

Our ref: MCR-18-542

Professor Flavio Menezes
Queensland Competition Authority
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Dear Professor Menezes

Declaration Review

Queensland Rail welcomes the opportunity to make a submission to the Queensland Competition Authority (QCA) in relation to its review into whether the declared services specified in section 250 of the Queensland Competition Authority Act 1997 (Qld) (**QCA Act**) should remain declared in whole or in part following the expiry of the existing declarations on 8 September 2020.

This letter provides background to Queensland Rail and its systems and services, and outlines the reasons why in Queensland Rail's view the services provided by Queensland Rail do not meet the access criteria in the QCA Act. The QCA staff issues paper titled *Declaration reviews: applying the access criteria* of April 2018 (**QCA Issues Paper**) is referenced where relevant below.

Overview

1. This review is the first opportunity the QCA has had to consider whether the services provided by Queensland Rail ought to be declared for the purposes of the access regime established by the QCA Act. Since the time the services specified in section 250 of the QCA Act were first declared by regulation in 1998, there have been significant and fundamental changes to the rail industry, both in terms of ownership and management of assets and above rail operations, and increasingly intense competition in the provision of freight transportation services from road operators.
2. Queensland Rail is no longer a vertically integrated service provider of rail transport services as its predecessor was at the time the services were first declared by regulation. While Queensland Rail continues to provide below rail services and some passenger services, Queensland Rail does not provide above rail freight services and the passenger services provided by Queensland Rail are governed by Queensland legislation and Queensland Rail's obligations to Government under the Rail Transport Service Contract entered into between the State of Queensland and Queensland Rail Limited on 20 July 2015 (**TSC**). Queensland Rail is thus no longer vertically integrated in a way that gives it an ability or incentive to control its rail systems to limit effective competition in dependent markets.
3. Further, Queensland Rail is materially constrained in the provision of below rail services to freight operators. Most significantly, for all freight other than some bulk commodities being transported over long distances, Queensland Rail faces intense and increasing competition from road operators. Road transportation offers an effective substitute service to rail, which has a significant and direct downward impact on the prices that Queensland Rail negotiates with access seekers.
4. In recognition of the competitive environment in which Queensland Rail operates, Queensland Rail receives transport service payments from the Queensland Government. With the exception only of the Mount Isa Line, each of Queensland Rail's rail systems (as well as each of its passenger operations) are supported by, and are commercially viable only because Queensland Rail receives, these subsidies. In 2016-17, the transport service payments amounted to almost \$1.6 billion, or almost 85 per cent of total Queensland Rail's revenue.
5. It is against this background that the QCA is considering whether to recommend declaration of Queensland Rail's services. The QCA can only recommend declaration of a service if it is affirmatively satisfied about all of the access criteria set out in the QCA Act. In light of the transformation of the rail industry since 1998, in Queensland Rail's opinion, the services provided by Queensland Rail do not meet all four of the declaration criteria and form the view that the services provided by Queensland Rail should not be declared.

Queensland Rail's network

6. Queensland Rail's rail network extends more than 6600 kilometres across Queensland and is used by freight and passenger trains. The network comprises seven regional systems and the Metropolitan System (being the system used to provide metropolitan passenger train services in Brisbane).¹ The condition, utilisation and performance of each of Queensland Rail's systems varies greatly due to differing supply chain dynamics, rail corridor characteristics and interactions with other rail traffics, in addition to their discrete geographic locations.
7. A map of the systems making up Queensland Rail's network is **attached**. Further details of each of Queensland Rail's systems are set out in the information packs for each system available on Queensland Rail's website.²
8. The most significant volumes of freight are carried on the West Moreton System (thermal coal), the Mount Isa Line (metals, minerals concentrate and chemicals) and the North Coast Line (intermodal freight and sugar). These three systems carried approximately 97 per cent of the freight tonnage transported on Queensland Rail's network in 2016-17.³
9. The key passenger operations on Queensland Rail's systems are:
 - (a) the Citytrain service on the Metropolitan System; and
 - (b) long distance passenger services on the North Coast Line.
10. Regular passenger and tourist services operate on the Mount Isa Line, West Moreton System, Western System, Central Western System and the Tablelands System, and a small number of infrequent or ad hoc heritage tourist services operate on various short segments of the network.
11. Access to Queensland Rail's network is subject to the QCA approved 2016 Access Undertaking. The 2016 Access Undertaking is effective until 30 June 2020.⁴
12. A number of access agreements have been entered into under the 2016 Access Undertaking and preceding access undertakings. The access arrangements entered into are specific to the purpose for which access is sought (for example, the transportation of general freight, transportation of coal, transportation of sugar, transportation of passengers). With limited exceptions, the access agreements relate to a single system (and, more specifically, a specified origin and destination points within that system).⁵
13. In 2016-17, Queensland Rail received access revenue of over \$160 million, approximately 8.7 per cent of total revenue. Queensland Rail receives substantial subsidies in order to maintain and invest in its network through the TSC.

