

SEGREGATION ARRANGEMENTS  
TO APPLY TO  
WESTNET RAIL

DRAFT OF THE DETERMINATION OF  
THE INDEPENDENT RAIL ACCESS REGULATOR

IN ACCORDANCE WITH THE REQUIREMENTS OF  
SECTIONS 28 TO 34 OF THE RAILWAYS (ACCESS) ACT 1998

24 APRIL 2002



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## Opportunities for further comment

Interested parties are invited to examine the draft of this Determination and provide comments to the Regulator by 15 May 2002.

The Regulator will consider the comments received in finalising the Determination. It is anticipated that the Determination will be finalised by 31 May 2002.

When finalised, this Determination is the mechanism by which the Regulator intends to give effect to Section 29(2) of the *Railways (Access) Act 1998*. Under this Section, the Regulator may confer with WestNet Rail (WNR) on any matter which relates to the way in which WNR's duty to segregate is to be carried out, with a view to the Regulator and WNR reaching agreement on the matter

The Determination requires WNR to address a number of issues and implement changes to its segregation arrangements to the satisfaction of the Regulator. In the event that agreement is not reached, the Regulator may give directions to effect the necessary changes in writing to WNR under Section 29(3) of the *Railways (Access) Act 1998*.

In subsequent discussions, WNR has already agreed to implement a number of the suggested changes. Even so, all of the required amendments have been fully documented in the Determination so that stakeholders can gauge the changes that are being required of WNR on its segregation submission as lodged with the Regulator in November 2001.

As soon as it is approved, the segregation arrangements will be made publicly available on the Office of the Rail Access Regulator's website.

The Regulator will be developing a set of key performance indicators in consultation with WNR to assess and monitor the effectiveness of segregation arrangements, and invites suggestions on the composition of these indicators.

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## 1. Introduction

WestNet Rail (WNR) is the principal provider of “below” rail freight infrastructure in Western Australia, covering approximately 5,000 kilometres of track in the southwestern corner of Western Australia. WNR is a subsidiary of the Australian Railroad Group (ARG), a consortium comprising Wesfarmers and Genesee Wyoming. ARG also has another subsidiary company, Australian Western Railroads (AWR), which provides above rail services in Western Australia.

Section 3 of the *WA Railways (Access) Act 1998* (“the Act”) defines a “railway owner” to mean the person having the management and control of the use of the railway infrastructure. Within this context, WNR is considered to be the railway owner for the Western Australian rail freight infrastructure.

Section 28 of the Act requires the railway owner to make arrangements to segregate its access-related functions from its other functions and to have appropriate controls and procedures to ensure that the arrangements in place operate effectively and are being complied with.

Segregation, which is often termed “ring-fencing”, refers to the separation of access related functions from other activities, in particular train (or above rail) operations. While WNR and AWR are independent subsidiaries of ARG, there are concerns within the rail industry that the separation of WNR access-related functions from ARG and AWR are not clearly defined and that there is a need to ensure effective arrangements are in place to separate contestable and non-contestable activities.

Under Section 29(1) of the Act, the railway owner is required to obtain the Regulator’s approval to the segregation arrangements it is proposing to implement. In early November 2001, WNR submitted its proposed segregation arrangements to the Regulator for his approval.

In considering WNR’s proposed segregation arrangements, Section 42 of the *Railways (Access) Code 2000* (“the Code”) requires that the Regulator publish a notice describing the requirements of Sections 28 and 29(1) of the Act and a general description of the proposed segregation arrangements in major newspapers, with details on where further information can be obtained and inviting submissions on the proposed arrangements. To this effect, on 17 November 2001, a notice was placed in *The West Australian* and *The Australian* newspapers. After an extension in the submission deadline, the closing date for submissions was 11 January 2002.

Ten public submissions were received on WNR’s segregation arrangements (Appendix 1). These submissions are available on the Office of the Rail Access Regulator’s website ([www.railaccess.wa.gov.au](http://www.railaccess.wa.gov.au)) along with WNR’s response to the submissions.

## 2. The WA legislative segregation requirements

The legislative requirements in relation to segregation are provided for in Sections 28 to 34 of the Act and these are summarised as follows.

### **SUMMARY OF LEGISLATIVE REQUIREMENTS TO SEGREGATE ACCESS-RELATED FUNCTIONS**

*(summarised from Part 4 of Division 3 of Railways (Access) Act 1998)*

#### **Duty to segregate (Section 28)**

A railway owner must make arrangements to segregate its access-related functions from its other functions, and have appropriate controls and procedures to ensure that the arrangements in place operate effectively and are being complied with.

#### **Powers of Regulator in relation to segregation (Section 29)**

The railway owner must obtain the Regulator's prior approval for its segregation arrangements or variations to such arrangements. The railway owner and the Regulator may confer to reach agreement on these arrangements. The Regulator may also provide written directions to the railway owner in relation to segregation and these directions are to be complied with. Railway owners who fail to comply with an arrangement, an agreement or a direction commit an offence (penalty: \$100,000).

#### **Matters to be covered as part of duty to segregate (Section 30)**

Without limiting Section 28, the railway owner must ensure that requirements specified in Sections 31 to 34 are met.

#### **Protection of confidential information (Section 31)**

There must be an effective regime to protect the confidential information of access seekers or rail operators from improper use and disclosure by officers of the railway owner. Confidential information is defined as information which has not been made public and by its nature is confidential; was specified as confidential by the person who supplied it; or it is known by a person using or disclosing it to be confidential.

#### **Avoidance of conflict of interest (Section 32)**

The segregation arrangements must ensure that relevant officers have no conflict in duties between the performance of access-related functions and other business of the railway owner.

#### **Duty of fairness (Section 33)**

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

#### **Maintenance of separate accounts and records (Section 34)**

A railway owner must ensure its accounts and records are in such form as to enable all income, expenditure, assets and liabilities relating to carrying out access related functions to be properly recorded and distinguished from the railway owner's other income, expenditure, assets and liabilities. Where necessary any income, expenditure, assets or liabilities that relate only in part to the access related function must also be apportioned in a fair and reasonable manner.

Section 20(4) of the Act provides the framework within which the Regulator's determination required under Section 29 of the Act is to be made.

Section 20(4) states:

*In performing functions under this Act or the Code, the Regulator is to take into account –*

- (a) the railway owner's legitimate business interests and investment in railway infrastructure;*
- (b) the railway owner's costs of providing access, including any costs of extending or expanding the railway infrastructure, but not including costs associated with losses arising from increased competition in upstream or downstream markets;*
- (c) the economic value to the railway owner of any additional investment that a person seeking access or the railway owner has agreed to undertake;*
- (d) the interests of all persons holding contracts for the use of the railway infrastructure;*
- (e) firm and binding contractual obligations of the railway owner and any other person already using the railway infrastructure;*
- (f) the operational and technical requirements necessary for the safe and reliable use of the railway infrastructure;*
- (g) the economically efficient use of the railway infrastructure; and*
- (h) the benefit to the public from having competitive markets.*

The nature of the decision-making power given to the Regulator under Section 29 is such that it is mandatory in so far as the Regulator must exercise it by taking into account all the factors listed in Section 20(4). However, under Section 29 the application of Section 20(4) is discretionary in so far as the Regulator may allocate such weight to each of the factors listed in Section 20(4) in a manner that the Regulator considers appropriate to ensure a balancing of competing and sometimes conflicting interests for the railway owner, access seekers and the community.

