INQUIRY INTO THE TRADE PRACTICES AMENDMENT BILL (NATIONAL ACCESS REGIME) BILL 2005
ARTC SUBMISSION

Background

The Senate has referred the provisions of the Trade Practices Amendment (National Access Regime) Bill 2005 ("Bill") to the Senate Economic Economics Legislation Committee for inquiry. The Bill implements the Government's response to the Productivity Commission's Inquiry Report No. 17, 'Review of the National Access Regime' and gives rise to amendments to the Trade Practices Act 1974 ("Act"). The Commission's report was released in September 2001 and the Government's final response, which endorsed the majority of the Commission's 33 recommendations and agreed that scope exists for improvements to the Regime, was handed down in February 2004.

ARTC was created after the Australian and State Governments agreed, in an Inter-Governmental Agreement ("IGA"), in 1997 to the formation of a 'one stop' shop for all train operators seeking access to the national interstate rail network. The IGA had a term of 5 years, which expired in 2003. ARTC is a company, under Corporation Laws, in which shares are owned by the Australian Government through the Ministers for the Departments of Transport and Regional Services and Finance and Administration.

Under the IGA, ARTC is responsible for negotiating access to the national interstate rail network between Brisbane and Perth by virtue of direct ownership or lease of certain parts of the network, or under wholesale arrangements to be negotiated with State Government owners of other parts of the network as applicable.

ARTC currently has responsibility for the management of the interstate standard gauge track, through ownership or long term lease, in South Australia, Victoria, Western Australia and NSW. Those parts of the interstate network not managed by ARTC lie between Kalgoorlie and Perth, within the Sydney metropolitan commuter network (to Parkes in the west), and in Queensland (to Brisbane).

In NSW, ARTC also manages, on behalf of the NSW Government, the regional branchline network in NSW consisting of around 40 track segments and being around 3350 km in length. ARTC carries out the maintenance and train control on the network under contract to the NSW Government, which is responsible for ongoing funding of investment in the branchline network.

The IGA provided for ARTC to negotiate wholesale access arrangements with each of the track managers in NSW, Queensland and WA, which would give ARTC exclusive rights to sell access for interstate operations to those parts of the interstate network within these jurisdictions. ARTC has negotiated an agreement with the West Australian Government (assigned to WestNet Rail) that gives ARTC such exclusive rights with respect to new agreements or the novation of existing agreements. WestNet Rail still effectively controls the maintenance, investment and operations between Kalgoorlie and Perth.

ARTC's objectives largely focus around increasing the role of interstate rail freight in national and regional transport supply chains through:

- Providing efficient access to users of the interstate rail network
- Pursuing a growth strategy for interstate rail through improved efficiency and competitiveness
- Improving interstate rail infrastructure through better asset management and coordination of capital investment, and,
- Promoting uniformity in access, technical, operating and safeworking procedures.

Since it commenced operations in 1998, ARTC has been actively pursuing these objectives, and whilst it has been generally accepted that the efficiency and competitiveness of interstate rail has improved significantly on east-west corridors through improvement in these areas, there are still many impediments to the efficiency of intermodal transport, particularly between capital cities on the eastern seaboard.

There is also a significant volume of bulk export commodities moved on the ARTC network. This primarily includes coal and grain. Around 80-85 million tonnes of export coal is carried on the Hunter Valley rail network leased by ARTC to Newcastle. Other coal is also carried on the ARTC network from the Blue Mountains and Southern Highlands fields to Pt Kembla.

A significant quantity of export grain is also carried on the ARTC network in three states. This includes grain from the Murray mallee and mid north in South Australia to ports in Adelaide and Pt Pirie; the western grain belt in Victoria to ports in Melbourne, Geelong and Portland; Grain from southern, central and northern NSW regions to ports at Newcastle and Pt Kembla.

As such, whilst volume on the ARTC network is predominantly interstate intermodal freight, significants parts of the network around Adelaide, Melbourne, Sydney and Newcastle carry large volumes of bulk export commodities from regional areas to port.

ARTC recognises that the service it provides, and influence it has, covers only part of a number of broader transport supply and distribution networks, both domestic and international. Overall improvement of the efficiency of these networks is the responsibility of many of the industry participants involved as well as regulators and governments. This

will involve greater cooperation between players and a more holistic view of the service provided by rail and transport generally, as well as the necessary investment to improve infrastructure capacity (track, rollingstock, terminals and ports) and performance.

