Competition Policy Review Panel –

Rio Tinto Iron Ore Submission on

Part IIIA of the Competition and Consumer Act

June 2014

Submission to Competition Policy Review Panel on Part IIIA

1 Introduction

1 This submission is made by Rio Tinto Iron Ore (***RTIO***). RTIO is the division of the Rio Tinto Group with responsibility for Rio Tinto's global iron ore interests, including its iron ore mines and the rail and port infrastructure servicing those mines in the Pilbara, Western Australia.

2 This submission responds to Chapter 5 ('Competition Laws') of the Competition Policy Review Panel Issues paper of April 2014 (the ***Issues Paper***). In particular, it addresses the following questions posed in the Issues Paper:

> Should the recommendations in the Productivity Commission's Report on the National Access Regime be adopted? Are there other changes that could be made to improve competition in the relevant markets?

3 In order to ensure that the National Access Regime enhances Australia's economic efficiency and export performance it is, in RTIO's submission, essential that:

(a) the preconditions to declaration under the National Access Regime, and the criteria for declaration, are framed appropriately so that declaration can occur only when access is essential to facilitate competition and enhance efficiency and is in the public interest; and

(b) the decision making framework in relation to declaration is robust, thorough and objective.

The costs of imposing access in the wrong circumstances, both for the companies concerned and for Australia, are enormous. There is a very real risk that the National Access Regime could significantly damage the Australian economy if it is not framed appropriately.

4 In order to ensure that the National Access Regime is framed appropriately, in Rio Tinto's submission:

(a) the 'uneconomical for anyone to develop another facility' declaration criterion (***criterion*** (***b)***) should continue to be a ***private profitability test*** (ie, it asks would it be privately profitable for anyone to develop another facility to provide the service). The Productivity Commission's recommendation that criterion (b) be amended so that it focuses instead on whether foreseeable market demand can be met at least cost by a single facility should not be adopted. If, contrary to this view, the Productivity Commission's recommendation is adopted, it is essential that ***all relevant costs are taken into account*** in assessing whether foreseeable market demand can be met at least cost by a single facility. These issues are discussed in ***section 2*** below;

(b) the Productivity Commission's recommendation that declaration should occur only where access is in the public interest (***criterion (f)***) should be adopted. Currently, criterion(f) is satisfied if access is not contrary to the public interest. This issue is discussed in ***section 3*** below;

(c) the importance of the Australian Competition Tribunal (***Tribunal***) to the National Access Regime needs to be recognised and some of the current limitations on the role of the Tribunal should be removed. This issue is discussed in ***section 4*** below;

(d) the production process exception needs to be reinforced, so that the exception can operate, as intended, as an effective gatekeeper against inappropriate declaration applications. This issue is discussed in ***section 5*** below.

5 RTIO has of course had extensive experience with the National Access Regime, in particular, with the declaration process. In 2007 and 2008 applications were made by Fortescue Metals Group for declaration of RTIO's rail facilities in the Pilbara, which form part of RTIO's iron ore production system. These applications were ultimately rejected following proceedings before the

Tribunal,[1] an appeal to the Full Federal Court[2] and a further appeal to the High Court of Australia[3] (referred to here as the ***Pilbara rail access proceedings***).

2 Criterion (b)

6 RTIO has argued consistently that a private profitability test is the appropriate test under criterion (b) and this has been endorsed by the Full Federal Court and the High Court (both of which have found, not only that the private profitability test is the test currently prescribed by Part IIIA, but that it is the most appropriate test). Nevertheless, administrative bodies such as the NCC and the Productivity Commission continue to press for a test which is often described as a natural monopoly test.

7 In the expectation that if Part IIIA is amended, the direction as to the appropriate test for criterion (b) is likely to be similar to that preferred by the Productivity Commission and the NCC (ie, some form of natural monopoly test), RTIO proposes to first address the most crucial issue in relation to the application of a natural monopoly test, and then to address the reasons that it believes the current private profitability test should be retained. While RTIO does not endorse a natural monopoly test for criterion (b), RTIO wishes to stress the importance of one aspect that must be unambiguously addressed if a natural monopoly test is applied. This is that **all costs** must be taken into account when determining whether 'the costs of an existing facility meeting total foreseeable market demand are lower than the costs that would be incurred under the least costly alternative scenario.'[4]