It should be noted that there is no requirement under the Act or Code for ARG to establish subsidiary companies for its above and below rail operations. The legal requirement for ARG to establish WNR and AWR was provided for by the Western Australian Government in the *Rail Freight System Act 2000* as a condition of sale of the State's rail freight business.

### **3. The WNR segregation arrangement**

The segregation arrangement submitted to the Regulator by WNR (“the Proposal”) contains a discussion of the position taken by WNR on segregation issues in support of its proposed arrangements as outlined in Section 10.3, “Segregation Arrangements to be adopted”.

As WNR has requested that the Regulator work from Section 10.3 of its submission to develop the final approved segregation arrangements, it is that section which has been assessed by the Regulator in this Determination.

The entire WNR submission is available on the Office of the Rail Access Regulator’s website ([www.railaccess.wa.gov.au](http://www.railaccess.wa.gov.au)).

### **4. Discussion of issues**

Issues raised in public submissions which are considered significant are discussed under the following headings:

- General – duty to segregate;
- Confidential information;
- Conflict of interest;
- Duty of fairness;
- Separation of accounts and records;
- Compliance with segregation arrangements;
- Other measures.

The following discussion commences with a summary of WNR’s position under each of the above headings and the comments received from the public consultation process. WNR’s response to the public comments is then provided, followed by the Regulator’s views and comments.

#### **General - duty to segregate (Section 28 of the Act)**

##### ***i) Summary of WNR’s Proposal***

In the preamble to its submission, WNR recognised its legislative responsibility to adopt appropriate segregation arrangements. WNR states that its primary role is in access related functions and it does not operate in the above rail market. As a result WNR believes that the segregation arrangements that it is proposing are fair and reasonable.

*ii) Comments from the public consultation process*

- WNR's Proposal is minimalist and requires substantial additional measures to adequately protect third parties. The system should be comprehensive with exemptions available where compliance costs exceed the net public benefit. Sections 31 to 34 are the minimum inclusions and that under Section 28 other protection measures can be established as required to protect third parties.
- The Queensland Rail (QR) Undertaking provides a sound template for an effective ring-fencing system and that it should be extensively utilised by the Regulator.
- The segregation arrangements need the addition of a "focus" (ie. how does it relate to the other requirements of the Code, including its importance to meeting those objectives). In addition any terms that are considered critical should be properly defined.

*iii) WNR's response*

- WNR rebuts the suggestion that its proposed segregation regime does not comply with Section 28 of the Act, having regard to:
  - ◇ the key indices for compliance in Section 28 set out in Sections 31 to 34, and the apparent key considerations which those sections manifest;
  - ◇ the considerations applicable to approval of the segregation regime under Section 20(4) of the Act and, in particular, a consideration that segregation arrangements should actively promote, rather than simply impose inefficient costs upon, the provision of access.
- WNR contends that its segregation arrangements meet or exceed Australian best practice for ring-fencing.
- WNR's access related functions are self contained, and operated in a manner calculated to extract maximum efficiency from the available support infrastructure without compromising confidentiality, a solution consistent with the paramount considerations under the Act.

*iv) Regulator's views and comments*

- Sections 31 to 34 of the Code are the minimum segregation requirements and Section 28 provides for additional protection measures to be established by the Regulator as required. WNR will need to make a number of additions and refinements to improve the overall effectiveness of the segregation arrangements. For example, WNR's segregation document needs to



clearly define how it links with the other aspects of the Code, such as costing principles.

- The QR Undertaking provides a guide for assessing the effectiveness of WNR's segregation arrangements. While information comparing requirements of other Australian segregation models are useful, any segregation arrangement must balance the interests of all parties, and it is noted that these interests may differ between jurisdictions.

The Regulator intends to periodically review other access regime developments and consider those arrangements that are applicable.

Confidential information (Section 31 of the Act)

i) *Summary of WNR's Proposal*

WNR believes it has established a regime of confidential information as defined in the Code including:

- a system of written record keeping that only allows appropriate WNR staff to access the records;
- a security system on electronic records that only allows appropriate WNR staff to access the records;
- appropriate controls on data, including information in the Rail Access Management System (RAMS) and costing and pricing information to protect confidential information;
- specific provisions in each access agreement providing contractual obligations on WNR to protect confidential information.

WNR states in its submission that it will keep information it receives in relation to access related matters confidential in accordance with the arrangements stipulated in its submission.

Where an employee of WNR has prescribed duties which include managing or conducting access related functions, WNR intends to apply the following procedure to ensure confidentiality is maintained:

- WNR will at the time of their permanent or temporary appointment, require the employee to sign a statement that they are aware of their responsibilities and obligations under the Code and specifically as it relates to confidential information as defined in the Code and in these arrangements.
- This process will be conducted on an annual basis in conjunction with a compliance audit.

*ii) Comments from the public consultation process*

- Access seekers should be able to require WNR to enter into a reciprocal confidentiality deed.
- WNR needs to be in separate premises to reduce the risks of improper use of confidential information as well as improving the perception that fair access to third parties is available.
- A tighter and more detailed definition of confidential Information is needed. Additionally, a list of examples of what is considered to be confidential information should also be provided in an appendix.
- The Rail Access Management System (RAMS) and Revenue Accounting System (RAS), as identified in WNR's submission, have highly sensitive confidential information and require far greater security protection measures. These measures need to be specifically detailed.
- Staff who can access confidential records should be defined by title and all other staff expressly restricted to such records. All such staff should sign confidentiality agreements.

*iii) WNR's response*

- WNR has no objection to marking access related material in an appropriate manner: "Confidential – WestNet Access Matter".
- WNR accepts that:
  - ◇ confidential access related material should be securely maintained;
  - ◇ WNR will treat an access application, including the fact of making the access application, as confidential.
- In any consideration of WNR's compliance with the obligations imposed by Sections 28, 30 to 34 of the Act, the following must be given consideration:
  - ◇ the factors listed in Section 20(4) of the Act;
  - ◇ the main object of the Act, namely to establish a rail access regime that encourages the efficient use of and investment in railway facilities by facilitating a contestable market for rail operations;
  - ◇ the law in respect of restraint of trade (this is particularly relevant to confidentiality undertakings between WNR and its employees, contractors and other third parties).

- Measures which go beyond what is reasonable to adopt in the circumstances are likely to work against the stated main object of the Act and in some cases be unenforceable.
- There appears to be some misapprehension as to the treatment of access related information:
  - ◇ When not in use, all physical access material is maintained in locked storage facilities (whether office or cabinet based) within WNR's access group. That access group in turn is within a separate area that is locked when not attended by WNR personnel;
  - ◇ Electronic materials are stored on WNR's file server, which is physically separate from that of ARG and password controlled;
  - ◇ Physical access to terminals that have access privileges to access related information is only available from within WNR's access group;
  - ◇ Train path planning and allocation, including planning of possible train paths for access applicants, is undertaken by WNR on its separate computing equipment and is not undertaken under RAMS;
  - ◇ Financial information in relation to an access application is processed within WNR's access group. While information may be extracted from MIMS, or RAS, as necessary, the processing and compilation of that material is undertaken on WNR's equipment;
  - ◇ RAMS access by AWR personnel or any other operator is restricted to AWR's or the other operators own train information. No information is input into RAMS until an access application has reached access agreement, and operational planning is required.
- The criteria of who should have access to which records will be determined in accordance to:
  - ◇ the purpose for which the information has been provided;
  - ◇ any requirements imposed by the law.
- The introduction of a register system for the recording of information in relation to access would simply result in additional costs with little demonstrable benefit.
- A requirement that all employees, executives and contractors sign undertakings of confidentiality and familiarity with the Act and Code (with penalties imposed) is a measure which exceeds what is reasonably required to protect the interests of the access seekers/users under the Act and Code

and to meet the objectives of encouraging the efficient use of an investment in railway facilities.