Whilst both the grain and coal industries are major contributors to Australia's economic activity and prosperity, the economics of the two industries are significantly different. This largely arises from differences in the level and volatility of global pricing and volume flow of the two commodities, geographical and logistical differences, and the type and quality of infrastructure supporting the respective supply chains. Each industry has its own distinct economic issues to deal with in regard to investment and efficiency.

Under the IGA, ARTC was required to submit a voluntary access undertaking in accordance with Part IIIA of the Trade Practices Act (1974) (TPA) to the Australian Competition and Consumer Commission (ACCC). An undertaking was submitted by ARTC in January 2001, and approved by the ACCC in May 2002. The undertaking applies to the interstate network controlled by ARTC, at the time, and sets out the framework under which access to that network can be negotiated with ARTC in a fair and balanced way. In endorsing ARTC's access undertaking, the ACCC recognized that a large part of ARTC's revenue is derived from rail operations that compete in markets subject to strong intermodal competition, particularly road. The ACCC also indicated that it saw ARTC's access undertaking as laying a foundation for the development of a consistent 'national' rail access regime in conjunction with other state based jurisdictions.

ARTC is currently developing access undertakings for ACCC endorsement relating to the existing ARTC network, as well as the interstate and Hunter Valley rail networks in NSW. Until endorsement is achieved, access to the rail network in NSW will continue to be governed by the existing NSW Rail Access Regime, a state based regime not certified by the National Competition Council (NCC) for the purposes of the Act.

Access to the interstate network in WA is currently governed by a state based access regime (also not certified by the NCC), whilst there is no applicable regime with respect to access to that part of the interstate network in Queensland. This infrastructure is not within the scope of the current QR Access Undertaking approved by the Queensland Competition Authority (QCA). As such, these parts of the interstate network are potential subject to possibly of declaration under the TPA, which would effectively take the negotiation of access away from the umbrella of the state based regime, and within the arbitration powers of the ACCC under Part IIIA of the TPA. Whilst state based regimes share a number of common threads with ARTC's Access Undertaking, there are still fundamental differences (including the identity of the regulator/arbitrator and pricing approach) that add to the difficulty of obtaining access to the interstate rail network.

ARTC participated in the Productivity Commission's review of the National Access Regime by way of submissions and attendance at hearings. The major issues raised by ARTC in its presentations to the Commission were:

- ARTC is of the view that there should be a single adjudicator with respect to regimes for access in Australia.

- ARTC is of the view that the differentiation of access regimes should be based on the access provider's market and industry positions.

- ARTC is of the view that Industry Codes should be able to be departed from by an access provider as long as it can be demonstrated to the ACCC that the proposed regime satisfies the requirements of an access undertaking.

ARTC is a vertically separated access provider and, as such, ARTC's income consists almost entirely of access fees charged to train operators on its network, and therefore seeks to encourage utilization of the network and has no commercial incentive to discriminate against ant user, or seeker, of access to its network.

The rail freight industry in Australia has undergone substantial change over the last ten years in terms of structure and ownership, largely designed to improve the financial performance of the industry by improving its intermodal competitiveness, and ability to effectively integrate into the broader national transport logistics network. The introduction of competition in the industry has proved to be an effective means to achieve these broader goals, particularly in those markets where rail operations and infrastructure compete strongly against other modes. In those markets where industry economics are such that rail is not a strong competitor and investment in the industry is marginal, the incidence, and impact, of competition is less evident.

The Bill

ARTC supports ongoing review of competition policy and regulation in Australia to ensure that the objectives and mechanisms used remain effective in an ever changing market.

Whilst the Productivity Commission considered the major issues raised by ARTC, final recommendations made by the Commission failed to fully incorporate provisions in the National Access Regime to recognize ARTC's views. Nevertheless, ARTC considers that some of the recommendations do go part-way towards addressing these issues by, in particular, seeking to increase the accountability and efficiency of regulatory activity and Government decision making in this area.

With regard to the issues previously raised by ARTC, it is noted from the recent inquiry into Australia's export infrastructure by the Prime Minister's Exports and Infrastructure Taskforce, that the Taskforce agrees with submission's made to it

'that governments should give consideration to the practicality and desirability of a single regulator'[1]

and,

'In some instances the national interest may require that the Australian Government be in a position to intervene when a six months period has expired but the situation is at an impasse, with no acceptable regulatory outcome in sight. To avoid this possibility stalling the process, the Commonwealth Minister could be given the power to declare the service, without reference to the NCC and without further appeal, and referring the matter to the ACCC for arbitration (again on the 'reasonable test, again with a strict six month time limit, and again with the right of appeal to the ACT. ' [2]

Further, ARTC still considers that there is scope in the National Access Regime to differentiate access regimes with respect to vertically integrated bottleneck facilities and non-integrated facilities, and draws some fundamental distinctions between third party and open access regimes.