The access criteria

14. The access criteria are as follows:⁶
 - (a) that access (or increased access) to the service, on reasonable terms and conditions, as a result of a declaration of the service would promote a material increase in competition in at least 1 market (whether or not in Australia), other than the market for the service;
 - (b) that the facility for the service could meet the total foreseeable demand in the market—
 - (i) over the period for which the service would be declared; and
 - (ii) at the least cost compared to any 2 or more facilities (which could include the facility for the service);
 - (c) that the facility for the service is significant, having regard to its size or its importance to the Queensland economy;
 - (d) that access (or increased access) to the service, on reasonable terms and conditions, as a result of a declaration of the service would promote the public interest.

¹ The Maryborough Area is treated as part of the North Coast Line

² <https://www.queenslandrail.com.au/>.

³ North Coast Line traffic that originates on the Metropolitan System is treated as originating on the North Coast Line

⁴ 2016 Access Undertaking, clauses 1.1 and 7.1

⁵ The primary exceptions include access agreements for the purposes of providing maintenance (which relate to all systems) and access agreements relating to the North Coast Line, West Moreton System, Western and South Western Systems where trains need to traverse the Metropolitan System (for example, to reach the Port of Brisbane).

⁶ Section 76 of the QCA Act

15. The access criteria in the QCA Act are intended to reflect those contained in the national access regime established by Part IIIA of the *Competition and Consumer Act 2010 (Cth)* (CCA). They were most recently amended in March 2018, in order to reflect the recent amendments to the CCA following the Productivity Commission's Inquiry into the National Access Regime of October 2013.
16. The access criteria, and the application of the criteria to the services provided by Queensland Rail, are described in turn below.

Definition of services

17. Each of the services provided by Queensland Rail entails the use of the rail transport infrastructure for providing transportation by rail on part of its network.
18. Queensland Rail provides eight services, being the use of the following eight facilities:
 - (a) the Mount Isa Line, being that part of the network bounded to the east by (and including) Stuart and to the west by (and including) Mount Isa and including all branch lines comprised in that part of the network;
 - (b) the North Coast Line, being those parts of the network bounded to south by (and including) Nambour station, to the north by (and including) Cairns and to the west by (but excluding) Stuart and including all branch lines, including those in the Maryborough area and Taragoala to Graham, comprised in that part of the network;
 - (c) the West Moreton System, means that part of the network comprising the rail corridor from (and including) Rosewood to Miles, and including the Meandarra branch line;
 - (d) the Western System, being those parts of the network bounded to the east by (and including) Miles and to the west by (and including) Quilpie and including all branch lines comprised in that part of the network, but excluding those parts of the network that are part of the West Moreton System;
 - (e) the South Western System, being that part of the network bounded to the west by (and including) Thallon, to the north by (and including) Toowoomba and to the south by (and including) Wallangarra and including all branch lines comprised in that part of the network including Wyreema to Millmerran branchline;
 - (f) the Central Western System, being that part of the network bounded to the east by (and including) Nogoia, to the north by (and including) Clermont and to the west by (and including) Winton and including all branch lines comprised in that part of the network;
 - (g) the Tablelands System, being those parts of the network bounded to the west by (and including) Normanton and to the east by (and including) Cairns and including all branch lines comprised in those parts of the network; and
 - (h) the Metropolitan System, being that part of the network bounded to the north by (and including) Nambour station and to the west by (and including) Rosewood and including all branch lines comprised in that part of the network.
19. Given the distinct nature of the rail systems managed by Queensland Rail, it is appropriate that any assessment against the access criteria of whether or not to declare the service, or part of the service, be performed on a rail system by rail system basis.

Criterion (a)

20. In order to recommend that the deemed declared service (or part of the service) be declared, the QCA must be positively satisfied that access (or increased access) to the service, on reasonable terms and conditions, as a result of a declaration of the service would promote a material increase in competition in at least one market (whether or not in Australia), other than the market for the service.
21. An assessment of whether criterion (a) is satisfied typically involves the following two steps:
 - (a) Identifying the relevant upstream and downstream dependent markets, which are separate from the market for the service in respect of which declaration is being considered.
 - (b) Assessing whether access (or increased access) to the service as a result of declaration will promote a material increase in competition in a dependent market. This involves a comparison of a future scenario in which the service is declared against a future in which there is no declaration.