- WNR and AWR are physically separated. Separation into separate buildings is not reasonably necessary to achieve objectives of the Act and Code.
- None of the other segregation models looked at, prohibit relocation of staff between provider and user or require separation of all staff. Most emphasise separation of operational from management and marketing staff, which is reflected in WNR's model.

*iv) Regulator's views and comments*

- It is noted that other jurisdictions have required the use of confidentiality deeds, acknowledgment registers or similar type instruments for staff of the below rail business. These are not only effective in, but will demonstrate WNR's commitment to, enhancing the ability of WNR to protect confidential information.

WNR staff positions dealing with confidential access-related information should be identified in an appendix to WNR's segregation arrangement guidelines.

Any staff accessing confidential information, whether they are permanent staff, advisers or contractors, should be covered by a confidentiality deed. Staff who have the potential to act in these positions should also be covered by confidentiality deeds.

Further, the merits of an access seeker and WNR signing their own confidentiality deed should be explored as part of the negotiation process.

- Some segregation arrangements used elsewhere require the use of separate premises and IT systems. This requirement may result in a loss of the synergies obtained from operating as a vertically integrated business. As the objectives of segregation can, on balance, be met by the application of stringent, but fair and reasonable measures, there should be no need for separate premises and IT systems. However, if it can be demonstrated that the segregation arrangements are not working effectively then this position will be reconsidered. Further, if at some stage the entire operation moves from its current location the matter could be revisited.

In the meantime, a more detailed specification of access restrictions to offices and IT systems will need to be contained within the segregation arrangements. Additional information on password and security pass controls, whether firewalls are to be utilised and the controls on the

administrators of these security systems will be sought from WNR.

- The definition of confidential information should be clarified by WNR. Examples of what constitutes confidential information should be listed by WNR.
- Protecting and safeguarding confidential information, particularly that in RAMS and RAS, is considered a key requirement.

In this regard, a general requirement is that access related financial records should not, wherever possible, be centralised outside WNR. If some access related financial records need to be provided to the parent company of WNR then strong control measures should be implemented to prevent the transfer of confidential information from the railway owner to train operators and vice versa.

WNR proposes to utilise ARG's Finance Group to provide accounting information support to it. To ensure that confidential information is protected, the Regulator is of the view that WNR must commit to being self-sufficient for finance but, for example, can share payroll and human resource functions.

WNR has advised that ARG provides a central registry of some non-confidential information, but that all confidential information on access is restricted to a small group of authorised WNR staff. Housing any confidential information within a parent entity increases the potential for misuse and accidental disclosure, and should be avoided. The segregation arrangement will require detailed procedures for safeguarding and managing the registry as well as detailed controls to protect its contents.

- The Regulator understands that it may be necessary to exchange confidential access-related information between WNR and WAGR:
  - ◇ as co-railway owners providing access to an operator;
  - ◇ in their respective roles as lessee and lessor of the rail freight infrastructure.

There must be an obligation to ensure that the information passed between WNR and WAGR is treated in a confidential manner. This requirement can be met with the use of confidentiality deeds.

#### *Avoidance of conflict of interest (Section 32 of the Act)*

##### *i) Summary of WNR's Proposal*

WNR believes that because of the separation of access related functions from

ARG that it has no existing conflicts of interest.

In the event that any staff are rotated within ARG and AWR to perform access related functions within WNR, WNR would ensure the personnel:

- did not have access to confidential information;
- were familiarised with the requirements of the Code;
- were appropriately supervised in the event a conflict of interest was to arise.

WNR states that it is required to provide management reports to both its own Board of Directors and to officers and members of the Board of ARG. With respect to such management information:

- reports to management of ARG are dealt with only in meetings where WNR and ARG management are present and no representatives of related entities operating train services, such as AWR, are present;
- members of the WNR Board are not members of the AWR Board;
- where confidential information is provided from the WNR Board to either ARG Management or the ARG Board it will be clearly identified.

*ii) Comments from the public consultation process*

- The common director of ARG and WNR and the reporting of WNR information to the ARG Executive require the need for detailed and precise controls to prevent conflicts of interest.
- Key finance and accounting staff must be a part of WNR, and not be a “shared” resource.
- The segregation arrangements and use of confidentiality agreements also need to fully apply to any advisers and consultants of WNR.

*iii) WNR's response*

- It was a requirement of the Government sale process that the business of Westrail Freight be sold to one purchaser, that is, it was sold as a vertically integrated business. Accordingly no legal separation is mandated by the Act and Code and mechanisms which seek to impose a measure of separation beyond that consistent with the proper and legitimate governance by ARG of its subsidiary assets are not required by, or legitimate under, the Code.
- As a general matter of corporate governance, WNR's prime obligation is to ensure the financial viability of its own operations. It does not have access

to, and is therefore not aware of, details of the financial position of AWR on an unconsolidated basis. Any ability of ARG to interfere in the conduct of WNR's operations in accordance with that principle is constrained by WNR's contractual commitments and the provisions of the Code.

- An access seeker who complies with Part 2 of the Code has a right to obtain access on terms determined by arbitration under Division 3 of Part 3 of the Code. The ability of ARG to inhibit, by "strategic" decision making in relation to WNR's operations (to the benefit of AWR) is effectively precluded.
- To the extent that there are concerns relating to information flow through the Board of ARG, WNR observes that:
  - ◇ the corporate structure in which WNR is a subsidiary of ARG is determined by the sale process and the *Rail Freight System Act 2000*;
  - ◇ however, principles of corporate governance of general application require that ARG receives sufficient information in relation to WNR's operations to permit ARG's directors to discharge their duties as directors of that company in relation to the assets of that company (which include WNR as a wholly owned subsidiary) and the provision of financial support to WNR for the undertakings of that company.
- To the extent that actual or potential conflicts of personal interest and directorial duty may arise in such circumstances, the obligations of the directors of ARG are already addressed by the general law of directors' duties and in particular Part 2D.1 Division 1 of the *Corporations Act 2001*.
- WNR will put in place, and will procure that ARG puts in place, protocols, to be embodied in a code of practice for dealing with access information for the Boards of WNR and ARG to:
  - ◇ embody the obligations in Sections 28, 31 to 34 of the Act;
  - ◇ ensure that no confidential information (as defined for the purposes of the Act) is improperly used or disclosed to a person who is a director of AWR by a member of the management of AWR.
- WNR will prepare a comprehensive statement of obligations, including reference to penalties (provided by Section 29 of the Act) to be signed by way of acknowledgment, by each relevant officer of WNR. Accordingly, a confidentiality deed is unnecessary given the duty of confidentiality is already imposed by the Act and Code to which penalties attach.
- WNR's arrangements in relation to security of confidential information will also apply to external contractors if it is reasonably foreseeable that

contractor may have access to confidential information in their capacity as an adviser to WNR which might place them in the position equivalent to that of a relevant officer under the Act or Code, might lead to a breach by WNR of its obligations of confidentiality under Section 31 of the Act.