A "third party" access regime, as applies where a vertically integrated track owner competes with third parties for above rail activity, is designed to regulate the activities of an organization which has a commercial imperative to minimize third party access to the infrastructure and reduce competition for its contestable activities ('closed shop'). The organization can give effect to this imperative in a range of ways both conspicuous and inconspicuous. The focus with respect to an access regime in this case is generally on ease of access, ring-fencing, information flows, anti-competitive conduct and dispute resolution. The access regime is generally designed to reduce the risk to third parties by restricting some of the more obvious behaviours associated with anti-competitive activities. Such activities include cross-subsidisation of above and below rail activities, hindering access to the network (at the negotiation stage or during operations) and internal flow of market information.

It is extremely difficult for a regulator to monitor and/or appropriately remedy the more inconspicuous behaviours which could occur, and for which the owner has a commercial incentive to carry out. Such behaviours may include the use of creative accounting techniques to disguise cross subsidization of activities, information 'leaks', day-to-day resolution of operational conflicts and strategic investment (or lack thereof) in contestable parts of the network. Such behaviours are difficult to detect, and only surface via a market

[1] 'Australia's Export Infrastructure: Report to the Prime Minister by the Exports and Infrastructure Taskforce' May 2005, p 43
[2] Ibid, p 46

outcome after the commercial damage, which can be significant, has been done. Penalties are often minor compared to the extent of damage that could be experienced by the third party.

The type of market resulting from a third party regime is usually thin and closed. Access is individually negotiated, lacks transparency and pricing more often reflects the users ability to pay. Such an arrangement is generally only suitable where the synergy benefits of vertical integration are necessary for the owner to compete effectively intermodally, and outweigh any benefit of having competition on rail. The Productivity Commission in its final report "Progress in Rail Reform" (August 1999) proposed that urban passenger and low volume branchline networks are more suited to this type of arrangement.

An "open" access regime applies where the track owner has a commercial imperative to maximize value through the encouragement of above rail activity to increase asset utilization. Access revenue is the sole revenue source. Above rail competition is seen as a catalyst for market growth. An open access regime generally focuses more-so on ensuring the owner does not extract monopoly rents from the asset, providing incentives to the owner to improve productivity, invest efficiently in the network, maintain or improve asset performance, and on appropriate risk sharing arrangements. Often, intermodal competition limits the ability of the owner to over-price. Disincentives for anticompetitive behaviours as described above need not be as strong, if at all relevant.

Under this arrangement, the market for access generally contains more participants and is open in nature. Pricing is often transparent and more equitable, and risks are appropriately shared. The market tends also to be more value driven and is conducive to such elements as secondary trading and auctioning.

Such an arrangement is appropriate where intramodal competition would drive intermodal competitiveness through reducing costs and improved service, further resulting in community benefits. This is currently the case with respect to the interstate network and this type of industry structure and regime is viewed as appropriate. Where intermodal competition is slight or not existent, as occurs on the Hunter Valley and Queensland coal networks, ARTC considers that a vertically separated, open access arrangement would be appropriate in all but a very limited number of circumstances, where separation would severely impede the 'production process' of the owner. The potential for the collection of monopoly rents would require a more 'heavy handed' regime in this area.

ARTC supports a number of amendments to the Act that will be brought into effect by the Bill. These amendments include:

- Insertion into Part IIIA of an objects clause that expresses two objectives being the importance of fostering efficient investment in new infrastructure, and the promotion of a consistent approach to access regulation in each industry (whilst recognizing that industry specific regimes accepted under Part IIIA may be divergent due to different market characteristics). The Bill also requires decision makers under Part IIIA to have regard to this objects clause when making their respective decisions. ARTC agrees that this will enhance regulatory accountability by promoting consistency and providing guidance in relation to a decision maker's approach.

- New provisions enabling access providers to lodge post-declaration undertakings with the ACCC. ARTC agrees that this amendment will provide a means for achieving greater certainty and access terms and conditions.

