 8).

Glencore proposed changing the 2013 DAU to include:

- *A restriction on removing rail transport infrastructure from the rail diagrams which is utilised for contracted access rights; and*
- *A right for access seekers/holders to dispute whether rail transport infrastructure should have been removed from the rail diagrams (Glencore sub. no. 34: 8).*

QCA analysis and draft decision

Passenger infrastructure

The QCA accepts that access seekers are entitled to seek access to declared services through the QCA Act, when access is not explicitly provided through an approved undertaking. However, the purpose of an approved undertaking is to provide clarity on the declared services that are subject to access. Given this, where possible, an approved undertaking should clearly outline the services that are subject to access and the processes through which any changes to these services can be made.

The 2008 undertaking applied the definition of rail transport infrastructure, consistent with the TI Act, namely, facilities necessary for operating a railway such as railway track and other infrastructure associated with a railway's operation (e.g. bridges, stations and platforms).

Queensland Rail has advised that freight operators are unlikely to require access to the passenger rail infrastructure services it proposed for exclusion because operators have their own operational facilities for crew changes, marshalling areas and designated areas to attach and detach wagons. However, the QCA cannot rule out circumstances where access to passenger rail infrastructure services may be necessary – for instance, emergency access where a freight train breaks down.

It is important to ensure that appropriate access to the declared service is granted consistent with the QCA Act. In its draft decision on Aurizon Network's 2008 DAU, the QCA said it was:

[2] All submissions by Xstrata are referenced as Glencore. Glencore merged with Xstrata in May 2013, and the group changed its name to Glencore plc in May 2014.

> *... important that access to the declared service is not diminished by a lack of access to land, electricity or ancillary services essential for the use of rail transport (QCA, September 2008 : 13-14).*

To do otherwise would create uncertainty for an access holder and access seeker and represent a potential 'hold-up' opportunity where a third-party operator may be unnecessarily prevented from accessing a declared service.

The QCA therefore requires Queensland Rail to define access consistent with the definition in Part 10 of the 2008 undertaking.

> *"Access" means the non-exclusive utilisation of a specified section of Rail Infrastructure for the purposes of operating Train Services*
>
> *"Rail Infrastructure" means Rail Transport Infrastructure including all stations and platforms*
>
> *"Rail Transport Infrastructure" as defined in the TI Act for which [Queensland Rail] or a related party of [Queensland Rail] is the railway manager*

The QCA understands that access to the stations, platforms, yards and depots in the metropolitan network may already be fully used by Queensland Rail's passenger freight business, particularly in peak periods. However, for the purposes of transparency and accountability, it is important that Queensland Rail's passenger businesses directly contract access rights in a manner similar to the process whereby third-party freight operators negotiate access agreements. Only in this way can the QCA properly consider any access disputes regarding access to Queensland Rail's declared services in the metropolitan network.

Draft decision 1.1

- **The QCA requires Queensland Rail to amend its proposal to align the definition of access with the definition of rail transport infrastructure in the TI Act and with the definition in Part 10 of the 2008 undertaking.**

Line diagrams

The QCA accepts Queensland Rail proposal to publish its line diagrams on its website is appropriate. In the 2013 DAU, the line diagrams are relied on only as a way of providing information. This is because Queensland Rail's network that is declared for access is defined by reference to s. 250(1)(b) of the QCA Act. This is in contrast to the 2008 undertaking where rail infrastructure for access is defined in part by reference to line diagrams.

That said, in a practical sense, line diagrams establish and clarify the boundaries of the network and provide certainty to access holders and a ready reference guide for access seekers during the access negotiation process. The accuracy of line diagrams is important for promoting competition in the above-rail markets.

Therefore, the QCA considers that Queensland Rail should ensure the accuracy of the online line diagrams. The QCA also considers that Queensland Rail should consult its customers before amending the line diagrams and the 2013 DAU should include a dispute resolution process for disputes relating to the accuracy of the online line diagrams. That mechanism will provide certainty to Queensland Rail's customers.

Draft decision 1.2

- **The QCA requires Queensland Rail to amend its proposal to:**
  - **(a) warrant the accuracy of the online line diagrams**
  - **(b) consult all existing access holders and access seekers of any proposed amendments to the line diagrams**
  - **(c) follow the Part 6 dispute resolution processes in the event an access holder or access seeker raises a dispute about the accuracy of the line diagrams**
  - **(d) update the online line diagrams, subject to the outcome of any dispute resolution process, and notify all access holders and seekers as soon as the line diagrams have been updated**
  - **(e) update the online line diagrams if the QCA identifies any inaccuracy in them (either due to its own investigations or in response to complaints from access holders and access seekers).**

Ownership test

The QCA Act states the following service to be declared by the Ministers for access under Part 5, division 2:

> *the use of rail transport infrastructure for providing transportation by rail if the infrastructure is used for operating a railway for which Queensland Rail Limited, or a successor, assign or subsidiary of Queensland Rail Limited, is the railway manager (s. 250).*

The QCA is obliged to regulate in accordance with the QCA Act. The QCA is not in a position to consider Queensland Rail's proposal to exclude or remove any part of the service that has been declared by Ministers.

Therefore, the QCA requires that the 2013 DAU should include access to all rail transport infrastructure for which Queensland Rail is the railway manager.

Draft decision 1.3

- **The QCA requires Queensland Rail to amend its proposal so that the 2013 DAU is consistent with s. 250 of the QCA Act, such that the 2013 DAU applies to all rail transport infrastructure for which Queensland Rail is the railway manager.**

1.3 Non-discriminatory treatment

The QCA Act requires that the access provider must not unfairly differentiate between access seekers in negotiating access agreements, and users in providing access, in a way that adversely affects their ability to compete (ss. 100(2) and 168C). This applies whether or not the access provider is vertically integrated.

These provisions were introduced by the 2010 amendments to the Act to address industry concerns that privatising Aurizon's integrated above- and below-rail coal business in central Queensland would adversely affect competition in above-rail services. Therefore, there are no corresponding provisions in the 2008 undertaking.

Queensland Rail's 2013 DAU

The 2013 DAU (like the 2012 DAU) proposed that Queensland Rail would apply the undertaking consistently between access seekers in the same circumstances and would not unfairly

differentiate between access seekers or access holders, in accordance with s. 100 and s. 168C of the QCA Act.

Queensland Rail said that although it was a vertically integrated business with above- and below-rail activities, its above-rail operations were passenger train services that did not compete with third-party train services. As it did not compete in its above-rail activities and its obligations as a railway manager were subject to the provisions in the TI Act, it effectively acted as a non-vertically integrated access provider in respect of access to its rail network (Queensland Rail, sub. no. 2: 14, 17, 21). In particular:

(a) The TI Act preserved train paths for regularly scheduled passenger train services and obliged Queensland Rail to give priority to regularly scheduled passenger train services in allocating available train paths (ss. 266 and 266A of the TI Act) (Queensland Rail, sub. no. 2: 18).

(b) The network management principles (NMPs) in the DAU were designed to ensure train operators (including Queensland Rail) were treated consistently and transparently in respect of scheduling and on the day of operations.

Stakeholders' comments

Stakeholders were concerned that Queensland Rail's proposed restrictions on differentiating between access seekers and users still left scope for Queensland Rail to hamper their ability to compete effectively. In particular:

(a) The requirement that the undertaking apply consistently between access seekers in the same circumstances was too restrictive, given the circumstances of all access seekers would differ in at least some respects (Aurizon, sub. no. 9: 15-16; sub. no. 27: 11).

(b) While Queensland Rail was not vertically integrated with a freight train operator, its vertical integration of passenger train and below rail operations had the potential to conflict with its obligations to provide access for freight services (Asciano, sub. no. 6: 8-9; sub. no. 26: 12-13; Aurizon, sub. no. 9: 15-16; sub. no. 27: 11). In this regard, Asciano said

    (i) Queensland Rail had an incentive to develop processes that minimised the potential for freight rail operations to interfere with Queensland Rail passenger operations. Typically these impacts related to operational issues such as pathing priority and track occupations or allocation issues with the costs of Queensland Rail's above-rail and below-rail services (Asciano, sub. no. 26: 12)

    (ii) it was more appropriate that the regulatory process treat Queensland Rail as a vertically integrated access provider, albeit one that had substantially reduced financial incentives to discriminate against third-party users of its network as they were not in direct commercial competition with Queensland Rail (Asciano, sub. no. 26: 13).

Stakeholders also commented on the need for ring-fencing arrangements due to Queensland Rail's vertically integrated structure – that matter is discussed in Section 1.4 of this draft decision.

QCA analysis and draft decision

The provisions in the QCA Act deal primarily with situations where a vertically integrated provider competes with third parties in an above-rail market. Queensland Rail's passenger

services do not compete in the freight services market and the requirements are less onerous for Queensland Rail than for Aurizon Network.

Nevertheless, Queensland Rail is a vertically integrated operator and the QCA Act requires that its undertaking have provisions that prohibit unfairly differentiating between access seekers and prevent recovery of costs not reasonably attributable to a service (s. 137(1A)).

Although Queensland Rail's above-rail passenger services do not compete with third-party above-rail operators for customers, Queensland Rail might favour its passenger operations in scheduling trains, beyond what is required in the TI Act.

The QCA accepts stakeholders comments that it is in the interests of access seekers and access holders for freight services to be assured that they will receive equivalent terms and conditions in matters such as train operations and scheduling, unless otherwise provided for in the undertaking and subject to the constraints of the TI Act.

Queensland Rail is a monopolist and unless constrained can discriminate between, and therefore adversely affect, the interests of access seekers or users. Therefore, it is relevant to have provisions that constrain Queensland Rail's behaviour.

In particular, Queensland Rail's proposal to only provide consistent treatment between access seekers 'in the same circumstances' is unclear, and leaves room for discrimination on the basis of irrelevant or trivial grounds, where the effects of that discrimination may have a material impact on the interests of access seekers and users. The QCA therefore requires that this restriction be removed.

Further, Queensland Rail has not set out in the 2013 DAU how it will apply the unfair differentiation rules in s. 137(1A) of the QCA Act. The QCA considers that the DAU should be amended to include key provisions from the general principles of non-discrimination and independence in Aurizon Network's 2010 undertaking (Aurizon Network, October 2010, cl. 3.2). These include requirements that Queensland Rail will not engage in conduct for the purpose of preventing or hindering access, or provide more favourable access to a related party. They also specify that Queensland Rail will provide consistent service, and an equal opportunity to obtain access rights, to all access seekers. These amendments should address stakeholder concerns that Queensland Rail has an incentive to favour its above-rail passenger operations.

These requirements are consistent with s.137(1A) of the QCA Act and in the interests of access seekers and access holders (ss. 138(2)(e) and (h)).

The QCA notes that it has also required changes to Queensland Rail's proposed NMPs to enhance the consistency and transparency of the train scheduling and control processes, in part to protect the interests of third-party above-rail operators (see Chapter 4 of this draft decision).

Draft decision 1.4

- **The QCA requires Queensland Rail to amend its proposal so that it clearly sets out how it will be prevented from unfairly differentiating between access seekers and holders, by:**
  - **(a) removing the reference to 'in the same circumstances' from cl. 1.3(a)**
  - **(b) amending cl. 1.3(b) to specify that, consistent with s. 100 and s. 168C of the QCA Act, Queensland Rail will**
    - **(i) not engage in conduct for the purposes of preventing or hindering an access seeker's or access holder's access**
    - **(ii) not provide access to related operators on more favourable terms than the terms on which it provides access to competitors of related operators**
    - **(iii) ensure all access seekers, irrespective of whether they are a Queensland Rail party or a third party, are provided with a consistent level of service and given an equal opportunity to obtain access rights, subject to the express provisions of the QCA Act, the TI Act and this undertaking.**

1.4 Ring-fencing

A vertically integrated enterprise could potentially use its monopoly power in the below-rail market to gain an unfair competitive advantage in the above-rail market. For example, the below-rail operator could pass confidential information about third-party operators to its competitive arm, thereby providing its above-rail business with an inappropriate competitive advantage. Thus, vertical integration may lead to an actual or perceived conflict between actions undertaken in the interest of the integrated organisation and obligations to third-party train operators.

The QCA considers that effective ring-fencing arrangements go some way in reducing this potential conflict. Those arrangements separate monopoly functions (i.e. below-rail) from other business functions (e.g. above-rail) for organisational and accounting purposes, and include processes and protocols for managing information flows between the separated business functions.

The ring-fencing arrangements in the 2008 undertaking seek to address these issues by including rules for accounting separation (cl. 3.2), decision-making in compliance with the undertaking (cl. 3.4) and compliance and enforcement obligations (cl. 3.5).

Queensland Rail said in the material accompanying its 2012 DAU that its passenger train services did not compete with third-party operators of train services; therefore it did not propose ring-fencing provisions (Queensland Rail, sub. no. 2: 8). Stakeholders said ring-fencing arrangements were required to ensure transparent cost allocation between Queensland Rail's passenger business and below-rail network business (Asciano, sub. no. 6: 3, 9-10; QRC, sub. no. 14: 3).

Queensland Rail's 2013 DAU

Queensland Rail reiterated that ring-fencing requirements were relevant only for a vertically integrated monopoly that competed with third-party operators in downstream competitive

markets. Queensland Rail said that, although it was vertically integrated, its passenger train services did not compete with third-party operators of train services, and said:

> *The nature and structure of Queensland Rail's business means there is no real scope for Queensland Rail to use its market power to limit competition in the above rail markets. Highly prescriptive ring-fencing requirements would therefore impose significant costs on Queensland Rail without benefiting third party access seekers or access holders or promoting effective competition in downstream markets (Queensland Rail, sub. no. 2: 34).*

Queensland Rail said its constitution precluded it from operating non-passenger services that competed in above-rail freight markets (Queensland Rail, sub. no. 2: 15). It said this made it similar to RailCorp in New South Wales and V/Line in Victoria, that were also integrated rail businesses whose above-rail services did not compete with third-party train services. Queensland Rail said RailCorp's access undertaking did not include specific ring-fencing arrangements and the Victorian access regime contained ring-fencing rules that were never applied (Queensland Rail, sub. no. 2: 34).

Nevertheless, Queensland Rail proposed provisions in the DAU to protect and manage the confidential information of access seekers/holders (cl. 2.2).

Also, Queensland Rail said it would maintain separate accounting records for its declared and non-declared services and comply with the costing manual approved by the QCA, in accordance with ss. 159 and 163 of the QCA Act. Queensland Rail said it would work with the QCA on those matters, and did not include those requirements in the DAU (Queensland Rail, sub. no. 2: 35).

Stakeholders' comments

Asciano said a ring-fencing regime would allow users of the monopoly service to operate in the market and make long-term investment decisions with a degree of confidence that they would not be disadvantaged in the future. This regime should impose a degree of vertical separation and transparent cost allocation on Queensland Rail, to minimise:

(a) any cost shifting or cross-subsidisation between the network business and passenger service business

(b) the potential for Queensland Rail decision-making on operational or commercial matters in its above-rail passenger business to disadvantage third-party users of the Queensland Rail below rail business (Asciano, sub. no. 26: 13).

QCA analysis and draft decision

Ring-fencing of activities and information is required when a vertically integrated entity combines monopoly services with related operations that compete with third parties in another market.

The QCA considers that, with Queensland Rail's existing operational structure, ring-fencing issues are unlikely to affect competition. This is because Queensland Rail's passenger operations do not compete with other above-rail operators. The QCA also accepts that Queensland Rail's constitution prevents it from establishing above-rail freight operations.

However, there is nothing to stop Queensland Rail's constitution from being changed to allow it to operate freight trains. Indeed, a recent report by a Queensland parliamentary committee recommended that Queensland Rail re-enter the rail freight business to carry agricultural commodities (Queensland Parliamentary Committees, June 2014: 112-13). If that were to happen, ring-fencing arrangements would be required. Similarly, the sale of the Mount Isa line

with the Port of Townsville may well raise other vertical integration and competition issues with the nearby terminals at Abbot Point.

Therefore, the QCA considers that Queensland Rail's undertaking should provide for ring-fencing arrangements to be submitted by Queensland Rail before it enters an above-rail or any other market in competition with third-party operators.

The QCA notes that there are other aspects of regulation that are related to ring-fencing of information, but that are dealt with separately in the DAU.

First, there is confidentiality of information. Queensland Rail has addressed that through its proposed cl. 2.2 (see Section 2.8 of this draft decision).

Second, there is separation of financial information that provides transparency about cost-shifting and cross-subsidisation. This is addressed through the reporting requirements and costing manual (see Section 5.4.2 of this draft decision).

Draft decision 1.5

- **The QCA requires Queensland Rail to amend its proposal so that it is required to implement arrangements for ring-fencing information from its related party above-rail operator, if it enters a market in competition with third parties.**

1.5 Duration of the 2013 DAU

The QCA Act provides that an undertaking must state the expiry date, that determines the term of the undertaking (s. 137(1)). For example, Aurizon Network's successive undertakings, including the 2008 undertaking that now applies to Queensland Rail, have had initial terms of about four years (excluding any subsequent extensions) and the first undertaking of Dalrymple Bay Coal Terminal (DBCT) was for 4.5 years.

In the 2012 DAU, Queensland Rail had proposed a term of between four and five years with a terminating date of 30 June. Stakeholders initially had differing views, and proposed terms varying from three to ten years. However, in subsequent submissions on the 2012 DAU, stakeholders indicated they were not opposed to a term of between four and five years.

In the June 2013 DAU, Queensland Rail proposed a term of less than four years, commencing on the undertaking's approval date and terminating on 30 June 2017 (cl. 1.1).[3]

Queensland Rail said the term proposed was consistent with relevant Australian rail regulatory precedent – for example, ARTC's first access undertaking in 2002 had a five-year term. Queensland Rail also argued there was a low risk of circumstances changing during the term proposed that would make the undertaking irrelevant or inappropriate, and said:

> *Too short a term may provide only limited certainty and too long a term risks circumstances changing so the access undertaking is either no longer relevant or is inappropriate (Queensland Rail, sub. no. 2: 19-20).*

New Hope said the term of the undertaking should be no more than four years from 1 July 2013. It said the light-handed approach to regulation that Queensland Rail had proposed in the DAU was untested (New Hope, sub. no. 28: 1).

[3] This is different from the February 2013 DAU that proposed a term of between four and five years, depending on when the new undertaking was approved within a financial year (the same as the 2012 DAU).

QCA analysis and draft decision

An access undertaking provides a degree of certainty to all parties about the terms and conditions of access over its life. In particular, the QCA Act requires the QCA to arbitrate any dispute between an access seeker and access provider in a way that is consistent with the terms of an approved undertaking (s. 119(1)(a)).

In that context, the QCA accepts Queensland Rail's view that an undertaking with too short a term will provide all parties with only limited certainty, while too long a term could result in changed circumstances such that the undertaking was inappropriate. An excessively long term would be particularly problematic for access seekers and users of the infrastructure as they have no ability to seek to amend an approved undertaking.

Ideally, the termination date would be later than Queensland Rail's proposal of 30 June 2017, as it is unlikely the new undertaking will be approved before 1 January 2015, and that will only leave 2.5 years before the term expires. Indeed, if past experience is anything to go by, the 2017 DAU will have to be submitted sometime in 2015.

That said, the proposed term provides certainty while the undertaking is in place. A relatively short term is also appropriate for a document that has been subject to the comprehensive changes proposed by Queensland Rail to all aspects of its regulatory regime and given the possible changes that may occur to the structure and management of the network into the near future. In addition, the only reference tariff in the DAU, for coal services on the western system, is being assessed over a period ending 30 June 2017.

Therefore, the QCA considers that Queensland Rail's proposed undertaking termination date of 30 June 2017 is in the interests of access seekers and in the public interest (ss. 138(2)(d) and (e) of the QCA Act). On this basis, the QCA proposes to accept Queensland Rail's proposal.

2 NEGOTIATION AND CAPACITY MANAGEMENT (PART 2)

Queensland Rail's 2013 DAU proposes the process for negotiating with access seekers including the nature of information exchanged, the circumstances when Queensland Rail could cease negotiations, the rules for allocating limited capacity between competing access seekers and the rules for renewal rights.

Stakeholders said that Queensland Rail's proposal gave it too much discretion over a number of those matters.

The QCA agrees with stakeholders comments and has proposed amendments so that the negotiating parties are well informed, negotiations are timely, the process is certain and balances the interests of access seekers and Queensland Rail as the below-rail operator.

The QCA has also proposed amendments to reinstate a queuing mechanism for allocating capacity between competing access seekers and modified Queensland Rail's proposed renewal rights so that the rules are more certain and balances the interests of existing access holders, who have sunk investments, and Queensland Rail.

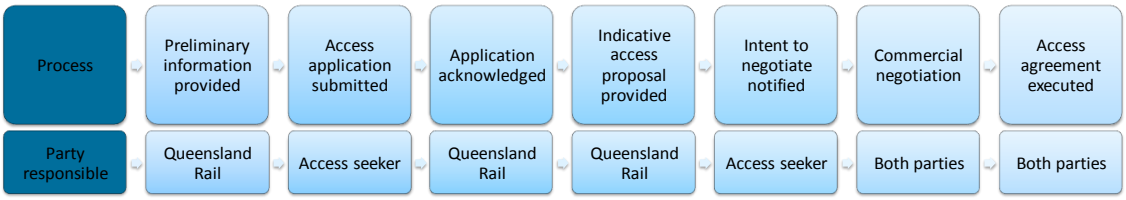
2.1 Introduction

The QCA Act establishes the central role of commercial negotiation for parties wishing to secure access rights.

An effective negotiation framework seeks to balance the legitimate business interests of an access provider as the owner or operator of the declared service and the interests of access seekers. It does so by defining the boundaries to, and the conditions of, negotiation enabling parties to negotiate in a timely manner and on reasonable terms as well as protecting an access provider from negotiating with a non-genuine access seeker. An effective negotiation framework can promote successful negotiations and hence facilitate access.

The 2008 undertaking set out the negotiation framework that outlines the responsibilities of Queensland Rail and access seekers during negotiation (see **Figure 2**).

Figure 2 The negotiation framework



Queensland Rail's 2012 DAU set out a similar negotiation framework. However it proposed changes to a number of elements, including the timeframes, the nature of information exchanged and the circumstances when Queensland Rail could cease negotiations. It also folded the capacity management section of the 2008 undertaking into the negotiations process. In doing so, it removed the queuing mechanism for allocating capacity between competing access seekers and modified the rules for renewing access rights.

Stakeholders (e.g. Asciano, Aurizon, New Hope, and Glencore) raised concerns with a number of those changes, reflecting a view that the 2012 DAU gave Queensland Rail absolute discretion on a number of matters.

2.2 Queensland Rail's 2013 DAU

Queensland Rail's 2013 DAU retained most of the 2012 DAU proposals. However, it amended the basis for ceasing negotiation and the rules for allocating capacity between competing access seekers as well as the rules for renewing access rights. This chapter considers key aspects of Queensland Rail's proposed negotiation framework, namely:

(a) nature of the information exchanged by parties (Section 2.3)

(b) timeframes for action (Section 2.4)

(c) Queensland Rail's right to reject an access application or cease negotiation (Section 2.5)

(d) rules for allocating capacity between competing access applications (Section 2.6)

(e) rules for renewing access rights (Section 2.7)

(f) other matters (e.g. confidentiality provision) (Section 2.8).

The related matter of developing new standard access agreements is considered in Chapter 7 of this draft decision.

2.3 Information exchange

The 2008 undertaking and the 2013 DAU set out two aspects of information exchange during the negotiations process, which are information:

(a) required by Queensland Rail from an access seeker

(b) provided by Queensland Rail to an access seeker.

2.3.1 Information required by Queensland Rail

The 2008 undertaking specifies the information an access seeker provided to Queensland Rail to describe its proposed train service and planned operations. Queensland Rail could also seek additional information if it could reasonably demonstrate it needed this information to prepare an indicative access proposal (IAP) (2008 undertaking, schedules C and D, cls. 4.1(b), 4.2(b), 4.5.2(a)(ii)).

Queensland Rail's 2013 DAU

Queensland Rail's 2013 DAU was unchanged from the 2012 DAU and proposed specifying the information requirements on its website rather than including them in any approved undertaking. It also proposed that it might seek additional information from access seekers when preparing an IAP.

Queensland Rail said it was not necessary to include the information requirements in an undertaking, as its passenger business did not compete with third party above-rail freight operators. Queensland Rail said that its proposal would result in a more efficient and timely process for updating those requirements, as it would not be required to submit a draft amending access undertaking (DAAU), which would enable it to keep the requirements up to date and readily available to customers (Queensland Rail, sub. no. 2: 46-47).

Stakeholders' comments

Stakeholders (Asciano and Aurizon) were concerned that Queensland Rail could unilaterally amend the website documents – i.e. amend the information an access seeker must provide to Queensland Rail without QCA approval (Asciano, sub. no. 31: 4; Aurizon, sub. no. 27: 11-12, 15).

Aurizon said that Queensland Rail could seek unreasonable or irrelevant information and cease negotiations if access seeker did not provide that information, while the access seeker did not have the ability to dispute the nature of that information.

Stakeholders suggested including provisions to protect the interests of access seekers (Aurizon, sub. no. 27: 11, 15; Asciano, sub. no. 31: 4).

Asciano said that Queensland Rail should consult stakeholders before amending the website documents, which should:

- *require Queensland Rail to justify any proposed changes;*
- *require Queensland Rail to consider comments from stakeholders and if these comments are not incorporated in the Queensland Rail final documents explain why they have not been incorporated; and*
- *require QCA to approve any proposed changes (Asciano, sub. no. 31: 4).*

Aurizon said that 'stakeholders should have the ability to access a dispute resolution mechanism if they consider Queensland Rail have not adequately addressed their concerns.'

QCA analysis and draft decision

The QCA recognises that it is in Queensland Rail's legitimate business interest to require information from access seekers to assess its ability to meet their access requirements. Access seekers' interests are also served to the extent Queensland Rail can prepare a better IAP based on the information provided by them.

That said, Queensland Rail's 2013 DAU proposal departs significantly from the 2008 undertaking. Queensland Rail proposes to specify the information requirements on its website. That is not, in itself, an issue, in particular if it removes unnecessary detail from the undertaking and increases Queensland Rail's flexibility in how it manages its access negotiations. The issue is that Queensland Rail's proposal contains only very limited external review and oversight provisions. Relevantly, Queensland Rail will be able to change its information requirements or seek additional information without reasonably justifying the need for that information.

The QCA recognises that Queensland Rail's passenger train services do not compete in the same markets with third party freight operators. But they do consume train paths that could otherwise be available for freight services, some of which are for network that is capacity constrained. The QCA also recognises that there is potential for Queensland Rail to seek more information from access seekers, with its associated cost, than might be necessary.

Moreover, the 2013 DAU is ambiguous about the relevant standards and requirements for operating trains that will be specified on Queensland Rail's website. In this regard, it is not clear whether Queensland Rail will publish an operating plan template on its website (which specifies these requirements).

Therefore, the QCA considers that Queensland Rail's proposal introduces the potential for arbitrariness into the information provision process for access negotiations. This creates uncertainty for access seekers and it is not in their interests.

Information requirements to be certain and subject to oversight

The QCA agrees with Asciano and Aurizon that the undertaking should provide certainty about the information that Queensland Rail requires for access negotiations and must provide an oversight mechanism for any changes to those requirements.

Accordingly, the QCA would favourably consider an undertaking where the first published versions of the information requirements – i.e. the access application form and the operating plan template, are approved by the QCA. In this context, it is noted that the QCA has reviewed those two documents and, if asked, is likely to approve them for publication on Queensland Rail's website, as they are largely consistent with the 2008 undertaking and stakeholders did not raise any concerns[4].

Furthermore, Queensland Rail must consult its customers (i.e. actual and potential access seekers) before making any amendments to those documents and the undertaking must include a dispute process should customers disagree with those changes. Queensland Rail must also report the number of those disputes, which will indicate how well this regime is working (see Section 5.3 of this draft decision).

This approach of initial regulatory approval of technical details not included in an undertaking and a consultation and dispute resolution process for subsequent amendments has been effectively used by the QCA in a number of circumstances. For example, it has been a feature of DBCT's undertaking since 2006 in relation to terminal regulations and of Aurizon Network's 2010 undertaking for system rules.

This still leaves a potential for Queensland Rail to seek additional information from access seekers in preparing an indicative access proposal without reasonably justifying the need for that information. The QCA considers that Queensland Rail can seek additional information, if it can reasonably demonstrate the need for that information.

[4] Aurizon suggested that the disclaimer in the access application form that it is not to be used for access to QR National rail network should refer to Aurizon Network (Aurizon, sub. no. 33: 59).

Draft decision 2.1

- **The QCA requires Queensland Rail to amend its proposal so that:**
  - **(a) for the access application form and operating plan template**
    - **(i) the undertaking provides that the operating plan template will be published on Queensland Rail's website**
    - **(ii) the QCA approves the first version of the access application and operating plan templates published on Queensland Rail's website**
    - **(iii) any amendment to a template is undertaken after Queensland Rail reasonably justifies the need for amending it and consults its customers**
    - **(iv) any dispute about an amendment is resolved through the dispute resolution process in the undertaking**
    - **(v) if an amendment takes effect, Queensland Rail publishes a marked up version of the template on its website and notifies its customers about the amendment**
    - **(vi) Queensland Rail reports separately the yearly number of disputes arising in relation to the access application form and the operating plan template**
  - **(b) Queensland Rail can seek additional information from an access seeker if it can reasonably demonstrate the need for that information in preparing an indicative access proposal (IAP).**

2.3.2 Information provided by Queensland Rail

The 2008 undertaking specifies the technical, operating and commercial information that Queensland Rail provides to an access seeker. It also requires Queensland Rail to provide other information as per s. 101 of the QCA Act (cl. 4.5.2(a)(i), and schedule D, part B, 4.(a) of the 2008 undertaking).

The QCA Act requires Queensland Rail to make reasonable efforts to satisfy the reasonable requirements of an access seeker and lists the information that Queensland Rail must give the access seeker, including information about access price (and the pricing methodology), costs (including capital, operating and maintenance) and asset values (and the asset valuation methodology), which could alternatively be given in the form of a reference tariff (ss.101(1), and 101(2) and 101(4)).

Queensland Rail's 2013 DAU

Queensland Rail's 2013 DAU, like the 2012 DAU, proposed that Queensland Rail will provide information if an access seeker could reasonably demonstrate the need, provided that information was ordinarily and freely available to Queensland Rail and did not breach its confidentiality obligations (cls. 2.1.3, 2.6.2(a)(i)).

Queensland Rail said that it was not necessary to specify, in the undertaking, the information it would provide in access negotiations. That was because it did not have the incentive to withhold information to hinder third party access, as its passenger business did not compete with third party above-rail freight operators (Queensland Rail, sub. no. 19: 13).

In particular, Queensland Rail said that it did not propose to provide detailed cost information for the Mount Isa and North Coast lines because:

(a) s. 101 of the QCA Act did not place an 'absolute obligation' on Queensland Rail to provide that information. Queensland Rail said the Act's requirement was 'subject to any ... approved undertaking' and the QCA would need to consider the Act's assessment criteria before determining the level of cost information disclosure in an undertaking.

(b) access pricing in those lines had traditionally been 'market based' and not 'cost based' because of strong intermodal competition; consequently, cost data was irrelevant (Queensland Rail, sub. no. 19: 20).

Queensland Rail said that it provided considerable information on its website and customer portal to assist access seekers and holders and considered its proposal was appropriate (Queensland Rail, sub. no. 19: 13).

Information in IAP

Queensland Rail's 2013 DAU retained some of the 2008 undertaking's provisions in relation to the information included in an IAP (e.g. providing a capacity analysis). However, it did not include information about the rolling stock and other relevant operating characteristics used to develop an IAP (cl. 2.4.2).

Stakeholders' comments

Concerns with Queensland Rail's proposal

Stakeholders said that Queensland Rail had proposed to provide insufficient information in access negotiations. They said that Queensland Rail's proposal created uncertainty because the information it would provide was subject to being 'ordinarily and freely available to Queensland Rail' (Aurizon, sub. no. 27: 4-5, 12, 14; Asciano, sub. no. 26: 7; Glencore, sub. no. 29: 3).

In particular, Glencore said there was a substantial risk that the proposal, if approved, could limit the 'disclosures required under s. 101 of the QCA Act' (Glencore, sub. no. 30: 5).

Stakeholders disagreed with Queensland Rail that it did not have the incentive to withhold information. Aurizon said that although Queensland Rail was not vertically integrated, that:

> *does not mean that it has no ability or incentive to charge monopoly rents, particularly when it faces competing operators and may be able to improve its returns at the expense of one over the other (Aurizon, sub. no. 27: 5).*

Glencore said that Queensland Rail was effectively a monopolist for bulk minerals train services on the Mount Isa line and set the market price for those services; consequently, it disagreed with Queensland Rail that information need not be disclosed if 'pricing is market based rather than cost based' (Glencore, sub. no. 29: 2-3).

Information disclosure in a negotiate-arbitrate model

Stakeholders said that an effective negotiate-arbitrate model required access seekers to have enough information to competitively negotiate with Queensland Rail. They said that the lack of cost information disadvantaged access seekers in negotiating access prices with Queensland Rail (Asciano, sub. no. 26: 7, 11; Aurizon, sub. no. 27: 4; Glencore, sub. no. 29: 3 and 30: 4-5). In particular, Aurizon said:

> *There is no publicly available information to assist access seekers in assessing the reasonableness of QRail's proposed access charge or what risks the access holder is exposed to over time in relation to the movement of access charges (27: 20).*

Stakeholders said that Queensland Rail must provide detailed information for line sections relevant to the service being negotiated on matters including:

(a) costs: capital, operating and maintenance costs (on stand-alone and incremental basis)

(b) assets: asset value (and the valuation methodology), asset life and depreciation

(c) prices: access price (and the pricing methodology), floor and ceiling prices where there was no reference tariff

(d) capacity: spare capacity estimate (including the way it was calculated), master train plans, capacity expansion options including triggers and estimated costs

(e) revenues: current and projected future revenue streams

(f) service quality information

(g) technical and operational issues: technical characteristics of infrastructure, infrastructure standards and protocols, section running times (Asciano, sub. no. 31: 12-14; Aurizon, sub. no. 27: 6, 12, 14, 18 and 33: 6; Glencore, sub. no. 29: 3-4 and 30: 6).

Glencore stated that the 2013 DAU should 'expressly reflect the requirements of s. 101 of the QCA Act' or state clearly that the undertaking's information disclosure provisions supplemented the QCA Act requirements (Glencore, sub. no. 29: 4).

Information in IAP

Aurizon said that the IAP should provide information about the rolling stock and other relevant operating characteristics used to develop the IAP and identify, for non-coal freight, material divergences from the standard access agreement (Aurizon, sub. no. 27: 14).

QCA analysis and draft decision

The rail network in Queensland has been declared since 1997. Since that time the operator of the network has had obligations to provide certain, basic information to access seekers.

The provision of some of that information can be excised if there is a reference tariff in place or if its disclosure can damage the operator's or a third party's commercial activities. The QCA notes that reference tariffs have applied to coal traffics in central Queensland since 2001 and the western system since 2006.

Consequently, these information provision requirements have existed for a long period of time for the networks operated by Queensland Rail. Therefore, it is anticipated that Queensland Rail would already have put in place systems to meet those information requirements.

Queensland Rail's 2013 DAU proposal seeks to take a step back and states that Queensland Rail will provide information that is readily available to it.

It is not clear what that means and this uncertainty has created a great deal of concern to stakeholders.

The QCA considers that the provisions of s. 101 of the QCA Act (including that of the 2008 undertaking) are not particularly onerous. They require Queensland Rail to provide access seeker information on matters such as:

(a) price of a service

(b) cost of a service (and elements of those costs)

(c) spare capacity, which requires an understanding of the extent of the network's capacity and of the capacity being consumed by existing traffic

(d) safety systems.

This is reasonably basic information that one would expect Queensland Rail's managers would be interested in and would, therefore, be freely and readily available.

They are also unlikely to be onerous to Queensland Rail as they are not new – these obligations have existed for over 15 years.

Therefore, the QCA would favourably consider an undertaking where Queensland Rail's information disclosure obligations remain consistent with the QCA Act and the 2008 undertaking.

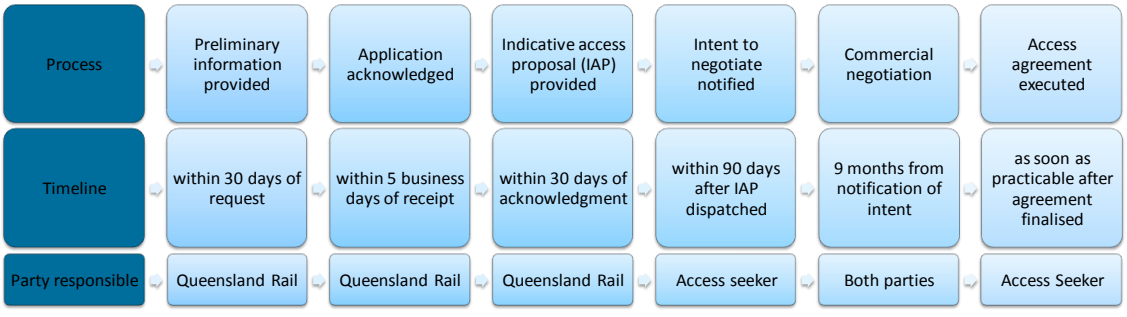
Draft decision 2.2

- **The QCA requires Queensland Rail to amend its proposal so that:**
  - **(a) for rail corridors where no reference tariffs apply, the undertaking specifies the cost and pricing information that Queensland Rail will provide for each corridor to an access seeker consistent with s. 101(2) of the QCA Act and Schedule D of the 2008 undertaking**
  - **(b) the undertaking specifies the capacity, technical and operating information that Queensland Rail will provide to an access seeker for each rail corridor it manages consistent with s. 101(2) of the QCA Act and Schedule D of the 2008 undertaking**
  - **(c) the undertaking specifies that Queensland Rail will provide additional information to access seekers that it can reasonably provide consistent with s. 101(1) of the QCA Act and Schedule D of the 2008 undertaking, subject to its confidentiality obligations**
  - **(d) Queensland Rail's indicative access proposal (IAP) to an access seeker includes information on the price at which Queensland Rail will provide the service (including the pricing methodology), the rolling stock and other relevant operating characteristics used to develop that IAP consistent with cl. 4.3 of the 2008 undertaking.**

2.4 Timeframes

The 2008 undertaking provides fixed timeframes for different stages of the negotiation process (see **Figure 3**).

Figure 3 Timeframes in the 2008 undertaking



However, it also provides some flexibility with protections in certain circumstances. For instance:

(a) Queensland Rail can delay providing an IAP if the application raises complex issues. An access seeker can dispute that if it considers the delay is excessive.

(b) Parties can agree to extend the time for an access seeker to notify its intent to negotiate. Queensland Rail can revise the IAP and restart the negotiation timeline if an access seeker delayed in notifying its intent to negotiate.

(c) Parties can agree to extend the negotiation period (2008 undertaking, cls. 4.2(c); 4.3(c); 4.3(a)(vii); 4.4(b); 4.5.1(e)(iv)(A)).

Queensland Rail's 2013 DAU

Queensland Rail's 2013 DAU was the same as its 2012 DAU. In the 2013 DAU, Queensland Rail retained the 2008 undertaking timeframes for acknowledging an access application and commercial negotiation, including that parties can agree to extend the negotiation period (cls. 2.3.2; 2.6.1(b)(ii)(D)).

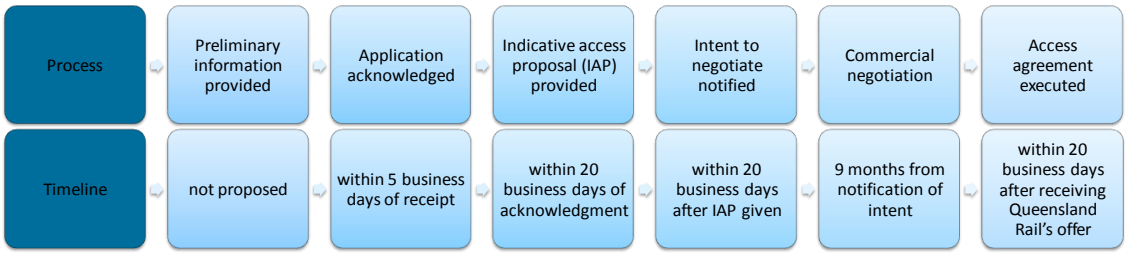
However, Queensland Rail:

(a) did not propose a timeframe for providing preliminary information but proposed reporting annually the number of requests for preliminary information and the average time it took to provide that information

(b) reduced significantly the time for an access seeker to notify its intent to negotiate

(c) introduced a time limit for an access seeker to execute the agreement (see **Figure 4**).

Figure 4 Timeframes proposed in the 2013 DAU



The 2013 DAU proposed that Queensland Rail could delay providing an IAP (cl. 2.4.1(a)). Queensland Rail said that it required 'the ability to extend the time period for complex IAP responses' (Queensland Rail, sub. no. 5: 2).

The 2013 DAU also proposed that if an access seeker:

(a) delayed in notifying its intent to negotiate (i.e. after 20 business days (see **Figure 4**) but before three months), Queensland Rail could revise the IAP at its absolute discretion, thereby retreating the application back to the IAP stage (cl. 2.5.2(a))

(b) did not notify its intent to negotiate within three months, Queensland Rail could reject the application at its absolute discretion (cl. 2.5.2(c))

(c) did not execute the access agreement within 20 business days, Queensland Rail could cease negotiations at its absolute discretion (cl. 2.7.6(a)).

Stakeholders' comments

Aurizon said the 2013 DAU did not clearly state the circumstances when Queensland Rail could exceed the timeframe for providing an IAP. It said that this created limited obligation for Queensland Rail to comply with that timeframe and that

> *is reinforced by QRail's obligation to only report the number of IAP's provided within the timeframe ... (Aurizon, sub. no. 27: 13).*

Aurizon suggested a longer timeframe for providing an IAP only when the infrastructure had to be extended or when parties agreed. Aurizon also suggested that Queensland Rail should report in ranges the time it took to provide the IAPs (Aurizon, sub. no. 27: 13).

It said that the undertaking should allow parties to continue negotiation where they agreed to extend the negotiation period (Aurizon, sub. no. 27: 14).

QCA analysis and draft decision

The QCA considers that negotiation timeframes are necessary to facilitate timely access, and the undertaking should specify timeframes that parties can reasonably be expected to meet. However, timeframes are not an end in themselves, and the undertaking should allow parties the opportunity to depart from those timeframes to deal with exceptional circumstances.

Preliminary information

While Queensland Rail did not propose a timeframe for providing preliminary information, it proposed reporting annually the number of requests for preliminary information and the average time it took to provide that information.

The QCA expects Queensland Rail should have the ability to readily provide a range of basic network information to access seekers (see Section 2.3.2 of this draft decision). Therefore, it is prudent to have in place a timeframe for Queensland Rail to provide that information. The QCA considers that Queensland Rail should reinstate into the 2013 DAU the timeframes consistent with the 2008 undertaking – i.e. provide preliminary information within 10 business days if that information has been previously compiled, otherwise within 20 business days.

The QCA considers that the undertaking should allow Queensland to extend the time for providing preliminary information, if it can reasonably justify that extension and the access seeker agrees to the extended time.

The QCA considers that Queensland Rail should also report in ranges the time it took to provide preliminary information, similar to its proposal for reporting on the overall negotiation period. This is considered further in Section 5.3 of this draft decision.

IAP and intent to negotiate

The 2013 DAU proposed the same timeframe of 20 business days for Queensland Rail to provide an IAP and for the access seeker to notify its intent to negotiate on the basis of that IAP.

The QCA agrees with Aurizon that the 2013 DAU allows Queensland Rail to extend the time for providing an IAP without justifying its action and without facing any apparent consequences for that delay. This creates the risk of unnecessary delays. On the other hand, an access seeker faces adverse consequences for notifying late its intent to negotiate – i.e. a delayed negotiation or a rejection, regardless of the complexity of its application that could justify that delay. Given this, the extension process is not balanced between Queensland Rail and access seekers.

The QCA considers that the undertaking should allow a departure from timeframes, if it can be reasonably justified and is done in a way that balances the parties' interests.

Therefore, the QCA considers that the undertaking should allow Queensland to extend the time for providing an IAP beyond 20 days and an access seeker to extend the time for notifying its intent to negotiate, if each can reasonably justify its decision and the other party agrees to the extended time.

The QCA also considers that reporting those timeframes would place greater accountability on Queensland Rail and access seekers to meet their obligations regarding timeliness. Therefore,

the QCA agrees with Aurizon that Queensland Rail should report in ranges the time it took to provide the IAPs. The QCA also considers that Queensland Rail should provide a similar report for the time access seekers took to notify their intent to negotiate. This is considered further in Section 5.3 of this draft decision.

Other matters

The QCA considers that the 2013 DAU allows parties to continue negotiations where they agree to extend the negotiation period, which addresses Aurizon's comment.

Stakeholders did not comment on Queensland Rail's proposed time limit for the access seeker to execute the access agreement. The QCA considers that it is a reasonable proposal as it encourages timeliness in executing an access agreement. That said, the QCA considers that the undertaking should allow a departure from that timeframe, if the party seeking an extension can reasonably justify it and parties agree.

The QCA does not accept that Queensland Rail should have an 'absolute discretion' in determining the consequence of non-compliance with timeframes, as it could result in arbitrary actions that cannot be challenged. The QCA would favourably consider an undertaking that allows Queensland Rail to act in its 'reasonable discretion'.

2.5 Refusal to provide access

The 2008 undertaking entitled Queensland Rail to cease negotiations to protect its legitimate business interests in circumstances where it considered an access seeker:

(a) had no genuine intention of obtaining/using access rights (e.g. whether the access seeker has a right to unload at its destination)

(b) was non compliant – i.e.

  (i) did not comply with a dispute outcome

  (ii) failed materially to comply with the undertaking's obligations and processes

  (iii) was unlikely to comply materially with an access agreement (e.g. if access seeker was insolvent or had defaulted materially on an access agreement) (2008 undertaking, cl. 4.6(b)).

Draft decision 2.3

- **The QCA requires Queensland Rail to amend its proposal so that for**
  - **(a) Preliminary information related to an access application:**
    - **(i) Queensland Rail provides that information to an access seeker within 10 business days if previously compiled, otherwise 20 business days**
    - **(ii) Queensland Rail can extend the time for providing preliminary information to an access seeker if it can reasonably justify that extension and the access seeker agrees**
    - **(iii) Queensland Rail's annual report on compliance with the undertaking includes the time taken to provide preliminary information to access seekers, broken down into less than 10 business days, 10 to 20 days, 21 to 40 days, and more than 40 days.**
  - **(b) IAP and intent to negotiate:**
    - **(i) Queensland Rail can extend the time for providing the IAP to an access seeker beyond 20 days and an access seeker can extend the time for notifying Queensland Rail of its intent to negotiate, if each party can reasonably justify its decision and the other party agrees to the extended time**
    - **(ii) Queensland Rail's annual report includes the time taken by Queensland Rail to provide the IAP to an access seeker and by an access seeker to notify its intent to negotiate, broken down into less than 10 business days, 10 to 20 days, 21 to 40 days, and more than 40 days.**
  - **(c) Execution of access agreement: Queensland Rail and an access seeker can agree to a different timeframe within which to execute an access agreement if the party seeking the extension can reasonably justify it.**
  - **(d) Consequences for non-compliance with negotiation timeframes: Queensland Rail must replace 'absolute discretion' in determining the consequence of access seeker's non-compliance with timeframes with the term 'reasonable discretion'.**

The 2008 undertaking entitled Queensland Rail to recover its negotiation costs from an access seeker that had no genuine intention of obtaining/using access rights.

Queensland Rail's 2012 DAU retained the circumstances for refusing access in the 2008 undertaking but extended these further to include where:

(a) it considered an access seeker was 'not reputable or of good financial standing',

(b) the access application was frivolous or adversely affected passenger safety.

The 2012 DAU also entitled Queensland Rail to recover its negotiation costs in a number of those circumstances.

Stakeholders said those new circumstances for refusing access gave Queensland Rail 'unfettered discretion' and favoured its passenger operations. They also said that Queensland Rail should recover negotiation costs only from access seekers that had no genuine intention to use access rights (Asciano, sub. no. 6: 13; Aurizon, sub. no. 9: 19-21; Glencore, sub. no. 15: 4-5).

Queensland Rail's 2013 DAU

Queensland Rail's 2013 DAU modified its earlier 2012 proposal (e.g. it removed the 'not reputable or of good financial standing' circumstance). The DAU broadly retained the 2008 undertaking's circumstances for refusing access, albeit with some changes. For instance, it removed the criteria for assessing whether an access seeker was 'unlikely to materially comply with an access agreement'. Additionally, Queensland Rail proposed new circumstances that entitled it to refuse to provide access – i.e. reject access application or cease negotiations, if it considered an access seeker:

(a) was non compliant; that is:

  (i) did not agree to comply with the undertaking obligations and processes when submitting its access application

  (ii) did not comply with certain negotiation timeframes (i.e. did not notify its intent to negotiate or did not execute the access agreement, within specified timeframes – see Section 2.4) (cls. 2.1.1(c); 2.5.2(c), 2.7.6(a)).

(b) did not meet prudential requirements – if access seeker was insolvent, had defaulted materially on an access agreement or Queensland Rail's undertaking, and did not have the financial capacity to honour an access agreement (cl. 2.6.3(a)(iv), 2.9)

(c) adversely affected passenger operations – if access seeker's train service was likely to adversely affect passenger safety or disrupt passenger train services in the metropolitan region, and no measure could be taken by the parties to mitigate those effects (cl. 2.6.5)

(d) was frivolous (cls. 2.6.3(a)(ii)(C), 2.6.4).

Queensland Rail said that its proposal to reject access applications on grounds of passenger issues would ensure efficient operation of passenger services in the metropolitan region, while providing appropriate protections for access seekers. It said:

> *The efficient running of passenger services in the Metropolitan Region is both in the public interest and Queensland Rail's legitimate business interests (Queensland Rail, sub. no. 19: 13).*

Queensland Rail stated it was in its legitimate business interest to reject applications that were 'clearly frivolous', and that it would not reject non-frivolous applications. It said that a frivolous application would result in its resources being allocated to that application 'potentially to the detriment of genuine Access Seekers and Queensland Rail's other business activities'. It added that the undertaking's dispute process protected the access seekers (Queensland Rail, sub. no. 5: 3).

Queensland Rail retained the circumstance in the 2008 undertaking for recovering its negotiation costs. It also extended its discretion to recover costs in a number of other circumstances – that is, when an access seeker did not comply with the dispute process/outcome, failed to comply with the undertaking, was unlikely to comply with an access agreement, did not meet prudential requirements, and was frivolous (cl. 2.6.3(c)). Queensland Rail said these circumstances effectively reflected that the access seeker was not genuine, adding that:

> *In such a case, it is reasonable that Queensland Rail should be reimbursed as there is no other avenue for cost recovery (i.e. via Access Charges) (Queensland Rail, sub. no. 5: 3).*

Stakeholders' comments

Stakeholders said that the 2013 DAU allowed Queensland Rail to refuse access either to protect its passenger interests or in circumstances that were ill defined.

Passenger services

Aurizon said that the proposal for Queensland Rail to refuse access on grounds of passenger operations protected Queensland Rail's business interests as an operator of passenger trains. Aurizon said this was different from Queensland Rail's legitimate business interests as an operator or owner of the declared service. It suggested that the proposal should be extended to address disruption to freight train services as well (Aurizon, sub. no. 27: 16).

Asciano said that an independent body, such as the QCA, should assess the adverse effects on passenger operations because of the potential conflict of interest for Queensland Rail; Aurizon said that the assessment should be 'a matter of fact' and not 'QRail's consideration' (Aurizon, sub. no. 27: 16; Asciano, sub. no. 26: 5).

Aurizon sought clarity on the adverse effects a freight train service would cause to passenger safety that would not be caused by a passenger train service (Aurizon, sub. no. 27: 16).

Other circumstances and negotiation costs

Aurizon said that the undertaking should include criteria to define the term 'frivolous' application. It also sought clarity on 'what would constitute a material default of the undertaking' in assessing prudential requirements (Aurizon, sub. no. 27: 16, 19).

Glencore and Aurizon said that Queensland Rail had proposed a broad set of circumstances when it could recover its negotiation costs. They suggested that Queensland Rail should recover costs only from access seekers that had no genuine intention of obtaining access rights (Aurizon, sub. no. 27: 15; Glencore, sub. no. 29: 7). Glencore said:

> *Access Seeker's already bear their own costs of negotiation and consequently are economically incentivised not to make unnecessary access applications (Glencore, sub. no. 29: 8).*

QCA analysis and draft decision

The QCA Act obliges Queensland Rail to negotiate an access agreement with an access seeker (s. 99). In doing so, Queensland Rail must negotiate in good faith and must make all reasonable efforts to satisfy the reasonable requirements of an access seeker (ss. 100 and 101). The QCA Act envisages that those negotiations will end in either the successful conclusion of an access agreement or in a QCA dispute resolution process (ss. 111 to 127D). The QCA Act does not provide for Queensland Rail to cease negotiations.

Notwithstanding this, the QCA considers it is reasonable for Queensland Rail to refuse to provide access in certain circumstances to protect its legitimate business interests, for example, when an access seeker has no genuine intention of using access rights. However, that right should be subject to appropriate checks and balances to prevent its misuse. In particular, the circumstances should be clear and based on objective criteria and Queensland Rail should be able to establish that its legitimate business interest as a below-rail operator will be harmed.

Passenger services

The QCA accepts Aurizon's argument that Queensland Rail's proposal could be interpreted to be biased against freight train services and therefore is discriminatory. The proposal also focuses on protecting Queensland Rail's passenger interests and not its legitimate business interests as a below-rail operator.

The QCA considers that the 2013 DAU has other provisions (e.g. interface risk assessment) and other means (e.g. passenger priority obligation in the TI Act) that allow Queensland Rail to protect its passenger interests. Achieving a better balance of Queensland Rail's passenger

priority needs, with the timely movement of freight trains, was also a particular focus of a recent Parliamentary Committee report (Queensland Parliamentary Committees, June 2014).

Taking all of these factors into account, the QCA considers that this clause should be removed. But, that is not to say that the QCA would not consider an alternative proposal that provides a better balance of Queensland Rail's legitimate business interests as a below-rail operator and the interests of access seekers.

Other circumstances

There are a range of other issues with Queensland Rail's proposal.

First, the QCA notes that Queensland Rail has not proposed criteria to define the newly proposed term 'frivolous' application; therefore the QCA considers that Queensland Rail's proposal creates uncertainty and gives Queensland Rail unnecessary discretion in refusing access applications.

The QCA considers that this clause should be removed. The QCA is willing to consider an alternative proposal that includes an objective and transparent criteria to define what constitutes 'frivolous' application, which cover situations not already covered by the circumstances set out in the 2008 undertaking.

Second, the QCA notes that Queensland Rail has not proposed criteria for assessing whether an access seeker was 'unlikely to materially comply with an access agreement'. The QCA notes that Queensland Rail's proposed criteria for assessing the newly proposed prudential requirements circumstance are similar as those in the 2008 undertaking for assessing whether an access seeker was 'unlikely to materially comply with an access agreement'.

Therefore, the QCA considers that an assessment of prudential requirements should enable Queensland Rail to assess whether an access seeker was 'unlikely to materially comply with an access agreement'.

Third, the QCA considers that the 2013 DAU already defines 'material default of the undertaking', which addresses Aurizon's comment.

Negotiation costs

Queensland Rail has proposed recovering its negotiation costs from access seekers in a number of circumstances – for instance, when an access seeker has no genuine intention of obtaining access rights, is not meeting prudential requirements or fails materially to comply with the undertaking.

The QCA agrees with Queensland Rail that each of those circumstances identify non-genuine access seekers. Therefore, the QCA considers that Queensland Rail's proposal is reasonable, subject to Queensland Rail complying with the QCA's draft decision on certain aspects of those circumstances (e.g. removing the frivolous application clause).

Draft decision 2.4

- **The QCA requires Queensland Rail to amend its proposal so that:**
  - **(a) the 2013 DAU deletes the clauses for the purpose of ceasing negotiations**
    - **(i) passenger safety and passenger operations (cl. 2.6.5)**
    - **(ii) frivolous application (cls. 2.6.3(a)(ii)(C) and 2.6.4)).**
  - **(b) for the purpose of ceasing negotiations the circumstance 'unlikely to comply materially with an access agreement' includes the assessment of prudential requirements (cls. 2.6.3(a)(ii)(A)) and 2.6.3(a)(iii)).**

2.6 Competing access requests

Competing access seekers are generally one of two types – those who seek access rights in case of:

(a) competitive tendering – compete to serve the same customer

(b) mutually exclusive paths – seek access to serve different customers in the face of insufficient capacity.[5]

In the case of competitive tendering, the 2008 undertaking provides that Queensland Rail will negotiate with each access seeker and provide a price and the terms and conditions of access. Eventually, Queensland Rail will execute an access agreement with the access seeker selected by the customer (2008 undertaking, cl. 7.4.1(l)).

In the case of competition for mutually exclusive paths, the 2008 undertaking provides a queuing mechanism for allocating the limited available capacity on a 'first-come first-served basis',[6,7]. However, Queensland Rail can re-order access seekers' position in a queue in defined circumstances[8]. Queensland Rail is required to provide feedback to access seekers for any change in their queue position (2008 undertaking, cl. 7.4.1).

Queensland Rail's 2012 DAU did not distinguish between the two types of competing access seekers, removed the queuing mechanism and the feedback provision and set out the factors (e.g. access charges and access agreement term) that Queensland Rail would consider in its absolute discretion to identify the most favourable access seeker to it, regardless of their type.

Stakeholders said the 2012 DAU gave Queensland Rail discretion in deciding between competing access seekers, particularly where they competed for the same customer. They wanted a mechanism in the undertaking for choosing between applications offering equivalent terms to Queensland Rail and a feedback provision for unsuccessful applicants (Asciano, sub.

[5] A third type is where a new access seeker competes for access rights with an existing access holder seeking to renew its access rights that raises the issue of access renewal rights; therefore it is considered separately in Section 2.7 of this draft decision.

[6] Applications of access seekers competing for the same customer are collectively positioned in the queue as though they were a single application.

[7] The issue of expanding network capacity to create additional available capacity is considered in Section 2.8 of this draft decision.

[8] For example, when a queue contains multiple applications for train services relating to different traffic types, an application of a traffic type presenting a higher net present value (NPV) of contribution to the below-rail common costs can be moved ahead of another traffic type presenting a lower NPV (2008 Undertaking, clause7.4.1(e)).

no. 6: 13; Aurizon, sub. no. 9: 18, sub. no. 10: 9; Glencore, sub. no. 15: 4; New Hope, sub. no. 11: 2).

Queensland Rail's 2013 DAU

Queensland Rail's 2013 DAU retained the 2012 DAU proposal and included provisions for choosing between equivalent applications and providing feedback to unsuccessful applicants.

Capacity allocation mechanism between competing access seekers

In the event of competing access seekers (regardless of their type), Queensland Rail proposed giving highest priority to the access seeker that it would assess, in its absolute discretion, was the most favourable to it considering:

(a) the expected access charges

(b) the cost and risk to Queensland Rail of providing access

(c) the ability of the access seeker to satisfy prudential requirements

(d) the term of the access agreement

(e) any other effects on Queensland Rail's financial and risk position (cls. 2.7.2(a) and 2.7.2(b)).

Furthermore, Queensland Rail proposed that if each competing access seeker was equally favourable, it would grant access rights to the first application received (cl. 2.7.2(c)).

Commenting on the 2008 undertaking's time-based queuing mechanism, Queensland Rail said that it was not appropriate for its business because a queue was suitable where:

(a) a vertically integrated organisation competed with third party operators for limited capacity, which did not apply to Queensland Rail as capacity for its passenger services was allocated by legislation

(b) access seekers railed the same product type on equal commercial terms, whereas Queensland Rail provided access to a diverse mix of traffic types on different commercial terms (Queensland Rail, sub. no. 2: 37-38; sub. no. 4: 14).

Queensland Rail also said that queuing imposed unnecessary administrative costs on it and potentially delayed the negotiation process and introduced gaming by access seekers to reserve capacity at the expense of other access seekers (Queensland Rail, sub. no. 2: 38).

Feedback to unsuccessful applicants

Queensland Rail proposed providing feedback to unsuccessful applicants by giving a checklist of the factors that caused it to reject their application (cl. 2.7.2(e)).

Queensland Rail said that its proposal balanced the objectives of protecting access seekers' confidential information and providing high level information to unsuccessful access seekers (Queensland Rail, sub. no. 19: 14).

Stakeholders' comments

Criteria for allocating capacity between competing access seekers

Stakeholders said that the capacity allocation mechanism should be clear and based on objective criteria to provide certainty to competing access seekers (New Hope, sub. no. 28: 2; Aurizon, sub. no. 27: 17; Asciano, sub. no. 6: 13; Glencore, sub. no. 15: 4; QRC, sub. no. 14: 11; Peabody, sub. no. 13: 5).

Stakeholders said that Queensland Rail's proposal was unacceptable as it:

(a) was based on Queensland Rail's absolute discretion; Queensland Rail therefore was not obliged to apply the proposed criteria (New Hope, sub. no. 28: 2)

(b) could create a perception of 'favoured treatment' where two or more access seekers sought to serve the same customer (Asciano, sub. no. 6: 13)

(c) allowed Queensland Rail to consider its own broad business interests rather than being limited to its below-rail interests (Aurizon, sub. no. 27: 7, 17).

In the case of competition for mutually exclusive paths, Asciano said that queuing was a transparent and objective mechanism for allocating capacity (Asciano, sub. no. 6: 14).

While, Aurizon and Glencore did not object to removing the queuing mechanism, they said that Queensland Rail's proposed mechanism did not meet the standard of being transparent and objective (Aurizon, sub. no. 10: 9; Glencore, sub. no. 15: 3). Glencore said that an objective test was required to ensure that:

> *... the absence of the queuing framework does not result in damaging the certainty of access and consequently hindering major developments of resource projects which depend on obtaining secure access rights (Glencore, sub. no. 15: 4).*

Assessing competing applications for mutually exclusive paths

Aurizon and New Hope raised concerns with Queensland Rail's proposed factors for assessing competing applications.

Aurizon said that transport service contract payments should be considered in assessing competing applications for coal and non-coal train services (Aurizon, sub. no. 27: 17).

New Hope's comment related to coal-carrying reference train services. New Hope said that Queensland Rail's proposal included irrelevant factors – that is, access charge and cost and risk to Queensland Rail, which were more appropriately considered during the reference tariff approval process (New Hope, sub. no. 28: 2).

New Hope said that competing applications for reference train services should be assessed based on contract term, credit risk and the extent to which each applicant was ready and able to use the paths sought – that is, had the necessary production capacity, approvals and network exit capability. New Hope said that if two such applications were equivalent:

> *... the first of these parties to apply for access should be the first to be allocated capacity (New Hope, sub. no. 28: 2).*

Feedback to unsuccessful applicants

Asciano and Aurizon had differing views on Queensland Rail's proposed feedback mechanism for unsuccessful applicants.

Asciano did not support providing 'even high level information' to unsuccessful applicants. It said that the same small group of access seekers competed for multiple hauls over time and a successful access seeker would wish to withhold certain information from its competitors (Asciano, sub. no. 26: 5).

On the other hand, Aurizon said that a checklist was not sufficient and that Queensland Rail could provide detailed information without breaching the confidentiality provisions (Aurizon, sub. no. 27: 17).

QCA analysis and draft decision

An effective negotiation framework requires rules for determining how access is allocated that are well defined, measureable and therefore subject to dispute resolution.

Rail undertakings in Queensland have provided separate arrangements for allocating access rights in the case of:

(a) competition for mutually exclusive paths

(b) competitive tendering.

Competition for mutually exclusive paths

Competition for mutually exclusive paths arises where there is not sufficient available capacity to meet all access requests and requires a transparent and objective mechanism to allocate that capacity. This is the reason for putting in place a 'first in first served' queuing mechanism to reserve capacity for the access seeker first in the queue. It provides access seekers with some surety over access rights during negotiations, which could assist with an access seeker's forward planning; therefore queuing protects their interests. At the same time, the access provider is allowed to re-order the queue in defined circumstances, for example, where the commercial performance of below-rail services is better served by granting access to a traffic type not first in the queue or where an access seeker has no genuine intention of obtaining/using access rights. This protects the access provider's legitimate business interests.

Queuing mechanisms may be necessary irrespective of whether vertical integration exists

Rail undertakings in Queensland have included a queuing mechanism in circumstances where there was vertical integration and thereby sought to preserve an access seeker's position in the queue early in the application process, to avoid circumstances where the access provider chose to deal with an application from a related party in a more timely and efficient manner than one received from an external party.

Other undertakings, for example the DBCT undertaking, include a queuing mechanism even though there is no vertical integration issue. The DBCT queuing mechanism ensures there is an orderly and fair process for allocating the limited available capacity – where access seekers know what they have to do to get access and there are clear criteria the access provider needs to follow when deciding on who to grant access rights (QCA, April 2005: 25-26).

Queensland Rail's 2013 DAU

Queensland Rail removed the 2008 undertaking's queuing mechanism and proposed granting access rights to the access seeker that offered the most favourable commercial terms to it. Queensland Rail's proposal raises a number of issues, as it proposed to prioritise applications for grant of access rights:

(a) in its absolute discretion, which could result in arbitrary actions that cannot be challenged

(b) by focusing on protecting its broad business interests and not its legitimate business interests as the owner/operator of the service, which means the use of a rail transport infrastructure and not train operations (ss. 70, 72 and 138(2)(b) of QCA Act)

(c) by applying an ambiguous factor – the so-called 'any other effects' on Queensland Rail's financial and risk position

(d) by considering factors that are not universally relevant, e.g. access charge and cost and risk to Queensland Rail are considered during the reference tariff approval process for coal-carrying reference train services

(e) by being ambiguous about whether it will negotiate with only the highest priority access seeker or all access seekers.

Taking all these factors into account, the QCA considers that Queensland Rail's proposal will create significant uncertainty for access seekers of the status of their access application and will not be in their interests. That is not to say that the QCA would not consider another alternative proposal that provides a better balance of Queensland Rail's legitimate business interests as a below-rail operator and the interests of access seekers.

An alternative proposal the QCA would favourably consider is one which reinstates the 2008 undertaking's queuing mechanism for granting access rights to mutually exclusive applications where Queensland Rail can re-order a queue in defined circumstances and feedback is provided to access seekers for any change in their queue position.

Competitive tendering

In the case of competitive tendering, the access provider negotiates with each access seeker (i.e. the above-rail operator) and eventually grants access rights to the access seeker selected by the customer. A queue would not be appropriate here, otherwise it would allow an access seeker to reserve particular paths when it is competing with other access seekers to provide train services to the same end-customer under a tender process.

The existing mechanism in the 2008 undertaking promotes above-rail competition, as access seekers compete to offer the best deal to the end-customer who chooses the access seeker for its haulage task. It also protects the access seekers' interests and the access provider's legitimate business interests, as access rights are granted based on commercially negotiated terms through a well defined negotiation process.

Queensland Rail's 2013 DAU

Queensland Rail proposed choosing the access seeker for the customer based on which access seeker is commercially most favourable to Queensland Rail.

Queensland Rail's proposal suffers from the same issues as discussed in the context of competition for mutually exclusive paths.

Additionally, Queensland Rail's proposal would create perverse incentives for access seekers (above-rail operators) as they would compete to agree to terms favourable to Queensland Rail and have little incentive to offer competitive terms to the customer in the form of a better price-product-service package. Thus, Queensland Rail's proposal may frustrate above-rail competition and increase the cost of freight transport infrastructure which would hamper freight transport and mining activity in Queensland.

It is reasonable that the choice of operator be determined by the end customer, subject to the above-rail operator complying with the necessary railing requirements specified in the undertaking.

Therefore, the QCA would favourably consider an undertaking that reinstates the 2008 undertaking's provisions of Queensland Rail negotiating with each access seeker and eventually granting access right to the access seeker chosen by the end-customer. The QCA does not consider it appropriate for Queensland Rail to provide feedback to the unsuccessful applicants,

as the end-customer (not Queensland Rail) chooses the successful access seeker. This should address Asciano's concerns of its information being revealed to its competitors.

Draft decision 2.5

- **The QCA requires Queensland Rail to amend its proposal to reinstate the mechanism for allocating capacity in the cases of competition for mutually exclusive paths and competitive tendering as contained in cl. 7.4.1 and related clauses of the 2008 undertaking.**

2.7 Access renewal rights

An existing access holder may compete with a new access seeker, if it seeks to renew its existing access rights.

In that case, the 2008 undertaking gives priority to an existing access holder who is operating coal carrying train services on Queensland Rail's network provided the access holder (and its customer) satisfies a number of conditions, including that it:

(a) retains access rights for the existing mine or a replacement mine as long as the renewed access rights use substantially the same train paths

(b) executes a new access agreement or extends the term of its existing agreement for a period of 10 years or the remaining life of the existing mine (2008 undertaking, cl. 7.5.1(b))[9].

Queensland Rail's 2012 DAU retained the principle of giving priority to existing access holders but proposed it only for reference tariff services – i.e. western system coal train services. Queensland Rail proposed that it 'will not' execute an access agreement with the competing access seeker until it has concluded negotiations with the existing access holder. It proposed a number of conditions for that negotiation, including that the existing access holder match the contract period sought by the competing access seeker for up to 10 years.

In their comments on the 2012 DAU, stakeholders said that the access renewal rights should be available to the end-customer's nominee to allow for cases where the customer changed the above-rail operator (i.e. the existing access holder). Stakeholders also wanted Queensland Rail to waive the condition of matching a competing access seeker's contract period where the existing customer's remaining mine life was short. Additionally, stakeholders wanted renewal rights for non-reference tariff services (QRC, sub. no. 14: 5; Glencore, sub. no. 15: 2; Aurizon, sub. no. 10: 8).

Queensland Rail's 2013 DAU

Queensland Rail's 2013 DAU continued to propose an access renewal right only for reference tariff services – i.e. western system coal train services. Queensland Rail said that renewal rights were not relevant for non-reference tariff services because those were generally priced below ceiling and stated that:

[9] Aurizon Network's 2010 undertaking has similar provisions, albeit limited to coal train services operating in the central Queensland region. In that undertaking, an existing access holder is given priority for renewal by being placed at the head of the queue. The access holder's position in a queue is subject to re-ordering, however it cannot be re-ordered on the basis of a contract period less than 10 years, provided it represents a reasonable estimate of the remaining life of its existing mine (2010 undertaking, cls. 7.3.4(f); 7.3.4(d)(ii)).

> *... where Access Charges are below ceiling Queensland Rail should have the right to seek the best commercial outcome upon the expiry of the Access Agreement (Queensland Rail, sub. no. 5: 3).*

Nevertheless, Queensland Rail amended its 2012 DAU proposal by extending the renewal right to a customer's nominee and providing an alternative option to renew access rights for a period of the remaining mine life.