- WNR presently has in place arrangements by which:
  - ◇ external legal advice is obtained in relation to access related matters (in-house legal resources are not used in those matters). The firm providing advice in relation to access matters to WNR does not advise AWR;
  - ◇ other contractors providing assistance to WNR in relation to access related matters, or who have access to information related to access matters for the purpose of advice do not act for AWR. Should it be necessary any time for a contractor who has acted for WNR to act for AWR, WNR will insist upon separation of personnel plus appropriate confidentiality instructions within that contractor and governing dissemination of information within that contract.
- A requirement that a formal threshold be established when a contractor is deemed to be an employee of WNR for ring-fencing purposes is not reasonably necessary.
- In relation to the reporting responsibilities of the MIM's security officer, that officer reports to the information services manager and ultimately the Chief Financial Officer within ARG. The MIM's security officer must obtain approval from WNR's General Manager before granting to any person access rights to WNR related information.
- It should be noted that Section 20(4) recognises that the railway owner's actual legitimate business interests have an overriding importance in determining the adequacy of segregation measures. The structure of the ARG Group and the efficiencies available to WNR from that group that are legitimate business interests.
- A requirement that any AWR employee rotating from AWR to WNR and back should sign an acknowledgment of confidentiality in accordance with WNR's confidentiality protocols and have their computer access files varied is accepted. However, WNR does not propose staff rotations. Rotations will only arise in emergency circumstances.

iv) *Regulator's views and comments*

- The need to fulfil directors' responsibilities under the *Corporations Act 2001*, while avoiding potential conflicts of interest, is an issue that relates to both



protecting confidential information (Section 31 of the Act) and avoiding conflicts of interest (Section 32 of the Act).

There is a need to achieve a balance between the *Corporations Act 2001* requirements for directors of, in particular, ARG to be fully informed about its subsidiary company, ie. WNR, with the more specific requirements specified in the Act; being the need for WNR to protect confidential information. Preventing potential conflicts of interest in this area is a key challenge in establishing effective segregation arrangements (ie. how to prevent directors from obtaining “deal level” information to the benefit of AWR and ARG as a whole).

Under the *Corporations Act 2001* the three key requirements for directors of companies in relation to segregation arrangements are to:

- ◇ exercise a duty of care (Section 180): in exercising their powers and discharging their duties with the degree of care and diligence that a reasonable person would exercise;
- ◇ act in good faith (Section 181): directors have a duty to act in good faith in the best interests of the company and for a proper purpose;
- ◇ disclose or avoid conflicts of interest (Section 191): directors must disclose any material personal interest in a matter that relates to the affairs of a company unless it is specifically exempt.

It is possible for directors of ARG to be able to fulfil their statutory duties as outlined above, and that they can avoid potential conflicts of interest by not being briefed down to “deal level” information.

The approach to safeguarding information (and yet still enable the Board and CEO to fulfil their statutory duties) would be to not provide the CEO and Board with “deal level” confidential information on new access proposals. Instead they could receive a report that provides in aggregate information new access business applications. However, in a practical sense, this may not be realistic and more detailed information may be required by the CEO and Board in order for them to carry out their responsibilities.

As a result, WNR will need to implement a protection mechanism for the purpose of not identifying the access seeker(s) and their preferred train operator when reporting such information to the CEO and ARG Board. Similarly, a clear procedure will have to be developed by WNR for briefing the CEO of ARG (outside of Board meetings) in relation to the access proposals of third parties.

In this regard, the arrangements specified by WNR in their submission lack detail and are in need of refinement. WNR is required to advise the Regulator on the procedures and strategies that it will implement to safeguard confidential information, such as the name of the access seeker and preferred train operator, from being distributed to an associated company, while still allowing the CEO and ARG Board to carry out their legal obligations.

- A key measure to prevent conflicts of interest is a requirement which restricts staff from being shared between (or working for both) WNR and AWR. If not addressed, such situations provide a perception that a conflict of interest may exist.

The segregation arrangements need to establish a protocol for restricting staff secondments (both short term and long term) between the key personnel of WNR and AWR. This is required for WNR's management and access staff and AWR's staff who deal with access and pricing issues.

Unless an "emergency" situation arises, staff of associated companies will be precluded from being rotated into nominated access-related positions. In the event of an "emergency" WNR will need to inform the Regulator accordingly. The employee will be required to sign a confidentiality deed with access to their computer files to be temporarily varied. Initially, WNR is required to inform the Regulator on what they consider to constitute an "emergency" situation.

The Regulator's preference is that ARG financial staff solely dedicated to WNR should be employed by WNR. Given that the ARG accountant provided to WNR will be solely dedicated to WNR issues, that accountant should be employed by WNR. The accountant should also be located within and report to WNR.

#### Duty of fairness (Section 33 of the Act)

##### *i) Summary of WNR's Proposal*

WNR acknowledges and accepts that it has a duty of fairness to access seekers relative to its treatment of other access seekers under the Code; and others granted access under other arrangements.

Its view is that the mechanism for ensuring the duty of fairness is two-fold:

- access seekers can determine the fairness of prices negotiated under provisions of Section 21(1) of the Code;
- provisions of WNR's standard access agreement provides for specific

consultation mechanisms; the provision of information; and dispute resolution mechanisms which would allow access seekers to test the duty of fairness related to other than price issues in the provision of access.

*ii) Comments from the public consultation process*

- Fairness needs to be regularly demonstrated via the public release of prices (for major hauls by associate companies and for key routes) and performance indicators (service quality and efficiency). Relying solely on mechanisms of dispute resolution and Regulator price assessments is inadequate.
- An expressly stated commitment not to price discriminate between affiliated parties and others, as well as publication of access prices for major associated company hauls and other key routes, is required.
- The Regulator should approve all associate contracts with a focus on pricing at efficient cost for a defined service quality.
- WNR should complete any train scheduling and control services.

*iii) WNR's response*

- The obligation to act fairly in relation to the performance of access functions is imposed by Section 33 of the Act, individually upon each officer performing an access related function.
- A duty of fairness does not equate to an obligation to afford absolute equality of treatment. That is not the model adopted in the Act and Code, nor is it necessary under the Competition Principles Agreement.
- The role of Regulator is to ensure a fair process. It does not extend to regulating individually negotiated access contracts – that is the role of arbitration under the provisions of Part 3 Division 3 of the Code.
- There is no express provision in the Act or the Code requiring that all new agreements between the railway owner and persons other than the railway owner for use of the rail infrastructure must be made under the Code. There is no foundation for that implication to be drawn from the Act.
- It is clear that it was always contemplated that access agreements between two arms of a vertically or partly vertically integrated operation would not be covered by the Act and that it was nonetheless envisaged that a contestable market (which is merely a means to encourage the efficient use of and investment in railway facilities) would be achieved because of the following provisions:

- ◇ in the negotiation of access agreements, the railway owner must not unfairly discriminate between the proposed rail operations of a proponent and rail operations associated with the railway owner including, without limitation, in relation to the allocation of train paths, the management of train control and operating standards: Section 16(2) of the Code. "Rail operations of the railway owner", for the purposes of that section, includes the rail operations of an associate of the railway owner;
  - ◇ relevant officers of the railway owner, in performing their functions, 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: Section 33 of the Act;
  - ◇ the railway owner must not discriminate between one proponent and another: Section 16(1)(b) of the Code.
- The existence of costing principles and overpayment rules which are approved or determined by the Regulator provides further controls on price discrimination.
  - There is a misconception of the nature of services provided by AWR (and to a lesser extent ARG) to WNR and their impact upon WNR's access functions (differentiating its functions in providing access from things that it may have to do in providing access, such as complying with the Act and Code).