8 RTIO has previously made detailed submissions to the Productivity Commission in relation to these matters.[5]

2.1 All costs should be assessed under a natural monopoly test for Criterion (b)

Productivity Commission Recommendations

9 The Productivity Commission has recommended that:

> Criterion (b) should be satisfied where total foreseeable market demand for the infrastructure service over the declaration period could be met at least cost by the facility. That is, criterion (b) should be satisfied where the costs from the facility meeting total foreseeable market demand over the declaration period are lower than the costs that would be incurred under the least costly alternative scenario. Total foreseeable market demand should include the demand for the service under application as well as the demand for any substitute services provided by other facilities serving that market. Cost estimates should include an estimate of any production costs incurred by the infrastructure service provider from coordinating multiple users of its facility.

10 If the Productivity Commission's recommendation in relation to criterion (b) is adopted, it is essential that all costs associated with meeting market demand using one facility are taken into account. For the reasons discussed below, excluding some costs (and perhaps considering them

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[1] *Re Fortescue Metals Group Ltd* (2010) 271 ALR 256 (***Re Fortescue***).

[2] *The Pilbara Infrastructure Pty Ltd v Australian Competition Tribunal* (2011) 193 FCR 57.

[3] *The Pilbara Infrastructure Pty Ltd v Australian Competition Tribunal* (2012) 246 CLR 379 (***TPI v Tribunal***).

[4] The quoted text is extracted from the test preferred by Productivity Commission. See PC Report, p.160-167. Under the Productivity Commission's preferred test criterion (b) would be satisfied where total foreseeable market demand for the infrastructure service over the declaration period could be met at least cost by the facility. That is, where the costs from the facility meeting total foreseeable market demand over the declaration period are lower than the costs that would be incurred under the least costly alternative scenario. Irrespective of which formulation of a natural monopoly test is applied, the crucial issue is that **all costs** are addressed.

[5] Rio Tinto Iron Ore Submission to the Productivity Commission's National Access Regime Review' dated 8 February 2013 and 'Rio Tinto Iron Ore Submission in Reply to the Productivity Commission Draft Report' dated 5 July 2013.

under criterion (f) instead) would be contrary to economic principle and be difficult and complex to administer in practice.

11 In this regard, RTIO is pleased that the Productivity Commission in its final recommendation has expressly recognised that costs from coordinating multiple users of a facility should be taken into account. As discussed below, however, RTIO is concerned that the recommendation could be construed as still intending to exclude some types of costs caused by having multiple users of the same facility such as lost throughput due to such things as congestion, loss of operational flexibility and delays to expansions. There is no basis for excluding such costs.

Economic principles support taking all costs into account

12 It is important to remember that natural monopoly tests do not traditionally focus upon the question of competitors sharing a facility at all. Natural monopoly tests arise in the context of an industry or market, focusing upon whether *one firm* can meet total market demand at a lower cost than two or more firms.[6] Assessing whether or not an industry is a natural monopoly is determined by assessing whether or not the cost function of supply across the industry is sub-additive. The classic natural monopoly test is not about a sharing arrangement.

13 If an adaptation of the classic economic test for natural monopoly is to be applied to address the distinct scenario of whether a facility owned by a firm can be shared with other firms to meet all demand at less cost than multiple firms using multiple facilities, the adapted test needs to reflect the circumstances of this different scenario – namely that multiple firms sharing a single facility will give rise to a range of costs not just 'production costs'.

14 By way of illustration, in the Pilbara rail access proceedings the Tribunal in its 2010 decision accepted that a large range of costs were likely to arise from mandated sharing, including:

- Inefficiencies results from congestion. To put this in context, if congestion caused by mandated access resulted in a 25% decline in train consist efficiency (a reasonable assumption for the key routes in the rail system) the extra consists required to achieve the same throughput would cost in the order of $2.5 billion;
- loss of flexibility in scheduling in a system that is currently very flexible, with moment to moment changes being made to accommodate such things as unexpected ore quality changes, breakdowns, unavailability of manpower, maximising the value of opportunistic maintenance windows, etc;
- inevitable delays to RTIO's planned expansion programs that would arise if third parties were involved in, or affected by, such programs. The Tribunal accepted that such delays were inevitable and that on a 'conservative assumption' the cost to revenue of expansion delays would be in the order of $10 billion;[7]
- delays in introducing new technologies and operating practices designed to achieve an increase in efficiency and throughput.