Additionally, Queensland Rail amended the provision that gave priority to existing access holders over new access seekers by proposing that it 'may not' (as opposed to 'will not' in the 2012 DAU) execute an access agreement with a competing access seeker until concluding negotiations with the existing access holder (cl. 2.7.3(c)).

Queensland Rail proposed a number of conditions for negotiating with an existing access holder, which related to the:

(a) terms at which it will renew access rights

(b) timeframes for concluding those negotiations.

Access renewal terms

Queensland Rail proposed a number of conditions.

First, Queensland Rail proposed that the existing access holder match the contract period sought by a competing access seeker (cl. 2.7.3(d)(iii)(C)(i)). In doing so, it removed the maximum 10-year period threshold in its previously submitted 2012 DAU.

Alternatively, Queensland Rail proposed that the existing access holder could renew its access rights for a period of the remaining life of its coal mine and in such cases proposed giving a 'one off' access renewal right. That is, the existing access holder would get priority over the new access seeker only once if it sought to renew its access rights for a period of its mine life. A subsequent access application by that access holder would be treated on the same basis as any other access seeker (cl. 2.7.3(d)(iv); Queensland Rail, sub. no. 19: 14).

Queensland Rail said that:

> *... a 'one off' right will protect Queensland Rail's legitimate business interests, while allowing mines to see out their mine life (Queensland Rail, sub. no. 19: 14).*

Second, Queensland Rail proposed that the existing access holder should seek to renew access rights equivalent to its existing rights, including for the same origin and destination (cl. 2.7.3(d)(iii)(B)).

Third, Queensland Rail proposed that it not be obliged to enter into a renewal access agreement on the same terms as the existing access agreement (cl. 2.7.3(e)). Queensland Rail said this provision would ensure that any renewal access agreement had the most relevant terms and conditions, as the 'new standard access agreement is likely to be in operation with new terms and conditions' (Queensland Rail, sub. no. 19: 15).

Timeframes

Queensland Rail proposed using 'reasonable endeavours' to notify the existing access holder (and the customer and its nominee) about a competing access seeker's application 'as soon as reasonably practicable after receiving it' and that:

(a) the existing access holder submit a renewal application within 20 business days of that notification and more than two years before its existing access agreement expired

(b) negotiations for renewal rights conclude within nine months of that notification (cls. 2.7.3(c) and (d)).

Queensland Rail said the two-year threshold for submitting a renewal application provided enough time so that if negotiations ceased after nine months 'Queensland Rail will have sufficient time to negotiate with the competing access seeker' (Queensland Rail, sub. no. 19: 14).

Stakeholders' comments

Stakeholders raised a number of concerns with Queensland Rail's proposal relating to access renewal terms and timeframes and wanted renewal rights for non-reference tariff services (Glencore, sub. no. 29: 5-6; New Hope, sub. no. 28: 2-3; Asciano, sub. no. 26: 6; Peabody, sub. no. 34: 2; Aurizon, sub. no. 27: 18).

Access renewal terms

First, New Hope and Glencore said that Queensland Rail's proposal of not providing renewal rights on the existing agreement's terms could enable Queensland Rail to request 'onerous terms for an extension' if there was a shortage of available capacity due to over-contracting by Queensland Rail (New Hope, sub. no. 28: 3; Glencore, sub. no. 29: 6).

New Hope said that an access holder should retain the renewal right despite any shortage of available capacity whereas Glencore said that the renewal right should be:

> *... on the terms of the existing access agreement other than price – with price to be determined by any applicable reference tariff, or agreement or, in the absence of a tariff and failing agreement, by QCA arbitration (Glencore, sub. no. 29: 6).*

Second, Asciano said that the renewal right should be available for use more than once because mining projects usually had uncertain lives due to physical and commercial factors (Asciano, sub. no. 26: 6).

Timeframes

First, Glencore said that Queensland Rail's proposal of notifying an access holder about a competing access seeker's application 'as soon as reasonably practicable' meant that the access holder could be required to apply for renewal at any time during the term of its existing access agreement (Glencore, sub. no. 29: 5).

Glencore considered that the access holder should be allowed to apply for renewal up until two years before the expiry of its access agreement, which was the timeframe the QCA approved in Aurizon Network's 2010 undertaking (Glencore, sub. no. 29: 6).

However, Asciano said that the access holder should be allowed to apply for renewal 'any time up to expiry' if a competing access request was submitted (Asciano, sub. no. 26: 6).

Second, Aurizon said that Queensland Rail's proposal gave priority only to those access holders whom Queensland Rail notified using reasonable endeavours, which did 'not provide the required level of certainty for renewing access seekers'. Aurizon suggested removing 'reasonable endeavours' so that all renewing access holders were notified (Aurizon, sub. no. 27: 18).

Third, New Hope said that Queensland Rail should notify existing access holders, regardless of whether a competing application was submitted. New Hope said that Queensland Rail's proposal meant that the access holder would lose its renewal right if no competing application was submitted more than two years before the expiry of the existing access agreement (New Hope, sub. no. 28: 3).

Non-reference tariff services

Stakeholders (Glencore, New Hope and Asciano) wanted renewal rights for non-reference tariff services. They said that the absence of renewal rights for such services meant that:

(a) other users (i.e. Glencore) that had made substantial upstream and downstream investment in facilities (e.g. mines, refineries and port facilities) would be exposed to the network owner's monopoly power during renewal access negotiation, as that investment was sunk and non-renewal was 'not a realistic option' (Glencore, sub. no. 29: 5)

(b) Queensland Rail might 'create competitive tension' between the existing access holder and the competing access seeker to drive up the access charge when, 'in reality capacity may exist to serve both hauls or could be created to serve both hauls through relatively small levels of investment' (Asciano, sub. no. 26: 6).

Glencore said:

> *If improved renewal rights are not provided for existing access holders who have invested substantial capital in long term investments dependent on long term access, it will have a chilling impact on future investment of that nature (which seems contrary to the public interest and promotion of competition in upstream and downstream markets) (Glencore, sub. no. 29: 6).*

New Hope said that Queensland Rail's proposal did not provide a renewal right for all coal-carrying train services such as Colton that operated under a negotiated access charge (New Hope, sub. no. 28: 3).

QCA analysis and draft decision

Renewal rights provide certainty to access holders and access seekers (who are in general future access holders) about retaining access rights at the expiry of their existing agreement, in the event that competing access applications are lodged for access rights.

The QCA considers that the interests of access holders/seekers in renewal rights should be appropriately balanced against the legitimate business interests of Queensland Rail.

Renewal rights for non-reference train services

Queensland Rail proposed giving renewal rights to existing access holders only for reference tariff services on the basis that the western system coal reference tariffs are near revenue ceiling limits. Queensland Rail is concerned that renewal rights for access charges which are not near ceiling revenue limits (i.e. non-reference tariff services) would adversely impact its ability to maximise revenue recovery from its network.

However, stakeholders want renewal rights for other bulk minerals train services to protect the interests of users that have made substantial investment in related facilities.

The QCA understands Queensland Rail's concerns and also sees merits in stakeholders' arguments.

The QCA considers that the absence of renewal rights exposes access holders to asset stranding risks for large sunk investments. This is particularly relevant in the Mount Isa line which is a key part of the supply chain for the north Queensland mineral industry.

Thus, if Glencore decided not to extend its economic activities in Mount Isa and Townsville, given the uncertainty about future access rights, it would have a significant impact on the communities involved. The importance of the Mount Isa line is discussed in Section 3.8 of this draft decision.

Therefore, the QCA considers that the undertaking should provide renewal rights for bulk mineral train services on the Mount Isa line. That would protect access holders from asset stranding risks for large sunk investments. Furthermore, as the Mount Isa line is underutilised, Queensland Rail will not be forgoing more profitable access agreements with other parties.

Access renewal terms

There are a number of issues in Queensland Rail's proposed conditions for access renewal terms.

First, Queensland Rail proposed giving priority to access holders if they met conditions relating to access renewal terms and timeframes. However, Queensland Rail's proposed drafting states that it 'may not' execute an access agreement with a competing access seeker, even if the access holder has met those conditions. This will create uncertainty for the access holder and should be replaced with 'will not' execute an access agreement with a competing access seeker.

Second, as a condition, Queensland Rail proposed that the access holder match the contract period offered by a competing access seeker, or alternatively use the one-off priority for a period of the remaining life of its coal mine.

The QCA considers it reasonable to reinstate the 2008 undertaking's maximum 10 years period up to which the access holder is required to match the contract period of a competing access seeker. That would create certainty for the access holder about the maximum term for which it can seek renewal rights and assist it in planning its future operations.

Alternatively, the QCA considers it reasonable for Queensland Rail to give a 'one off' renewal right to an access holder that is seeking a term to match the remaining life of its mine if it is less than 10 years.

Thus, a condition for renewal rights the QCA will be minded to approve is one where the access holder gets a first right of refusal each time it matches a competing access seeker's contract period up to 10 years and alternatively a one-off right if it chooses the contract period of the remaining life of its mine.

Third, Queensland Rail did not propose renewal rights for a replacement mine as given in the 2008 undertaking. The QCA considers that renewal rights should apply to a replacement mine which would enable mine operators to renew access rights from existing access agreements for another project as long as the access rights use substantially the same train paths.

Fourth, a number of stakeholders have raised concerns that Queensland Rail might impose onerous terms if it was not obliged to renew access rights on the terms of the existing agreement. However, Queensland Rail said its proposal would ensure that a renewal access agreement had the most relevant terms.

The QCA considers that Queensland Rail's proposal is reasonable in that a renewal access agreement should be consistent with the standard access agreement (in case of reference tariff services) and access agreement principles (in the case of non-reference tariff services). Furthermore, Chapter 9 of this draft decision proposes amendments that provide clarity and certainty to access seekers in the extension process and protect Queensland Rail's legitimate business interests.

Fifth, the QCA considers that the access charge at renewal for a reference tariff service will be governed by the QCA approved reference tariff. There are no reference tariffs on the Mount Isa line and the QCA has in Section 3.8 of this draft decision proposed a pricing rule at renewal based on the access charge of existing agreements and recovery of incremental capital expenditure, which would provide certainty to access holders and Queensland Rail.

The QCA considers that an access holder for bulk mineral train services on the Mount Isa line seeking to renew access rights should offer a price at renewal consistent with the pricing rule recommended in Section 3.8 of this draft decision. If there is not enough capacity to accommodate a new access seeker who is willing to offer a higher access price, then the QCA expects Queensland Rail to explore funding options with that access seeker to expand capacity.

Timeframes

Given that the arrangements considered above provide access holders for western system coal train services and Mount Isa bulk minerals train services with the benefit of having the option of continuing access for existing train services, it is important that they provide an early signal of their intention to renew capacity. At the same time, it is important that the renewal application should not be triggered at any time during the term of the access holder's existing agreement.

The QCA considers that Queensland Rail's proposal has no limit as to how early it can notify an access holder as its proposal uses the term 'as soon as reasonably practicable'. The QCA requires Queensland Rail to delete this term.

The QCA considers that the undertaking allow an access seeker to apply for renewing existing access rights less than three and more than two years before the expiry date of its access agreement, which is also consistent with Aurizon Network's 2010 undertaking. The QCA considers that access holders wishing to renew access rights should apply for renewal within that time period, regardless of a competing access application.

The QCA considers those timeframes would be sufficient to enable appropriate forward planning by Queensland Rail (including, in identifying whether it is possible to accommodate all access applications or requirements for expanding below-rail capacity).

Draft decision 2.6

- **The QCA requires Queensland Rail to amend its proposal for renewal of access rights so that it places access holders for western system coal train services and Mount Isa bulk mineral train services in front of a queue, provided the relevant access holder (and its customer)**
  - **(a) retains access rights for an existing mine or a replacement mine as long as the renewed access rights use substantially the same train paths**
  - **(b) matches the contract period of the competing access seeker up to 10 years or alternatively the remaining life of its existing mine if less than 10 years (in which case it gets a 'one-off' renewal right)**
  - **(c) executes an access agreement on terms that are consistent with the standard access agreement (in case of reference train services) or access agreement principles (in case of non-reference train services)**
  - **(d) in the case of Mount Isa bulk mineral train services, accepts a price consistent with the renewal pricing rule recommended in Section 3.8**
  - **(e) applies for renewal negotiations to begin no less than two years and no more than three years before the expiry of its access agreement, regardless of a competing access application.**

2.8 Other matters

This section considers a number of other negotiation related matters Queensland Rail proposed about which stakeholders raised concerns.

First, on confidentiality, Queensland Rail no longer proposed to define confidential information with reference to commercial damage if disclosed, as is in the 2008 undertaking (cl. 7.1). Aurizon said that reference to commercial impact should be included (Aurizon, sub. no. 27: 13).

The QCA considers it reasonable to include reference to commercial damage in defining confidential information, consistent with the 2008 undertaking (cl. 3.3(a)).

Second, on contracting available capacity, Queensland Rail proposed that it was not obliged to enter into an access agreement with an access seeker if there was insufficient available capacity and it had not agreed to extend the network to meet the access seeker's access requirements (cl. 2.7.4). New Hope said that this clause should not apply to renewal applications (New Hope, sub. no. 28: 3).

The QCA considers that Queensland Rail's proposal has the effect of denying access to the Act's dispute resolution process if parties cannot agree to meet the access seeker's access requirements in the face of insufficient capacity. The proposal is also inconsistent with Part 5 of the QCA Act which provides that in making an access determination the QCA may require Queensland Rail to extend the network or permit the extension of the network (s.118(1)(d)) albeit the Act places limits on that access determination (for instance, under s.119(2)(c) Queensland Rail is not required to fund the costs of extending the network[10]). The QCA considers that the 2013 DAU should obligate Queensland Rail to facilitate (but not fund) an extension of the network if there is insufficient capacity to meet an access seeker's requirements (this is considered in Chapter 9 of this draft decision). Taking all relevant matters into account, the QCA requires that Queensland Rail should delete this clause from the 2013 DAU.

Third, other matters about which stakeholders raised concerns are considered elsewhere in this draft decision – standard rail connection agreement (Section 7.3); amending interface standards (Section 4.8) and resumption, relinquishment and transfer of access rights (Section 7.2).

Draft decision 2.7

- **The QCA requires Queensland Rail to amend its proposal to:**
  - **(a) include reference to commercial damage in the definition of confidential information as contained in clause 3.3(a) of the 2008 undertaking**
  - **(b) delete clause 2.7.4 that does not oblige Queensland Rail to enter into an access agreement if there was insufficient capacity.**

[10] Unless Queensland Rail has voluntarily agreed to do so within its access undertaking (s. 119(4A)).

3 PRICING PRINCIPLES (PART 3)

Pricing principles should provide stakeholders with some certainty about how Queensland Rail will set and negotiate prices for access to its network.

The pricing principles in Part 3 of the 2013 DAU outline processes to develop access charges, including how the pricing principles will be applied, limits on price differentiation and revenue limits.

Stakeholders said Queensland Rail's proposed pricing principles give it too much discretion in setting access charges, thereby creating uncertainty.

The QCA accepts stakeholder concerns and has proposed amendments that provide Queensland Rail flexibility to price differentiate between access seekers in some circumstances, but in a manner that provides certainty to users in the negotiation process.

3.1 Background – pricing principles

It is widely accepted in economic literature that an efficient price will not cover the efficient costs of a natural monopoly. That is, pricing at marginal (or incremental) cost will result in a revenue shortfall for a monopoly business (e.g. rail network) that exhibits high fixed (or common) costs. Therein lays the reason for a market failure and the need for regulatory intervention.

Solutions to this efficiency issue involve a range of options, such as: government subsidies; price discrimination (based on a customer's ability to pay); and/or multi-part tariffs (e.g. a fixed access charge and a variable access charge based on marginal cost). But, each of these solutions can create their own distortions and detract from economic efficient outcomes.

Economic efficiency and revenue certainty can involve trade-offs. The extent of those trade-offs depends on the pricing regime and how well it is designed.

Part 5 of the QCA Act recognises these monopoly pricing issues, and indeed provides some guidance to the QCA when assessing an undertaking.

The objective of Part 5 of the QCA Act (s. 69E) emphasises the efficient provision of services with the effect of promoting competition in upstream and downstream markets. To assist in this, the criteria for approving an undertaking (s. 138(2)) require the QCA to have regard to the interests of the various parties as well as a number of pricing principles (s. 168A), namely that prices for a declared service should:

> *(a) generate expected revenue for the service that is at least enough to meet the efficient costs of providing access to the service and include a return on investment commensurate with the regulatory and commercial risks involved; and*
>
> *(b) allow for multi-part pricing and price discrimination when it aids efficiency; and*
>
> *(c) not allow a related access provider to set terms and conditions that discriminate in favour of the downstream operations of the access provider or a related body corporate of the access provider, except to the extent the cost of providing access to other operators is higher; and*
>
> *(d) provide incentives to reduce costs or otherwise improve productivity (s. 168A).*

Pricing principles are a mechanism to provide Queensland Rail's customers with confidence that prices are consistent with those objectives and criteria.

The QCA has reviewed the 2013 DAU's pricing principles in accordance with s. 138(2) and s. 168A of the QCA Act and has focused on

(a) hierarchy of pricing principles (Section 3.2)

(b) limitations on price differentiation (Section 3.3)

(c) price and revenue limits (Section 3.4)

(d) take or pay (Section 3.5)

(e) asset valuation methodology (Section 3.6)

(f) new reference tariffs (Section 3.7)

(g) Mount Isa tariff (Section 3.8).

3.2 Hierarchy of pricing principles

Queensland Rail's 2008 undertaking has a hierarchy of four pricing principles, in the following order of precedence:

(a) limits on price differentiation – requires Queensland Rail not to differentiate access charges between access seekers and/or access holders for the purpose of adversely affecting competition within a relevant market

(b) pricing limits – sets ceiling and floor price limits based on upper and lower revenue limits for individual train services and train service combinations

(c) rail infrastructure utilisation – provides for Queensland Rail to set and vary access charges when available capacity is limited

(d) revenue adequacy – provides for Queensland Rail to set prices at a level that enables an adequate rate of return on the value of assets required to provide its services.

Queensland Rail's 2013 DAU

Queensland Rail's 2013 DAU (unchanged from the 2012 DAU) has retained the four pricing principles, but removed their hierarchy of application. Queensland Rail said the nature of its new business (which has no above-rail operations), gives little scope for direct conflict between the pricing principles.

However, Queensland Rail has made the four principles subject to two overriding objectives – revenue adequacy and network utilisation (Queensland Rail, sub. no. 4: 7).

Stakeholders' comments

Aurizon was concerned that the 2013 DAU's revenue adequacy objective went beyond the statutory pricing principles of the QCA Act (cl. 3.1.1). Aurizon also said that after removing the hierarchy of pricing principles, Queensland Rail could potentially charge an access price for services that sought to reflect a return on previously installed assets that were not related to the service for which access was sought (Aurizon, sub. no. 33: 6).

QCA analysis and draft decision

The intent of the pricing principles is to provide a transparent framework for determining price limits, the structure of access charges and associated pricing matters. This framework should afford stakeholders a reasonable degree of certainty surrounding the processes for developing access charges for Queensland Rail's below-rail network.

The pricing principles should also protect the legitimate business interests of Queensland Rail, above-rail operators and end customers. For example, pricing principles that do not permit Queensland Rail to generate sufficient revenue to recover efficient costs could act as a disincentive to future investment, or promote insufficient maintenance of the network. Conversely, pricing principles which allowed Queensland Rail to realise excessive profits or distort above-rail competition would promote monopolistic behaviour and suppress competition.

In this context, a hierarchy of pricing principles in the order outlined in the undertaking provides certainty to access seekers and access holders about which principle will prevail in the event of a conflict.

Replacing the hierarchy with an overriding objective of revenue adequacy provides Queensland Rail with excessive discretion in setting prices. It may enable Queensland Rail to achieve revenue adequacy without observing the constraints on price differentiation (i.e. by unfairly discriminating between access seekers to maximise revenues).

Indeed, the QCA has previously said that:

> *... limits on price differentiation within a market take precedence over revenue adequacy as a pricing principle. That is, price differentiation within a market cannot be justified on the basis of achieving revenue adequacy (QCA Draft Decision 2005: 138).*

The QCA also considers that the price limits should take precedence over revenue adequacy. This is to preclude Queensland Rail from charging more than the stand-alone cost of a service in order to achieve revenue adequacy. This will go towards addressing Aurizon's concern that Queensland Rail's proposal would enable it to charge an access price to recover costs that are not related to providing a service. The separate issue of the extent to which access seekers and holders should pay for sunk costs (e.g. pre-1995 assets for the western system) is discussed in Chapter 8.

Given these considerations, the QCA's draft position is to reinstate the hierarchy of pricing principles contained in the 2008 undertaking.

Draft decision 3.1

- **The QCA requires Queensland Rail to amend its proposal to reinstate the hierarchy of pricing principles for developing access charges as contained in cl. 6.1 of the 2008 undertaking.**

3.3 Limits on price differentiation

The 2008 undertaking requires that the access charge provided to an access seeker for a train service only vary from the access charge for other access seekers seeking the same train service (i.e. in the same market) to reflect:

(a) costs or risks to Queensland Rail of providing access for train services of that type

(b) changes in the Transport Service Contract (TSC) payments

(c) changes in market circumstances.

Moreover, the 2008 undertaking prohibits Queensland Rail from setting access charges for the purpose of preventing or hindering access by third party access seekers into any market in competition with Queensland Rail (cl. 6.1.2).

Queensland Rail's 2013 DAU

The 2013 DAU (unchanged from the 2012 DAU), proposes to relax the limits on Queensland Rail's ability to vary access charges between access seekers, namely:

(a) to give Queensland Rail additional scope to distinguish between train services – i.e. Queensland Rail will be able to distinguish between train services, based not just on the market in which it operates (e.g. on an origin to destination or commodity specific basis), but also on the characteristics of the train services (e.g. the duration and quality of the train path, the nature of the rolling stock and the duration and terms of the access agreement)

(b) to change the trigger for price differentiation from changes to TSC payments to a new trigger of its ability to 'commercially provide access'.

Queensland Rail has also proposed removing the prohibition on setting access charges for the purpose of preventing or hindering access by third-party access seekers. Queensland Rail said that, given it no longer operated above-rail freight services, there was no scope for the business to use price differentiation to prevent or hinder access to benefit its own operations.

Stakeholders' comments

Aurizon said the changes included in the 2013 DAU created uncertainty about when Queensland Rail may price differentiate. Aurizon noted that whereas the trigger for price differentiation in the 2013 DAU was Queensland Rail's ability to commercially provide access, in the 2008 undertaking such trigger was a change in the TSC Payment (Aurizon, sub. no. 9: 21).

QCA analysis and draft decision

A natural monopoly needs the ability to price discriminate (or implement multi-part tariffs) to recover its efficient costs. This price discrimination needs to be based on an underlying rationale of improving network utilisation and revenue recovery opportunities for it to have positive efficiency implications.

Price differentiation is not something that can either be random or at the absolute discretion of the facility owner. This could have adverse impacts on competition in other markets or on economic efficiency more generally. It could also create uncertainty which could have adverse impacts on access seekers and the public interest, in particular if this uncertainty adversely affected investment and employment opportunities in Queensland.

For these reasons the 2008 undertaking (and those before it) limited price discrimination within markets where the distortions, and adverse impacts on competition, from price discrimination are likely to be largest. Such discrimination is allowed provided it can be demonstrated to be based on the higher/lower costs or risk of an alternative service. That is, price discrimination in a market must be based on the demonstrable characteristics of a particular train service.

These limitations were particularly important, as the then QR Network was vertically integrated and may have had an incentive to adversely affect competition. While Queensland Rail is not vertically integrated with an above-rail freight operation, it is not to say that won't change over the life of this undertaking. Moreover, it does operate passenger services.

The ability to discriminate outside a particular market is more open-ended, but is subject to the negotiate/arbitrate model of part 5 of the QCA Act.

The June 2013 DAU seeks to provide Queensland Rail with more open-ended discretions than are allowed for in the 2008 undertaking.

Price discrimination for trains with similar characteristics

Queensland Rail has proposed that its ability to price discriminate be limited to costs or risks where trains services have similar characteristics. There are fewer limitations on price discrimination where train services are dissimilar.

Queensland Rail has included a broad and open-ended series of matters it can have regard to in determining whether a train service has similar characteristics.

Some of those matters relate to the dimensions of the market within which the train service operates (e.g. the commodity being transported, the geographical area and the arrival and departure times of the day). These matters are not exceptional.

Train service characteristics also includes other matters and these include, and are not limited to, the terms and duration of an access agreement, the nature of the rolling stock and the duration and quality of the train path. However, Queensland Rail's proposal goes beyond this and potentially provides it with scope to distinguish between access seekers on the basis of whatever train characteristic it chooses. Indeed, it is possible, albeit improbable, it could include the colour of the train.

The result is that there are now a much broader range of matters that can be taken into account when determining whether two trains are similar. For example, two trains could be operating in the same market and have a similar train service description (e.g. axle load, length and speed), but they could be dissimilar because one is a red train and the other is a blue train. The 2013 DAU would allow Queensland Rail to determine that they are trains with dissimilar characteristics and that they can price differentiate in a way unfettered by the cost or risk constraint.

Queensland Rail's proposal makes the cost or risk constraint potentially redundant as there is scope for Queensland Rail to deem that almost any two train services within a market have different characteristics and therefore are different, allowing price differentiation on almost any basis.

Queensland Rail's proposal intermingles:

(a) some of the matters to be taken into account when determining whether two train services operate within the same market, with

(b) those matters that affect costs and risks and therefore determine the limits on price discrimination.

Therefore, the QCA does not object to the range of matters included in Queensland Rail's proposal. Rather, it objects to the way the test has been constructed.

The QCA considers that price differentiation on this basis could have adverse competition and efficiency impacts. It could also create uncertainty which could have adverse impacts on access seekers and the public interest, in particular if this uncertainty adversely affected investment and employment opportunities in Queensland.

The QCA does not object to Queensland Rail distinguishing between access seekers within a market on the basis of cost or risk. What constitutes the same market is a concept that has been well tested in competition law, in particular with reference to assessments of mergers. The key factor relates to the substitutability of the good or service. Markets can also have geographical or time dimensions. These are all matters identified in Queensland Rail's proposal.

Moreover, the 2008 undertaking provides for price discrimination based on costs and risks, but it does that in a way that places measurable limits on the extent of price discrimination within a market.

Given this, the QCA rejects Queensland Rail's amendments and requires that the relevant provisions of the previous drafting be reinstated.

'Commercially provide access'

The 2013 DAU also provides that the trigger for price differentiation is Queensland Rail's ability to 'commercially provide access'. In contrast, the 2008 undertaking provides a narrower trigger for price differentiation that is a change in the TSC Payment (Aurizon, sub. no. 9: 21).

It is reasonable for Queensland Rail to recover at least its incremental costs, and any TSC payment contributes to this. As such, it is not unreasonable for Queensland Rail to increase prices where there is a reduction in the relevant TSC payment.

However, Queensland Rail's proposal goes beyond this and provides it with very broad discretion as to when it may engage in price discrimination. Indeed, the absence of a definition of 'commercially provide access' leaves it open for Queensland Rail to potentially discriminate between access seekers on any matter of commercial relevance to Queensland Rail. This could include an access holder's or customer's ability to pay (i.e. charging more profitable access holders within a market more).

On this basis, the QCA does not accept Queensland Rail's amendments to allow it to discriminate based on its ability to commercially provide access and requires that the relevant provisions of the undertaking be reinstated.

'Preventing or hindering access'

Queensland Rail separately wants to remove the prohibition in the undertaking on setting access charges for the purpose of preventing or hindering access by third-party access seekers.

The QCA accepts that while Queensland Rail is vertically integrated, its above rail operations relate to passenger services for which there are no competitors. However, that is not to say that at some point in the future Queensland Rail may undertake above-rail operations in competition with another provider.

The QCA notes that s. 104 of the QCA Act precludes Queensland Rail preventing or hindering access. Therefore, Queensland Rail cannot engage in conduct that prevents or hinders access by a third party irrespective of whether any approved undertaking contains this requirement.

As such, the QCA does not consider that there will be any material change to Queensland Rail's obligations from the inclusion or exclusion of this provision from the undertaking.

Given this, the QCA proposes to accept Queensland Rail’s position to omit the preventing or hindering requirement in the 2013 DAU.

Draft decision 3.2

- **The QCA requires Queensland Rail to amend its proposal so that the pricing principles in the undertaking for developing access charges specify that Queensland Rail can only seek to differentiate access charges between access seekers/holders**
  - **(a) where a reference tariff is applicable, to reflect differences in cost or risk to Queensland Rail of providing access for the train service compared to the reference train service**
  - **(b) where there is no reference tariff applicable for the relevant train service type, subject to requirements reinstated from cl. 6.1.1(c) of the 2008 undertaking**

3.4 Pricing and revenue limits

Pricing and revenue limits are established to assure access seekers/holders and their customers that prices (and/or revenues) will fall within a certain range. In particular, tariffs are largely cost reflective and one customer (or group of customers) should not subsidise another customer (or group of customers). These limits are that one customer (or group of customers):

(a) at least pays for the services that only they use (i.e. not below incremental costs)

(b) does not pay for the services they do not use (i.e. not above stand-alone costs).

Such pricing limits result not only in equitable prices (i.e. the 'user pays' principle) but can have important dynamic efficiency impacts (i.e. by ensuring that a customer does not demand services that it then asks someone else to pay for).

The 2008 undertaking enables the setting of floor and ceiling prices and revenues. The floor price ensures that access charges do not fall below the incremental costs of providing access, while the ceiling price reflects the expected stand-alone cost of providing access to an individual/combination of train service(s).

The 2008 undertaking also provides for the floor and ceiling prices to have regard to TSC payments provided by the government.

Queensland Rail's 2013 DAU

Queensland Rail's 2013 DAU (unchanged from the 2012 DAU) is similar to the 2008 undertaking to the extent that it retains floor and ceiling pricing and revenue limits.

However, it now provides for Queensland Rail to determine, at its absolute discretion, the methodology, rates and other inputs that it will use to calculate access charges where:

(a) access charges are supplemented by TSC payments

(b) there is a reduction in TSC payments

(c) an offsetting increase in the access price is necessary to ensure that Queensland Rail's revenues do not fall below the floor revenue limit.

In other words, Queensland Rail proposes to have the discretion to change the access charges if there is a change in TSC payments; that is, where Queensland Rail would otherwise receive less than the floor revenue limit.

Stakeholders' comments

Stakeholders did not comment on the principle to apply floor and ceiling price and revenue limits for access price negotiations, other than in specific reference to the western system and the Mount Isa line – these matters are discussed in Section 3.8 and Chapter 8 below.

QCA analysis and draft decision

It is reasonable for Queensland Rail to earn sufficient revenue to cover its incremental costs (i.e. its floor price and lower revenue limit).

In some cases, Queensland Rail may set access charges at a level below the floor price as it gets additional TSC funding from the government that supplements the revenue from the access holder.

In these circumstances, where TSC funding is reduced, Queensland Rail's proposal that it be able to increase the access charge to offset the reduction in TSC payments is reasonable. In this regard, the QCA notes Queensland Rail has proposed that the increase only be to the level necessary to recover its incremental costs – i.e. to reach the floor price.

However, the QCA does not consider that this discretion can be absolute, but rather requires that it be exercised reasonably.

Draft decision 3.3

- **The QCA requires Queensland Rail to amend its proposal so that it is required to act reasonably when seeking to increase an access charge to offset a reduction in a transport service contract (TSC) payment.**

3.5 Take or pay

Take or pay provisions require an access holder to pay for some or all of the services for which it has contracted, regardless of whether it uses them.

Take or pay is included in access arrangements to achieve a number of outcomes, including supporting revenue certainty for the access provider and encouraging customers to contract for the capacity they are most likely to need.

The 2008 undertaking only addresses take or pay for the western system for Queensland Rail (Schedule F, Part C, cl. 5). The undertaking entitles Queensland Rail to collect take or pay revenue of 80% of the amount it would have received if all contracted services had run, less any services that did not run for a Queensland Rail cause.

The 2008 undertaking also provides for approximately 90% take or pay for central Queensland[11], in a section that does not apply to Queensland Rail (Schedule F, Part B, cl. 2.2). This same 100% take or pay for central Queensland is included in Aurizon Network's 2010 undertaking.

Queensland Rail's 2013 DAU provides for 80% take or pay for the western system, consistent with that in the 2008 undertaking. It does not address take or pay for any other part of Queensland Rail's network.

[11] In central Queensland take or pay is equivalent to 100% of AT2-AT4 tariffs. AT1 is excluded as it relates to incremental network maintenance costs which varies with volume.

Stakeholders' comments

Aurizon said the western system take or pay regime was biased in favour of Queensland Rail, and created the potential for windfall gains, unless there was a cap on total take or pay recovery. This was because Queensland Rail could collect take or pay payments from an access holder that under-railed, while at the same time collect tariff payments from other access holders or customers for providing paths above their contract entitlements. Aurizon said,

> *... these gains amount to a penalty and are not necessary to offset or mitigate any genuine economic loss (Aurizon, sub. no. 48: 22).*

Aurizon proposed take or pay revenue should be capped so that revenue in excess of target revenue under a price cap should not be comprised of take or pay revenue. This would require that the undertaking include an annual target revenue that was adjusted each year by CPI (Aurizon, sub. no. 33: 14; sub. no. 48: 16-23).

Glencore said 100% take or pay 'blunts' the economic incentives to meet contracted volumes and perform necessary maintenance. It said take or pay, at least for the Mount Isa line, should be limited to 80%, the same as the western system (Glencore, sub. no. 30: 7-8).

QCA analysis and draft decision

The purposes of take or pay include encouraging customers to contract for the capacity they are most likely to need, and giving access holders an incentive to relinquish or transfer capacity they do not need.

However, for Queensland Rail's network, where all systems used by freight services operate with spare capacity, the primary purpose is to provide a degree of revenue certainty for Queensland Rail.

Aurizon has argued that the take or pay on the western system more than achieves this objective, and should therefore be capped to ensure that Queensland Rail does not receive take or pay income when that take or pay increases its recovery to more than the annual revenue used to develop the reference tariff (Aurizon, sub. no. 48: 23).

The QCA considers that Queensland Rail's proposal to retain 80% take or pay for the western system is reasonable, as it helps ensure revenue adequacy for Queensland Rail, while also leaving some incentive for Queensland Rail to perform.

However, the QCA considers that the take or pay regime should be about protecting revenues, not increasing them. It therefore accepts Aurizon's proposal that Queensland Rail should be able to use take or pay to lift its annual revenue to 100% of the target revenue used in developing its western system reference tariffs. But Queensland Rail should only be able to recover more than 100% of that target revenue by outperforming – delivering more than the total paths or tonnes that it has contracted to provide.

The QCA considers this is a reasonable limit that is in Queensland Rail's legitimate business interests, while at the same time being in the interests of access seekers and access holders, consistent with the QCA Act (ss. 138(2)(b), (e) and (h). It should also promote the efficient use of capacity (s. 138(2)(a)).

For this limit to apply, the annual target revenue will need to be published with the western system reference tariff in schedule A. This is discussed in Chapter 8.

For non-reference tariffs, including those on the Mount Isa line, the QCA acknowledges Glencore's point that 100% take or pay removes Queensland Rail's exposure to volume risks, and therefore blunts its incentives to enable higher volumes.

However, the QCA does not consider this concern is sufficient reason to constrain commercial negotiations between Queensland Rail and access seekers. In particular, the term and terms of a take or pay agreement are part of the package of risks, costs and entitlements the facility owner and access seeker will assess as they negotiate an agreement. The situation is different on the western system and in central Queensland, where the approved take or pay regimes have been applied in the context of reference tariffs, with known risks and rewards.

The QCA notes that, should an access seeker consider that a take or pay requirement proposed by Queensland Rail breaches the pricing principles, including the pricing limits, the matter can be brought to the QCA for arbitration.

Draft decision 3.4

- **The QCA requires Queensland Rail to amend its proposal so that**
  - **(a) it can only require take or pay on the western system up to the amount required to lift its annual revenue to 100% of the target revenue used in developing the western system reference tariffs**
  - **(b) the annual target revenue relating to this take or pay limit is published with the western system reference tariff in schedule A.**

3.6 Asset valuation methodology

The QCA Act specifies that the price of access to a service should 'include a return on investment commensurate with the regulatory and commercial risks involved' (s.168A(a)). It does not prescribe any particular way of establishing the amount of investment on which that return should be calculated.

The QCA has used a building blocks approach for assessing rail reference tariffs in central Queensland. In doing so, it has established the investment amount by estimating the value of the assets used to provide the below-rail service.

The 2008 undertaking specifies that the asset value will be determined

(a) 'in accordance with schedule FB' (i.e. through a roll-forward of the asset base from year to year, taking into account inflation, depreciation and capital expenditure), or

(b) where there is no relevant asset value, using 'the Depreciated Optimised Replacement Cost (DORC) methodology' (cl. 6.2.4(c)).

Queensland Rail's 2013 DAU specifies that the value of assets will be determined using a DORC methodology for each regulatory period (cls. 3.2.3(a) and (c)). Additionally, Queensland Rail proposed to include additional sections into the western system asset base at DORC value (Schedule AA, cl. 1.2(a)(ii)).

Queensland Rail's proposed pricing principles do not provide for rolling forward of the asset base, as in the 2008 undertaking.

Stakeholders said the QCA Act did not prescribe a DORC valuation and neither should Queensland Rail's undertaking. Glencore said

> *... it seems highly inappropriate for the QCA to bind itself to applying a DORC valuation methodology in future pricing arbitrations where it is completely unclear whether that will be appropriate for the part of the network to which a future dispute relates and what the consequences for access charges payable by access seekers would actually be (Glencore, sub. no. 30: 6).*

New Hope said

> *... DORC is not an appropriate methodology when considering an 'outlier' corridor such as the western system which has limited scale economies, standards far from modern engineering equivalents, and significant above rail cost impositions due to those standards restricting both train length and axle load (New Hope, sub. no. 50: 19).*

The QCA notes that Queensland Rail operates a widespread rail network, with tracks in a variety of states of repair and utilisation, used by a diverse mixture of traffic types. DORC valuation remains one way of looking at valuation of those assets. However, for the QCA to perform its function, consistent with the QCA Act, it needs the flexibility to choose the appropriate way to value assets in each case.

For instance, while the QCA has adopted a DORC methodology as the basis for setting tariffs on the western system (see Chapter 8), it is yet to consider what asset valuation methodology should be adopted for the Mount Isa line (see Section 3.8).

The QCA also notes that Queensland Rail's drafting in its 2013 DAU appears to require that a new DORC valuation be used at the 'commencement of the Evaluation Period' (i.e. the start of the period over which an undertaking applies) (cl. 3.2.3(a) – definition of 'AV0') and for including additional sections into the western system asset base (Schedule AA, cl. 1.2(a)(ii)). This would create uncertainty for access seekers and holders and Queensland Rail about the treatment of assets in subsequent regulatory periods.

The QCA therefore requires that Queensland Rail delete those clauses requiring that the DORC methodology be used to set asset values for determining a ceiling revenue limit.

Draft decision 3.5

- **The QCA requires Queensland Rail to amend its proposal to remove the requirement that the asset value for determining a ceiling revenue limit be set through a depreciated optimised replacement cost methodology, by deleting cl. 3.2.3(c) and cl. 1.2(a)(ii) in Schedule AA.**

3.7 New reference tariffs

Queensland Rail's 2008 undertaking includes a reference tariff for the western system and provides for the QCA to require Queensland Rail to submit a new

> *... Reference Tariff for a new Reference Train Service if the QCA has a reasonable expectation that there is sufficient interest from Access Seekers to warrant the development of a Reference Tariff for a new Reference Train Service (cl. 6.4.2(c)).*

The 2013 DAU (like the 2012 DAU) does not include any provision for the QCA to require Queensland Rail to submit a new reference tariff for a reference train service. Queensland Rail said this lack of prescription was to 'reduce the overall complexity of the document' and that:

> *... if during the term of an access undertaking Queensland Rail determines that a new reference tariff is required for a particular service or group of access seekers, it would be possible for the business to submit a draft amending access undertaking to seek QCA's approval of the proposed new reference tariff (Queensland Rail, sub. no. 2, PwC report on Pricing Principles: 15).*

Stakeholders said Queensland Rail's undertaking needed to have a mechanism for reference tariffs to be put in place outside the western system, or include other reference tariffs from the outset. Glencore said the ability for an access holder or seeker to require that a reference tariff be developed was 'an important protection that should be available' (Glencore, sub. no. 15: 7). Asciano called for reference tariffs for services such as intermodal haulage and minerals haulage

(Asciano, sub. no. 6: 6; sub. no. 26: 11). However Aurizon said that providing a western system tariff, but no other reference tariffs, was reasonable as 'other traffics are unlikely to be near the revenue ceiling' (Aurizon, sub. no. 9: 21).

QCA analysis and draft decision

Reference tariffs can reduce the transaction costs associated with negotiating an access price, and help address the information asymmetry between an access seeker or holder and a monopoly access provider. However, developing a reference tariff is a time- and resource-consuming exercise that should only take place when there is a benefit that exceeds the costs.

The QCA is not minded to require that Queensland Rail develop reference tariffs other than for the western system in the 2013 DAU. At the same time, the QCA does not consider it sufficient that Queensland Rail, as a monopoly service provider, has the sole option to determine the circumstances and time when it might propose a reference tariff.

The QCA considers it would be more balanced if both Queensland Rail and its customers had the ability to trigger a reference tariff process. This has been addressed in the 2008 undertaking by giving the QCA the ability to require Queensland Rail to develop a reference tariff if warranted (cl. 6.4.2(c)).

Queensland Rail has said that removing this provision from the 2013 DAU will 'reduce complexity'. However the QCA agrees with Glencore that in reducing complexity, Queensland Rail has taken away an important protection for access seekers and holders. The QCA therefore requires that Queensland Rail reinstate the ability for the QCA to require Queensland Rail to develop a new reference tariff.

Draft decision 3.6

- **The QCA requires Queensland Rail to amend its proposal so that the QCA can require it to submit a proposed reference tariff if the QCA considers it is warranted.**

3.8 Mount Isa tariff

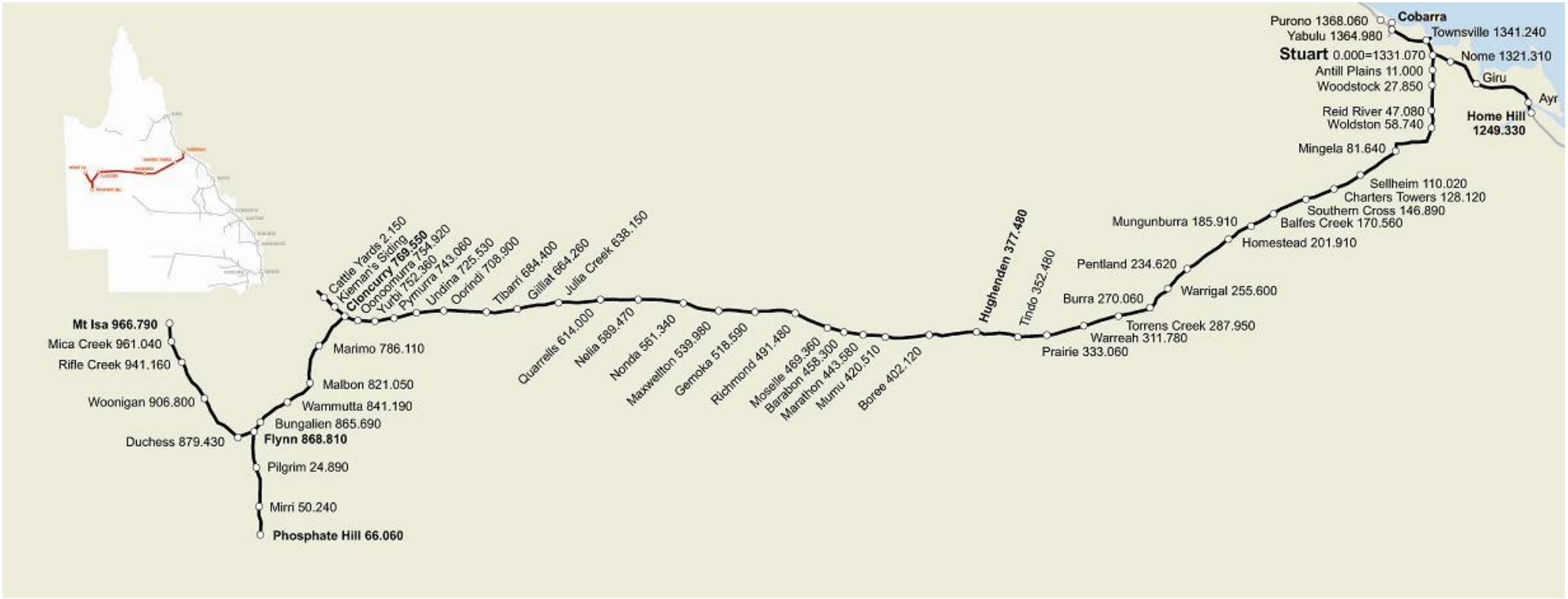
The Mount Isa line includes 1,032 kilometres of track and was constructed in the early 20th century, first for the wool and livestock trade and then to serve the silver and lead mines (see **Figure 5**). The line has been upgraded several times since and now supports kilometre-long trains with 20-tonne axle loads at maximum speeds between 60 and 80 km/h.[12] Each year it carries around five million tonnes of freight (e.g. copper and zinc concentrates, fertiliser, acid, fuel, cattle and general freight containers), plus the twice-weekly Inlander passenger service.[13]

Negotiations for access to the Mount Isa line have been covered by a succession of approved undertakings since 2001. Prices and other terms of access have been agreed by negotiation between the below-rail operator and its customers. Unlike for coal train services in central Queensland and on the western system, there has never been an approved reference tariff for traffics on this line.

[12] http://www.queenslandrail.com.au/NetworkServices/Documents/Mt%20Isa%20System%20Information%20Pack%20-%20Issue%202.1%20-%20May%202007.pdf

[13] For comparison, Aurizon Network's central Queensland coal network includes 2,670 kilometres of track and carried 211 million tonnes of coal in the year to June 2014.

Figure 5 Mount Isa line map



Source: Queensland Rail

Queensland Rail's 2013 DAU (like the 2012 DAU and all other approved undertakings before now) did not include any specific provisions to cover pricing or other aspects of access to the Mount Isa line.

Stakeholders' comments

Stakeholders have raised several concerns relating to tariffs and access to the Mount Isa line as part of their submissions on the 2012 and 2013 DAUs.

Glencore said changes to Queensland Rail's approach to pricing and transparency in access negotiations were 'critically required to make the negotiate-arbitrate model more effective at preventing QR's abuse of its monopoly power' (Glencore, sub. no. 30: 4).

Glencore said that during negotiations on the Mount Isa tariff, Queensland Rail had provided 'little discernible methodology' for calculating proposed access charges and was unable to demonstrate the costs of providing the service on a stand-alone and incremental basis. Glencore said it was concerned that it would:

> *... receive little more than a price with assertions that it is based on a 'market price' (which is fairly nonsensical in the context of a monopoly service provider who itself sets the market) or is 'below the ceiling price' (Glencore, sub. no. 30: 5).*

Asciano said Queensland Rail should provide floor and ceiling prices to address this information asymmetry, while Aurizon and Glencore said that, if Queensland Rail provided additional information, the negotiating parties were likely to arrive at an efficient price without approved floor and ceiling prices (Asciano, sub. no. 31: 12; Aurizon, sub. no. 33: 6; Glencore, sub. no.30: 4).

Glencore said that Queensland Rail needed to be required to provide that additional information, as it was:

> *... inappropriate for a regulator to simply be relying on the goodwill of a regulated entity on an issue which, if not fixed, completely undermines the validity of the proposed approach to regulating QR's pricing' (Glencore, sub. no. 30: 6).*

Glencore also said take or pay, at least for the Mount Isa line, should be limited to 80%, the same as the western system. (Glencore, sub. no. 30: 7-8).

In addition, Glencore was concerned that the 2013 DAU did not provide a right of renewal when an access agreement expired, and that Queensland Rail might seek 'onerous terms' at renewal for access holders on the Mount Isa line and other parts of the network. Glencore said Queensland Rail had an incentive to 'seek a bidding war between an existing access holder and a new applicant' (Glencore, sub. no. 29: 6-7). It said:

> *If improved renewal rights are not provided for existing access holders who have invested substantial capital in long term investments dependent on long term access, it will have a chilling impact on future investment of that nature (which seems contrary to the public interest and promotion of competition in upstream and downstream markets) (Glencore, sub. no. 29: 6).*

Many of the concerns raised in relation to the Mount Isa line also apply to other parts of the network. These matters are addressed in other sections of this draft decision, including:

(a) proposed pricing principles in Sections 3.2 to 3.4

(b) information provision and reporting in Chapters 2 and 5

(c) the process for renewing and negotiating access agreements in Chapter 2

(d) take or pay in Section 3.5.

This section (Section 3.8) therefore considers price-setting issues specific to the Mount Isa line, particularly when access agreements are renewed.

QCA analysis and draft decision

Earning a reasonable return on its investments is in the legitimate business interests of Queensland Rail.

Equally, the Mount Isa line is a key part of the supply chain for the north Queensland mineral industry. Therefore it is in the public interest to ensure that the access and pricing approach supports the long-term growth of mining and other industries and communities served by the rail infrastructure.

The commercial issues confronting the Mount Isa line are not dissimilar to those of the western system; that is, both lines require a large amount of infrastructure to carry a relatively small amount of traffic. For instance, the central Queensland coal network has 2.5 times the track kilometres of the Mount Isa line but carries 40 times the volume. Indeed, the Mount Isa line is three times as long as the western system, yet carries about two-thirds of the volume.

Stakeholders have said that the information provided by Queensland Rail during access negotiations is not sufficient for customers to form a view on the level of the ceiling price. Queensland Rail has also not provided information as part of the public consultation process on the 2013 DAU to inform the QCA or stakeholders on what that ceiling price might be or under what circumstances it might be charged.

This creates a great deal of uncertainty for the users of the Mount Isa line at a time when decisions are being contemplated about future mineral processing options that may call for new investment, including user-funded upgrades to the rail infrastructure. This lack of information is not conducive to the efficient development of economic activities that rely on the Mount Isa line or to the future development of the line itself.

The negotiate-arbitrate approach to access pricing is likely to be most effective when the positions of the access provider and access seeker are evenly balanced (e.g. when a customer is contemplating a greenfields project). On one hand, Queensland Rail wants to find customers for its capacity, while on the other hand a customer is unlikely to sink its investment unless it can develop an economically viable business case, that includes certainty on recovering its investment and costs over a given time period.

This balance of negotiating positions is less likely to be the case when a contract is to be renewed. At that time, both the access provider and customer have investments that are sunk, and economic rents could be extracted from the party in the less favourable position. In the short term, this could be viewed as a transfer of resources with little impact on economic efficiency. However, in the longer term, an expectation of a future transfer of resources will impact on anticipated returns and therefore on investment decisions, and that will have an impact on economic efficiency[14].

In the case of declared infrastructure, it can be anticipated that the access provider is likely to be in the more favourable negotiating position – although this is less clear cut on the Mount Isa line where Glencore is the dominant user and has, as a result, significant countervailing market power.

[14] For a discussion of fairness in pricing where access holders have sunk costs, see QCA, August 2013: 27-29.

But there is a risk. If Glencore decided that it did not want to extend its economic activities in Mount Isa and Townsville, given the uncertainty on future rail access charges, then it would have a significant impact on the communities involved. The QCA does not consider that Queensland Rail's 2013 DAU adequately addresses stakeholders' concerns about future pricing uncertainty on the Mount Isa line. This uncertainty is not in the public interest, in particular the future economic prosperity of the communities that rely on and service that line.

To address these concerns, the QCA does not consider it is necessary to publish floor and ceiling prices (or even a reference tariff), as long as Queensland Rail provides more comprehensive information as set out in Chapters 2 and 5 of this draft decision. The remainder of this analysis therefore considers the issue of pricing on the Mount Isa line when contracts are renewed.

Contract renewal pricing mechanism

While price certainty at renewal is a desirable objective, it is hard to achieve in practice, particularly on an old, long, low-volume network like the Mount Isa line.

The QCA notes that the QCA Act requires it to have regard to both the interests of the facility owner, including the need for a return on investment (s. 138(2)(b) and s. 168A(a)) and the interests of access seekers and access holders, (ss. 138(e) and (h)). In particular, Queensland Rail should recover at least its incremental costs of providing below-rail services to Mount Isa customers, but should not recover more than the stand-alone cost of providing those services (the ceiling price) (see Section 3.4).

With this in mind, the QCA has sought to provide Queensland Rail with some ability to increase the recovery of its assets over time, while providing protection to access holders when they renew their contracts through a price path at renewal.

The QCA considers that, for the Mount Isa line, the price at renewal should be limited to no more than:

(a) the tariff agreed between Queensland Rail and its access holder in its expiring access agreement, increased by annual inflation plus 2 percentage points, applied over the period of the previous contract, plus

(b) the normal regulatory return on incremental capital expenditure incurred to increase capacity on the network, including

  (i) spending on infrastructure specifically built for the access holder's service

  (ii) a reasonable allocation of incremental spending for all services.

The maximum renewal price would start on the approval date of this undertaking. This will give an incentive for Queensland Rail and users to invest in additional capacity.

The QCA notes that this approach of capping annual price increases is not novel and has been applied for water and electricity prices paid by irrigators. In each case, the QCA has developed a mechanism to limit annual price shocks while increasing regulated tariffs over time to achieve greater cost recovery.[15]

[15] See http://www.qca.org.au/Water/Rural/Irrigation-Pricing-Review/Irrigation-Prices-2013-17/Final-Report/Irrigation-Prices-for-2013-17#finalpos and http://www.qca.org.au/getattachment/79e1794c-0e3c-454d-bdfa-f363cfc82dab/Transitional-arrangements-for-electricity-prices-f.aspx

This approach is also similar to, and consistent with, the approach the QCA is proposing for the western system coal services to pay for incremental capital investment on the metropolitan system (see Chapter 8).

This Mount Isa price-capping approach provides all parties with some certainty. Customers know that Queensland Rail will not be able to levy access charges in its absolute discretion and thereby strand their future investments. At the same time, it is in Queensland Rail's legitimate business interest as it provides potential for future, but not open-ended, price increases.

Further, it is unlikely that there will be an opportunity cost from applying the 'inflation plus 2%' limit, as the Mount Isa line is underutilised, so Queensland Rail will not be forgoing more profitable access agreements with other parties.

This approach to pricing certainty will also determine the price that an access holder will need to match at renewal, to exercise its right to continue access in the face of a competing application. This is explained in detail in Section 2.7.

Price differentiation

While the inflation plus 2% principle will provide Mount Isa access holders with some comfort they will not face onerous price increases, they will also have the protection of the price differentiation rules (see Section 3.3).

The differentiation rules prevent Queensland Rail from charging different prices for customers competing in the same end market, except for reasons of cost or risk.

This means that, whatever price is indicated by the 'inflation plus 2%' calculation, Queensland Rail will be able to charge no more than it has agreed to charge another access seeker hauling the same product.

The QCA notes that there could be some issues with applying these price differentiation rules for contracts whose terms overlap, but end at different times. For example, the differentiation rules could have the effect of preventing Queensland Rail from raising its prices for an access holder at renewal, if it has subsequently agreed to an access agreement at a price below 'inflation plus 2%' for another customer in the same market. However, Queensland Rail can address this by including a mechanism to reopen the pricing for the second access holder at the time the first access holder's contract comes up for renewal.

Draft decision 3.7

- **The QCA requires Queensland Rail to amend its proposal so that the price for a renewing access holder on the Mount Isa line is limited to no more than:**
  - **(a) the tariff agreed between Queensland Rail and its access holder in the expiring access agreement, increased annually by CPI plus 2 percentage points per year of the expiring agreement, plus**
  - **(b) the normal regulatory return (consistent with cl. 3.2.3) on incremental capital expenditure incurred to increase capacity on the network, including**
    - **(i) spending on infrastructure specifically built for the access holder's service**
    - **(ii) a reasonable allocation of incremental spending for all services**

  with the accumulation of the maximum renewal price for an existing access contract starting on the approval date of this undertaking.

4 NETWORK MANAGEMENT PRINCIPLES AND OPERATING REQUIREMENTS MANUAL (PART 4)

The network management principles (NMPs) should provide a consistent and equitable mechanism for Queensland Rail to demonstrate capacity, coordinate maintenance and schedule and operate trains.

The QCA proposes to accept much of Queensland Rail's proposed NMPs, as they are consistent with the interests of access seekers and holders, and Queensland Rail. However, the QCA has proposed amendments to provide for more transparency and to require Queensland Rail to consult more frequently when changing its scheduling documents. The QCA has also sought to ensure that all train services are subject to the same scheduling and operating rules and limit Queensland Rail's discretion to act to favour its own passenger services.

Queensland Rail also proposed bringing the operational requirements together in one document to be published online, separate from the undertaking. However, in doing so, Queensland Rail has significantly shifted the risk profile of obligations and responsibilities towards the operator.

While the QCA proposes to accept the Operating Requirements Manual (ORM) to be placed online, amendments have been proposed to ensure that rights and responsibilities are more equitably shared between the parties.

4.1 Introduction

Once access has been contracted and prices set, access holders have a reasonable expectation that their train services will be delivered and that they will know how they will be delivered. The NMPs seek to fulfil this role by specifying how Queensland Rail will: demonstrate that its capacity is sufficient to provide for both contracted train paths and necessary maintenance; and schedule and control trains.

The NMPs for the Queensland rail networks have largely remained unchanged since 2001 and are broadly consistent with those of the ARTC. These NMPs have also sat within all past QR Network undertakings given their importance to all access holders, and their customers. This ensures that Queensland Rail manages its network for all access holders in accordance with the same rules. This is clearly necessary for the safe operation of the network. It is also equally necessary for the efficient and equitable coordination of a network that has a complex and diverse mixture of rail services.

Queensland Rail's 2013 DAU retains important aspects of the 2008 undertaking principles, including:

(a) specifying that the NMPs guide how Queensland Rail will

  (i) provide capacity-related information to access holders

  (ii) perform scheduling, train control and associated services (cl. 4.1(a)).

(b) prescribing two key scheduling documents in the NMPs, namely

  (i) the master train plan (MTP), a long-term document that demonstrates there is sufficient capacity and provides information on planned maintenance

  (ii) the daily train plan (DTP), a short-term document, derived from the MTP that shows the actual expected schedule on the day.

However, the NMPs in Queensland Rail's 2013 DAU include a number of key changes. In particular, the proposed principles provide only for timetabled and not for cyclic traffics (e.g. traffic specified as a certain number of paths over a set period, that do not have specific timetabled running times). They therefore do not include principles for allocating cyclic paths between different users (i.e. an intermediate train plan or a contested train path decision-making process).

Queensland Rail's 2013 DAU also proposes to publish a new document, the ORM, that specifies the largely technical rights and responsibilities of Queensland Rail and its access holders. The content in the ORM is largely drawn from the 2008 undertaking's standard access agreements.

The NMPs are set out in schedule B of the 2013 DAU, while the ORM has been provided as a separate document that will not form part of the undertaking.

The QCA has reviewed the NMPs and ORM to determine whether they provide sufficient transparency and protection for access holders and their customers, while also allowing Queensland Rail the necessary discretion to operate its network efficiently. The QCA's consideration of these matters is divided into:

(a) issues relating to the MTP and DTP, including

  (i) maintenance planning and changes to train plans – consider the best approach to new or changed possessions (Section 4.2)

  (ii) transparency – considers how capacity should be demonstrated and schedules published for the MTP and DTP (Section 4.3)

  (iii) cyclic traffics – consider whether the treatment of non-timetabled (i.e. cyclic) services needs to be explicitly set out in the NMPs (Section 4.4).

(b) NMPs and SAAs – consider issues with the treatment of network management in the SAAs, including the need for consistent principles for all users of Queensland Rail's tracks (Section 4.5)

(c) other NMPs issues – passenger priority and the interface with Aurizon Network (Section 4.6)

(d) ORM – includes both the content of the manual and related documents and the appropriate process for amending them (Section 4.7).

4.2 Maintenance planning and changes to train plans

The 2008 undertaking provides for Queensland Rail to change the MTP and DTP to close the track for maintenance and construction and to restrict train weights or speeds. These 'operational constraints' can include:

(a) planned possessions – typically known between three months and two years in advance of the day of operation

(b) urgent possessions – correcting 'potentially dangerous' problems less than three months after they are detected

(c) emergency possessions – fixing 'serious faults' within five days.

As all of these may affect delivery of an access holders' TSEs, the access agreement principles in the 2008 undertaking require Queensland Rail to use reasonable endeavours to minimise disruption to train services from operational constraints (2008 undertaking, schedule E, cl. 6). If the operational constraint affects an access holder’s train services in a way not consistent with

the relevant access agreement, Queensland Rail must consult with, and procure the agreement of, the affected access holder. The access holder must not unreasonably withhold its agreement (2008 undertaking, schedule G, part 1).

The 2008 undertaking also requires that, when Queensland Rail varies the MTP and DTP, it must consult with infrastructure service providers – suppliers of maintenance, construction and other related services for Queensland Rail's infrastructure.

While structure and content of the NMPs in the 2012 DAU were broadly similar to those in the 2008 undertaking, stakeholders were concerned the proposed NMPs gave Queensland Rail too much discretion to perform maintenance and construction activities without sufficient consultation (Aurizon, sub. no. 9: 23).

Queensland Rail's 2013 DAU

The 2013 DAU (similar to the 2012 DAU) requires Queensland Rail to consult with access holders when modifying the MTP (2013 DAU, schedule B, cl. 1.1(h)(i)), and

(a) procure the agreement of access holders whose train services would be affected in a way not allowed for under the relevant contract

(b) provide 30 days' notice to access holders affected by an MTP modification (2013 DAU, schedule B, cl. 1.1(d)).

However, Queensland Rail has proposed to alter the treatment for operational constraints, so that

(a) for changes to the MTP it does not have to consult with or obtain the agreement of access holders if it considers none would be adversely affected (2013 DAU, schedule B, cl. 1.1g(ii))

(b) for changes to the DTP it would be required to consult with affected access holders, but not obtain their agreement (2013 DAU, schedule B, cl. 1.2(f)(i)-(ii)).

Queensland Rail said this flexibility was necessary as the:

> *… safe running of the rail network and Queensland Rail's accreditation are dependent upon Queensland Rail being able to implement Possessions and other Operational Constraints as necessary. The NMP strike an appropriate balance between Queensland Rail's need to schedule Possessions and an access holder's interest in the operation of its train services (Queensland Rail, sub. no. 2: 9).*

The 2013 DAU provided that Queensland Rail need only provide the DTP to infrastructure service providers but not consult with them.

Stakeholders' comments

Stakeholders were concerned Queensland Rail's proposed treatment of changes to the train plans for operational constraints, including maintenance possessions, gave it too much discretion and provided too little information to access holders and other parties. They said:

(a) Queensland Rail should not be able to amend the MTP/DTP without consulting access holders that were affected by operational constraints, particularly those imposed by Queensland Rail (Glencore, sub. no. 29: 9-10; Asciano, sub. no. 31: 6).

(b) Queensland Rail should provide timely notice and consult with access holders on the impact a possession would have on TSEs, for all possessions that resulted in the MTP being amended – with the only exception being that it need not consult in the case of urgent and emergency possessions (Aurizon, sub. no. 33: 20).

(c) For DTP variations, Queensland Rail should both consult and secure the agreement of access holders whose scheduled train services would not be met because of operational constraints (Asciano, sub. no. 31: 6). Glencore said this should apply to both the MTP and DTP (Glencore, sub. no. 29: 9-10).

(d) Queensland Rail should be required to mitigate the impact of possessions on train operators and use reasonable endeavours to provide useable paths (Aurizon, sub. no. 9: 23).

(e) It was inappropriate for Queensland Rail to modify the MTP to allow for possessions based solely on Queensland Rail's opinion that no access holders were adversely affected (Aurizon, sub. no. 9: 24; see 2013 DAU, schedule B, cl. 1.1(g)).

(f) in the event of a dispute, the changes should only take effect after the dispute was resolved, instead of at the end of the 30-day notice period for changes to the MTP (Aurizon, sub. no. 9: 24).

QCA analysis and draft decision

Queensland Rail has an obligation and a right to maintain and manage its network in a manner that keeps it safe and fit for purpose. However, the way maintenance and construction are managed and timetabled can impact on access holders' ability to use their TSEs, so Queensland Rail needs to do this in a way that considers the legitimate interests of other supply chain participants.

There are three levels of action Queensland Rail can take when changing the MTP or DTP – notify, consult and seek agreement. Stakeholders have also raised issues about disputes and Queensland Rail's ability to decide that stakeholders are not affected. These matters are considered below.

Notifying

The QCA considers that notifying all relevant parties of proposed or implemented changes to the MTP or DTP is a minimum requirement. It should apply not only to access holders, but also to other affected infrastructure service providers and supply chain participants including, where relevant, ports and other below-rail operators. This notification needs to be provided at the earliest opportunity, so other parties can make necessary adjustments to manage the impact of track closures or operating restrictions with the least disruption to their own business.

Consulting

The QCA shares stakeholder concerns that Queensland Rail's proposal gives it too much discretion to impose operational constraints without consulting (Glencore, sub. no. 29: 9-10; Asciano, sub. no. 31: 6). The QCA accepts Aurizon's view that the only cases where Queensland Rail should be able to impose operational constraints without consulting are for urgent and emergency possessions.

For all other possessions that result in the MTP or DTP being amended, Queensland Rail should at least consult with access holders, give those access holders the opportunity to assess whether they are adversely affected and use best endeavours to mitigate the impact of possessions on train operators.

Seeking agreement

Most maintenance for rail infrastructure is planned long in advance. Indeed, for its western system reference tariff proposal, Queensland Rail provided a four-year maintenance forecast.

Still, from time to time, Queensland Rail will need to alter its plans to reflect changed circumstances, with the best approach depending on the timing of the change.

Queensland Rail has proposed that it be able to change the DTP for operational constraints without seeking agreement from access holders whose scheduled train services will not be met (Schedule B, cl. 1.2(f)) This is reasonable as the issues it will be seeking to address will be urgent and will need to be addressed in the short term. As discussed above, the QCA proposes that Queensland Rail will still have an obligation to consult about such changes to the DTP.

However, for changes to a long-term planning document like the MTP, Queensland Rail should be required to seek agreement from access holders where the changes affect their TSEs. Given that planned possessions, by definition, are scheduled at least three months in advance, there should be sufficient time to adjust such plans to address access holders' concerns. This approach of seeking agreement well in advance is also consistent with coordinating maintenance to maximise efficiency for all participants in the supply chain.

Disputes

The QCA accepts Aurizon's view that, where an MTP amendment other than an urgent or emergency possession is disputed by an access holder, the change should take effect after the dispute is resolved, rather than the 30-day generic timeframe (2013 DAU, schedule B, cl. 1.1(d)).

While urgent and emergency possessions should be to address safety concerns or pressing operational constraints, the other likely causes for changes to the MTP include new or altered TSEs, or long-term maintenance planning. In such cases, it is not reasonable that Queensland Rail be able to impose a change, without consulting with access holders and addressing an access holder's concerns about any adverse impact caused by that change.

Reasonable opinion

Queensland Rail has proposed that it may change the MTP without consultation, where 'in Queensland Rail's opinion no Access Holders are adversely affected by the modification' (Schedule B, cl. 1.1(g)(iv)).

The QCA considers that this gives Queensland Rail too much discretion and its assessment that a change did not adversely affect access holders should be subject to challenge. The clause should therefore be amended to read in Queensland Rail's 'reasonable opinion' and a change to the MTP should always be subject to 'consulting with access holders that may be affected'.

Infrastructure service providers

Queensland Rail has proposed that, consistent with the 2008 undertaking and Aurizon Network's 2010 undertaking, 'Infrastructure Service Providers' be defined as providers of rail maintenance and construction services. The QCA considers that it is at least as important that operators of ports and connected rail networks that rely on and interact with Queensland Rail's below-rail services also be aware of changes to the MTP and DTP. The QCA therefore requires that the definition of 'Infrastructure Service Providers' be amended to include these parties.

Draft decision 4.1

- **The QCA requires Queensland Rail to amend its proposal so that the network management principles:**
  - **(a) require Queensland Rail to promptly notify access holders, affected infrastructure service providers and supply chain participants including, where relevant, ports and other below-rail operators, of proposed or implemented changes to the master train plan (MTP) or daily train plan (DTP)**
  - **(b) only allow Queensland Rail to impose operational constraints without consulting access holders in cases of urgent and emergency possessions**
  - **(c) require Queensland Rail use best endeavours to mitigate the impact of possessions and other operating constraints on access holders**
  - **(d) require that Queensland Rail secure agreement from access holders where changes to planned possessions in the MTP affect their train service entitlements (TSEs)**
  - **(e) provide that, where an MTP amendment other than an urgent or emergency possession is disputed by an access holder, the change to the MTP should take effect after the dispute is resolved**
  - **(f) require in Schedule B, cl. 1.1(g)(iv) that 'in Queensland Rail's reasonable opinion no access holders are adversely affected by the modification, and any access holders that may be affected have been notified and consulted'**
  - **(g) amend the definition of 'Infrastructure Service Providers' to include ports and other below-rail operators that are affected by the availability of Queensland Rail's Network.**

4.3 Transparency of train plans

The NMPs in the 2008 undertaking provide a detailed set of procedures for Queensland Rail to:

(a) use the MTP to detail TSEs and planned possessions 'in a form that indicates the time/distance (location) relationship of the Train Services and other activities on the Rail Infrastructure' (schedule G, cl. 2.a)[16]

(b) modify the MTP if it creates a new or modified TSE, or changes its planned possessions for maintenance or other activities (see Section 4.2)

(c) prepare a weekly train plan that largely addresses issues with scheduling cyclic services (see Section 4.4)

(d) prepare and amend DTPs

(e) give notice to, consult with and seek agreement from access holders affected by modifications to the MTP and DTP

[16] The 'time/distance (location) relationship' can be shown either in a train graph, that shows each train's transit over the network in a graphical form (for a simplified example, see QCA, April 2013: 11), or in a tabular format, that lists the times each train will pass a series of points on the network (similar to the passenger rail timetables published for a passenger network such as the Queensland Rail suburban commuter trains).

(f) allow access holders to assess the train-control decision making process by providing them with

(i) train control diagrams showing the actual running of their train services against the relevant DTP

(ii) information about other train services using the network (2008 undertaking, schedule G, part B, cl. (f)(ii) and (iii)).

The 2008 undertaking also requires that the MTP and DTP provided to access seekers not include the identity of other access holders, or the terms and conditions of other access holders' TSEs (schedule D, Part A, cl. 1 and Part B, cl. 1a)).[17]

Other below-rail operators, including ARTC, publish a detailed MTP for their networks. For example, ARTC's MTP for the Moree to Muswellbrook journey in the Hunter Valley in New South Wales includes the names of all operators using that infrastructure for a given day. It also details each train service's identification numbers and includes information on arrival, departure and dwell times of the various train services.[18]

Queensland Rail's 2013 DAU

The 2013 DAU does not preclude Queensland Rail from providing the information in the MTP or DTP to access seekers or holders. Indeed, Queensland Rail proposes to provide control diagrams for an access holder's own services, and information about other train services as well, subject to reasonable terms and conditions (Schedule B, 2(e)).