The only services provided by AWR to WNR are "operational" train scheduling services. Those services do not include:

- ◇ preparation of master train control diagram; or
- ◇ the alteration, on any basis, of any other party's scheduled train path.

Effectively, AWR's "operational" scheduling services are limited in their capacity to effect traffic upon the network to the scheduling of trains which AWR itself controls.

Such scheduling is undertaken only after an access agreement is put in place. Whether WNR used AWR or an external contractor, the question of confidentiality would exist and would need to be (and is) addressed by confidentiality terms in the agreement. WNR and AWR have existing contractual arrangements in relation to this service under which AWR has confidentiality obligations.

It is impractical to have operational scheduling conducted separately by AWR and a third party – there can be only one single point of scheduling for

self evident safety reasons.

In the event of a network emergency, WNR itself resumes control of scheduling and makes all decisions relevant to the rescheduling of train services. A party to whom access is provided under an access agreement is entitled to their scheduled train paths. That entitlement is defined by the access agreements negotiated by WNR, and planned by WNR. Any changes that AWR makes in relation to daily scheduling matters are passed to train control, which is under the control of WNR and WNR is responsible for resolving any scheduling conflicts. The Train Management Guidelines detail the procedures for this.

*iv) Regulator's views and comments*

- The common theme to ensuring fairness, as derived from public submissions, is that WNR and AWR be required to operate at arms length and on a competitively neutral basis from one another in that terms, prices and conditions should resemble those which would be negotiated between a third party and the railway owner.

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.

- Under the Code, the Regulator's responsibility is to approve for each route section the floor and ceiling costs based on efficient and lowest current costs, and if appropriate modern equivalent assets. For those seeking access under the Code, the access seeker and railway owner negotiate the price in between the floor and ceiling, but must take into account various costing principles as stipulated by Clause 13, Schedule 4 of the Code.

It should be noted that negotiations do not need to take place under the Code.

The Regulator will require WNR to inform access seekers of their rights to negotiate "inside" and "outside" of the access regime as part of Section 6 of the Code.

- As demonstrated by the comments received from the public consultation process, a major concern of stakeholders is the potential for WNR to provide favourable treatment to associated companies. In assessing whether preferential treatment has been provided, the Regulator has also noted the common view of stakeholders that the Regulator obtain and assess the accounts of any associated companies to WNR.

On this issue, the Regulator notes that no evidence has been provided to the Regulator to suggest that WNR is providing preferential treatment to associated companies. Furthermore, the Act only allows the Regulator to obtain information from the railway owner. In any event, the purpose of the segregation arrangements in this Determination is to prevent any potential for WNR to provide preferential treatment to associated companies.

The Act and Code provide the basis for establishing effective segregation arrangements. Under Section 21 of the Code access seekers can approach the Regulator to seek his views on whether the price offered by WNR is fair and reasonable. In providing this opinion the Regulator can benchmark the access prices offered by WNR with those offered elsewhere. These measures combined, in addition to this Determination, provide the basis for ensuring that WNR treats all access seekers on fair and reasonable terms.

It should be noted that arbitrators could also take into consideration access prices afforded to operators gaining access “outside” the access regime when resolving a dispute.

- In relation to releasing publicly the terms and conditions of any access agreement, the Regulator is limited in the type of information the Regulator can disclose by Section 50(3) of the Code. Nonetheless, it is the intention of the Regulator to monitor all contracts and this information may be used, when approached by an access seeker under Section 21 of the Code.
- Clause 13(c), Schedule 4 of the Code provides the limits on which WNR is allowed to price discriminate between various access seekers. Prices are to reflect as far as reasonably practicable the standards of the infrastructure concerned and the operations proposed to be carried on by the access seeker, the relevant market conditions and any other identified preference of the access seeker.
- In relation to key performance indicators (KPIs) these will be developed by the Regulator in consultation with WNR to assess and monitor the effectiveness of the segregation arrangements. The development of KPIs is being undertaken in a comprehensive manner across several Determinations (Segregation, Train Path Policy, Train Management Guidelines, Costing Principles) and will be finalised when these Determinations are completed. Details of the KPIs that the Regulator will use will be identified in a separate report. Where appropriate, this information will be released on the Regulator’s website.
- For the purpose of this Determination it is suffice to note that the KPIs that may be used include:
  - ◇ number of breaches referred by WNR to the Regulator;

- ◇ number of potential breaches referred by access seekers to the Regulator for assessment;
  - ◇ percentage of potential breaches referred by access seekers to the Regulator that are substantiated.
- Section 49 of the Code also allows the Regulator to inquire into the effectiveness of the Code and make recommendations to the Minister to that effect. While there is no indication of this at this time, if the Regulator considers that WNR is not working within the spirit of the Code then the Regulator can make appropriate recommendations to the Minister to address this inadequacy. This could take the form of recommending an amendment to the Act.
  - The Code does not allow the Regulator to approve or disapprove the negotiated outcome of an access seeker and railway owner. In any event the measures proposed in this response should ensure a “duty of fairness” within the arrangements.
  - 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.

Separation of accounts and records (Section 34 of the Act)*i) Summary of WNR's Proposal*

WNR has stated that it will maintain separate accounts and records with the accounting service to be provided by the accounting group within ARG.

The protection of the confidentiality of that information is established by:

- WNR having a designated accountant within ARG who performs no other accounting functions;
- The provisions as stated in Section 4 of the Proposal.

*ii) Comments from the public consultation process*

- The Regulator should specify a pro-forma template for reporting the railway owner's financial statements.
- The ARG overhead cost allocation method needs to be fair and transparent to prevent WNR being overloaded with excessive costs.

*iii) WNR's response*

- The treatment of information in relation to an access application is handled entirely outside the accounting system. Access application information is processed within the WNR access group and financial analysis is conducted (using information drawn from MIMS), wholly within that group by WNR personnel. WNR maintains an "access costing model" for that purpose. WNR's finance function (provided by ARG) becomes involved only once an access agreement is reached, and it is necessary to input budgets in relation to the provision of the access service, and establish an invoicing procedure.
- A different accountant at ARG will be responsible for WNR from that for AWR.

*iv) Regulator's views and comments*

- Under the Determination on costing principles, WNR will be required to develop regulatory accounts. Those accounts need to provide detailed accounting rules to ensure a fair separation of costs and revenues between WNR and the train operator. Access seekers can be assured that all information that is allowed to be publicly available will be presented in a format that is transparent.
- The intent of Section 34 of the Act is to prevent "cost shifting", ie. the attribution of costs from providing an unregulated service to a regulated



service to potentially deter entry by third parties due to higher than reasonable access prices. Consequently, it is noted that all stakeholders were keen to understand how WNR intended to allocate costs and structure their regulatory accounts to ensure that perceived or actual cost shifting does not occur. This issue will be dealt with in the Regulator's determination on costing principles.

- As indicated earlier, the ARG accountant provided to WNR should be employed by WNR.