22. Queensland Rail therefore respectfully does not agree with the preliminary view expressed in the QCA Issues Paper that the relevant inquiry under criterion (a) is whether declaration would 'promote a materially more competitive environment'.⁷ Such a threshold is too low and is contrary to the stated legislative intention of increasing the threshold to ensure that declarations are only sought when increases in competition are not trivial in amending criterion (a). Further, the interpretation is based on the Tribunal's decision in *Sydney International Airport* [2000] ACompT 1,⁸ whereas the Tribunal in that decision was interpreting criterion (a) as it then was (i.e. an inquiry into whether declaration would 'promote competition'), and not criterion (a) in its current form (which requires an inquiry into whether declaration would 'promote a material increase in competition'). While the Tribunal rejected the notion that 'promoting competition' requires an increase in competition,⁹ this is precisely what is required having regard to the words of criterion (a) in its current form.
23. Queensland Rail also observes that, in discussing criterion (a), the QCA Issues Paper cites a guide to declaration by the NCC published in August 2009. This guide is no longer current. The NCC's current guide to declaration (published in April 2018) reflects the wording of the current provision in summarising its approach to criterion (a). That is, the guide states that the NCC 'assesses whether the access (or increased access) resulting from the declaration would promote a material increase in competition in any of the dependent markets'.
24. The requirement that declaration promote a 'material increase' in competition thus requires that, in order to recommend declaration, the QCA must be affirmatively satisfied that declaration would promote a significant and non-trivial increase in competition.
25. Criterion (a) is not satisfied in relation to any part of Queensland Rail's deemed declared service. In summary, this is because:
- (a) Queensland Rail does not have the ability or incentive to exercise market power to adversely affect competition in any dependent market:
- (i) Even without addressing each of the constraints on Queensland Rail, it is evident that Queensland Rail does not have the ability or incentive to use any market power to adversely affect competition in a dependent market. In particular, and with the exception of the West Moreton System where reference tariffs currently apply, the prices for access currently charged by Queensland Rail on its systems result in revenues well below the ceiling imposed by the 2016 Access Undertaking, and near to the floor. In addition, each of Queensland Rail's systems (with the exception only of the Mount Isa Line) are supported by, and are commercially viable only because Queensland Rail receives, transport service payments under the TSC with the State of Queensland.
- (ii) In the future without declaration, Queensland Rail would be materially constrained in the provision of below rail services for the purposes of transporting freight by:
- a. Strong competition from road operators, which provide a closely substitutable service in respect of the transportation of freight, other than some bulk commodities being transported over long distances. Parties requiring freight transportation services can readily shift to moving freight by road in the event of an increase in access price and/or decline in quality of service provided.
- b. Customers' ability to pay, which constrains the access prices that can be imposed by Queensland Rail, including for the purposes of transporting bulk commodities.
- c. Queensland Rail's statutory obligations and position as a statutory authority, including obligations to have approved and comply with strategic and operational plans, as well as its obligations under the TSC.
- d. Queensland Rail's incentives to maximise demand for its below rail services due to significant spare capacity on its systems.
- e. The fact that Queensland Rail is not vertically integrated in a relevant respect.
- f. The threat of regulation or declaration under Parts 3 or 5 of the QCA Act.
- g. The passenger services provided by Queensland Rail are heavily regulated, including in relation to scheduling and pricing.

⁷ QCA Issues Paper, page 19 (section 4.3, paragraph (c)). See also page 18 (section 4.2).

⁸ QCA Issues Paper, page 18 (section 4.2)

⁹ *Sydney International Airport* [2000] ACompT 1 and [106]