Stakeholders' comments

Stakeholders said they wanted better information on capacity and maintenance planning. Peabody wanted a transparent master plan so that any capacity analysis for expansions was not completed in isolation or on an arbitrary basis (Peabody, sub. no. 34: 1). Glencore said it wanted greater certainty that Queensland Rail was not over-contracting (Glencore, sub. no. 16: 6).

QCA analysis and draft decision

The two key planning documents specified in the NMPs are:

(a) the MTP – serves the separate but related long- to medium-term functions of

(i) demonstrating that there is sufficient capacity to serve all TSEs, as well as planned possessions (i.e. times allocated for maintenance and construction)

(ii) providing information on planned maintenance and construction work, to enable access holders and other supply chain stakeholders to coordinate their activities

(b) the DTP – short-term, produced a week or two before the trains run and shows the actual expected schedule on the day, including transient changes requested by access holders or Queensland Rail.

The QCA considered a number of issues relating to these documents in its final decision on Aurizon Network's Capricornia system rules. One of the key conclusions was that the MTP and DTP were more effective if they were published with all potential and contracted train paths

[17] The QCA understands that Aurizon Network has applied these restrictions to supply an incomplete MTP and DTP to access holders as well as access seekers in central Queensland (see QCA, February 2014: 18).

[18] ARTC's MTP (in tabular form) is available at http://www.artc.com.au/Content.aspx?p=161.

included. The QCA said that publishing complete and transparent MTPs and DTPs had the benefit of:

> *(a) showing there is sufficient capacity to provide all contracted paths, after allowing for the paths needed to accommodate supply chain variability, and for the maintenance possessions required to keep the network fit for purpose*
>
> *(b) allowing access seekers and their customers to see what paths are available to be contracted*
>
> *(c) allowing access holders and their customers to see what paths might be available for receiving their TSEs and for running any ad hoc services*
>
> *(d) enabling access holders, their customers, and other supply chain participants to confirm that paths have been allocated equitably (QCA, February 2014: 16).*

The QCA noted that Aurizon Network's 2010 undertaking contained restrictions on making the documents fully transparent, but said this would need to be addressed as part of the review of Aurizon Network's replacement undertaking.

The QCA considers that all the benefits of transparent and public train plans also apply to Queensland Rail. This is particularly true of assessing capacity. While the MTP in itself is not sufficient to complete a rail capacity analysis, it is one of the key inputs to understanding whether there is sufficient capacity for all train services and necessary maintenance (see Chapter 9 for more on capacity analysis).

It is also relevant for efficient operation of the network, as access seekers and holders will be able to use the MTP and DTP to assess whether there are available paths they can contract for access over the long term, or use on a particular day.

While Queensland Rail has not proposed any clauses to prevent it from publishing or providing a complete MTP or DTP, it has not explicitly set out that it will do so. The QCA therefore considers that Queensland Rail should amend its NMPs to specify that it will:

(a) publish a complete MTP for each system on its website, either in train graph or tabular form, consistent with those published by ARTC, and update it every six months, or more often at an access holder's request, if the MTP is modified

(b) provide a complete DTP, showing all services, to an access holder on request.

This should not be an onerous requirement for Queensland Rail, as it already prepares MTPs and DTPs. It will provide a substantial benefit to access seekers and access holders, in understanding how their TSEs are provided. It will also enable better planning of rail network expansions by providing clarity about available train paths. The QCA notes that this is consistent with a finding of the Queensland Parliament's inquiry into rail freight use by the agriculture and livestock industries that also wanted greater clarity of how train paths are allocated (Queensland Parliamentary Committees, June 2014).

The QCA notes that the 2013 undertaking allows Queensland Rail to provide train control diagrams of an access holder's own services, and information about other access holders' services, subject to reasonable terms and conditions. The QCA considers this is reasonable, as greater transparency will help access holders assess whether train control is being applied consistent with the NMPs, while at the same time the release of confidential information is covered by the terms of the SAAs.

Draft decision 4.2

- **The QCA requires Queensland Rail to amend its proposal so that it is required to:**
  - **(a) publish a complete MTP for each system, either in train graph or tabular form, consistent with those published by ARTC, and update it every six months, or more often at an access holder's request, if the MTP is modified**
  - **(b) provide a complete DTP, showing all services, to an access holder on request.**

4.4 Cyclic traffics

The 2008 undertaking allows for train services to either operate to a timetable, or to be 'cyclic traffics' that are allocated a number of paths that can be used within a particular time period, but will have their specific running times set through the process of developing a daily train plan from the master train plan. To date, cyclic traffics have operated only in the CQCR systems that are now operated by Aurizon Network – all of Queensland Rail's access agreements are for timetabled services.

The NMPs in Queensland Rail's 2013 DAU do not explicitly provide for cyclic services. However, Queensland Rail's proposed definition of a TSE is:

> *... an Access Holder's entitlement under an Access Agreement to operate a specified number and type of Train Services over the Network 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 (2013 DAU, cl. 7.1).*

Aurizon said it would be efficient for Queensland Rail to allow cyclic traffics to operate on the network as the transport of bulk commodities is generally more cyclic in nature than timetabled. It noted that:

> *... [c]yclic paths were included in the 2001 undertaking to account for the circumstance that the network can be used more efficiently by providing a certain number of train paths in a given period and allowing the access holder to manage the variability of supply (Aurizon, sub. no. 33: 19).*

The QCA accepts that there may be circumstance, in the future, where it may be necessary and efficient for Queensland Rail to provide access on a cyclic basis, as Aurizon Network already does for coal trains in central Queensland.

The QCA also notes that, while Queensland Rail's proposed NMPs do not provide for cyclic traffics, they do not explicitly preclude them.

The QCA does not propose to require Queensland Rail to reinstate provisions for cyclic traffic that will not apply to any of its existing services. However, it is not possible to anticipate what sort of access requests Queensland Rail or its successor companies will receive over the course of the 2013 undertaking period.

The QCA therefore requires that Queensland Rail include a provision that it will submit a DAAU to reinstate provisions for cyclic traffic equivalent to those in the 2008 undertaking, if necessary to accommodate an access request, or to address any issues raised by integration of its operations with a port or other supply chain entity. These would include provisions for a weekly or intermediate train plan, and a contested train path decision-making process.

Draft decision 4.3

- **The QCA requires Queensland Rail to amend its proposal so that it is required to submit a DAAU, if requested by the QCA, to reinstate provisions for cyclic traffic equivalent to those in the 2008 undertaking, if necessary to accommodate an access request, or to address any scheduling and train control issues arising from the integration of its operations with a port or other supply chain entity.**

4.5 NMPs and SAAs

Queensland Rail has a large network and a wide variety of traffics ranging from non-profit heritage passenger trains and suburban commuter services to freight trains and bulk mineral and coal trains.

These services interact with each other at various points on the network. Those interactions need to be safe and efficient. Also, different services and access holders need to be treated in a transparent and consistent manner.

The 2008 undertaking seeks to achieve this by requiring the SAAs to refer to scheduling and other network management protocols in the NMPs. The 2008 undertaking's Operator SAA:

(a) sets out the contractual framework within which Queensland Rail must undertake maintenance and construction activities and also requires Queensland Rail to perform those activities in a form consistent with the NMPs

(b) obliges Queensland Rail to use its reasonable endeavours to minimise disruption to train services, so access holders can operate train services in accordance with their TSEs (2008 Operator SAA, cl. 6.2(b)(i))

(c) requires above-rail operators to operate their train services in accordance with the relevant train schedule in the NMPs (2008 Operator SAA, cl. 6.2(a)(ii))

(d) requires Queensland Rail's train control directions to be consistent with the NMPs and have regard to the safe conduct of rail operations (2008 Operator SAA, cl. 4.2).

In the 2008 undertaking, both passenger and freight train services had to negotiate access agreements with Queensland Rail, that required access holders and Queensland Rail to comply with the NMPs in the undertaking. For passenger services, these were internal access agreements between QR Network and QR Passenger, both subsidiaries of the then QR Ltd.

Queensland Rail's 2013 DAU

The 2013 DAU's SAA (like the 2012 SAA) proposed to allow Queensland Rail to perform its maintenance and construction activities, and to impose related operational constraints, without access holders' consent (2013 SAA, cl. 5.1(b) and 6.2(iv)).

The SAA did not specify whether Queensland Rail had to use reasonable endeavours to minimise train disruptions when performing maintenance and construction activities, or whether Queensland Rail had to follow the NMP when making train control decisions (2013 DAU SAA, cl. 5.2).

The 2013 DAU did not include a requirement for passenger train services to have access agreements with Queensland Rail. Queensland Rail said that its TI Act passenger priority obligations negated the need for internal access agreements, but the NMPs still applied to passenger services (Queensland Rail, sub. no. 2: 25). The NMPs were:

... intended to ensure that all operators are treated consistently and transparently in respect of scheduling and on the day of operation. Queensland Rail's passenger train services and the train services of all third party access holders will be scheduled by Queensland Rail into the MTP and DTP and are subject to the NMP (Queensland Rail, sub. no. 2: 42).

Stakeholders' comments

Stakeholders said Queensland Rail's SAAs should clearly link Queensland Rail's ability to undertake maintenance and construction activities works to the NMP in the undertaking. They said:

(a) the level of discretion proposed by Queensland Rail was inconsistent with the NMPs, since the NMPs clearly identified the circumstances in which Queensland Rail needed to consult with access holders when intending to undertake maintenance and construction activities (Aurizon, sub. no. 33: 18)

(b) the SAA should require Queensland Rail to use reasonable endeavours to minimise disruptions to scheduled train services when conducting maintenance and construction activities, have regard to the requirements of affected operators and their customers and comply with the relevant procedures in the IRMP (Aurizon, sub. no. 9: 32; Glencore, sub. no. 30: 26).

Aurizon was also concerned that:

(a) the definition of 'Train Control' in the 2013 SAA was broader than the 2008 SAA and, as it was not linked to the NMP, had the potential to undermine an operator's contractual entitlement. For example, the definition in the 2013 SAA covered the control, management and monitoring of the proper, efficient, and safe operation of the rail network, while that of the 2008 SAA only required Queensland Rail to have regard to the safe conduct of rail operations (Aurizon, sub. no. 9: 11; sub. no. 33: 29).

(b) if Queensland Rail did not have internal access agreements for its passenger trains, it was not clear the NMPs would apply consistently across its passenger trains and freight (or external passenger) trains that would have access agreements (Aurizon, sub. no. 27: 7).

QCA analysis and draft decision

There are good reasons why there should be a single set of NMPs that apply to all train services on Queensland Rail's network so that all train services are subject to the same set of scheduling rules and train control decisions. In particular:

(a) The SAAs should specify that the NMPs at all times will be those in the undertaking, and be applied for all relevant activities including scheduling and train control.

(b) The undertaking should specify that passenger services will at all times be subject to the NMPs.

The NMPs, as approved in an undertaking, can only be altered through a public consultation and approval process – which provides certain safeguards that contractual rights cannot be unilaterally overridden. Further, the network is operated for the benefit of all traffics, including passenger, freight and bulk commodity services, so any amendments to the NMP will need to be in the interests of all those groups, as well as the interests of the facility owner.

NMPs references in SAA

The QCA accepts Aurizon's view that the 2013 SAA does not clearly link to the NMPs in the 2013 DAU. Indeed, the 2013 DAU provides that Queensland Rail can undertake maintenance and

construction activities without access holders' consent. The QCA therefore requires Queensland Rail to ensure the SAA adopts an approach that is consistent with the NMPs in the undertaking.

The QCA also accepts stakeholders' suggestion that the SAAs should require Queensland Rail to minimise disruptions to train services due to operational constraints. The QCA therefore requires Queensland Rail to reintroduce the term 'Operational Constraints' from the 2008 undertaking and SAA.

The issues relating to the treatment of the NMPs in the 2013 DAU SAA are addressed in more detail in Chapter 7 of this draft decision.

NMPs for passenger services

While the QCA accepts that Queensland Rail need not have access agreements with its passenger services, the QCA considers it important that the NMPs apply consistently across Queensland Rail's passenger and non-passenger trains, regardless of how they are contracted.

Queensland Rail's explanatory note to the 2013 DAU states the NMPs will apply to both Queensland Rail's passenger trains and other train operators. However, it is not clear to the QCA that the NMPs in the 2013 DAU would be applied in this way. Indeed, the 2013 DAU does not explicitly state that the NMPs will apply to passenger services.

The QCA therefore requires Queensland Rail to include a clause in the 2013 DAU that clearly specifies the NMPs in the undertaking will apply to all services including Queensland Rail's own passenger services.

Draft decision 4.4

- **The QCA requires Queensland Rail to amend its proposal so that the NMPs in the undertaking clearly specify that they will apply to all services including Queensland Rail's own passenger services.**

4.6 Other NMPs issues

4.6.1 Passenger priority

Queensland Rail's passenger priority obligations in the TI Act, allow it to give priority to passenger services over non-passenger services when scheduling and controlling trains. Queensland Rail only operates passenger services, while non-passenger services (i.e. coal, general freight and livestock) are operated by third parties. Therefore, the operators of non-passenger services need to be confident that Queensland Rail does not give priority to its own passenger train services in an unfair or inefficient manner.

The TI Act requires Queensland Rail to seek to bring a delayed passenger service back to its scheduled running time, but in doing so Queensland Rail may have regard to other matters, such as the impacts on non-passenger train services (TI Act, s. 265).

The 2008 undertaking seeks to give effect to this requirement, as it provides that Queensland Rail can prioritise a passenger service over other train services to manage its passenger priority obligations under the TI Act (2008 undertaking, appendix 2, rule 5).

In its 2012 DAU, Queensland Rail sought to extend this arrangement to allow it to bring a late passenger service back to being punctual, and to act to avoid a punctual passenger service from becoming late (2012 DAU, schedule B, cl. 2(i)(ii)). The proposed 2012 SAA included similar provisions (2012 DAU SAA, cls. 5.2(e);. 5.3(e)(i)-(iii)).

Aurizon said Queensland Rail had overstated the TI Act's passenger priority obligations, that required Queensland Rail to act reasonably and fairly in balancing those obligations with the terms and conditions of its access agreements with freight train operators (Aurizon, sub. no. 9: 7).

Queensland Rail's 2013 DAU

The 2013 DAU and related SAA (like the 2012 DAU and SAA) provided for Queensland Rail to give priority to a passenger service over other train services if its train controller considered it necessary to make a late passenger service punctual or avoid a punctual passenger service becoming late (2013 DAU, schedule B, cl. 2(i)(ii)).

However, in response to stakeholders' comments, Queensland Rail sought to limit its ability to take pre-emptive action to prevent a passenger train being delayed, so that it only applied in the metropolitan region during a peak period (2013 SAA, cl. 5.2(e)(i)-(iii); 2013 DAU, schedule C, cl. 5.2(e)(i)-(iii)).

Queensland Rail said:

> *... [t]he efficient running of passenger services in the Metropolitan Region is both in the public interest and Queensland Rail's legitimate business interests. Queensland Rail has modified this clause so that it better reflects its intended purpose. (Queensland Rail, sub. no. 19: 27).*

Stakeholders' comments

Aurizon maintained its view that Queensland Rail's proposal went beyond the requirements of s. 265 of the TI Act. It said:

(a) The clause allowing pre-emptive action to prevent a passenger train being delayed should be removed from the SAA, and instead the NMPs should be amended to mirror the passenger priority obligation in the TI Act (Aurizon, sub. no. 33: 30).

(b) The NMP should be amended to reflect the legislative obligation in the TI Act that Queensland Rail has to endeavour to bring a delayed passenger service back to its scheduled running time and to consider the impact on all train services in doing so (Aurizon, sub. no. 27: 7).

Aurizon said the TI Act provision:

> *... does not make the Passenger Priority provision absolute, nor does it empower Queensland Rail to alter, in every instance, existing contractual entitlements of non-passenger train services. (Aurizon, sub. no. 9: 7)*

QCA analysis and draft decision

The QCA accepts that the NMPs and SAA must not overstate Queensland Rail's passenger priority obligations.

The QCA also accepts that Queensland Rail is not required to take pre-emptive action under the TI Act to avoid passenger trains being delayed (TI Act, s. 265). But in some circumstances, pre-emptive action may be reasonable, in particular to avoid delays that would otherwise have a material impact on the operation of passenger services.

Queensland Rail has now sought to restrict its ability to take pre-emptive action to peak periods – the times at which the impacts of delays are greatest and where delays could have a cascading effect on timetabled passenger services. The QCA considers this appropriately balances the interests of operators of passenger and non-passenger services.

The QCA notes that, while Queensland Rail included the provision relating to 'metropolitan region during any peak period' in the 2013 DAU SAA, this was not mirrored in NMPs (see 2013 DAU, schedule B, cl. 2(i)(ii)). The QCA understands that this was an oversight and Queensland Rail has indicated this will be addressed in its response to this draft decision.

Separately, the QCA does not accept Aurizon's position that Queensland Rail must necessarily take the impact on all train services into consideration when endeavouring to bring a delayed passenger service back to its scheduled running time. This is because the TI Act provides that Queensland Rail may have regard to matters the rail manager considers relevant when complying with this requirement (TI Act, s. 265(3)). This means that Queensland Rail has some discretion to decide how best to meet its passenger priority obligations, provided that its choice of action is consistent with the NMPs.

Draft decision 4.5

- **The QCA requires Queensland Rail to amend its proposal so that the NMPs and SAA restrict its ability to take pre-emptive action to avoid passenger trains being delayed to peak periods in the metropolitan region.**

4.6.2 Interface with Aurizon Network

Past rail undertakings in Queensland were designed for a single network operator when the networks, now operated separately by Queensland Rail and Aurizon Network, were both part of the former QR Ltd business.

Since the 2010 split of QR Ltd, trains on the north coast line and other parts of Queensland Rail's network have had to deal with two railway managers – Queensland Rail and Aurizon Network. The coordination issues associated with multiple networks will become even more significant if railways to new coal basins are constructed in central Queensland or there is a change in the ownership or management of some of Queensland Rail's assets.

The 2008 undertaking's NMPs were silent on the issue of interface between two networks as there was only one railway manager when they were approved.

Queensland Rail's 2013 DAU, like its 2012 DAU, did not address interactions with adjoining infrastructure.

Stakeholders' comments

Stakeholders were concerned that, since two separate undertakings were being developed (2013 DAU for Queensland Rail and UT4 for Aurizon Network), the NMPs for the two networks would diverge. They said:

(a) Queensland Rail's NMPs should, to the extent possible, be consistent with those in Aurizon Network's 2010 undertaking (Asciano, sub. no. 6: 11; Asciano, sub. no. 31: 6-7).

(b) An access holder whose train services operated across both networks should be able to withhold consent to MTP/DTP amendments where the adjoining infrastructure manager did not agree to provide an uninterrupted train path (Aurizon, sub. no. 9: 24; sub. no. 33: 19 – see 2013 DAU, schedule B, cl. 1.1(h)(ii)(B) and 1.2(f)(ii)).

(c) Interface risk assessments relating to a network interface point (NIP) needed to include both network managers (Aurizon, sub. no. 9: 27; sub. no. 33: 19).

(d) Queensland Rail should therefore use interface agreements to coordinate its scheduling and maintenance activities with Aurizon Network for train services using both networks (Aurizon, sub. no. 9: 27; sub. no. 33: 19). These interface agreements should:

  (i) provide for Queensland Rail's amendments to system-wide requirements (NMPs and related provisions) to have regard to those of Aurizon Network

  (ii) allow an operator using both networks to withhold consent to a request from Queensland Rail for a long-term change to the times at which the operator's services ran, if the operator was unable to secure an uninterrupted path from Aurizon Network for the affected train service(s)

  (iii) be appended to the 2013 SAA (Aurizon, sub. no, 9:27).

QCA analysis and draft decision

When train schedulers and controllers manage services crossing between two or more networks they will inevitably have to address the coordination issues this creates. The NMPs therefore need to guide how this will be managed safely and efficiently. And, where possible, the rules for the different networks should be aligned.

The QCA has already considered these issues in relation to Aurizon Network's system rules for the Capricornia system, where train services from the Moura and Blackwater systems in the CQCR need to be coordinated with services on Queensland Rail's north coast line (see QCA, February 2014).

The approved Capricornia system rules guide the interaction Aurizon Network has with adjoining network managers, (e.g. Queensland Rail), including that it will:

(a) coordinate its maintenance activities with adjoining network managers so trains operating across both networks face minimal disruption (Aurizon Network, April 2014: 12)

(b) take into consideration timetabled through-running trains to and from adjoining rail infrastructure when developing its MTP (Aurizon Network, April 2014: 11).

The QCA also accepts Asciano's view that the NMP in Queensland Rail's 2013 DAU should be aligned, in a general sense, with those in Aurizon Network's undertakings. The QCA notes alignment is not something that can necessarily be achieved by Queensland Rail on its own – the QCA will coordinate the treatment of the NMPs and related provisions for both networks' undertakings as they are finalised over the coming months

In addition, the alignment will not necessarily be complete. As Queensland Rail is not vertically integrated with a freight operator, and only operates timetabled traffics, its NMPs can reflect these characteristics, and therefore differ from those of Aurizon Network.

However, the two railways' NMPs will need to provide for operation of trains across the two networks to be as seamless as possible. To this end, Queensland Rail will need to have regard to Aurizon Network's NMPs, the approved Capricornia system rules, and any other approved system rules, where relevant.

The QCA is not at this time proposing to require user interface agreements for either below-rail operator, as suggested by Aurizon. Rather, the QCA considers it sufficient, from Queensland Rail's point of view, for its NMPs to:

(a) provide for Queensland Rail's amendments to system-wide requirements to have regard to those of Aurizon Network

(b) allow access holders to withhold consent to MTP/DTP amendments (with the exception of possession-related changes) by Queensland Rail that cannot be accommodated by the adjoining network manager.

Draft decision 4.6

- **The QCA requires Queensland Rail to amend its proposal so that its NMPs:**
  - **(a) require it to coordinate its maintenance activities with adjoining network managers so trains operating across both networks face minimal disruption**
  - **(b) require Queensland Rail to take into consideration through-running trains to and from adjoining rail infrastructure when developing its MTP**
  - **(c) provide for Queensland Rail's amendments to system-wide requirements to have regard to those of Aurizon Network, including its NMPs, the approved Capricornia system rules and any other approved system rules, where relevant**
  - **(d) allow access holders to withhold consent to MTP/DTP amendments (with the exception of possession-related changes) by Queensland Rail that cannot be accommodated by the adjoining network manager.**

4.7 Operating Requirements Manual

Background

The ORM is a document that is proposed to be published on Queensland Rail's website. It sets out requirements and other information about train control and the access to and use of the network by train operators. These requirements include those related to:

(a) interface risk management, including environmental risk management

(b) safe working procedures and safety standards

(c) incident and emergency response procedures

(d) various technical requirements for train control and network planning

(e) commercial requirements such as those for forecasts by the operator of expected train services and how and when safety notices will be issued.

In the 2008 undertaking, operational requirements were individually negotiated between Queensland Rail and an operator as part of an access agreement. Queensland Rail in its supporting submission to the 2013 DAU said it was inefficient to have to renegotiate these issues separately for more than 30 access agreements. Therefore, Queensland Rail proposed one document that applies to all access seekers/holders to be published on its website.

> *... amendments to operational requirements ... will then flow through to the access holders without the need to vary contracts. This process will introduce greater efficiencies for all parties (Queensland Rail, sub. no. 19: 19).*

The content of the ORM is formed by shortening operational requirements of the 2008 undertaking, namely the Standard Access Agreement (SAA) (Volume 2) of Queensland Rail's 2008 undertaking (see **Table 1** for a summary of key changes).

Table 1 Consolidating the ORM

Queensland Rail 2013 DAU - Operating Requirements Manual (ORM)	*Queensland Rail undertaking*
Section: 2. Interface risk management	Queensland Rail 2008 undertaking (cl. 8.1)
2.3 Risks to the environment	Queensland Rail 2008 undertaking (cl. 8.2)
3. Safe working procedures and safety standards	Queensland Rail, undertaking, SAA, Volume 2 (cl. 10)
4. Incident and emergency response	Queensland Rail, undertaking, SAA, Volume 2 (cl. 7)
5. Authorisation of rolling stock and train configurations	Queensland Rail, undertaking, SAA, Volume 2 (cl. 5.9)
6. Train Control and Network Planning	Queensland Rail, undertaking, SAA, Volume 2 (cl. 5)
7. Commercial considerations 7.1 Forecasts	Queensland Rail, undertaking, SAA, Volume 2 (cl. 3.4)

Stakeholders' comments

Stakeholders generally supported the idea of bringing the operational requirements together in one document and out of the undertaking. For instance, AMEC said that it supported the concept of moving the ORM to Queensland Rail's website as it believed it established clarity and certainty and full transparency for the operator (AMEC, sub. no. 8: 3).

However, stakeholders said that by shortening the provisions in the ORM, Queensland Rail departed significantly from the balance of risks and responsibilities between Queensland Rail and operators that underpinned the 2008 undertaking and its SAAs. Given that, stakeholders said the proposed ORM now provided too much discretion to Queensland Rail.

Stakeholders' (Asciano and Aurizon) key concerns are summarised below and detailed in Appendix A.

Imbalanced approach

Asciano and Aurizon said that Queensland Rail proposed an imbalanced approach on a range of requirements across the ORM. For example, Asciano and Aurizon said the allocation of controls to handle risks related to the interaction between the network provider and the operator were imbalanced in Queensland Rail's favour (Asciano, sub. no. 33: 17; Aurizon, sub. no. 33: 59-65). Asciano proposed that

> *... these requirements for monitoring, competence, complaint handling, audit, inspection and review should be even handed and open for both operator and access provider (Asciano, sub. no. 33: 17).*

Likewise, stakeholders raised concerns about the fair allocation of mutual responsibilities regarding environmental risk compliance requirements and information provision related to incident and emergency response (Asciano, sub. no. 31: 17-20; Aurizon, sub. no. 33: 59-65).

Increased operational obligations

Asciano and Aurizon said Queensland Rail proposed increased operational and information compliance obligations to be placed on the operator, including record keeping for emergency and incidence response where Queensland Rail is responsible for the overall coordination and management of the response to a network incident (Asciano, sub. no. 31: 17-20; Aurizon, sub. no. 33: 59-65). Other examples included the proposed requirement that the operator provide

information on the location of waterways across the network to Queensland Rail, as well requiring the operator to undertake environmental baseline monitoring.

Lack of clarity

Asciano and Aurizon said that the allocation of responsibilities between parties is unclear. For example they said that although Queensland Rail provides a framework for risk control, it does not specifically allocate individual responsibilities for residual risks (Asciano, sub. no. 31: 17-20; Aurizon, sub. no. 33: 59-65). Stakeholders also said that Queensland Rail requires information that is either too broad or duplicates other clauses, for instance:

> *... the obligation for the operator to provide 'any information in relation to anything referred to in section 4' (i.e. emergency and incident response) seems too broad. This point should be narrowed to a more specific request for information. (Asciano, sub. no. 31: 18)*

> *... QRail to clarify as to how the information required is materially different from the requirement to provide information regarding the details of any additional hazards, risks and non-compliances as required under cl. 2.2(b)(ii)(A). (Aurizon, sub. no. 33: 59)*

QCA analysis and draft decision

Asciano and Aurizon have identified a range of areas where they consider the ORM should be improved to give a better balance and clarity to the various obligations.

The QCA supports the view that the ORM should reflect a fair and balanced allocation of risks and responsibilities. For economic efficiency reasons these risks and obligations should be placed on the party that is in the best position to manage those risks.

Based on stakeholder comments, it is evident that Queensland Rail's proposal falls short of that ideal.

The QCA has previously considered the need for appropriately functioning and transparent operating requirements and the appropriate balancing of risks and responsibilities in the context of the 2010 Aurizon Network undertaking. The QCA's position on this has been developed and refined over successive undertakings.

These matters are equally relevant to Queensland Rail as both network service providers manage the provision of the network to above-rail service provides. It is also not apparent that, in general, a different risk profile for operating requirements is necessary for Queensland Rail, compared to Aurizon Network.

Given this, the QCA requires where possible, that the ORM be amended to reflect the balance of risks and responsibilities as contained in the relevant sections of the Aurizon Network undertaking. The exception to this position is where there are circumstances specific to Queensland Rail.

Where there are shared responsibilities and obligations, the terms of the ORM should be proportional to each party's ability to manage those risks. For example, Queensland Rail proposed that operators should gather baseline environmental information before they commence on the network. In most circumstances, the QCA notes that it would be economically more efficient for Queensland Rail to gather this information given it should have a detailed knowledge of the environmental condition of its network before an operator commences operating. This can also ensure greater consistency in information collected across systems. Given this, the QCA recommends that Queensland Rail undertakes baseline environmental monitoring, rather than delegating this responsibility to the operator.

Similarly, where one party has an information advantage over the other (e.g. the train operator observes in the normal course of their operations a technical or environmental risk to the good

operation of the network) the ORM should facilitate cooperative behaviours to share the information rather than seek to transfer rectification responsibilities onto the party that is simply a witness to a set of adverse events. For example, Queensland Rail proposed that the operator must provide Queensland Rail with information and assistance in an investigation (for example after an emergency response). While the QCA supports this requirement, the QCA also recommends that a reciprocal obligation be placed on Queensland Rail.

And similarly, if Queensland Rail is aware that the network faces operational challenges they should be obliged to advise the train operators to, for instance, stop at a signal to avoid a collision or to meet a specified speed restriction to avoid a derailment. Likewise, the operator should inform Queensland Rail of matters it becomes aware of that may impede the efficient operation of the network. At the same time, it is not reasonable for Queensland Rail to expect the operator to inform it of matters that it should be clearly aware of (e.g. location of waterways).

In summary, the ORM needs to reflect the reasonable allocation of responsibilities between the network operator, train operators and their customers. In doing so, it will engender a cooperative approach to the management of all matters that occur on a day-to-day basis.

Appendix A provides further detail on stakeholder concerns and the QCA's proposed amendments to address those concerns. The QCA proposes to amend Queensland Rail's drafting to reflect similar provisions in the Aurizon Network undertaking, unless there are clear differences in Queensland Rail's risk profile or which are related to its proposal to place the ORM materials on the web (which Aurizon Network does not do).

Draft decision 4.7

- **The QCA requires Queensland Rail to amend its proposal so that the risk allocation matrix applied to Aurizon Network's 2010 undertaking underpins the principles of the Operational Requirements Manual.**

4.8 Dispute process for ORM and related documents

The ORM includes matters previously set out in undertaking and the SAAs.

The possibility for amendments to the operating requirements imposes significant uncertainty and potentially large compliance costs onto the train operator (the access holder). Given this, it is reasonable for the operator to be informed of potential amendments and for there to be a clearly defined dispute resolution process that provides operators with protection and certainty by allowing all affected parties to challenge proposed amendments.

Queensland Rail's 2012 DAU did not include any provisions relating to amendments to the ORM and how disputes to amendments are dealt with. In response, stakeholders raised concerns regarding a lack of transparency on the process for amending the ORM.

Queensland Rail's 2013 DAU

Queensland Rail's 2013 DAU proposed provisions for amending the ORM and for disputes to be raised where stakeholders had concerns.

Amending the ORM

Queensland Rail said it would notify stakeholders about proposed amendments to the online ORM as well as provide the operator with reasonable timeframes to implement proposed

amendments. Specifically, Queensland Rail said it would notify and consult with operators who are materially adversely affected (in Queensland Rail's opinion) by a change to the ORM.

In these circumstances, Queensland Rail said it would allow a reasonable time period for operators to implement any obligations arising out of amendments to the ORM.

However, Queensland Rail proposed not to consult with a train operator, where an amendment to the ORM relates to:

(a) a safety matter

(b) a material change

(c) a change to the assets, equipment, facilities, infrastructure, processes, procedures or systems used for the purposes of any train management system for the purpose of improving safety, network capabilities, network capacity or system reliability.

Queensland Rail also did not include a provision to compensate the operator for cases where the operator's services are fundamentally frustrated over a period of time as a result of any proposed amendments.

Queensland Rail did not provide a rationale for either position.

Disputes about amendments to the ORM

Queensland Rail's 2013 DAU proposed a dispute mechanism for matters on which it consults with the operator. The dispute is triggered when an operator considers that an amendment to the ORM 'unfairly differentiates' between operators, which is defined as meaning:

> *… unfairly differentiates between operators in providing access in a way that has a material adverse effect on the ability of one or more of the operators to compete with other operators (Queensland Rail, February 2013: 66).*

As part of the dispute process, the operator is required to give Queensland Rail notice of the dispute. Queensland Rail proposed that the dispute is resolved under the provisions about disputes of cl. 6.1.4 of Queensland Rail's 2013 undertaking.

Liability

Queensland Rail proposed that it is not in breach of the ORM if it fails to comply with its provisions, provided that its actions are 'reasonable' and in 'good faith.'

Stakeholders' comments

Stakeholders were generally supportive of Queensland Rail's intention to reduce its administrative overheads and complexity of the 2013 DAU by placing the ORM on its website (Peabody, sub. no. 13: 7; Aurizon, sub. no. 33: 21; AMEC, sub. no. 8: 3).

Amendments

However, stakeholders were concerned about the triggers to the consultation process with operators when Queensland Rail proposes amendments to the ORM. For instance, Aurizon said that Queensland Rail allowed itself too much discretion to make changes without consultations (Aurizon, sub. no. 33: 21).

To make amendments to the ORM a fair and transparent process, stakeholders said that Queensland Rail must ensure that operators/access holders as well as their major customers be alerted to any amendment to the online ORM and online network diagrams as well as ORM related documents (i.e. network business master train plan protocol, the network, business daily train plan protocols and the network business possession planning protocols) (Peabody,

sub. no. 13: 7; Peabody, sub. no. 34: 5; Aurizon, sub. no. 33: 21; AMEC, sub. no. 8:3; Asciano, sub. no. 6: 18; Glencore, sub. no. 30: 8; New Hope, sub. no. 32: 3).

Aurizon and New Hope said that amendments should be reasonable and consider potential effects on the supply chain and operator's customers. (Aurizon, sub. no. 33: 21; New Hope, sub. no. 32: 3). Aurizon and Glencore added in this regard that Queensland Rail should provide compensation to operators where Queensland Rail receives a benefit at a cost to the operators (Aurizon, sub. no. 33: 21; Glencore sub. no. 30: 11), while Glencore proposed a solution by saying that Queensland Rail should reinstate:

> *... provisions regarding compensation for changes to 'systemwide requirements' in the existing standard access agreement so they apply to amendments to the Operating Requirements Manual ... (Glencore, sub. no. 30: 11,12)*

Dispute process

In relation to the dispute process, stakeholder criticised a lack of clarity and fairness about the triggers to access the dispute process (Asciano, sub. no. 31: 5; Aurizon, sub. no. 33: 21; New Hope, sub. no. 32: 3). For instance, Aurizon said that disputes based on 'unfair differentiation' can lead to inefficiencies in relation to operator's supply chain over time (Aurizon, sub. no. 33: 21).

Asciano and Aurizon added that the proposed amendments suggested that all amendments made on safety grounds should be exempted from the dispute process. Both stakeholders said that only amendments made on 'urgent safety' grounds should be exempted (Asciano, sub. no. 31: 5; Aurizon, sub. no. 33: 21).

Furthermore, New Hope said that every material change to either the ORM or the online documents referred to in the ORM, that have a potential to affect the operator or their customers should be able to be disputed (New Hope, sub. no. 32: 3).

Liability

Stakeholders were collectively concerned that the lack of liability or consequences for Queensland Rail when it failed to comply with the ORM shifted risk to operators.

Aurizon said that Queensland Rail should be liable for its negligence or breach in relation to making amendments to the ORM or associated documents (Aurizon, sub. no. 33: 21). Asciano added that liabilities should be borne by whichever party is best able to control the risk and continues:

> *... Asciano believes that Queensland Rail's approach to indemnifying itself from any impact of amending the ORM (regardless of Queensland Rail negligence) continue to shift risk from the party which can best manage and control the risk. Queensland Rail should bear the risk of the consequences of amending its own document (Asciano, sub. no. 31: 5).*

QCA analysis and draft decision

Queensland Rail proposes to reduce its administrative obligations by placing the ORM on Queensland Rail's website. However, given that the document is online there is the potential that Queensland Rail may make amendments at its discretion.

In particular, Queensland Rail shifted the risk allocation towards the operator by allowing itself too much discretion in relation to making amendments, the dispute process and accepting liability for non-compliance.

Amendments

The QCA appreciates stakeholders' concerns that Queensland Rail does not propose to alert operators or their customers about every amendment to the ORM and related documents.

Indeed, Queensland Rail proposed not to consult with stakeholders about material changes or those relating to assets, equipment, facilities, infrastructure, processes, procedures or systems used for the purposed of any train management system for the purpose of improving safety, network capabilities, network capacity or system reliability.

Clearly these are matters which could significantly impact on the ability of operators to use the system and on their ability to fulfil the contractual entitlements of end use. Moreover, Queensland Rail proposed to, at its discretion, determine which operators will be affected by any change, and notify only these operators.

Consequently, there is a risk that Queensland Rail places obligations on operators and their customers without their knowledge or consent (particularly where Queensland Rail has failed to exercise its discretion properly and notify operators who should have otherwise been affected). Without knowledge of amendments, operators relinquish their right to veto such amendments, adversely impacting both themselves and their customers.

To improve transparency and restore an appropriate risk balance between Queensland Rail and the operators, the QCA recommends that Queensland Rail should notify all operators and their major customers of any proposed amendments.

It is also reasonable that operators be compensated for major amendments. Compensation can restore the risk balance between the two parties. This is because Queensland Rail would have to evaluate the costs and benefits of any amendment consideration to weigh up its overall benefits not only to Queensland Rail but also the operators.

If Queensland Rail has no obligation to compensate the operator for significant material financial impacts it has an incentive to implement a range of amendments just to increase its own revenue, decrease its costs or reduce its liabilities. This would shift the risk balance between the two parties in favour of Queensland Rail. Compensating the operator for such amendments will prevent Queensland Rail from implementing amendments at its own discretion.

The QCA recommends adopting an approach as outlined under cl. 5.10 of Aurizon Network's 2010 SAA, as the matter of compensation is consistent across both networks.

The 2010 SAA states that if a proposed amendment causes a significant net material financial impact of 1% or greater of the annual access charges directly as a result of the proposed amendments, both parties negotiate an appropriate financial agreement between them (QR Network, October 2010b: 56).

If both parties cannot come to a mutually agreed solution, it would then be open for parties to seek for the matter to be transferred to the QCA for dispute resolution. However, where amendments to the ORM are made on 'urgent safety' grounds, the QCA recommends that each party funds its own costs of implementing the proposed amendments.

Dispute process

The QCA accepts stakeholder concerns that the triggers of the dispute process lacked clarity and transparency and cannot work effectively. In particular, the QCA considers that restricting the dispute process to where it 'unfairly differentiates' between operators creates uncertainty.

For instance, there are a range of amendments that may not 'unfairly differentiate' one operator compared to another, but require all operators to implement amendments that are equally detrimental for all.

Given this, the QCA recommends that all amendments should be disputable, not only if they 'unfairly differentiate'.

However, for those amendments Queensland Rail considers where necessary, based on 'urgent safety grounds', it is reasonable to allow Queensland Rail to implement them, with any dispute still being able to be raised. This approach balances the need to make amendments on safety grounds with the rights of operators to raise concerns with the operation of the amendments.

Liability

The QCA also accepts that the liability provisions are imbalanced and do not place sufficient liability on Queensland Rail for its own actions. The QCA agrees with stakeholders that Queensland Rail proposes to be exempted of all liability for amendments to the ORM which Queensland Rail believed were in compliance, even if they were in fact not.

It is reasonable to expect Queensland Rail to know the grounds on which any amendment was made, but the QCA also accepts that mistakes can be made. Moreover, if Queensland Rail allows itself a 'good faith' provision, it should do the same for the operator, as rules should apply to both parties symmetrically, otherwise there will be a risk of imbalance in Queensland Rail's favour. However, this has not been proposed by Queensland Rail.

As an alternative, the QCA recommends that Queensland Rail's exemption from liability be narrowed and Queensland Rail should only be exempt for liability for amendments made in good faith, where they are limited to urgent safety based amendments.

Draft decision 4.8

- **The QCA requires Queensland Rail to amend its proposal so that the risk allocation between Queensland Rail and the operator is balanced. In this respect, the QCA requires Queensland Rail to implement the following amendments to its ORM:**
  - **(a) Queensland Rail should notify all operators and their major customers of any proposed amendments to the ORM.**
  - **(b) Queensland Rail should compensate the operator if a proposed amendment causes significant net material financial impacts of 1 % or greater.**
  - **(c) Queensland Rail should make all amendments disputable, not only if a proposed amendment 'unfairly differentiates' between operators.**
  - **(d) Queensland Rail should narrow its liability clause and limit the 'good faith' clause to urgent safety-related amendments.**

5 REPORTING (PART 5)

Reporting should allow access holders/seekers and their customers to form a view on the extent to which Queensland Rail is complying with the undertaking and the QCA Act.

The QCA proposes to largely accept Queensland Rail's proposed reporting on its network performance, its access negotiations and the way its regulatory accounts are developed. The QCA has, however, added some information requirements to reflect stakeholders' concerns, namely:

- *to extend Queensland Rail's proposed audit regime to allow the QCA to request a compliance audit of all aspects of the undertaking*
- *that Queensland Rail be required to report on the cost and scope of its maintenance activities and capital spending.*

5.1 Introduction

Public and regulatory reporting is a mechanism to provide Queensland Rail's customers with some level of confidence that it is not misusing its dominant position in the Queensland transport market. This reporting covers the broad activities undertaken by Queensland Rail, including:

(a) performance reporting ¬– provides assurance that Queensland Rail is not taking advantage of limited competition to provide a low level of service (see Section 5.2)

(b) access reporting – indicates whether Queensland Rail is acting reasonably and efficiently in negotiating contracts with customers (Section 5.3)

(c) cost reporting – informs access holders and their customers about costs, such as capital expenditure and maintenance (Section 5.4.1)

(d) regulatory accounts – guided by the costing manual, provides further information on the costs and revenue of the declared below-rail services provided by Queensland Rail (Section 5.4.2)

(e) auditing – helps customers to be confident about the accuracy of the reported information (Section 5.5).

Each of these aspects of Queensland Rail's proposed reporting obligations in its June 2013 DAU is discussed in turn below.

5.2 Performance reporting

The 2008 undertaking requires Queensland Rail to report quarterly on aspects of its operations, including on-time performance, speed restrictions and cancellations (2008 undertaking, cl. 9.1). The reporting is aggregated into coal and mineral services, freight services and long-distance passenger services.

Queensland Rail's 2012 DAU proposed to retain these reporting parameters, split between coal and non-coal (i.e. freight and bulk minerals) services. Stakeholders wanted Queensland Rail to provide more information by reporting performance on a system basis (Aurizon, sub. no. 9: 24).

Queensland Rail's 2013 DAU

Queensland Rail's 2013 DAU sought to address stakeholders' comments on its 2012 DAU by proposing to split its performance reporting between: the western system, North Coast, Mount Isa and all services outside those three systems (cl. 5.1.2(b)).

Stakeholders' comments

Stakeholders supported most of Queensland Rail's proposed reporting of operational matters, in particular the move to system-based reporting. However, they proposed the quarterly reports should also include greater information on the causes of operational constraints and cancellations (i.e. whether they were force majeure events or other issues) and what was being done to resolve issues in Queensland Rail's control (Glencore, sub. no. 29: 8).

Queensland Rail has proposed removing a number of documents from the undertaking and the standard access agreements and publishing them on its website. As discussed in Chapter 4 of this draft decision, the QCA is proposing to accept this approach provided that amendments to those documents have to be approved by the QCA if a stakeholder disputes the amendment. Stakeholders indicated that Queensland Rail should report on the number of disputes about these web documents, as well as about the application of the network management principles (Aurizon, sub. no. 27: 7).

QCA analysis and draft decision

Performance reporting should give access seekers/holders and their customers a good understanding of whether the rail network is being maintained and operated to the contracted standard. This can provide some level of assurance that Queensland Rail is not taking advantage of a lack of competition to provide a low level of service.

Queensland Rail's proposed approach to performance reporting in the 2013 DAU is largely consistent with the reporting regimes in the 2008 undertaking and in ARTC's interstate undertaking.

The QCA supports Queensland Rail's proposed system-based reporting as most of the performance measures (e.g. track condition and speed restrictions) affect all users of a particular system – and polluting those statistics with performance from other systems will not be particularly helpful for users interested in monitoring their own system.

Reporting of causes of performance issues

Stakeholders were broadly comfortable with Queensland Rail's proposed approach to reporting operational matters such as speed restrictions and cancellations. However, they said reporting should go beyond merely recording these outcomes – they wanted reporting on causes of changes in performance and on the measures taken to address areas of underperformance.

The QCA accepts that such reporting would allow access holders and their customers to assess whether they are receiving value for the access charges paid, which is a reasonable objective. In particular, reporting on the causes of significant changes in operating performance will help stakeholders assess whether the issues are largely beyond Queensland Rail's control, such as force majeure events, or are due to matters within Queensland Rail's control (e.g. maintenance). The QCA therefore proposes that the reporting include provision for discussing these causes.

However the level of performance, particularly for services without reference tariffs, is a matter for the access agreements negotiated between Queensland Rail and its access holders. The QCA therefore considers measures being taken to address area of underperformance should be

addressed through the terms of the access contracts. These issues can also be dealt with at user group meetings for individual systems, but the QCA considers that formal public reporting is not necessary to enable such discussions (see Chapter 7 on access agreements).

Reporting of complaints

Queensland Rail's 2013 DAU includes a new approach to dealing with some of the detail contained in the undertaking and the standard access agreements – i.e. some documents will be published on its website rather than included in the undertaking (see Section 4.7 of this draft decision). While removing unnecessary detail from the undertaking makes sense, it also introduces a risk to access seekers and holders if Queensland Rail removes or amends these documents in a way that significantly alters their rights or obligations.

To address this risk, there needs to be a proper process for amending these documents (see Chapter 4) and an associated disclosure regime so the QCA and current and prospective customers have a sense of whether there are a substantial number of complaints about the application of this new approach.

A number of the 'web documents' (e.g. the operating requirements manual and the interface risk management plan) can affect the way the network management principles are applied. In addition Queensland Rail has proposed a number of changes to the network management principles (see Chapter 4).

Clearly, the QCA will learn of significant issues in the event of formal disputes about how the network management principles are to be applied. However, neither the QCA nor third-party stakeholders will know about complaints that are resolved without resort to the QCA arbitration. Reporting on such disputes will help the QCA and stakeholders gain a better understanding of whether the overall operating regime is working effectively.

The QCA therefore requires that the quarterly performance reports be amended to include information on the number of operational complaints, including those about:

(a) the operating requirements manual and other documents Queensland Rail posts on its website that affect access-holders' access rights[19]

(b) the application of the network management principles.

Draft decision 5.1

- **The QCA requires Queensland Rail to amend its proposal so that its quarterly performance reports include information on:**
  - **(a) the causes of significant changes in operating performance**
  - **(b) the number of operational complaints by access holders, including those about**
    - **(i) Queensland Rail's operating requirements manual and related documents, and other documents Queensland Rail posts on its website**
    - **(ii) the application of the network management principles.**

[19] These other documents include the Interface Risk Management Plan, the Environmental Investigation and Risk Management Report, Rolling Stock Authorisation (see Chapter 4 of this draft decision).

5.3 Access reporting

The 2008 undertaking requires Queensland Rail to report annually on whether it has complied with the undertaking in various aspects of its access negotiation process, including the amount of time taken to respond to access requests, the average delay in responding to and providing indicative access proposals (IAPs), the average length of a negotiation period and the number of disputes – including those where it was found to be in breach of the undertaking.

Aspects of this reporting are also covered in the monthly breach reports, where Queensland Rail notifies the QCA of any breaches of the undertaking, including those in relation to access negotiations (e.g. exceeding the prescribed period for providing IAPs).

While Queensland Rail's earlier 2012 DAU largely maintained the 2008 undertaking's annual access reporting regime, it also included a number of deletions – including removing the requirement for monthly breach reports to the QCA. Stakeholders were critical of a number of Queensland Rail's proposed deletions. Queensland Rail addressed some, but not all, of these criticisms in its 2013 DAU. The unresolved matters are discussed below.

Queensland Rail's 2013 DAU

Queensland Rail has replaced the obligation to report on the average time to complete access negotiations with a proposal to report on the time taken for negotiations by breaking down the access agreements into those negotiated in less than three months, three to six months, six to 12 months, or more than 12 months (cl. 5.2.2(j) of the 2013 DAU).

Queensland Rail said it would not report on the average length of negotiation, as this provided little value to access seekers.

> *The length of a negotiation is not dependent upon the actions of the access provider alone, but also depends on the Access Seeker being ready to progress towards an Access Agreement (Queensland Rail, sub. no. 19: 19).*

Queensland Rail said its proposed reporting on access negotiations went beyond that in the ARTC Interstate Access undertaking, which did not contain a requirement to report on the negotiation process (Queensland Rail, sub. no. 19: 19).

Stakeholders' comments

Aurizon said there was value in reporting the time Queensland Rail took to issue an IAP in a manner similar to that Queensland Rail had proposed for the negotiation of access agreements (Aurizon, sub. no. 27: 13-14).

QCA analysis and draft decision

Access seekers and their customers are entitled to information that allows them to assess whether Queensland Rail is acting reasonably and efficiently in negotiating access contracts.

Queensland Rail has proposed a reporting regime in the 2013 DAU that is largely consistent with that in past undertakings. In addition, it has responded to requests from stakeholders by proposing to provide information on:

(a) the time taken to negotiate access agreements

(b) all matters referred to the dispute resolution process.

However, stakeholders have suggested that Queensland Rail's reporting on the time it takes to issue IAPs be changed from the average delay proposed in the 2013 DAU, to reporting in ranges, similar to its proposal for reporting on the overall negotiation period. This is a reasonable

suggestion that would provide consistent information to access seekers and would not be an onerous requirement on Queensland Rail.

The QCA therefore requires Queensland Rail to amend its provisions for the annual report on the negotiation process to include the time taken to issue IAPs, broken down into less than 10 business days, 10 to 20 days, 21 to 40 days and more than 40 days. This would replace the information on IAP timing provided in the 2008 undertaking's breach reports, albeit with a longer time lag, while reducing the reporting burden on Queensland Rail.

Furthermore, as discussed in Section 2.4 of this draft decision, the QCA considers that Queensland Rail should provide a similar report for the time it took in providing preliminary information and the time access seekers took in providing their intent to negotiate. Additionally, as discussed in Section 2.3.1 of this draft decision, the QCA considers that Queensland Rail should report the number of disputes arising in relation to the access application form and the operating plan template that Queensland Rail proposes to publish on its website.

Draft decision 5.2

- **The QCA requires Queensland Rail to amend its proposal so that its annual report on the negotiation process includes:**
  - **(a) the time taken by Queensland Rail to provide preliminary information and issue IAPs to access seekers, and by access seekers to provide their intent to negotiate, broken down into less than 10 business days, 10 to 20 days, 21 to 40 days and more than 40 days**
  - **(b) the yearly number of disputes arising in relation to the access application form and the operating plan template.**

5.4 Financial and cost reporting

The QCA Act includes a number of requirements about an access provider's financial disclosures, including that it must:

(a) provide tariff-related information (e.g. the costs of providing a service and the value of its assets) or provide a reference tariff (ss. 101(2)(b) and (c); s. 101(4))

(b) keep separate accounts for its declared service, in a manner approved by the QCA (s. 163). The Act gives the QCA the power to require a costing manual that sets out how those accounts will be prepared (s. 159).

The QCA's discussion of these requirements is divided into:

(a) tariff-related reporting, including maintenance costs and scope, for both reference and non-reference tariffs (Section 5.4.1)

(b) regulatory accounts and costing manual (Section 5.4.2).

Related matters are also considered in the discussions of pricing and tariffs (see Section 3.5 of this draft decision) and negotiation (see Section 2.3).

5.4.1 Tariff-related reporting

Schedule F of the 2008 undertaking includes mechanisms for developing and varying reference tariffs for the CQCR. It also includes ongoing reporting requirements for various costs and values that are used in deriving those tariffs, including:

(a) actual maintenance costs (cl. 9.2.3)

(b) changes to the regulatory asset base (cl. 9.2.4 and schedule FB)

(c) system volume forecasts (schedule F, cl. 3.1.2).

However, these reporting requirements related only to the CQCR. The 2012 DAU did not include any provisions for Queensland Rail to report on costs or assets, as it did not include any reference tariffs.

Queensland Rail's 2013 DAU

Queensland Rail's June 2013 DAU included proposed reference tariffs for western system coal services, a proposed mechanism for deriving those tariffs and a proposed approach to rolling forward the associated regulatory asset base to reflect new capital spending (see Section 3.6 and Chapter 8 of this draft decision). However, it did not propose ongoing public reporting on any of the inputs to the tariff during the term of the undertaking.

Stakeholders' comments

Stakeholders were concerned they had not received sufficient information during the 2008 undertaking period to properly assess the western system tariff proposal (Aurizon, sub. no. 43: 5-6, 30).

Glencore said it wanted separate reporting for the Mount Isa line, including on the maintenance activities actually conducted (Glencore, sub. no. 29, p. 8-9).

QCA analysis and draft decision

Reporting for reference tariffs

The QCA Act specifies that an access provider can give pricing-related information to an access seeker in the form of a reference tariff (s. 138(4)). However the QCA considers that, even where that information is reflected in an access price assessed by the QCA, customers are entitled to as much transparency as possible about how the tariff has been derived.

This entitlement is a natural justice issue – access holders and their customers should have sufficient information to understand the basis of a QCA decision on reference tariffs and form a view over the life of the undertaking whether the cost and volume forecasts were reasonable.

The reference tariff regime in central Queensland is supported with substantial disclosure about the asset base and forecast costs while prices are being assessed, and ongoing reporting about capital investment, maintenance and volumes during the course of an undertaking. The QCA considers that the western system reference tariff should include a similar reporting regime.

The QCA notes that the reporting needs to include information on both the cost and the scope of maintenance activities.

Draft decision 5.3

- **The QCA requires Queensland Rail to amend its proposal so that for systems with reference tariffs it reports annually for the relevant financial year on:**
  - **(a) maintenance costs of its system and scope of maintenance, compared with the maintenance forecasts used to develop the tariff**
  - **(b) operating expenditure, compared with the forecasts used to develop the tariff**
  - **(c) capital investment and a roll-forward of its regulatory asset base**
  - **(d) system volumes (broken down by type of traffic).**

Reporting for non-reference tariffs

Where there is no reference tariff, the QCA Act requires Queensland Rail to provide access seekers with information on the cost of providing below-rail services, including asset values, while they are negotiating access (see s. 101 of the QCA Act and Section 2.3 of this draft decision).

However, there is no ongoing obligation for Queensland Rail to report publicly on its activities once below-rail contracts have been signed.

While aspects of ongoing reporting can and will be covered by the terms of the access agreements, for a system shared by multiple access holders and/or end users, there is a range of ongoing information that is most useful and relevant on a system-wide basis (see Section 2.3 of this draft decision). The basic information required to form a view on costs per train path on a system is:

(a) total maintenance spending

(b) total operating expenditure

(c) total capital expenditure

(d) total volumes.

While different traffics will have different operating characteristics, this basic system-wide information will allow interested parties to address some of the information imbalance in forming a view on the incremental cost of providing their service. The QCA notes that this is similar to the reporting for a system with a reference tariff. This is reasonable, as users on such a system lack the protections that a reference tariff provides, yet still face information asymmetry.

Draft decision 5.4

- **The QCA requires Queensland Rail to amend its proposal so that for systems without reference tariffs it reports annually for the relevant financial year on:**
  - **(a) maintenance costs of its system and scope of maintenance performed**
  - **(b) operating costs of its system**
  - **(c) the capital investment in the previous financial year and expected capital investment over one and five years**
  - **(d) volumes, in train paths, net tonnes and gross tonne kilometres (broken down by commodity, where appropriate)**

  provided that, where a system includes multiple corridors, the reporting should include a breakdown by corridor, for all of the above categories of information.

5.4.2 Regulatory accounts and costing manual

The 2008 undertaking requires that Queensland Rail's network business publicly releases financial statements within six months after the end of the relevant financial year (cl. 9.2.1).

The 2008 undertaking also requires that Queensland Rail's financial statements separately identify the CQCR from the rest of the network and be developed in accordance with the methodology and format set out in the costing manual (cl. 3.2.1(a)).

Queensland Rail's 2012 and 2013 DAUs did not include any reference to the regulatory financial accounts. Queensland Rail said in its explanatory documents that the provisions in the QCA Act enabled the QCA to address both accounting separation and cost allocation and it did not consider it necessary to duplicate those requirements in the undertaking (Queensland Rail, sub. no. 2: 35).

Aurizon and Asciano said the regulatory accounts produced in accordance with the costing manual could help address the information asymmetry between Queensland Rail and its customers, although Asciano said this would be 'second best' compared with reference tariffs (Aurizon, sub. no. 27: 21; Asciano, sub. no. 26: 11).

Aurizon said this information should be provided at a corridor level, split between Mount Isa, North Coast, West Moreton (i.e. western system) and other. It said:

> *The benefit to operators of audited below rail financial statements is two fold: (i) they provide a level of certainty that there is no cross subsidisation of costs (relevant to QRail in relation to the passenger versus network businesses; and (ii) provide information on actual costs that in the absence of other financial information can be used to assess future access prices and risk regarding service levels (Aurizon, sub. no. 27: 21-22).*

Given that the regulatory accounts are governed by the QCA Act and that the costing manual gives the QCA the ability to specify how those accounts should be prepared, the QCA considers there is no need to duplicate this in the undertaking.

In this regard, the costing manual has already been amended to separate the costs for the western system from those for the rest of Queensland Rail's declared below-rail operations. The QCA is minded to require further amendments to the costing manual, consistent with that precedent, so that the regulatory accounts include a similar separation for the Mount Isa and north coast systems.

This should address stakeholders' concerns, without including provisions in the undertaking that govern how to prepare the regulatory accounts. The QCA will seek stakeholder comments on

Queensland Rail's proposed costing manual when it is submitted after the new undertaking is approved.

5.5 Certification and audit

The 2008 undertaking provides for audit and certification to give access seekers, access holders and their customers confidence that information provided by Queensland Rail is accurate and that Queensland Rail is complying with its undertaking.

The QCA can also require Queensland Rail to audit decisions made by Queensland Rail, if it 'has a reasonable basis for believing that a decision … has resulted or may result in a material adverse effect on an Access Seeker's or Access Holder's rights under this undertaking or an Access Holder's Access' (cl. 3.5.2(a) and 3.4).

In addition, the 2008 undertaking requires that the financial statements be certified by the chief executive (cl. 3.2.1(b) and 9.2.1).

The 2012 DAU proposed that the QCA would be able to request that Queensland Rail provide documents 'for the purpose of complying with this undertaking', but did not include any audit provisions (cl. 5.3.2). Stakeholders said the QCA should have the ability to audit Queensland Rail's compliance with its access undertaking, including audits of the quarterly and annual reports (Asciano, sub. no. 6: 15).

Queensland Rail's 2013 DAU

Queensland Rail's 2013 DAU provided that the QCA could require Queensland Rail to audit a quarterly or annual report if it believed that the information in the report was inaccurate in a material way (cl. 5.3.3(a)). The QCA would be able to publicly release an audit statement specifying whether or not the auditor found the information in the report was materially inaccurate, but it would not be able to publish the audit report which explained the conclusions in the audit statement (cls. 5.3.3(b)(vii) and (d)).

Queensland Rail's 2013 DAU also provided for:

(a) the chief executive of Queensland Rail to sign 'responsibility statements' for the performance and access reports (cls. 5.1.1(c) and 5.2.1(c))

(b) the QCA to request by written notice 'information or a document that the QCA reasonably requires for the purpose of complying with this undertaking' (clause 5.3.2).

In support of its submission, Queensland Rail said it had 'moved away from drafting a prescribed undertaking to a light handed approach similar to that of ARTC's Interstate Access undertaking'. It said the responsibility statement from the chief executive would 'provide stakeholders comfort that due diligence has been exercised in relation to the content of the reports' (Queensland Rail, sub. no. 19: 18).

Stakeholders' comments

Stakeholders said Queensland Rail's proposed audit provisions were insufficient and the 2013 DAU should be amended to give the QCA greater ability to audit both compliance and performance. This would include:

(a) giving the QCA the right to request audits of compliance with not just the undertaking, but also the QCA Act or an access agreement (Glencore, sub. no. 29: 10)

(b) requiring confirmation in the annual compliance audit that consistent arrangements have been offered to access seekers (Aurizon, sub. no. 27: 11)

(c) providing that performance audits cover not just inaccuracies in the quarterly and annual reports, but any conduct or decisions where Queensland Rail might need to comply with the undertaking (Glencore, sub. no. 29: 10; Aurizon, sub. no. 27: 21). Glencore said:

> *It is critical to the effectiveness of a regulatory regime that the regulator has sufficient mandatory information production powers to both assess compliance with the requirements of the undertaking and to determine how to exercise the powers the regulator has under the undertaking (Glencore, sub. no. 29: 10).*

QCA analysis and draft decision

Light-handed approach

Queensland Rail has called for a light-handed approach to regulating its declared infrastructure. The QCA considers this is a reasonable goal. However, any light-handed approach needs to be backed up with a regime of monitoring and investigation that gives access seekers, access holders, their customers and other stakeholders confidence the QCA will be able to discover and address conduct which is contrary to the QCA Act or undertaking.

The QCA therefore welcomes Queensland Rail's proposal to have a regime based on its chief executive taking responsibility for its quarterly and annual performance and access reports, supported by provisions for the QCA to require Queensland Rail to undertake compliance audits, or provide information and documents.

This chief executive certification should be a sufficient replacement for the annual performance audit regime in the 2008 undertaking that applies to Queensland Rail, but was developed for QR Network.

Investigation powers

Although certification is a good approach for Queensland Rail, the QCA agrees with stakeholders that the monitoring and investigation proposed in the 2013 DAU is not robust enough to support such a light-handed regulatory regime.[20]

In particular, the QCA considers its power to request audits should apply not just to the accuracy of the information in the performance and access reports, but to compliance with all provisions in the undertaking and the QCA Act (cl. 5.3.3(a)).

This will give the QCA investigation powers that, as Glencore said, enable it to both assess compliance with the undertaking and to determine how to exercise the powers it has under the undertaking (Glencore, sub. no. 29: 10). It would include the ability to require Queensland Rail to demonstrate that consistent arrangements have been offered between access seekers, should that be a concern.

The QCA also considers that Queensland Rail's proposed treatment of the audit reports is too restrictive, in that the only public document will be an auditor's opinion, with no useful background on how the auditor assessed the issue (cl. 5.3.3(d)).

The QCA considers this is not consistent with natural justice. Access holders and seekers and other interested parties should be able to understand how the auditor reached its conclusions. While this explanation could be less detailed than the audit report provided to the QCA, it needs to provide some of that information and background, subject to confidentiality considerations.

[20] While the QCA Act was amended in 2010 to give the QCA some powers to require information about compliance with an undertaking, this provides only for the regulated party to provide 'stated information' about its compliance (s.150AA). It does not provide for the QCA to require an audit of compliance.

Draft decision 5.5

- **The QCA requires Queensland Rail to amend its proposal so that the regulatory audit requirements:**
  - **(a) allow the QCA, acting reasonably, to require an audit of compliance with any aspect of the undertaking or QCA Act**
  - **(b) allow the QCA to publish a report from an auditor that includes not just the auditor's opinion, but also enough information on the audit process and conclusions for access holders and seekers and other interested parties to understand how that conclusion was reached.**

6 ADMINISTRATIVE PROVISIONS (PART 6)

The undertaking includes administrative provisions that should give access seekers/holders and their customers certainty on how Queensland Rail will give effect to its obligations in the undertaking.

The QCA proposes to accept Queensland Rail's structural changes to streamline the operation of administrative provisions. However, the QCA has requested amendments to clarify the dispute resolution process, and proposed that tariff-related reporting apply from the beginning of the tariff period, even though it is not required in the 2008 undertaking.

The QCA also proposes that the 'QCA decision-making principles' be removed from the 2013 DAU as they repeat requirements already included in the Judicial Review Act 1991 (QLD).

6.1 Background

The administrative provisions in Queensland Rail's 2013 DAU are broadly consistent with those contained in the undertaking, although they are now streamlined and consolidated in a single part of the undertaking (Part 6).

The consolidated provisions relating to notices are not controversial as they clarify the contents of a notice and how a notice should be given. The QCA's analysis in this chapter therefore focuses on Queensland Rail's proposed:

(a) dispute and complaint resolution process (Section 6.2)

(b) transitional provisions (Section 6.3)

(c) QCA decision-making processes (Section 6.4).

6.2 Dispute resolution

The 2008 undertaking establishes a three-step dispute resolution process that includes referral of a dispute:

> *first to the chief executive and, failing resolution, to either:*
>
> *(1) an expert, whose decision is final unless a party can demonstrate to the QCA there has been a 'manifest error', or*
>
> *(2) to the QCA.*

In the 2012 DAU, Queensland Rail removed the option of expert referral. Stakeholders objected as they considered using an expert would be more timely and cost effective (Asciano, sub. no. 6: 15; Aurizon, sub. no. 10: 10).

Queensland Rail's 2013 DAU

Queensland Rail's 2013 DAU provides for:

(a) Option 1:

  (i) referral to an internal organisational representative, and failing resolution referral to the Chief Executive of each party, and failing that

  (ii) referral to the QCA

(b) Option 2: parties to agree a different dispute resolution process.

Neither option includes explicit provision for referring a dispute to an expert (though parties could agree to this under Option 2 if they wished).

Stakeholders' comments

Aurizon was concerned that Queensland Rail's proposal allowed stakeholders to agree to expert resolution under Option 2 but that if either party was not satisfied with the outcome they could then seek dispute resolution by the QCA.

Aurizon said:

> *... the requirement to have the QCA, in effect as an intermediate to the resolution of the dispute, will add time and cost to the resolution of the disputes (Aurizon sub. no. 27: 20).*

QCA analysis and draft decision

The QCA accepts that parties should have the option to agree a dispute resolution process that best suits the dispute. For instance, parties should be free to elect for dispute resolution by an expert, particularly where the dispute is of a technical nature. This can reduce the time and cost of resolving disputes.

The QCA supports Queensland Rail's amendment that provides for parties to agree a dispute resolution process (i.e. Option 2 above). Under this option, parties could seek resolution by an expert or through alternative means.

However, the QCA is concerned that the 2013 DAU does not preclude a party subsequently seeking another dispute resolution process (including referral to the QCA) if they are not satisfied with the outcome of the dispute resolution process they initially chose. This creates uncertainty for the parties and can add time and cost to resolving any dispute.

The QCA notes that the 2008 undertaking provided for an expert determination to be final and binding, unless a party could demonstrate that there was a 'manifest error' (2008 undertaking, cl. 4.7.3(i)). The 2013 DAU should also provide for a binding outcome, apart from limited grounds for appeal similar to those in the 2008 undertaking.

Given this, the QCA requires that the 2013 DAU be amended to clarify that any upfront agreement by the parties on the relevant dispute resolution to be used is binding, and the parties cannot subsequently elect to change the nature or result of the dispute resolution process by bringing the matter to the QCA for reconsideration, except in a case of manifest error.

Draft decision 6.1

- **The QCA requires Queensland Rail to amend its proposal so that if Queensland Rail and an access seeker or holder select a particular dispute resolution option under the undertaking, that decision is binding, and the parties cannot subsequently elect to change the nature or outcome of the dispute resolution process, unless they appeal to the QCA on the grounds there has been a manifest error.**

6.3 Transitional provisions

Effective transitional arrangements help minimise delays in finalising access agreements as a result of the new undertaking coming into effect. This in turn can reduce parties' administrative costs and provides confidence that access seekers/holders are able to continue operations over a period that spans more than one undertaking.

The 2008 undertaking allows access seekers to elect to continue negotiations in accordance with key aspects of the 'non-pricing' provisions of the old undertaking even if a new undertaking becomes effective (2008 undertaking, cl. 2.5 (b)). This flexibility is granted, if access seekers made an access application under existing arrangements and received an indicative access proposal (IAP) before the commencing date.

The 2008 undertaking does not specify how reporting requirements will be managed during the transition from one undertaking to the next.

Queensland Rail's 2013 DAU

Queensland Rail's 2013 DAU proposes two key changes to the transitional provisions, namely that:

(a) all matters and negotiations that have started under the provisions of the 2008 undertaking have to be finalised under the 2013 undertaking once it has been approved

(b) regulatory reporting will be on the basis of the approved undertaking (i.e. for the period when the undertaking was in place the information to be reported will be the same as that required by the undertaking).

QCA analysis and draft decision

Transitional provisions are necessary to provide confidence to access seekers and their customers on how matters relevant during one undertaking period will be dealt with if they extend into the life of another undertaking. Access seekers need to know what provisions and undertaking applies at any point in time in their dealings with Queensland Rail so they can make informed business decisions.

There is an apparent asymmetry of approaches in when Queensland Rail would like the 2013 arrangements to apply (e.g. negotiations) and when the 2008 arrangements should apply (reporting).

Stakeholders' submissions did not comment on these matters.

Negotiating for access

The 2008 undertaking allows the access seeker who made an access application under pre-existing arrangements and received an IAP before the commencement date of the replacement undertaking to elect to continue negotiations in accordance with the 'non-pricing' provisions of the previous undertaking.

In contrast, Queensland Rail proposes that for matters that extend across the 2008 and 2013 undertakings, aspects of those matters will be deemed to have been done under the 2008 undertaking, while the remainder will have to be completed based on the provisions of the 2013 undertaking.[21]

The proposed amendment in the 2013 DAU reduces access seekers' flexibility to choose under which undertaking they wish to conclude negotiations. This may be particularly relevant where access negotiations are well advanced and where the approved 2013 undertaking is materially different from the 2008 undertaking. At the same time, the proposal simplifies things for

[21] The 2008 Undertaking included all the material terms of the 2006 undertaking, with the only changes being to reflect a restructuring of the then QR Ltd to make QR Network a separate but wholly owned subsidiary. The transitional provisions in the 2008 Undertaking therefore reflect the transition from the 2001 undertaking (i.e. the previous undertaking) to the 2006 undertaking (i.e. the replacement undertaking).

Queensland Rail as it will only have to finalise negotiations under one framework once the 2013 undertaking is approved.

Whether this particular proposal is more, or less, in the interests of Queensland Rail or access seekers/holders, will depend on the terms of the 2008 undertaking relative to those in the approved 2013 undertaking.

In the absence of stakeholder comments, it is not evident which is best. Accordingly, the QCA is inclined to accept Queensland Rail's proposal.

Operational reporting

Access seekers/holders are entitled to transparent information that allows them to assess whether Queensland Rail acts reasonably and efficiently, both within an undertaking period and across undertakings.