15 These are all real costs, not just to an incumbent such as RTIO, but more importantly to the Australian economy. It is imperative that they be included when comparing the costs of sharing a facility with the costs of developing/using the next best alternative. Moreover there is no reason, from an economic or logical perspective, to exclude any of them.

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[6] See, for example, Kahn, A, *The Economics of Regulation: Principles and Institutions*, Volume II (1988) 119; Sharkey, W, *The Theory of Natural Monopoly* (1982) 54; Posner, R, *Natural Monopoly and its Regulation*, (1999), p.1; Panzar, J, 'Technological Determinants of Firm Structure and Industry Structure' in Shmalensee, R and Willig, RD (ed), *Handbook of Industrial Organization*, Volume 1 (1989)3, 24. See also *Re Services Sydney Pty Limited* [2005] ACompT 7 at [102].

[7] *Re Fortescue* at [1328]

16 There was broad support from the economic experts in the Pilbara rail access proceedings for the proposition that a natural monopoly type test for criterion (b) required that a broad range of costs needs to be taken into account. For example, Professor Ordover provided the following opinion:

> "engineering" costs generally will underestimate the costs that will have to be incurred by the incumbent firm if it is required to provide access. That is, the costs of moving a particular quantity of iron ore (for example) produced in the incumbent's mines to the incumbent's storage and processing facilities will differ materially from the costs of moving the same aggregate tonnage that originates partly from the mines of the incumbent and partly from the mines of the access-seeker (or a third party). In particular, line sharing may result in loss of effective capacity on the line due to inefficiencies resulting from the need to coordinate shipments from different users. There may also be additional costs – such as unplanned congestion and delays – that cannot be fully accounted by each party but which nevertheless are "real" and which impose a burden on the incumbent firm (but also on the access-seeker). And there will be costs incurred by the managements of both firms in designing contracts, coordinating schedules, resolving disputes, and so on. …. **If a natural monopoly test is to be applied, it is essential that these costs are taken into account (as well as the direct engineering type costs)** when assessing whether it is cheaper to have one facility, rather than two facilities, service the foreseeable demand.[8] (emphasis added)

17 Professor Gans, Professor of Management (Information Economics) at the University of Melbourne, who appeared on behalf of the access seeker in the proceedings, also provided an expert opinion that a broad range of costs should be taken into account when applying the test he was advocating, which was not materially different from the test recommended by the Productivity Commission. Professor Gans opined that a facility will be uneconomic to duplicate if the revenue of access seekers from using the provider's facility less the full cost of access (*including coordination costs, opportunity costs and additional capital costs*), is greater than the revenue of access seekers from using the other facility less the costs of using and developing that facility.[9]

18 When the Tribunal explicitly asked whether a natural monopoly test under criterion (b) should be confined to a limited range of costs and should exclude the diseconomy and inefficiency costs that arise from sharing, all of the economic experts to whom the question was put rejected such an approach. For example, Dr Williams, Executive Chairman of Frontier Economics Pty Ltd, observed:

> If you put things together you have extra costs, like coordination costs, then they are relevant to the test of natural monopoly, because natural monopoly is defined as when the function over its length is sub-additive, that is, when it's cheaper to do it all together than – than the sum of them when they're separate., So it seems to me quite improper not to take into account anything that makes it more expensive or less expensive when you do it all together than the sum of the costs when you do it separately.[10]

19 In summary, in assessing whether market demand can be met at least cost by a single facility, there is no economic reason not to take into account all costs arising as a result of multiple users using a single facility.

20 The Productivity Commission seems, at least in broad terms, to have accepted this proposition and its final report (unlike its draft report) recommended that the assessment of costs under criterion (b) include an estimate of *'any production costs incurred by the infrastructure service provider from coordinating multiple users'*.[11] While expressly stating that its list was not

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[8] Affidavit of Janusz Ordover (3 July 2009), Annexure "JO-2" at p.7.

[9] Second Affidavit of Joshua Gans (12 June 2009), Annexure "JSG-3" at [50].