26. Further, and in any event, in response to the impending expiry of the declaration of its services, Queensland Rail will put in place a binding and enforceable framework under which it will provide access, for the purposes of both freight and passenger rail services, which will provide certainty for customers, competitive pricing and aim to promote more freight on rail.
27. The Access Framework and Standard Access Agreement will be based on the 2016 Access Undertaking and provide as much regulatory certainty for access seekers and access holders as currently exists. The fit for purpose Access Framework will retain each of the key features of the 2016 Access Undertaking, with amendments made primarily to allow for administrative or process changes to improve efficiency for access seekers, access holders and Queensland Rail. The Access Framework will ensure access to the services provided by Queensland Rail on reasonable terms and conditions even if the services are not declared in future.
28. Finally, key relevant dependent markets are effectively competitive, and would be with and without declaration. It is well established that if a dependent market is effectively competitive, improved access is unlikely to promote a material increase in competition.
29. Further, Queensland Rail agrees with the views expressed in the QCA Issues Paper that, in considering whether access criterion (a) is met, the QCA is required to take into account any mechanisms, contracts or arrangements that impact on access to Queensland Rail's services. That is, there may be other mechanisms, contracts or arrangements that affect a regulated entity's ability and/or incentive to exercise market power to affect competition in a dependent market in the absence of declaration.
30. As highlighted in the QCA Issues Paper, access arrangements negotiated under the 2016 Access Undertaking that will remain in effect after the expiry of the declaration are one example of arrangements that should be taken into account.
31. The second matter relevant to consider in assessing the effects of declaration on competition is the range of possible outcomes resulting from a material increase in competition in dependent markets and whether these outcomes are likely.
32. It is well established that if a dependent market is already workably or effectively competitive, improved access is unlikely to promote a material increase in competition and declaration of the service is therefore unlikely to satisfy criterion (a).

Criterion (b)

33. Access criterion (b) requires the QCA to be satisfied that each of the rail systems managed by Queensland Rail could meet the total foreseeable demand in a market that encompasses the relevant rail service over the period for which the service would be declared and at the least cost compared to any two or more facilities (which could include the relevant rail system).
34. The need to determine whether each of the facilities could meet total foreseeable demand in the market, means that the QCA will have to identify the scope of the markets in which each of the rail services is provided.
35. The key issue in market definition for each of the rail services will be the potential for substitution by access seekers – or the users of services provided by access seekers – between the relevant service and other services. In particular, the QCA will need to determine whether the product dimension of the market for the relevant services includes road haulage services. As discussed above, road is a practical and commercial alternative to rail transport for all but the transportation of some bulk commodities over long distances.
36. The QCA will have to identify total foreseeable demand in the market that encompasses the services provided by each of the distinct rail facilities over the declaration period.
37. Queensland Rail's rail infrastructure is used by above rail service providers. However, demand for Queensland Rail's rail infrastructure by those rail service providers is itself derived from those wishing to move freight or passengers between various points along a rail system.
38. As the QCA recognises in the QCA Issues Paper, criterion (b) involves a consideration of how resources can be allocated in meeting demand optimally from a social economic welfare perspective, rather than whether it is in the private commercial interests of an entity to meet demand in an inefficient way.

Criterion (c)

39. In the QCA Issues Paper, the QCA requested that Queensland Rail (and stakeholders) advise whether they agree with the QCA's interpretation of criterion (c) and assist the QCA with its declaration review by applying this criteria to inform the QCA's assessment of whether the currently declared services provided by each facility satisfy all of the declaration criteria.
40. The test to be applied in relation to criterion (c) is an economic and legal test. The objects clause of Part 5 of the QCA Act provides that the regime is directed towards the 'economically efficient operation of, use of and investment in, significant infrastructure by which services are provided, with the effect of promoting effective competition in upstream and downstream markets (emphasis added).'
41. It is critical that the economic significance is not conflated with cultural, historical or societal significance when applying criterion (c). Many of Queensland Rail's lines have undoubted importance from a heritage, regional, societal and/or cultural perspective. However, this is not a relevant consideration when applying criterion (c). To name one example, the track, bridges and tunnels of the Tablelands System preserve significant heritage, and this cultural significance is in no way diminished by arguing that the Tablelands System is not of economic significance for the purposes of criterion (c), as the test in relation to the declaration is a legal and economic test.
42. Further, it is important to note that the vast majority of infrastructure assets in Queensland are not declared facilities under the QCA Act. For example, all of Queensland's ports excluding the Dalrymple Bay Coal Terminal are not declared and there is no doubt as to the significance of these facilities to the Queensland economy. Put another way, an 'undeclared' status in no way diminishes the importance of these facilities, and this background is critical in understanding the intentionally rigorous threshold for a facility to be declared under Part 5 of the QCA Act. For context and to emphasise that not being declared in no way diminishes the significance of the infrastructure, please refer to the table below for some examples of Queensland infrastructure assets that are not declared.