There are two aspects of Queensland Rail's reporting that are covered by the transitional provisions, namely requirements where:

(a) the reporting in the new undertaking will be broadly similar to that in the 2008 undertaking

(b) there is no equivalent reporting requirement in the new undertaking compared with the 2008 undertaking – e.g. reporting for western system and Mount Isa line access charges.

The QCA accepts that where the reporting requirements in the 2008 undertaking are broadly similar to those in the undertaking that replaces it, the previous reporting regime can apply for reporting periods that span the change to the new undertaking.

However, Queensland Rail's proposed transitional mechanisms in the 2013 DAU would not provide for reporting on matters such as actual costs, volumes and maintenance scope for the western system for the period from 1 July 2013 to the date the new undertaking commences, as the western system tariff is only being considered as part of the 2013 DAU process.

Stakeholders have a reasonable expectation to know how western system reference tariffs are derived and how Queensland Rail is tracking against forecast costs and other performance targets (see Chapter 8 of this draft decision).

The only tariff that the QCA has approved for the Queensland Rail network is for coal train services on the western system. Given this, the QCA proposes that transitional reporting, based on 2013 undertaking rules, should apply to the western system from July 2013. These additional reporting requirements for the western system are not intended to be open-ended but relate to specific information that should be readily available to Queensland Rail such as:

(a) actual maintenance costs and scope

(b) changes to the regulatory asset base

(c) system volumes

Tariff-related reporting is discussed in greater detail in Section 5.4.1.

Draft decision 6.2

- **The QCA requires Queensland Rail to amend its proposal so that it will provide tariff-related reports for the western system to access seekers, as set out in the 2013 undertaking, backdated to the start of the undertaking period, once the undertaking has been approved.**

6.4 QCA decision-making

Effective decision-making processes provide confidence to stakeholders that their views are being properly considered as part of the regulatory process.

If stakeholders consider their rights have not been reflected, they can challenge a decision based on principles established by common law and the Judicial Review (JR) Act 1991 (Qld) and provides for affected parties to challenge any decision of the QCA on the basis of:

(a) natural justice – including the ability to assess the information on which the decision-maker has based its conclusions

(b) an error of law – occurs when the decision-maker has misunderstood or misapplied a law

(c) not taking into account a relevant consideration

(d) taking into account an irrelevant consideration.

In addition, the 2008 undertaking provides for parties to challenge a decision of the QCA in developing standard access agreements (cl. 5.2) and establishing reference tariffs for new reference train services (cl. 6.4.2) that repeats cls. 21 and 24 of the JR Act.

Queensland Rail's 2013 DAU proposal

Queensland Rail has taken the clause from the JR Act that is included twice in the 2008 undertaking,[22] and placed it in the administrative provisions of the 2013 DAU. Queensland Rail has also altered the applications of grounds on which a decision of the QCA can be challenged so that it:

(a) applies more broadly to a decision by the QCA under the undertaking (rather than for two specific areas in the undertaking)

(b) only provides for the Queensland Rail to challenge a decision (i.e. it does not provide for an access seeker/holder to challenge a decision).

Queensland Rail said in the material accompanying the 2013 DAU that the clauses on the QCA's decision-making processes did not displace the JR Act, and that they did:

> *... not affect the right of any party to seek any other form of remedy or relief ... or to seek review under the [JR Act] (Queensland Rail, 2013 DAU, cl. 6.2(ix)(d)).*

QCA analysis and draft decision

The QCA accepts its decision-making process must be robust, and must be seen to be robust, so stakeholders can be confident that proper procedures and decision-making criteria have been applied and all relevant matters have been considered.

[22] The excerpt from the JR Act was included in the 2008 Undertaking as part of the process for QCA decisions requiring QR Network to submit a new standard access agreement (cl. 5.2) and reference tariff (cl. 6.4.2).

When the decision-making clauses went into the 2006 undertaking there was some uncertainty about the ability of parties to dispute a decision the QCA made under the undertaking:

(a) The QCA's view was, and is, that the undertaking is a statutory instrument so its decisions under an undertaking are subject to judicial review under the JR Act. Therefore, including these clauses in an undertaking is unnecessary as they reflect a right that already exists under the JR Act.

(b) QR Network [as it was at that time] did not accept that a QCA decision under an undertaking was subject to the JR Act and it was, therefore, left exposed as there would not be an appropriate appeal mechanism. It wanted the additional clauses included in the undertaking to address this perceived exposure.

(c) The QCA accepted QR Network's proposal to include these clauses as it addressed an uncertainty, so it is clear that the QCA's decisions are subject to judicial review in a way that is entirely consistent with the equivalent provisions in the JR Act.

Queensland Rail's proposed treatment of the clauses in the 2013 DAU has both expanded and narrowed the decision-making provisions.

The QCA remains of the view that these clauses do not need to be in the undertaking. However, if they have to be there to address a perceived exposure, they need to fully reflect all stakeholders' rights under the JR Act. In particular, Queensland Rail's proposed clauses are drafted as being solely for the benefit of Queensland Rail and do not cover the effect of decisions on other stakeholders, while the JR Act covers both.

Therefore, the QCA requires that the decision-making provisions be amended so that they apply to the effect on both Queensland Rail and other relevant parties.

Draft decision 6.3

- **The QCA requires Queensland Rail to amend its proposal so that the provisions on QCA decision-making apply to both Queensland Rail and other relevant parties (cl. 6.2).**

7 STANDARD ACCESS AGREEMENTS

An access agreement sets out the agreed terms and conditions for access to Queensland Rail's network. Clause 2.7 of the 2013 DAU says how an access agreement will be developed with schedule C summarising the principles to be included in an access agreement. Schedule F sets out the Standard Access Agreement (SAA) to apply to train operators carrying coal on the western system.

Access principles and the SAA are included in the 2013 DAU to guide access negotiations. Access principles are generally designed to reflect a reasonable allocation of risks between the access provider and seeker to achieve the underlying purposes of the QCA Act and to reflect the relevant provisions in the approved undertaking.

Queensland Rail and access seekers can develop, by mutual agreement, an access agreement that differs from the access principles and SAA. However, any access dispute considered by the QCA must be arbitrated in accordance with the QCA Act, schedule C and the SAA (as may be applicable).

Stakeholders have expressed concerns that the Queensland Rail's proposal is imbalanced and provides it with excessive discretions across a range of contracting matters.

The QCA notes that many of the contracting matters are common across both Queensland Rail and Aurizon Network and that these matters have been addressed in detail in the context of the 2010 Aurizon Network Access undertaking. In doing so, the QCA sought to appropriately balance the rights and responsibilities of the various parties.

Given this, the QCA's position is that Queensland Rail's proposed SAA and schedule C principles should be amended to be consistent with those contained in the 2010 Aurizon Network undertaking. The exception to this would be where there are differences in Queensland Rail's business and risk profile which require an alternative approach or where stakeholders are in agreement.

7.1 Background

The key commercial elements of the 2013 DAU are the access agreement principles and the SAAs. These elements identify the contractual commercial template through which Queensland Rail will provide access to its customers consistent with the approved undertaking. The access principles and SAAs have applied to all Queensland Rail's customers since 2001.

The access principles and SAAs attached to Queensland Rail's 2008 undertaking (as updated in 2010) are identical in nature and content to those for QR Network's 2006 undertaking. When the QCA approved the 2008 undertaking (updated in 2010) the only amendments made to the 2006 QR Network access undertaking were to reflect the corporate restructuring process which occurred prior to the privatisation of Aurizon in 2010. The QCA's approval of the 2010 updated amendments reflected the implementation of privatisation and the extension of the expiry date for Queensland Rail's undertaking. Accordingly, the 2013 DAU is the first regulatory undertaking process undertaken by Queensland Rail.

Queensland Rail's 2008 undertaking contained access agreement principles to be reflected in all access agreements (schedule E) and provided access seekers with two SAA templates. Depending on which entity wants to hold the access rights, the two SAAs were:

(a) operator access agreement – allows rail operators to acquire access rights on behalf of the end customer to provide a 'one-stop shop' rail haulage service to coal companies

(b) access holder access agreement – allows coal companies to acquire access rights and subcontract rail operations to a rail operator.

Queensland Rail used the QR Network SAA templates as a precedent for all access agreements outside of central Queensland. In particular, Queensland Rail's:

(a) executed western system coal access agreements are based on its 2008 SAA

(b) 2008 SAA mirrors Aurizon Network's 2006 SAA and all access agreements executed by Aurizon Network before September 2010 (these can be downloaded from the QCA's website)

(c) agriculture, livestock, containerised, coal and bulk freight access agreements mirror the front section of the 2008 SAA and differ only with respect to the schedules attached to the SAA. The different schedules simply particularise each access agreement relative to the specific needs of the industry accessing Queensland Rail's network (e.g. dangerous goods, livestock movements, mixed cargo freight and single freight traffics).

Aurizon Network's 2010 access undertaking included these two types of SAAs. While this regulatory process resulted in some amendments to the Aurizon Network SAAs, it largely reflected the underlying risk allocations in the 2006 and 2008 SAAs. In approving these arrangements the QCA's primary focus was in clarifying Aurizon Network's rights and obligations in negotiating access rights and providing an avenue for coal customers to negotiate access directly with Aurizon Network.

More recent developments

The 2010 access undertaking not only approved the old form of access agreements, but it also included requirements for a more flexible contracting structure. After some time this was ultimately reflected in the approved 2013 undertaking as a split form of access agreement (which embodies the principles included in both the pre-existing end user and train operator access agreements). The new form of SAA allows end customers and rail operators to hold different components of the same access rights for the coal being hauled. Contractually, it simply re-allocates the existing risk allocation matrix underpinning Aurizon Network's operator access agreement to the three parties to the new contract.

Queensland Rail's 2013 DAU

The QCA reviewed Queensland Rail's access agreement principles (Schedule C) and the operator SAA (Schedule F) in the 2013 DAU. The QCA has identified significant departures from the QCA's previously approved regulatory risk profile, access principles and SAA – let alone an attempt to provide the contractual flexibility that Aurizon Network agreed to as part of the split form of access agreement process.

Queensland Rail's proposed arrangements tilt the schedules in Queensland Rail's favour by:

(a) removing contractual responsibilities and obligations previously held by Queensland Rail in providing access services to access holders and seekers

(b) providing Queensland Rail with discretion to decide whether an access seeker has met the mandatory access obligations

(c) increasing the risks and uncertainty of the access rights held by an access holder

(d) reducing the commercial worth of the access rights held by an access holder (e.g. removing renewal rights).

These changes have been made without Queensland Rail adequately identifying why previously approved access agreement principles and SAA rights and obligations are no longer applicable in the context of the 2013 DAU.

QCA regulatory precedent

The QCA has considered the risk allocation matrix underpinning rail access agreement principles and SAAs over successive regulatory periods (2001, 2006, 2008 and 2010). In each process the QCA carefully considered any changes to the regulatory regime, amendments to the SAAs and all relevant submissions to seek to ensure the risk allocation matrix within the SAAs reflected the criteria in the QCA Act and the risk allocation matrix established in the relevant approved access undertaking.

The QCA considers that, as a general proposition, the allocation of risk is efficient when the risk is borne by the party that is best positioned to control and manage that risk. In developing the risk allocation matrix for both Queensland Rail and Aurizon Network access undertakings the QCA has previously considered the identification, assessment, analysis, and mitigation measures available and allocated the risks between the contracting parties. In Aurizon Network's 2010 access undertaking the QCA reconsidered the risk allocation matrix to seek to ensure to the extent practicable that risks were allocated to the party where the risk is within that party's control.

The QCA's approved risk allocation matrix in the 2010 Aurizon Network access undertaking resulted primarily in a symmetrical risk allocation with both parties being held responsible for risks within their immediate control. This symmetrical risk allocation is mirrored in each SAA developed by Aurizon Network, including the access holder agreement, the split form of access agreement and the connection agreement.

The application of a symmetrical risk allocation matrix is the most efficient contracting approach as it results in:

(a) lowest overall cost for access because neither party has to include cost contingencies for possible losses caused by another party's actions

(b) clear assignment of accountabilities between the parties

(c) alignment of contracting parties to the contractual obligations and entitlements

(d) open and transparent communication channels in the delivery of contracted access services

(e) minimal disputes between the contracting parties.

The QCA is of the view that Aurizon Network's 2010 access principles and SAAs are the most fully considered regulatory precedent in Queensland that appropriately balances risks and responsibilities between the parties. Given this, the QCA's draft position is that any Queensland Rail deviations from the provisions in Aurizon Network's 2010 undertaking must be fully considered by the QCA, consistent with the QCA Act. In particular, the QCA is looking for Queensland Rail to adequately demonstrate that there are sufficient reasons for specific cost and risk differences in its operations over the 2013 regulatory period to justify a change to the past arrangements.

7.2 Access principles

Access principles guide the development of access agreements by outlining how the key rights and responsibilities of Queensland Rail and an access seeker will be translated into contractual provisions in an access undertaking.

Access principles are contained in the undertaking which applies to Queensland Rail as well as the 2010 Aurizon Network access undertaking.

Queensland Rail's 2013 DAU

Queensland Rail's 2013 DAU stipulates that, in the absence of a relevant SAA, access agreements must be consistent with the undertaking and the access agreement principles in schedule C. As Queensland Rail has proposed a coal specific SAA, the access principles would apply to all other traffics.

Queensland Rail has proposed a set of access agreement principles to guide negotiations with access seekers. These principles are intended to underpin the development and execution of an access agreement and include:

(a) term – applies for a defined period and specifically excludes a right of renewal

(b) accreditation – an access holder's train operator must be accredited under Queensland's rail safety legislation but there is no specific requirement for Queensland Rail to be accredited

(c) access charges – to be agreed between the parties and may include an adjustment methodology

(d) network management – Queensland Rail is responsible for managing the network and can, at any time, impose operational constraints on the network

(e) train operations – access holder can only operate train services in accordance with the access agreement unless with Queensland Rail's prior written permission

(f) interface risk management – access holder must comply with its interface risk management plan and must advise of any non-compliance

(g) environmental and emergency management plan requirements – blanket prohibition on carriage of dangerous goods unless Queensland Rail gives its permission, acting reasonably. Access holders must comply with any Queensland Rail requirements necessary to prevent environmental harm, develop an emergency management plan and not cause any obstruction of the network

(h) noise mitigation – access holders must pay a contribution as reasonably determined by Queensland Rail to comply with statutory noise levels or limits or prudent practices as determined by Queensland Rail

(i) inspection and audit rights – will provide reasonable terms on which Queensland Rail can carry out audits of compliance by access holders

(j) risk and indemnities – access holder must indemnity Queensland Rail against all claims which may be brought against it by any party. The access holder must indemnify Queensland Rail for any loss arising from the carriage of any dangerous good. The access holder is responsible for all employees, agents and passengers on its train services

(k) limitation of liability – liabilities of the parties for default are limited and excluded as agreed in the access agreement. No parties are liable for consequential loss, except for

the access holder who remains liable if any third party makes a claim against Queensland Rail. Queensland Rail's liability is also excluded in relation to a list of matters and for any matter listed matter listed where liability cannot be excluded then the liability is limited to $1.00

(l) insurance – access holder will provide appropriate insurances to Queensland Rail;

(m) security – access holder will provide a security deposit as a bank guarantee on terms acceptable Queensland Rail. The security deposit can be increased or decreased in accordance with Queensland Rail's risk factors

(n) adjustments – access agreement will provide a mechanism for adjustments where there is an adverse financial effect on Queensland Rail. Queensland Rail may determine certain disputes

(o) disputes – access agreement will provide a dispute resolution process and identifies that any dispute referral to the rail safety regulator overrides the dispute resolution provisions in the agreement

(p) force majeure event – the obligations of both parties (other than monies payable) are suspended during a force majeure event. If part of the network is damaged, Queensland Rail is not obliged to repair or replace the infrastructure unless the parties agree as to which party will fund the work. An access agreement may be terminated in the event of a prolonged force majeure event

(q) reduction and relinquishment of access rights – access agreement will include provisions which allow Queensland Rail to reduce an access holder's access rights where they are being underutilised. It will also include provisions which allow an access holder to relinquish some or all of its access rights, subject to a fee payable to Queensland Rail

(r) assignment – Queensland Rail may assign or novate its rights and obligations under the access agreement without the consent of the access holder. The access holder can only assign or novate its access rights and obligations with the consent of Queensland Rail

(s) representation and warranties – access agreement may set out representations and warranties given by the Access Holder in favour of Queensland Rail.

Queensland Rail amended the 2008 schedule E principles in the 2013 DAU across most provisions. In doing so, Queensland Rail has generally removed references to its responsibilities and obligations and focused only on the responsibilities, obligations and liabilities of access holders. For example, for risks and indemnities, Queensland Rail required access holders to indemnify Queensland Rail against specific claims but did not provide a mutual indemnity to access holders. Likewise, Queensland Rail required inspection and audit rights of an access holder's compliance with the access agreement but did not provide a mutual right for access holders to inspect or audit Queensland Rail's compliance. In relation to network management, Queensland Rail has given itself potentially broad powers to impose operational constraints without consultation with access holders. In such cases Queensland Rail has removed any controls or procedures it must follow in implementing operational constraints on the network.

Stakeholders' comments

The majority of stakeholders (Asciano, Aurizon, QRC, Glencore and New Hope) all expressed concerns with the risk allocation matrix underpinning the access agreement principles in Schedule C.

The principles in Schedule C suffer from being so high level they provide no protections for access seekers. (Glencore, sub. no. 15: 10)

The complete exclusion of liability in relation to matters listed in 11.2 is unreasonable. For example, it would appear from the drafting that QR will not be liable if any 'thing carried by a train service' is lost regardless of the nature of QR's contribution to this event. This would include, for example, where QR was negligent, grossly negligent, or in breach of an agreement including where QR wilfully breached an agreement. (New Hope, sub. no. 31: 6)

Aurizon notes that the explanatory document does not provide a rationale behind the risk and indemnities. On the face of it, Q Rail is trying to exclude liability for absolutely everything under the agreement. (Aurizon, sub. no. 33: 41)

... Asciano continues to have concerns that an efficient liability and risk management regime should be based on the principle that the party that is best able to manage the risk should bear the risk (that is the party that is can control the cost of managing the risk bears the risk). This approach to establishing an efficient liability and risk management regime is not evident in the 2013 DAU. (Asciano, sub. no. 26: 10)

Stakeholder concerns with the access agreement principles centred on the removal of key risk and access protections provided in the 2008 undertaking. Stakeholders said that the proposed schedule C changes increased the risks and uncertainty for access holders, adversely impacted the value of the access rights held by access holders and left access seekers and access holders vulnerable to Queensland Rail exercising monopoly power in the negotiation of, or renewal of, an access agreement.

Stakeholders were particularly concerned that Queensland Rail proposed to:

(a) remove the right to negotiate in good faith a renewal for train operators who have invested significant capital in rolling stock and customers who have invested significant capital in mine assets, wholly reliant on access to the network (Glencore, sub. no.27: 5, Aurizon, sub. no. 27: 18; QRC, sub. no. 14: 5)

(b) remove Queensland Rail's specific obligation to maintain the network consistent with objective infrastructure standards and contractual entitlements (Glencore, sub. no. 30: 25, New Hope, sub. no. 31: 3, Peabody, sub. no. 34: 4; Asciano, sub. no. 7: 11-12)

(c) reduce certainty of access rights by giving Queensland Rail the ability to impose operational constraints and undertake works without consultation (Asciano, sub. no. 31: 6-7, Aurizon, sub. no. 33: 20, Glencore, sub. no. 27: 9-10; New Hope, sub. no. 31: 3-4)

    (i) reference to any relevant network management principles, service standards or interface coordination protocols

    (ii) consultation with access holders and end customers

    (iii) any recourse for access holders who experience significant disruption to train services

(d) remove and/or substantially amend the QCA's previously approved more symmetrical treatment of risks, liabilities, indemnities, insurance and assignment provisions (Asciano, sub. no. 31: 9-11, Aurizon, QRC; Glencore, sub. no. 30: 27-28 and New Hope, sub. no. 31: 3-6)

(e) impose a new indemnity provision on access holders in the access principles in relation to carriage of mixed goods train services which significantly increases the risk profile for rail operators and customers in haulage of dangerous goods (and QR proposes a blanket prohibition on the carriage of dangerous goods in the Standard Access Agreement) (Asciano, sub. no. 27: 8-9, Aurizon, sub. no. 33: 37; Glencore, sub. no. 30: 23-24)

(f) impose noise mitigation costs on an access holder/seeker with limited customer consultation and review (Asciano, Aurizon, and Glencore).

QCA analysis and draft decision

There are clear similarities between the commercial activities of Aurizon Network and Queensland Rail which are both monopoly below-rail access providers. Prior to the 2013 DAU, both Queensland Rail's undertaking and Aurizon Network's 2010 access undertaking contained identical access principles in schedule E of the relevant access undertakings. These access principles were consistently applied to all traffic types operating across Queensland's declared rail network.

The QCA considers that the access agreement principals outlined in Schedule E of Aurizon Network's 2010 access undertaking represent a more considered and balanced approach which provides a reasonable benchmark for the purposes of comparison and consideration, as well as being the 'current standard principles' that all stakeholders are familiar with. Whilst the QCA considers that there are benefits in retaining the current standard principles, it is prepared to consider differences in circumstances and risk that might justify Queensland Rail taking a different position as compared to the current standard principles or where there is consensus across parties. However, apart from a number of discrete issues (e.g. access renewal rights, dangerous goods, noise mitigation and risks and liabilities), Queensland Rail has not provided detailed reasoning for the extensive changes made to its proposed Schedule C of the 2013 DAU.

The QCA undertook a detailed review of the differences between Queensland Rail's proposed access agreement principles and the current standard principles. This review identified material differences in the risk allocation matrix underpinning Queensland Rail's access agreement principles compared to the current standard principles in the 2010 Aurizon Network access undertaking. At this stage, Queensland Rail has not adequately demonstrated why there are differences in circumstances and risk which should justify an alternative approach to that adopted by Aurizon Network.

The material changes have been grouped as follows and are addressed in turn:

(a) access renewal rights

(b) network maintenance obligations

(c) allocation of risks and indemnities

(d) limitation of liabilities

(e) dangerous goods

(f) noise mitigation

(g) treatment of remaining provisions.

Access renewal rights (cl. 1 of Schedule C)

Queensland Rail has expressly withdrawn the right for an access holder to negotiate in good faith to renew its access agreement on expiry. It is recognised that the provisions in cl. 2.7.3 of the 2013 DAU provides a limited right of priority for a 'Renewal Access Seeker' in certain circumstances where reference tariffs apply. Given reference tariffs only apply to western system coal traffics, any renewal right is limited to the coal industry.

The current standard principles have a provision for an access agreement to include a good faith negotiation process for the renewal of access rights.

It is not clear why Queensland Rail has excluded the right to negotiate in good faith for access holders. The removal places access holders at risk of Queensland Rail exercising monopoly power in access negotiations, particularly where reference tariffs have not been approved by the QCA. The change has an adverse material impact on:

(a) access holders, who make significant investments in rolling stock in anticipation of utilisation over an extended period

(b) end customers, who have sunk significant capital in brownfield mine operations or other facilities and whose commodities can only be transported to market by bulk freight trains

(c) access seekers, who have significant investment hurdles in establishing greenfield projects and require logistic certainty over the investment lifecycle.

Whilst the current standard principles do not guarantee renewal, a commitment to good faith negotiations provides less risk and more certainty for access seekers and access holders. Accordingly, the QCA recommends retaining the current standard principles' provisions for access rights, and including a good faith negotiation process for renewing access rights.[23]

The good faith provisions will mean that Queensland Rail is obliged to initiate access negotiations with access holders for access services two years prior to the expiry of an access agreement. If the access holder does not to take up the negotiation offer then Queensland Rail is free to negotiate with all access seekers for the capacity to be freed up on expiry of the access agreement. Chapter 2 outlines the access application process to be followed by Queensland Rail, including the treatment of access renewals and competing access requests.

Draft decision 7.1

- **The QCA requires Queensland Rail to amend its proposed access agreement principles to restore the access rights provisions (cl. 1) contained in Schedule E of the Aurizon Network 2010 access undertaking.**

Network maintenance obligations (cl. 5 of Schedule C)

Queensland Rail has significantly weakened its obligation with respect to maintaining the network and delivering contracted train services to an access holder. Queensland Rail has done this by proposing to:

(a) remove any reference to maintaining the network in accordance with agreed rolling stock interface standards

(b) give itself the right to impose operational constraints on the network at any time without access holder consultation and without taking into account the operational impacts on contracted train services

(c) remove the obligation on itself to use reasonable endeavours to minimise service interruptions on contracted train services

(d) require access holder to indemnify Queensland Rail against a number of claims which may be brought against it. In certain scenarios the access holder may be indemnifying Queensland Rail from claims arising from losses caused or contributed to by Queensland Rail

[23] See also Chapter 2 of this Draft Decision.

(e) exclude Queensland Rail's liability in relation to a broad list of claims and where liability cannot be excluded, Queensland Rail limits its liability to $1.00

(f) limit an access holder's claims for damages for the non-provision of train services in any access agreement, to situations where the access holder can show that the non-provision of a service was caused by Queensland Rail's negligence or a breach of the relevant access agreement.

In combination, all these elements of the access agreement principles remove or substantially weaken any obligations or liability Queensland Rail previously had in the undertaking to maintain the infrastructure consistent with objective engineering standards and to provide access rights consistent with contractual entitlements. This increased discretion would enable Queensland Rail to manage the network in a way which might minimise its own costs but leave an access holder bearing risks and uncertainty as to whether contracted services will be delivered within the term of the contract. This is an unacceptable risk profile for access seekers and access holders and could deter future entrants to the market.

In contrast, the current standard principles place responsibility on the access provider to manage and control the network consistent with objective rolling stock interface standards and to deliver contractual entitlements. The access provider may impose operational constraints for the protection of persons, property or to facilitate maintenance work. However, the access provider must use reasonable endeavours to minimise its service interruptions. The current standard principles also include:

(a) audit rights for access holders to inspect the rail infrastructure to ensure it is consistent with rolling stock interface standards

(b) the access provider being liable for the failure to maintain infrastructure consistent with the agreed rolling stock interface standards

(c) the access provider being liable for the failure to maintain infrastructure consistent with the agreed rolling stock interface standards.

Queensland Rail has not adequately explained or established reasons for significantly reducing its obligations to maintain the network. The proposed changes place access holders at significant risk that Queensland Rail may reduce or interrupt contracted service entitlements post execution of an access agreement and appear to leave access holders with limited, if any, recourse for failure to maintain. The changes may have an adverse material impact on access holders as they are required to bear the risk of, but have very little, if any, control over, Queensland Rail's delivery of contracted services. This also creates operational and commercial uncertainty for new entrants in particular.

The QCA believes Queensland Rail's maintenance and network management access principles inappropriately transfers risk on to access holders. As such, the QCA considers that Queensland Rail should restore the current standard principles' provisions on network and infrastructure management, maintenance obligations and the associated risk, indemnities and liability provisions with respect to Queensland Rail.

Draft decision 7.2

- **The QCA requires Queensland Rail to amend its proposed access agreement principles and restore the infrastructure management (cl. 6) and maintenance risk allocation provisions contained in Schedule E of the Aurizon Network 2010 access undertaking.**

Allocation of risks and indemnities (cl. 11 of Schedule C)

Queensland Rail has sought to fundamentally alter the risk allocation matrix with respect to risks and indemnities. The 2013 DAU proposes the access holder indemnify Queensland Rail against all claims brought against Queensland Rail and for all losses as included in the list in cl. 11(a)(i) to (vi). The list of claims captured by this clause covers a very wide and potentially overlapping range of claims which may arise over the life of the agreement. There is also potential for the various qualifications/exclusions in each sub-paragraph to overlap, creating uncertainty for access holders on how the provisions will apply.

Only the access holder is required to give indemnities. The access holder is also specifically held 'responsible' for all its employees, agents, consultants, customers and for the conduct of each passenger on the train.

In the current standard principles, each party indemnifies the other for loss (personal injury, death or property damage) caused by or to the extent contributed to by the wilful default or negligence of that party. In addition, under the current standard principles, an access holder is solely liable for and must indemnify Queensland Rail for any damage to property or personal injury or death of any person being transported on its train services (except to the extent that such harm is caused or contributed to by the wilful default or negligent act or omission of Queensland Rail or its staff).

An access holder is also required to extend any limitations or exclusion of liability under the terms of carriage (with customers) to Queensland Rail. There is also a provision obliging Queensland Rail to maintain the infrastructure is maintained to the specified standard.

Queensland Rail has not adequately explained or established reasons for changing the current standard principle's symmetrical risk allocation matrix with respect risks and indemnities. Relevantly, Queensland Rail's proposal moves away from the general risk principle that the QCA endorsed in the context of the 2010 Aurizon Network undertaking, namely that risks should be allocated to the party which can best manage that risk.

Queensland Rail's changes to the risk allocation matrix are material and adverse to access holders. At the same time, Queensland Rail has significantly reduced its risk profile without sufficiently identifying any material differences in circumstances and risk that might justify Queensland Rail taking a different position to the current standard principles. Accordingly, the QCA recommends Queensland Rail restore the risks and indemnities provisions contained in the current standard principles.

Draft decision 7.3

- **The QCA requires Queensland Rail to amend its proposal so that it deletes the risk and indemnity provisions in its access agreement principles and restore the risk and indemnity provisions (cl. 14) contained in Schedule E of the Aurizon Network 2010 access undertaking.**

Limitation of liabilities (cl. 12 of Schedule C)

Queensland Rail stipulates that the liabilities of the parties will be limited as agreed in the access agreement. The proposed access agreement principles then specify:

(a) that consequential loss is excluded from the indemnity provisions, except where arising out of a claim by a third party including a customer

(b) liability exclusions which are in Queensland Rail's favour and relate to a potentially wide list of matters, including

  (i) any loss of anything carried by a train service

  (ii) any matter for which an access holder bears or assumes risk or liability (including the access holder's representations and warranties)

  (iii) any act or omission by Queensland Rail in relation to notification requirements regarding environmental harm and other incidents and in relation to removing and rectifying obstructions

  (iv) any exercise of a right, or compliance with an obligation by Queensland Rail in accordance with the access agreement

  (v) any data collected in connection with train services

(c) that where Queensland Rail's liability cannot be excluded then liability is limited to $1.00.

These provisions provide increased risk and uncertainty for the access seeker and access holder. These provisions do not provide any incentive for Queensland Rail to seek to manage potential consequential losses for matters for which are within its control.

Exclusion of consequential loss from the indemnity provisions places the access holder in a worse position than Queensland Rail. This is because the indemnity is only given by the access holder and so leaves the access holder potentially liable for consequential loss where a third party has suffered loss and makes a claim against Queensland Rail. Moreover, the liability exclusions which favour Queensland Rail are widely drafted and potentially negate the intention of any other specific clauses (e.g. in the few instances where Queensland Rail excludes the access holder from liability, or where Queensland Rail may on general principles otherwise be liable, for losses caused or contributed to by Queensland Rail). The end result may be that Queensland Rail's risk for not complying with any of its obligations in an access agreement is either excluded or limited to $1.00 (i.e. it is negligible).

The current standard principles stipulate that the liabilities of the parties will be limited as agreed in the access agreement. However, in the current standard principles:

(a) neither party has any liability for consequential loss (except as otherwise provided)

(b) there are no other specific exclusions from liability for either party.

Under the current standard principles, each party remains liable to the other party for damages (including consequential loss) arising from the conduct of an audit or inspection or suspension

of train services if no reasonable person could have formed the view that the stated grounds for such an audit, inspection or suspension existed. Both parties are, however, subject to a specific duty to mitigate any losses arising from the conduct of an audit or inspection or suspension.

The current standard principles allocate risks in a more considered and balanced way as between Queensland Rail and access holders.

Queensland Rail has not adequately explained or established reasons for fundamentally changing the symmetrical risk allocation matrix in the current standard principles. Queensland Rail's position on the limitation of liabilities is heavily weighted in favour of itself. Its removal of any obligation to mitigate losses in the specified circumstances also exposes an access holder to potentially higher costs and risks. It is possible that the increase in commercial and contractual uncertainty for access holders could deter access seekers from entering the market.

Queensland Rail's changes to the risk allocation matrix are material and adverse to access holders. Accordingly, the QCA recommends Queensland Rail re-insert the limitation of liability provisions contained in the current standard principles.

Draft decision 7.4

- **The QCA requires Queensland Rail to amend its proposal so that it deletes the limitation of liability provisions in its access agreement principles and restores the liability provisions (cl. 15) contained in Schedule E of the Aurizon Network 2010 access undertaking.**

Dangerous goods (cl. 8 and 11 of Schedule C)

Queensland Rail has prohibited the movement of dangerous goods across its network except where an access seeker has Queensland Rail's prior written permission. To obtain written permission an access holder must satisfy Queensland Rail that the carriage of dangerous goods is compliant with any applicable laws, authorities and the Dangerous Goods Code and must ensure relevant authorisations are available for inspection. The access holder must advise Queensland Rail of any trains services carrying dangerous goods as soon as practicable and prior to the operation of the train service.

Queensland Rail treats dangerous goods differently dependent on whether the train service is a unit train service or a mixed goods train service. A unit train means the train service is hauling a single commodity (which may be 100% dangerous goods) and a mixed goods train service is said in the 2013 DAU to be any service which is not a unit train service. This would include a train which is hauling containerised freight, with some containers carrying dangerous goods. Queensland Rail treats the two types of train services differently:

(a) For a unit (i.e. coal) train service, Queensland Rail proposes that it only be liable for claims or losses that are caused or contributed by Queensland Rail's negligence.

(b) For a mixed goods train service, Queensland Rail proposes that it not be liable for any claim or loss arising from the carriage of dangerous goods regardless of cause. In this scenario, Queensland Rail only accepts liability for the part of a claim or loss that would have arisen regardless of whether the dangerous goods were being carried.

Queensland Rail also commissioned PwC to analyse Queensland Rail's approach to dangerous goods to the treatment of liabilities and indemnities for dangerous goods in the 2013 DAU. The

PwC report provided information in support of Queensland Rail's proposed treatment of dangerous goods.[24]

The QCA has considered Queensland Rail's proposed treatment of dangerous goods within the context of the risk allocation matrix underpinning the access agreement principles and the 2013 DAU. Of particular note for the QCA are the following:

(a) the weakening of Queensland Rail's maintenance obligations by removing any reference to objective rolling stock interface standards

(b) Queensland Rail's absolute discretion to impose operational constraints on train services without restriction

(c) Queensland Rail's failure to provide symmetrical indemnities to the access holder

(d) removing specific provisions intended to protect the access holder against the risk that network infrastructure may cause or contribute to an incident involving dangerous goods;

(e) Queensland Rail's exclusion from liability for a wide range of matters and where liability has not been excluded, Queensland Rail has limited its liability to $1.00.

In combination, the 2013 DAU Schedule C provisions places access seekers and access holders who carry dangerous goods (whether in a unit or mixed train), in a significantly and materially worse commercial position compared to existing access holders operating under access agreements negotiated consistent with Queensland Rail's undertaking. Queensland Rail's undertaking position on dangerous goods mirrors the dangerous goods provisions contained in Aurizon Network's 2010 access undertaking and the current standard principles.

Dangerous goods carried by unit trains

The current standard principles have no specific provisions relating to dangerous goods.[25] The risk allocation matrix in the current standard principles holds Aurizon Network liable for damage due to its negligence, regardless of whether dangerous goods are transported.[26].

The current standard principles provide a symmetrical and balanced treatment of indemnities:

(a) Relevant procedures for dangerous goods are captured under the definition of environmental harm. Environmental and safety interface plans cover risks, procedures and plans relating to dangerous goods, with access holders required to comply with all applicable regulatory laws, authorities and safety standards.

(b) Access holders indemnify the access provider (Aurizon Network) from any claims and losses relating to property transported by rail, except to the extent loss is caused or contributed to by the wilful default or negligent act or omission of the access provider.

[24] Queensland Rail's PwC submission, Treatment of Dangerous Goods - supporting analysis for submission to the QCA, 10 July 2012.

[25] The QCA considered treatment of dangerous goods in its review of Aurizon Network's 2009 DAU proposal to make the access holder liable for the carriage of dangerous goods, regardless of whether Aurizon Network was negligent or in wilful default. In the QCA's draft decision on the 2009 DAU, the QCA observed that the proposal was inconsistent with the general risk allocation principle that the party best placed to control a risk should be liable for that risk. In the 2009 DAU, for example (a) Aurizon Network was transferring a risk to the access holder which they were in no position to; and (b) Aurizon Network was well placed to take measures to protect against its own negligence and prevent its own negligence or wilful default.

[26] Aurizon Network 2010 access undertaking Schedule E, clause 14.

(c) The access provider has the benefit of the limitation of liability provisions applying to the terms of carriage as between the rail operator and the end customer. As a consequence of wider indemnity and liability provisions the access provider may be liable to the extent it caused or contributed to the loss.

There are also a number of provisions in the current standard principles which provide the means, through which Aurizon Network can control its risks with respect to the carriage of dangerous goods, including:

(a) Operational obligations (cl. 5) which specify the access provider and the access holder must comply with all laws/authorities, regulatory procedures and safety standards, including rolling stock interface standards

(b) Maintenance obligations (cl. 6) which require the access provider to maintain the network in accordance with objective rolling stock infrastructure standards and consistent with contractual entitlements

(c) inspection and audit rights (cl. 12) which provide the access provider and the access holder with rights to monitor, inspect and audit infrastructure or rolling stock to ensure compliance with all laws/authorities, regulatory procedures and safety standards, including rolling stock interface standards.

As identified, the general risk principle applied by the QCA in allocating risk is whether the risk is borne by the party that is in the best position to manage the risk. In the current standard principles, the QCA accepted some limitation on Queensland Rail's liabilities in relation to certain risks, including dangerous goods, where Queensland Rail did not cause or contribute to the incident occurring. Now, in the 2013 DAU, Queensland Rail is proposing, amongst other matters noted, to remove or substantially limit any liability for incidents where Queensland Rail may have caused or contributed to the incident.

This proposal is not consistent with the current standard principles because it transfers risks to access holders who generally are not the best placed or able to control these risks. For example, Queensland Rail is best placed to manage and implement measures to ensure its infrastructure will not cause or contribute to an incident involving a contracted train service.

Queensland Rail has not sufficiently demonstrated that it is appropriate for it to limit its liability in the transport of dangerous goods on unit trains. Accordingly, the QCA recommends Queensland Rail restore the dangerous goods, operational, maintenance and inspection provisions contained in the current standard principles of Aurizon Network's 2010 access undertaking.

Draft decision 7.5

- **The QCA requires Queensland Rail to amend its proposal so that it restores the operational, maintenance, inspection and liability provisions in the same way they apply to dangerous goods (cl. 5, 6, 12, 14 and 15) contained in Schedule E of Aurizon Network's 2010 access undertaking.**

Dangerous goods carried by mixed trains (cl. 11 of Schedule C)

In the 2013 DAU Queensland Rail has identified a number of issues to justify a different dangerous goods liability regime[27] for mixed trains compared to unit trains, namely:

(a) insurance costs – prohibitive costs to insure increases the cost of access when rail operators may more efficiently insure their operations

(b) information asymmetries – Queensland Rail is not necessarily aware of what goods are being carried on mixed trains when they are scheduled

(c) maintenance costs – the cost of maintaining a network to eliminate all risks of an incident are prohibitive and subject to diminishing returns in terms of effectiveness

(d) public interest – prohibitive costs of hauling dangerous goods will transfer the carriage risk to road transport.

At face value, the economic reasoning provided by Queensland Rail and PwC paper appears reasonable. However, the PwC report did not provide supporting evidence to substantiate the economic theory.

Many stakeholders raised similar concerns with the application of a different liability regime for dangerous goods carried by a mixed goods train services, including.[28]

(a) An incident involving a mixed train may be solely due to QR's breach of contract or negligence in failing to maintain the track to an appropriate standard consistent with rolling stock interface standards and contractual entitlements. In such cases Queensland Rail should be liable for all damages due to its negligence

(b) The removal of objective rolling stock standards leaves access holders vulnerable to internal management decisions on how much or less Queensland Rail maintains the track

(c) There is no flexibility regarding the different types of dangerous goods carried by access holders as some dangerous goods are not likely to cause contamination issues if an incident occurs.

The QCA's recommendation to restore the current standard principles with respect to dangerous goods means the reinstatement of a number of risk protections in favour of Queensland Rail with respect to dangerous goods being carried by mixed train services, including:

(a) Detailed risk interface, environmental management, obstructions and incident management plans required to be completed prior to commencement of access services should provide all necessary information, procedures and responses required with respect to dangerous goods

(b) Interface and environmental management plans require the access holder to advise Queensland Rail of the nature and type of dangerous goods being carried by mixed goods train services

(c) Liability in respect to maintenance practices are matters within the direct control of Queensland Rail

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[27] Queensland Rail's PwC submission, Treatment of Dangerous Goods - supporting analysis for submission to the QCA, 10 July 2012.

[28] Aurizon submission July 2012, Sept 2012, April 2013, May 2013, Asciano submissions July 2012, Sept 2012, April 2013, May 2013, Glencore submission, May 2013, QRC and New Hope submissions.

(d) Maintenance plans must be implemented to ensure the infrastructure is maintained to an objective standard and consistent with contractual entitlements

(e) Information with respect to the carriage of dangerous goods would be generally available to Queensland Rail during the negotiation of access agreements.

Accordingly, the QCA recommends Queensland Rail closely consider whether a different liability regime is required for mixed goods train services in light of the QCA's recommendation to restore the dangerous goods and liability provisions contained in the current standard principles. Where Queensland Rail considers material differences in risk and cost exist with a particular class of goods or particular quantity of goods for a mixed goods train service, then the QCA invites Queensland Rail to submit amendments to the current standard principles and provide supporting evidence to substantiate the changes based on cost and risk information. Stakeholders will then be given an opportunity to comment on the amendments through a QCA consultation process.

Draft decision 7.6

- **The QCA requires Queensland Rail to amend its proposal and restore the dangerous goods and liability provisions for train services (cl. 14 and 15) contained in Schedule E of Aurizon Network's 2010 access undertaking.**
- **The QCA invites Queensland Rail to propose a different liability regime for mixed goods train services and to provide supporting evidence to substantiate any proposed amendments based on cost and risk differences when compared to the liability regime for unit trains.**

Noise mitigation (cl. 9 of Schedule C)

In addition to requirements set down in the interface risk and environmental management provisions, Queensland Rail has included an obligation that an access holder must pay a financial contribution, as reasonably determined by Queensland Rail, towards any measures which Queensland Rail deem necessary to comply with 'Prudent Practices', noise levels or limits applicable. There is no caveat on Queensland Rail exercising its discretion in identifying the measures required, except that such measures must be considered necessary in accordance with Prudent Practices, or to comply with applicable laws. The Prudent Practices do not include objective criteria and Queensland Rail is only required to use reasonable endeavours to consult with an access holder before exercising its discretion.

The current standard principles do not contain a similar provision. The current standard principles focus on an access holder's compliance with 'Environmental Laws' which is broadly defined such that compliance with it includes, amongst other things, compliance with relevant regulations and guidelines in relation to noise mitigation. In respect of the risk allocation matrix, this places responsibility for environmental harm on the party who is best placed to manage the risks. In terms of noise mitigation, a rail operator is required to monitor its noise levels and ensure they are within acceptable environmental limits. This places the onus on the rail operator to implement efficient and effective measures to ensure noise levels are not exceeded.

It is not clear why Queensland Rail has changed the risk allocation matrix with respect to a rail operator's compliance with Prudent Practices and noise mitigation. Imposing the additional requirement on a rail operator to comply with Queensland Rail's discretionary interpretation of what Prudent Practices require in order to comply with noise mitigation levels imposes an additional burden (and uncertainty) on an access holder. The proposed wording does not

appear to provide any quantifiable benefit over and above a rail operator's direct compliance requirements with respect to its own accreditation. For example:

(a) An accredited rail operator carries the operational risk of its activities. Operators must comply at all times with prudent railway practices, regulatory approvals, authorities and safety standards or risk losing its accreditation

(b) The threat of losing its licence to operate a haulage business is sufficient incentive for a rail operator to comply with safety, regulatory, environmental and noise requirements.

The QCA recognises that cl. 9 of the proposed Queensland Rail access principles is similar in some aspects to cl. 8.4 of the Aurizon Network 2010 operator access agreement. The QCA considers cl. 8.4 provides a more objective approach and also allows independent dispute resolution without the uncertainty of whether the matter involves issues to be determined by Queensland Rail itself. Additionally, cl. 8.4 must be considered in the wider context of the Aurizon Network 2010 operator access agreement (including the symmetrical risk allocation matrix) rather than in isolation.

Accordingly, the QCA recommends Queensland Rail remove any specific reference to noise mitigation provisions and restore the environmental protection provisions (cl. 8) contained in the current standard principles in Aurizon Network's 2010 access undertaking.

Draft decision 7.7

- **The QCA requires Queensland Rail to amend its proposal so that it removes any specific reference to noise mitigation provisions and restores the environmental protection provisions (cl. 8) contained in Schedule E of Aurizon Network's 2010 access undertaking.**

Treatment of remaining provisions (entirety of Schedule C)

The risk allocation matrix underpinning the current standard principle is based on the general risk allocation principle that risk should lie with the party best positioned to manage the risk (to avoid or minimise the risk). Whilst this general risk principle has been applied as a base position in access negotiations, it is possible for both parties to agree to assume a different risk profile for commercial reasons.

Queensland Rail has fundamentally altered the risk allocation matrix embedded in the current standard principles to the material detriment of access seekers and access holders. Appendix D provides a detailed analysis of all the changes made with respect to the risk allocation matrix contained in schedule C of the 2013 DAU. As outlined in the discussion above, Queensland Rail has removed or minimised its liabilities and risks associated with providing a contracted access service to access holders.

The lack of appropriate levels of certainty and accountability in the provision of a service is unacceptable to stakeholders and also to the QCA (having regard to the objects of, and criteria in, the QCA Act). For reasons outlined above, the QCA is also concerned with the overall shift away from the more symmetrical and reasonable risk profile established across the terms of the current standard principles. Accordingly the QCA recommends Queensland Rail restore the entirety of the access agreement principles contained in the current standard principles in Aurizon Network's 2010 access undertaking.

Draft decision 7.8

- **The QCA requires Queensland Rail to amend its proposal so that it restores the entirety of the access agreement principles contained in Schedule E of Aurizon Network's 2010 access undertaking.**

7.3 Standard access agreement

Schedule F of the 2013 DAU provides a pro forma SAA to apply to train operators carrying coal on the western system network.

Queensland Rail's 2013 DAU proposal

Queensland Rail submitted one pro forma SAA with its 2013 DAU, namely the Operator Access Agreement which allows rail operators to acquire access rights on behalf of the end customer to provide a 'one-stop shop' rail haulage service to coal companies. Queensland Rail did not submit an Access Holder SAA with its 2013 DAU.

Clause 2.8 of the 2013 DAU provides the QCA with the ability to give Queensland Rail a notice requiring Queensland Rail to submit a proposed SAA that is for a specified type of train service not covered by the coal SAA and consistent with the access undertaking. If QCA serves such a notice, Queensland Rail is obliged to respond in the same way it would as if issued with a draft undertaking notice under the QCA Act.

Queensland Rail's draft 2013 DAU SAA applies to its western system coal traffics and is generally reflective of the revised access agreement principles contained in Schedule C of the 2013 DAU. The draft 2013 DAU SAA schedules specifically relate to the coal industry and the calculation of access charges is in accordance with the reference tariff schedule in Schedule A. Queensland Rail has explicitly stated the draft 2013 DAU SAA does not apply to the carriage of dangerous goods.

Stakeholders' comments

Stakeholders (Aurizon, sub. no. 9, 10, 27 & 33; Asciano, sub. no. 6, 7, 26 & 31, Glencore, sub. no. 15, 16, 29 & 30; New Hope, sub. no. 11, 12, 28 & 32) raised significant concerns with the SAA attached to the 2013 DAU. Particular concerns raised were:

(a) Implementation of the revised risk allocation matrix underpinning the access agreement principles means the draft 2013 DAU SAA is unfairly tilted in Queensland Rail's favour in relation to risk and potential liability.

(b) Lack of a split form of SAA enabling an end user to hold the access rights and a rail operator to hold the operating access rights to result in the contractual benefits, risks and liabilities being allocated to all parties connected with the provision of access, namely Queensland Rail, the rail operator and an end user.

(c) Demand for a non-coal SAA to provide a safety net for non-coal traffic and a reference point for the negotiation of access agreements in areas of the network not regulated by reference tariffs.

QCA analysis and draft decision

The QCA considers there should be a strong framework in the proposed 2013 DAU to support the development of SAAs since the terms and conditions of a SAA generally form the basis for access negotiations. Queensland Rail and an access seeker may agree to terms and conditions

that differ from the draft 2013 DAU SAA. However, in the event of an access dispute, the QCA is required to make an access determination consistent with the QCA Act and the approved access undertaking, which includes the draft 2013 DAU SAA.

SAA for coal traffic

In considering the access agreement principles contained in the 2013 DAU, the QCA recommended a return to the risk allocation matrix and principles contained in the current standard principles contained in Aurizon Network's 2010 access undertaking (see Appendix D). Similarly, with respect to the draft 2013 DAU SAA for coal traffic contained in the 2013 DAU, the QCA recommends Queensland Rail:

(a) generally adopt the drafting of the body of Aurizon Network's operator access agreement for coal traffic

(b) amend the draft 2013 DAU SAA schedules consistent with related QCA recommendations with respect to:

  (i) the reference tariff schedule A (see Chapter 8 of this draft decision)

  (ii) Operating Requirement Manual (ORM) (Section 4.7)

  (iii) Network Management Principles (NMP) (Sections 4.5 and 4.6)

  (iv) reintroduction of the process regarding potential changes to system wide requirements (defined as changes to the ORM and NMP) (Section 4.8).

This will ensure the draft 2013 DAU SAA directly reflects the QCA's recommendations with respect to the 2013 DAU's access agreement principles.

Draft decision 7.9

- **The QCA requires Queensland Rail to amend its SAA so that it is consistent with:**
  - **(a) Aurizon Network's Operator Access Agreement**
  - **(b) the QCA's recommendations on other aspects of the 2013 DAU.**

SAA treatment of dangerous goods

Aurizon Network's 2010 Operator Access Agreement contains provisions to manage the risks in the carriage of dangerous goods. The dangerous goods provisions reflect the access agreement principles recommended by the QCA in Section 7.2 above.

Clause 8.3 of Aurizon Network's Operator Access Agreement stipulates that if a train service is to carry dangerous goods, the rail operator must:

(a) ensure all requirements of the Dangerous Goods Code are fully complied with, including obtain any authorisation or prior approvals under the code (all approvals must be available for Aurizon Network to inspect)

(b) advise Queensland Rail of the details of the dangerous goods prior to the operation of the relevant train

(c) ensure all procedures for responding to an incident involving the dangerous goods to be carried are included in the operator's emergency response plan consistent with the interface and environmental risk management plans.

The QCA recommends that the dangerous goods provisions in Aurizon Network's 2010 operator access agreement be included in Queensland Rail's draft 2013 DAU SAA to apply in the event

that the non-coal traffics requests an SAA for use on the Queensland Rail's network. Should Queensland Rail develop a SAA for non-coal traffics, then the dangerous goods provisions can be removed from Queensland Rail's coal SAA.

Draft decision 7.10

- **The QCA requires Queensland Rail to amend its proposal so that it retains the dangerous goods provisions in Aurizon Network's Operator Access Agreement (cl. 8.3) in Queensland Rail's SAA to apply to non-coal traffics on its network.**

SAA treatment of insurance

Aurizon Network's 2010 Operator Access Agreement contains insurance provisions in cl. 13 and Schedule 7. In the drafting, cl. 13 refers to the rail operator obtaining insurance with a corporation licensed to conduct insurance business in Australia.

In Queensland Rail's 2013 DAU, Queensland Rail removed the necessity for insurance to be obtained from a corporation licensed to conduct insurance business in Australia. This position is reasonable and recognises the specific insurance issues raised by Asciano in its 2012 submission to the QCA. Specifically, Asciano advised Queensland Rail and the QCA of the difficulties in obtaining insurance for rail operations from an Australian insurer for the monetary amounts required by Queensland Rail (Asciano, Sept 2012).

Accordingly, the QCA recommends Queensland Rail amend cl. 13.1 of its SAA and remove any reference to an insurance company licensed to operate in Australia. Instead, the QCA recommends Queensland Rail adopt the insurance position that all rail operators must obtain insurance from an insurance company with an insurance financial rating of 'A' or better by Standard and Poor's rating, or, a rating which most closely corresponds to that rating by an agency or person which is recognised in global financial markets as a major ratings agency.

Draft decision 7.11

- **The QCA requires Queensland Rail to amend its proposal so that it uses an amended cl. 13.1 to enable rail operators to obtain insurance from an insurance company with an insurance financial rating of A or better by Standard and Poor's or, a rating which most closely corresponds to that rating by an agency or person which is recognised in global financial markets as a major ratings agency.**

SAA treatment of key performance indicators

Aurizon Network's 2010 Operator Access Agreement contains key performance indicator provisions (KPIs) in cl. 5.6 and schedule 5. In the 2010 Operator Access Agreement drafting, cl. 5.6 refers to the access provider complying with any KPIs contained in schedule 5. However, schedule 5 does not contain any KPIs. Rather schedule 5 identifies that KPIs will be agreed within 12 months of the commencement date.

Both Asciano and Aurizon identified the need for greater transparency around Queensland Rail's operations and more information on the interface between maintenance and service level standards being delivered by Queensland Rail (Aurizon, sub. no. 9, 10, 27 & 33; Asciano, sub. no. 6, 7, 26 & 31). Aurizon specifically recommended the inclusion of KPIs in schedule 5 which mirror the KPIs in schedule G of ARTC's 2008 indicative access agreement.

The QCA sees merit in including key network KPIs in Schedule 5 of draft 2013 DAU SAA. This would provide performance information to access holders and end customers and enable them to consider whether the service level standards are being maintained throughout the term of the contract.

In reviewing ARTC's approved 2011 access undertaking, the QCA believes both schedule G in ARTC's 2008 indicative access agreement and schedule D in ARTC's 2011 Hunter Valley access undertaking provides a starting point for the development of a list of performance measures to be used by access holders and end customers as a ready reference guide to gauge performance levels. Accordingly the QCA recommends Queensland Rail include a similar KPI schedule in its SAA which mirrors the KPI development in ARTC's 2011 access undertaking.

Draft decision 7.12

- **The QCA requires Queensland Rail to amend its proposal so that it adopts schedule D of the ARTC 2011 access undertaking for the KPIs for inclusion in schedule 5 of the SAA.**

SAA for non-coal traffics

In Queensland Rail's network, access rights are held by rail operators for the provision of bulk, general, containerised, agriculture and livestock freight tasks. Aurizon identified that only 20% of Queensland Rail's revenue is derived from coal traffics and the majority of revenue is generated from the other traffics on the network (Aurizon, sub. no. 33: 15). The implication is that for the majority of traffics on Queensland Rail's network, the SAA is unsuitable as the starting base for access negotiations.

Indeed, Queensland Rail itself highlights this uncertainty in relation to non-coal traffics in the 2013 DAU SAA by referring to it as only applicable to coal traffics. This leaves the majority of its customers reliant only on the access agreement principles and subject to the risk and uncertainty of how these principles would translate into a base contract.

This is of particular concern to the QCA because the majority of Queensland Rail's traffics are unregulated in terms of access charges. Access seekers and access holders seeking to renew access rights are particularly vulnerable in the 2013 DAU to Queensland Rail exercising monopoly power in the development of a base access agreement, particularly with respect to the allocation of risks and liabilities as between the parties.

The commercial viability of access agreements is a combination of both price and risk. In the unregulated parts of its business, Queensland Rail has significant monopoly power to pressure access seekers and access holders into trading off the QCA's approved risk allocation matrix for competitive access charges. Whilst such a trade could be a legitimate commercial outcome for both parties, the QCA is concerned to ensure that any trade-off is willingly entered into and not forced on an access seeker by Queensland Rail exercising its monopoly power.

The QCA's recommendation to restore the Aurizon Network 2010 access agreement principles will provide a level of regulatory confidence with respect to the appropriate risk allocation matrix required to underpin any non-coal access negotiations. Moreover, if any access dispute is triggered by either party in an access negotiation, the QCA will make a determination consistent with the risk allocation matrix embedded in the access agreement principles.

At the same time the QCA recognises there is stakeholder demand for a non-coal SAA. Under cl. 2.8 of the 2013 DAU, it is open to the QCA to formally request Queensland Rail develop a

non-coal SAA. In the QCA's opinion, a non-coal SAA would likely mirror the majority of the front body of the coal SAA, with changes to the schedules to reflect the different operating characteristics of train services and access charging frameworks required for non-coal traffics.

On this basis, the QCA recommends Queensland Rail review the draft 2013 DAU SAA and identify what clauses in the draft 2013 DAU SAA would not apply to non coal traffics. In this way non-coal access seekers can use the draft 2013 DAU SAA as the contractual framework for the negotiation of access rights across Queensland Rail's network. If this arrangement does not meet the needs of stakeholders then the QCA will consider issuing Queensland Rail with a cl. 2.8 notice to develop a non-coal SAA following finalisation and approval of the 2013 DAU.

Draft decision 7.13

- **The QCA requires Queensland Rail to amend its proposal to identify what clauses in the revised SAA do not apply to non-coal traffics.**

Split form of SAA

Queensland Rail indicated the absence of an SAA for access holders in the 2013 DAU is reflective of the fact that it has only executed operator access agreements since the commencement of regulation. Moreover, the inclusion of cl. 2.8 in the 2013 DAU enables the QCA to issue Queensland Rail with a notice to develop a new SAA where there is significant interest from access seekers within the term of the regulatory period.

Some stakeholder submissions (New Hope and Glencore) have requested that Queensland Rail develop a split form of access agreement similar to the agreements approved by the QCA in 2013.

The split form of access agreement takes the risk allocation matrix contained in the 2013 DAU and re-allocates the rights and obligations of access to the three parties to the contract, namely Queensland Rail, the rail operator and end customer. This form of agreement is appropriate for unit train services where the commodity or product carried by the train service is the property of one end customer. Whilst developed to meet the demand of the coal industry, such agreements are equally applicable to the movement of unit trains on Queensland Rail's network.

Given cl. 2.8 of the 2013 DAU, the QCA is prepared to consider issuing Queensland Rail with a cl. 2.8 notice to develop a standard split form of access agreement following finalisation and approval of the 2013 DAU. However, it is open to Queensland Rail to include a split form of access agreement in any new draft access undertaking submitted to the QCA.

Standard rail connection agreement

In the 2013 DAU, Queensland Rail identifies the need for parties to enter into a rail connection agreement in relation to projects which require the connection of private rail infrastructure to Queensland Rail's network. Cl. 2.6.2(b) of the 2013 DAU imposes an obligation on Queensland Rail to negotiate with an access seeker on the terms of a connection agreement. However the 2013 DAU is silent on the regulatory and contractual principles which would underpin the development of a connection agreement.

The QCA considered this issue as part of its Aurizon Network 2010 access undertaking deliberations. Clause 8.3 of Aurizon Network's 2010 access undertaking outlines the rights and obligations of all parties involved in the connection of private infrastructure to the regulated

network. Clause 8.4 requires Aurizon Network to develop a standard rail connection agreement within a specified timeframe. In 2013, the QCA approved a standard rail connection agreement covering connections to Aurizon Network's network. The rail connection agreement reflects the risk allocation matrix embedded in Aurizon Network's 2010 access undertaking.

A rail connection agreement is a fundamental component of a workable, viable and credible user funded investment framework. Whilst no stakeholders have requested the development of a standard connection agreement at this stage, the QCA recognises there may be a demand for such an agreement within the term of the next regulatory period.

Whilst pursuant to cl. 2.8 of the 2013 DAU, the QCA is able to issue an undertaking notice to Queensland Rail to develop a SAA. The drafting of this clause does not expressly allow the QCA to issue Queensland Rail with an undertaking notice to develop a standard rail connection agreement.

In anticipation of customer demand for a rail connection agreement in the future, the QCA recommends Queensland Rail:

(a) include a new section in its access agreement principles to mirror the rail connection access principles outlined in cl. 8.3 of Aurizon Network's 2010 access undertaking

(b) amend cl. 2.8 of the 2013 DAU to provide scope for the QCA to give Queensland Rail a notice requiring it to develop a SAA and/or proposed standard connection agreement that is consistent with the 2013 DAU.

Draft decision 7.14

- **The QCA requires Queensland Rail to amend its proposal so that it:**
  - **(a) includes a new section in its access agreement principles (Schedule C) to mirror the connecting infrastructure principles outlined in cl. 8.3 of Aurizon Network's 2010 access undertaking; and**
  - **(b) amends cl. 2.8 of the 2013 DAU to provide scope for the QCA to give Queensland Rail a notice requiring it to develop a SAA and/or proposed standard connection agreement that is consistent with the 2013 DAU.**

8 WESTERN SYSTEM TARIFF

The western system was originally constructed in the 1860s. Compared with central Queensland, the western system is not a heavy haul network – its volumes are low and its coal trains are short, have low axle loads and need to operate around the passenger services on Brisbane's metropolitan network.

The condition of the network and lack of economies of scale have meant that the western system coal tariff is relatively high. The 2013–14 tariff was $18.56/'000 gtk, which is around $8.21/net tonne, in contrast to $3.45/net tonne on the Goonyella system in central Queensland.

Queensland Rail's 2013 DAU proposed a tariff increase to $22.22/'000 gtk, which is partly based on an 82% increase in maintenance costs.

The QCA accepts that the western system is an old network that needs significant investment and maintenance to maintain current usage levels. Accordingly, the QCA proposes to accept most of Queensland Rail's claim for maintenance and operating costs. It also proposes to accept that all of Queensland Rail's proposed capital expenditure be included in the capital indicator for tariff calculation purposes.

Some stakeholders argued that this higher maintenance cost reflected the poor state of the network and that it should be valued accordingly. Others simply wanted a lower tariff. In support of these views, some stakeholders argued that as coal trains only started operating on the western system (i.e. from Wilkie Creek) in 1996–97, the tariff should reflect the value placed on those assets at that time, which was Queensland Rail's 'scrap value' from 1995.

The QCA's June 2014 consultation paper sought to address these comments by including two pricing options:

- *'historical cost' option – $13.59/'000 gtk, that placed a zero value on the pre-1995 assets*
- *'revised DORC' option – $17.21/'000 gtk, that adjusted the 2009 valuation to reflect an updated assessment of the network's condition.*

The QCA received detailed responses on its consultation paper indicating that stakeholders continued to have quite different expectations on the future tariff. In effect, Queensland Rail argued that the tariff generated by revised DORC option was too low whereas others said that the tariff under the historical cost option was high.

In reviewing those submissions and making this draft decision, the QCA accepts that the two tariff options in the consultation paper have shortcomings. Many of the pre-1995 assets remain relevant for operating coal services today. Yet, at the same time, access seekers should not be asked to pay for assets that are already fully life expired.

Accordingly, the QCA has set aside the historical cost option and has reviewed the revised DORC option. The QCA now proposes to provide a zero value on assets where the asset's actual life has extended past its regulatory life (e.g. 100 years for tunnels).

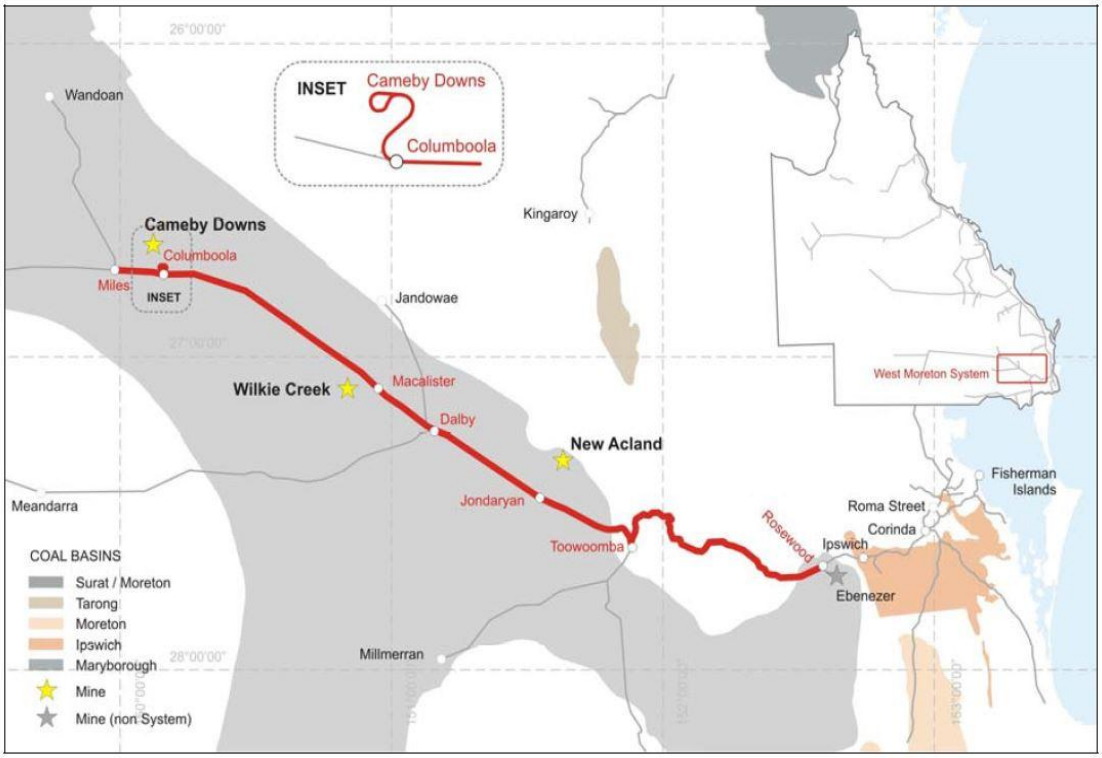
Along with other proposed changes, this draft decision proposes a western system tariff of $14.29/'000 gtk for 2013–14, which is around $7.16/net tonne.

8.1 Background

Queensland Rail owns and manages the entire rail network in Queensland, apart from the tracks in central Queensland owned by Aurizon Network Pty Ltd. One part of that network is the western system that was originally constructed in the 1860s to connect Brisbane to the agricultural districts of the Darling Downs.

Export coal rail services from the Darling Downs coalfields west of Toowoomba began in 1996–97 when a mine, developed at Wilkie Creek, began railing using the Macalister loading point. Coal exports through Brisbane had previously begun in the early 1980s, from mines near Ipswich, but the haulage was entirely within the metropolitan system east of Rosewood, and therefore did not use the western system (see **Figure 6**).

Figure 6: Western System Map



Queensland Rail's Proposal

The 2013 DAU proposed a western system reference tariff of $22.22 per '000 gtk be applicable from 1 July 2013. The proposed tariff is 20% higher than the $18.56/'000 gtk tariff applying at that time. This increase is largely driven by:

(a) a revised DORC valuation of the western system assets of $419.6 million

(b) an increase in the allocation of the:

  (i) the pre-1995 capital asset base to coal services from 60.5% to 61.7%

  (ii) most post 1995 capital expenditure on the western system to coal services from 75.6% to 100%

(c) an 82% increase[29] in maintenance costs to $104.5 million

(d) an over 60% increase[30] in the operating cost allowance to $23.5 million

(e) a decrease in the freight traffic blackout period on the metropolitan network from 20% to 15%.

Queensland Rail's proposed weighted average cost of capital (WACC) was based on the inputs used to derive Aurizon Network's WACC in its 2010 undertaking, with only the time-variant components adjusted (i.e. the risk-free rate and the debt margin). Volume estimates were based on contracted volumes.

Stakeholder and QCA initial analysis

Stakeholders disagreed with many aspects of Queensland Rail's proposal and argued that the proposed tariff was significantly higher than coal rail tariffs elsewhere (Yancoal, sub. no. 47: 1-2, Peabody sub. no. 45: 1-2).

On 6 June 2014, the QCA released its western system consultation paper that summarised stakeholders' initial views and provided preliminary estimates of the effects of those views on a western system coal tariff. In doing so, it sought to facilitate further stakeholder discussion on the appropriate approach to western system pricing.

Aurizon and three coal industry customers (Bentley, New Hope and Yancoal) made submissions in response and maintained the view that the tariff was too high and that the high maintenance costs indicated that the network was not fit for the purpose of carrying coal traffics. Conversely, Queensland Rail maintained that its tariff of $22.22/'000 gtk was appropriate in light of its legitimate business interests, including the right to earn an adequate return on its investment.

Given the building block model the QCA uses to assess tariff proposals, this chapter addresses both the efficiency of the costs included in that model and the way those costs are converted into a tariff estimate:

(a) maintenance and operating costs (Section 8.2)

(b) the regulatory asset base and regulatory return (Section 8.3)

(c) the approach to the tariff (Section 8.4).

8.2 Maintenance and operating costs

8.2.1 Maintenance costs

Queensland Rail estimated total maintenance costs of $104.5 million for the period 2013–14 to 2016–17, for the western system extending from Rosewood to Columboola.[31]

Queensland Rail allocated around 90% of this to coal traffics based on forecast gtks and used the resultant $95.2 million ($89.1 million in June 2013$) maintenance costs to derive the

[29] By comparing maintenance costs for the Rosewood to Macalister section (see section 8.2.1 of this draft decision).

[30] By comparing operating costs for the Rosewood to Macalister section (see section 8.2.2 of this draft decision).

[31] For presentation purpose, we use Columboola as the western end of the western system, recognising that it actually extends 15 km west of Columboola to Miles.

western system coal tariff for the 2013 DAU regulatory period (Queensland Rail, sub. no. 36: 17-18).

Queensland Rail said its proposed maintenance costs were significantly more [around 82% higher[32]] than those approved in the QCA's December 2009 draft decision, which reflected its intensive maintenance program to ensure service reliability on a poor condition network (Queensland Rail, sub. no. 38: 4-6, 44).

Stakeholders said, in their submissions on the 2013 DAU, that the maintenance costs were inflated and reflected inefficiencies and wanted the QCA to assess them for prudency (New Hope, sub. no. 44: 19-20; Aurizon, sub. no. 43: 36).

The QCA's consultant B&H observed that the western system was one of the most difficult railways in Australia to maintain because it was not designed as a heavy-haul freight railway and identified that:

(a) just over half the total maintenance costs (i.e. $53.3 million of the $104.5 million) reflected usual maintenance activity and were comparable with benchmarks from other jurisdictions

(b) the remaining half (i.e. $51.2 million) was associated with activities (e.g. mechanised resleepering) that were necessary to improve the standard of the existing infrastructure to compensate for its poor state, noting that those activities were more of a maintenance nature (B&H, May 2014: 15, 26-27).

On that basis, B&H accepted as reasonable most of Queensland Rail's proposed maintenance costs. The only exception was a portion of the proposed mechanised resleepering costs. B&H observed that Queensland Rail's proposed resleepering unit rate ($346 per sleeper) was excessive compared with rates observed in other jurisdictions and recommended adjusting it down to $200 per sleeper. B&H also observed that Queensland Rail's maintenance activities were not informed by any coherent business strategy and that resulted in inconsistent maintenance standards and potentially wasteful activities (B&H, May 2014: iv-vi, 7-9).