### Compliance with segregation arrangements

#### *i) Summary of WNR's Proposal*

WNR believes compliance with its proposed segregation guidelines will be achieved in the following manner:

- WNR will instruct its internal auditors (currently outsourced to Ernst and Young) to conduct a compliance audit in relation to the segregation arrangements on an annual basis. This report will be submitted to the Regulator.
- WNR will report any breach of the segregation arrangements of which it becomes aware to the Regulator in writing within 5 business days.
- By access seekers or existing users approaching the Regulator at any time they consider a breach may have occurred. WNR states that the Act and Code provide wide powers for the Regulator to investigate any alleged breaches of the segregation arrangements.

#### *ii) Comments from the public consultation process*

- Regular independent compliance audits are essential. The auditor should be Regulator appointed and directed, but funded by WNR. Suggested frequency is at least annual. Additionally, the capability to complete special audits of alleged breaches is required.
- Regular compliance reporting by the railway owners to the Regulator is also essential. Suggested frequency is at least annual.
- Any potential or actual breaches should be notified to the Regulator within 5 business days.
- Third parties should be able to refer a suspected breach of the segregation arrangements to the Regulator for action.
- Breaches of segregation arrangements should be subject to a liquidated

damages clause in Confidentiality Deeds or the Access Agreement, with specific financial penalties to apply.

*iii) WNR's response*

- WNR proposes an internal compliance and audit function. Internal compliance is cost effective, integrated, and ensures “whole of organisation” review by a dedicated resource, on a regular basis. External compliance review, including “auditing”, has inevitable limitations due to the nature of the audit process and, at best, should be used to test a compliance system where an access seeker, or operator, makes a substantive and substantiated allegation of a failure of the compliance system. In those circumstances the Regulator has abundant power to intervene. Otherwise, external audit simply imposes an additional cost on access provision.
- WNR is of the view that there is no merit in a review period so short that it becomes, effectively, a continual review, and that 24 months is the minimum period between reviews. The Regulator has powers of intervention under Sections 29(2) and (3) which are more than sufficient to address any issues raised and which are supported by criminal sanctions.
- WNR submits that liquidated damages clauses are not reasonably necessary.
- A breach of an arrangement approved by the Regulator under Section 29 of the Act is a relatively serious criminal offence. To add a civil obligation onto conduct that Parliament has already characterised would be plainly inconsistent with the legislature’s stated intentions as to the remedies for any breach of the segregation arrangements.

*iv) Regulator's views and comments*

- The Regulator has a number of powers to monitor compliance by WNR with the segregation arrangements. Annual audit programs will be the key monitoring tool for assessing compliance.

To assess compliance with the segregation arrangements an independent external audit will be required. In this regard WNR will need to advise the Regulator who it intends to engage for the purpose of conducting the annual audit at the appropriate time.

- The annual independent audit may be supplemented by special audits, which would be commissioned following the identification of a material complaint. The audit program would ensure that there is, among others, a continued fair separation of costs and revenues between WNR and associated train operator. This is essential to ensuring the effectiveness of

the segregation arrangements.

- The Regulator will require the creation of a WNR Compliance Manual detailing the appropriate segregation arrangements, including the types of behaviour which breach segregation requirements and the appropriate corrective action for each breach and notification procedure.
- Consistent with WNR's view, any breaches of the segregation arrangements should be reported to the Regulator within 5 business days. Under Section 21 of the Act, WNR is required to respond to written directions from the Regulator within a timeframe specified by the Regulator. The Regulator would use this power to obtain, where warranted, additional information on the breach and the reasons for that breach. If the need arises, the Regulator could use that information to instruct WNR of a need for a special audit to take place.
- With regards to liquidated damages, third parties should be able to refer a suspected breach of the segregation arrangements to the Regulator for action. If upon assessment the Regulator believes that there is a need to incorporate extra provisions in the segregation arrangements the Regulator is able to instruct WNR to do so under Section 29(3) of the Act. It should also be noted that breaches of the segregation arrangements attract a penalty of \$100,000 under Section 29(4) of the Act.

#### Other measures (Section 30 of the Act)

##### *i) Summary of WNR's Proposal*

WNR is of the view that the only segregation arrangements that they need to comply with relate to Sections 31 to 34 of the Act.

##### *ii) Comments from the public consultation process*

- a) Regulator approval of any organisational change that may affect segregation arrangements be required prior to its implementation.
- b) Arrangements should place an obligation on railway owners to provide adequate training on segregation and for monitoring of compliance with these arrangements.
- c) The Standard Access Agreement should be amended to require compliance with all segregation arrangements.
- d) Appointment of a Ring-fencing Compliance Officer to review and promote compliance.
- e) There be a procedure for dealing with access proposals, which establishes a

detailed queuing policy to prevent any access party receiving inappropriate priority in dealing with its access proposal.

- f) The details of access arrangements entered into by WNR prior to the proclamation of the Code be provided and made publicly available.

*iii) Regulator's views and comments*

Section 30 of the Act allows the Regulator to place other segregation arrangements upon railway owners, arrangements that are not covered by Sections 31 to 34 of the Act. The following are the Regulator's views on the additional matters raised in the public consultation process:

- a) The effectiveness of organisational changes and their impact on the segregation arrangements will be covered in the annual audit. In addition, WNR has proposed to provide the Regulator with details of breaches in the segregation arrangements within five working days. Presumably, if an organisational change has adversely impacted upon the effectiveness of the segregation arrangements this would be brought to the Regulator's attention prior to the annual review.
- b) WNR's staff, particularly those covered by confidentiality deeds, should be trained in their segregation obligations, including the protection of confidential information.
- c) The Segregation Determination is a stand-alone document that provides the conditions that apply to WNR. These requirements apply independently of an access agreement. Any breach of segregation conditions, such as WNR disclosing confidential information, may result in a penalty being applied.
- d) The responsibility to review, report on and promote compliance with segregation arrangements rests with WNR. It is not necessary for the Regulator to determine whether an officer with responsibility for ring-fencing issues within WNR is required.
- e) Section 9 of the Code requires the railway owner to respond to an access seeker, within specified timeframes, on their access proposal. In this regard the need for a queuing policy is questionable.

The issue is how an access seeker can obtain the train path suitable to its needs and this is being addressed in the Train Paths Policy Determination.

- f) The details of access arrangements entered into by WNR prior to and after the proclamation of the Code is confidential and Section 50(3) of the Code limits the Regulator's ability to disclose information that is confidential without the consent of each person to whom the protection of confidentiality

belongs.

As stated previously access seekers can approach the Regulator to ask whether the access price provided to them by WNR is fair and reasonable. In providing that assessment, the Regulator will take into account the terms and conditions offered in the various access agreements that WNR has with other access seekers.

## 5. Required amendments

The assessment in this Determination has been limited to Section 10.3 of the WNR submission "Segregation Arrangements to be adopted". The refinements and additions that are being sought to WNR's Proposal have accordingly been directed to that section of the submission.

In subsequent discussions, WNR has agreed to implement a number of the suggested changes detailed below. Even so, these required amendments are provided in full in the following table so that stakeholders can gauge the changes that are being required of WNR on its segregation submission as lodged with the Regulator in November 2001.