- The Bill applies non-binding time limits to various decisions under Part IIIA (requiring publishing of any notices of extension) including declarations and certifications (National Competition Council and Ministerial decisions), undertakings (ACCC) and appeals (Australian Competition Tribunal). These decision makers are also required to publish decisions and recommendations, as well as reasons. ARTC considers that these amendments will improve regulatory and Government accountability and transparency.

- The Bill introduces a process to expedite extensions of certifications, and access undertakings of codes allowing service providers to avoid potential regulatory uncertainty and delay. ARTC supports this amendment, but considers that a fast tracking mechanism should only be available for regimes with shorter durations, and that the regulator should have discretion over the duration of any extension so that flexibility is not reduced.

Amendments that ARTC does not support, or expresses some caution about include:

- The establishment of statutory pricing principles in relation to Part IIIA to be determined by the Commonwealth Minister. The ACCC would be required to take into account these principles when making assessments or determinations on access undertakings. The principles would be included in Clause 6 of the Competition Principles Agreement (to ensure regulatory consistency). Whilst ARTC accepts that the amendment will increase consistency in access pricing, ARTC has previously expressed concern that forcing a service provider to operate within an explicit pricing framework may restrict entrepreneurialism. Further, flexibility is needed at the undertaking level to develop a pricing approach which best meets the needs of the relevant industry. As technology and commercial practices alter over time, the industry may require an approach that is not envisaged in Part IIIA.

- The Bill amends the Act to explicitly prevent the ACCC from accepting an access undertaking or code where a decision is in force that a state or territory access regime is

effective. Whilst ARTC recognizes that enabling an access provider to lodge an undertaking in such circumstances has the potential to introduce 'forum shopping', ARTC also supports single adjudication for regimes across Australia. This amendment effectively eliminates the option for a service provider to seek more consistent, national, regulation by the ACCC where a state based regime has been certified by the National Competition Council ("NCC"). Whilst national consistency is one of the considerations for certification of a regime, the NCC is yet to require a state based regime to provide for ACCC regulation or arbitration, meaning that many national businesses utilising state infrastructure (in more than one state) will still be subject to jurisdictional regulation, increasing regulatory uncertainty and efficiency.

- The Bill introduces a mechanism to enable the ACCC to grant (and thereafter revoke) immunity from declaration for services to be delivered by government sponsored infrastructure, where construction and operation of the facility is to be awarded through a competitive tendering process, and where reasonable terms and conditions of access will be a key consideration in selecting the proposed tenderer.

  ARTC considers that this mechanism would essentially bypass the lodging of an access undertaking with the ACCC by the service provider, and the public consultation process that would result. ARTC is very cautious about the application of the amended circumstances. Presumably the ACCC would need to be satisfied that the terms and conditions of access are fair and reasonable. This decision could be made by the ACCC without a process of public consultation, and the decision cannot be appealed. The key difference with the undertaking path is that the ACCC would be required to undertake public consultation. Further, a later amendment provides for appeal of ACCC decisions on undertakings.

  ARTC cannot see where, because a build and operate contract is tendered on a competitive basis, that the successful tenderer would have less incentive to seek monopoly rents than any other service provider. As such, ARTC considers that an application by a state or territory to the ACCC for approval of a tender process should be subject to the same procedural arrangements as an access undertaking. Effectively, the tender should have an 'attached' access undertaking approved by the ACCC.

- The Bill introduces new appeal rights with respect to access undertaking and access code decisions by the ACCC. It is argued that this will make the access route through an undertaking or code consistent with other access routes under Part IIIA (declaration/certification), and will encourage the use of undertakings by providing for regulatory accountability.

  Whilst ARTC accepts that the amendment will provide for consistency between access routes such as declaration and certification, ARTC believes that reduced regulatory uncertainty and efficiency may offset any such benefit. The approval of an access

undertaking relies on the ACCC, following public consultation, determining a reasonable balance between the competing aims and desires of the access provider, access seeker and the wider community. Such a balance is often achieved through the undertaking as a whole where trade-off's and concessions are made with respect to the various elements of the undertaking.

Rarely is a particular party happy with the outcome with respect to all aspects of an undertaking. Where an interested party to a new access undertaking is not happy with one or more particular aspects of the undertaking, these aspects effectively become isolated from consideration of the undertaking as a whole. Enabling that party to seek a review of the merits of the ACCC decision on the undertaking based on some isolated elements without balancing consideration of other elements that are more favourable to that party will result in a movement away from a reasonable balance of position for the undertaking as a whole.

In essence, the process of approval or rejection of an access undertaking by the ACCC is likely to be a more inclusive process than the appeal process.