In its June 2014 consultation paper, the QCA accepted that the nature and condition of the western system mean that maintenance costs are higher than would normally be expected on a new, modern network configured for coal traffics. Given this, the QCA accepted B&H's assessment that the majority of Queensland Rail's maintenance costs (90%) should be approved to ensure that the system remains functioning and can cater to coal traffics. That said, the QCA proposed to reduce the mechanised resleepering costs by $10.0 million, thereby accepting B&H's assessment. This gave a total maintenance cost of $94.5 million for the western system as a whole (i.e. from Rosewood to Columboola) (QCA, June 2014: 26).

The QCA accepted Queensland Rail's proposed gtk-based allocator for apportioning total maintenance costs to coal traffic in the Rosewood to Macalister and Macalister to Columboola sections. That gave a coal-specific maintenance cost allowance of $86.0 million ($80.7 million in June 2013$) for deriving the western system reference tariff for the term of the 2013 DAU (QCA, June 2014: 26).

[32] By comparing maintenance costs (in June 2013$) for the Rosewood to Macalister section, which works out to $81.7 million over the term of the 2013 DAU compared with $44.8 million over the term of the existing undertaking.

The QCA noted B&H's observation about the lack of a coherent business strategy in Queensland Rail's maintenance program and proposed that Queensland Rail should report annually on actual versus forecast maintenance costs and activities (QCA, June 2014: 26).

Stakeholder submissions

Bentley did not support the level of QCA's proposed maintenance costs and said that Queensland Rail had not sufficiently justified the significant increase in its proposed maintenance costs. Rather, Bentley suggested that 'a modest increase in expenditure to that of the last undertaking period be applied' (Bentley, sub. no. 49: 4).

On mechanised resleepering costs, New Hope accepted the QCA's proposed downward adjustment stating that 'the analysis undertaken by B&H has sufficient rigour and professionalism to be relied upon by the QCA' (New Hope, sub. no. 50: 10).

However, Queensland Rail said the QCA's proposed mechanised resleepering costs were based on flawed assumptions. Queensland Rail said that it 'recently' undertook a detailed review of the mechanised resleepering costs for the western system and identified cost efficiencies through better coordination of that activity between the western system and nearby non-coal systems. Accordingly, Queensland Rail suggested a lower mechanised resleepering unit cost (Queensland Rail, sub. no. 51: 3, 21-22).

On the nature of maintenance activities, New Hope said that costs incurred to make the western system suitable for a 'heavy-haul' purpose should be treated as capital expenditure and recouped over future periods (New Hope, sub. no. 50: 10). Aurizon said that the majority of the mechanised resleepering activity was proposed between Toowoomba and Columboola, which should be capitalised as its benefit was anticipated to last beyond the term of the 2013 DAU (Aurizon, sub. no. 48: 31-32).

QCA analysis and draft decision

The QCA maintains its position in the consultation paper that the majority of Queensland Rail's proposed maintenance expenditure needs to occur given the nature and condition of the western system.

However, the QCA proposes to retain its adjustment for mechanised resleepering costs. While Queensland Rail advised that it undertook a review of these costs, this review was not provided to the QCA nor did Queensland Rail provide further information to justify its original resleepering costs (B&H, May 2014: 7-8).

That said, the QCA notes that B&H recommended a 2013$ unit rate for the resleepering program whereas Queensland Rail proposed undertaking that activity in the last two years of the regulatory period (i.e. 2015–16 and 2016–17). That requires escalating the 2013$ unit rate with forecast CPI giving a nominal unit rate of $213 for 2015–16 and $218 for 2016–17. This means that Queensland Rail's proposed mechanised resleepering costs should be reduced by $9.0 million (instead of the $10.0 million reduction proposed in the QCA's consultation paper).

Thus, the QCA proposes a total maintenance cost allowance of $95.5 million for the western system as a whole (i.e. from Rosewood to Columboola), which is 91% of Queensland Rail's proposed costs of $104.5 million.

Applying the gtk-based allocator gives a coal-specific maintenance cost allowance of $87.0 million ($81.5 million in June 2013$) for deriving the western system reference tariff for the term of the 2013 DAU.

On the nature of maintenance activities, the QCA accepts that the same activity (e.g. mechanised resleepering) may be treated as either maintenance or capital expenditure, depending on the circumstances. In this case, the QCA is inclined to accept B&H's view that such activities are maintenance in nature and required to compensate for the poor state of the network.

The QCA understands that the benefit of network strengthening activities is likely to last beyond one regulatory period. At the same time, the QCA considers that those costs should be borne by users that have triggered the need for such activities. Therefore, on this occasion the QCA accepts Queensland Rail's proposed activities as maintenance.

8.2.2 Operating costs

Queensland Rail said the operating cost allowance approved in the QCA's December 2009 draft decision was no longer appropriate for the western system, following the separation of QR Limited into Aurizon and Queensland Rail (Queensland Rail, sub. no. 36: 19).

Rather, Queensland Rail used a total operating cost allowance of $23.5 million ($22.3 million in June 2013$) to derive the western system coal tariff for the 2013 DAU regulatory period[33] that was calculated by, among others:

(a) escalating with CPI the operating costs reported in its 2011–12 below-rail financial statements

(b) reducing the escalated costs by applying a glide path to efficiency that accounted for its planned efficiency improvements over the term of the regulatory period

(c) allocating the resultant costs to coal traffic in the Rosewood to Macalister and Macalister to Columboola sections by applying section and coal train path allocators (Queensland Rail, sub. no. 36: 20-21).[34]

Stakeholders said in their submissions on the 2013 DAU that Queensland Rail's proposed operating cost allowance was inefficient and was higher than would be expected from an efficient service provider. They specifically said that Queensland Rail's yearly train control costs of over $3 million were excessive (New Hope, sub. no. 44: 20; Aurizon, sub. no. 43: 37).

The QCA in its consultation paper considered that Queensland Rail's 2011–12 costs were inefficient and therefore proposed to reject operating cost allowance based on those costs. The QCA also proposed to reject Queensland Rail's glide path to efficiency in large part because Queensland Rail is yet to demonstrate that it has a business plan for delivering efficiency improvements (QCA, June 2014: 29).

The QCA considered that a better basis for establishing an allowance for operating costs should be the more recent data from Queensland Rail's 2012–13 financial statements. The QCA largely accepted operating costs in the 2012-13 financial statements but with train control costs adjusted downward to $2.0 million from $2.8 million to reflect efficient costs as recommended by B&H (QCA, June 2014: 29-30).

[33] Queensland Rail's proposed operating cost allowance is around 64% higher – by comparing coal-specific operating costs (in June 2013$) for the Rosewood to Macalister section, which works out to $20.7 million over the term of the 2013 DAU compared with $12.6 million over the term of the existing undertaking.

[34] Queensland Rail proposed allocating operating cost between different western system sections based on 50% train kilometres (tkms) and 50% gross tonne kilometres (gtks) and between coal and non-coal traffics based on train path allocations.

The QCA accepted Queensland Rail's proposed allocators for apportioning operating costs to coal traffic in the Rosewood to Macalister and Macalister to Columboola sections (QCA, June 2014: 30).

The QCA ultimately proposed an operating cost allowance of $20.4 million ($19.2 million in June 2013$) for the western system for the term of the 2013 DAU, that was 13% lower than Queensland Rail's proposed allowance of $23.5 million (QCA, June 2014: 30).

Stakeholder submissions

New Hope supported the QCA's proposed operating cost allowance, including the downward adjustment to Queensland Rail's train control costs. New Hope also supported the QCA's position to reject Queensland Rail's glide path proposal, noting that the western system users should not bear the costs of Queensland Rail's inefficiencies (New Hope, sub. no. 50: 11).

Queensland Rail accepted that the 2012–13 financial statements were an appropriate basis for estimating the operating cost allowance (Queensland Rail, sub. no. 51: 25).

However, Queensland Rail did not support the QCA's proposed downward adjustment to train control costs. Queensland Rail said 'the QCA's consultation paper fails to take account of Queensland Rail's true train control costs, adversely affecting its ability to achieve adequate cost recovery' (Queensland Rail, sub. no. 51: 3).

Queensland Rail said that the western system's standard and operating characteristics created a more labour intensive approach to train control relative to other rail networks. Accordingly, its train control costs reflected the quantum of tasks required for the safe and efficient operation of services (Queensland Rail, sub. no. 51: 24).

Queensland Rail said that it would be in both the public interest and Queensland Rail's legitimate business interests if it was allowed the opportunity to continue its reform program of delivering efficiency gains, while ensuring adequate cost recovery. Queensland Rail said:

> *While prices reflecting the efficient cost of a service promote economic efficiency, a sudden decrease from actual costs can impose 'substantial' adjustment costs on the regulated business. The regulator would impinge on legitimate business interests of the regulated business by reducing actual costs without providing an entity such as Queensland Rail the opportunity to reduce these costs (Queensland Rail, sub. no. 51: 26).*

Accordingly, Queensland Rail proposed that train control costs should initially be based on its 2012–13 financial statements (i.e. $2.8 million) and reduced gradually over the term of the 2013 DAU period by applying its proposed glide path to efficiency. Queensland Rail said that approach would eventually reduce the train control costs to $2.1 million in 2016–17 (Queensland Rail, sub. no. 51: 25-26).

QCA analysis and draft decision

Queensland Rail did not accept the QCA's downward adjustment of its annual train control costs. However, Queensland Rail neither demonstrated that it has a business plan to delivery efficiency improvements in train control costs nor provided evidence to show its train control costs were more labour intensive.

Queensland Rail's proposal of recovering inefficient costs is not consistent with the pricing principles in the QCA Act (s. 168A(a)). It is also not consistent with protecting the legitimate business interests of the owner/operator (s. 138(2)(b)), which includes allowing the owner/operator to recover its efficient costs of providing access to the service (QCA, November 2013: 48).

Therefore, the QCA's draft decision retains the approach proposed in its consultation paper.

That said, the QCA has revised the operating cost allowance of $20.4 million proposed in its consultation paper to reflect:

(a) a change in train path allocations (see Section 8.4.1 of this draft decision) that reduces the operating cost allowance by $1.2 million

(b) a working capital allowance of 0.3% based on the QCA's proposed total revenue for the western system that reduces the allowance by $0.3 million.

Based on these changes, the QCA's draft decision proposes a total operating cost allowance of $18.9 million ($17.8 million in June 2013$).

8.3 Regulatory asset base and regulatory return

8.3.1 Incremental capital expenditure

Queensland Rail proposed in its June 2013 DAU to establish:

(a) a capital indicator process – where a provision for future capital expenditure was reflected in the proposed reference tariffs

(b) a subsequent prudency assessment process, with any adjustments being made through the capital carryover provisions (schedule AA).

Under these processes, Queensland Rail requested approval for $79.7 million in past capital expenditure and $81.7 million in proposed future capital works.

New Hope said Queensland Rail's proposed capital expenditure from Rosewood to Macalister appeared excessive and requested the QCA review Queensland Rail's proposed capital expenditure.

In its June 2014 consultation paper, the QCA indicated that there did not appear to be any strategy for the line except to provide service and retain confidence in the organisation. For instance, the QCA considered that there was little evidence of business planning for projects, demonstrated by a lack of options analysis and the absence of a clear rationale for different standards across different assets.

That said, the QCA noted that there was no evidence that past capital expenditure was unnecessary or excessive. Given that, the QCA proposed to accept Queensland Rail's past expenditure and the planned expenditure for the purposes of the capital indicator. However, the QCA said it would subsequently assess the prudency of the planned works in detail through an annual process as has occurred for Aurizon Network. The QCA also said that a key aspect of this assessment would be to determine whether Queensland Rail has appropriate frameworks within which capital expenditure is considered, including exploring the feasibility of alternative solutions.

Stakeholders' comments

Stakeholders did not comment on the QCA's acceptance of Queensland Rail's proposed capital expenditure in the capital indicator for tariff calculation purposes.

However, stakeholders did comment on the capital indicator process itself. In particular, Aurizon observed that the proposed capital expenditure in the western system was effectively limited to improving asset reliability and not capacity expansion. Aurizon said that the capital carryover account provisions should recognise maintenance costs that offset any under-investment over the regulatory period. (Aurizon, sub. no. 48: 14).

QCA analysis and draft decision

The QCA proposes to accept Queensland Rail's proposed capital expenditure in the capital indicator for tariff calculation purposes.

The QCA notes Aurizon's point that the capital expenditure approval provisions should recognise maintenance costs that may offset any under-investment in a regulatory period. However, the QCA considers that a detailed assessment of this trade-off, between maintenance and capital expenditure, should occur as part of its detailed *ex post* assessment of the prudency of the capital expenditure, and not part of its *ex ante* assessment of the capital indicator.

The QCA has also reviewed Queensland Rail's proposed capital indicator and prudency assessment process in Schedule AA of the 2013 DAU. Queensland Rail has proposed a number of amendments that are materially different to its 2008 undertaking and that have not been supported or justified in its accompanying submission. These are not amendments that could reasonably be attributed to the changed corporate structure or lack of vertical integration in non-passenger services. These are matters that seek to alter the balance of roles and responsibilities between Queensland Rail, access seekers, its customers and the QCA.

For instance, Queensland Rail has proposed that the QCA must make a determination within 45 business days on the prudency of capital expenditure, otherwise the QCA will be 'taken to have made a determination to accept Queensland Rail's request' (cl. 2.2(d) in Schedule AA). This time period can only be extended where the QCA seeks further information.

It is not evident that this proposal is reasonable as the ability of the QCA to adequately assess a capital expenditure proposal depends on the quality of the information provided by Queensland Rail. However, it is not clear from past practice that Queensland Rail is able to provide timely and high quality information in all circumstances.

For instance, while the first version of the replacement DAU was submitted in March 2012, a western system tariff proposal was only received in June 2013. Moreover, key supporting information to enable the QCA to assess Queensland Rail's proposal was only received four months later.

It is also not appropriate for the QCA to be placed in the position where its ability to adequately consider Queensland Rail's capital expenditure proposals is constrained by a deemed approval within a (relatively short) time-frame. In particular, the QCA envisages circumstances where it may be necessary for it to consult with interested parties in forming its view on the appropriateness of the capital expenditure.

Indeed, the QCA notes that Queensland Rail's proposal could also be reversed in that it could provide for mandatory rejection of capital expenditure unless it was approved within the 45-day time-period. Clearly, this would not be appropriate as it would not allow for Queensland Rail's proposal to be given due consideration in accordance with the assessment criteria in s. 138(2) of the QCA Act.

This proposal is also inconsistent with the period provided in Part 5 of the QCA Act for access-related matters (ss. 117A and 147A) and seeks to make the timeline the end of the prudency assessment process, which is also inconsistent with the assessment criteria in s. 138(2) of the QCA Act.

The QCA also identified a range of other issues with Queensland Rail's proposal for approving capital expenditure, namely:

(a) *stakeholder consultation*: the QCA is not provided the right to consult stakeholders for assessing the prudency of Queensland Rail's capital expenditure (cl. 2.2(a) of Schedule AA)

(b) *prudency of costs*: the QCA's acceptance of the prudency of costs where there is an approved procurement strategy is largely based on an auditor's report rather than QCA's own assessment (cl. 5.2)

(c) *confidential information*: the QCA must keep as confidential the information provided by Queensland Rail, 'except to the extent that Queensland Rail agrees otherwise' (cl. 1.3(c)). This is inconsistent with the confidential information provisions in the QCA Act (ss. 187 and 239), that prevent the QCA from disclosing information if its disclosure would damage Queensland Rail's commercial activities and not be in the public interest

(d) *escalation factor*: prudent costs of works in excess of that required to accommodate reasonable demand will be set aside and escalated with WACC (cl. 3.3(b)(i)), rather than with CPI as provided in the 2008 undertaking.

Taking the aforementioned matters into account, the QCA proposes to not approve Schedule AA of the 2013 DAU. The QCA considers that the capital indicator and prudency assessment process in Schedule A of Aurizon Network's 2010 undertaking represents a more considered and balanced approach that provides a reasonable benchmark. Therefore, the QCA's draft decision is that the 2013 DAU should be amended to be consistent with Schedule A of Aurizon Network's 2010 undertaking.

Draft decision 8.1

- **The QCA requires Queensland Rail to amend its proposal to make Schedule AA in the 2013 DAU that relates to the maintenance of regulatory asset base, consistent with Schedule A in Aurizon Network's 2010 undertaking.**

8.3.2 Opening asset value

Background

A western system reference tariff has been part of an approved undertaking since 2006. However, that tariff has never been calculated on the basis of a settled asset value.

While the existing tariff is based on a draft asset value that was included in the QCA's December 2009 draft decision, QR Network objected to key aspects of the QCA's proposed asset valuation. For instance, QR Network objected to the QCA's proposed allocation of capital costs between coal and non-coal train services, deductions due to the impact of the Brisbane metropolitan network and exclusion of certain investments. So, while a tariff was approved in 2010, it was not based on an agreed value or indeed an agreed underlying set of assumptions and facts.

Aspects of these outstanding matters from 2010 remain contentious today. We note that Queensland Rail's 2013 DAU largely sought to roll forward the asset value in the 2009 draft decision and in doing so relied on the earlier asset register and unit values. However, it also revisited the same matters that QR Network objected to in relation to the QCA's 2009 draft valuation.

We also note that stakeholders have raised a number of material concerns with Queensland Rail's proposed asset value, some of which relate to the contentious matters previously identified with the 2009 draft valuation. However, stakeholders also raised new concerns that

question the condition of the network and therefore key aspects of Queensland Rail's 2013 proposed asset value and the QCA's 2009 draft valuation that preceded it.

In light of (i) the failure to agree on a valuation in previous determinations and (ii) more recent stakeholder submissions, the QCA has been persuaded to reconsider the opening value of the western system assets – a matter that was not previously settled and that is the subject of new information and arguments provided by both Queensland Rail and other stakeholders.

Asset valuation methodologies

There are a variety of methodologies available for valuing assets that can be broadly categorised as either value-based or cost-based. Each methodology has advantages and shortcomings, particularly in the context of pricing for a regulated monopoly business (see Appendix B of this draft decision).

Value-based approaches determine the economic value of an asset largely from its cash generating capacity. These approaches are consistent with the approach in competitive markets where the asset values are determined by the income earning potential of the assets and where prices are determined by the interaction of many buyers and many sellers.

In non-competitive or monopoly markets, there is the problem of circularity. That is, the price charged for a product or service will determine the economic value of the assets used to produce the product or service. However, the regulator needs the economic value of the assets to determine the price to be charged.

Cost-based approaches relate the value of an asset to the cost of establishing the asset, or the service potential embodied in the asset, either at the original cost (historical cost) or the current cost (reproduction or replacement cost). The most commonly used cost-based asset valuation methods are depreciated actual cost (DAC) and depreciated optimised replacement cost (DORC).

DAC represents the original cost of establishing the asset adjusted by the proportion of the asset service that has expired.

The advantage of a historical cost approach, such as DAC, is that it avoids double counting of assets by limiting the facility owner to earning a return on funds actually invested – a notion that is relevant in a regulatory context. It also avoids the expense and subjectivity associated with determining current asset values and is relatively easy to establish, provided data and detailed asset registers are available. A DAC approach can also provide a good correlation to replacement values, notably in an environment of low inflation and little technological change.

DORC measures the current cost of replacing existing assets with a set of assets that are optimised and adjusted for depreciation, to provide equivalent services and capacity to the asset being valued.

The advantage of a replacement cost approach, such as DORC, is that it may better approximate the cost a new entrant into the market might face to provide the same level of service. This is particularly relevant where there has been over-engineering or significant technological change (e.g. telecommunications) as a DORC valuation will be lower than a DAC valuation and will avoid the incentives for inefficient new entry and by-pass.

Where there is competition, markets are generally good at valuing commodities and assets as they reflect information on values and costs from many buyers and sellers across a large number of trades. An asset valuation methodology, such as DORC, does not have the information advantage of a market-based valuation. It has the complexity and subjectivity surrounding judgements on estimates of depreciation, replacement cost, optimisation and

useful life. Further, if a subsequent review extends the remaining useful life of an asset, this might result in double counting of costs and allow the facility owner to earn excess returns.

Regulators in the USA have placed some emphasis on DAC approaches. In those cases, there are good accounting records and a long-standing relationship between the regulator and the facility owner. This ensures that the regulated entity neither over- nor under-recovers its incurred costs.

These circumstances do not exist in Australia where facilities have been created and operated by government agencies where the norms of commercial activities (e.g. long-standing accrual accounts) have not applied.

In Australia, asset valuations of infrastructure have either been done by governments or by regulators. When done by governments, there has been no evident preference for a particular methodology, rather the emphasis has been on achieving a range of economic, financial or social objectives.

Alternatively, when it has been left to the regulator to do the initial asset valuation the regulator has tended to apply a DORC methodology. This has happened in part because it is inappropriate to apply a value-based approach and in part because the information does not exist to do a DAC approach.

However, the DORC approach is generally not a legislative requirement, nor is applying one uniform set of principles set in stone. In the QCA's case, the QCA Act gives no specific guidance on asset valuation or methodology, beyond saying that the expected revenue for the access provider should 'include a return on investment commensurate with the regulatory and commercial risks involved' (s. 168A(a)). The QCA Act therefore does not require a DORC valuation or a roll-forward approach. Nor does it prohibit reconsidering an asset value at all, or in the circumstances that prevail here where an asset value has never been settled.

We note that other regulators have tended to deviate from a 'pure DORC' or 'pure new market entrant' approach to establishing an opening asset value. For example, electricity regulators have tended to adopt a historical cost roll forward approach to valuing easements within a DORC style framework.

The QCA has in the past applied a 'brownfields' DORC assessment for DBCT and the central Queensland coal network. In the latter case, the QCA accepted as given the existing alignment and the narrow gauge. Relevantly, consistent with the QCA Act, the QCA has also sought to limit double counting of costs (e.g. the 2001 valuation of Queensland's gas distribution networks and forecast asset replacement on the western system – see QCA March 2001: 128; QCA October 2001: 151; QCA December 2009: 82-83).

In line with past practice, the QCA's considerations of the value of the western system assets have been on the basis of a brownfields DORC methodology. In doing so, the QCA's proposed DORC assessment has been informed by submissions from Queensland Rail and other stakeholders and has focused on the life and condition of the western system assets.

For a more extensive discussion of the economic and regulatory approaches to asset valuation methodologies including DORC, see Appendix B.

History of western system valuation

Pricing for coal services on the western system has been a difficult issue to resolve. Since 2004, the QCA has considered different proposals from Queensland Rail and its predecessors for deriving a western system tariff (for more details see Appendix C of this draft decision).

On each occasion the QCA has learnt more about the condition of the western system and, indeed, how it differs from the central Queensland coal network.

QR Network's 2009 DAU was the first time a western system tariff proposal was based on a DORC valuation. QR Network's valuation of $351.6 million ($387.9 million in 2013$) was based on Connell Hatch's technical assessment of the network from Rosewood to Macalister.

In assessing that proposal, the QCA drew on its experience with rail infrastructure in central Queensland, including the West Blackwater (i.e. Minerva) reference tariff that the QCA had approved around the same time in 2009 (see QCA, March 2009; QCA, August 2009).

In doing so, the QCA sought to apply to the western system asset valuation the asset allocation principles that it used in approving the West Blackwater reference tariff – i.e. fully include dedicated coal assets, fully exclude non-coal related assets and allocate the common assets based on the proportion of train paths used by coal and non-coal services.

The QCA's consultant at the time, Everything Infrastructure (EI), focused on the asset register and unit costs. In the absence of stakeholders' suggestions to the contrary, EI's assessment of the condition of the network was informed by the maintenance activities proposed at the time and Connell Hatch's proposal that all the assets were half life-expired.

The QCA's December 2009 draft decision proposed a value of $278.5 million ($307.3 million in 2013$) for the western system's common network assets.[35]

QR Network rejected key components used to derive the tariff proposed in the QCA's 2009 draft decision, including the asset valuation and cost allocations. Nevertheless QR Network ultimately resubmitted the tariff included in the 2009 draft decision.

In approving the western system tariff for the period 2009–10 to 2012–13, the QCA noted that it had 'not achieved its desired objective of finalising a repeatable and transparent methodology for deriving the western system tariff' (QCA, June 2010: 89).

Queensland Rail's June 2013 DAU

In its June 2013 DAU, Queensland Rail proposed a western system tariff based on an opening asset value of $340.9 million for the Rosewood to Macalister section and $419.6 million (in June 2013$) for the western system as a whole.

This value was linked to a roll-forward of aspects of the DORC value in the QCA's December 2009 draft decision. In doing so, Queensland Rail sought to change several assumptions in ways that resulted in an uplift to the asset value, including changing the asset allocations between coal and non-coal traffics and reinstating the net present value (NPV) of the Western System Asset Replacement (WSAR) project, that the QCA had removed from its 2009 draft DORC value to avoid double counting (Queensland Rail, sub. no. 38: 4).[36]

As part of its submission, Queensland Rail also proposed to spend $81.7 million on capital investment and $104.5 million on maintenance works over the term of the proposed

[35] The QCA said: 'QR Network's proposed maintenance spending on the western system works out to $5.83/'000gtk. This compares with a range of $1.48/'000gtk to $3.19/'000gtk for the central Queensland systems. The Authority accepts that QR Network faces comparatively high maintenance costs on the western system, given the route and age of the network – both of which are reflected in the DORC valuation, as adjusted by the Authority' (QCA, December 2009: 88).

[36] The QCA had in 2009 proposed to remove the $22.4 million NPV of works included in the WSAR project that continues during the AU1 regulatory period. EI said this work was necessary to bring the assets up to the standard assumed in the DORC valuation (see QCA, December 2009: 82-83 and B&H, May 2014: 35-38).

undertaking. The future investment proposal was consistent with the level of investments that had occurred over the term of the existing undertaking. However, the proposed maintenance costs were 82% higher than the maintenance allowance assessed by the QCA's consultant for the term of the current undertaking, that was used in deriving the QCA's proposed tariff in the 2009 draft decision.[37] Queensland Rail said that the maintenance and capital works proposed in the 2013 DAU were needed because of the standard and alignment of the network (Queensland Rail, sub. no. 38: 4).

Stakeholders said Queensland Rail's proposed opening asset value was excessive. They argued that the poor condition of the infrastructure had become evident in the information Queensland Rail provided to support its June 2013 DAU, in particular the high maintenance and capital expenditure requirements.

Stakeholders said that either the DORC valuation should be reassessed, or any value ascribed to assets that were in place before western coal train services began should be disregarded (they nominated a cut-off date of 1995, although the first western system coal services did not begin until the Wilkie Creek mine started railing in 1996–97).

The QCA noted stakeholders' earlier concerns about the standard of the network and the constraints on coal train services. The step change in proposed maintenance costs further highlighted the possibility that the 2009 valuation had been too high.

Consultation paper

Given the difficulty in balancing the objectives of a reasonable return on investment for Queensland Rail and the interests of access seekers and access holders, the QCA published its June 2014 consultation paper, seeking further comments from stakeholders.

In the consultation paper the QCA drew on stakeholders' comments on Queensland Rail's June 2013 DAU and, in doing so, explored different ways to address the issues they raised. The QCA provided two indicative options for an opening asset value for deriving western system coal tariffs – namely a revised DORC-based valuation and a historical cost valuation – to illustrate the effect of stakeholders' suggestions.

The QCA's revised DORC valuation option was based on the asset register and unit costs QR Network and the QCA had used for the December 2009 draft decision.

However, the revised DORC valuation sought to address concerns that the assumption in the 2009 DORC valuation that all assets were 50% life-expired was too simplistic and did not reflect the actual condition of the rail infrastructure as revealed by the proposed maintenance cost increase. The QCA's current consultant, B&H, therefore reassessed the likely condition and remaining life of the assets, in particular the formation, as at 30 June 2013 (for further details see B&H, May 2014). That DORC value was then allocated between coal and non-coal traffics based on their shares of train paths on the western system.

The historical cost valuation option was based on Queensland Rail recovering none of the pre-1995 assets and all of the post 1995 capital expenditure. This option was based on the observation that the pre-1995 assets are part of a much older network and, in some respects, could be regarded as sunk (the business itself had valued them at a scrap value in 1995). Much of the growth in traffic on the western system has in fact occurred since 1996–97 when coal exports from the Darling Downs started.

[37] The 82% increase is for the sections between Rosewood and Macalister, as the Macalister to Columboola sections were not assessed in the 2009/10 undertaking process – see section 8.2.1.

The consultation paper requested further comments from stakeholders on how best to address the tension between the high maintenance and capital costs and, as viewed by some, a proposed high asset value.

Stakeholders' comments

Queensland Rail and other stakeholders had, in general, divergent views on an appropriate value for the western system assets and, in particular, the two options set out in the QCA's June 2014 consultation paper. Some of these comments highlighted outstanding concerns about the condition and, therefore, the value of the network. Some concerns focussed on detailed aspects of the revised DORC valuation while others were of a procedural or decision-making nature.

In-principle asset valuation matters

Some stakeholders questioned whether key assumptions that underlie a DORC valuation were relevant to the western system assets.

Aurizon said it was 'implausible that a railway built to modern engineering equivalents which is 55% life-expired would incur maintenance costs as material as those proposed by Queensland Rail' (Aurizon, sub. no. 48: 13). New Hope said the western system was 'not a "modern engineering equivalent" and therefore cannot provide a service level which is competitive with other systems' (New Hope, sub. no. 50: 5). Bentley said:

> *The system bears little, if any resemblance to a "modern engineering equivalent" necessitating significant moderation of the derived DORC valuation to more accurately reflect the service standard that the asset delivers (Bentley, sub. no. 49: 3).*

Aurizon, New Hope and Yancoal said the lower axle loads and shorter trains on the western system raised above-rail costs – e.g. each train service in central Queensland or the Hunter Valley was four or five times as productive as a western system train service (Aurizon, sub. no. 48: 8; New Hope, sub. no. 50: 5; Yancoal, sub. no. 52: 1). Yancoal said that if the western system had been built to a modern standard, its single line capacity would have accommodated much higher volumes than it now carried. 'We again reiterate that this is an extreme outlier system in terms of scale, standard and impact on above rail efficiency' (Yancoal, sub. no. 52: 1-2)

Yancoal said it supported the historical cost approach, but that the resulting asset value should be reviewed to reflect a 'significant concern that the value of the post 1995 assets does not reflect efficient planning and construction activities' (Yancoal, sub. no. 52: 2).

Aurizon said it favoured the historical cost approach because it allowed actual maintenance costs to be used for deriving the tariff, whereas with a DORC approach maintenance costs would need to be adjusted down to reflect the higher assumed standard of the asset. Aurizon also said that a DORC-based tariff might end up similar to a historical cost-based tariff if some of the assumptions used for the consultation paper's DORC approach were adjusted to address the difference between the assumed standard of the assets and the actual standard. These adjustments included recognising tunnels at actual cost, assuming train payloads were at the higher level implied by the DORC valuation and reducing the maintenance costs to a more reasonable level (Aurizon, sub. no. 48: 10-14).

Aurizon said:

> *If QR obtains the benefit of the higher asset valuation implied by DORC, then it cannot at the same time expect to obtain a maintenance allowance that reflects non-optimised asset condition. This is a 'heads I win, tails you lose' proposition – users would pay a capital*

component that reflected a modern engineered railroad, yet at the same time pay a maintenance charge that reflected a degraded network (Aurizon, sub. no. 48: 12).

Detailed asset valuation matters

Queensland Rail and Aurizon raised a number of concerns about detailed aspects of B&H's DORC assessment and the QCA's financial model, including that they:

(a) inappropriately applied a weighted average asset life to calculate depreciation over entire asset classes instead of calculating depreciation by individual asset class (Queensland Rail, sub. no. 51: 2, 7-8)

(b) used distance to split the valuation between Rosewood to Macalister and Macalister to Columboola, which did not consider the comparative asset quality of each section and the considerable past capital spending on the Rosewood to Macalister sections (Queensland Rail, sub. no. 51: 2-3, 9)

(c) failed to consider financing and transaction costs (Queensland Rail, sub. no. 51: 3, 10)

(d) had not sufficiently justified extending the life of rail assets beyond 50 years (Queensland Rail, sub. no. 51: 8-9)

(e) should be adjusted to reflect the actual nature of the assets, including removing the value of the tunnels, as

  (i) they were fully depreciated and '[t]he preservation of the assets is managed with the maintenance costs allowance'

  (ii) 'Aurizon does not believe that s. 168A of the QCA Act imposes a requirement to value tunnels at replacement costs' (Aurizon, sub. no. 48: 11)

(f) the value of the 'top 600' should be removed as its function is being performed by excess ballast (Aurizon, sub. no. 48: 32).

Procedural matters

Stakeholders' views were divided on the regulatory interpretation of the valuation approaches illustrated in the QCA's consultation paper. On one hand, Queensland Rail said the historical cost approach departed from regulatory precedents and was not consistent with the QCA Act. New Hope and other stakeholders took a contrary view and said the historical cost approach was consistent with the QCA Act but the DORC approach was not.

In summary, Queensland Rail said both the tariff options failed to:

(a) give appropriate weight to Queensland Rail's legitimate business interests (s. 138(2)(b) of the QCA Act)

(b) fully consider the effect of excluding the pre-1995 assets for pricing purposes (s. 138(2)(f))

(c) have full regard to the pricing principles in the QCA Act, particularly the requirement that the price generate a return on investment commensurate with the regulatory and commercial risks involved (ss. 138(2)(g) and 168A(a)) (Queensland Rail, sub. no. 51: 2-3).

By contrast, the miners and Aurizon said:

(a) the historical cost approach was consistent with the criteria as it

  (i) promoted economically efficient operation of, use of and investment in infrastructure, including avoiding asset stranding (s. 138(2)(a))

(ii) served the legitimate business interests of Queensland Rail and complied with the pricing principles by giving a full return on post-1995 investment and ongoing capital spending, maintenance and operating expenditure (ss. 138(2)(b) and (g))

(b) the DORC approach was not consistent with the criteria as it was

(i) against the interests of access seekers (s. 138(2)(e))

(ii) not in the public interest because it would reduce competition in markets and was likely to reduce employment and coal royalties (s. 138(2)(d)) (New Hope, sub. no. 50: 6-8; Yancoal, sub. no. 52: 2; Aurizon, sub. no. 48: 4; Bentley, sub. no. 49: 3, 5).

Queensland Rail said the historical cost approach departed from previous valuation approaches the QCA has used and provided a report from PricewaterhouseCoopers in support of this argument (Queensland Rail, sub. no. 51, PwC Report: 5-18, 22). New Hope provided advice from law firm Gilbert+Tobin that there was no requirement in the QCA Act that the QCA use DORC as the basis for valuing regulated assets (New Hope, sub. no. 50, Gilbert+Tobin Memorandum).

QCA analysis and draft decision

Economic theory indicates that prices should either reflect short-run marginal costs in times of excess capacity or long run marginal costs when capacity is fully utilised. It also indicates that it would be reasonable to provide a scrap value to a sunk asset like the western system. Alternatively, to prevent inefficient new entry, prices should be capped at the new entrant's or the by-pass costs.

This suggests that there tends to be a wide range of possible efficient prices that either represent a floor price reflecting an asset value based on a scrap value assessment or a ceiling price based on a new entrant's costs. Much of the focus of the submissions has been on the high maintenance and replacement costs and therefore the condition of the existing network – i.e. on the new entrant's cost of an equivalent asset.

Given the age and condition of the western system it is apparent that it needs significant ongoing investment and maintenance to maintain the current level of usage – irrespective of what additional investments might be required to actually increase capacity. Indeed, Queensland Rail's proposed investment and maintenance costs over the regulatory period are sizable and represent almost half of Queensland Rail's proposed opening asset value. In contrast, Aurizon Network's proposed replacement capital expenditure and maintenance costs over a similar period are around a quarter of its proposed opening asset value.[38]

While stakeholders have suggested that one option might be to adjust these capital and maintenance costs to reflect the implicit standard of the network, that is not the QCA's preferred approach. Rather, the QCA considers that it is in the interests of Queensland Rail and access seekers and holders that Queensland Rail is given a capital expenditure and maintenance cost allowance that reflects the nature and condition of the assets on the ground and reflects the efficient expected costs of keeping the network fit for purpose. Doing so provides Queensland Rail with incentives to continue to invest in the network and maintain it as fit for the purpose of carrying coal train services, which would be in the interests of both Queensland Rail and its customers. This is consistent with the economic thinking that indicates that valuations on sunk assets have very little incentive effect on future activities.

[38] This excludes Aurizon Network's ballast-cleaning costs as that activity is not relevant to the western system.

Accordingly, the QCA proposes to largely accept Queensland Rail's claim for maintenance costs (see Section 8.2.1). The QCA also proposes to accept that all of Queensland Rail's proposed capital expenditure be included in the capital indicator (see Section 8.3.1).

However, the QCA proposes not to accept Queensland Rail's proposed asset valuation as it is inconsistent with the approval criteria in the QCA Act. In particular, Queensland Rail's valuation, and therefore the implied condition of its network, is not consistent with the maintenance and capital spending required to keep the network fit for purpose. The proposed return on investment overcompensates Queensland Rail for the regulatory and commercial risks involved (ss. 138(2)(g) and 168A(a)). While the valuation may be consistent with the legitimate business interests of Queensland Rail, it is not consistent with the efficient investment in and use of the rail infrastructure or the interests of access seekers and holders (ss. 138(2)(b), (a), (e) and (h)).

The issue then becomes one of ensuring that the value of the network used to calculate the tariff is consistent with the relatively high level of ongoing capital and maintenance costs.

This was the basis of the QCA's revised DORC valuation included in its June 2014 consultation paper. However stakeholders raised a number of additional matters in relation to both the DORC approach and the historical cost approach in the consultation paper.

Queensland Rail's concerns

Queensland Rail raised several technical concerns about the way the DORC valuation in the consultation paper was prepared. The QCA accepts Queensland Rail's concerns about the treatment of asset lives, the splitting of assets between different sections of the network, and the treatment of financing and transaction costs. The QCA has addressed these concerns in this draft decision, in the manner set out below.

Queensland Rail also raised a number of process or legal concerns when it said that neither of the tariff options in the consultation paper gave appropriate weight to its legitimate business interests, the effect of excluding assets for pricing purposes and the need for a price that generates a sufficient return (ss. 138(2)(b), (f) and (g) and 168A(a) of the QCA Act – see Queensland Rail, sub. no. 51: 2-3).

The QCA rejects the notion that it did not take into account Queensland Rail's interests, including the effect of excluding assets and the need for a sufficient return, in preparing the options in the June 2014 consultation paper.

Be that as it may, the QCA in making this draft decision has taken into account all aspects of the approval criteria in s. 138(2) of the QCA Act, including the interests of Queensland Rail and access seekers.

Other stakeholders' concerns

The other stakeholders who responded to the consultation paper also considered the two indicative tariff options against the approval criteria in the QCA Act and said that the historical cost option was more consistent with those criteria (New Hope, sub. no. 50: 6-8; Yancoal, sub. no. 52: 2; Aurizon, sub. no. 48: 4; Bentley, sub. no. 49: 3, 5).

However, the three miners and Aurizon reiterated their concerns that DORC was not appropriate because the standard of the western system fell well short of the modern equivalent asset assumption on which a DORC valuation was based. They said that the level of maintenance spending proposed by Queensland Rail was inconsistent with the DORC valuation applied in the consultation paper and that either the valuation or the maintenance allowance needed to be adjusted.

Aurizon made several specific suggestions, including that the maintenance costs be adjusted downwards to reflect benchmarks from Aurizon Network's Moura system and that the tunnels be excluded from the asset valuation.

In reviewing the submissions, and having had regard to s. 138(2) of the QCA Act, the QCA accepts that both asset valuation options in its consultation paper have shortcomings.

The historical cost approach raises concerns because, as observed by Queensland Rail, it excludes all pre-1995 assets, portions of which remain necessary and relevant for the operation of coal services.

Yet, at the same time, the QCA accepts stakeholders' (e.g. Aurizon and New Hope) concerns that the DORC approach applied in the consultation paper asks access seekers to pay for assets that are ageing and in poor state.

Therefore, both the DORC and historical cost approaches illustrated in the consultation paper do not accord with the pricing principles in the QCA Act (s. 168A(a)) – the historical cost approach does not provide Queensland Rail with an appropriate return on its investment while the DORC approach provides a return that overcompensates for the regulatory and commercial risks involved. For the same reasons, these options are not consistent with promoting efficient investment in, and use of, the network (s. 138(2)(a)). Further, while the historical cost option is not in the legitimate business interests of Queensland Rail, the DORC option in the consultation paper is not in the interests of access seekers and holders (ss. 138(2)(b), (e) and (h)).

Revised valuation approach

In light of stakeholders' submissions on the QCA's June 2014 consultation paper, the QCA has further considered the best way to approach the asset lives and depreciation that were included in the 2009 draft decision. As with its previous consideration of this issue, the QCA has sought to provide a reasonable return to Queensland Rail, while also taking into account the interests of access holders and access seekers (ss. 138(2) (b), (g), (e) and (h) of the QCA Act).

Regulatory practice in Australia and elsewhere has framed the discussion of a reasonable return to a facility owner in terms of the principle of financial capital maintenance (FCM). In general terms, FCM ensures that investors receive reasonable compensation for their capital investment and have an incentive to make efficient investments in the future, while customers pay reasonable prices to access regulated monopoly infrastructure.

The QCA considered a number of issues relating to FCM in its February 2014 information paper on Financial Capital Maintenance and Price Smoothing, noting that:

> *In the regulatory context, FCM is applied in an ex ante sense, meaning that investors of a regulated firm can expect to recover the opportunity cost of their capital and the nominal value of their initial investment over time. This is referred to as the FCM principle. As long as the present value (PV) of future regulated returns, calculated on the basis of an appropriate opportunity cost discount rate, is equal to the value of the regulatory asset base (RAB), the FCM principle is achieved. The FCM principle in an exact sense is often referred to as the NPV=0 principle (QCA February 2014: 1).*

The FCM principle of a reasonable return on and of a facility owner's investment over time is typically applied in a forward-looking way, once a RAB has been set. In this way the FCM (and NPV=0) principle has a particular incentive impact, as it indicates to facility owners and access seekers that costs efficiently incurred into the future will be reflected in future tariffs. This is clearly consistent with the objects clause of part 5 of the QCA that points to the efficient use of the network and where prices (and underlying asset values) are an important determinant of efficient use.

There is, however, little efficiency or incentive effect in the way that sunk assets are valued. However, that is not to say that the FCM principle is an irrelevant consideration in valuing those sunk assets. In particular, it is relevant in relation to the s. 138(2) criteria for approving an undertaking that point to, amongst other things, the legitimate business interests of the facility owner and the interests of access seekers.

One way of looking at FCM is that investors should receive a return on their investments, but not more than once. For example, if an asset's actual life exceeds its expected useful life it can be reasonably anticipated that it has been fully depreciated. It should not then be revalued and included in the RAB again for the investment to be recovered a second time. It follows that a life expired asset should not be included in the initial asset base, as this would also be double recovery of the investment.

The historical cost approach illustrated in the consultation paper is one way of avoiding this double counting. However the historical cost approach has the disadvantage that it does not recognise pre-1995 investments by Queensland Rail, such as the rails, that have not been fully depreciated and are still required to provide the service.

Accordingly, the QCA has sought to further adjust the DORC valuations in its 2009 draft decision and June 2014 consultation paper. In particular, the QCA proposes to place a zero value on assets whose actual life exceeds their expected useful life.

A number of the western system assets have been in place for longer than their useful lives as assessed by B&H[39], without any evident replacement capital expenditure having been recorded. For some asset classes (e.g. wooden sleepers, wooden bridges[40] and fences) this is due to maintenance work. For other asset classes (e.g. tunnels and earthworks), the life is beyond what could have reasonably been anticipated by Queensland Rail and its predecessors. The QCA proposes that it is reasonable to consider that these assets have been fully depreciated and including them would amount to 'double counting'.

The QCA therefore proposes to adjust the DORC by placing a zero value on assets whose actual life is in excess of their expected useful life estimated by B&H based on technical and regulatory precedents and the particular circumstances of the western system. We note that this proposed approach is consistent with the QCA's past practice of relying on a DORC valuation methodology. It is also consistent with other regulatory precedents. For instance, in its March 2001 decision on gas distribution networks the QCA said that:

> *... in the absence of a remaining life value, those assets that are still functioning yet have already exceeded their estimated useful lives, would be depreciated down to a zero value (QCA, March 2001: 128-129).* [41]

More recently, the QCA sought to address a double counting issue in its 2009 draft decision on the western system tariff, when it removed the $22.4 million[42] of capital spending that was required to bring the assets up to the standard assumed in the DORC valuation.

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[39] For B&H's assessment of expected useful lives of western system assets, see the B&H reports of May 2014 (published with QCA's consultation paper) and September 2014 (published with this draft decision).

[40] Wooden bridges have a 100-year design life under Australian Standard AS5100 (see B&H, September 2014: 9).

[41] This principle was accepted by the QCA in its final decision on this matter.

[42] The $22.4 million was the net present value of works included in the Western System Asset Replacement (WSAR) project that continued during the AU1 regulatory period (see QCA December 2009: 82-83).

Addressing double counting of western system assets

Given all the above considerations, the QCA asked B&H to further adjust the 2009 DORC valuation to address asset life expiry and other issues highlighted by Queensland Rail and other stakeholders by:

(a) using the 2007 Connell Hatch asset register and the 2009 Everything Infrastructure unit costs from the 2009 draft decision

(b) taking into account the modelling and valuation concerns raised by Queensland Rail in its response to the consultation paper by

  (i) assessing depreciation by individual asset class rather than applying a weighted average asset life (Queensland Rail, sub. no. 51: 2, 7-8)

  (ii) refining the split of values between Rosewood to Macalister and Macalister to Columboola to take into account factors other than distance, including the comparative asset quality and past capital spending (Queensland Rail, sub. no. 51: 2-3, 9)

  (iii) considering Queensland Rail's financing and transaction costs, in particular interest during construction (Queensland Rail, sub. no. 51: 3, 10)

  (iv) limiting the assessed useful life of the rails to 50 years, even where the low volumes would justify a longer technical life (Queensland Rail, sub. no. 51: 8-9)

(c) placing a zero value on assets (e.g. tunnels and earthworks) built so long ago that they can be reasonably considered to be fully life expired

(d) placing a zero value on assets (e.g. wooden sleepers) that are still in service after their assessed (i.e. expected) useful lives have expired, because of ongoing maintenance (as assessed by B&H in May 2014)

(e) taking into account Queensland Rail's historical capital expenditure on the western system, subject to data availability.

In summary, the QCA considers this approach is consistent with its obligations under s. 138(2) of the QCA Act, including:

(a) the object of Part 5 (s. 138(2)(a)) – as it promotes efficient investment in Queensland Rail's infrastructure by reflecting the actual investment Queensland Rail has made and will make in its infrastructure and will promote effective competition in coal markets

(b) the legitimate business interests of Queensland Rail (ss. 138(2)(b) and (c)) – as Queensland Rail continues to earn a return on assets whose actual life does not exceed their expected useful life

(c) the public interest (s.138(2)(d)) – as it promotes the future development of the coal industry by signalling to customers that they will not have to pay for life expired assets

(d) the interests of access seekers and users of the western system (ss. 138(2)(e) and (h)) – as Queensland Rail continues to have an incentive to invest in the network to ensure that it remains fit for purpose, thereby enabling users to access the infrastructure and better compete in downstream markets

(e) the effect of excluding assets for pricing purposes (s. 138(2)(f)) – the QCA has not excluded any assets for pricing purposes but has rather assigned a zero value to those assets which it considers are life expired. This will enable Queensland Rail to generate revenue from the western system to more than meet the efficient costs of providing

access to the service, but in a manner consistent with the principle of financial capital maintenance

(f) the pricing principles (ss. 138(2)(g) and 168A)) – as it provides a return on Queensland Rail's investments made to provide access, and comprise assets that are not already life expired.

The 'no double counting' approach is not applicable for replacement capital expenditure, as it is reasonable for Queensland Rail to earn a return on these renewal assets and recover them over their asset lives. This includes long-lived renewal assets, particularly the rails, that were installed well before 1995 but still have substantial remaining expected useful life.

The effect of the valuation approach is to place a zero value on longstanding assets including timber and steel sleepers, tunnels and roads. However $8.41 million is included for timber bridges and $130,000 for earthworks to reflect capital spending, to replace some of those assets, that is not life-expired. Much of the assessed value of the network is in the rails and concrete sleepers and bridges that have substantial remaining lives. Overall, the QCA's proposed common network DORC is $246.6 million for Rosewood to Columboola, compared with $427.0 million proposed in the June 2014 consultation paper. B&H's analysis, including the different assets' values and remaining lives at July 2013, is illustrated in **Figure 7** below. B&H's report setting out its valuation analysis in detail is published with this draft decision (B&H, September 2014).

Comments welcome

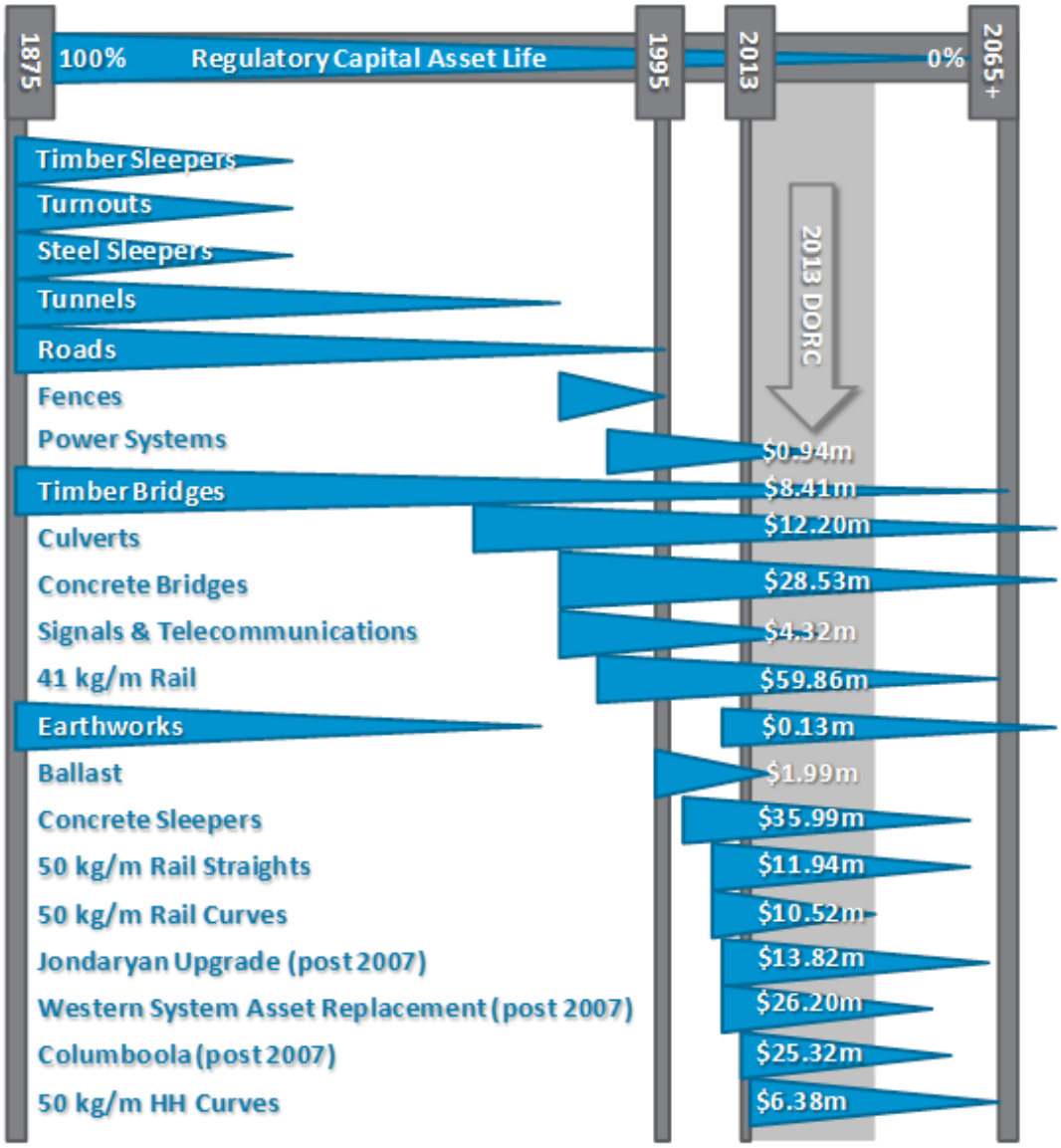
This proposed approach is not final and the QCA invites submissions from stakeholders on this matter. The QCA will be particularly interested in stakeholder views of whether this approach balances the legitimate business interests of Queensland Rail, including the requirement that it receive a return on investment, against the interests of access seekers and access holders (ss. 138(2)(b), 168A(a), 138(2)(e) and (h)).

Certainty

In line with its approach in other regulatory circumstances, once the QCA forms its final view on the western system asset valuation, it will not seek to optimise that investment in the future. There are three provisos to this. First, if the QCA made its initial decision to include the investment into the asset base on the basis of information provided by Queensland Rail that Queensland Rail knew to be false or misleading at the time it provided the information. Second, if circumstances arise in the future where demand has deteriorated to such an extent that regulated prices on an unoptimised asset would only exacerbate the decline in demand and the associated revenue impacts for Queensland Rail. Third, there may also be a need for reconsideration if it subsequently became clear that there was a possibility of actual (not hypothetical) bypass.

These are matters that could be formalised by including them in the undertaking or they could be subject to a separate application under the ruling provisions of Part 5, Division 7A of the QCA Act.

Figure 7: Asset breakdown for revised B&H DORC valuation



Note: The dark blue triangles depict asset lives as they progressively decline over time. Where asset lives have expired before 1 July 2013, they are not included in the DORC valuation.
Source: B&H, September 2014.

8.3.3 Weighted average cost of capital (WACC)

In its 2013 DAU, Queensland Rail proposed a WACC of 6.93% based on using the March 2013 quarter risk-free rate and debt margin, and the non-time-variant parameters from the 2010 Aurizon Network access undertaking. However, Queensland Rail indicated it expected the risk-free rate and debt margin to be adjusted once the timing for determining them was agreed between the QCA and Queensland Rail (Queensland Rail, sub. no. 36: 14).

Both New Hope and Aurizon said the proposed WACC parameters should be assessed for reasonableness, despite the parameters being based on the 2010 Aurizon Network access undertaking (New Hope, sub. no. 44: 17; Aurizon, sub. no. 43: 15).

The QCA in its consultation paper noted that it was considering the Queensland Rail and Aurizon Network 2013 DAUs at the same time. Given this, there was a threshold issue on the extent to

which the QCA's views of an appropriate WACC for Queensland Rail should be guided by its corresponding views for Aurizon Network (QCA, June 2014: 21-22).

However, for purposes of its consultation paper, the QCA relied on Queensland Rail's submitted WACC parameters; that is, the QCA has used a WACC of 6.93% (reflecting a WACC margin of 3.81%).

Stakeholder submissions

Queensland Rail requested that the risk-free rate and the debt margin be set on the 20 business days immediately prior to the start of the regulatory period on 1 July 2013 (Queensland Rail, June 2014).

New Hope said that Queensland Rail's WACC should not overcompensate it for the risks it faced (New Hope, sub. no. 50: 18). Yancoal said the QCA should consider 'the extent of risk faced by QR in the context of their (QR) risk avoiding access agreements' and said:

> *QR is not exposed to significant risk within a regulatory period due to take or pay contracts and the ability to earn higher returns if actual volumes exceed forecast volumes (Yancoal, sub. no. 52: 3).*

QCA analysis and draft decision

The pricing principles in s. 168A of the QCA Act require that the price should:

> *... include a return on investment commensurate with the regulatory and commercial risks involved [for the regulated entity].*

In considering whether Queensland Rail's WACC is appropriate, the QCA notes that there are similarities between Queensland Rail's and Aurizon Network's coal network activities. Both entities provide monopoly rail infrastructure services in Queensland and have their demand risks limited through customers' take or pay obligations.

However, the QCA notes there are also significant differences between the entities that suggest that Queensland Rail's risks are unlikely to be less than those faced by Aurizon Network. In particular, Queensland Rail:

(a) is more exposed to movements in the economy as it is subject to a price cap. In contrast, Aurizon Network has revenue certainty through its revenue cap

(b) obtains revenues from only two coal mines (Cameby Downs and New Acland) on the western system. In contrast, Aurizon Network's revenue is from around 50 mines and over 15 companies across the CQCR

(c) provides for the transport of relatively low-margin thermal coal, where one mine has recently closed (Wilkie Creek). In contrast, Aurizon Network transports a large proportion of higher-margin coking coal and its coal traffic has not traditionally been related to Australian (or Queensland) economic and stock market cycles.

The QCA has conducted a detailed analysis of Aurizon Network's risk profile, including by benchmarking it with other comparable firms. On this basis, the QCA is proposing an equity beta of 0.8 which is what Queensland Rail proposed but is also what the QCA is proposing for Aurizon Network. The QCA has also recently undertaken a review of the WACC market parameters. The QCA has used these revised market parameters as part of this draft decision including a market risk premium of 6.5% and a gamma of 0.47. Additionally, the QCA estimated the risk-free rate for a term that aligns with the term of the regulatory cycle (i.e. four years), which is consistent with the position outlined in the QCA's WACC parameters decision.

Further information on this matter is available in the QCA's draft pricing decision for Aurizon Network and in its WACC market parameters decision – both of which are available on its website.

To date, the QCA has not received submissions to suggest Queensland Rail's business risks are lower than those of Aurizon Network.

For the purpose of this draft decision, the QCA has therefore accepted Aurizon Network's non-time variant parameters for Queensland Rail.

The only change between the decisions is that Queensland Rail nominated a different WACC averaging period for the setting of the time variant parameters (i.e. the risk free rate and the debt margin). The QCA has accepted Queensland Rail's proposed WACC averaging period as it is consistent with common regulatory practice. Indeed, had the QCA accepted the same averaging period for Queensland Rail as it did for Aurizon Network, it would have proposed an identical WACC across both entities.

On balance, the QCA has, for the purposes of this draft decision, proposed that Queensland Rail be provided with more generous WACC parameters than it had sought. This results in a higher WACC margin for Queensland Rail of 4.12% compared to the 3.81% margin it had proposed in its submission.

Given this, the QCA proposes a WACC of 6.93% for Queensland Rail. This is coincidentally what Queensland Rail had originally submitted in its DAU.

Further information is provided in **Table 2** below.

Table 2 Queensland Rail WACC Parameter Comparison

Parameter	*QCA Pricing Draft Decision (2010 DAU)*	*Queensland Rail 2013 DAU proposal*	*QCA Draft Decision (2013 DAU)*
Credit Rating	BBB+	BBB+	BBB+
Risk-Free Rate	5.19%	3.12%	2.81%
Market Risk Premium	6.0%	6.0%	6.5%
Asset Beta	0.45	0.45	0.45
Gearing	55%	55%	55%
Equity Beta	0.80	0.80	0.80
Gamma	0.50	0.50	0.47
Equity Margin	4.80%	4.80%	5.20%
Cost of Equity	**9.99%**	**7.92%**	**8.01%**
Debt Margin (Pre Allowances)	3.62	1.87%	3.02%
Refinancing Risk Allowance – Credit Default Swap (Proxy)	0.83%	0.83%	–
Refinancing Risk Allowance – Interest Rate Swap	0.175%	0.175%	0.113%
Debt Issuance Allowance	0.125%	0.125%	0.108%
Debt Margin	4.75%	3.00%	3.24%
Cost of Debt	**9.94%**	**6.12%**	**6.05%**
WACC Margin	4.77%	3.81%	4.12%
WACC	**9.96%**	**6.93%**	**6.93%**

Source: Queensland Rail, sub. no. 36: 14; Incenta, August 2014; QCA, August 2014a, August 2014b and September 2014

8.4 Tariff approach

This section considers the:

(a) allocation of the asset base between coal and non-coal (Section 8.4.1)

(b) tariff mechanism for the metropolitan system (Section 8.4.2)

(c) form of regulation and the tariff structure (Section 8.4.3)

(d) tariff level (Section 8.4.4).

8.4.1 Allocating common network asset base between coal and non-coal

On a shared system, the common network asset base needs to be allocated amongst the different classes of users.

The QCA's December 2009 draft decision proposed that for the western system between Rosewood to Columboola coal traffic should pay, for:

(a) *post-1995 assets*: 75.6% of the investment on the common network, reflecting coal's proportion of the total available paths (i.e. 80 of 106 available paths)

(b) *pre-1995 assets*: 60.5% of the common network asset base, reflecting a further adjustment to the path allocation taking into account the 20% capacity sterilised by the metropolitan peak-hour blackout (i.e. 80% metro adjustment of 75.6% path allocation giving 60.5% of the pre-1995 common network asset value) (QCA, December 2009: 80).

The rationale for treating the pre-1995 asset base separately was to ensure that Queensland Rail did not receive a return for sunk costs when western system coal train services began in 1995, that related to paths that were not available to those trains because of the metropolitan capacity constraints (QCA, December 2009: 84).

This section considers separately the allocation of the:

(a) post-1995 asset base including the treatment of assets underwritten by customers

(b) pre-1995 asset base including the treatment of metropolitan blackout.

Allocating post-1995 asset base

In the 2013 DAU, Queensland Rail proposed that for the Rosewood to Macalister section coal traffic pay, for post-1995 assets:

(a) 100% of the capital spending ($127.0 million in June 2013$) on the common network that Queensland Rail required miners to underwrite or Queensland Rail determined was required solely to facilitate coal services

(b) 72.6% of the remainder of spending ($49.3 million in June 2013$), reflecting coal's proportion of the total contracted paths (i.e. 77 of 106 contracted paths) (Queensland Rail, sub. no. 36: 8-10).[43]

In its submission on the 2013 DAU, New Hope said it accepted that investments incurred specifically for coal services should be fully allocated to coal services in the tariff. Similarly,

[43] Queensland Rail applied a similar approach to propose coal train path allocation percentage for the Macalister to Columboola section i.e. for post-1995 assets coal traffic pay 100% of end-user funded and coal-specific spending and 50% of the remainder of spending, reflecting coal's share of contracted paths (i.e. 14 of 28 contracted paths).

investments in non-coal services should be fully allocated to those services (New Hope, sub. no. 44: 14).

In its June 2014 consultation paper, the QCA observed that most of the post-1995 western system capital expenditure has been on the shared network and said that although one business (coal) is growing and another business (non-coal) is not, this is not a reason for coal to pay for 100% of the new infrastructure (QCA, June 2014: 35).

The QCA's consultation paper proposed for the DORC approach that coal traffic pay 72.6% of the common network spending, using Queensland Rail's proposed share. In doing so, the QCA proposed to depart from its December 2009 draft decision and accept an asset allocation based on coal's share of contracted (106) paths rather than available (112) paths, as it considered that contracted paths were verifiable and reflected clear evidence of customer demand (QCA, June 2014: 9, 35).[44]

Stakeholder submissions

On the allocation of end-user funded assets, Queensland Rail did not support QCA's position of allocating to coal a proportion of the assets customers had underwritten through access facilitation deeds (AFDs). Queensland Rail said the QCA's treatment created a disconnect between the reference tariff, in terms of a return on and of the relevant capital amount, and the rebate Queensland Rail was contractually required to provide to a customer-funder, noting that:

> *… the coal tariff reflects 72.6 percent of the capital costs of the relevant assets, but the rebate is set at 100 percent of the capital costs of the relevant assets (Queensland Rail, sub. no. 51, PwC report: 21).*

Queensland Rail said this would result in a revenue shortfall as the non-coal tariff was not equal to the coal reference tariff. Accordingly, Queensland Rail said that 'customer funded assets (through AFDs) must be preserved at 100% of their value' (Queensland Rail, sub. no. 51: 11).

On the 72.6% coal train path allocation, Queensland Rail accepted QCA's approach of using total contracted capacity for assessing the share of coal and non-coal services on the western system. Queensland Rail also said the path allocation should be allowed to vary over time to provide incentives for Queensland Rail to increase the number of paths available for coal and increase the efficiency of the network (Queensland Rail, sub. no. 51: 20; PwC report: 20).

However, New Hope said the use of contracted train paths provided Queensland Rail an incentive to limit the number of contracted paths, as:

> *Customers will pay the full cost of the true capacity when railing at the contracted path usage, then will overpay for this same capacity if this tariff is applied to path usages in excess of contract … Payment of the full tariff for additional paths provides an incentive to QR to limit the contracting of these paths, as QR's revenue will be maximised by withholding these paths from contracts and offering the paths on an ad-hoc basis (New Hope, sub. no. 50: 3).*

QCA analysis and draft decision

User-funded assets

On the allocation of end-user funded assets (through AFDs), the QCA considers it reasonable to apply a *pro rata* allocation to such assets based on coal's share of total train paths. That is

[44] Alternatively, the QCA's historic cost approach proposed allocating to coal traffic 100% of the post-1995 capital spending on the common network but none of the pre-1995 common network asset base. The historic cost allocation approach is not considered further, as the QCA's draft decision proposes to adopt the DORC approach for valuing assets (see section 8.3.2 of this draft decision).

based on the view that the underlying investment, where it is on the common network shared with other traffics, improves the standard of the track for all traffics that benefit from the resulting increased reliability and lower maintenance requirement.

In its December 2009 draft decision, the QCA proposed to assess coal reference tariffs on the basis that all traffics paid the same price, so each user's train service covered an equal proportion of the common network asset base (QCA, December 2009: 80). The QCA considers that this cost-sharing principle should apply regardless of who underwrote those assets.

The QCA also considers that any anticipated shortfall in non-coal revenue is a commercial matter for Queensland Rail and that tariffs charged to coal services should not subsidise the non-coal services.

Moreover, the QCA considers that a *pro rata* allocation of the incremental common network spending will create incentives for Queensland Rail to increase the number of train paths allocated to coal and promote efficient use of the network, as more capacity will be allocated to the highest and best possible use (i.e. coal train services).

Taking all this into account, the QCA proposes to apply a *pro rata* allocation based on coal's share of train paths to all incremental capital expenditure on the common network.

Allocation percentage

On train path allocation percentage for coal, the QCA accepts Queensland Rail's comment that it should be allowed to vary and considers that it should be reviewed at the beginning of each regulatory period. This provides an incentive to increase volumes allocated to the highest and best use (i.e. coal).

That said, the QCA notes that the denominator used for calculating the coal train path allocation is an issue for stakeholders. In its December 2009 draft decision, the QCA accepted Queensland Rail's proposal of using total *available paths* as the denominator. However, in its June 2014 consultation paper, the QCA proposed to accept Queensland Rail's denominator of total *contracted paths* (106 paths for Rosewood to Macalister) rather than the total *available paths* (112 paths for Rosewood to Macalister).[45]

Queensland Rail supported QCA's approach but New Hope said it created incentives for Queensland Rail to contract less and offer uncontracted paths on the tariff that was derived based on contracted paths.

Upon further consideration, the QCA considers that there is merit in the denominator for the train path charge reflecting all train paths, not just contracted paths. In doing so, the QCA accepts that the use of total available paths will provide Queensland Rail with better incentives to increase the number of paths for coal train services, which will promote the efficient use of the network. Relevantly, the QCA's position is also consistent with its earlier position in the December 2009 draft decision.

Therefore, the QCA proposes to apply coal train path allocation based on the total number of available paths rather than contracted paths i.e.:

(a) 68.8% for the Rosewood to Macalister section based on 77 of 112 available paths

(b) 41.2% for the Macalister to Columboola section based on 14 of 34 available paths.

[45] Queensland Rail reported the number of total available paths (112) in its supplementary submission on QCA's information request about its maintenance expenditure (Queensland Rail, November 2013(a)).

Allocating pre-1995 asset base

In the 2013 DAU, Queensland Rail proposed that for the Rosewood to Macalister section coal traffic pay, for pre-1995 assets, 61.7% of the common network assets. That share was based on adjusting the 72.6% coal path allocation with its proposed 15% sterilisation effect due to the metropolitan blackout (i.e. 85% metro adjustment of 72.6% path allocation) (Queensland Rail, sub. no. 36: 8-10)[46].

Stakeholders in their submissions on the 2013 DAU disagreed with Queensland Rail's proposed metropolitan effect. New Hope said that mobilising passenger trains before and after the peak periods coupled with frequent maintenance shutdowns meant the metropolitan effect was 31% (New Hope, sub. no. 44: 12-14; Aurizon, sub. no. 43: 9).

In its consultation paper, the QCA proposed to accept the 22% sterilisation effect identified by its consultant, B&H, rather than Queensland Rail's proposed number of 15% and proposed that coal traffic pay, for pre-1995 assets, 56.6% of the common network asset base (i.e. 78% metro adjustment of 72.6% path allocation) (QCA, June 2014: 7, 35).

Stakeholder submissions

Stakeholders presented differing views on the effect of the metropolitan peak-hour blackout on western system capacity.

Queensland Rail did not support reducing the western system asset base to reflect the metropolitan blackout. Queensland Rail said the rationale for reducing the value of pre-1995 assets to account for the metropolitan blackout period introduced asset stranding risk and added that:

> *This approach is effectively the same as the QCA taking the view that Queensland Rail was imprudent in its design of the pre-1995 assets, and has designed and constructed a network with 22 percent excess capacity. There has been no suggestion that the pre-1995 network was "over-built" (Queensland Rail, sub. no. 51: 10).*

Queensland Rail also said that if the QCA applied a metropolitan blackout, the sterilisation effect should be 12.1% based on its modification to B&H's methodology, as it considered B&H used a 'theoretical approach' rather than the 'operational approach' applied in QCA's 2009 and 2010 draft decisions (Queensland Rail, sub. no. 51: 13-19).

Conversely, other stakeholders (New Hope, Bentley and Aurizon) said B&H's estimate of 22% sterilisation effect underestimated the actual impact of metropolitan blackout on western system capacity (New Hope, sub. no. 50: 2; Bentley: 49: 2; Aurizon, sub. no. 48: 14-15). New Hope said B&H used a sound methodology for assessing the metropolitan blackout effect but suggested that it could be refined with access to further information from Queensland Rail by considering a wider time band (i.e. shoulder peak periods) and the timing of maintenance possessions between metropolitan system and western system (New Hope, sub. no. 50: 2).

QCA analysis and draft decision

The QCA considers that metropolitan peak-hour blackout is one of the key constraints on the use of the western system's infrastructure, particularly given that there is limited ability to marshall trains west of Rosewood to maximise use of off-peak metro train paths.

[46] Queensland Rail applied a similar approach to propose coal train path allocation percentage for the Macalister to Columboola section for pre-1995 assets of 42.5% (i.e. 85% metro adjustment of 50.0% path allocation).

The QCA considers that the metropolitan blackout effect has no bearing on the prudency/imprudency of capital spending since 1995, as it only applies to assets that were in place before coal services began in 1995 and were not built for hauling large volumes of coal. Therefore, it is appropriate to apply the metropolitan blackout to the pre-1995 assets to ensure that Queensland Rail did not get a return for capacity that was not available to coal trains.

That said, stakeholders retain very divergent views on the impact of the blackout period. Queensland Rail proposed an even lower blackout period of 12.1% than in its original submission of 15%. Likewise, other stakeholders considered the QCA's estimate of the blackout period of 22% to be conservative.