It is the view of the Regulator that the required amendments below appropriately address and balances the differing needs of WNR, access seekers and the community under Section 20(4) of the Act. In addition, the required amendments detailed below have also taken into account the issues to be considered by the Regulator under Section 41(b) of the Code, being:

- the comments derived from public submissions;
- the "public interest" as determined by the Regulator;
- any other issues that the Regulator considers to be relevant.

The adoption of these required amendments in the segregation arrangements should ensure the effectiveness of the State's access regime, in addition to meeting the requirements of Section 20(4) of the Act and Section 41(b) of the Code.

WNR's proposed segregation arrangements	Changes required to WNR's segregation arrangements
<p><b>Part 1</b></p> <p><b>Legislative context</b></p> <p>WestNet Rail Pty Ltd ("WestNet") is the "owner" as defined in the Railways (Access) Act 1998 ("Act") of a rail network in Western Australia which is subject to the provisions of the Act to the extent that the network is defined in Schedule 1 of the</p>	<p><b>Part 1</b></p> <p>Within the opening section the following is required:</p> <ul style="list-style-type: none"> <li>▪ A clear and concise statement of the objective of the segregation arrangements.</li> </ul>

WNR's proposed segregation arrangements	Changes required to WNR's segregation arrangements
<p>Railways (Access) Code 2000 ("Code") which is established under the Act. WestNet Rail recognises its obligation to comply with the Act and the Code and specifically Sections 28 and Sections 31 to 34 of the Act.</p>	<ul style="list-style-type: none"> <li>▪ A summary of the over arching principles on how WNR will segregate its access-related functions from its other functions.</li> <li>▪ A section containing definitions of all key terms (or in Part 2).</li> </ul>
<p><b>Part 2</b></p> <p><b>Segregation of Access Functions</b></p> <p>WestNet defines Access Related Functions as;</p> <p>(i) negotiation of Access Agreements (either under the Regime or on a commercial basis) and granting of access rights;</p> <p>(ii) management of Access Agreements including performance monitoring and day to day operation issues;</p> <p>(iii) the collection; use, and dissemination of train running data including manifest details; and access usage.</p> <p>(iv) train scheduling train path allocation, publication of working timetables, control planning; and the granting of ad-hoc train path entitlements.</p> <p>(v) train control which includes provision of appropriate authorities for trains to use scheduled train paths (train orders or signals); real-time management of trains.</p> <p>(vi) emergency management of the network including co-ordination of emergency service responses</p> <p>(vii) development, maintenance and monitoring compliance with appropriate safety standards for WestNet staff, its contractors and operators on the Network</p> <p>(viii) development and authorisation of the WestNet's Rules (including the General Appendix and Working Timetables) and the issue of special notices, instructions and warnings related to the rules.</p> <p>(ix) the development of train operating standards (to the extent they relate to the infrastructure) such as maximum braking distances, maximum train lengths etc., and also the maintenance standards for the infrastructure itself.</p> <p>(x) the maintenance of the track and infrastructure including signalling and communications maintenance.</p>	<p><b>Part 2</b></p> <ul style="list-style-type: none"> <li>▪ Specifically mention the other parts of the Code that such Access Functions apply to, ie. costing principles, overpayment rules, calculating floor and ceiling costs and Regulator approval of costs.</li> <li>▪ Terms within Access Related Functions also need definitions eg. Contractor, Working Timetable, Ultimate Control, WNR Rules.</li> <li>▪ Include "ensure suitable controls, measures and procedures are established to provide an effective system of segregation" as an Access Related Function.</li> </ul>

WNR's proposed segregation arrangements	Changes required to WNR's segregation arrangements
<p>Where WestNet engages contractors or other parties to provide any part of the access related functions it will;</p> <p>(a) retain ultimate control of the function by establishing contractual arrangements; and</p> <p>(b) ensure that any contractor is aware and complies with any obligations imposed by the Act or the Code.</p>	
<p><b>Part 3</b></p> <p><b>Confidential Information</b></p> <p>WestNet Rail has established a regime of Confidential Information as defined in the Code including;</p> <p>(a) a system of written record keeping that only allows appropriate WestNet staff to access the records;</p> <p>(b) a security system on electronic records that only allows appropriate WestNet staff to access the records;</p> <p>(c) appropriate controls on data, including information in the Rail Access Management System (RAMS) and costing and pricing information to protect confidential information.</p> <p>(d) specific provisions in each access agreement providing contractual obligations on WestNet to protect confidential information.</p> <p>WestNet Rail is required to provide management reports to both its own Boards of directors and to officers and members of the Board of its parent company, the Australian Railroad Group (ARG). With respect to such management information;</p> <p>(i) reports to management of ARG are dealt with only in meetings where WestNet and ARG management are present and no representatives of related entities operating train services, such as AWR, are present.</p> <p>(ii) Members of the WestNet Board are not members of the AWR Board;</p> <p>(iii) Where confidential information is provided from the WestNet Board to either ARG Management or the ARG Board it will be clearly identified.</p> <p>WestNet confirms it will keep information it receives in relation to access related matters</p>	<p><b>Part 3</b></p> <p>The following changes are required:</p> <ul style="list-style-type: none"> <li>▪ This section to provide further detail on WNR's system and procedures for "safeguarding Confidential Information", including the physical location of staff.</li> <li>▪ 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: <ul style="list-style-type: none"> <li><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> <ul style="list-style-type: none"> <li>- <i>Is not already in the public domain;</i></li> <li>- <i>Does not become available to the public through means other than a breach of confidentiality;</i></li> <li>- <i>Was not in the other party's lawful possession prior to such disclosure;</i></li> <li>- <i>Is not received by the other party independently from a third party free to disclose such information."</i></li> </ul> </li> </ul> </li> <li>▪ In relation to (a), hard copy Confidential Information should be catalogued and contained in a central secure registry that additionally is housed in a secured part of the building. Greater detail on the proposed system needs to be inserted; eg. staff should sign-in and sign-out this information each time it is utilised.</li> <li>▪ In relation to (b), greater detail on the proposed security system for electronic</li> </ul>

WNR's proposed segregation arrangements	Changes required to WNR's segregation arrangements
<p>confidential in accordance with the Arrangements as set out herein.</p> <p>Where an employee of WestNet has prescribed duties which are managing or conducting access related functions, the following procedure will apply. WestNet will at the time of their permanent or temporary appointment, require the employee to sign a statement that they are aware of their responsibilities and obligations under the Code and specifically as it relates to confidential information as defined in the Code and in these Arrangements.</p> <p>This process will be conducted on an annual basis in conjunction with a compliance audit.</p>	<p>records needs to be inserted.</p> <ul style="list-style-type: none"> <li>▪ In relation to (c), greater detail specifying the exact nature of the "appropriate controls" on data systems (eg. RAS and RAMS) and costs/price information is required.</li> <li>▪ In relation to (a) and (b), list the position titles of all WNR staff, including contractors (ie the "appropriate WNR staff") who will handle confidential information and prohibit any other staff from accessing it. Individuals on this list are to be covered by confidentiality deeds.</li> <li>▪ ARG financial and accounting staff solely dedicated to WNR should become WNR employees.</li> <li>▪ Specify the nature of the contents of management reports on WNR given to ARG management and directors. WNR must detail the procedures it will follow for the protection of confidential information, particularly the name of the access seeker and preferred train operator, while allowing the ARG Board to carry out its statutory duties.</li> <li>▪ Provide a procedure for briefing the CEO of ARG (outside of Board meetings) in relation to the access proposals of third parties and the level of detail provided.</li> </ul>
<p><b>Part 4</b></p> <p><b>Conflicts of Interest</b></p> <p>Because of the separation of access related functions WestNet Rail believes that there are no existing conflicts of interest.</p> <p>In the event that any staff are rotated within ARG, especially the related entity AWR, to perform Access Related Functions within WestNet, WestNet would ensure the personnel:</p> <p>a) did not have access to confidential information;</p> <p>b) were familiarised with the requirements of the Code; and</p> <p>c) were appropriately supervised in the event a conflict of interest were to arise</p>	<p><b>Part 4</b></p> <ul style="list-style-type: none"> <li>▪ Modify opening sentence to provide a commitment from WNR to ensure no conflicts of interest exist.</li> <li>▪ WNR is required to complete internally (or via a non-ARG entity) all train control and scheduling functions.</li> <li>▪ Staff is precluded from being shared between (or working for both) WNR and AWR on those jobs covered by a confidentiality deed. The only exception is in the case of emergencies. However, whenever these instances arise the Regulator is to be informed accordingly. WNR to specify the conditions which constitute an emergency in this regard.</li> <li>▪ An amendment be made to preclude other staff of associated companies being rotated into those WNR positions relating to access and dealing with confidential information.</li> </ul>