[10] Transcript of oral testimony before the Tribunal of Dr Williams (5 November 2009) T1719.25-40.

[11] PC Report, p.250.

exhaustive, the Commission identified 'Coordination Costs' that it considered relevant to the cost-benefit assessment to be undertaken under criterion (b) as including the costs of:

(a) building the physical access or interface to the facility to allow for third party use, as well as any increased maintenance costs;

(b) reduced operational flexibility and efficiency; and

(c) measures taken to coordinate investments that are necessary for the facility to meet total foreseeable market demand for the infrastructure service at least cost (noting that delays to facility expansions or the adoption of new technologies that improve the efficiency of the service may arise as a result of the incumbent having to deal with multiple users).[12]

21 There is a risk that the Productivity Commission's reference to 'production costs', and the specific examples it gives, could be read as an intention to exclude costs that would arise because of reduced throughput (eg, due to congestion, loss of operational flexibility and expansion delays). The reference in the Commission's list to reduced operational flexibility suggests that perhaps reduced throughput costs were intended to be included, but the reference to 'production costs' suggest perhaps not. Costs such as reduced throughput are just as “real” as production costs – in fact from the national economy’s perspective they are probably even more important than additional production costs. As the Pilbara rail access proceedings demonstrated, these types of costs (referred to generically as 'diseconomies') are potentially very significant indeed. In order to gain a true picture of whether the costs of multiple users using a single facility do, or do not, outweigh the costs of duplication, all such costs must be taken into account as well as the more direct additional costs such as production costs.

22 In summary, if criterion (b) is to be amended, it is essential that the legislation makes clear that in applying the proposed new test, all costs of having multiple users use a single facility should be taken into account.

23 In RTIO's view a general statement to this effect should be included in the legislation rather than setting out a list of categories of cost that could be taken into account under criterion (b). The wide range of types of costs identified in the context of the Pilbara's rail infrastructure will not, for example, be the same as the types of costs that might arise from mandated sharing of other types of infrastructure with different forms of ownership and use. As the Productivity Commission has observed: 'It is not possible to envisage every type of cost that may arise from sharing infrastructure.'[13]

Practical reasons not to exclude costs

24 It is sometimes suggested that it does not matter if costs are excluded from consideration under criterion (b) because they can still be considered under criterion (f), the public interest test. Excluding costs from consideration under criterion (b), in addition to making no economic sense, however, would also create a legal issue and a practical issue.

25 The legal issue arises because of the High Court's finding that the Tribunal cannot 'lightly depart' from a designated Minister's assessment of the public interest under criterion (f). The Tribunal is much more limited in its review of the Minister's decision under criterion (f) than it is in reviewing the Minister's decision under criterion (b).[14] The consequences of excluding any category of costs from criterion (b) and considering them under criterion (f) would be that the technical and fact intensive examination of some of the costs of sharing would not be subject to detailed review by

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[12] PC Report, pp.164-165.

[13] PC Report, p.166.

[14] *TPI v Australian Competition Tribunal* at [112].

the Tribunal. This is impractical, would lead to endless disputes as to which criterion the relevant costs should be assessed under and it is flawed to the extent that the assessment of such costs may require the technical and detailed expertise and processes that are available to the Tribunal, but not the NCC and the Minister (eg, the ability to call for clarifying material and to test assertions via cross examination). There is therefore no justification for introducing different treatment and a different level of scrutiny in respect of the various categories of cost that arise from sharing a facility.

26 In addition to this legal difficulty, excluding some costs from criterion (b) and considering them instead under criterion (f) creates a practical problem. The NCC, Minister and Tribunal will need to consider each type of cost and determine which category that cost should be allocated to, with different legal consequences flowing from the classification, as discussed above. In relation to many costs, different views might legitimately be held about which category the costs should fall into. As also discussed above, this creates the potential for protracted legal dispute and wasted cost and effort for no particular benefit.

27 It makes far more sense, both in terms of principle and practical application, to have technical matters like the true economic costs of multiple users sharing a facility assessed together under criterion (b).

28 This division would still leave significant work for criterion (f). Broader public interest factors – such as environmental issues, security concerns and impacts on overall investment incentives – would appropriately be considered here.

