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Attention: Bruce Chan
Office of the Rail Access Regulator
27th Floor
197 St Georges Terrace
PERTH WA 6000

By facsimile: 9486 4607

Dear Mr Chan

WestNet Rail Pty Ltd - Submissions

Thank you for the opportunity to comment upon Dr Michael's Draft Determination.

In general, WestNet Rail Pty Ltd ("WestNet") concurs with the Regulator's proposed approach, but there are a number of matters which require some elaboration, as some of the perceptions, both of market conditions and WestNet's internal structures and operations, still appear not to reflect the reality of the regulatory regime and WestNet's role within it.

1 General

The Regulator's observations in relation to the general segregation proposal are:

- (a) that sections 31 to 34 provide the minimum segregation requirements, which is plainly correct; and
- (b) that section 28 provides for "additional protection measures" to be established as required.

The implication (expanded in the Draft Determination on a topic by topic basis) is that additional segregation measures follow as a matter of course. If that implication is to be properly drawn from the Regulator's general statement it is of course incorrect, in that before there can be "additional protection measures" there

must be an identified deficiency in “segregation”. It is important always that the Regulator’s mind is directed to the question of segregation of access related functions, not cosmetics or non-segregation issues. Finally, it must be recalled that the Access regime was developed, specifically, around a vertically integrated rail operation (Westrail) which was subsequently divested in part on terms which explicitly required ongoing integration through a statutorily defined structure.

That is made particularly pointed by the following comment that the proposed segregation arrangements need to define how they link in with other aspects of the Code such as costing principles. Given compliance with the stated minimum requirement in section 34, that is the obligation to ensure that accounts and records are in such *form* to ensure that income, expenditure, assets and liabilities relating to the carrying out of access related functions are distinguishable from the other income, expenditure, assets and liabilities of any other function (irrelevant in WestNet’s case as its only function is the provision of access) is difficult to see what interaction exists with “costing principles”.

WestNet also observe, generally, that there is no justification to refer to other segregation models for *outcomes* of those models. Those models may provide useful information as to the inputs, or relevant considerations which might be taken into account, but the whole scope of the enquiry by the Regulator is limited by the Act and Code, and the existence, or *outcomes* of any other regulatory model is not a relevant consideration within section 20(4) of the Act.

2 Duty of Fairness

On page 30 in the first dot point under changes required you seek “a commitment to treat all access seekers and train operators (associates and third parties) equitably”.

The proposal is:

“The opening acknowledgment to contain a commitment to treat all access seekers and train operators (associates and third parties) *equitably* in relation to prices, service quality, paths and priorities.”

WestNet has a concern with the use of the term “equitably” as it has a quite different connotation to the term and concept used in the Act and the Code, which is defined by section 33:

“33. Duty of fairness

In performing their functions relevant officers must not have regard to the interests of the railway owner in a way that is *unfair* to persons seeking access or to other rail operators..”

The statutory obligation is defined in the negative: “not *unfair*”. Parliament has chosen specific language to circumscribe the duty of WestNet as access provider. It is inappropriate to “translate” that obligation into other language which does not have parliamentary sanction and which may connote a different meaning

Butterworth’s Encyclopaedic Australian Legal Dictionary, for example gives a number of instances of the use of both words to widely different ends:

“Unfair competition: Misappropriation of what equitably belongs to a competitor through underhand or sharp conduct.

Unfair contract: In relation to employment, a contract of employment liable to be declared void on the ground that it is unfair, harsh, or unconscionable, provides a total remuneration that is less than a person performing the work would receive as an employee performing the work, is against the public interest, or is designed to avoid the provisions of an industrial instrument.

Unfair dismissal: The termination of a contract of employment in circumstances that are unfair, harsh, unjust, or unreasonable. What is 'fair' depends on the circumstances of the case.

Unfair loan: A loan to a company where the interest on the loan or the charges in relation to the loan are or were extortionate. Whether the interest or charges were extortionate requires consideration of such matters as the lender's risk, the value of any security, the term of the loan, the payment schedule and the amount of the loan.

Unfairness: Unconscionable (or unconscientious) conduct. Unfairness is judged not by some generalised or colloquial sense of unfairness, but by the general principles of equity acting upon a person's conscience. Thus, inadequate consideration under a contract is evidence of unfairness, but is not itself unfairness

Equitable: Pertaining to or valid in equity, as distinguished from the common law.