WNR's proposed segregation arrangements	Changes required to WNR's segregation arrangements
<p><b>Part 5</b></p> <p><b>Duty of Fairness</b></p> <p>WestNet acknowledges and accepts it has a duty of fairness to access seekers relative to its treatment of other access seekers under the Code; and others granted access under other arrangements.</p> <p>The mechanism for ensuring the duty of fairness is two-fold:</p> <ol style="list-style-type: none"> <li>1. access seekers can determine the fairness of prices negotiated under provisions of Section 21(l) of the Code; and</li> <li>2. provisions of WestNet's standard access agreement provides for specific consultation mechanisms; the provision of information; and dispute resolution mechanisms which would allow access seekers to test the duty of fairness related to other than price issues in the provision of access.</li> </ol>	<p><b>Part 5</b></p> <ul style="list-style-type: none"> <li>▪ 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.</li> <li>▪ Addition to the proposed two-fold mechanisms, pro-active mechanisms should be established to reinforce the duty of fairness for third parties, such as: <ul style="list-style-type: none"> <li>- A commitment that the key terms and conditions of internal access agreements for all existing services will be broadly comparable to those provided to or offered to third parties.</li> <li>- Key performance indicators, (ie. service quality, cost efficiency, etc) which indicate the effectiveness of segregation arrangements to be developed by the Regulator in consultation with WNR.</li> <li>- WNR should refer to Part 5 of the Code on its commitment to train management guidelines, statement of policy, costing principles and over-payment rules.</li> </ul> </li> <li>▪ As part of Section 6 of the Code, inform access seekers of their rights to confidentiality when negotiating inside and outside the access regime, together with a protocol for access seekers who "move" from negotiating outside the access regime to under the regime.</li> </ul>
<p><b>Part 6</b></p> <p><b>Separation of Accounts and Records</b></p> <p>WestNet will maintain separate accounts and records with the accounting service to be provided by the accounting group within ARG.</p> <p>The protection of the confidentiality of that information is established by:</p> <ol style="list-style-type: none"> <li>1. WestNet having a designated Accountant within ARG who performs no other accounting functions;</li> <li>2. The provisions of section 4 of these Guidelines.</li> </ol>	<p><b>Part 6</b></p> <ul style="list-style-type: none"> <li>▪ WNR must commit to being broadly self-sufficient for finance but, for example, can share payroll and human resource functions. WNR's designated accountant within ARG should be employed by WNR. The accountant should also be located within and report to WNR.</li> </ul> <p>Part 6 should also contain a commitment to:</p> <ul style="list-style-type: none"> <li>▪ Present the regulatory accounts in a Regulator</li> </ul>

WNR's proposed segregation arrangements	Changes required to WNR's segregation arrangements
	<p>approved format.</p> <ul style="list-style-type: none"> <li>▪ Specify which other related access records such as access billing or train path planning documentation needs to be held separately and protection measures for such records.</li> <li>▪ Reference the need to comply with the equitable and reasonable cost allocation system as defined in the Costing Principles approved by the Regulator.</li> </ul>
<p><b>Part 7</b></p> <p><b>Compliance with these principles</b></p> <p>Compliance with these guidelines will be achieved by:</p> <p>WestNet will instruct its internal auditors (currently outsourced to Ernst and Young) to conduct a compliance audit in relation to the segregation arrangements on an annual basis. This report will be submitted to the Regulator.</p> <p>WestNet will report any breach of the segregation arrangements of which it becomes aware to the Regulator in writing within 5 business days.</p> <p>Access seekers or existing users can approach the Regulator at any time they consider a breach may have occurred. The Act and Code provide wide powers for the Regulator to investigate any alleged breaches of the segregation arrangements.</p>	<p><b>Part 7</b></p> <p>The following should also be included in Part 7 of WNR's document:</p> <ul style="list-style-type: none"> <li>▪ A separate detailed annual independent audit of compliance with other aspects of the Segregation Guidelines on a negative assurance basis. The Regulator may select and manage the auditor with costs paid by WNR.</li> <li>▪ A statement pointing out the Regulator's ability to commission special audits on any issue or area where additional assurance is sought.</li> <li>▪ The provision of an annual Compliance Report detailing a Compliance Plan with specific procedures for ensuring segregation arrangement compliance and measures for monitoring compliance. This report will also detail all instances of non-compliance and rectification strategies.</li> <li>▪ The creation of a Compliance Manual detailing the appropriate segregation arrangements, including the types of behaviour which breach segregation requirements and the appropriate corrective action for each breach and notification procedure.</li> <li>▪ Staff training in segregation be undertaken through the Compliance Manual, particularly those staff covered by confidentiality deeds.</li> </ul>

Under the Act and Code, the Regulator can modify the segregation arrangements at any time. While it may be possible to commence with a relatively simple segregation system and implement refinements over time if the need arises, establishing effective segregation for vertically integrated entities is considered an important pre-requisite

for a fair system of third party access. Every endeavour has been made to establish such a system.

It is recognised that the additional requirements identified in this Determination may add to the compliance costs for WNR but on balance these changes are considered necessary so as to ensure effective segregation arrangements are put in place for WNR. Indeed, the Regulator notes that most submissions considered the increase in compliance costs would be offset by the higher benefits attained from having effective segregation arrangements in place.

## **6. Determination**

The proposed segregation arrangements submitted by WNR dated November 2001 are not approved. WNR will be required to make the amendments as tabled in section 5 of this Determination and resubmit them for the Regulator's consideration within 30 days of the receipt of the Determination. The Regulator notes that in the event that agreement is not reached on the required amendments, the Regulator may give directions in writing to effect the necessary changes under Section 29(3) of the Act.

Ken Michael

**ACTING RAIL ACCESS REGULATOR**

24 April 2002

**Appendix 1 – Submissions received from the public consultation process**

1. Alcoa World Alumina Australia
2. Australian Rail Track Corporation Ltd
3. Australian Western Railroads
4. AWB Limited
5. Chamber of Commerce and Industry Western Australia
6. Freight Corp
7. Grain Pool of Western Australia
8. Portman Iron Ore
9. WMC Resources Limited
10. Worsley Alumina