Significant Queensland infrastructure that is <u>not</u> declared under Part 5 of the QCA Act	
Port infrastructure	Port of Brisbane, Port of Townsville, Gladstone Ports, Ports North, North Queensland Bulk Ports
Airports	No airports are declared under the QCA Act

43. Queensland Rail submits that the Metropolitan System, Mount Isa Line and North Coast Line are rail systems of sufficient 'size' and/or of sufficient 'importance to the Queensland economy' to satisfy criterion (c).
44. Each of the West Moreton System, the Western System, the South Western System, the Central Western System and the Tablelands System are facilities of insufficient 'size' and insufficient 'importance to the Queensland economy' for the QCA to be satisfied that any of these lines satisfy criterion (c).
45. However, the West Moreton System, Western System, South Western System, Central Western System and Tablelands System do not satisfy criterion (c). These systems are not relevantly of significance for the purposes of criterion (c) for several reasons, including a lack of economic significance due to:
- (a) the low volume/value of freight hauled on each system with regard to contribution to, as appropriate, Queensland's exports, imports, or the domestic freight industry;
 - (b) high under-utilisation rates, often related to the impact of modal competition with road; and
 - (c) the high degree of dependence on TSC revenue on these facilities indicating lack of commercial viability.

Criterion (d)

46. Queensland Rail submits that the QCA cannot be satisfied that access (or increased access), on reasonable terms and conditions as a result of declaration of the below-rail service provided on each facility will promote the public interest.
47. In summary, the reasons are as follows:
- (a) Access on reasonable terms and conditions under the proposed Access Framework will promote significant public benefits
 - (i) Promotes efficiencies by removing unnecessary regulatory burdens.
 - (ii) The proposed access framework promotes increased flexibility and proportionality.
 - (b) There are significant direct costs of declaration
 - (i) Compliance and regulatory costs borne by Queensland Rail.
 - (ii) Costs of the QCA performing its regulatory functions, passed on to users of the network.
 - (iii) Direct administration costs borne by the QCA.
 - (c) There are significant indirect costs of declaration
 - (i) Declaration introduces the risk of regulatory error.
 - (ii) Declaration is inconsistent with the object of Part IIIA of the CCA and Part 5 of the QCA Act, which provides for consistency in the regulation of access within industries.
 - (iii) There is intrinsic public detriment in superfluous regulation.
 - (iv) Declaration reduces the efficiency of substantial Government investment in Queensland Rail's network.
 - (v) Some public benefits from declaration are likely to accrue to foreign owned companies and this must be appropriately discounted.
 - (vi) Private benefits accruing to Queensland Rail as a result of non-declaration ultimately accrue to the Queensland public due to Queensland Rail's institutional relationship with Government and commercial incentives to increase utilisation of its railways.
 - (d) Policy arguments as to why declaration does not promote the public interest
 - (i) Efficiencies promoting increased competitiveness of rail results in environmental and safety benefits from increased rail modal share.
 - (ii) Non-declaration is consistent with Queensland Government's 'Moving Freight Strategy'.
 - (iii) Non-declaration enables Queensland Rail to more efficiently adhere to safety obligations.

Summary

In summary, in relation to criterion (a), Queensland Rail does not believe that it has the ability or incentive to exercise market power to adversely affect competition in any dependent market, and on this basis that criterion (a) is not satisfied for any of Queensland Rail's network.

In respect to criterion (b), Queensland Rail has raised matters for the QCA's consideration.

Further, Queensland Rail submits that other than the Metropolitan System, Mount Isa Line and North Coast Line rail systems, Queensland Rail's network is not of sufficient 'size' and/or of sufficient 'importance to the Queensland economy' to satisfy criterion (c).

Finally, in relation to criterion (d) Queensland Rail submits that access (or increased access) to the below-rail services provided by Queensland Rail by the use of each facility, on reasonable terms and conditions, as a result of a declaration of the service would not promote the public interest due to the inefficiencies of regulation and the additional direct and indirect costs.

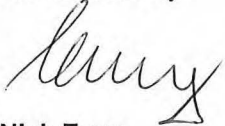
As outlined above, the services provided by Queensland Rail do not meet all four of the access criteria and, therefore, applying the requirements of the QCA Act, the services should not be declared.

Queensland Rail is able to provide further detailed submissions on each of the declaration criteria, provide a fully detailed Access Framework and a proposed deed poll to give legal effect to the proposed framework as a demonstration of the detailed consideration given to this important matter, including a fit for purpose framework that offers certainty for customers, competitive pricing and aims to promote more freight on rail.

Queensland Rail is committed to continue to work with industry on the implementation of future access arrangements.

I would welcome the opportunity to meet with you and elaborate on this submission. I can be contacted on (07) 3072 0781.

Yours sincerely



Nick Easy
Chief Executive Officer

30 May 2018

Attachment 1: Queensland Rail's network



Queensland Rail ABN 68 598 268 528