2.2 The Private Profitability Test for criterion (b)

Private profitability test best achieves the objectives of Part IIIA

29 RTIO believes that the private profitability test applied by the High Court, is the correct test to apply. There is no reason to amend the existing legislation.

30 In answer to the question it posed – 'when might the benefits of regulated access outweigh the costs?' – the Productivity Commission observed:[15]

> … the benefits of access regulation are more likely to outweigh the costs where there is a monopoly provider of infrastructure services. Competition between service providers will generally be preferable to access regulation in markets where two or more infrastructure service providers are able to provide the same service (or an effective substitute service).

Of the various alternative interpretations put forward for criterion (b), the private profitability test best reflects this principle.

31 Importantly, the purpose of the private profitability test is not to decide whether there should be one facility or two, it is to decide how the decision of sharing or duplication will be made – via private negotiation and market forces or by regulatory intervention.

32 Where duplication is privately feasible, the facility owner and access seeker have a commercial incentive to find the least cost arrangement. If it would cost less to share the facility than it would to duplicate the facility, then the facility owner has a commercial incentive to provide access so long as it can charge an access fee that is greater than the cost of providing access. The access seeker has the incentive to share the facility rather than build its own facility provided the access fee is less than the cost of duplication. The parties' commercial incentives will result in the facility being shared at an access price struck somewhere between the cost of providing access and the cost of duplication. Importantly, this conclusion applies irrespective of whether or not the facility owner has market power in a downstream market. Because it will be privately profitable for a new

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[15] PC Report, p.8.

facility to be developed, new entry will occur and market power will be lost irrespective of whether or not the facility owner provides or refuses access. Conversely, if the true costs of access would outweigh the costs of constructing a separate facility, no sharing arrangement will be agreed and duplication will occur. In this way, if the incumbent's facility can be profitably duplicated, the interplay of market forces will determine whether it is more efficient to build an alternative facility or have the existing incumbent's facility shared based on commercially agreed access terms. The assessment of whether the true costs of access outweigh the costs of duplication is best made by market participants rather than by a regulator.

33 On the other hand, if an incumbent's facility cannot be profitably duplicated, then that facility could be a bottleneck and declaration may be appropriate if the other declaration criteria are met. The private profitability test is therefore the right filter to apply as it will allow market forces to work where possible but potentially allow regulatory intervention when there is truly a bottleneck.

34 In contrast, a natural monopoly type test still allows for the possibility that criterion (b) can be satisfied, potentially leading to regulatory intervention, where there is actual or potential duplication of infrastructure and facilities-based competition is occurring. A new entrant is likely to be motivated to focus narrowly on which option is lower cost for it (regardless of whether this would impose costs on the incumbent as a result of operational inefficiencies, increased infrastructure requirements, delays to expansions and technological developments etc). Potential new entrants will be encouraged to 'roll the regulatory dice' to see if a favourable deal will be mandated. As a result, the efficiencies that would be generated through a new, alternative facility (which may utilise newer technology and lower-cost operations) and the facilities-based competition it would bring, will be foregone.

35 It is only in circumstances where market forces cannot be relied upon to ensure the most efficient outcome that regulatory intervention is justified. Forcing rivals to cooperate through mandated access runs the danger of blunting competition between them. Furthermore, mandating access removes the potential for facilities-based competition developing in the market for the service. The incumbent's monopoly position is being locked in and regulation substituted for competing facilities.

Productivity Commission reservations about the private profitability test are unwarranted

36 The Productivity Commission considered there is a greater chance of 'false negatives' under the private profitability test (when contrasted to a natural monopoly test) due to a perceived risk that a decision maker will incorrectly decide that a facility is profitable to duplicate, or difficulties in being satisfied that a facility is unprofitable to duplicate. The Productivity Commission expressed doubts about a decision maker's ability to estimate uncertain measures such as costs, prices, demand, capacity, and required rates of return.[16]

37 RTIO believes that the Productivity Commission's concerns about the private profitability test are overstated. The private profitability test can be performed in a relatively straightforward fashion with a minimum number of assumptions and predictions. Essentially it requires an assessment of whether constructing an alternative facility would generate a sufficient return on the capital that would be employed in developing that facility.