Equitable interest: An interest in property enforced and created by the Court of Chancery in the situation where it would have been unconscionable for the legal owner of the property to retain the benefit of the property for himself or herself.

Equity: OF – *équité* – fair, even

1. The separate body of law, developed in the Court of Chancery, which supplements, corrects, and controls the rules of common law.
2. A right recognised by a court of equity, based on ethical concepts, and justifying in certain cases the judicial intervention of that court. The term denotes: the right to obtain an injunction or other equitable relief."

The legal definitions are supplemented by a presumption in equity that "equality is equity".

That of course is explicitly not the premise of an access regime designed to promote economic efficiency rather than equality by providing for market based negotiated outcomes, with scope for Ramsey pricing. One sees, however, in some of the public submissions, the translation of section 33 into a duty of "equality" which is contrary to the whole purpose of the Act and Code.

That notion must be dispelled, not promoted, by proper rigour in the use of language.

3 Separation of accounts and financial records

The Australian Railroad Group because of its company structure and because it is operating under an accounting class order under Corporations Law (approved by ASIC) prepares consolidated accounts. Therefore whilst the individual companies have separate accounts they are all consolidated for *statutory* reporting.

It is important to draw distinctions between *statutory* accounting for Corporations Act and corporate governance purposes, which depends upon actual costs and revenues accounted for in accordance with generally accepted accounting principles and *regulatory* accounting which depends upon actual revenues relating to access functions and constructs of costs based upon modern equivalent assets and efficient practices. Elements of the statutory accounting materials

The role of the WestNet Accountant (a position in the ARG corporate finance group) is primarily to act as the internal management accountant on behalf of WestNet Rail and provide financial status reports to line managers. Functions typically undertaken by the WestNet Accountant are to:

- prepare operating and capital budgets;
- prepare monthly management reports and the WestNet executive P&L report;
- conduct expenditure analysis reports; and
- deal with the daily accounting matters within WestNet.

These are primarily *cost* rather than *revenue* accounting matters and deal with *statutory* rather than *regulatory* accounting.

Many related functions, for example GST accounting, credit control, collection and banking, are performed by other ARG finance group personnel. Each has limited, task specific, knowledge for the purpose of performing their respective roles. Each is an area specialist, producing economic efficiencies because WestNet does not have the volume or value of transactions to employ dedicated staff in these specialist functions.

The role of the Access Policy Manager (a position in WestNet structure) is to manage all access related policy and financial matters. Functions typically undertaken include:

- process proposals for access;
- respond to proponents on all access related issues;
- provide all pricing information in relation to third party access applications;
- manage all financial models dealing with pricing under the Access Code;
- prepare revenue budgets; and
- monitor and maintain appropriate registers relating to access agreements and proposals.

The access management group within WestNet, which is autonomous, is solely responsible for *regulatory* accounting, pricing and revenue management. This

group draws information from the *statutory* accounting function, but supplies only limited and specific information to that function.

The distinction raises a significant and an important corporate governance consideration. Sections 323 to 323B of the Corporations Act (a law of the Commonwealth which by virtue of section 109 of the Commonwealth Constitution prevails over any inconsistent law of a State) WestNet must provide to ARG and its auditors all information necessary to prepare consolidated financial statements and the notes to those statements for the preparation of *statutory* accounts. ARG will always have access to the relevant information, and must have that access, in relation to the *statutory* accounting, and corporate governance functions of ARG. The question is what effective arrangements can be put in place that that confidential financial information in relation to access revenue and the *regulatory* accounting function does not find its way into the hands of AWR.

Rather than focus on positions or structures (which are subject to change over time in any event) WestNet believes that the proper approach is to identify the information and financial records that may give rise to concern where they are disclosed outside WestNet and to ensure there is a process that these are contained within WestNet and reporting is only on an aggregated level (subject to any supervening statutory obligation).

4 Train Scheduling

The Draft Determination poses a significant operational question in relation to train scheduling. The conclusion that WestNet should be required to undertake scheduling activities is stated to be a "value judgment" but the factor driving the value judgment appears to be the suggestion that there is a *possibility* of a *perception* that the above rail operator (AWR) could use train scheduling to obtain an unfair advantage. Set against the train path policy it is very difficult how this conclusion can be reached – as explained in the segregation submission AWR's ability to schedule in the course of routine operations is it constrained by the allocated train paths of all other users.