The QCA and its consultant, B&H, have further considered the blackout period in light of stakeholder comments. However, to date, the QCA has not received compelling new information to change its view.

In this regard, B&H advises that:

> *A more robust method of determining capacity is through a dynamic simulation, extended over a long period … QR has indicated it may provide evidence (such as train control charts or log records) to quantify the degree of alignment in maintenance possessions of the Western System and Suburban System. This data has not yet been made available (B&H, September 2014: 12).*

These matters have been communicated to Queensland Rail that has informally agreed to provide further information on the closure program for the western and metropolitan systems, master train plans demonstrating what actually occurred and a static saturation model of the master train plan.

Given this, the QCA is inclined to retain its earlier view of a metropolitan blackout period of 22% and will revisit this matter as part of forming a final view in its pending final decision.

8.4.2 Metropolitan system

Surat Basin coal trains travel through the metropolitan system for more than one-quarter of their journey from mine to port. Queensland Rail proposed (consistent with the QCA's 2009 draft decision) that the tariff derived from a cost build-up for rail infrastructure between Rosewood and Columboola (i.e. west of Rosewood) be applied to coal services' travel across the metropolitan system (i.e. east of Rosewood).

Queensland Rail said this was reasonable as it was likely the metropolitan asset valuation would be high and subsequent optimisation and allocation processes would be complex.

Queensland Rail said its proposal relied on the assumption that capital spending was proportional to the shares of gross tonne kilometres between the metropolitan and western systems. This would mean that the tariff per '000 gtk for one section would not be unreasonably increased by spending on another section (Queensland Rail, sub. no. 36: 7-8).

New Hope did not support Queensland Rail's proposal as other freight services paid 'much lower tariffs through the metropolitan system' and it was fair and equitable that all freight services paid a similar tariff through the suburban network.

The QCA in its consultation paper proposed to accept Queensland Rail's broad approach of extending the tariff derived for the rail infrastructure between Columboola and Rosewood, so it applied for the sections of the metropolitan system used by coal trains.

However, the QCA did not accept Queensland Rail's claim that there would be a consistent split in future capital investment between tracks to the east and west of Rosewood.

Rather, the QCA considered there needed to be an explicit mechanism for Queensland Rail to recover coal- and freight-specific investment in the metropolitan network. It proposed to do this by deriving an annual revenue requirement using a metropolitan-specific asset base, while fixing the remainder of the tariff for crossing the western system and indexing it by CPI.

The QCA said there had been substantial AFD-backed investment in the metropolitan system and a metropolitan asset base for incremental capital spending would provide Queensland Rail with revenue to cover the rebates on those AFDs.

Stakeholders' comments

The miners and Aurizon said it was right to have a separate tariff asset base for the metropolitan system, to give incentives to invest.

New Hope said the western system maintenance and operating costs should be extended across the metropolitan system, but the asset base should not be extended. This would mean that the metropolitan tariff would reflect operating and maintenance costs consistent with the western system, plus a return on and of coal-specific spending on the metropolitan system since 1995 (New Hope, sub. no. 50: 15-17).

Yancoal said that extending the western system tariff across the metropolitan system was 'understandable but considered heavy-handed given there is very limited coal specific infrastructure in that system' (Yancoal, sub. no. 52: 4).

Yancoal and New Hope said that given the potential for a split that would have ARTC managing the western system and Queensland Rail managing the metropolitan system, the QCA should consider separating the asset bases and/or tariffs for the two systems. Yancoal said this would 'avoid future problems' (Yancoal, sub. no. 52: 4). New Hope was concerned the split could result in combined tariffs higher than the tariff that was approved if the network was not divided (New Hope, sub. no. 50: 16).

Queensland Rail said its 'initial view' was that the QCA's approach of extending the western system tariff across the metropolitan system was reasonable. However, it was concerned that the QCA proposal created a 'de facto' metropolitan RAB, so it reserved the right to further consider the matter (Queensland Rail, sub. no. 51: 30).

Aurizon also said its analysis of the way the metropolitan asset charge had been derived showed that 20 years' remaining life had been used for the assets and that was different from the western system asset lives used elsewhere in the QCA's consultation paper. It asked that the QCA clarify the way the charge was derived (Aurizon, sub. no. 48: 33).

QCA analysis and draft decision

The QCA proposes to retain the treatment of the metropolitan tariff that it set out in the consultation paper.

As stakeholders have suggested, a separate and transparent approach for the metropolitan tariff will be particularly important if the western and metropolitan systems end up under separate ownership or management.

The QCA notes that New Hope has suggested extending the operating and maintenance costs from the western system across the metropolitan system, but not extending the asset-based costs (i.e. the return on and of capital).

However, the QCA considers that it is reasonable for coal services to pay for a portion of the capital cost of the existing metropolitan network, and that the simplified approach set out in the consultation paper is a reasonable way to do this.

Moreover, as Queensland Rail has not presented an alternative approach, and has said its initial view is that the consultation paper approach is reasonable, the QCA sees no reason to change its position.

Accordingly, the QCA proposes to set the metropolitan tariff so that it gives Queensland Rail an incentive to make efficient investments in the metropolitan system by:

(a) maintaining an asset base for future investment to support coal and freight traffic in the metropolitan system and using it to derive an annual revenue requirement

(b) using all metropolitan coal services, including paths used by services to the Ebenezer loading point, to calculate the component of the access price that recovers the metropolitan asset base

(c) fixing the remainder of the tariff for crossing the metropolitan system at the level derived in approving the 2013 DAU, and then increasing it annually by CPI.

The QCA confirms the analysis by Aurizon that the metropolitan asset charge in the consultation paper was modelled in such a way that the remaining life was 20 years, and did not decline in each year of the roll-forward. In this draft decision, the QCA has corrected the treatment of depreciation of the metropolitan asset base to be consistent with the approach for other similar assets in the western system. This means that the assets are depreciated over 35 years, on a straight-line basis.

8.4.3 Form of regulation and tariff structure

The QCA's 2009 draft decision, and its 2010 pricing draft decision, set out a price cap form of regulation for the western system coal tariff. The western system coal tariff was based on the undertaking's pricing principle that, for the purpose of assessing revenue adequacy on a capacity constrained system, the QCA could assume all services were paying the highest tariff (2008 undertaking, cl. 6.3.1(b)(ii)).

Queensland Rail's 2013 DAU proposed to retain that revenue adequacy provision from the 2008 undertaking. It proposed a two-part tariff, split between a train path charge, and a weight-and-distance-based component (i.e. $/'000 gtk). This was consistent with the structure in the QCA's December 2009 draft decision and June 2010 pricing decisions.

Aurizon said Queensland Rail's 2013 DAU proposal was asymmetric, as it gave all the benefit of efficiency improvements (e.g. through reduced costs or increased volumes) to Queensland Rail. At the same time, Queensland Rail was protected from downside risks by take or pay arrangements that would largely recover revenue lost to non-performance of contractual services (Aurizon Holdings, sub. no. 43: 11-12).

In its June 2014 consultation paper, the QCA proposed to accept Queensland Rail's proposal for a price cap as it provided incentives for Queensland Rail to support volume increases. The QCA also supported a two-part tariff (i.e. half being a per train path charge and the other half a volume- and distance-based charge) as:

(a) both tariff components gave Queensland Rail an incentive to find extra train paths, and to work with train operators to find ways to use more intensively the existing paths

(b) the train path charge limited the gains for increases in volumes per rail consist (i.e. increases caused by above-rail investment in new rolling stock), as it did not vary with cargo size.

The QCA noted there was some potential for tariffs paid by coal services to recover more than 100% of the post-1995 assets from the historical cost tariff, under a price cap approach, if actual volumes were higher than forecast volumes. However, since the tariff would only be for the term of the undertaking, any over-recovery of revenues would be reassessed and re-set at the end of the four-year tariff period.

Stakeholders' comments

Aurizon said it favoured a price cap for the western system because a revenue cap did not provide an incentive for Queensland Rail to deliver the additional capacity that was available but not contracted (Aurizon, sub. no. 48: 17, 26).

Aurizon said the take or pay mechanism, combined with the price cap approach, was flawed as it had the effect of allowing Queensland Rail to use take or pay to exceed its target revenue without exceeding its target volumes (Aurizon, sub. no. 48: 16-23).

However Aurizon said the two-part tariff proposed by the QCA blunted the incentive for Queensland Rail to increase payloads per train. It said that a straight $/'000 gtk charge would provide a stronger incentive for Queensland Rail to increase axle loads to 20 tonnes, and would provide the extra revenue to help pay any associated maintenance costs if train weights increased (Aurizon, sub. no. 48: 24-25).

New Hope said it favoured a two-part tariff, as that allowed the benefits of efficiencies from higher capacity trains to be shared (New Hope, sub. no. 50: 18).

Stakeholders also said the tariff should be clearly split between the metropolitan system and the western system, for transparency, to address the potential that the two systems will end up with different owners and to ensure that the correct investment recovery and incentives were provided for each system (New Hope, sub. no. 50: 19; Yancoal, sub. no. 52: 4).

QCA analysis and draft decision

The QCA agrees with stakeholders that a price cap provides appropriate incentives for Queensland Rail to provide additional capacity. The QCA therefore proposes to accept the price cap approach that Queensland Rail has proposed in the 2013 DAU, consistent with the pricing approach that has applied in the 2006 and 2008 undertakings' western system tariffs.

The QCA notes Aurizon's argument that a one-part tariff based on gtks would provide Queensland Rail with an even greater incentive to increase volumes. However it is not evident that the increased incentive would be more effective than that from the two-part tariff. In any case, the two-part tariff also has the effect of rewarding Queensland Rail for providing additional train paths, while giving incentives for efficiencies in the downstream (i.e. above-rail) market that increase train capacity.

Further, the two-part tariff creates a distance taper that encourages development of coal resources, which is in the public interest.

Therefore QCA proposes to retain the two-part tariff that Queensland Rail has proposed, consistent with the tariff that has applied in the 2008 undertaking, as amended with new prices in 2010.

The QCA agrees with stakeholders that a clear split of the charges between the western system and the metropolitan system will aid transparency, particularly if the two systems end up under different ownership or management. These prices are set out below in Section 8.4.4.

The QCA also notes Aurizon has also called for changes to the way take or pay is calculated. This is discussed in Section 3.5 of this draft decision.

8.4.4 Tariff level

Queensland Rail proposed a tariff of $22.22/'000 gtk based on the methodology in its submission.

Stakeholders said the western system tariffs were much higher than those charged on other comparable and competing rail systems including the Moura system in central Queensland, and the Hunter Valley coal network in New South Wales. This meant that, even though their on-mine costs were low, the rail costs made their operations uncompetitive (New Hope, sub. no. 44: 5-9; Peabody, sub. no. 45: 1-2; Yancoal, sub. no. 47: 1-2).

The QCA in its consultation paper proposed a number of changes to the costs and allocations in Queensland Rail's DAU, including:

(a) a metropolitan blackout of 22% (compared with 15% proposed by Queensland Rail)

(b) a capital indicator of $81.7 million over the four-year undertaking period

(c) maintenance spending of $86.0 million over the four years

(d) operating costs of $20.4 million over the four years.

The QCA used these inputs to calculate two different tariff options, consistent with the DORC train path allocation and the historical cost approaches discussed in Section 8.3.2.

For the DORC approach, the QCA applied:

(a) a train path allocation to coal of 72.6% (50% for Macalister to Columboola) and annual volumes of 7.5 million tonnes

(b) an opening asset value for Rosewood to Columboola of $259.0 million.

This gave a tariff of $17.21/'000 gtk, split into $4220 per train path and $8.61/'000 gtk.

For the historical cost approach, the QCA estimated that a price of $13.59/'000 gtk would provide for recovery of post-1995 capital spending of $133.3 million, and ongoing operating and maintenance costs, but nothing for pre-1995 assets. This would be split into $3,332 per train path, and $6.79/'000 gtk.

Stakeholder submissions

The miners and Aurizon reiterated their past comments that western system coal tariffs were much higher than those in competing coal systems, while Queensland Rail said it was not the QCA's role to take into account the effect of short-term cost pressures or market conditions on Queensland Rail's customers.

Queensland Rail said the QCA should 'determine a ceiling price based upon appropriate and pure building blocks, with the approved reference tariff being a reasonable return that is not influenced by external factors which exist at a particular point in time' (Queensland Rail, sub. no. 51: 27).

Queensland Rail said it had demonstrated its goodwill towards the coal industry reinstating, largely at its cost, the Toowoomba Range after the 2011 floods. And, in a similar vein, it said it

might choose to negotiate directly with end users for price relief as a temporary subset of the ceiling price in cases of genuine hardship (Queensland Rail, sub. no. 51: 29).

Queensland Rail also said there was 'no existing requirement in Queensland Rail's DAU' to compare prices with other coal systems. 'Adjusting tariffs on the basis of benchmarking against other systems risks contradicting the pricing principles by forcing comparability where there are valid costs and/or risk differences' (Queensland Rail, sub. no. 51: 28).

Yancoal said that if Queensland Rail took a long-term view and priced at a level that assumed higher tonnages, then there was a stronger chance that mines could expand. For example, Yancoal said that its Cameby Downs mine (that uses the Columboola loading point) had plans to expand from 1.4 million tonnes to 8 million tonnes (Yancoal, sub. no. 52: 3). New Hope said that while there was a risk that high prices could create a 'downward spiral' and strand Queensland Rail's assets, competitive above- and below-rail tariffs could allow western system volumes to be at least 20 million tonnes (New Hope, sub. no. 50: 14).

QCA analysis and draft decision

The QCA notes the comments from coal miners that a high price for coal haulage on the western system will stifle growth or cause the industry to shrink. It also notes the comments from Queensland Rail that relative prices are not a matter the QCA should consider.

While the QCA does not consider that it is precluded from taking into account relative prices, it accepts that such comparisons are among a range of factors that it must take into account when assessing a tariff under the approval criteria in the QCA Act.

In the case of the western system tariff, the QCA considers it may be in Queensland Rail's interest to adjust prices to stimulate demand, given the potential for both Queensland Rail and its customers to capture benefits from economies of scale if volumes rise.

However, the QCA has in this assessment focused on ensuring Queensland Rail receives a reasonable return on its investment in the western system, and recovers efficient costs of providing below-rail services (ss. 138(2)(b) and (g) and 168A(a) of the QCA Act). At the same time, it has had regard to the other approval criteria, including the efficient operation, use of and investment in Queensland Rail's infrastructure and the interests of access seekers and holders (ss. 138(2)(a), (e) and (h)).

With those criteria in mind, based on the factors discussed in the earlier sections of this chapter (Chapter 8), the QCA has applied:

(a) a metropolitan blackout of 22%

(b) a capital indicator of $81.7 million ($78.8 million in June 2013$) over the four-year undertaking period

(c) maintenance spending of $87.0 million ($81.5 million in June 2013$) over the four years

(d) operating costs of $18.9 million ($17.8 million in June 2013$) over the four years

(e) a train path allocation to coal of 68.8% (41.2% for Macalister to Columboola)

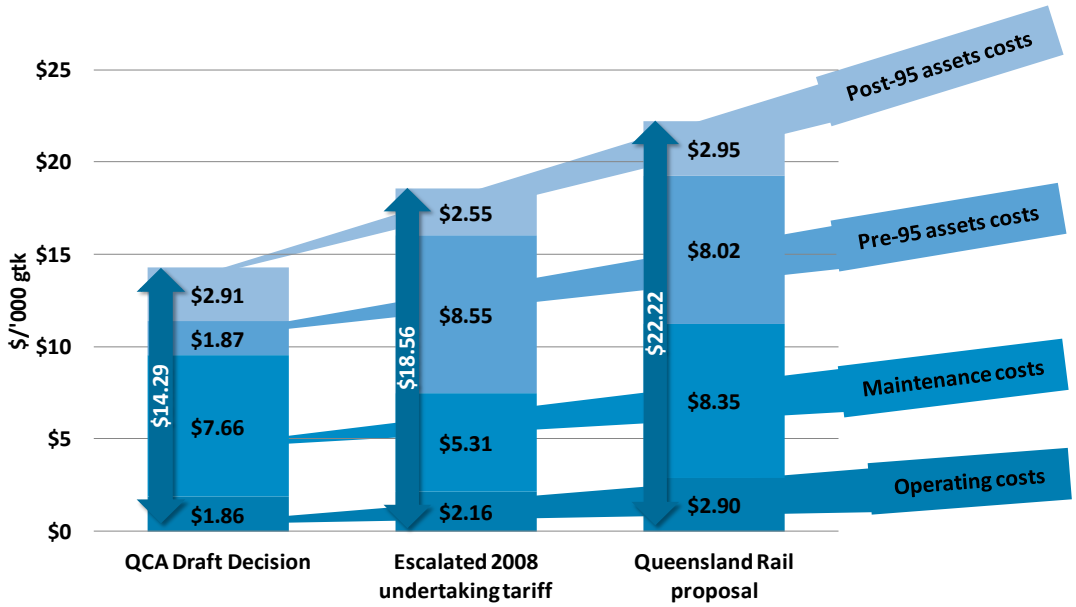
(f) annual volumes of 7.5 million tonnes (77 weekly loaded coal paths)

(g) an opening asset value for Rosewood to Columboola of $155.7 million.

This gives a tariff of $14.29/'000 gtk, split into $3,510.13 per train path and $7.15/'000 gtk. This is 36% lower than Queensland Rail's proposed 2013–14 tariff of $22.22/'000 gtk, and 23% lower than the 2013-14 tariff of $18.56 that applied under the existing (2008) undertaking.

The breakdown of the main components of the QCA's proposed tariff, the existing tariff and the tariff Queensland Rail proposed in its June 2013 DAU is illustrated in **Figure 8** below. It shows that the QCA's proposal includes most of the maintenance costs submitted by Queensland Rail and almost all of the post-1995 asset costs. The big change is the lower amount proposed by the QCA for the return on and of pre-1995 assets, which reflects the application of the QCA's assessment of asset values (see Section 8.3.2 of this draft decision). It is noted that the lower amount for operating costs in the QCA's proposed tariff reflects both the QCA's adjustments to the operating costs proposed by Queensland Rail and a lower allowance for tax.

Figure 8: Cost breakdown comparison for 2013-14 tariffs



Note: a) Asset costs are comprised of return on and of capital. b) Operating costs include an allowance for tax.

It is noted that, for the period of the 2013 DAU (2013–14 to 2016–17) the volume and distance based charge will be $7.15/'000 gtk for both the western system and the metropolitan system. However this is likely to change when the subsequent undertaking is approved, given the proposed treatment of the metropolitan tariff (see Section 8.4.2).

The western system train path charge is divided into $2,518.89 for the western system (i.e. west of Rosewood), and $991.24 extended across the metropolitan system (i.e. east of Rosewood).

Metropolitan incremental asset charge

The QCA has also calculated the additional train path charge for the metropolitan incremental asset base, as discussed in Section 8.4.2. It has amended the asset lives to 35 years (increased from 20 years used in the consultation paper) to be consistent with the treatment for the western system.

The metropolitan opening asset value is $12.28 million, largely reflecting the spending on new coal-only holding tracks at Fisherman Islands, that were built during the 2009–13 tariff period. The required addition to the 2013–14 charge to recover the return on and of capital on this amount is $98.18/train path.

Ebenezer trains will pay the $14.29/'000 gtk tariff extended from the western system, plus this additional charge of $98.18/train path.

The total metropolitan system train path charge, for trains originating in the western system, will be $1,089.42 (the $991.24 charge extended from the metropolitan system, plus the $98.18 metropolitan asset base tariff).

Draft decision 8.2

- **The QCA requires Queensland Rail to amend its proposal to include a western system coal tariff of $14.29/'000 gtk, based on the assumptions and inputs set out in this Chapter 8. The tariff will be levied on the basis of:**
  - **(a) for trains originating in the western system**
    - **(i) an AT1 tariff component of $7.15/'000 gtk**
    - **(ii) an AT2 tariff component of $2,518.89 per train path for the western system and $1,089.42 per train path for the metropolitan system (including the $98.18 metropolitan asset tariff)**
  - **(b) for trains originating in the metropolitan system**
    - **(i) an AT1 tariff component of $14.29/'000 gtk**
    - **(ii) an AT2 tariff component of $98.18/train path (the metropolitan asset tariff).**
- **For the purposes of the take or pay mechanism discussed in Section 3.5 of this draft decision, the annual target revenue for 2013–14 for the western system is $38.8 million and for the metropolitan system it is $17.2 million.**

9 INVESTMENT FRAMEWORK, PLANNING AND COORDINATION

The 2013 DAU should provide stakeholders with clarity and certainty on Queensland Rail's obligations regarding the extension of its network.

Part 1 of the 2013 DAU outlines Queensland Rail's investment obligations.

Stakeholders said Queensland Rail has given itself too much discretion and removed any obligation to extend the network. This is not consistent with the requirements of Part 5 of the QCA Act.

The QCA accepts stakeholder concerns and has proposed amendments to oblige Queensland Rail to extend the network regardless of who funds the extension. The proposed amendments seek to protect Queensland Rail's legitimate business interests and provide clarity and certainty to access seekers in the negotiation process.

9.1 Introduction

A key component of an effective rail access undertaking is an efficient, transparent and accountable capacity and investment framework to underpin the development and investment in extensions to the rail network. Consistent with S. 138 of the QCA Act, an access undertaking must have regard to the interests of persons who may seek access to the service as well as the broader public interest and the benefits of expanding access to promote competition in related markets.

The diverse, complex and disparate needs of Queensland Rail's customers requires a flexible and efficient capacity and investment framework. Queensland Rail's customer base includes the Queensland Government, coal and bulk resources industries, agriculture and livestock industries, general freight transportation and rail haulage operators. Any future investment in Queensland Rail's network must consider multi-faceted demand scenarios over the medium to long term. However, it must do this concurrently with short term market demand fluctuations and varying degrees of passenger freight intensity within the Brisbane metropolitan network and Traveltrain.

Queensland Rail has traditionally managed and maintained its network to meet its legislative obligations as a rail infrastructure manager and to deliver its contracted traffic task. In the last 15 years, Queensland Rail has relied on upfront capital contributions from new customers where their access to the service was conditional on asset upgrades to the rail network (e.g. increasing axle loads, strengthening infrastructure and lengthening passing loops). Upfront capital contributions were also sought for new spur lines required to connect a rail load out to the network. These capital contributions typically involved one customer, were structured simply and provided a funding customer with a guaranteed revenue stream (equal to the return on and of capital recovered by Queensland Rail through access charges) over the economic life of the asset. This approach was adopted by Queensland Rail in the western system and enabled coal companies to commence operations and export coal through the Port of Brisbane.

The issues associated with user funding rail upgrades became more complex when the QCA considered these matters in the context of Aurizon Network. This is because user funding arrangements required for central Queensland mainline and greenfield rail expansions involved multiple customers and significant funding obligations (e.g. the Goonyella Abbot Point Expansion and Wiggins Island Rail Project both involved significant expenditure of at least $900

million). Whilst both projects were ultimately funded by Aurizon Network (with side funding agreements and/or access conditions), coal customers sought the right to fund such projects without recourse to Aurizon Network's funding demands for an above regulatory rate of return.

The establishment of a balanced user funding rail investment framework was a key outcome from the Aurizon Network 2010 Access undertaking. The ARTC subsequently included an investment and user funding framework in its approved 2011 Hunter Valley Access undertaking. In approving these user funding investment frameworks, the QCA and ACCC were guided by the relevant legislative obligations contained in the QCA Act and the Competition and Consumer Act 2010.

Developing an effective and balanced standard user funding framework has been a specific focus of the QCA since the approval of Aurizon Network's 2010 Access undertaking. In May 2014, the QCA released a Position Paper on Aurizon Network's 2013 Standard User Funding Agreement (SUFA) Draft Amending Access undertaking (DAAU). This included an independent report prepared by Grant Samuel which identified a number of third party financing principles required to deliver a workable, bankable and credible user funding agreement consistent with the QCA Act. The QCA is working with both Aurizon Network and the coal industry to translate these third party financing principles into a SUFA which would then become a standard template for future investment transactions.

There are a number of key lessons in these previously approved undertakings and subsequent SUFA processes that are not referenced in Queensland Rail's 2013 DAU. These need to be addressed for the investment framework in the 2013 DAU to be approved by the QCA.

Indeed, having regard to this regulatory precedent, the 2013 DAU includes network extension obligations that are unfairly balanced in Queensland Rail's favour. Many of the issues the QCA raise with the investment obligations in Part 1 of the 2013 DAU are based on previous QCA and ACCC regulatory decisions covering Aurizon Network and ARTC. Whilst these regulatory processes are summarised below, Queensland Rail should refer to the detail contained in these previously approved access undertakings. This will enable Queensland Rail to better reflect its rights and obligations around the development of extension projects within its 2013 DAU. This analysis will demonstrate that many of the recommendations contained in this chapter have already been implemented in other rail infrastructure regulatory regimes.

Aurizon Network's investment framework

Aurizon Network's 2010 Access undertaking outlines Aurizon Network's obligations to facilitate, but not fund, an extension and third-party investment in its network. Specifically, Schedule J (see Appendix E) identifies four foundation principles for an effective user funding framework.

(a) Aurizon Network cannot be forced to fund an extension other than in accordance with an approved access undertaking or the provisions of the QCA Act regarding the determination of access disputes.

(b) To the extent that Aurizon Network does invest in rail transport infrastructure to provide a declared service, the QCA can determine the rate of return that is commensurate with the risk of that investment.

(c) Aurizon Network should not be able to exploit its monopoly power.

(d) Users should have the right to fund extensions.

While these principles seem straightforward, the complexity of developing an effective SUFA has been made evident in the period since the Aurizon Network's 2010 Access undertaking was

approved. Aurizon Network and the Queensland Resources Council (representing Queensland's coal companies) have negotiated for over three years to develop a detailed, viable SUFA. These negotiations resulted in Aurizon Network resubmitting another SUFA DAAU with the QCA in July 2013. However, it was apparent that stakeholders still had material concerns with the resubmitted SUFA. After considering the DAAU and stakeholder submissions, the QCA indicated in its May 2014 Position Paper that the 2013 SUFA DAAU was not a credible competitive alternative to Aurizon Network exercising its monopoly power in the funding of new extensions.

The May 2014 Position Paper outlined the three overarching principles required for developing an effective SUFA:

(a) workable – a SUFA must achieve the intended outcome with an appropriate allocation of risk and liabilities. It must recognise the legitimate business interests of the access provider and be in the interests of access seekers and investors in the network. It must be able to be executed by all parties without negotiation, if necessary

(b) bankable – a SUFA must be financeable by access seekers and third party financiers with recourse to the funded assets and rights. This requires there be a high level of confidence that the expected returns will be delivered and that the asset will be appropriately operated and maintained over its lifecycle

(c) credible – a SUFA must not create unnecessary risks and uncertainties for users and potential financiers or overlay unnecessarily high transaction, tax or finance costs on an extension project otherwise the funding agreement can never be a credible alternative to Aurizon Network undertaking the extension itself.

The QCA's consideration of the 2013 SUFA DAAU is ongoing and it is continuing to consult on the most appropriate SUFA financing structure.

The May 2014 Position Paper also highlighted the importance of an effective expansion process to underpin the negotiation of a workable, fundable and credible SUFA. The QCA is considering the expansion issues in Aurizon Network's 2013 DAU. The QCA understands the need for a robust expansion process inclusive of a study funding agreement. A customer must be able to align the development of a rail expansion project to its internal coal mine investment review process. A robust expansion process removes a customer's risk that Aurizon Network could use its monopoly power in rail infrastructure to hold up studies on expansion projects and extract a premium from a customer who is constrained by its own investment timeframes for a mine project.

ARTC's investment framework

In approving ARTC's 2011 Hunter Valley Access undertaking, the ACCC acknowledged the QCA's decision on Aurizon Network's 2010 Access undertaking. The ACCC also noted the differences between ARTC, as a vertically separated service provider, and Aurizon Network, as a vertically integrated service provider. This consideration informed the level of regulatory intervention deemed necessary by the ACCC.

ARTC's 2011 Hunter Valley Access undertaking has a capacity and investment framework (i.e. Chapters 7-11) which sets out clear and accountable capacity expansion processes to underpin future extensions to its network to address increasing demand, regardless of who funds the extension.

ARTC highlighted four key elements essential to a robust, transparent and efficient capacity and investment framework:

(a) an annual ARTC Hunter Valley corridor capacity strategy, with a detailed industry consultation process underpinning its development

(b) processes whereby ARTC will identify, study, fund and construct additional capacity

(c) processes whereby access holders, access seekers and supply chain groups (Rail Capacity Group (RCG) and Hunter Valley Coal Chain Coordinator (HVCCC)) and coal companies can identify investment projects to increase capacity in the network

(d) processes whereby access holders, access seekers, supply chain groups and coal customers can user-fund the study and construction of an expansion project when ARTC decides it is not willing to fund the study and/or construct the expansion project.

The user funding option is an essential component of ARTC's capacity and investment framework. In particular, it includes financial and technical criteria to provide an objective test against which ARTC's expansion decisions can be reviewed. These criteria then inform the ACCC's deliberations on any access disputes brought before them for arbitration.

Whilst not developing a pro-forma SUFA, ARTC has highlighted that any future user funding agreement will include the following four elements:

(a) ARTC and investors are each entitled to receive a regulated rate of return on the capital they have invested in the Regulatory Asset Base (RAB). This return will reflect the return on and of the capital each party has invested over the economic life of the assets in the RAB. ARTC will rebate the return to investors as it is recovered through the payment of access charges and end of year adjustments.

(b) Defined timelines within which ARTC would deliver a user funded project (from concept and feasibility assessment through to construction and commissioning).

(c) Clarity on project controls and triggers whereby ARTC or other stakeholders can take a new rail project through each investment study stage to the point where a funding agreement can be executed for the construction of the project.

(d) Transparent processes through which ARTC or an investor/coal company can seek ACCC or RCG pre-approval to incorporate a new asset into the RAB.

ARTC is not a construction company and tenders out all construction works to the private sector. Given legal precedent on standard commercial construction contracts, ARTC has left this issue to be managed via the standard contracting process, backed up by arbitration and the commercial courts.

Queensland Rail's investment framework

In considering Queensland Rail's extension obligations in the 2013 DAU and having regard to the assessment criteria in s. 138(2) of the Act, the QCA considers that Queensland Rail should provide a robust investment pathway for access seekers to access the declared service in situations where such access is conditional on an extension to the network being constructed and commissioned. The QCA is also aware of the benefits of consistency between Queensland Rail and Aurizon Network's capacity and investment frameworks. This means the QCA is considering Queensland Rail's 2013 DAU in light of recent developments in Aurizon Network's SUFA DAAU and 2013 DAU processes.

Importantly for the QCA, Queensland Rail's capacity and investment framework should be balanced in a way which protects the legitimate business interests of Queensland Rail whilst providing regulatory certainty that an extension pathway exists and can be triggered by an

access seeker or an access seeker's customer, irrespective of whether Queensland Rail or a third party funds the extension.

In considering a more balanced capacity and investment framework in the 2013 DAU, the QCA has focused on how Queensland Rail has proposed to deal with these matters in its 2013 DAU, namely:

(a) Obligation to Extend (cl. 1.4.1 of the 2013 DAU)

(b) Funding Arrangements (cls. 1.4.2 and 1.4.3 of the 2013 DAU).

9.2 Obligation to extend

The QCA Act allows the QCA to make an access determination requiring Queensland Rail to extend the network or permit the extension of the network if it is required by an access seeker in order to gain access to the declared rail service (s. 118(1)(d)). However, the QCA cannot require Queensland Rail to fund the costs of extending the network (s. 119(2)(c))[47].

The QCA considers that Queensland Rail should provide certainty and clarity regarding how an access seeker can obtain access to the network when an extension to the network is required to provide that access.

Queensland Rail's 2013 DAU

The 2013 DAU obliges Queensland Rail to extend its network when an access seeker requires an extension to access the network and Queensland Rail is willing to fund the extension. The 2013 DAU defines an extension to include an enhancement, expansion, augmentation, duplication or replacement of all or part of the network (excluding private infrastructure).

Where Queensland Rail decides (in its absolute discretion) that it will not fund the extension, then the 2013 DAU only obliges Queensland Rail to discuss funding options with an access seeker or an access seeker's customer and use reasonable endeavours to negotiate and enter into a funding agreement on terms agreeable to both parties (cl. 1.4.1(b)).

Moreover, the 2013 DAU identifies a number of extension project preconditions which must be met by access seekers before Queensland Rail will extend the network. A number of these preconditions give Queensland Rail discretion to decide whether or not the preconditions have actually been met.

Queensland Rail's proposed preconditions are:

(a) The access seeker funds the costs and expenses to be incurred by Queensland Rail in connection with construction and meets Queensland Rail's creditworthiness test (this test is not defined) (cl. 1.4.1(a)(iii)).

(b) Queensland Rail bears no cost or risk in relation to constructing, owning and managing the extension (cl. 1.4.1(a)(iv))

(c) The access seeker obtains all necessary authorisations and other consents required for Queensland Rail to construct the extension (cl. 1.4.1(a)(v)).

(d) The access seeker obtains all rights and interests in land which in Queensland Rail's opinion are necessary for the extension (cl. 1.4.1(a)(vi)).

[47] Unless Queensland Rail has voluntarily agreed to do so within its access undertaking (s. 119(4A)).

(e) The extension meets Queensland Rail's technical, safety, engineering and operational requirements and does not adversely impact on existing capacity or Queensland Rail's legitimate business interests (cl. 1.4.1(a)(vii)).

(f) The access agreements underpinning the extension are executed on terms and conditions satisfactory to Queensland Rail (cl. 1.4.1(a)(viii)).

(g) The access agreements have become unconditional except for conditions relating to the construction of the extension (cl. 1.4.1(a)(ix)).

(h) All construction, funding, operational and other arrangements relating to the extension have been executed and become unconditional (cl. 1.4.1(a)(x)).

Stakeholders' comments

A lack of balance

All stakeholders said that Queensland Rail's obligation to extend the network was imbalanced (New Hope, Glencore, Yancoal, Peabody, Asciano, Aurizon and QRC). They argued the drafting in the 2013 DAU gives Queensland Rail absolute discretion when determining whether an access seeker has met all the preconditions required for an extension of the network. For example:

> *The requirement that QR bears no cost or risk in relation to constructing, owning, operating and managing the extension is unlikely to ever be achievable (New Hope, sub. no. 31: 2).*
>
> *Given the number of items on which QR's opinion, satisfaction or discretion is involved, the current cl. 1.4.1 effectively gives QR complete discretion as to whether it should be required to make an investment in an Extension (Glencore, sub. no. 30: 12).*
>
> *The 2013 DAU investment framework section 1.4.1a)(iv) indicates that Queensland Rail should bear no cost or risk in relation to constructing, owning, operating or managing the extension. Asciano believes that requirement that Queensland Rail bear no risk is too broad and the requirement should be limited to Queensland Rail bear no costs of constructing the extension (Asciano, sub. no. 31: 14)*

Definition of extension allows for deferral of maintenance

All stakeholders were also concerned with the definition of 'extension' in the 2013 DAU, namely its inclusion of a specific reference to asset replacement. They are concerned Queensland Rail may defer or delay maintenance costs so that access seekers will be required to user fund the replacement of assets as a precondition to renewing existing access rights. There is also a concern any deferral or delay in maintenance activities within the term of existing access agreements will adversely impact the contracted standard of service. Stakeholders have requested that the 2013 DAU incorporate a specific obligation on Queensland Rail to invest in the network to meet its existing contractual obligations.

QCA analysis and draft decision

A balanced framework

The QCA accepts that an obligation on Queensland Rail to extend the network must be implemented in a way which protects Queensland Rail's legitimate business interests in a manner consistent with the QCA Act. At the same time, an extension obligation must be sufficiently balanced so access seekers or an access seeker's customer have regulatory and commercial certainty that an extension can be constructed regardless of whether Queensland Rail is willing or able to fund it; and within a timeframe which aligns with an access seeker's own expansion plans.

The 2013 DAU is clearly imbalanced. It provides excessive discretion to Queensland Rail when considering an extension to the network. It removes the QCA's ability to arbitrate any access disputes regarding an extension to the network. It is also silent on the rights of a user funder in seeking to fund an investment in the network. This makes Queensland Rail's proposal unworkable and inconsistent with the QCA's undertaking approval criteria in the QCA Act.

A balancing of the rights and obligations of all parties to an extension is essential to provide a workable, bankable and credible investment alternative to Queensland Rail. Consistent with QCA's position paper on Aurizon Network's SUFA DAAU, Queensland Rail must address its own rights and obligations as well as an access seeker's rights and obligations in gaining access to the declared service. This means an extension obligation in the 2013 DAU must provide certainty and objectivity around Queensland Rail's decision making criteria regarding access applications involving an extension to the network, a transparent, objective and staged investment process for a third party to fund an extension, clarity on the provision of access to the network and certainty of the regulatory return payable to the investor in the extension.

Where Queensland Rail and access seekers are unable to resolve differences in the negotiation of an extension project, then either party must be able to refer the matter for independent arbitration in accordance with the arbitration processes in the QCA Act and the dispute resolution processes in the 2013 DAU. Any future arbitration must be able to reference legislative obligations and clearly defined, objective decision making criteria in order to resolve a dispute.

Accordingly, the QCA requires amendments to cl. 1.4.1 of the 2013 DAU so that access seekers have a genuine alternative to obtain access to the network when access is conditional on an extension to the network and Queensland Rail is unwilling to fund. In addressing the lack of balance in Queensland Rail's investment framework, the QCA is seeking clarity, objectivity and reasonableness on Queensland Rail's:

(a) investment decision making process

(b) eligibility rules for parties to fund an extension

(c) financial capacity test to be met by funding parties

(d) obligation to extend where it is at no cost to itself

(e) technical, safety, environment and land responsibilities

(f) obligation to maintain the operational integrity of the network.

These recommendations are consistent with the QCA's approach with Aurizon Network and the ACCC's approval of ARTC's 2011 Hunter Valley Access undertaking.

Draft decision 9.1

- **The QCA requires Queensland Rail to amend the extensions provisions in its proposal (cl. 1.4.1) to:**
  - **(a) remove all discretionary references in Queensland Rail's decision to extend**
  - **(b) include an obligation on Queensland Rail to extend the network regardless of which party funds the extension.**

Third party funding

The 2013 DAU refers only to an access seeker or an access seeker's customer being a User for the purposes of negotiating a user funding agreement (cl. 1.4.1(b)(i) and (ii)). The requirement for a funder to be an access seeker or an access seeker's customer is unnecessarily restrictive and should be amended to include a reference to an access seeker's nominee or an access seeker's customer or nominee.

The QCA's May SUFA Position paper identified that a key element of an effective SUFA is its ability to be funded by both users and third party financial institutions. If a SUFA is not financeable through third-party debt and equity markets, its utility is limited to those users with the financial capacity to absorb the risks associated with a SUFA. The QCA recommends Queensland Rail broaden the investment base to third party financiers to increase the ability for rail operators and their customers to secure the most efficient investment funding for an extension to the network.

Significant resources have been expended by Aurizon Network, industry stakeholders and the QCA in obtaining expert technical, legal, financial and tax advice on developing a workable, bankable and credible SUFA. There is little merit in the QCA duplicating this process with respect to Queensland Rail's 2013 DAU. The QCA expects that many of the technical, legal, financial and tax issues to be resolved through the SUFA process, will be applicable to Queensland Rail. Accordingly, the QCA recommends the 2013 DAU require Queensland Rail take account of any SUFA developed, or which is being developed, by Aurizon Network, when negotiating a funding agreement with an access seeker.

Draft decision 9.2

- **The QCA requires Queensland Rail to amend the extension provisions in its proposal (cl. 1.4.1) to:**
  - **(a) provide for third-party funding of an extension to the network**
  - **(b) have regard to, as far as it is relevant to Queensland Rail, the SUFA developed, or which is being developed, by Aurizon Network.**

Financial capacity test

The 2013 DAU gives Queensland Rail the ability to dictate the financing terms and conditions through which an access seeker is to provide funding for an extension project (cl. 1.4.1(a)(iii)).

(a) The inclusion of the words 'in advance' implies Queensland Rail would require an access seeker to pay 100% of capital upfront to Queensland Rail. In situations where the project may have a long construction profile (i.e. 6 to 18 months), Queensland Rail could financially benefit from any unspent capital sitting in its bank balance over the life of the construction period.

(b) The inclusion of a financial capacity test satisfactory to Queensland Rail creates uncertainty on what financial tests might be applied to access seekers and how those financial tests might be applied to different access seekers.

A financial capacity test must exist to protect Queensland Rail from the default risk in an extension. Where an investor in an extension suffers financial difficulty and is unable to fully meet funding obligations, then it is not in Queensland Rail's legitimate business interests to be left with a half-finished extension, unpaid construction and commissioning costs and/or a need to incur substantial costs removing a partly constructed extension from the network.

At the same time, a financial capacity test must be reasonable, objective and efficient. Examples of objective financial tests include:

(a) the application of a 100% Bank Guarantee to cover the construction costs of the extension. This financial test is waived where investing companies have an investment grade credit rating. This approach is proposed by Aurizon Network in its SUFA DAAU with additional safeguards around the provision of a defined level of project funding upfront and rolling three-month cash calls

(b) the application of a 100% Bank Guarantee to cover the cost of termination and returning the network to its pre-extension standard.

Draft decision 9.3

- **The QCA requires Queensland Rail to amend its proposed extensions provisions so that its proposal (cl. 1.4.1) includes clear, objective and transparent financial tests to be applied to investors in user funded extension projects.**

No cost test

The 2013 DAU removes Queensland Rail's obligation to extend the network in situations where it bears any cost or risk in constructing, owning, operating and managing the Extension (cl. 1.4.1(a)(iv). This limitation is not consistent with the requirements of the QCA Act.

Sections 118 and 119 of the QCA Act are focused on not incurring the costs of an extension. They make no reference to the ownership costs of an extension, including maintenance, operating and management costs. Section 119 empowers the QCA to make a decision relating to the ownership of an extension asset.

In the 2010 Aurizon Network Access undertaking, the QCA took the position that the contiguous and interrelated nature of any extension to the existing rail network meant that any user funded expansion must be owned, maintained, operated and managed by Aurizon Network. The QCA has not received any information that would lead it to change this position.

Accordingly, the QCA considers that whilst an access seeker or access seeker's customer or nominee may fund the extension, ownership of that extension asset (and its attendant responsibilities) will reside with Queensland Rail. This means the funding agreement in the 2013 DAU is the funding mechanism for developing and constructing a network extension and the access agreement is the funding mechanism for maintaining, operating and managing of the network, inclusive of the extension. In a situation where approved reference tariffs exist, Queensland Rail can seek a tariff adjustment to reflect the incremental increase in costs associated with owning the extension asset. This should address Queensland Rail's concerns regarding the costs of an expansion that it owns.

The 2013 DAU provides an additional discretion in favour of Queensland Rail with respect to executed access agreements. The 2013 DAU stipulates that Access Agreements for capacity inclusive of the extension must be on terms and conditions satisfactory to Queensland Rail (cl. 1.4.1(a)(viii)). This caveat undermines the validity of an executed Access Agreement negotiated consistent with Part 2 of the 2013 DAU. It also means that if an access seeker for capacity created by an extension wants to trigger an access dispute, the QCA would not be able to arbitrate where Queensland Rail has applied its discretion on whether an Access Agreement is satisfactory or not.

The QCA is of the view that if Queensland Rail is not willing to execute an Access Agreement for the capacity created from the extension, the access seeker should maintain the right to trigger the dispute resolution provisions in the 2013 DAU and have it arbitrated by the QCA according to Part 2 of the 2013 DAU.

The 2013 DAU also includes reference to Access Agreements, funding, operation and other agreements relating to the extension (cl. 1.4.1(a)(ix) and (x)). The clause unnecessarily gives Queensland Rail absolute discretion to agree to an Access Seeker's request to proceed without those agreements becoming unconditional. This is an unnecessary qualification. To the extent both parties are willing to vary any of the terms agreed in the Access Agreement or Funding Agreement, it is a commercial decision for both parties.

Draft decision 9.4

- **The QCA requires Queensland Rail to amend the extensions provisions in its proposal (cl. 1.4.1) to:**
  - **(a) remove Queensland Rail's discretion to decide if an Access Agreement's terms and conditions are satisfactory to Queensland Rail where an extension is being funded by an access seeker or access seeker's customer or nominee;**
  - **(b) acknowledge that an access seeker or an access seeker's customer or nominee can fund the design, development and construction of an extension with the execution of a funding agreement;**
  - **(c) acknowledge that an access seeker or an access seeker's customer will fund the management, maintenance and operation of the network (inclusive of the extension) with the execution of an access agreement; and**
  - **(d) oblige Queensland Rail to extend the network if funding and access agreements have been executed.**

Technical, safety, environment and land responsibilities

The 2013 DAU provides for an access seeker to:

(a) obtain all necessary authorisations and consents identified by Queensland Rail (cl. 1.4.1(a)(v))

(b) obtain all the necessary rights and interests in land identified by Queensland Rail (cl. 1.4.1(a)(vi))

(c) design an extension project which meets all Queensland Rail's technical and safety requirements (cl. 1.4.1(a)(vi).

The inclusion of discretionary language in the development of the preconditions impinges on the QCA's ability to undertake a balanced review of Queensland Rail's decisions with respect to the extension project. The QCA considers that all preconditions to an extension and any

decisions made with respect to the preconditions should be subject to the dispute resolution process in the 2013 DAU including review by the QCA. This means discretions, such as 'on terms satisfactory to Queensland Rail', must be deleted from these clauses.

The QCA acknowledges the technical, safety, environment and land obligations are necessary preconditions to constructing an extension. Importantly though, is what party to the extension should hold responsibility for ensuring an extension complies with project preconditions. The 2013 DAU implicitly recognises that when Queensland Rail funds an extension, Queensland Rail will accept responsibility for complying with these preconditions. However, responsibility for such preconditions is not easily transferred to the access seeker or an access seeker's customer when a third party funds the extension.

Information and structural asymmetries exist when developing of an extension project for Queensland Rail's network. Queensland Rail owns the existing network, owns or has rights and interests in land underneath the infrastructure, is responsible for complying with authorisations and consents for the new extension, sets the engineering, operational and safety requirements for the network. Queensland Rail will own, operate and maintain the extension asset being funded by an access seeker.

In many circumstances Queensland Rail is the entity required to initiate and obtain the necessary authorisations and rights/interests in land. Queensland Rail is also the entity that must provide all technical and service standards to underpin the design, study and construction stages of an extension project.

In this regard, the QCA has previously noted that:

> *... [a]n expansion of the network will often involve expanding part of the multi-user mainline infrastructure (e.g. passing loops and duplications or other modifications to existing assets) [Therefore] significant operating difficulties would be created if user-funded infrastructure were owned by the funding users. (QCA, September 2010: 32)*
>
> *... feasibility studies and detailed design work should take place irrespective of which party or parties ultimately fund an expansion. (QCA, September 2010:32)*
>
> *... the Authority sees merit in an arrangement where QR Network can request funding for a feasibility study from access seekers. Any such funding should be subject to a user-funding agreement. Thus users who have funded a feasibility study should be repaid through the same arrangements as applies to user funding for the entirety of the expansion project. (QCA, September 2010: 34)*

The QCA believes the access seeker's obligation to comply with these preconditions must be jointly shared by Queensland Rail. Specifically, Queensland Rail must use reasonable endeavours to assist an access seeker to develop an extension project and comply with all necessary project preconditions.

At the same time, the QCA acknowledge that Queensland Rail should not internalise the costs incurred in providing this assistance. Where Queensland Rail's assistance and involvement is required, it is reasonable that an access seeker must reimburse all Queensland Rail's reasonable costs incurred, including funding any land purchases which may be required. Reasonable costs incurred by the access seeker will be treated as a cost of the project and included in the RAB if the extension is commissioned or expensed if the project is shelved.

Draft decision 9.5

- **The QCA requires Queensland Rail to amend the extensions provisions in its proposal (cl. 1.4.1) to:**
  - **(a) remove all discretionary language applied in decisions on whether an extension complies with the extension preconditions**
  - **(b) give Queensland Rail and an access seeker joint responsibility for complying with all the preconditions set for an extension**
  - **(c) oblige the access seeker to reimburse all of Queensland Rail's reasonable costs expended in assisting the extension project complies with the extension preconditions.**

Operational integrity of the network

The QCA notes that Queensland Rail's definition of 'extension' is consistent with the definition of extension in the QCA Act. Nevertheless, stakeholders have raised genuine concerns about the uncertainty of Queensland rail's statutory and contractual obligations under the 2013 DAU and executed access agreements. In particular, stakeholders are concerned that Queensland Rail may seek to defer or delay maintenance so users are required to fund replacement works.

The QCA is of the view that the meaning of the words enhancement, expansion, augmentation, duplication and replacement must be interpreted in the context of the stated intention of an extension which is to add to the network to enhance, increase capacity or duplicate part of it. It is not the replacement of existing assets that simply maintain the capability of the existing network. This is expenditure incurred as part of Queensland Rail's normal expenditure to maintain the operational integrity of the network.

The QCA therefore considers it more likely that the use of replacement in the context of the definition of extension is to be interpreted to involve the notion of where an existing part of the facility is being replaced by something equivalent but better in terms of releasing additional capacity in the system or increasing the functionality of the network. The QCA does not consider the meaning of replacement as used in the definition of extension in the 2013 DAU to include any capital expenditure which essentially repairs and renews the existing network.

However, to put this matter beyond doubt, the QCA recommends that the 2013 DAU include a specific obligation on Queensland Rail to maintain the operational integrity of the assets in the RAB and manage the network so rail operators can operate train services consistent with their contracted access rights. This approach is consistent with the maintenance obligation contained in Queensland Rail's existing standard access agreement. Elevating the principle into the access undertaking simply recognises that Queensland Rail's obligation to maintain the network underpins its provision of access services to access holders.

Draft decision 9.6

- **The QCA requires Queensland Rail to amend its proposal so that it inserts a new clause in the access undertaking (potentially in Part 4 of the access undertaking) to oblige Queensland Rail to maintain the operational integrity of its network consistent with the:**
  - **(a) Network Management Principles**
  - **(b) Operating Requirements Manual**
  - **(c) access rights contracted with access holders.**

9.3 Funding agreements

Consistent with the QCA Act, where Queensland Rail is unwilling to fund an extension to the network, Queensland Rail must facilitate an access seeker or an access seeker's customer or nominee to fund an extension in order to obtain access to the network.

In this regard, Queensland Rail said:

> *Section 137(2)(g) of the QCA Act specifically provides for an access undertaking to include terms relating to extending a facility.*
>
> *In the event of an access dispute, section 118(1) of the QCA Act recognises that access determinations may '...require the access provider to extend, or permit the extension of, the facility' or '...require the access provider to permit another facility to be connected to the facility'.*
>
> *Section 119(2) of the QCA Act states that...if the authority makes an access determination that requires or permits the extension of a facility [and] none of the costs of the extension are to be paid for by the access provider.*

In the case of the Aurizon Network and ARTC rail networks, significant work has been done in identifying key SUFA funding principles and establishing regulatory processes to facilitate third party investment in rail networks. These principles and processes are outlined in Aurizon Network's 2010 Access undertaking, Aurizon Network's SUFA DAAU regulatory process and ARTC's 2011 Hunter Valley Access undertaking.

Clauses 1.4.2 and 1.4.3 of the 2013 DAU have been considered in the context of these regulatory precedents. The QCA is firmly of the view that the user-funding principles included in the 2013 DAU must facilitate the development of a credible funding alternative. The intention is to enable third parties to finance the costs of an extension to accommodate an access seeker's capacity requirements and timeframes

Queensland Rail's 2013 DAU

Queensland Rail has proposed limits on its obligation Queensland Rail to enter into negotiations with access seekers on the funding of an extension. In particular, Queensland Rail said:

> *Cl. 1.4.1(b)(2) use reasonable endeavours to negotiate, on a timely basis, and, if terms are agreed, enter into arrangements with that access seeker or that access seeker's Customer (as applicable) (User) in relation to the funding of the Extension.*
>
> *Cl. 6.1.2 identifies that any dispute, complaint or questions...between Queensland Rail and an access seeker in relation to any provision of this undertaking will be resolved in accordance with the dispute and complaint resolution processes (Queensland Rail 2013 DAU)*

Clauses 1.4.2 and 1.4.3 of the 2013 DAU outline key principles for a SUFA to:

(a) be consistent with the 2013 DAU (cl. 1.4.2(a))

(b) provide a return to Queensland Rail no greater than the regulated return (cl. 1.4.2(b))

(c) not use a financing structure which adversely affects Queensland Rail with respect to tax, duty and accounting treatments (cl. 1.4.2(c))

(d) protect Queensland Rail's legitimate business interests (cl. 1.4.2(d))

(e) not result in Queensland Rail bearing any cost or risk in relation to constructing, owning, operating or managing an extension or as a result of the financing structure (cl. 1.4.2(e))

(f) require Queensland Rail to construct an extension efficiently and to operate and manage the extension consistent with Queensland Rail's operation and management of the network (cl. 1.4.2(f))

(g) provide the investor in an extension with the return on and of capital over the economic life of the asset. The return on and of capital invested is equal to the revenue on and of capital which Queensland Rail recovers from access charges which can be directly attributed to the capacity created by the extension. The application of this clause is made subject to, among other things, Queensland Rail not being adversely affected by the payment of the rebate (cl. 1.4.3).

Stakeholders' comments

Regard to Aurizon Network SUFA processes

QRC referenced the Aurizon Network SUFA process being considered by the QCA. QRC recommend including high level SUFA principles in the 2013 DAU, but without locking in a specific financing structure. QRC's preference was to leave further detail on the financing structure and associated standard contracts to be progressed through the Aurizon Network's SUFA DAAU process. However, QRC did recommend the 2013 DAU include a trigger mechanism to enable access seekers and access holders to require Queensland Rail to develop a SUFA for approval by the QCA. QRC said the trigger mechanism should also empower QCA to develop its own SUFA if Queensland Rail's SUFA is not submitted or is rejected by the QCA.

Principles to be balanced

Glencore pointed out that user funding principles need to be balanced to protect access holders and access seekers from Queensland Rail's ability to exercise monopoly power.

> *Cl. 1.4.1(b) 2013 DAU merely provides an obligation to use reasonable endeavours to negotiate a user funding agreement. At a bare minimum cl. 1.4.1(b) should reflect cl. 7.5 of the ARTC's Hunter Valley Access undertaking which provides for good faith negotiations and the express power for the regulator to arbitrate the terms of the user funding arrangements where agreement is not reached. (Glencore, sub. no. 30: 16)*

New Hope said a number of Queensland Rail's SUFA principles require redrafting to ensure user funding represents a credible alternative to Queensland Rail funding. Specifically, New Hope proposed amendments to provide security and certainty in calculating the return on invested capital and the monthly cash flows. New Hope said this certainty is fundamental to potential investors in extension infrastructure (New Hope, sub. no. 33: 1-3).

Obligations to develop master plans

Stakeholders were also concerned with the absence of any detail on how a user will negotiate and execute an Access Agreement which requires an extension that Queensland Rail is unwilling to fund. They argued that the 2013 DAU should include obligations on Queensland Rail to develop system master plans for key rail corridors within its network.

Master planning should map out clear and transparent process whereby rail expansions and related supply-chain investments can be planned in such a way that rail bottlenecks are understood well ahead of customer demand. (QRC, sub. no. 14: 7)

... a transparent master plan would quantify the existing capacity of the West Moreton System and allow capacity expansion options to be developed to facilitate network growth, while maintaining the preservation of the commuter system and ensuring that any capacity analysis undertaken for expansions is not completed in isolation or on an arbitrary basis. (Peabody, sub. no. 45: 2)

QCA analysis and draft decision

The QCA is focused on developing an effective SUFA which provides a competitive alternative for companies seeking to extend the network in order to obtain access. The development of an effective SUFA is relevant for both Aurizon Network and Queensland Rail. Both rail providers have a number of customers who require access to their networks to compete in the marketplace.

In May 2014, the QCA released a position paper on the nature and content of a SUFA. This paper represented the QCA's existing thinking and included a detailed package of measures designed to deliver a workable, bankable and credible SUFA.

The package of measures is based on two overarching financing principles.

(a) Security and certainty over cash flows - including a security agreement to guarantee the methodology of the rental stream from the investment and mandatory distribution of rental returns to investors

(b) Construction, the expansion process and pre-approval - ensuring construction risks and liabilities are appropriately allocated between SUFA parties; there is certainty on capacity being delivered by an expansion; and certainty on the treatment of costs incurred through the expansion study and construction cycle. This second category relies on a number of sub-elements, including:

  (i) establishing an expansion process capable of delivering feasibility studies to a level of accuracy required to provide clarity on the expansion cost to be financed

  (ii) allowing investors in an expansion to trigger a regulatory capital pre-approval process to obtain investment certainty the expansion costs will be included in the RAB for the purposes of calculating rental cash flows

  (iii) ensuring SUFA assets are managed, operated and maintained on a non-discriminatory basis

  (iv) providing third party funders with all necessary information to allow them to undertake a robust financing and risk assessment prior to execution of a SUFA.

Aurizon Network's SUFA DAAU process is not expected to be finalised prior to the release of this draft decision. Nevertheless, the QCA is in a position to provide guidance to Queensland Rail with respect to the funding principles which must be included in the 2013 DAU.

These principles must form the basis for any SUFA negotiation between Queensland Rail and access seekers or an access seeker's customer or nominee. Where funding negotiations are not successful, there must be an option for either party to refer a dispute to the QCA for arbitration. In the event of a dispute, the QCA will consider the dispute with reference to these overarching investment principles.

The QCA has considered the above matters and stakeholder comments by:

(a) providing clarity on the foundation investment principles by requiring provisions similar to those in Schedule J of the 2010 Aurizon Network at Appendix E.

(b) increasing certainty around the financial returns to be earned through third-party investment in the network

(c) providing better clarity on processes to trigger an expansion.

Foundation investment principles

The QCA believes the 2013 DAU should include a schedule of investment principles, not dissimilar to Schedule J of Aurizon Network's 2010 access undertaking. Queensland Rail should be obliged to negotiate a funding agreement underpinning an extension to the network consistent with these principles. If any party to the negotiation triggers an access dispute, then the QCA will arbitrate that dispute consistent with the investment framework principles.

Draft decision 9.7

- **The QCA requires Queensland Rail to amend the extension provisions in its proposal to:**
  - **(a) include a new schedule which is similar to Schedule J of Aurizon Network's 2010 access undertaking**
  - **(b) require any funding agreement negotiated between Queensland Rail and an access seeker or an access seeker's customer or nominee to be consistent with this new schedule.**

Certainty of financial returns from an investment

The QCA accepts that the primary benefit of investing in Queensland Rail's network is the investment security based on obtaining a regulatory return over the life of the asset. To be a workable, fundable and credible investment framework, the QCA's May SUFA position paper highlighted the need for a funding agreement to provide:

(a) security and certainty over cash flows - including a security agreement to guarantee the methodology of the rental stream from the investment, with mandatory distribution of rental returns to investors

(b) an ability for investors to incorporate Access Conditions into an extension project to reflect potential variations in terms and conditions commensurate with the risk profile of a specific extension[48]

(c) an ability for investors to trigger a regulatory capital pre-approval process to obtain certainty that the expansion cost will be included in the RAB for the purposes of calculating investment cash flows.

These regulatory protections are not contained in the 2013 DAU and the funding obligations are imbalanced in favour of Queensland Rail. In fact, the 2013 DAU:

(a) specifically references that Queensland Rail is not obliged to provide returns to an investor if Queensland Rail is adversely affected by the payment stream

[48] An example where Access Conditions have been approved is in respect of the QCA's approval of WIRP Access Conditions.

(b) is ambiguous in the calculation of rental returns because it ring-fences certain traffic types as non-users of any extension asset and so increases the investment risk associated with the extension

(c) references the need for an extension to not impose any cost or risk on Queensland Rail, including as a result of the financing structure, funding terms and tax, duty and accounting treatments

(d) removes the previous cl. 6.5.2 of the undertaking which provided an ability for Queensland Rail to apply to the QCA to obtain Access Conditions to an extension to mitigate the financial risks associated with an extension

(e) does not oblige Queensland Rail, where requested by an investor, to undertake the Schedule AA regulatory pre-approval process for an extension

(f) does not oblige Queensland Rail to maintain the extension infrastructure in the same way it maintains, operates and manages the rest of its rail network (i.e. on a non-discriminatory basis).

Certainty of a revenue cash stream to meet interest and principal repayments from an investment is of paramount importance to access seekers and third party financiers. However, in the 2013 DAU, Queensland Rail has created significant investment uncertainty regarding revenue security and the removal of key investment protections.

The 2013 DAU must therefore be amended to improve certainty around the financial returns to be earned through third party investment in the network.

Draft decision 9.8

- **The QCA requires Queensland Rail to amend its proposal so that the funding agreement provisions in its proposal (cls. 1.4.2and 1.4.3):**
  - **(a) remove all discretionary language**
  - **(b) establish the methodology for the rental stream from an investment, with mandatory distribution of rental returns to investors**
  - **(c) enable an investor to obtain an independent audit of the rental methodology and the returns paid over the economic life of the asset**
  - **(d) includes clauses consistent with cl. 6.5.2 and related clauses of the 2010 Aurizon Network undertaking to enable Queensland Rail and investors acting reasonably to include Access Conditions to an extension to mitigate the financial risks associated with an extension**
  - **(e) enable third-party investors in the rail network to trigger the regulatory pre-approval processes to be included in Schedule AA to gain certainty over their investment returns.**

Clarity on processes to trigger an investment

Under the QCA Act, Queensland Rail is required to outline the terms, conditions and processes which an access seeker must follow to trigger an extension to enable it to access Queensland Rail's network.

Capacity and expansion planning processes are a key component of access undertakings covering coal systems in central Queensland and the Hunter Valley. Aurizon Network and

ARTC's access undertakings contain specific chapters and schedules outlining the processes for industry consultation and development of system master plans.

(a) ARTC's industry consultation process has an ability for access seekers to initiate and fund the development of a capacity project from study phase (concept, pre-feasibility and feasibility) through to the execution of an Access Agreement and Funding Agreement where required.

(b) Aurizon Network's 2010 access undertaking (Part 8 and Schedule A) details the industry consultation, master planning and customer voting process to underpin significant expansions.

(c) Despite this regulatory precedent, Queensland Rail removed from the 2013 DAU any reference to the coal rail master planning provisions contained in Schedule FB of its undertaking. It is unclear why this was done, particularly given Queensland Rail undertook its own master planning process with the Mount Isa Rail Corridor Study in 2012.

Accordingly, the QCA recommends the inclusion of industry consultation, master planning and symmetrical regulatory pre-approval processes for extensions to the network. Such provisions will enable a prospective access seeker to be able to be in a position to commercially negotiate with Queensland Rail to execute the Access and Funding Agreements required in extending and accessing the network.

This approach is consistent with the QCA's approval of Aurizon Network's 2010 Access undertaking and the ACCC's approval of ARTC's 2011 Hunter Valley Access undertaking. It is also consistent with a June 2014 Queensland Parliamentary Committee report on rail freight use by the agriculture and livestock industries. In this report, the Parliamentary Committee recommended rail freight master planning functions covering Queensland Rail's network and credible user funding frameworks to facilitate rail projects to support the agriculture and livestock industries.

Draft decision 9.9

- **The QCA requires Queensland Rail to amend its proposal so that it inserts a new section in the extension provisions (following cl. 1.4.3) which outlines the capacity and investment process Queensland Rail will follow to facilitate extensions to the network. This new section must include the following elements:**
  - **(a) an annual master planning process for each of the major corridors in Queensland Rail's network in consultation with relevant stakeholders;**
  - **(b) a reasonable staged pathway through which an access seeker or an access seeker's customer or nominee can require Queensland Rail to undertake/oversight the concept, prefeasibility and feasibility stages of an extension project;**
  - **(c) study funding principles for access seekers to fund all of Queensland Rail's reasonable costs in managing/conducting each study stage of an extension project leading up to the execution of a SUFA and an access agreement; and**
  - **(d) a regulatory pre-approval process through which Queensland Rail, an access seeker or an access seeker's customer or nominee can obtain QCA pre-approval to an extension to the network.**

QCA review trigger mechanism

The 2013 DAU obliges Queensland Rail to use reasonable endeavours to negotiate a funding agreement on a timely basis. Any disputes which may occur through a negotiation process may be referred to the QCA for arbitration.

It is anticipated that the 2013 DAU will be finalised prior to the conclusion of Aurizon Network's SUFA DAAU process. The specific SUFA issues being considered by the QCA in the Aurizon Network DAAU process are critical to the establishment of a workable, fundable and credible funding agreement. It is important any outcomes with respect to Aurizon Network's SUFA can also be applied within the context of the Queensland Rail access undertaking.

To ensure consistency between the Queensland Rail and Aurizon Network investment frameworks, the QCA recommends the 2013 DAU include a review trigger for the QCA to review capacity and investment principles in the 2013 DAU to address any new issues that may emerge from Aurizon Network's SUFA DAAU. The review trigger must also give the QCA the authority to request Queensland Rail develop a SUFA for submission to the QCA. Should Queensland Rail not submit a SUFA or submit a SUFA which is not approved by the QCA, then the QCA will develop a SUFA to apply to Queensland Rail.

Draft decision 9.10

- **The QCA requires Queensland Rail to amend its proposal so that the funding agreement provisions (cl. 1.4.2) include a review trigger to allow the QCA to:**
  - **(a) reconsider the capacity and investment framework during the term of the undertaking and require Queensland Rail to submit an amended capacity and investment framework**
  - **(b) require Queensland Rail submit a SUFA and Standard Study Funding Agreement to the QCA for approval**
  - **(c) to prepare an amended capacity and investment framework and SUFA (the framework documents) if Queensland Rail fails to submit these framework documents or the framework documents submitted by Queensland Rail are not approved by the QCA.**

GLOSSARY

A	
ACCC	Australian Competition and Consumer Commission
AFD	Access Facilitation Deed
ARTC	Australian Rail Track Corporation
AU1	Queensland Rail's 2013 DAU (2013-14 to 2016-17 period)
B	
B&H	B&H Strategic Services Pty Ltd
C	
CPI	Consumer price index
CQCR	Central Queensland coal region
D	
DAC	Depreciated actual costs
DAAU	Draft Amending Access Undertaking
DAU	Draft Access Undertaking
DBCT	Dalrymple Bay Coal Terminal
DORC	Depreciated optimised replacement cost
DTP	Daily train plan
F	
FCM	Financial Capital Maintenance
G	
gtk	gross tonne kilometre
H	
HVCCC	Hunter Valley Coal Chain Coordinator
I	
IAP	Indicative access proposal
IRMP	Interface risk management plan
J	
JR Act	Judicial Review Act 1991 (Qld)
K	
kg/m	kilogram per metre
M	
MEE	Modern engineering equivalent
MTP	Master train plan
N	
NMPs	Network management principles
NPV	Net present value

O	
ORM	Operating requirements manual
Q	
QRC	Queensland Resources Council
R	
RAB	Regulated asset base
RCG	Rail Capacity Group
S	
SAA	Standard Access Agreement
SUFA	Standard User Funding Agreement
T	
TI Act	Transport Infrastructure Act 1994 (Queensland)
Tkm	Train kilometres
TSC	Transport service contract
TSE	Train service entitlement
W	
WACC	Weighted average cost of capital
WSAR	Western system asset replacement project

APPENDIX A: STAKEHOLDER COMMENTS ON THE OPERATING REQUIREMENTS MANUAL

	Topic	*Description of issue/resolution*	*QCA position*
	Interface Risk Management		
(1)	Interface risk management sets out the process for developing an interface risk management plan (IRMP) and risk management processes. It also deals with risks to the environment such as the management of noise, community liaison and contamination. (cl. 2)	Asciano said residual risks were not explicitly dealt with in the interface risk management clauses, so it was not certain which party was responsible for managing them.#	The QCA recommends re-instating part 8.1 (interface risk management process) of Aurizon Network's 2010 undertaking. It sets out a balanced approach to interface risk management, which has been previously developed by Aurizon Network and the QCA through successive regulatory periods. The approach in part 8. deals with general interface responsibilities, and risk assessments as well as the principles for the interface risk management plan and the interface risk management process. It also sets up technical aspects such as the provision of assistance by the network provider and rolling stock authorisation as well as audit, inspection and review principles. Specific aspects covered in the interface risk management plan are: (a) monitoring, awareness, competence (of the operator) and complaint handling as well as the audit, inspection and review regime (b) sharing of all relevant information, that is reasonably available, between both parties Specific aspects covered in the interface risk management process are: (c) provision of certainty on environmental standards, such as noise levels, while leaving scope for the access provider to change the requirements to ensure consistency with applicable laws (d) provision of clarity to operators to avoid issues such as incorrect or too much information and specific role allocations in emergency responses

	Topic	*Description of issue/resolution*	*QCA position*
			(e) management of residual risks, while they should be dealt with by both parties, according to defined processes that identify residual risks and allocate the most appropriate party to deal with these.
	2. Interface risk management plan		
(2)	The IRMP 'typically' identifies associated risks, control measures to manage risks and responsible parties to implement the control measures. (cl. 2.1)	Aurizon suggested changing the word 'typically' to the word 'include' in this clause. It said this would add clarity.*	QCA agrees with Aurizon's suggested resolution as the term 'typically' is open-ended. Replacing this term with 'include' will provide certainty about the purpose and content of an IRMP.
(3)	The IRMP specifies the control measures agreed between Queensland Rail and the operator to manage interface risks to an acceptable level, including requirements for monitoring, awareness, competence (of the operator) and complaint handling as well as the audit, inspection and review regime. (cl. 2.1(b)(iii), iv))	Asciano said there should be a requirement for both operator and access provider to handle such requirements 'evenly'.#	See row 1.
	3. Interface risk management process		
(4)	The interface risk management process deals with the review or amendment of an interface risk assessment or with the IRMP. Queensland Rail proposed that both parties nominate qualified representatives to ensure that the information provided is accurate. To identify risk, Queensland Rail and the operator are proposed to provide information to each other. (cl. 2.1(b)(iii))	Asciano said that the obligation for the operator to provide information on products transported should be limited to the type of information required on a manifest.#	See row 1.
(5)	As part of the interface risk management process, Queensland Rail proposed that both parties should provide information to each other to assist with the identification of risks, of any applicable noise levels or limits. (cl. 2.2(b)(i)(D))	Aurizon said Queensland Rail should specify the applicable noise levels and limits.*	See row 1.
(6)	As part of the interface risk management process, Queensland Rail proposed that the operator provide Queensland Rail with information on the types of products or commodities to be transported. (cl. 2.2(b)(ii)(B))	Aurizon argued this was too broad and requested flexibility depending on the type of traffic. For example, Aurizon said information for containerised traffic varied and Queensland Rail should focus on particular concerns it might have in the transportation of dangerous goods for	See row 1.