38 As the High Court observed when it endorsed the private profitability test for criterion (b), the question of whether it would be economically feasible to develop an alternative facility, involving as it does the making of forecasts and the application of judgment, is 'a question that bankers and investors must ask and answer in relation to any investment in infrastructure. Indeed, it may properly be described as the question that lies at the heart of every decision to invest in

[16] PC Report, p.157-158 and 160.

infrastructure, whether that decision is to be made by the entrepreneur or a financier of the venture'.[17]

39 In any event, forecasts of many of these factors – costs, demand and capacity – are inevitably involved in the application of the proposed alternative natural monopoly test as well. Further, it is much less likely that there will be occasions where market evidence is readily available to demonstrate whether or not the natural monopoly test is made out, compared to the private profitability test where public announcements, internal company assessments, external reports, and actual construction, are readily available to provide real world indicators of whether the private profitability test can be satisfied.

40 The Productivity Commission was also concerned that even where a decision maker correctly determines that duplication of a facility is profitable, there was a risk of a false negative because the eventual duplication of that facility might not lead to effective competition in circumstances where the profitability of the alternative facility is only marginal.[18]

41 This concern appears to be based on the premise that where a facility is privately profitable to duplicate, the market cannot be relied upon to ensure access is granted where that would be a lower cost option than having a duplicate facility built.

42 As discussed above, this premise is erroneous. Under the private profitability test, when the true costs of access are less than the costs of constructing a new facility, the marketplace will ensure that access on commercially-negotiated terms is granted. Conversely, where the true costs of access are greater than the costs of a new facility, a new facility will be constructed. The development of an alternative facility is likely to lead to more intense competition between the facility owner and the access seeker than would an access declaration. The availability of alternative facilities will expand the overall capacity available to access seekers and the facility owner, which will stimulate greater competition, not only between the parties, but with new potential access seekers. This is particularly so in the case of infrastructure facilities with high initial fixed cost and relatively low operating costs. Further, the development of alternative facilities is likely to incorporate newer technology which may give the entrant a competitive edge over the incumbent. Thus a new entrant's operating costs may well be lower than those of the incumbent.

43 As a result the current private profitability test is the correct approach to criterion (b) and the Productivity Commission's recommendation that criterion (b) should be amended should not be adopted.

3 Criterion (f)

44 RTIO agrees with the Productivity Commission's finding that the current test, which is satisfied if access is not contrary to the public interest, sets too low a hurdle. As the Commission recommends access should be required only where it is positively in the public interest. Introducing an affirmative public interest test as the Commission recommends will assist to ensure that access regulation is applied only where it is likely to generate net benefits to the community.[19]

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[17] *TPI v Australian Competition Tribunal* at [106].

[18] PC Report, p.158-159, referring to *Re Fortescue* at [818].

[19] PC Report, p.178-179.

4 Part IIIA decision makers and role of the Tribunal

45 The Productivity Commission did not recommend any changes to the availability of merits review by the Tribunal under Part IIIA and highlighted that there are many reasons merits review may enhance the operation of the regime and help to ensure that access regulation is 'judiciously applied'.

46 RTIO agrees that the ability to seek merits review by the Tribunal of a designated Minister's declaration decision is crucial to ensuring that parties have confidence in the declaration regime because it contributes to decision making which is rigorous, transparent, fair and reasonably certain and more likely to be correct against the declaration criteria. This contributes to a regulatory environment which does not discourage investment in infrastructure.

47 This was vividly illustrated in the Pilbara railways matters. RTIO asserted that significant costs were likely to result from declaration of its railways, but the NCC and Minister were unable to adequately test the likely extent of such costs. The Tribunal, however, undertook a thorough, expert review of the evidence and conducted its own investigations. This rigorous merits review enabled the Tribunal to conclude that costs in the region of billions of dollars were likely to result from declaration of the RTIO railway lines, which in all 'probability' would have 'dwarfed' the benefits of access being granted.[20] These significant costs would not be borne by RTIO alone, as the flow-on effects to Australia in terms of lost exports, royalties and income taxes would be enormous.

48 Since the Tribunal's decision in the Pilbara Railways matters, Part IIIA has been amended and the Tribunal is now limited to looking at information taken into account by the original decision maker, subject to the ability to request additional information the Tribunal considers reasonable and appropriate.[21] These amendments, and the High Court's decision in *TPI v Australian Competition Tribunal* in relation to the appropriate role of the Tribunal, mean that the Tribunal's powers are much more confined than previously thought.