The process of reasoning appears to be thus:

"In essence, access seekers require assurances from the regulatory authority that the infrastructure owner will not give preferential treatment to an associated company in relation to, for example, the processing of a train path adjustment or obtaining a new train path and the price of access."

Developing from this the Draft Determination states:

"An internal separation in the organisational structure is a critical part of segregation to avoid conflicts of interest. There has been significant debate over whether network control should be located with WNR (to avoid potential for discrimination of third parties) or the train operator (to ensure the prime user has required the control to reduce safety risks). It is noted that the Queensland Competition Authority (QCA) is insisting that network control (for all but the metro passenger network) be transferred to the QR Network Access Group.

The alternative to this model is for WNR to establish a clear and transparent service level agreement or protocol that stipulates the rights of third party operators and attempts to ensure the equitable treatment of all operators.

While this issue is addressed under ‘Duty of Fairness’ the issue of AWR undertaking some scheduling functions for WNR also raises conflict of interest issues. The same conflict of interest issues would arise were WNR to contract out train scheduling to any entity that also operates above rail services using WNR’s below rail infrastructure. In these instances the perception that the above rail operator can use train scheduling to gain an unfair advantage can be equally as strong as the practice actually occurring. Such perceptions could prevent potential access seekers from entering the rail market.

In effect, this issue becomes a value judgement. On balance, it is the view of the Regulator that train control and scheduling should only be undertaken by WNR.“

The function of train scheduling and timetabling is an access related function and is and will continue to be controlled and managed by WestNet. WestNet maintains and will continue to maintain the Master Train Control Diagrams and the Working Timetable. Requests for change to the Master Train Control Diagrams and the Working Timetable will be dealt with in accordance with the Train Path Allocation policy.

Daily train operations will be managed in accordance with the Train Management Guidelines. Operators, including AWR, may prepare amendments to the daily train plan especially for services which experience variable demand or variable destinations. WestNet will approve those amendments if they are consistent with the Train Path Allocation policy and the relevant access agreement and implement those changes through train control, which is a WestNet function..

5 Confidential Information

We believe that the definition of Confidential Information in the Act is in substance the same as the preferred QR definition and we do not believe it is wise to seek to extend or vary the definition in the Act is these guidelines (much judicial authority cautions against attempts by subordinate legislation to vary the explicit wording of primary legislation).

The proposal is	While the Act says:
<ul style="list-style-type: none"> ▪ Revise definition of “confidential information” to include confidential information as defined in the Act plus more specific access information which is confidential along the lines of that contained in the QR Undertaking definition ▪ ▪ ▪ 	<p>31. Protection of confidential information</p> <p>(1) There must be an effective regime designed for the protection of confidential information relating to the affairs of persons seeking access or rail operators from —</p> <p>(a) improper use; and</p> <p>(b) disclosure by relevant officers, or other persons, to other officers or employees of the railway owner or other persons, except for proper purposes.</p> <p>(2) In this section —</p>

<p>▪ Confidential information::</p> <p><i>“Information which is not publicly available and the disclosure of which might reasonably be expected to affect materially the commercial affairs of a person, where such information:</i></p> <ul style="list-style-type: none"> - <i>Is not already in the public domain;</i> - <i>Does not become available to the public through means other than a breach of confidentiality;</i> - <i>Was not in the other party’s lawful possession prior to such disclosure;</i> - <i>Is not received by the other party independently from a third party free to disclose such information.”</i> 	<p>“confidential information” means information that has not been made public and that —</p> <ul style="list-style-type: none"> (a) is by its nature confidential; (b) was specified to be confidential by the person who supplied it; or (c) is known by a person using or disclosing it to be confidential.
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The Act’s provisions are in fact more prescriptive in that they require, under limbs (b) no more than that the information be specified to be confidential. The four bullet points in the QR definition substantively do no more than expound what is “public” information, but the QR definition requires a value judgment to be made about the importance of that information which is not present in the Act. There is potential for unfortunate confusion in attempting to impose new standards by the Determination materially inconsistent with the Act.

Yours faithfully

T.F. Ryan
General Manager