	Topic	*Description of issue/resolution*	*QCA position*
		the purposes of the *Dangerous Goods Act*.*	
(7)	As part of the interface risk management process, Queensland Rail proposed that the operator should provide Queensland Rail with the locations of any waterways. (cl. 2.2(b)(ii)(D))	Asciano and Aurizon argued that Queensland Rail should provide information on waterways as part of their role as the manager of the rail corridor.*#	QCA agrees with stakeholder's suggested resolution, as this information is readily available by Queensland Rail. However, the operator should also inform Queensland Rail of matters that may impede the effective operation of the network.
(8)	As part of the interface risk management process, Queensland Rail proposed that the operator should provide Queensland Rail with the anticipated environmental impact of the operator's activities on the network. (cl. 2.2(b)(ii)(E))	Asciano and Aurizon said that Queensland Rail should clarify how the required information was materially different from the requirement to provide information regarding the details of any additional hazards, risks and non-compliance that was required under cl. 2.2(b)(ii)(A).*#	See row 1.
(9)	As part of the interface risk management process, Queensland Rail proposed that the operator provide Queensland Rail with any information in relation to anything referred to in section 4. (cl. 2.2(b)(ii)(G))	Asciano and Aurizon said that this clause was phrased too broadly. Queensland Rail should clarify information requirements in relation to incident and emergency response in the IRMP.*#	See row 1.
	4. Risk to the environment		
(10)	In relation to risks to the environment, Queensland Rail proposed that the operator specifies measures, to prevent risks to the environment such as exceeding applicable noise levels from the operator's train services. (cl. 2.3 (b))	Aurizon said that there was a lack of acknowledgement of the dual responsibilities between operator and network provider with regard to noise mitigation, the cumulative nature of activities contributing to noise issues and the lack of baseline data by Queensland Rail. Aurizon added that there was also no distinction between areas of high noise concerns such as urban corridors with high track curvature and steep gradients with non built up areas. Also there was no reflection of Queensland Rails' and the rail operator's obligations as accredited rail entities. There was no transparency to the operator regarding their potential exposure to risk relative to the negotiated position between Queensland Rail and the Queensland Government in relation to the transport services contract.*	QCA agrees with Aurizon and recommends adopting an evenly handed approach by re-instating part 8.2 environmental risk management process of Aurizon's 2010 undertaking. Part 8.2 of Aurizon's 2010 undertaking sets out a balanced approach to environmental risks that the operator commissions a suitably qualified person, reasonably acceptable to both parties, to prepare an Environmental Investigation and Risk Management Report (EIRMR), identifying: (a) possible risks of environmental harm arising out of the proposed use of the rail infrastructure (b) the manner in which the operator proposes to address the identified risks, as well as the roles and responsibilities. Queensland Rail should provide all relevant information to the third party for the preparation of an EIRMR. Queensland Rail will determine the adequacy of the EIRMR. Assisting Queensland Rail with this determination,

	Topic	*Description of issue/resolution*	*QCA position*
			the operator should disclose all relevant information to Queensland Rail.
(11)	In relation to risks to the environment, Queensland Rail proposed that prior to commencing train services, the operator should have an environmental management system in place that conduct baseline monitoring to establish benchmarks that allow for a comparison of environmental values before and after the operator accessed the network. (cl. 2.3(g)(iv)(B))	Asciano and Aurizon said that Queensland Rail should be responsible for baseline assessments where required.*#	QCA recommends that Queensland Rail undertakes regular baseline monitoring as part of the EIRMR. Queensland Rail should provide any baseline data such as the level of soil contamination to the operator before the operator enters the network. The operator should have a right to audit Queensland Rail's data at times of the operator's convenience. Both parties should make baseline data available to each other in a timely manner.
	Safeworking Procedures and Safety Standards		
	5. En Route Locomotive Provisioning		
(12)	Queensland Rail proposed that an operator must ensure that no en route locomotive provisioning occurs in respect of the operator's trains except as otherwise agreed by Queensland Rail and the operator. (cl. 3.5)	Aurizon said that provisioning should be negotiable on mainlines with low traffic volumes. Aurizon understood that provisioning on a mainline could cause capacity loss and lower the efficiency of the rail network. However on lines with low traffic volumes, provisioning would not result in capacity loss issues and so should be negotiable.*	QCA recommends that provisioning should be subject to negotiation. Provisioning should occur in a reasonable manner where the operator does not hold-up other train services (e.g. on lines with low traffic volumes).
	6. Competence of Workers		
(13)	Queensland Rail proposed that the operator must provide to Queensland Rail the names and positions titles of all of the operator's associates who, enter any railway corridor managed or controlled by Queensland Rail. (cl. 3.6(b))	Asciano and Aurizon said that there was no transparency of the purpose of providing a list of names and position titles for all of the operator's associates who entered the railway corridor. Asciano and Aurizon added that there was a general obligation to ensure operators' associates had accreditation. Assurance to Queensland Rail was provided via the operator's accreditation and legislative requirements that each of their associates must hold and maintain qualifications, under any law or under an IRMP in relation to any entry on any railway corridor managed or controlled by Queensland Rail.*#	QCA agrees with stakeholder's suggested resolution. It is the operator's obligation to ensure workers have undertaken appropriate training. QCA recommends that assurance to Queensland Rail may be provided via the operator's accreditation requirements and can be demonstrated in the course of an audit if required. Increasing information requirements pose unnecessary compliance costs on the operator.

	Topic	*Description of issue/resolution*	*QCA position*
	Incident and Emergency Response		
(14)	Incident and emergency response refers to incident and emergency management and response and sets out how the operator should provide assistance to Queensland Rail in major investigations. (cl. 4)	Asciano said that there needed to be a requirement on Queensland Rail to have incident and emergency response plans and discuss these plans with operators to ensure that the plans of both parties were aligned.#	QCA recommends re-instating cl. 7 of Aurizon's 2010 SAA. This will provide a balanced risk allocation to the management of emergency response. This clause sets out an emergency response plan, developed through negotiation between the operator and the network provider, providing both parties with clarification about clean-up and reporting responsibilities. It also outlines the responsibilities and obligations for reporting regarding environmental reporting and risk management.
	7. Incident/ Emergency Management		
(15)	As part of the incident/emergency management requirements, Queensland Rail proposed that the operator's emergency management plan must be consistent with emergency management standards and must include requirements for relevant authorities to be informed immediately of any incident. (cl. 4.1(b)(iv))	Asciano and Aurizon said that Queensland Rail should redraft this requirement to clearly define reporting and clean up responsibilities as well as responsibilities to notify the Environment Authority. *#	See row 14.
(16)	As part of the incident/emergency management requirements, Queensland Rail proposed that the operator's emergency management plan must be consistent with emergency management standards and must include the method for the clean-up of any substance caused or contributed to by an incident and may harm any person, property or the environment. (cl. 4.1(b)(v))	Asciano said that Queensland Rail should clarify the method and the party that was responsible for the cleanup after an incident. If no clarification was provided, Queensland Rail should refer to a document where this was outlined in more detail.#	See row 14
(17)	As part of the incident/emergency management requirements, Queensland Rail proposed that the operator's emergency management plan must be consistent with emergency management standards and must include requirements for all incidents and all measures taken in response to incidents. This information is proposed to be recorded on a central register. (cl. 4.1(b)(vi))	Asciano and Aurizon said that Queensland Rail appeared to transfer reporting obligations to operators. Stakeholders considered Queensland Rail to be in the best position to keep a central register for all incidents and all measures taken in response to incidents.*#	See row 14
	8. Incident/Emergency Response		

	Topic	*Description of issue/resolution*	*QCA position*
(18)	As part of the incident/emergency response requirements, Queensland Rail proposed to be responsible for the overall coordination and management of the response to a network incident. (cl. 4.2)	Aurizon said that Queensland Rail's emergency procedures included minimal reference to environmental management associated with emergencies and incidents. It suggested clarifying Queensland Rails obligations for reporting to regulators and management of environmental incidents.*	See row 14
(19)	As part of the incident/emergency management requirements, Queensland Rail proposed that the operator must comply with all directions given by Queensland Rail during the recovery and restoration. (cl. 4.2(a))	Aurizon said that an operator should only be required to comply with 'reasonable' directions given by Queensland Rail, as an operator should be able to question a direction if they consider that there was additional safety or other risk factors that need to be taken into consideration. Aurizon suggested amending the wording such that it read: 'the operator must comply with all reasonable directions given by Queensland Rail during the recovery and restoration'.*	See row 14
	9. Assistance in investigations		
(20)	Queensland Rail proposed that if Queensland Rail undertakes an investigation in respect of an incident, then the relevant operator must provide Queensland Rail with information and assistance as is reasonably required by Queensland Rail. (cl. 4.3)	Asciano and Aurizon said that assistance provided in an investigation should be reciprocal, to the extent that the operator provided information and emergency assistance to Queensland Rail, while Queensland Rail should be required to assist the operator. Additionally stakeholders recommended that copies of draft reports should be provided to all affected parties for comment before the investigation was finalised.*#	See row 14
	Train Control and Network Planning		
	10. Operator requirements		
(21)	Queensland Rail proposed that the operator must provide to Queensland Rail the details for the operator's controller, including name, position and contact details. The operator must be contactable by Queensland Rail Train controllers and comply with section 6 at all times, when any of the operator's trains are on the network and at least 2 hours prior to entering the network. (cl. 6.2.1)	Asciano and Aurizon said they did not agree with the proposed operator requirements, stating that operators had 24-hour control centres and it was not necessary to provide the name and position of the Rail Train controller to Queensland Rail separately.*#	The QCA recommends re-instating Part 3 of Schedule 3 of Aurizon's 2010 SAA, which outlines that the movement of the operator's trains controlled by a 24-hour control centre. Queensland Rail can obtain from the control centres the required information at any suitable time.

	Topic	*Description of issue/resolution*	*QCA position*
(22)	As part of the operator requirements, Queensland Rail proposed consultation between Queensland Rail train controller and the operator's train crew. Prior to a train reaching its destination, the operator's controller must determine whether the train crew requires relief, and consult with Queensland Rail to: (a) determine times/locations for relief (b) arrange relief for the train crew (c) advise of relief arrangements. (cl. 6.2.2)	Asciano and Aurizon said that the information requirement was too extensive. They suggested that operator's reporting obligations should be limited to: (a) compliance with schedule run times (b) scheduled entry and exits to the network (c) managing their train crew in order to achieve these obligations*#	The QCA does not consider Queensland Rail's operator information requirements are too extensive. However, for consistency, the QCA recommends the information requirements be similar to those outlined in Appendix 2 of Schedule 10 in Aurizon Networks's 2010 SAA. This Appendix deals with consultation between the relevant Queensland Rail train controller and the operator's train crew. Re-instating this clause will provide for clarity on Queensland Rail's responsibility regarding communication (for example, relaying messages and document amendments) between the operator and Queensland Rail and details obligations and procedures for shunting/entering and exiting the nominated network and yards.
(23)	As part of the operator requirements, Queensland Rail proposed that in the case that the operator's controller and train crew can't contact each other, a Queensland Rail train controller may relay a message from one to the other. (cl. 6.2.2(e))	Asciano said in the event that the operator's controller and the operator's train crew could not contact each other Queensland Rail should be obliged to relay a message. #	See row 22
(24)	As part of the operator requirements, Queensland Rail proposed that the operator must comply with the procedures for shunting, entering and exiting yards and any other terminating yard procedures provided to the operator by Queensland Rail from time to time. (cl. 6.2.3(d))	Aurizon said that this clause did not provide for the ability to operators to negotiate exit and entry procedures for yards. It suggested to continuing the existing access agreement provisions that, requiring the operator to advise Queensland Rail of the anticipated departure of their trains at least two hours before departure, with permission to negotiate variations.*	See row 22
(25)	As part of the operator requirements, Queensland Rail proposed Radio Procedures, by which Queensland Rail will make the listed train control radio channel coverage maps available to the operator on Queensland Rail's website. To ensure that Queensland Rail can contact the operator's train drivers, Queensland Rail proposed that the operator must ensure that the relevant communications system used by its train drivers complies with the relevant	Asciano said that in the event that any of the documents at the web addresses listed in this section changed, Queensland Rail should be obliged to notify the operator of the change, even if only to inform them that the documents on the website had changed.#	See row 22 and row 27

	Topic	*Description of issue/resolution*	*QCA position*
	requirements set out in the relevant IRMP. (cl. 6.2.4)		
	11. Operator's Notifications to Queensland Rail Train Controller		
(26)	As part of the operator requirements, Queensland Rail proposed that at least 15 min prior to the departure of the operator's train, the operator's controller must enter information about the train service into the nominated information system in accordance with any procedures specified by Queensland Rail from time to time. (cl. 6.3(b)(ii)). Queensland Rail also proposed that if the operator's controller cannot comply with cl. 6.3(b)(ii) because the information system is not accessible, then the Queensland Rail controller is required to provide a range, but not all of the information requested under 6.3(b)(ii). (cl. 6.3(c)(i))	Aurizon said that Queensland Rail had proposed three additional fields for inclusion in the train list to be provided, namely the access agreement, the train route acceptance (TRA) and the accredited operator. Aurizon said that the train ID had traditionally been the information that was provided to Queensland Rail to link to the TRA, access agreement and accredited operator. Requiring the additional fields would require a system change with associated costs. Aurizon suggested that Queensland Rail should be required to justify this new requirement on a cost-benefit analysis.*	See row 22
	12. Train Control Centres		
(27)	Queensland Rail proposed to provide train control for the operator's trains through the network control centres and network control regions, with details provided on an online map. (cl. 6.5)	Asciano said that in the event that the document at the web address listed in this section changed then Queensland Rail should be obliged to notify the operator of the change, even if only to inform them that the documents on the website had changed.#	QCA agrees and recommends including a clause that provides that any amendments to the online documents should be formally communicated with the operator.
	13. Network Interface Points between QR National and Queensland Rail		
(28)	Queensland Rail proposed to provide network interface points between the Aurizon and Queensland Rail networks and proposes to provide details on an online map. (cl. 6.6)	Asciano said that in the event that the document at the web address listed in this section changed then Queensland Rail should be obliged to notify the operator of the change, even if only to inform them that the documents on the website had changed.#	See row 27
	Commercial Consideration		
	14. Safety Notices		
(29)	Queensland Rail proposed to give the relevant operator(s) notice if a safety incident has or may occur. It is also proposed that Queensland Rail will provide details of the	Asciano and Aurizon said that in this provision, Queensland Rail may give only notice of that incident, if Queensland Rail considered that the operator is affected	The QCA recommends re-instating Part 3 of Appendix 2 of Schedule 10 of Aurizon's SAA. This clause outlines a balanced approach to the communication of safety

	Topic	*Description of issue/resolution*	*QCA position*
	incidents through a safety alert to the operator, detailing any requirements that the operator needs to comply with. The operator must ensure that the operator's associates are aware of the contents of the safety alert. (cl. 7.2.1)	by an incident. However, the operator should be able to determine whether or not they were affected by an incident.*#	incidents between Queensland Rail and the operator. It sets out that the network provider uses weekly notices to communicate safety-related information about permanent and temporary changes. It also deals with the timing and the requirement to provide notices in a clear and transparent manner.
(30)	As part of the provision of safety notices Queensland Rail proposed to provide information about permanent or temporary changes to safety requirements, set out in weekly notices, prior to the change taking effect. Queensland Rail also anticipated making changes outside the weekly notice. If so, Queensland Rail also proposed to make available to the operator an abridged weekly notice that extracts information. The operator must ensure that the operator's associate is aware of, and complies with, the information in each abridged weekly notice. (cl. 7.2.2)	Asciano and Aurizon raised concerns regarding the information provision about permanent or temporary changes to safety requirements. Aurizon added that Queensland Rail should only provide weekly notices to operators on a fixed day regarding permanent or temporary changes to safety requirements, in a clear and transparent manner.*#	See row 29
	15. Document Control Procedures		
(31)	As part of the document control procedures, each operator must notify Queensland Rail of the name, position and contact details for the operator's associate who is responsible for document control. The operator must ensure the ongoing distribution of this document to the relevant operator's associates. (cl. 7.3)	Aurizon said that the proposed document control procedure did not address Queensland Rail's obligations with regard to the document controller in relation to all of the access agreement. Names were not relevant but rather positions and contact details. Similar information was required regarding Queensland Rail's document controller. Therefore, remove reference to names.*	The QCA recommends re-instating Part 6 of Appendix 2 of Schedule 10 of Aurizon's SAA. This part sets out an even-handed approach to Queensland Rail's obligations regarding the management of updates and revisions of these documents. However, the QCA disagrees with Aurizon on removing the reference to names and believes this is a reasonable requirement. Indeed Aurizon Network requires it in its own SAAs.
	16. Cooperation between Parties		
(32)	As part of the cooperation between party's provisions, Queensland Rail proposed that each operator must notify Queensland Rail of the name, position and contact details of the operator's associate who will be the operator's representative for operational/contractual meetings. The operator's and Queensland Rail's representative for operational/contractual meetings are required to meet, at	Aurizon said that there was a lack of balance in terms of key performance information requested by Queensland Rail. Queensland Rail provided the position and phone contact details for Queensland Rail's representative but required the operator to provide additionally the name of the operator's representative.*	The QCA recommends re-instating Part 3 of Appendix 2 of Schedule 10 of Aurizon's SAA. It outlines a balanced approach to the information requirements for both parties, whereby no names for either representative is required. If both parties agree, the QCA recommends increasing the requirements for both parties to include the names of each representative.

	Topic	*Description of issue/resolution*	*QCA position*
	a time and place agreed between both parties to discuss operational/contractual matters. When both parties agree, either party may invite a guest to an operational/contractual meeting. (cl. 7.4.1; 7.4.2)		
	Government supported infrastructure		
(33)	Queensland Rail proposed to provide government supported infrastructure on an online map. (cl. 7.5)	Aurizon said that government-supported infrastructure maps were out of date. These maps should be included in the preliminary information provided by Queensland Rail in the undertaking.*	QCA recommends updating the map and including the map as part of preliminary information in undertaking.
	Glossary		
(34)	Glossary (cl. 9)	Aurizon said that the glossary contained references to Queensland Rail documents that had been superseded on the customer portal.*	QCA recommends Queensland Rail ensures that the documents listed in section 9 and 10 of the ORM (relating to the glossary) are current at the time of publication of the ORM (post QCA approval).
(35)	Queensland Rail documents (cl. 10)	Aurizon said that Queensland Rail's document listing included documents that were not included on the customer portal. The list also included superseded documents. Queensland Rail needed to ensure that the documents listed in section 10 of the ORM were up-to-date.*	See row 34

- * Aurizon, sub. no. 33: 57 – 65
- # Asciano, sub. no. 31: 17 -20

APPENDIX B: THEORY AND PRACTICE IN THE APPLICATION OF DORC

Asset valuation is a critical component of the regulatory task. The two principal methods used to value the assets of a regulated firm are historical cost and replacement cost. Australian regulators, including the QCA, typically use a replacement cost methodology to establish the initial RAB. This Appendix reviews the theoretical economic basis for using replacement cost methodology as well as its practical application.

Introduction

An asset value is a price, and it serves a similar function to the price for any other commodity or service. Prices play a significant role in determining the allocation of resources, how much is produced, how much is consumed and in what activities does that consumption occur (whether that be as an intermediate input into a further production process or by consumers as part of final demand). That is, prices are central to allocative efficiency.

These results are based on the fundamental economic principle of choices made under conditions of scarcity. This is reflected in the notion of 'opportunity cost'. For example, if I buy an apple I cannot use the same money to buy a pear or an orange. That is, the opportunity cost of buying the apple, is the inability to buy the pear or the orange.

In the theoretical ideal of perfect competition, prices reflect the cost of producing, and the benefit associated with consuming, an extra unit of output. For a product, the price, marginal benefit and marginal cost will tend to be equated across activities. That is, the price for selling a product into one market or another will be the same and will be the same as producing an extra unit of that product. In a perfectly competitive market these prices will be readily observable as these trades occur frequently, there is full information (e.g. no transactions costs) and the product in question is fungible, i.e. it can be produced and consumed in reasonable lot sizes.

These efficiency properties of a perfectly competitive market tend to be more difficult to achieve for capital goods where trades occur less frequently or where location specific issues affect asset values. These issues are not insurmountable as, for example, property markets tend to be well functioning albeit not perfectly competitive.

The efficiency properties of competitive markets deteriorate in the presence of market failures such as in the case of a natural monopoly (e.g. a railway or a channel at a port). In these cases, monopoly profits can be earned as prices are no longer set at the value of the marginal cost to the supplier and the marginal benefit to the consumer. The declining cost nature of the activity will also act to exclude new entrants. Regulation can be seen to be the response to this market failure.

However, the regulator must have some sense of an asset value in order to set an efficient price for the efficient use of that asset. From an economic perspective, the value of that asset should reflect its:

(a) opportunity cost – i.e. what is the value of this asset if it was employed in another activity?

(b) efficient replacement cost – what would it cost to reproduce, today, the same service potential of the existing asset?

The answer to those questions would be the same in the limited circumstances of equilibrium in a perfectly competitive market.

But in the case of infrastructure that has large and lumpy fixed costs and is location specific opportunity cost and replacement cost will diverge. Accordingly, there are alternative views on how an infrastructure asset should be valued.

First, an existing piece of infrastructure that has limited alternative uses should be viewed as a 'sunk asset' and should have a scrap value attached to it. This scrap value could well be close to zero given the likely dismantling and environmental reparation costs.

The second alternative is to value the asset at the cost that a new market entrant would bear to provide the same service potential as the existing asset. The DORC valuation methodology has been developed to provide a view on this new market entrant valuation.[49]

However, DORC is an arms-length or benchmark assessment that can lack the integrity and information of a price, or asset valued, for a good or service that is revealed in the market place through a large number of repeated and transparent transactions - and can lead to problems as discussed below.

A third alternative is to use the historical value of the asset. In the case of the initial valuation, it may be possible to consider what the value would have been had adequate records been maintained.

This appendix considers some of the issues associated with trying to use the alternative valuation methodologies, including DORC, to reveal asset values.

Asset valuation methodologies

From an investor perspective the economic value of a productive asset is the net present value of the future stream of income the assets are expected to produce. This value cannot be used to determine the regulated firm's allowable revenue because the building blocks model used by Australian regulators to set prices produces the stream of income needed to determine the asset value. In other words, the asset value is a function of the allowed revenue and the allowed revenue is a function of the asset value. The solution to this circularity problem is to determine the asset value exogenously (i.e. through a cost based approach).

Two principal methods are used to determine asset values exogenously – accounting or historical cost methods and replacement cost methods.

Accounting or historical cost methods

Accounting or historical cost methods use the accounting value of an asset rather than the economic value to determine asset values. The accounting value of an asset is the original purchase price less depreciation. In cases where an asset is no longer able to produce value for a company it may be 'written down'. The terms 'historical cost' or depreciated actual cost (DAC) are used to denote the accounting value of an asset, which reflects both depreciation and write-downs.

The advantage of a historical cost approach, such as DAC, is that it avoids double counting of assets by limiting the facility owner to a return on funds actually invested – a notion that is relevant in a regulatory context. It also avoids the expense and subjectivity associated with determining current asset values and is relatively easy to establish, provided data and detailed asset registers are available. A DAC approach can also provide a good correlation to replacement values, in particular in an environment of low inflation and little technological change.

However, a DAC approach requires good accounting records to exist on actual costs. Moreover, it does not address over-engineering or an environment where technological change means that a new entrant can enter the market in a different manner to the incumbent.

[49] The distinctions between a scrap value and new entrant cost arise in the context of sunk assets and non-contestable markets. In the theoretical ideal of a perfectly competitive market, it would be expected that an asset would have the same value (i.e. has the same earning potential) across a range of alternative uses and that value would be equal to the new entrant cost.

Regulators in the USA have placed quite some emphasis on DAC approaches. In those cases, there are good accounting records and a long-standing relationship between the regulator and the facility owner. This ensures that the regulated entity neither over- or under-recovers its incurred costs. These circumstances generally do not exist in Australia where facilities have been created and operated by government agencies where the norms of commercial activities (e.g. long-standing accrual accounts and subjecting investment to prudency tests) have not applied.

Replacement Cost approaches

The second principal asset valuation method is replacement cost. The replacement cost methodology values company assets at the current market (replacement) cost that would be faced by a hypothetical new entrant. For regulatory purposes the replacement cost may be scaled down to reflect the fact that the actual asset on the books of the company is not new and may have an altered remaining life. This can be accomplished by setting the replacement cost equal to what it would be if it had been depreciated to the same extent as the actual asset on the books. In other words, if the asset is 10 years old, the depreciated replacement cost (DRC) would be the current market cost of replacing the asset less 10 years of depreciation.

The hypothetical new entrant test is sometimes justified as providing a result that would be generated in a competitive market. Kahn (1970) submits that:

> *... the single most widely accepted rule for the governance of the regulated industries is regulate them in such a way as to produce the same results that would be produced by effective competition, if it were feasible. (Kahn, 1970: 17)*

This statement may appear to endorse application of the hypothetical new entrant test to asset valuation. But Kahn is not suggesting that a monopoly firm should be allowed to charge higher prices based on the replacement costs of its assets. He is endorsing marginal cost pricing.

Many regulated monopoly investments are sunk. That is, the investment has no (or very little) value except in its current use – the opportunity cost is zero. The cost of such investment does not enter a marginal cost calculation. Therefore, consistent with Kahn's proposition, the proper valuation of these investments is zero (or scrap value) and there is no economic efficiency basis for pricing based on a replacement cost approach.

However, pricing at marginal cost would force an entity to operate at an accounting loss. Thus there would be no incentive for the firm to make the investments. To address this, it has been argued that there is an implicit regulatory contract that allows firms investing in sunk assets to recover the costs from their customers in most circumstances. This contract need only allow recovery of the costs actually incurred by the firm in order to provide the proper investment incentives.

Depreciated optimised replacement cost

The competitive market standard

Unregulated firms in competitive markets faced with rapid declines in the cost of fixed inputs are forced to reduce their prices. Failure to do so would invite expansion by existing competitors or new entry from potential competitors. As a result competitive firms will choose to write-off assets that are no longer productive. On the other hand, a rapid increase in fixed input prices may allow unregulated incumbents to increase prices without fear of attracting new entry. For example, environmental controls on new development may increase the cost of entry for potential competitors and provide the incumbents with an opportunity to charge higher prices. The result is an economic 'rent' – income in excess of that needed to induce the firm to supply output.

There is a widespread belief that prices charged by regulated monopoly firms should be set as if the market is contestable. In a contestable market entry and exit are costless. Any attempt by an incumbent firm to charge prices higher than the competitive level would be immediately thwarted by entry of new firms willing to charge the competitive price (Baumol 1982).

Regulators use the basic building blocks model to deal with the infeasibility of pricing at marginal cost. The building blocks model for economic regulation assumes that 'first best' marginal cost pricing is infeasible and aims for a 'second best' solution where the monopoly firm is able to recover all of its costs, including sunk costs, but no more. The return on and of sunk capital allows for financial capacity maintenance and ensures the revenue adequacy that incentivises monopoly firms to invest in sunk assets. In other words, the building blocks model accepts that the competitive market ideal is unattainable and deals instead with market realities.

As discussed above, a DORC valuation is seen as a means to achieve contestable market pricing for a regulated monopoly by costing inputs at the level a hypothetical new entrant would pay. Pricing according to this 'hypothetical new entrant test' would force price reductions when the cost of entry falls, but allow price increases when the cost of entry rises, even if the result is an economic rent. Optimisation at replacement cost effectively forces the write-offs in the absence of competition.

Application of DORC

An asset on the books would not necessarily be replaced with an exact replica. For example, if technology has improved, assets that originally cost $1,000 might be replaced with equipment that could perform the same tasks but cost only $500. In this case the existing assets can be 'optimised' by valuing the old equipment at the cost of replacing it with the new equipment. The result would be the optimised replacement cost or ORC. If this value is depreciated to reflect the reduced remaining life of the existing asset, the value is the DORC.

Optimisation can be applied more broadly. The optimised value of the totality of the firm's assets would be based on current, state of the art design and technology, with no unwarranted excess capacity. For example, if a piece of equipment in the asset base would not be needed to supply any of the current demand, its value would be optimised to zero.

Discussions of DORC are typically focused on the inputs – pieces of equipment and their configuration. The implicit assumption is that the outputs of the network – the services provided – are unchanged. However, the services provided over a network can change over time. The DORC of a network designed to provide the services for which the network was originally designed may be quite different than the DORC of a hypothetical network built to provide the services that the market currently demands.

The advantage of a replacement cost approach, such as DORC, is that it may better approximate the cost a new entrant into the market might face to provide the same level of service. This is particularly relevant where there has been over-engineering or significant technological change (e.g. telecommunications) as a DORC valuation will be lower than a DAC valuation and will avoid the incentives for inefficient new entry and by-pass.

Implementation costs of DORC

Opponents of DORC point out that the valuations are complex, expensive and subject to a great deal of uncertainty. The principal problem is that 'reproduction cost is an imaginary cost' (Phillips, 1988: 319). Phillips (following Wilcox 1971) lists the following questions that must be answered in order to do a DORC valuation:

> *(1) What is it that is being reproduced: a modern replacement for an old plant, the old plant in its original condition, or the old plant as it stands today ...*

> *(2) Under what conditions is replacement cost to occur: those originally existing or those existing at the present time? ...*
>
> *(3) What methods of reproduction are to be assumed? Simultaneous rebuilding of the whole plant involving large-scale operations and employing modern techniques, or piecemeal reconstruction on a small scale with techniques no longer in use? ...*
>
> *(4) What prices are to be taken as representing reproduction cost: the spot prices of a particular day, the average prices of a recent period, or figures based on forecasts of the future? ...*

The complexities that arise with a changing mix of services can be added to this list.

In actual practice the feasibility of DORC accounting depends on the nature of the assets. Engineers may be able to provide reasonable estimates of replacement costs for equipment (e.g. sleepers, track, ship loaders and conveyor belts). However, the cost of civil works is site specific and depends on unknown contingencies. Therefore, costing civil works can be problematic.

Practical application of DORC

Some of the perceived shortcomings of DORC have been factored into recent regulatory decisions about whether, and if so, how to apply DORC. As a result, DORC as it has been applied in practice does not always adhere to the theoretical basis used to justify the method. Many actual regulatory decisions, including decisions about initial asset values, have deviated from theoretical DORC principles in fundamental ways in order to respond to the conceptual problems discussed above.

Greenfields versus brownfields

DORC valuation comes in many 'flavours'. Optimisation could be undertaken on a 'scorched earth' or 'greenfields' basis. The optimal set of assets need bear no relation to the existing network. The network that the engineers would design and build using current demand and technology could be used as the basis for the asset valuation.

In practice, DORC valuations often take certain existing network parameters as given. The location of links and nodes could be accepted and optimisation would consider the costs of new, state of the art equipment to populate the network. That is, the nodes and links could be 'scorched', but their locations would be fixed. This is often referred to as a 'scorched node' or 'brownfields' approach.

Australian regulators have tended to apply DORC on a brownfields basis. However, a hypothetical efficient new entrant would not care about the specific assets of the incumbent or their configuration. The hypothetical new entrant would consider entry using an optimal configuration of nodes using the most efficient locations.

Specific assets

Even regulators that have implemented DORC concepts for initial asset valuations have determined that some assets should be treated differently. Two examples are land and easements.

In ruling on the appropriate asset valuation method of land acquired by the Sydney Airport Corporation Ltd (SACL), the ACCC determined that:

> *In light of the uncertainty surrounding the estimation of opportunity cost, it is the Commission's view that an indexed historic cost basis provides SACL with a return sufficient to provide them with an incentive to continue operating an airport at the Mascot site. While an historic cost approach does not necessarily send all the appropriate signals regarding the optimal location for an airport, this decision is likely to involve an evaluation of the full costs and benefits of alternative locations, not merely the private costs to SACL. In this regard, an indexed historic cost valuation sends signals at least as good as SACL's proposal. Furthermore, an historic cost approach obviates the need for the regulator to attempt such an exercise. (ACCC 2001: 150-151)*

A particular issue with airport land is that valuing the land at its opportunity cost using the value of adjacent land obviously would produce a distorted result. The surrounding land is presumably much more valuable simply because the airport has been built adjacent to it.

Similarly, regulators have consistently refused to place a hypothetical replacement value on easements despite the fact that they obviously have value for the firm, and a hypothetical new entrant would typically have to acquire easements in order to build a network. As Yarrow et al (2010) point out:

> *... an incumbent might have been granted easements in the past in order to facilitate and promote the development of a utility system. A [hypothetical new entrant] test may ask how much it would cost to obtain such easements today, which could be a much higher number. However, to incorporate such value into the asset base and, as a result, to raise prices could be considered perverse in circumstances in which the relevant concessions were granted for the ultimate benefit of the community as whole, as consumers, not for the ultimate benefit of shareholders. By incorporating the value of past concessions into the asset base, and hence allowing that value to be 'remunerated' by higher cash flows consequent on higher allowable prices, a [hypothetical new entrant] approach could lead to an unintended re-distribution of income from consumers to shareholders. (Yarrow et al, 2010: 30)*

What is being optimised?

Changes in the nature or mix of services provided will impact the optimisation choices. To anticipate some of the issues involved in estimating the DORC of rail assets, an optimised passenger and commodity network may not look like an optimised network for carrying high frequency coal trains from large scale mining operations. The replacement cost of assets installed for the former would have no relevance to a network optimised for carrying coal. Moreover, using the hypothetical cost of replacing assets originally built for one standard of service with assets suited for the new optimal standard of service would produce a result that bears little relationship to the service that is actually being provided to customers.

One implication of calculating replacement costs for a network not suited for purpose for the existing customer base is that there will also be implications for other cost elements. A truly optimised network design will minimise total – both operating expenditure and capital expenditure – costs. But in evaluating a study that calculates replacement costs for a network that is by definition actually not optimised needs to recognise the implications for operating expenses. If the network has not been maintained to adequate standards for the original purpose, the problems will be exacerbated.

Avoiding double counting of returns

Under a cost-based methodology (including a DORC or DAC methodology), investors receive a return on their investment through a return on capital (i.e. the weighted average cost of capital) and through a return of capital (i.e. depreciation).

The core objective of economic regulation is to protect customers of monopoly suppliers from inefficiently high prices while at the same time ensuring that monopoly firms have proper incentives to invest in necessary infrastructure. The building blocks model has evolved to ensure that these twin goals are met. A key feature of the building blocks model is to provide investors with a return of, and on, capital sufficient to incentivise investment but not so high as to result in prices in excess of economic cost.

As a consequence, investors need only receive a return on and of their investments once.

So, for example, if an asset has already been fully depreciated – i.e., whose actual life exceeds the expected useful life, it should not be re-valued and included in the RAB again for the investment to be recovered a second time, as this would also be double recovery of the investment.

For some asset classes this could be due to maintenance work. For other asset classes, the actual life could simply be beyond the period that a regulated entity could have reasonably envisaged they would last at the time of construction.

Allowing a return on assets whose cost has already been recovered means that the regulated firm's customers would pay excessive prices. Value should therefore not be attributed for rate setting purposes for assets that have been paid for once.

This avoidance of double counting (including by placing a zero value on assets whose original expected useful life has expired) is consistent with a DORC valuation methodology that seeks to estimate a reasonable regulatory asset base by applying an appropriate amount of depreciation. Moreover, this approach is also consistent with the principle of financial capital maintenance that underlies the building blocks approach (see Section 8.3.2 of this draft decision).

Preventing double counting by valuing the fully depreciated assets at zero would not reduce incentives for investment in new infrastructure. Future investment will be made by the regulated firm as long as its investors can reasonably anticipate that future cash flows allowed by the regulator will return the initial investment plus the opportunity cost of their capital.

APPENDIX C: WESTERN SYSTEM BACKGROUND

Queensland Rail's intra-state below rail network is declared for access under Part 5 of the *Queensland Competition Authority (QCA) Act 1997* (the QCA Act). It is also subject to the terms of the access undertaking the QCA approved in 2008, as amended by a Transfer Notice at the time of the separation of the former QR Ltd.

While the entirety of Queensland Rail's intra-state network is subject to the declaration and the 2008 undertaking, a reference tariff only exists for coal train services on the western system. Pricing for other train services and the remainder of Queensland Rail's intra-state network is subject to the negotiation-arbitration framework and the pricing principles contained in Part 5 of the QCA Act and in the 2008 undertaking.

History of western system tariff

The western system is an ageing line that has not had sufficient volumes to justify upgrading it to a heavy-haul railway standard as has been the case, say, on the Blackwater system in central Queensland. However, Queensland Rail has been able to operate and maintain that line in a way that has allowed it to use the network to transport coal and, in turn, to facilitate the development of coal mines in the Surat Basin.

The exact condition of that line has not been readily apparent. The QCA and others have had to rely on information supplied by Queensland Rail to form a view on the condition of the asset and in turn the value of that asset.

It has become increasingly apparent that the western system is not a heavy-haul railway in the sort of terms that would be commonly associated with the transport of bulk commodities (e.g. coal and iron ore) elsewhere in Australia. For example, it does not have the volumes to take advantage of economies of scale and the coal trains on the western system are relatively short, have low axle loads and have to deal with the scheduling constraints of crossing the Brisbane metropolitan network.

2005/2006 DAUs

A reference tariff for coal services on the western system was first introduced into the 2006 undertaking.

QR's 2005 DAU proposed a two-part tariff, with part of the price paid per train path, and the remainder based on weight and distance – i.e. as a charge per gtk.

The proposed tariff was split into three clusters, with the average tariff being around $12.50/'000gtk – up to 270% higher than tariffs for other western system traffics and more than any tariffs QR charged coal services in central Queensland.

QR did not initially provide a methodology to support its 2005 DAU western system tariff proposal. It subsequently proposed an asset valuation of $800,000/km for the 213 km from Rosewood to Macalister (a total of $170 million), then raised that estimate to $1.5 million/km ($320 million) and later proposed a replacement cost of $3.6 million/km ($767 million) (QCA, December 2005: 74-76).

The QCA rejected QR's proposed replacement cost approach and indicated that:

(a) QR had 'not proposed a clear or consistent methodology for determining western system coal tariffs'.

(b) An assessment of future western system 'reference tariffs based on replacement costs rather than, for example, actual book value, should be conducted within a well-accepted framework such as the DORC methodology'

(c) The actual age of the system assets needed to be considered, as 'many of the assets included in the valuation either have reached, or are approaching, the end of their economic lives' (QCA, July 2005: 74; QCA, December 2005: 77).

The QCA proposed a tariff of $8.50/'000 gtk, based on the $1.5 million/km asset value estimated by QR and benchmarked against QR's Moura tariff in central Queensland. The 2006 undertaking ultimately included a tariff of $10.50/'000 gtk. This was 20% lower than the access charges that QR had previously applied for the western system (QCA, June 2006: 8).

By the June quarter of 2009, the original western system tariff of $10.50/'000 gtk had been indexed to $11.99/'000 gtk, which equated to an average haulage cost of around $5.36/net tonne.

2009 DAU

In the 2009 DAU, QR Network calculated a ceiling price for its western system tariffs reflecting, among other things:

(a) a DORC asset value for the non-metropolitan part of the western system prepared by Connell Hatch, based on an asset register verified through an August 2007 survey of the rail infrastructure. Connell Hatch, at QR Network's direction, optimised out a number of sidings, maintenance areas and sections of dual track that were assumed not to be required for a standalone coal network (Connell Hatch, August 2008: 8).

(b) an allocation of pre-1995 assets across all (coal and non-coal) train paths and post-1995 capital expenditure only to coal

(c) no adjustment for restrictions on coal trains operating in the metropolitan network

(d) an extension of tariff west of Rosewood across the metropolitan system

(e) an estimate of coal-related maintenance costs

(f) an estimate of operating costs – based on the average of the standard allocators assigned to Moura and Newlands for group-wide costs

(g) the same weighted average cost of capital as for central Queensland

(h) contracted volumes from Macalister to Rosewood

QR Network indicated that this methodology could justify a ceiling price of around $34.00/'000gtk for coal traffics on the network west of Rosewood.

Ultimately, QR Network proposed a tariff of $22.07/'000 gtk (QR Network, September 2008).

2009 draft decision

The QCA's December 2009 draft decision on the western system tariff had regard for a number of characteristics that made the western system unlike the central Queensland network, including that

(a) the rail infrastructure was old and not built to modern standards

(b) the network carried a range of traffics other than coal

(c) the service to access holders was subject to constraints including the small size of the trains and the interaction with the metropolitan system

(d) Queensland Rail was charging tariffs two or three times those in central Queensland and other competing coal supply chains.

The QCA sought to assess the western system tariff based on the building block approach that had been established for setting coal tariffs in central Queensland. It also had regard for precedents set in assessing the West Blackwater (Minerva) tariff that the QCA had approved in August 2009. The West Blackwater line had some similarities to the western system in that it was built in the late 19th century for mixed freight and passenger services and upgraded in 2005 to allow for heavy-haul coal services. For West Blackwater, the tariff was assessed by:

(a) applying a DORC methodology that optimised out assets (e.g. passing loops and signalling) that were not needed for the coal service

(b) allocating the asset value between coal and non-coal services based on the proportion of train paths they used (QCA, March 2009: 6).

The QCA's approach to the western system tariff had a particular focus on allocating the costs of the shared parts of the network between coal and non-coal traffics because the western system (unlike the central Queensland network) has a substantial proportion of non-coal services.

To this end the QCA's consultant, EI, reviewed a DORC-based asset value for the non-metropolitan section of the western system – this was derived by

(a) re-optimising the track to create a common network, including reinstating some duplicated track and optimising out coal-only sidings (that the QCA added in to the asset base after the common network was allocated between coal and non-coal services)

(b) checking the asset register and correcting errors, including adding in turnouts that had been omitted from the Connell Hatch valuation

(c) adjusting unit rates, including changes to reflect average rather than peak prices.

Nevertheless, the EI assessment generally accepted the assumption in the Connell Hatch report that the assets were half life expired. EI did not focus on the state of 'invisible' assets, such as formation, where the condition was not readily apparent.

Ultimately, EI proposed to reduce the Connell Hatch DORC valuation of $351.6 million (at August 2007) for the network from Rosewood to Macalister by 18.6% to $286.3 million.[50]

In its December 2009 draft decision, the QCA found that QR Network's proposed tariff of $22.07/'000 gtk was excessive. The QCA proposed a tariff of $16.81/'000 gtk that reflected the EI DORC assessment and was based on, among other things

(a) allocating assets on the common network between coal and non-coal traffics based on the proportion of train paths they used

(b) allocating coal-only assets (e.g. sidings for loading trains) 100% to coal services

(c) removing $22.4 million from the initial asset value to avoid double counting of forecast capital expenditure that EI said was required to bring the infrastructure up to the standard assumed in the DORC valuation

[50] The $286.3 million valuation by EI was based on an allocation of assets east and west of Macalister based on track kilometres (the same methodology applied by Connell Hatch, which had valued the network from Rosewood to Columboola). However the EI allocation incorrectly attributed some of the tunnel valuation to the network west of Macalister that has no tunnels. After this was corrected, the EI valuation for Rosewood to Macalister was $312.3 million, or 11.2% less than the Connell Hatch estimate.

(d) reducing the allocation of pre-1995 assets to coal to reflect that 20% of potential western system paths were unavailable because of the peak-hour metropolitan blackout

(e) extending the tariff west of Rosewood across the metropolitan system

(f) reducing the maintenance cost allowance to reflect EI's lower estimates of the efficient maintenance costs and a lower margin

(g) reducing operating costs to reflect half of the average of the standard allocators assigned to Moura and Newlands for group-wide costs

(h) accepting the same weighted average cost of capital as for central Queensland

(i) using contracted volumes updated by QR Network.

In response to the December 2009 draft decision, QR Network submitted a tariff of $16.81/'000 gtk, that was approved by the QCA.[51] However, in making that proposal QR Network indicated it did not accept the rationale that sat behind the QCA's earlier draft decision. This meant that, while a reasonable tariff had been approved, the QCA's desire from 2006 that a western system tariff be derived within a well accepted framework had not been met.

2013 DAU

The state government split Queensland Rail and QR National (now Aurizon) at the end of June 2010, in preparation for privatising QR National later that year. Queensland Rail retained the 2008 undertaking approved for QR Network, as amended in June 2010 to include tariffs for 2009–10 to 2012–13, including for the western system. Since then, Queensland Rail has made a number of submissions of a replacement undertaking, namely the March 2012, February 2013 and June 2013 DAUs. The June 2013 DAU was the first one to include a proposed tariff for western system coal traffics for 2013–14 to 2016–17.

Queensland Rail's June 2013 tariff reset submission proposed a reference tariff of $22.22 per '000 gtk to be applicable from 1 July 2013. This proposal was based on key aspects of the QCA's December 2009 draft decision, including:

(a) a DORC-based asset value for the non-metropolitan part of the western system

(b) a similar approach to estimating operating costs, although revised to reflect Queensland Rail's separation from Aurizon Network in 2010.

However, the Queensland Rail proposal differed from the QCA's December 2009 draft decision in that it proposed:

(a) changes to the asset valuation, including reinstating $18.9 million of the $22.4 million NPV of future capital expenditure that the QCA had proposed in its 2009 draft decision to deduct to avoid double counting

(b) a near-doubling of maintenance costs (an 82% increase for the Rosewood to Macalister section, compared with the maintenance costs proposed by the QCA in the December 2009 draft decision)

(c) most capital expenditure on the common network after 1995 to be allocated 100% to coal services

[51] The QCA proposed a western system tariff in its December 2009 draft decision on QR Network's 2009 DAU (QCA, December 2009: 69-94). QR Network submitted a tariff largely consistent with the December 2009 draft decision in its 2010 DAU, in April 2010. The QCA proposed to approve that tariff in its draft decision on pricing aspects of the 2010 DAU, on 2 June 2010 (QCA, June 2010a: 87-90). The QCA gave final approval to the western system tariffs in its 30 June 2010 final decision to approve an extension of the 2008 undertaking, with new prices for 2009-10 to 2012-13 (QCA, June 2010b).

(d) a 15% (not 20%) blackout period to reflect the capacity lost due to restrictions on crossing the metropolitan system

(e) a Rosewood to Columboola tariff (as opposed to Rosewood to Macalister in the 2009 DAU), reflecting the start of mining at Cameby Downs.

Stakeholders' comments on the DAU focused on the proposed asset value, and its relation to the standard of service on the western system and the proposed increase in maintenance costs.

The step change in maintenance costs and continued high level of capital expenditure[52] served to reinforce the QCA's longstanding concerns about the age, condition, service levels and relative tariff levels on the western system. It therefore called into question the assumptions that supported the asset valuation proposed in the December 2009 draft decision.

The QCA therefore asked B&H, the consultant that had been retained to review the proposed western system maintenance and capital spending in the 2013 DAU, to also review the DORC-based asset valuation proposed by Queensland Rail. B&H's May 2014 review was consistent with the EI/Connell Hatch review that informed the 2009 draft decision as it:

(a) largely accepted the 2009 DAU asset register prepared by Connell Hatch and rolled it forward to 2013 using CPI

(b) accepted EI's unit costs but adjusted some elements, particularly the lower value for steel rail, so it was only applied to the rail itself, and not to the associated installation costs.

However B&H adjusted the 2009 draft decision DORC to address concerns that the approach to remaining asset lives was too simplistic by

(a) reassessing the remaining life of the assets taking into account evidence about their condition from submissions by Queensland Rail, and from the past and forecast maintenance and capital spending

(b) in doing so, extending their asset lives to reflect the low volumes of traffic on the western system.

B&H also recommended approving most of Queensland Rail's proposed maintenance costs and including all of Queensland Rail's proposed spending in the capital indicator. B&H considered this maintenance and capital work was necessary to keep the rail infrastructure fit for purpose.

The QCA's June 2014 consultation paper presented two indicative asset valuation options driven by stakeholders' comments. One used only historical costs since 1995, as that was shortly before coal haulage began on the western system in 1996-97. The QCA also presented a DORC-based tariff option that drew on the asset valuation set out by B&H in its May report and allocated the assets between coal and non-coal services based on the proportion of train paths they used (B&H, May 2014: xi, 56-81; QCA, June 2014: 35).

The tariff options both allowed most of the maintenance costs and all of the capital spending proposed by Queensland Rail. The DORC option also applied a 22% metropolitan blackout adjustment to assets in place before 1995.

Stakeholders' submissions on the consultation paper and the QCA's consideration of a new approach to the western system asset value are discussed in Section 8.3.2 of this draft decision.

[52] Queensland Rail proposed capital expenditure of $78.8 million (in 2013$) during the 2013–14 to 2016–17 undertaking period, compared with $78.6 million (in 2013$) during the 2009–10 to 2012–13 undertaking period.

APPENDIX D: PROPOSED QUEENSLAND RAIL (QR) 2013 ACCESS AGREEMENT PRINCIPLES AND STANDARD ACCESS AGREEMENT

Material differences in risk allocation/material issues

Item No.	Topic (per Schedule C)[53]	Proposed QR 2013 Schedule C (QR Proposed Principles) and QR 2013 SAA[54]	Aurizon Network (AN) AUT 2010 Schedule E ('2010 Principles') and AN 2010 SAA	Material difference(s)	Comments
(1)	Term (cl. 1)	The Access Agreement will apply for a defined period (subject to any earlier termination rights) and not include an option to renew Access Rights.	Access Agreements will be for a specified term and include a good faith negotiation process for renewal (cl. 1.4).	QR Proposed Principles specifically excludes any option or right to renew.	The QR Proposed Principles are less reasonable in excluding any right to renew. This clause should be read with the limited priority contemplated in 2.7.3 of the 2013 DAU which relates to renewals. It is not clear why QR have excluded the right to negotiate in good faith. The change may be material for a train operator as significant

[53] Note that this table uses the clause topics of Schedule C as its base. Comments in relation to the comparison of the access principles are contained in the white boxes. Comments in relation to the comparison of the Proposed QR 2013 SAA and the 2010 SAA (Operator Access Agreement Coal) are contained in the grey-shaded boxes. The Proposed QR 2013 SAA provisions, when directly corresponding to a provision/topic of Schedule C, immediately follow the Schedule C comments. However, where there are provisions within the Proposed QR 2013 SAA which do not have a direct corresponding provision in Schedule C an extra comments row has been added in an appropriate position and the SAA provision noted in the grey shaded box.

[54] Note also that this table does not include a review of the proposed schedules to agreements, relevant undertaking provisions or the technical/operational documents related to either the 2010 SAA/Principles or QR's proposed SAA/Principles.

Item No.	Topic (per Schedule C)[53]	Proposed QR 2013 Schedule C (QR Proposed Principles) and QR 2013 SAA[54]	Aurizon Network (AN) AUT 2010 Schedule E ('2010 Principles') and AN 2010 SAA	Material difference(s)	Comments
					investments in rolling stock may have to be made in anticipation of utilisation over an extended period. Similarly, it will affect customers with investments in existing projects and those considering expansions or new investments. Whilst the 2010 Principles did not guarantee renewal, the commitment to good faith negotiations provides more certainty.
	SAA reference				All comments in relation to the relevant provisions of the Proposed QR 2013 SAA are substantially the same as comments above in relation to the Proposed Principles.
(2)	Grant of Access Rights (cl. 2)	QR will grant a non-exclusive right to operate Train Services. The Train Service must only commence after the relevant provisions of the Access Agreement are completed and complied with.	Access Agreement to provide for non-exclusive Train Service Entitlements for the operation of Train Services in terms of agreed service levels (cl. 1.1). Train Services must only commence after the relevant provisions of the Access Agreement are completed and complied with. QR will use all	QR Proposed Principles place no obligation on QR to use reasonable endeavours to facilitate the process.	It is not clear why QR should not use reasonable endeavours to facilitate the process. Given QR's requirements in respect of access applications and general knowledge of the process, the process should run more efficiently and should be more likely to

Item No.	Topic (per Schedule C)[53]	Proposed QR 2013 Schedule C (QR Proposed Principles) and QR 2013 SAA[54]	Aurizon Network (AN) AUT 2010 Schedule E ('2010 Principles') and AN 2010 SAA	Material difference(s)	Comments
			reasonable endeavours to facilitate the Access Holder's completion or compliance with such requirements (cl. 3.1).		achieve the purposes of the QCA Act and the Undertaking. It is difficult to see any material detriment to QR if QR is obliged to use reasonable endeavours, as required under the 2010 Principles.
	SAA reference				Comments are substantially the same as comments above.
(3)	Accreditation (cl. 3)	An Access Holders' Nominated Railway Operator must be accredited in accordance with Part 5 of the TRSA at all material times.	Operator of Train Services must maintain accreditation as a Railway Operator. QR must also have and maintain accreditation as a Railway Manager (cls. 1.3 and 9).	QR Proposed Principles place no accreditation obligations on QR. The 2010 Principles more accurately reflect the statutory position under the Rail Safety Act (TRSA), Queensland.	It would provide greater certainty for an Access Holder to know that QR has a contractual commitment to have and maintain accreditation. Again, it is difficult to see any material detriment to QR.
	SAA reference				Comments are substantially the same as comments above.
(4)	Access Charges (cl. 4)	Access Agreement must set out the Access Charges and other related provisions agreed between the parties and may provide a mechanism whereby any changes in the Access Charge are backdated.	Access charges are to be agreed between the parties and payable in accordance with reasonable payment terms set out in the Access Agreement (cl. 2).	The 2010 Principles do not specifically allow changes in Access Charges to be backdated. There are no specific protection mechanisms for an access holder including QCA review.	It would be preferable to include protection mechanisms including that any back charges are subject to review by the QCA.
	SAA reference				Comments are substantially the same as comments above.
(5)	Management and control of Network (cl. 5.1)	QR is responsible for the management and control of the Network. QR will maintain	QR is responsible for the management and control of the Network. QR may impose	QR Proposed Principles allow QR a potentially broad power to impose operational	The QR Proposed Principles allow QR greater control whilst increasing uncertainty and risk

Item No.	Topic (per Schedule C)[53]	Proposed QR 2013 Schedule C (QR Proposed Principles) and QR 2013 SAA[54]	Aurizon Network (AN) AUT 2010 Schedule E ('2010 Principles') and AN 2010 SAA	Material difference(s)	Comments
		the Network such that the Access Holder can operate the relevant Train Services in accordance with the terms of the Access Agreement. QR may, at any time (and without the Access Holder's consent) impose operational constraints and perform Rail Infrastructure Operations.	operational constraints for the protection of persons or property or to facilitate maintenance work. In carrying out such work QR will use reasonable endeavours to minimise interruptions (cl. 6). The Access Holder may inspect the rail infrastructure prior to operations to satisfy itself as to risks. QR is not liable for claims in relation to the infrastructure except where QR have failed to maintain the infrastructure subject to agreed criteria (including in the Network management Principles) so rail infrastructure is consistent with the agreed Rolling stock Interface Standards so that the Access Holder may operate the Train Services in accordance with its Train Service Entitlements (cl. 6.6).	constraints. Operational constraints under AN 2010 Principles are limited to safety, and maintenance or enhancement requirements as well as emergency situations. Under QR Proposed Principles there is no obligation on QR to use reasonable endeavours to minimise interruptions. The 2010 Principles contain a specific statement that QR will be liable for failure to maintain the rail infrastructure in certain circumstances. Whilst the QR Proposed Principles state that QR will maintain the Network, there is no specific statement as to QR's liability. The relevant cl. 5.1(b) is to be read in the context that QR gives no indemnities and that QR's liability may be excluded or limited to $1.00 depending on the circumstances (and the interpretation of cl. 11 and 12). See comments in items 18 and 23 below in particular.	for the Access Holder as to when trains may run. This may in turn increase costs for the Access Holder in rescheduling trains and rostering staff. It may also have adverse impacts along the supply chain and result in increased wharfage and shipping costs or potentially mean freight is not delivered to contractual delivery times. The 2010 Principles reflect a more reasonable approach where there is more of a balance of the interests of QR in maintaining the Network and the interests of the Access Holder in relation to certainty of train services. The obligation of QR to maintain rail infrastructure is clearly a central and important issue. Cl. 5.1 of the QR Proposed Principles is to be read with cl. 11 (where no indemnity is provided by QR) and with the limitations on QR's liability (cl. 12). The

Item No.	Topic (per Schedule C)[53]	Proposed QR 2013 Schedule C (QR Proposed Principles) and QR 2013 SAA[54]	Aurizon Network (AN) AUT 2010 Schedule E ('2010 Principles') and AN 2010 SAA	Material difference(s)	Comments
					combined effect is that the Access Holder's risk is materially greater under the QR Proposed Principles. The 2010 Principles reflect a more reasonable approach. Comments below also apply. Please see comments under items 18, 23 and 24 in particular.
	SAA reference	The Proposed QR 2013 SAA also includes a specific provision excluding QR's liability for any 'Third Party Works' on, under or over the land on which the Network is located (cl. 5.1(c)). 'Third Party Works' is very widely defined.			Substantially the same as comments in Item 5above. Note also, cl. 5.1(c) of the QR 2013 SAA contains a wide exclusion of liability for any Third Party Works. There are no provisions limiting the ambit of the clause. There are no protection mechanisms for access holders.
		Claims in respect of non-provision of access The Operator will only have a claim against QR in respect of the non-provision of access if	The AN 2010 SAA provisions are contained in cl. 15.There is no specific percentage for cancelled services but a reference to performance regimes and no wide exclusion	The ability of the Operator to claim against QR for the non-provision of access appears much more limited than under the AN 2010 SAA.	The additional limitation regarding 'Queensland Cause Events' is very broad. This risks access rights despite QR contracting specifically to provide access rights. This is

Item No.	Topic (per Schedule C)[53]	Proposed QR 2013 Schedule C (QR Proposed Principles) and QR 2013 SAA[54]	Aurizon Network (AN) AUT 2010 Schedule E ('2010 Principles') and AN 2010 SAA	Material difference(s)	Comments
		the events in cl. 11.6(a) to (e) are satisfied. cl. 11.6(d) requires cancellation in excess of 10% of total Train Services per month. cl. 11.6(e) requires the Claim not be a Queensland Rail Cause. The definition of 'Queensland Rail Cause' includes a very broad definition in subsection (d) of 'any other action by QR…' and also excludes any event 'in any way' attributable to the Operator.	as in cl. 11.6(e).		particularly so when read with other limitations on liability in the Proposed SAA.
(6)	Train Control (cl. 5.2)	QR will perform scheduling and Train Control in accordance with the Access Agreement. Access Holders must comply with QR's Train Control directions and the Network Management Principles. QR must comply with all relevant train operation requirements and safety standards etc. and is not liable to Access Holder if doing so is otherwise inconsistent with the Access Agreement. QR is entitled to give priority to other Train Services to ensure passenger Train	QR is to have responsibility for Train Control and shall exercise Control having regard to the safe conduct of rail operations (cl. 4.1). The Network Management Principles and the Access Agreement will establish the procedures QR Network must follow in varying the Daily Train Plan. The operation of Train Services can be varied in the situations outlined in the Access Agreement and/or the Network Management Principles (which normally	QR Proposed Principles contain fewer provisions regarding objective scheduling criteria. QR Proposed Principles do not state that the Network Management Principles are relevant to the procedures for varying a Daily Train Plan, nor that Long Term Train Service Entitlements can only be varied in accordance with agreed scheduling procedures.	Generally, the QR Proposed Principles allow QR a greater discretion or ability to affect train services. The 2010 Principles reflect a more reasonable approach.

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		Services are not delayed in certain situations.	include safety considerations, force majeure, incidents or emergencies, track possessions) (cl. 4.2 and 4.3).		
	SAA reference				Comments are substantially the same as comments above.
(7)	Operation of Train Services and Rolling stock (cl. 6.1)	Access Holder must only operate Train Services in accordance with the Access Agreement unless permitted under the Access Agreement to do otherwise (including the Network Management Principles) or has QR's prior written permission. If an Access Holder is not able to operate a Train Service in accordance with its scheduled time it must notify QR (unless permitted to do otherwise under the Access Agreement or the parties otherwise agree) and QR will use reasonable endeavours to provide an alternative schedule (but QR is not obliged to incur additional expense in doing so or to alter another Train Service's scheduling). The Access Holder is	QR and the Access Holder will ensure that the operation of Train Services is in accordance with entry and exit times in the relevant Daily Train Plan. The Daily Train Plan can be varied in accordance with the Network Management Principles or in the circumstances specified in the Access Agreement (cl. 4). Long Term Train Service Entitlements can only be varied in accordance with agreed scheduling procedures specified in the Access Agreement (or as otherwise agreed between the parties). Network Management Principles should guide the performance of the scheduling function by QR and be incorporated by reference in	QR Proposed Principles make no reference to the Daily Train Plan. All scheduling will be performed by QR in accordance with the terms of the Access Agreement and an Access Holder must notify QR of any variation required to its Train Services. QR Proposed Principles do not expressly state that Long Term Train Service Entitlements can only be varied in accordance with agreed scheduling procedures. The AN 2010 principles contain a specific statement that QR will be liable for failure to maintain the rail infrastructure in certain circumstances.	The QR Proposed Principles allow QR a greater discretion or ability to affect train services. See comments under item 6 above also. The 2010 Principles reflect a more reasonable approach.

Item No.	Topic (per Schedule C)[53]	Proposed QR 2013 Schedule C (QR Proposed Principles) and QR 2013 SAA[54]	Aurizon Network (AN) AUT 2010 Schedule E ('2010 Principles') and AN 2010 SAA	Material difference(s)	Comments
		responsible for the operation of the Rolling stock on the Network and must ensure its operation does not affect the safe operation of the Rolling stock or the Network.	the Access Agreement (cl. 1.2).		
	SAA reference	The Proposed QR 2013 Schedule C also includes cl. 6.6(d) which deems any intellectual property in relation to the Operator's business or Train Services in connection with the relevant Data to be the property of QR.			Comments are substantially the same as comments above. The intellectual property clause may be of concern to Access Holders.
(8)	Authorisation of Rolling stock and Train Configurations (cl. 6.2)	Access Holders must obtain certification for Rolling stock from an appropriately qualified person approved by QR. Access Holders must ensure that the Access Holder's Rolling stock and Train Configurations are as agreed between the parties in the relevant Interface Risk Management Plan (IRMP). QR has a right to view the certification and test results to ensure that the configurations are as agreed. If the Access Holder wishes to modify any of the Rolling stock or Train	Access Agreement will specify all reasonable operational, communication and procedural requirements for Train Services (cl. 5.1). The Access Holder is responsible for the safe operation of its Rolling stock. cl. 5. Access Holder must obtain certification for its Rolling stock and Rolling stock Configurations. QR has a right to view the certification to ensure that the configurations	The processes for approval of Rolling stock appear more onerous under the QR Proposed Principles There is no reference in QR Proposed Principles to performance incentives.	The QR Proposed Principles appear to have a broader discretion in approving Rolling stock. This may discourage investment or potentially discourage new entrants. It would be preferable to have some balance by requiring QR to act reasonably. (It is recognised that QR would have legitimate concerns in relation to operational and safety issues). The 2010 Principles contemplate (at least) that the parties will agree incentives

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		Configurations, then the Access Holder must first comply with cl. 6.2(a) (the process outlined generally above) and the parties must agree to amend the Access Agreement as reasonably necessary.	are as agreed. The Access Agreement will specify relevant Rolling stock Interface Standards which may be varied as agreed or for safety reasons. The parties should agree specific performance levels which may be enforced via financial incentives and sanctions (cl. 5.2, 5.3 and 5.5).		for performance. This does not appear contemplated in the QR Proposed Principles. Generally speaking, incentives may lead to more efficient operations. It is difficult to see any detriment to QR in including a general obligation to agree on these matters. The 2010 Principles reflect a more reasonable approach.
	SAA reference				Comments are substantially the same as comments above.
(9)	Entering and exiting the Network (cl. 6.3)	Access Holder is solely responsible for and bears the cost and risks of obtaining any rights to access Private Infrastructure. Access Agreements are not subject to an Access Holder obtaining any rights to Private Infrastructure.	No similar provision.	QR Proposed Principles specifically place the risk on access to Private Infrastructure on the Access Holder.	As a general comment, it is appropriate that the Access Seeker/Access Holder bear the risk of access to Private Infrastructure as this is a matter for the Access Holder and generally outside the control of QR. However, it is appropriate that there is a provision in the Principles or the 2013 DAU which clarifies that QR will allow connection of the Private Infrastructure to the rail infrastructure. These comments to be read with proposed cl. 2.8 of the 2013 DAU.
	SAA reference				Comments substantially the

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					same as comments above.
(10)	Notification of damage or disrepair (cl. 6.4)	Access Holder must notify QR of any damage or disrepair etc. of any part of the Network of which the Access Holder becomes aware.	Access Agreement to contain provisions requiring the parties to provide advice to each other in relation to factors that could affect the operation of the Access Holder's Train Service or the integrity of the nominated network (cl. 6.5).	QR Proposed Principles only place obligations on the Access Holder.	There may well be matters which QR knows of which could impact on train operations and which are not known to the Access Holder. Failure of QR to provide information may have safety implications, may affect efficient running of train services, and may well avoid unnecessary costs due to delays or accidents. The 2010 Principles reflect a more reasonable approach.
	SAA reference				Comments are substantially the same as comments above.
(11)	Interface risk management (cl. 7)	Access Holder must comply with its IRMP and notify QR of any non-compliance. Access Agreement must provide for the regular review of the IRMP by the parties. Any disagreement regarding the IRMP review may be referred to dispute resolution.	Safety and risk management must be addressed by the formulation of an IRMP. The parties to comply with the IRMP (cl. 11).	In the 2010 Principles both parties are required to comply with the IRMP. In the QR Proposed Principles, the obligations lie with the Access Holder to a greater extent.	As a general comment it appears that the QR is seeking to impose a higher level of obligation on the Access Holder than QR is willing to accept itself. The 2010 Principles reflect a more reasonable approach.
	SAA reference	Substantially the same as the QR Proposed Principles provisions except that the obligation to comply with the	The parties must conduct any Interface Risk Assessment jointly with QR prior to commencement and the	No material differences between the Proposed QR 2013 SAA provisions and the 2010 SAA provisions.	Unlike the Proposed Principles the Proposed QR 2013 SAA places mutual obligations on the parties to observe and

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		IRMP rests on both parties. In the QR Proposed Principles, the obligation was only on the Access Holder. There is also a process for annual review; disputes may be referred for dispute resolution under cl. 17.	agreed outcomes must be incorporated into an IRMP (cl. 11).		comply with the IRMP and includes a process for annual review.
(12)	Dangerous Goods (cl. 8.1)	Access Holder must not carry Dangerous Goods except as expressly provided in the Access Agreement or with QR's written permission. Before QR will permit Dangerous Goods the Access Holder must comply with all relevant Laws and Authorisations and give a specific accurate description of the goods as soon as practicable prior to operation of Train Service. (cl. 8).	No specific provision relating to Dangerous Goods. Relevant procedures should be covered under environmental obligations or safety and risk provisions/plans.	The QR Proposed Principles provide QR unfettered discretion to provide consent which applies over all goods falling within the wide definition of Dangerous Goods. The provisions are not limited to 'mixed goods' train services.	The discretion of QR to consent or not may limit the scope of train operators or customers to transport goods. Some consideration could also be given to limiting the proposed clause to particular classifications of dangerous goods by reference to the relevant statute. See also comments in Item 18 relating to the Dangerous Goods indemnity. The 2010 Principles treatment of dangerous goods reflects a more reasonable approach.
	SAA reference	The Operator must not carry Dangerous Goods on any Train Service. The QR 2013 SAA does	If the Operator is to carry Dangerous Goods on a Train Service it must ensure that (a)	The Proposed QR 2013 SAA expressly forbids the carriage of Dangerous Goods. AN 2010	No 'Dangerous Goods' may be carried under the proposed QR 2013 SAA.

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		not include the detailed provisions included in Schedule C Proposed Principles.	all requirements of the Dangerous Goods Code are fully complied with; (b) QR is advised of the details of the Dangerous Goods prior to the operation of the relevant Train; and (c) any authorisation or prior approvals under the Dangerous Goods Code have been obtained (cl. 8.3(a)). The Operator's Emergency Response Plan must also include procedures for responding to an incident involving Dangerous Goods where applicable (cl. 8.3(b)).	SAA contemplates that Dangerous Goods may be carried by an Operator but places obligations in relation to their carriage on the Operator.	See also comments in Item 16 below.
(13)	Environmental damage (cl. 8.2)	Access Agreement must include a process that allows QR to notify the Access Holder of anything that is likely to result in environmental harm; and, any requirement that QR or any relevant Authority considers necessary to prevent or mitigate environmental harm. The Access Holder must comply with those	All Environmental Laws must be complied with, failure to comply with obligations under the EP Act or directions from the EPA may be an event of default. Auditing requirements should be linked to the environmental risks posed by an Access Holder's Train Services and be established in that Access Holder's Environmental Investigation and Risk Management Report	The QR Principles include a requirement for the Access Holder to comply with directions to prevent, mitigate or remedy any environmental harm but is not limited to incidents caused by the Access Holder. There are different approaches with the AN 2010 Principles focusing on the EIRMR process.	When read with the indemnity and liability provisions, liability for environmental harm rests with the Access Holder. The QR Proposed Principles do not clearly accept or exclude responsibility or liability for environmental harm caused or contributed to by QR. Also, drafting is not clear and cl. 8.2 may over ride later clauses. The QR Proposed Principles do not have the balance of the

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		requirements as well as take proactive steps to prevent and mitigate environmental harm.	(EIRMR). An Access Holder must inform QR of any non-compliance and must rectify non-compliance as soon as practicable. QR reserves to the right to suspend the right of an Access Holder to operate on a nominated network if, in QR's reasonable opinion, the Access Holder's Train Services cause or threaten Material or Serious Environmental Harm (cl. 8).		2010 Principles. Also see comments under items 18,19 and 23 below in particular. The 2010 Principles reflect a more reasonable approach.
	SAA reference				Comments are substantially the same as comments above.
(14)	Emergency management plan (cl. 8.3)	Access Holder must develop a suitable emergency management plan that is compatible with QR's emergency management plan including matters outlined in the Operating Requirements Manual. The Access Holder must obtain a notice from QR stating that QR has no objection to the emergency management plan.	See comment in item 13 above. Also, Access Holder must develop an emergency response plan which must be compatible with QR's emergency procedures (cl. 7.1).	QR Proposed Principles require notice from QR that QR has no objection to the emergency management plan. There is no requirement on QR to act promptly or reasonably.	The 'no objection' requirement may be justified from a safety/operational perspective. However, this is an additional requirement which again provides discretion to QR to the potential detriment of an Access Holder. The QR Proposed Principles do not provide 'balancing' mechanisms for access holders (to avoid unnecessary delays, and/or unreasonable exercise of this discretion) There are no obligations on QR to act

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					promptly and reasonably in not objecting to the emergency management plan.
	SAA reference				Comments are substantially the same as comments above.
(15)	Obstructions and notifications (cl. 8.4 and cl. 11(a)(iii))	Access Holder must not cause or permit any obstruction of the Network. The Access Agreement must include notification requirements (to QR's satisfaction) regarding a wide range of matters including obstructions, non-compliance, environmental harm, incidents involving Dangerous Goods and the like. QR may do anything it considers necessary to deal with obstructions. An Access Holder will be reimbursed its reasonable direct costs if given a Train Control Direction to assist with an obstruction by QR (if caused or contributed to by another Rail Transport Operator).	QR is responsible for the management of incident responses and may take any reasonable action to recommence services as soon as possible. Access Holder must assist with the restoration of the network in accordance with directions from Train Controllers. Access Holder should be adequately compensated for doing so. QR has the right to pass through the cost of clearing a blockage to the party that caused the damage. Investigations into incidents must be carried out in accordance with the process specified in the Access agreement (cls. 7.2, 7.3 and 7.4).	QR Proposed Principles include a specific provision for QR to pass through costs if the Access Holder caused the obstruction. Note also under the QR Proposed Principles – the Risk and Indemnity provisions – specifically require that QR be indemnified by the Access Holder, in relation to obstructions, to the extent the loss or damage was caused or contributed to by the Access Holder.	The QR Proposed Principles more clearly set out QR's rights to recovery. Again, when read with the indemnity and liability provisions, it is not clear what responsibility or liability QR accepts for obstructions. See comments under items 18,19 and 23 below in particular. The 2010 Principles reflect a more reasonable approach.
	SAA reference		Under cl. 8.5(c), an Operator has a specific right to refer disputes over costs to an expert.		Substantially the same as comments above in relation to the related Proposed Principles, note also, cl. 8.5 of the Proposed SAA which

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					obliges QR to give notice regarding incidents. This addresses the concerns raised in the Proposed Principles Comments above (which required an Access Holder to give notice but not QR).
(16)	Noise mitigation (cl. 9)	In addition to any requirements under the IRM, the Operator must pay a contribution, as reasonably determined by QR for any measures which QR considers necessary either in accordance with Prudent Practices or to comply with any noise levels or limits applicable. QR will use reasonable endeavours to consult with an Access Holder first and give a notice stating how it will determine costs. There is no specific dispute procedure. It is not clear if disputes fall within those to be determined by QR. 'Prudent Practices' is defined as the exercise of that degree of diligence, care, foresight, prudence and skill that would reasonably be expected from a	No similar specific provision. Covered under environmental provisions and general requirements to apply with applicable laws.	QR Proposed Principles allows QR to recover costs as QR 'reasonably' determines with no objective criteria. Consultation is on a 'reasonable endeavours' basis.	The QR Proposed Principles process favours QR and allows QR a potentially wide discretion in relation to matters which could become an important issue. There is little transparency in terms of QR providing its calculations of costs or allowing a mechanism for reasonable review prior to implementation. It should be clarified that any amount payable should be directly attributed to QR's costs in relation to noise caused or to the extent contributed to by the particular Access Holder. The obligations apply in addition to statutory requirements. There is no specific provision

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		competent, skilled and experienced person in the same type of undertaking in the same or similar circumstances.			allowing an Operator to dispute QR's assessment of the contribution required. Disputes should be resolved under the general provisions of cl. 17 (except if becoming or part of a matter where QR resolves the dispute). The 2010 Principles reflect a more reasonable approach.
	SAA reference	The provisions substantially reflect the provisions in the QR Proposed Principles.	In addition to any noise management measures which may form part of the EIRMP, the Operator shall contribute to, as reasonably determined by QR, the costs incurred by QR in taking reasonably necessary noise abatement measures to reduce noise to within the Noise Planning Levels (cl. 8.4). The Noise Planning Levels means the planning levels for railways referred to in the QR Code of Practice: Railway Noise Management. An Operator may dispute any determination made by QR in relation to Noise	The applicable noise levels under 2010 SAA are determined by reference to an identifiable code whereas the Proposed QR 2013 SAA refers to more discretionary 'Prudent Practices'.	The 2010 SAA refers to a more objective code and is clear as to the dispute process. Other comments are substantially the same as above.

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			Management.		
(17)	Inspection and audit rights (cl. 10)	Access Agreement will specify reasonable terms on which QR can carry out audits of Access Holder's compliance with the Access Agreement. QR may require the Access Holder to divert or delay a Train Service for inspection.	Rights of inspection and audit in relation to each party's compliance with the Access Agreement and inspection of Trains and Rolling stock to be included in the Access Agreement. Each party will give the other reasonable notice and use reasonable endeavours to minimise disruption to the other party's operations. (cl. 12).	QR Proposed Principles are not mutual .There are no obligations on QR to use reasonable endeavours to minimise disruptions to an Access Holder's operations.	QR's Proposed Principles allow greater powers to QR and reduce the protection for the Access Holder. There are no obligations on QR to use reasonable endeavours to minimise impact on an Access Holder's operations nor does an Access Holder have rights of inspection in relation to QR's compliance with the Access Agreement. Again, the QR Proposed Principles lack the balance of the 2010 principles.
	SAA reference	Substantially the same as in the QR Proposed Principles.	Substantially the same as above note also that, the mutual powers of inspection in the QR 2010 SAA are also quite detailed and regulated. Parties will need to comply strictly with cl. 12.	Substantially the same as above.	Comments are substantially the same as comments above. See also, comments on new warranties in Item 35.
(18)	Risk and indemnities (cl. 11)	Access Holder must indemnify QR against all claims which may be brought against QR and, [also] [?] all of the losses listed in sub cl. (a)(i) to (vi) inclusive. (i) caused or contributed to by the Access Holder (and related parties) or Customer's;	Each party indemnifies the other for loss (personal injury, death or property damage) caused by or to the extent contributed by the wilful default or negligence of that party or its staff. However, an Access Holder is	Indemnities are not mutual under the QR Proposed Principles. Only the Access Holder gives Indemnities. Under 2010 Principles, the Access Holder is only liable to the extent it had caused or contributed to the loss and is not liable for loss caused or	The QR Proposed Principles alter the risk position of the parties materially in that only the Access Holder is to provide indemnities. Also the indemnities are no longer generally limited to losses to the extent that the

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		(ii) subject to Dangerous Goods provisions, damage to property or persons except to the extent caused or contributed by QR's negligence; (iii) in connection with obstructions to the extent caused, or contributed to, by Access Holder; (iv) arising/in association with Dangerous Goods (subject to limitations: see separate comments on Dangerous Goods Indemnity); (v) relating to claims by Customers; (vi) relating to data collected. It is not clear if the subparagraphs apply to both claims against QR and losses or only losses. Presumably both: drafting should be clearer. There is potential for overlap between the various sub paragraphs and of different levels of, and exceptions to, liability. Again, the drafting is not clear.	solely liable for and must 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 such harm is contributed to by the wilful default or negligent act or omission of QR or its staff) (cl. 14.2). The Access Holder extends any limits or exclusions under the terms of carriage (with Customers) to QR.	contributed to by third parties except where there is damage to persons or property being transported. Under the QR Proposed Principles; >only items 11(a)(i) and (iii) limit the Access Holder's liability to the loss caused or contributed to by the Access Holder. Accordingly, except for these paragraphs, the Access Holder could be liable for all damages suffered by QR whether or not the Access Holder was in some way responsible. > only item 11(a)(ii) (property/personal loss) specifically excludes Access Holder liability for loss caused or contributed to by QR. (However see specific comments relating to Dangerous Goods below); >paragraphs (a)(v) and (vi) may be interpreted such that the	Access Holder caused or contributed to the loss. That is, loss is not generally limited to matters within the immediate control of the Access Holder. There is also potential for overlap in the application of the sub clauses of clause 11(a) (i) to (vi). This results in uncertainty as to the liability of the Access Holder. Uncertainty may lead to unnecessary disputes and inefficiency in (contractual) outcomes. The effect of the QR Proposed Principles is to move the risk to the Access Holder to the extent possible under statute. Also note that in the circumstances where the liability of the Access Holder excludes loss caused or contributed to by QR, the effect is that the amount payable by the Access Holder to QR is reduced by this amount. This does not mean the QR agrees to be liable to the Access Holder (or any

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				Access Holder could be liable for loss even though contributed to by QR (subject to statutory limitations); >the Access Holder may also be liable for any Consequential Loss suffered by QR where a claim is made by a third party including a Customer (see cl. 12 (c)).	other person) or to indemnify the Access Holder, for this amount. If the intention is that QR is to be liable and is to provide an indemnity, this should be clearly stated. In summary, the 2010 Principles generally reflect a more balanced commercial position and are more certain on the face of the clauses. See comments under item 23.
	SAA reference	Generally reflect the provisions of the Proposed Principles. However, there is no specific indemnity in relation to 'Dangerous Goods' (consistent with this QR 2013 SAA prohibiting the carriage of Dangerous Goods).	Substantially the same as the Proposed Principles. However, the indemnity provided by the Operator in cl. 14.3 is wider than in AN 2010 SAA, as cl. 14.3 relates to 'all claims due to or arising out of this agreement in respect of …' but still excludes damages to the extent caused or contributed to by QR as above. Note also cl. 14.2 and 14.4 in relation to indemnities by QR; and also, cl. 14.7 and 14.8 in relation to apportionment of liability.	The risks and indemnities in the Proposed QR 2013 SAA relate only to the risks borne by the Operator and indemnities given by the Operator to QR. The AN 2010 SAA includes mutual indemnities and apportions risk in a more balanced way.	Comments are substantially the same as comments above in relation to the Proposed Principles. Additionally, cl. 14.3 of the AN 2010 SAA is somewhat wider than the AN 2010 Principles and is relevant to discussions of liability in relation to Dangerous Goods. In the AN 2010 SAA cl. 14.2 and 14.4 specifically include indemnities by QR in the circumstances stated and that cl. 14.7 and 14.8 reflect a more reasonable approach in relation to determining liability

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					as between QR and the Operator. Also see comments under item 23 below.
(19)	Dangerous Goods Indemnity (cl. 11(a)(iv)) – Mixed Goods	Access Holder is to indemnify QR for loss arising from Dangerous Goods in relation to a mixed goods train service whether or not caused or contributed to by QR – but excluding any part of the claim that would have arisen regardless of whether any Dangerous Goods were being carried (cl. 11(a)(iv)). This exclusion is not entirely clear. It appears to be excluding loss that would have occurred if only general goods were carried – so contamination or the like caused by the Dangerous Goods could be recovered by QR from the Access Holder under the indemnity but not what might be described as general damages which would have occurred in any event. The drafting should be clearer. Also the Access Holder would	The specific Access Holder indemnity for property transported in cl. 14.2 would apply to any incidents. The Access Holders liability is limited to exclude any damage caused or contributed to by QR. QR would have the benefit of any limitation liability provisions applying to the terms of carriage as between the train operator and the Customer.	Under both Schedules only the Access Holder provides a specific indemnity in relation to potentially relevant goods or property. In the 2010 Schedule, the Access Holder's indemnity does not include loss caused, or to the extent contributed to by QR. The Access Holder could be liable under other paragraphs. As QR gives no indemnities and has attempted to substantially limit its liability, the Access Holder may have not rights to recover from QR for the Access Holder's damages or damages claimed by third parties	In the QR Proposed Principles it is uncertain if the Access Holder has any rights to recover any damages from QR for the Access Holder's losses or amounts claimed by third parties against the Access Holder for damages caused or contributed to by QR (for example for failure to maintain the Network). QR does not specifically accept liability. There is no indemnity provided by QR. Also cl. 12 of the QR Proposed Principles may well limit any liability of QR under general law in any event. If it is intended that QR accept liability in particular circumstances this should be stated. Again the Proposed QR Principles do not reflect the more symmetrical risk matrix adopted under the 2010 Principles. The 2010 Principles

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		be liable for the damage caused by the Dangerous Goods themselves even if the incident occurred due to QR if whole or in part. The Access Holder could potentially be liable also under other provisions, for example but not limited to cl. 8.2, 8.4, cl. 11(a) (i) or (v), as these are not drafted to be subject to (a)(iv). QR does not provide any indemnity and there is no specific statement that QR would be liable for damage including relating to a 'Unit Train Service'. It is also not clear if cl. 12 (e) would apply to limit any possible liability of QR in any event.			reflect a more reasonable approach.
	SAA reference				The Proposed SAA does not contain any provisions specifically related to a Dangerous Goods indemnity. This is consistent with the blanket prohibition on the carriage of Dangerous Goods under the Proposed SAA.

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(20)	Liability for employees/agents/customers (cl. 11(b))	The Access Holder is specifically 'responsible' for all employees, agents etc. and 'responsible' for the conduct of each passenger (cl. 11(b) and (c). It is not clear if this drafting is intended to extend liability beyond the usual position. Again, the drafting should more clearly reflect the position under the 2010 Principles.	The indemnities contain more traditional references to 'a party and its staff' (cl. 14).	The QR Proposed Principles are more specific in stating that the Access Holder is responsible. It is not clear if the new wording is intended to create some additional responsibility or whether cl. 11(b) and (c) are to be read subject to cl. 11 (a). The provisions are not mutual.	The proposed wording in the QR Proposed Principles may be seeking to impose some greater obligation on the Access Holder. The fact that the provisions are not mutual reflects that QR appears to accept little, if any, liability. Again , the AN 2010 Principles generally reflect a more balanced position and are more certain on the face of the clauses. See comments in Item 23 also.
	SAA reference	Substantially the same as the Proposed Principles but the provisions in cl. 10.3 of the Proposed SAA are more detailed and expansive.	Under cl. 10.1 the Operator is fully responsible and liable for the health and safety of the Operator's Staff. The Operator also indemnifies and releases QR from any liability in relation to the Operator's Staff, except to the extent that such liability is caused by the wilful default or negligence of QR or QR's staff.	The 2010 SAA specifically excludes the Operator from liability in relation to the Operator's staff which is due to the wilful default or negligence of QR.	The relevant clauses are to be read with the general indemnity and limitation of liability provisions in each SAA. Again the 2010 SAA reflects a more reasonable and balanced approach.
(21)	Limitation of Liability –general (cl. 12)(a)	The liabilities of the parties for default will be limited or excluded as agreed in the Access Agreement.	The liabilities of the parties for default will be limited as agreed in the Access Agreement.	No material difference in this general statement, however, the exclusions from liability result in substantial differences.	Please see comments in Items 18, 22 and 23 in particular.

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	SAA reference				Substantially the same as comments in Item 23 of the Principles Schedule.
(22)	Limitation of Liability – Consequential Loss (cl. 12)(b)	Except as provided in the Access Agreement, no party will be liable for Consequential Loss. However, Consequential Loss is excluded from the indemnity given in cl. 11 except where arising out of a claim by a third party including a customer. Accordingly, the Access Holder may be liable for Consequential Loss under cl. 11 where a third party has suffered loss and makes a claim against QR. The indemnity in cl. 11 is only provided by the Access Holder. Consequently only the Access Holder is potentially liable for Consequential Loss. QR is not liable for Consequential Loss.	Except as otherwise provided in the Access Agreement, neither party has any liability for Consequential Loss. However, either party may be liable to the other for any damages (including Consequential Loss) arising from an audit or inspection or suspension of Train Services if no reasonable person could have formed the view that the stated grounds for such an audit or review existed ('Liability Trigger') and the parties are subject to each party being under a specific duty to mitigate loss) (cl. 15). Whilst there is a general duty at common law to mitigate damages, the specific obligation may reduce uncertainty of simply relying on the common law obligations.	Both Access Principles specifically exclude Consequential Loss subject to exceptions noted. However, under the QR Proposed Principles, only the Access Holder may be liable for Consequential Loss (as only the Access Holder gives the indemnity under cl. 11). Additionally, the circumstances in which the Access Holder may be liable for Consequential Loss are wider under the QR Proposed Principles as the circumstances under the AN 2010 Principles are limited to audit and inspection and suspension and to the Liability Trigger. The specific obligation in the AN 2010 Principles to use reasonable endeavours to mitigate loss also potentially reduces uncertainty for the party liable for the loss (that is,	The QR Proposed Principles materially increase the potential liability of an Access Holder by expanding the matters for which the Access Holder must indemnify QR to Consequential Losses where a third party makes a claim. Only the Access Holder is, by operation of cl. 11, liable for Consequential Loss. Again, the 2010 Principles generally reflect a more balanced commercial position. The removal of the specific obligation to mitigate loss also exposes the Access Holder to potentially greater risk.

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				the Access Holder).	
	SAA reference				Comments are substantially the same as comments above.
(23)	Limitation of Liability – specific exemptions (cl. 12)(e)	QR's liability is also excluded in relation to a potentially wide list of matters listed in cl. 12(e)(i) to (v) inclusive and if QR's liability cannot be excluded is limited to $1.00. The extent of liability excluded is difficult to determine as the items listed are not clearly defined. This in itself leads to greater uncertainty as well as greater risk for an Access Holder. In addition to being widely drafted, it is not clear from the drafting if these exclusions apply to override specific provisions relating, for example, to Dangerous Goods or Train Services. For example (but not limited to), exclusions (e)(i) and (ii).	There are no specific exclusions from liability in the AN 2010 principles for either party. Accordingly each party's position is the same.	The parties risk position is different as QR has the benefit of exclusions whilst the Access Holder does not. Additionally the exclusions are potentially very wide and may exclude QR from liability in many cases. The drafting also creates greater uncertainty for an Access Holder.	In cl. 12(e)(i) to (iv) inclusive the QR Proposed Principles, QR is proposing to exclude its liability under general law including for breach of contract or negligence completely in relation to the matters specified. If liability cannot be excluded at law, QR's liability is limited to $1.00. The exclusions are widely drafted. Also, the exclusions may well negate the intention of other specific clauses. The end result may be that QR's risk for not complying with its obligations is excluded or limited to $1.00. Again the balance would move materially in favour of QR. The commercial and contractual risk for the Access Holder changes substantially as QR

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					has potentially wide and unclear rights of exclusion from liability. The QR Proposed Principles are heavily weighted in favour of QR. They represent a very strong starting point for any negotiation and may deter entrants due to their lack of commercial balance and particularly as it is not clear what responsibility QR accepts for fulfilling its obligations (if any). The 2010 Principles reflect a more reasonable approach.
	SAA reference				Comments are substantially the same as comments above.

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(24)	Limitation of Liability – Train Movements/Train Services (cl. 12)(g) and (h)	The Access Agreement will specify the circumstances in which either party has a claim in relation to Train Movements caused by a breach of the agreement or negligence. The Access Agreement will also specify the circumstances in which QR is liable for the non-provision of Access or cancellation of Train Services.	The Access Agreement will specify the circumstances in which an Access Holder has a claim against QR for the non-provision of Access or the cancellation of a Train Service. The Access Agreement will specify the circumstances in which each party has a claim against the other party for delays. QR will not be liable for claims in relation to the standard of the infrastructure except where QR fails to maintain so that the Access Holder cannot operate its relevant Train Services (cl. 6.6).	See comments under Item 5 above.	See comments under Item 5 above.
	SAA reference	A party affected by a delay to Train Movements may have a claim to the extent that the matters in cl. 11.3 (a) and (b) and either (c)(i) or (c)(ii) have occurred.	The provisions contained in cl. 15.4 of the AN 2010 SAA are similar to the Proposed QR 2013 SAA.	No material difference. However, note limitations on liability generally.	The provisions need to be read in the context of the rest of the relevant agreement. The related provisions of the AN 2010 SAA reflect a more reasonable approach.
(25)	Liability – limits amounts and time (cl. 12)(h) and (i)	Claims by either party must be lodged within 2 years and only claims over $500,000 may be lodged. Parties are to use best endeavours to give notice of claims within 12 months.	Claims must be made within 12 months. There is no value limit on claims under 2010 Principles.	The requirement that claims only be made if over $500,000 limits rights to recovery as compared to the 2010 Principles. The requirement to lodge a	Whether the proposed minimum claim amount is reasonable depends upon the extent of the liability accepted by QR.

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				claim within 2 years is slightly more advantageous to an Access Holder, however given the requirement to use best endeavours to lodge within 12 months and the other limitations on liability of QR, this is of minimal, if any, value for an Access Holder. Whilst these clauses are to apply to both parties, under QR Proposed Principles the wide limits on the liability of QR may mean that the clause is most likely to apply to (and limit) claims against the Access Holder. However, in the very limited circumstances in which QR may be liable (if any), the Access Holder may prefer a different amount.	The AN 2010 SAA proposes a $100,000 limit which is below QR's proposed $500,000 limit. The AN 2010 SAA reflects a more reasonable approach to claims management.
	SAA reference	Substantially the same as the QR Proposed Principles.	The time limit on Claims is 12 months and the monetary limit (either for a single event or in aggregate for multiple events) is $100,000.	The limits to a Claim have been increased by 1 year and to $500,000.	Comments are the same as comments above.
(26)	Default, suspension and termination (cl. 13)	Access Agreement will specify events of default and rights of suspension and termination.	Access Agreement will specify 'reasonable' events of default and mutual rights of suspension and termination (cl. 18).	The AN 2010 Principles require reasonable provisions.	Again, the QR Proposed Principles favour QR in that there is no requirement for 'reasonable' provisions.

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			QR reserves the right to suspend an Access Holders right (with notice) to operate on a given network in the event of breach or (acting reasonably) anticipated breach of any laws relating to rail safety, QR Network Train Control Directions, Safeworking Procedures or Safety Standards (cl. 10).		The 2010 Principles generally reflect a more balanced commercial position.
	SAA reference	Suspension – QR may, by notice in writing, immediately suspend the Operator's Train Services in the wide range of circumstances listed in cl. 13.1(a) to (j) of the agreement, or the Operator fails to comply with a notice from QR that the Operator is causing or threatening environmental harm; or, the Operator has failed (in QR's opinion) to comply with a relevant law or the agreement.	The events which may result in suspension are outlined in cl. 19.1 of the AN 2010 SAA. These are similar and of similar effect. However, cl. 19.3(b) specifically provides that QR may be liable to the Operator if no reasonable person would have formed the view that the grounds for suspension exist.	The AN 2010 SAA events resulting in suspension, when of a subjective nature, provide tests of reasonableness or further threshold tests before operations can be suspended. See for example, cl. 19.1(ii)(A) and (B). Suspension under cl. 12.1(a)(iii) of the Proposed QR 2013 SAA on the other hand, is predicated on QR's opinion (which does not have to be reasonable). Also the proposed QR 2010 SAA does not contemplate any liability for QR.	The requirements for a 'reasonable' threshold in the AN 2010 SAA and the prospect of liability under cl. 19.3(b) limit QR's ability to act in a discretionary manner. For example (but not limited to) pursuant to cl. 13.1(h).
		Termination –			

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		The events listed in cl. 13.1(a) to (j) are also events which allow QR to terminate the Access Agreement. These events are generally typical termination events however, 13.1(h) grants QR a right to terminate for even a minor breach of a Train Service Description (subject to the remedy provisions). Termination by the Operator is limited to those events listed in cl. 13.2. Under cl. 13.2(c) an Operator may terminate if QR breaches the Access Agreement except where the agreement excludes QR's liability for that breach or limits that liability to $1.00 or where QR is not otherwise liable under the agreement. QR or the Operator may terminate for a breach of one of the events listed in cl. 13.1 or 13.2 (respectively) subject to first complying with the Notice to Remedy provisions in cl. 13.3. Except for events in cl.	Under AN 2010 SAA QR may terminate immediately (subject to QR first exercising its right of suspension under cl. 19.1) upon the occurrence of the events listed in cl. 20.1. These are, for the most part, typical events of termination. Most of the events of default must continue for a number of days (generally 30 to 60) after QR has given notice of the default. The Operator may terminate for the events listed in cl. 20.2, including cl. 20.2(d) which contains a general right to terminate if QR is in default of the due performance of 'any other obligation' under the agreement and such default continues for 60 days after the Operator gives QR notice of its default. There is a right for the Operator to terminate if QR's Accreditation is cancelled and QR cannot perform its obligations (cl. 20.2(b)).	Under the AN 2010 SAA, the listed events giving rise to termination are more specific (cl. 13.1(a)). The Proposed QR 2013 SAA gives QR a general right to terminate for any 'material' breach of the SAA, this provides QR with more discretion to terminate. Additionally, in relation to certain events of default in the AN 2010 SAA, QR must first exercise its corresponding right of suspension under cl. 19.1 before terminating. The Operator's right to terminate for QR's breaches of the Access Agreement is restricted by reference to cl. 11.2. Under the Proposed QR 2013 SAA, there is an opportunity to remedy a default before terminating. Certain provisions are excluded however, including importantly, the Land Tenure event (cl. 13.1(d)). The AN 2010 SAA does not contain a similar notice to remedy provision	Given the broad limitations on QR's liability under the agreement and specifically under cl. 11.2 (see also Items 18, 22 and 23 of the Principles Schedule), an Operator's right to terminate for QR's breaches is unreasonably restricted. This limit on a right to terminate is compounded by QR's exclusions from liability so that an aggrieved Operator may find itself in a situation where QR has breached its obligations under the agreement but an Operator cannot terminate nor claim compensation. These matters materially increase the risk and uncertainty from an Access Holder's perspective and particularly risk and uncertainty as to QR's commercial commitment to provide the services. The QR 2013 SAA may well deter or inhibit potential Train Operators and ultimately end

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		13.1(c) to (f) where no notice to remedy is required. Under cl. 13.3(ii)(B) to avoid termination for an event which cannot be remedied, the Defaulting Party will be required to take action to ensure such an event does not recur and may be required to pay reasonable compensation to the Terminating Party. Note that QR's compensation under this clause is limited by any other provisions which limit QR's liability (for example those which limit QR's liability to $1.00)		however, most of the termination events must continue for a period of between 30 and 60 days before a party can terminate. This continuing period of default leaves the Access Holder a chance to remedy in any event. There is no specific provision whereby a defaulting party compensates a non-defaulting party in the AN 2010 SAA.	users.
(27)	Insurance (cl. 14)	Access Agreement will provide for appropriate insurances to be effected by the Access Holder.	Access Agreement will provide for appropriate insurances to be effected by the parties. cl. 13.	QR Proposed Principles only places insurance obligations on Access Holders.	The QR Proposed Principles clause is consistent with QR accepting little risk (see comments above). QR should state its obligation in relation to insurance. The Access Holder will not be fully able to assess its risk if QR does not have or does not specify its insurance obligations. This could also impact on the cost of

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					insurance for the Access Holder. The AN 2010 Principles reflect a more balanced and reasonable approach.
	SAA reference	The Operator must effect and maintain insurance in accordance with Prudent Practices (as defined under cl. 26). The insurance must cover the risks associated with the Operator's indemnities of QR and must note the interests of QR. The insurance must also include public liability insurance for an amount not less than $350M which has a maximum deductible of $500,000; a carrier liability insurance policy for an amount not less than $10M. The Public liability insurance must include, cover in respect of, amongst other things, damage arising out of the accidental discharge of smoke, vapours, acids, alkalis, toxic chemicals, liquids or gases, contaminants or pollutants (cl. 14.1 footnote 2).	The Operator must take out and maintain insurance for the risks and on the terms specified in Schedule 7 of the QR 2013 SAA. The terms in Schedule 7 include public liability for an amount not less than $350M (deductible to be inserted). This Public liability insurance must include The Public liability insurance must include, amongst other things, substantially the same dangerous goods as are required under the Propose QR 2013 SAA (see Schedule 7, cl. 13(a)). Only the Operator is obliged to take out insurance (as compared to the AN 2010 Principles which indicate that the obligations to insure should be mutual).	Specific insurance clauses are not materially different. Claims are to be read with the balance of each agreement.	Whilst under the Proposed QR 2013 SAA an Operator is specifically prohibited from carrying Dangerous Goods the Operator is required to insure against damage caused by any accidental release or discharge of dangerous goods. See also separate comments in relation to Dangerous Goods.

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		The Operator must provide evidence or copies of its insurance to QR and to QR's reasonable satisfaction at least 10 business days prior to the Commitment Date. The Operator's compliance with any Insurances does not limit the Operator's liabilities under the Access Agreement (cl. 14.9).			
(28)	Security (cl. 15)	Access Holder must provide a security deposit such as a bank guarantee to QR on terms acceptable to QR. The amount of the security deposit may be increased or decreased by QR in accordance with QR's risk factors.	In appropriate cases QR may require lodgement of a bank guarantee to secure performance by the Access Holder of its obligations and having regard to QR's reasonable assessment of the creditworthiness of the Access Holder (cl. 2).	Under the 2010 Principles the obligation to provide a bank guarantee is not mandatory but rather is only required in 'appropriate cases'.	The QR Proposed Principles mandatory requirement potentially increases the financial burden on an Access Holder. It is more reasonable that an Access Holder give security in 'appropriate cases'. This should also be read with cl. 2.9 of the 2013 DAU whereby an Access Holder is required to demonstrate to QR that it is has the financial capability to perform its obligations under an Access Agreement. The 2010 Principles generally

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					reflect a more balanced commercial position.
	SAA reference	The terms of the Proposed QR SAA generally reflect the terms of the Proposed Principles above. QR can call on the security in a broad range of occurrences. QR is to have uninhibited access to the bank guarantee on demand. QR may call on the bank guarantee if the Operator fails to pay any payable amounts; or, if QR suffers a Loss in respect of which the Operator is required to indemnify QR (cl. 15.2). If an Insolvency Event occurs or QR (acting reasonably) suspects that an Insolvency Event has occurred. QR may review the Security Amount at any time and determine, acting reasonably, that the Security Amount should be increased or decreased. The Operator must amend or replace the bank guarantee in accordance with	Under the AN 2010 SAA (cl. 2.4) the provision of security is mandatory. This may be reviewed under cl. 2.4(g) having regard to the creditworthiness of the Operator and the security may be returned pursuant to cl. 2.4(c). Under the terms of the AN UT 2010 Principles, provision of security is only required in 'appropriate cases'. Under the AN 2010 SAA the security is given for 'performance of the Operator's obligations and QR may only call on the security in circumstances where QR suffers direct loss or damage as a result of default by the Operator under the agreement and is entitled to be compensated for such loss or damage under the agreement.	Although both Standard terms require provision of security, only the AN 2010 SAA anticipates that a creditworthy Operator may apply to have its security reviewed. Also, under the AN 2010 SAA, the purposes for which the security is given and QR's ability to draw on the security are more limited. Under the Proposed QR 2013 SAA QR's recourse to the security is much less restricted and includes, for instance, losses which could be attributable to a third party but for which an Operator has agreed to indemnify QR.	The changes in the Proposed SAA provisions favour QR. The AN 2010 SAA are somewhat more balanced in that they include an opportunity for review.

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		QR's decision within 10 business days (cl. 15.3). QR must only return the security at the termination or expiration of the agreement and, in QR's reasonable opinion, there is no prospect of further money being owed to QR (cl. 15.4).			
(29)	Adjustments (cl. 16)	Access Agreement will provide a mechanism for adjustments where there is a net adverse financial effect on QR. The mechanism will place QR in the position it would have been if the change had not occurred. The change could include taxes, credits, laws and funding. Disputes regarding the adjustment may be referred to dispute resolution. Access Agreement may also include rate review provisions as referred to in cl. 3.5 of the Draft Access Undertaking.	Access Charges will be adjusted to reflect the net impact of any material change where such a change results in a variation to the net cost to QR. The effects of any material change should be assessed in consultation with the Access Holder (cl. 16).	QR Proposed Principles limit the adjustment to an adverse financial effect on QR whereas AN 2010 Principles allow savings as well as costs to be adjusted.	The QR Proposed Principles only contemplate adjustments in favour of QR. The 2010 Principles generally reflect a more balanced commercial position.
	SAA reference				Comments are substantially the same as comments above.
(30)	Disputes (cl. 17)	Access Agreement to provide a dispute resolution escalation process which includes the	Any dispute between the parties must follow the escalation process outlined in	Further, cl. 17(c) in QR Proposed Principles gives QR the ability to determine	The QR Proposed Principles referral to the Safety Regulation is appropriate. It

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		ability of the Rail Safety Regulator under the TRSA to resolve disputes. A referral to the Rail Safety Regulator overrides the dispute resolution provisions of the Access Agreement to the extent of any inconsistency. QR will be able to determine disputes in relation to amendments to an IRMP, safety, environment and land (including the use of the Network), if the dispute is not resolved under the Access Agreement, by agreement, by an expert or by the Rail Safety Regulator.	cl. 17 which results in determination by an expert, an arbitrator or the Courts.	disputes in the specified circumstances; this is not the case under the AN 2010 Principles.	would be preferable that an independent party determine any dispute in which QR is involved as with the 2010 Principles. The 2010 Principles generally reflect a more balanced commercial position.
	SAA reference			Note that cl. 17.4 and 17.5 of the Proposed QR 2013 SAA contain the additional steps noted above.	Comments are substantially the same as comments above.
(31)	Force Majeure Event (cl. 18)	The obligations of a party (other than monies payable) are suspended during a Force Majeure Event (FME) to the extent the obligations are affected by the FME. If part of the Network is damaged QR is not obliged to repair or replace that part unless the	The Access Agreement will provide relief in respect of payment of Access Charges to the extent that QR is unable to provide Access Rights due to a FME. QR has no obligation to repair or replace specified lightly trafficked infrastructure damaged by a FME unless the	The release from repair obligations applies more broadly in QR Proposed Principles in that QR is not obliged to repair any part of the network which is damaged or destroyed by an FME. Both Schedules provide that an Access Agreement may be	The QR Proposed Principles limitation on QR's obligation to repair materially alters the balance of risk in the favour of QR. QR could use its increased discretion to repair or not to its advantage in any subsequent negotiations between an affected Access

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		parties agree as to funding the cost of that work.	parties agree as to the funding of the work (cl. 19).	terminated due to a prolonged FME. The 2010 Principles provide specific relief to an Access Holder from paying Access Charges in to the extent that QR is unable to provide Access Rights because of a FME.	Holder. The relief from paying Access charges in the 2010 Principles is more reasonable considering the Access Holder will not be able to use the relevant parts of its Access Rights.
	SAA reference	The terms of the Proposed QR 2013 SAA are generally reflected in the Proposed Principles. Note also that under cl. 18.1(d)(iii) QR is not obliged to commence any agreed construction work unless the Operator pays the costs of such work first. There is no provision for apportionment of costs between Access Holders.	Generally similar to the provisions of the 2010 Principles however, the relief in respect of Access Charges to the extent that Access Rights are affected due to an FME, which is contained in the 2010 Principles, is not reflected in the terms of the AN 2010 SAA. Also note that those parts of the Network which QR does not have an obligation to repair or replace (unless funded by the Operator) if damaged by a FME are to be listed in Part 2 of Schedule 2.	The relief from paying Access Charges which relate to damaged Network (in the AN 2010 Principles) does not appear to have been reflected in the AN 2010 SAA.	Comments are substantially the same as comments above in relation to the Proposed Principles. However note the comment in the 'material differences' column.
		FME: Termination for Delay - If a delay caused by an FME continues for more than three consecutive months, either	If either party cannot perform its obligations under the agreement due to an FME for	Under the Proposed QR 2013 SAA there is no obligation to attempt to find alternative	The AN 2010 SAA terms are more reasonable by comparison as they include an

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		party may terminate the agreement by giving 20 business days' notice to the other party.	more than three consecutive months, the parties must meet in an endeavour to identify an alternative viable means to provide the suspended Access Rights and failing an alternative being agreed upon within one month, the parties may terminate on 30 days' notice.	Access Rights before terminating.	obligation that the parties endeavour to provide an alternative viable means of continuing with the agreement. This also provides somewhat more certainty for an Access Holder.
(32)	Reduction of Access Rights (cl. 19.1)	Access Agreements must include provisions which allow QR to reduce an Access Holder's Access Rights where the Access Rights are under-utilised. The Access Agreement must also set out objective criteria for the purpose of assessing whether the Access Rights are consistently under-utilised.	Access Agreement will contain provisions about the resumption of capacity by QR. Objective criteria must be used in assessing under-utilisation. There is a requirement that there be either a reasonable expectation of a sustained alternative demand or a reasonable expectation of a commercial benefit for the provision and management of the infrastructure sufficient to justify the resumption. There must also be a dispute resolution process conducted by an expert.	Under AN 2010 Principles there are 'alternative demand' or 'commercial benefit' thresholds before a resumption can take place. In the QR Proposed Principles these threshold requirements to a resumption do not exist. There is also no express requirement for a dispute resolution provision in QR Proposed Principles.	The QR Proposed Principles threshold requirements for a resumption and the dispute resolution provisions reflect a clearer balance. However, the 'objective criteria' for assessing under-utilisation, are not stated and appear somewhat vague. Again the 2010 Principles reflect a more balanced and reasonable approach.
	SAA reference	In addition to the above, note also cl. 19.1(a) provides that QR may remove rights if an Operator fails to operate all	QR may remove rights if an Operator does not operate over any 4 consecutive quarters, at least 85% of the	There is a notable change in the under-utilisation criteria and methodology.	Substantially the same as comments above. Also note that the Proposed SAA potentially increases the risks

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		Train Services for any 7 or more weeks out of 12 consecutive weeks. QR may (simply) give notice deleting the relevant train path (cl. 19.1(a)).	Train Services allowed under its Train Service (cl. 3.2). There is a detailed procedure for QR to give notice of intention to resume and a specific dispute process (cl. 3.2). Note also AN 2010 SAA includes cl. 3.6 which provides for the pro-rated reduction of Access Rights of Access Holders who were granted Conditional Access Rights, conditional on the expected completion of additional infrastructure where that infrastructure (when completed) provides less than the planned capacity.	There is no similar pro-rated reduction in Access Rights in the QR 2013 SAA to that contemplated in cl 3.6 of the AN 2010 SAA.	of unreasonable reduction in Access Rights. The AN 2010 SAA reflects a more balanced approach.
(33)	Relinquishment (cl. 19.2)	Access Agreement must include provisions which provide that an Access Holder may relinquish all or part of its Access Rights; and, any such relinquishment is subject to a fee calculated in accordance with cl. 19.2(b).	No similar provision.	QR includes relinquishment provisions in the Proposed Principles.	QR's Proposed Principle provides clarity for access seekers that relinquishment provisions may be included in a negotiated access agreement, particularly for non-coal traffics. The QR Proposed Principles reflect a balanced approach.
	SAA reference	In addition to the above, cl. 19.2 sets out a process for	An Operator may relinquish or transfer its Access Rights in	The relevant provisions are similar except for the	The AN 2010 SAA is more reasonable by comparison in

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		relinquishment including by way of transfer. This relinquishment provision is with respect to coal traffics.	accordance with cl. 3.3. This also includes the payment of a Relinquishment Fee. Note also that cl. 3.3(i) of the AN 2010 SAA requires QR Network to not unreasonably delay negotiations and execution of an Access Agreement with that existing or prospective Railway Operator, if, entering into that Access Agreement would result in a lessening of the current Operator's Relinquishment Fee.	obligation on QR not to unreasonably delay entering an Access Agreement if it would lessen an Operator's Relinquishment Fee.	that it includes an obligation that QR not unreasonably delay negotiation of access with an alternative user of the relinquished rights..
(34)	Assignment/Encumbrances (cl. 20)	QR may Assign and novate its rights and obligations under the Access Agreement without the consent of the Access Holder. The Access Holder may Assign and novate its rights and obligations with the prior consent of QR. The proposed assignee must agree to be bound by the terms of the Access Agreement. An Access Holder may only grant a security interest over its rights under the Access	An Access Holder may assign the whole of its rights/obligations under the Access Agreement to a related body corporate, provided that the assignor remains liable for the performance of the obligations. The Access Holder may assign its rights/obligations to a non-related body corporate, with the prior consent of QR not to be unreasonably withheld. A change in control of a	The QR Proposed Principles do not require QR to act reasonably when its consent is required. They also allow QR to assign without any consent. There are no provisions regarding permitted encumbrances in the 2010 Principles. There is no deemed assignment provision in the QR Proposed Principles.	The QR Proposed Principles allow wide rights for QR to assign. It would be more balanced if the provisions are mutual. The QR Proposed Principles are more restrictive in that any proposed chargee is not required to enter into a deed binding it as though it were the Access Holder. The 2010 Principles reflect a more balanced and usual

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		Agreement if, the holder of the security interest, the Access Holder, and QR have entered into a deed where the chargee must only exercise rights under the charge as though the charge was the Access Holder.	publicly listed Access Holder will be deemed to be an assignment (cl. 20).		approach in that QR is specifically required to act reasonably when its consent is required.
	SAA reference	Similar to the above, however, note that by comparison with the QR Proposed Principles, that QR's consent is not to be unreasonably withheld if QR is satisfied that the proposed assignee is financially competent and relevantly accredited (cl. 20.2).	QR will not unreasonably withhold consent where the QR is satisfied the proposed assignee is: financially sound; accredited and otherwise capable of performing the obligations of the Operator.	The provisions are similar. See comments above.	The QR 2013 SAA is somewhat less restrictive in that there is no requirement as to 'capability' to perform.
		Termination – Change of Control QR may terminate the Access Agreement immediately if there is a Change of Control (as defined under cl. 26). The definition excludes specified dealings in shares in entities listed on the ASX.	QR has a right to terminate (subject to any other limitations on termination) if the Operator purports to assign any of its rights other than as permitted under the agreement. Under cl. 21.2(d) a change of control is deemed to be an assignment except where the Operator is listed on the ASX. Cl. 21.2(e), however, contains additional restrictions which do not appear limited to	No material difference except for the potentially more restrictive words in cl. 21.1(e) of the AN 2010 SAA.	On balance, QR's proposed SAA appears to have a more reasonable definition of Change of Control. The QCA is comfortable if QR chooses to reflect this wording in preference to the wording in the AN 2010 SAA.

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			unlisted companies.		
		Encumbrance/Charging The Operator may only encumber or charge its interests over its rights under the agreement if the proposed chargee enters into a tripartite deed which covenants in favour of QR in accordance with cl. 20.3	cl. 21.3 contains substantially similar restrictions on encumbrances; however, the restrictions apply to both parties.	Under the AN 2010 SAA both parties are restricted in relation to granting security over their interests in the agreement. In the Proposed QR 2013 SAA, the restrictions only apply to the Operator.	The AN 2010 SAA reflects a more balanced approach.
(35)	Representation and warranties (cl. 21)	Access Agreement may set out representations and warranties given by the Access Holder in favour of QR.	No similar provision.	QR Proposed Principles contemplate Access Holder representations and warranties will be required.	It would be preferable if this requirement was mutual.
	SAA reference	In addition to any other express or implied warranties in the agreement, the Operator gives the warranties and representations listed in cl. 21(a)(i) to (ix) (inclusive). These warranties are generally quite standard corporate warranties. Under cl. 21(a)(viii) the Operator agrees that it has assessed the Network and it is satisfied as to the Network's suitability for the purposes of operating its Train Services. This warranty is coupled with	The Parties represent and warrant that they have full power to enter into and perform their obligations under the agreement (cl. 22.6). QR must carry out Maintenance Work such that the Operator can operate the agreed, scheduled, Train Services (cl. 6.2(a)). An inspection by a party does not release the other Party of its obligations under agreement (cl. 12.9).	The warranties in the Proposed QR 2013 SAA are greatly expanded. cl. 21(a)(viii) of the Proposed QR 2013 SAA is a warranty which deems the Operator to be satisfied with the suitability of the Network. Under the AN 2010 SAA, inspection of the Network is optional and it is not a deemed explicit warranty. Further, cl. 12.9 expressly states an inspection does not release the other Party of its	cl. 21(a)(viii) will likely further limit QR's liability in relation to an Access Holder. The warranty allows QR to move risks associated with the functionality of the Network onto the Operator/Access Holder. (See also Item 5 (Management and Control of Network). The warranty in relation to inspection of the track materially impacts on the risk profile of the Operator. This warranty could also impact on the rights and remedies of the

Item No.	Topic (per Schedule C)[53]	Proposed QR 2013 Schedule C (QR Proposed Principles) and QR 2013 SAA[54]	Aurizon Network (AN) AUT 2010 Schedule E ('2010 Principles') and AN 2010 SAA	Material difference(s)	Comments
		the right of the Operator (at the Operator's cost) to inspect the Network (cl. 21(c) and (d)). QR will maintain the Network in a condition such that the Operator can operate Train Services in accordance with the agreement (cl. 5.1(a)).		obligations under the agreement which broadly speaking negates any implied warranty.	Operator in relation to Dangerous Goods. The AN 2010 SAA again reflects a more balanced and more reasonable approach by comparison.
(36)	Confidentiality (cl. 22)	The Access Agreement may include a confidentiality provision if required by either party.	No similar provision.	Again, this is a new addition to the QR Proposed Principles.	There is concern the provision could be used to remove the access agreement from dispute resolution under the regulatory regime. The inclusion of this clause may be retained so long as it is explicitly stated that any confidentiality clause will not prevent an access holder from referring any issue, regardless of confidentiality, to the QCA for review in accordance with the dispute resolution processes in the QCA Act and the (as applicable) undertaking.
	SAA reference	The confidentiality clause places obligations on each party not to disclose Confidential Information (defined quite broadly under	The Parties are to comply with the provisions of the confidentiality deed set out in Schedule 12 (Schedule 12 is blank).	Under the Proposed QR 2013 SAA, the parties sign up to the confidentiality provisions upon signing the SAA. Under the AN 2010 SAA, the confidentiality	As above.

Item No.	Topic (per Schedule C)[53]	Proposed QR 2013 Schedule C (QR Proposed Principles) and QR 2013 SAA[54]	Aurizon Network (AN) AUT 2010 Schedule E ('2010 Principles') and AN 2010 SAA	Material difference(s)	Comments
		cl. 26.1).		schedule attached to the AN access undertaking would be open to further negotiation between the parties.	
(37)	Land tenure (cl. 23)	The Access Holder must comply with the requirements of QR's land tenure. If there is any inconsistency between QR's land tenure and the Access Agreement, the land tenure prevails. QR is not liable to the Access Holder for any loss suffered due to changes of QR's land tenure.	No similar provision.	Material limitations on QR obligations/liabilities in relation to land access.	This provision further limits QR's risk, specifically in relation to land tenure. QR is better placed to identify any risks in relation to relevant land. QR should disclose any limitations. The QR Proposed Principles create material risk and uncertainty for an Access Holder. It would be reasonable for QR: to warrant that it has appropriate rights to grant access; to be under a positive obligation to comply with its obligations under arrangements relating to land tenure; notify the Access Holder immediately of any of the matters in cl. 23(c); provide an indemnity to the Access Holder in

Item No.	Topic (per Schedule C)[53]	Proposed QR 2013 Schedule C (QR Proposed Principles) and QR 2013 SAA[54]	Aurizon Network (AN) AUT 2010 Schedule E ('2010 Principles') and AN 2010 SAA	Material difference(s)	Comments
					relation to the above. Land tenure is critical to the access rights to be granted. An Access Holder or customer may well be reluctant to invest in Rolling stock or mining or other infrastructure when there is uncertainty as to QR's land tenure. The 2010 Principles reflect a more balanced approach.
	SAA reference	The Operator acknowledges that the land on which the Network will operate is held under a Sublease or other form of land tenure and that the agreement is subject to the terms of the relevant land tenure. QR will not be liable to the Operator for any Claims which may be brought against or made upon the Operator, or any losses which the Operator may incur in connection with any land tenure (cl. 25.18).	QR does have a limited right to terminate as noted below.	See comments above in relation to land tenure	Substantially the same comments as above.
		Termination – Land Tenure Under cl. 13.1(d), QR is able to terminate if QR ceases to hold (for any reason) any Land	Under cl. 22.18(e) if QR's rights in respect of land, not included in the definition of 'Access' in	In relation to termination for loss of land tenure the Proposed QR 2013 SAA	In relation to land tenure, in the Proposed QR 2013 SAA the rights of termination are more

Item No.	Topic (per Schedule C)[53]	Proposed QR 2013 Schedule C (QR Proposed Principles) and QR 2013 SAA[54]	Aurizon Network (AN) AUT 2010 Schedule E ('2010 Principles') and AN 2010 SAA	Material difference(s)	Comments
		Tenure which permits QR to grant any of the relevant Access Rights. This clause is also to be read with cl. 25.18 (Sub Lease). See comments above.	the UT and identified in the relevant SAA schedule, which is controlled by a landowner (other than QR) are terminated (for any reason other than a default by QR or by agreement with the relevant landowner) then QR may suspend or terminate the relevant Access Rights insofar as they relate to that part of the Network which is situated on that land.	provisions effectively allow QR to terminate an entire Access Agreement due to the loss of any portion of relevant land. In the AN 2010 SAA, the right to terminate or suspend for loss of land tenure is limited to certain land identifiable before entry into the SAA and does not apply to default by QR or agreement by QR.	heavily in QR's favour. Again, this type of provision may well deter or inhibit investment and places existing investment at new risk.

APPENDIX E: AURIZON NETWORK INVESTMENT FRAMEWORK PRINCIPLES

SCHEDULE J

INVESTMENT FRAMEWORK PRINCIPLES

Foundation premises

1. QR Network cannot be forced to fund an Extension other than in accordance with an approved access undertaking or the provisions of the Act regarding determination of access disputes.

2. To the extent that QR Network does invest in rail transport infrastructure used in the provision of declared services1, including Significant Investments, the QCA can determine the rate of return that is commensurate with the risk of the investment.

3. QR Network should not be able to exploit its monopoly power.

4. Users should have the right to fund Extensions (other than replacement capital expenditure) at their option.

Undertaking coverage

5. All Extensions in respect of rail transport infrastructure used to provide the Declared Service must take place under the auspices of an access undertaking approved under the Act to ensure even-handed dealing with all parties.

6. QCA will have the following roles in addition to those already in the previous undertaking:

    (a) determining whether proposed capital expenditure forms part of a Significant Investment or not;

    (b) approving Access Conditions sought in respect of Significant Investments;

    (c) approving a Standard User Funding Agreement; and

    (d) making binding arbitration determinations in relation to:

        (i) Users' claims that they are unable to fund their shares of a Significant Investment via debt financing on reasonable terms obtained from a reputable financial institution; and

        (ii) the terms of a proposed or existing User Funding Agreements including: (A) security requirements, and (B) any variations from a Standard User Funding Agreement approved by the QCA.

(i) Network investment

[1] The declaration regarding provision of access to the QR Network rail infrastructure will not cover access to railway lines to new coal basins. Access seekers will have to seek declaration of these services via the QCA Act which has been amended to allow access to privately owned railway lines which meet the QCA Act's access criteria.

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Network Extensions

7. Subject to paragraph 8, Extensions should accommodate the needs of all Users who are seeking Access Rights which require additional Capacity and who are willing to commit to the approved terms and conditions of investment in the Extension during the Extension Process, whether or not these Users agreed to provide funding for the Extension.
8. However, where there is a Funding Shortfall in respect of a Significant Investment, only Funding Users are guaranteed to have their Capacity requirements accommodated in the relevant Extension.
9. If a User Funded Extension or Extension funded solely by QR Network produces Available Capacity, that Available Capacity and any pre-existing Available Capacity will be treated equally in future allocations of Available Capacity between Access Seekers.
10. All Available Capacity, whether funded by QR Network or Users, will be allocated in accordance with the Undertaking's capacity allocation rules.

Funding

11. Users may opt to fund Extensions (other than replacement capital expenditure) and other system investments2, even in circumstances where QR Network is willing to do so. Users need not provide the funding themselves directly but may involve other parties (e.g. Users may seek debt financing).
12. If Users intend to fund an Extension, all potential Users for the Capacity to be created by an Extension must be given the opportunity to participate in the funding of the Extension in proportion to the Capacity the Access Rights they are seeking would utilise.
13. If Users fund an Extension, they will be compensated for their investment by receiving an amount equal to the return on and of the capital component of Access Charges from any Users of the Capacity created by their investment who did not participate in the user funding (with QR Network being entitled to receive an amount equal to the components of Access Charges based on operation and maintenance costs).
14. QR Network must fully fund:
    (a) replacement capital expenditure;
    (b) Expansions which are valued at less than $300 million and are required to produce Available Capacity needed for provision of Access Rights sought by Access Seekers; and
    (c) capital expenditure valued at less than $300 million needed to respond to a Capacity shortfall resulting from either a change in System Operating Assumptions or an incorrect forecast of capacity delivered by Infrastructure Enhancements.

[2] Investments that are not strictly 'Extensions', such as 'robustness' projects proposed in previous QR Network Master Plans.

The Regulated WACC will apply to any such investments and Access Conditions cannot be sought in respect of access which is dependent on such investments other than in accordance with Clause 6.5.2 of the Undertaking. An Extension may include a number of related projects on different parts of the network. There may also be more than one such Extension over the Term. In the case of a dispute, the QCA will determine whether capital expenditure forms part of a Significant Investment or comes within this provision.

15. QR Network has no obligation to fully fund Significant Investments or Customer Specific Branch Lines. However, it is anticipated that QR Network will want to fund all or part of Significant Investments and Customer Specific Branch Lines where it considers it is in its commercial interests to do so, unless:

    (a) it is unable to raise finance or in doing so would prejudice its capital management; or

    (b) Users propose to fund all or part of such an Extension.

As discussed later, QR Network may seek approval for Access Conditions and/or additional returns in respect of Significant Investments.

If QR Network indicates that it is unwilling to fund all or part of an Expansion, the board of directors of QR Network must, or where the unwillingness to fund is based on a decision of its holding company, QR Network must procure that the board of its ultimate holding company, provide the QCA with a statement setting out the reasons for this, for publication on the QCA's website.

(A) Smaller users and difficulties in providing user-funding

16. QR Network must fund up to 30% of a partially User Funded Significant Investment, if requested to do so by Users that are unable to raise their own share of the funds by debt funding on reasonable terms from reputable financial institutions. QR Network can seek approval from the QCA for special terms and conditions for that funding to the extent justified by special risks and costs being borne by QR Network.

17. The obligation to partially fund Significant Investments in accordance with paragraph 16 is subject to QR Network having a maximum commitment of $300 million in respect of such funding for the Term.

18. If QR Network disputes that a User is unable to fund its share of the costs of a Significant Investment (by debt funding on reasonable terms from reputable financial institutions) and is unwilling to fund the User's share, the QCA will arbitrate. The onus of proof will rest with the User claiming they are unable to raise debt funding on reasonable terms from reputable financial institutions. If the QCA concludes that the User could have raised its share of the funds by debt funding on reasonable terms from reputable financial institutions, the User will not be eligible for QR Network funding under this provision.

19. While QR Network will not be otherwise obliged to provide funding for a Significant Investment, QR Network will have the right to participate in a User Funded Extension up to the level of the Capacity that is created in excess of that needed by the Funding Users.

Consequences of insufficient funding for Significant Investments

20. Where the aggregate of the development costs:

    (a) QR Network has voluntarily decided to fund;

    (b) Funding Users have decided to fund; and

    (c) QR Network has been obliged to fund in accordance with paragraph 16 above,

in respect of a Significant Investment (together the Committed Funding) is:

    (d) more than QR Network's estimate of the cost of building the smallest efficient Extension, then:

        (i) QR Network will design the level of Planned Capacity to be created by the Extension to reflect the Committed Funding; and

        (ii) the Capacity created by the Extension will be first allocated to all of the Funding Users (in the proportions their funding bore to the total development cost) and any remaining Available Capacity will be allocated among the other Users who put forward an expression of interest in accordance with paragraph 50 but did not provide User Funding based on the formation of a queue in accordance with the principles in the approved access undertaking;

    (e) is less than QR Network's estimate of the cost of building the smallest efficient Extension (with the difference being the Funding Shortfall):

        (i) QR Network will advise the Funding User of the Funding Shortfall and the Funding Users will be given a reasonable opportunity to elect to fund the Funding Shortfall (in which case they will be given the first right of refusal of Planned Capacity proportionate to the additional funding provided);

        (ii) if the Funding Users in aggregate fail to provide sufficient additional funding to rectify the Funding Shortfall, then QR Network is not obliged to develop the Extension (but may do so if it wishes to itself fund the Funding Shortfall); and

        (iii) if the Funding Shortfall is rectified, the Extension will be developed to reflect the smallest efficient Extension with Capacity created by the Extension being first allocated to all of the Funding Users (in the proportions their funding bore to the total development cost except to the extent a Funding User providing funding but did not exercise their right of first refusal) and any remaining Available Capacity will be allocated among the other Users who put forward an expression of interest in accordance with paragraph 50 but did not provide User Funding based on the formation of a queue in accordance with the principles in the approved access undertaking.

If QR Network is unwilling to fully fund a Significant Investment and some Users who are seeking additional Capacity are unable or unwilling to raise their shares of the funding, the Users who are willing to fund the Significant Investment will have to meet the full cost of the Significant Investment, subject to paragraph 16 above, and QR Network will not be obliged to develop the Significant Investment until such funding arrangements between Users are agreed or one or more Users will fund the Funding Shortfall in return for being allocated the remaining uncontracted Planned Capacity.

Ownership

21. QR Network will own and operate the rail transport infrastructure utilised to provide the declared service, including Extensions other than Customer Specific Branch Lines which are wholly funded by Users. Access to parts of the rail network created by Extensions to other coal basins will not automatically be declared and QR Network may or may not be the owner or operator for such Extensions.

22. Users will have the right to own and operate Customer Specific Branch Lines while QR Network must facilitate their connection to the existing network and ongoing operation.

Security

23. In relation to any User Funded Extension, each Funding User (or Funding User's financier where debt financed) may take security over the contracts, including the User Funding Agreement, and associated cash flows and QR Network's creditors may take security over its cash flows and the resulting Rail Infrastructure.

Construction

24. QR Network must construct all Expansions because of operational/safety concerns with multiple parties accessing an operating railway with multiple Users, subject only to the step-in rights described in paragraph 26.

25. Prudent cost overruns on construction will be incorporated into the Regulatory Asset Base and passed on to Access Holders via Access Charges, unless special Access Conditions are approved by the QCA which provide differently. QR Network will absorb all other cost overruns (as is the case now).

26. QR Network must expeditiously construct Extensions, including Extensions funded by Users. QR Network must, prior to developing an Extension, provide Users with an indicative timetable for the construction of the Extension. If QR Network unnecessarily delays the construction of an approved User Funded Extension, including an Extension that QR Network has agreed to fund, Users may undertake the construction at Users' expense. If there is a dispute regarding whether QR Network has unnecessarily delayed construction the QCA will arbitrate (having regard to QR Network's indicative timetable and any circumstances QR Network claims have delayed the construction). In the event of such a step-in right being exercised QR Network must use its best endeavours to facilitate Users' undertaking the construction of the Extension including, to the extent it can do so, by:

(a) providing access to land and electricity required for the development of the Extension;

(b) providing the Users with details of the required standards and specifications for the Rail Infrastructure;

(c) providing the Users with details of the current status of the work on the Extension;

(d) keeping all relevant Users informed regarding operations of the Rail Infrastructure which may impact on the development of the Extension;

(e) providing the funds it has received through User Funding that it has not spent in the development of the Extension to the Users undertaking the development of the Extension;

(f) assigning or novating contracts required for the development of the Extension or, where assignment or novation is not practicable, entering into back-to-back arrangements where QR Network on-supplies goods or services to the Users on the same terms as they are supplied to QR Network by third party suppliers; and

(g) assisting the Users undertaking the development to obtain all necessary licences and approvals for the development (by assignment from QR Network or otherwise).

27. Users will be permitted to construct Customer Specific Branch Lines to their own specifications, with interface standards approved by QR Network. QR Network must facilitate Users developing their own Customer Specific Branch Line including by providing access to land which QR Network has the power to provide and entering into a Rail Connection Agreement in respect of the Connecting Infrastructure.

WACC/Rate of Return/Access Conditions

28. The Regulated WACC provides an appropriate return on capital for normal monopoly infrastructure risks that are systematic.

29. The WACC that applies will be the same whether infrastructure investment is undertaken by QR Network or Users, reflecting the same infrastructure investment risk. Coal-company WACCs are not appropriate to User investment in coal rail transport infrastructure as they relate to the risks associated with coal-mine ownership (e.g. production, sales, prices etc) and not coal rail transport infrastructure risks.

30. All investments in Rail Infrastructure (by QR Network or Users) will earn the Regulated WACC, unless they incur risks in addition to those that are compensated for in the Regulated WACC. Such risks might include demand risk, asset stranding risk and construction risk.

31. If QR Network intends to impose Access Conditions in respect of the provision of access which is dependent on a Significant Investment it must seek approval from the QCA for such Access Conditions. The QCA may approve special Access Conditions including additional returns to address any additional risks associated with Significant Investment. Special Access Conditions may relate to matters such as: the

depreciation period and/or profile, take or pay arrangements or the term of contracts. To the extent that QR Network seeks additional returns to compensate it for additional risks, the risks should be accounted for in the cash flows to which the Regulated WACC rate is applied, with the cash flows being determined considering the possible outcomes and the probabilities of the outcomes as a consequence of the additional risks.

32. If QR Network considers that its cost of funds for a Significant Investment is inconsistent with the Regulated WACC, then QR Network may ask the Authority to approve an uplift on the Regulated WACC (the Varied WACC). The circumstances in which the QCA will approve a Varied WACC will be limited to changes in the risk free rate and debt margin in respect of the Significant Investment unless QR Network can show that, as a result of funding the Significant Investment, it has a materially different gearing ratio or credit rating. Users will have the option to accept a Varied WACC approved by the QCA, or to pursue User funding instead.

33. QR Network must obtain the QCA's approval for any proposed Access Conditions or other risk adjustments. However, parties will first have the opportunity to commercially negotiate the terms of access.

The QCA will approve Access Conditions that are commercially agreed between QR Network and all relevant Users unless:

(a) it is not in the public interest, including the public interest in having competition in markets;

(b) it may disadvantage the interests of parties who are not parties to the agreement;

(c) QR Network has failed to provide the required information to Users regarding risk and return (see below); or

(d) it would contravene a provision of the Act or the Undertaking.

34. As part of the process for negotiating the proposed Access Conditions, QR Network must provide upfront a detailed analysis to both the QCA and the Users of the additional risks faced by QR Network and the Access Conditions (including additional returns) it considers are required to mitigate or to compensate for those risks. Failure to provide this analysis will be grounds for the QCA to refuse to approve Access Conditions.

35. If parties are unable to agree terms within 60 days of the detailed analysis being provided by QR Network, or such further period of time approved by the QCA, the QCA will arbitrate the matter. The QCA will not grant extensions that take the total negotiation period to more than 120 days, unless a majority by number of the Access Seekers or Customers ask for such an extension. All periods referred to in this paragraph commence on the date that the QCA considers the price negotiations to have effectively commenced. Unless particular circumstances indicate otherwise, the QCA would consider the negotiation period to begin on the date when QR Network issues its detailed analysis of the additional risks and Access Conditions for an Extension. If the QCA has reason to believe that QR Network has commenced negotiating with Users regarding Access Conditions in

respect of an Extension, it may require QR Network to provide the detailed analysis required by this Investment Framework to all relevant Users within 10 Business Days and cease negotiating the content of Access Conditions until that analysis has been provided.

36. Users may at any time decide to refer the matter to the QCA for arbitration or to fund the Extension themselves. In considering the appropriateness of the proposed Access Conditions, the QCA will consult with stakeholders. The QCA may decline to arbitrate during the process, where it considers the referral is vexatious or the referring party has not negotiated Access Conditions in good faith.

37. Whether or not QR Network accepts the Access Conditions that the QCA considers to be reasonable, the QCA will publish its decision, which will indicate the Access Conditions the QCA considers reasonable.

38. QR Network may not seek to impose, and the QCA will not approve, any Access Condition that:

    (a) restricts Access Seekers or their Customers from raising disputes with the QCA or disclosing proposed Access Conditions or other contract terms to the QCA;

    (b) requires Access Seekers, Access Holders, or their Customers to disclose information that is confidential to one or more of them, to any other Access Holder, Access Seeker, or their Customer in circumstances other than those permitted by this Undertaking; or

    (c) results in QR Network earning Access Charges based on a Varied WACC or otherwise earning above the return provided by Reference Tariffs based on the Approved WACC, other than as approved by the QCA.

Pricing

39. Access Charges in respect of Access which is able to be provided by virtue of Extensions should be determined in accordance with the pricing principles incorporated in the undertaking, (i.e. a uniform tariff that sits between incremental and stand-alone costs), unless the QCA considers, on application from QR Network, that an alternative approach is appropriate in the circumstances.

40. The QCA will revise Reference Tariffs when a Significant Investment occurs, based initially on forecast costs and subsequently on actual costs.

41. Where a User Funded Extension is deemed by the Authority to have created Available Capacity in excess of that needed for an efficient expansion of the network (e.g. a User may want to construct a facility with excess Capacity), the cost of the excess Capacity may not be incorporated in the Regulatory Asset Base for the purposes of calculating current Access Charges and may instead be carried forward (at the Regulated or Varied WACC, as applicable to Access Charges for train services which utilise the Extension) for inclusion in Access Charges at a later date.

42. User funding will cover the capital costs of the Extension, with ongoing maintenance and operating costs included in the Reference Tariff in the usual way.

43. The Funding Users will have their capital investment (including any amounts of a relevant feasibility study) refunded to them in accordance with the depreciation profile associated with the capital expenditure, together with the Regulated or Varied WACC (as applicable) on the un-refunded balance, subject to QR Network receiving Reference Tariffs in respect of the user funded Capacity that are sufficient to cover the amount of the refund after meeting approved operating and maintenance costs. If Reference Tariff revenues are not sufficient, QR Network is obliged to refund only the amount it has received from such Reference Tariffs net of approved operating and maintenance costs. Users must also be refunded any financial benefits that accrue to QR Network as legal owner of the Rail Infrastructure. The arrangements should be such that QR Network receives no benefit (tax or cash flow) from wholly User Funded Extensions, with QR Network retaining only the portion of Reference Tariffs related to operating and maintenance costs.

44. If a shortfall (or surplus) in Reference Tariff revenue occurs in respect of Capacity funded by QR Network or Users, the shortfall (or surplus) will be met by (or refunded to) all Access Holders in the relevant Individual Coal System through the existing revenue cap adjustment process. A shortfall (or surplus) caused solely by a Funding User will be to the account of that Funding User.

45. No additional fees or on-costs may be charged by QR Network in respect of User Funded Extensions, unless there are additional costs or risks assumed.

Extension Process

46. The investment decision process (deciding on the reasonableness of/need for the investment in the Extension) should be independent of who funds the investment – QR Network, Users or a combination of the two.

47. QR Network will initiate an Extension Process where it:

    (a) believes an Extension is required to meet demand within the coal supply chain; or

    (b) is requested to do so by the owner or operator of an expanding or new unloading facility that services users of the Rail Infrastructure; or

    (c) is requested to do so by a coal supply chain group such as the DBCT Coal Chain Coordinator, the Gladstone Coal Export Executive and the BMA Hay Point Coal Chain;

    (d) has received access requests which would utilise in excess of 70% of the Planned Capacity to be developed by the smallest efficient Extension of the Rail Infrastructure; or

    (e) has received access requests for less than 70% of the Planned Capacity to be developed by the smallest efficient an Extension, but those Users are willing to meet 70% of the costs associated with development of the Extension.

48. The Extension Process must include timetables, deadlines and information requirements.

49. Where a need for further Infrastructure Enhancements can be reasonably anticipated, QR Network must undertake the necessary scoping and planning studies (including pre-feasibility and feasibility studies). Access Seekers seeking Access that is dependent on such Infrastructure Enhancements can be requested to underwrite the studies and all prudent costs of the studies will be:

    (a) considered as User Funding in respect of determining how Planned Capacity to be developed by an Extension is allocated and in respect of return of capital; and

    (b) included in the Regulatory Asset Base irrespective of whether the project is completed through to the commissioning stage.

If QR Network unreasonably delays the necessary studies, Users may undertake the necessary work at their cost and QR Network must give the Users all reasonable assistance, including any necessary information and site access.

50. A mechanism must be in place to inform all Users who would reasonably be expected to have an interest in gaining Access Rights which might be generated by a potential Extension of the network (including those listed on the Committed Capacity Register or in a queue for Available Capacity), and invite all Users to put forward an expression of interest in respect of the Access Rights they are seeking.

51. Funding Users must be given the opportunity to collaborate with QR Network in relation to all key matters affecting the cost and timing of the Extension, including, but not limited to project scope, cost, procurement strategy, construction and timing.

Dispute Resolution

52. Disputes arising between potential or existing Funding Users and QR Network in respect of:

    (a) proposed user funding terms, or

    (b) existing User Funding Agreements;

    can be referred to the QCA for determination, or to commercial arbitration if the QCA does not hold the power to hear the matter

Finalisation of the Investment Framework

53. QR Network will be required to submit:

    (a) a Standard User Funding Agreement; and

    (b) a draft amending access undertaking which incorporates the principles set out in this Investment Framework into the approved access undertaking,

with QR Network having 3 months from Approval Date to finalise the Standard User Funding Agreement and amendments to the Authority's satisfaction.

54. If QR Network fails to do so, the QCA will have the power to finalise and approve a Standard User Funding Agreement and amendments to the approved access undertaking to incorporate the principles set out in this Investment Framework.

55. In the interim, the QCA will require Parts 4, 6 and 7 of the approved undertaking to incorporate the most critical elements of these principles. As such, Extensions which are currently being progressed or considered such as Wiggins Island are covered by the new investment framework. However, in respect of Extensions which are currently in process (such as Wiggins Island), it will be treated as if QR Network had formed the intention to negotiate Access Conditions on the Approval Date.

56. Definitions

    For the purposes of this Schedule the following terms have the meanings given below:

Committed Funding has the meaning given in paragraph 20.

Customer Specific Branch Line means an Extension that when constructed will solely connect an Access Holder or Customer's single loading facility to Rail Infrastructure.

Expansion means an Extension that is not a Customer Specific Branch Line.

Extension of Rail Infrastructure includes an enhancement, expansion, augmentation, duplication or replacement of all or part of the Rail Infrastructure. An Extension may include a number of related Infrastructure Enhancements on different parts of the Rail Infrastructure.

Extension Process means the process described in paragraphs 47-51.

Funding Shortfall has the meaning given in paragraph 20.

Funding User means a User which has entered a User Funding Agreement with QR Network.

Infrastructure Enhancement means new Rail Infrastructure or a modification to existing Rail Infrastructure.

Investment Framework means the principles set out in this Schedule.

Major Expansion means an Expansion for the purpose of creating or providing additional Capacity substantially as a result of or in connection with a single Major External Development.

Regulated WACC means 9.96% per annum.

Significant Investment: means investment applying to a Major Expansion estimated to cost in excess of $300 million.

Standard User Funding Agreement means a pro forma User Funding Agreement

Users means Access Seekers and/or their Customers.

User Funding Agreement means an agreement by which a User agrees to provide funding to QR Network for the development of Infrastructure Enhancements.

User Funded Extension means an Extension, the costs of which are to be wholly or partly funded by Users pursuant to User Funding Agreements.

Varied WACC means a weighted average cost of capital different to that of the Regulated WACC.

Where a term has not been specifically defined in this Schedule, the definitions in Part 12 of the Undertaking apply.

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APPENDIX F: LIST OF SUBMISSIONS

Organisation/individual	*Submission number*
Asciano	6, 7, 26, 31
Bentley Resources	49
Association of Mining and Exploration Companies	8
Aurizon	9, 10, 27, 33, 43, 48
New Hope	11, 12, 28, 32, 44*, 50*
Peabody	13, 34, 45
Queensland Rail	1, 2, 3, 4, 5, 18, 19, 20, 21, 22, 23, 24, 25, 35, 36*, 37*, 38*, 39*, 40, 41, 42, 51*
Queensland Resources Council	14, 46
Glencore Queensland	15, 16, 29, 30
Yancoal	17, 47*, 52*

*Claims of confidentiality have been made for part or all of these submissions

REFERENCES

Australian Competition and Consumer Commission (ACCC). May 2001. Sydney Airports Corporation Ltd, Decision, Aeronautical Pricing Proposal.

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