49 RTIO is concerned that the effect of the 2010 amendments and the High Court decision on the appropriate role of the Tribunal will result in declaration decisions being made without detailed primary evidence and the opportunity to test that evidence. The great strength of the Tribunal process prior to the amendments was that primary evidence in the form of affidavits from lay and expert witnesses was filed and that evidence was tested through cross-examination and, in the case of experts, joint expert evidence, or 'hot tubs'. This allowed a much more rigorous examination than is possible before the NCC or Minister and is therefore much more likely to arrive at the correct result. Given that by definition, the National Access Regime applies to nationally significant information, it is vital that the decision making frameworks maximise the chance of arriving at the correct result.

50 It has been suggested that as a result of the 2010 amendments, parties in declaration matters will be encouraged to provide primary evidence in the form of affidavits from lay and expert witnesses before the NCC, in order to avoid the risk that they may be precluded from producing evidence in relation to a particular issue at the Tribunal stage. The tight timelines within which the NCC and the Minister must make decisions make it impossible, however, for a party to put forward all of the primary evidence necessary for a thorough review of the facts. Furthermore, neither the NCC nor the Minister have the necessary processes to test lay and expert evidence put before them, eg, in the form of cross-examination of witnesses or 'hot tubs'. Although the Tribunal may request additional material, the Tribunal will not be aware what relevant material is available or might

[20] *Re Fortescue* at [1319].

[21] *Competition and Consumer Act 2010* (Cth) (***CCA***) s 44ZZOAAA.

assist it in its tasks. This issue is further exacerbated by the tight timelines within which the Tribunal must also make its decision.

51 In summary, in RTIO's view by restricting the ability of parties to put evidence to the Tribunal the 2010 amendments will lead to more decisions being made based on untested assertions in submissions and decision makers' intuitions rather than a detailed examination of the facts from the bottom up. This greatly increases the risk of incorrect decisions being made, potentially to the great detriment of Australia's economic performance.

52 RTIO accepts that there is a need to ensure that decisions are reached in a timely manner. An appropriate balance could be reached if parties were restricted from introducing new ***issues*** before the Tribunal without a direction from the Tribunal to that effect. The parties should, however, be able to introduce before the Tribunal primary evidence that goes to the issues that were raised before the NCC and the Minister and any updating material in the event there have been changes in circumstances that are relevant to the review which have taken place after the NCC's decision. In this way, the process can proceed by way of submission before the NCC and the Minister (which is the only practical alternative given the tight timelines), with primary evidence to support those submissions, but not raising new issues (unless directed by the Tribunal), being submitted to the Tribunal if the decision is subject to Tribunal review.

5 Production process exception

53 Section 44B of the CCA defines the services that are amenable to declaration under Part IIIA. Expressly excluded from the definition is the use of a production process, except to the extent it is an integral but subsidiary part of the service in question.

54 In *BHP Billiton Iron Ore Pty Ltd v National Competition Council* [2008] HCA 45, the High Court found that the exception is not attracted for services that are used by the facility owner as part of its production process, unless the access seeker seeks access to the production 'process' itself. In that case, although the High Court found that the Newman and Goldsworthy lines were an integral part of the rail operator's production process for a marketable commodity, it considered that the use of the railway lines by an access seeker did not constitute a use of that production process.

55 The Productivity Commission concluded that although the legal distinction between what is and is not a production process is 'imperfect', the exception as currently drafted and interpreted by the High Court would prevent declaration in 'obvious cases' where the coordination costs of access would exceed any competition benefits. This is misconceived – the High Court's interpretation of the production process exception does not entail any analysis of the coordination costs versus competition benefits. The Productivity Commission also considered that it would be difficult to define a more comprehensive exception that would exclude only facilities for which access regulation would not result in net benefits, particularly because Part IIIA is not an industry specific regime. RTIO disagrees that any such difficulty would arise. The production process exception was clearly intended to prevent access by a third party to an incumbent's key production facilities and this could be articulated as addressed below.

56 RTIO submits that the purpose of the production process exception is to act as a gatekeeper against the inappropriate declaration of infrastructure that is integral to an operator's production process for a marketable commodity. The exception seeks to avoid the significant inefficiencies and investment disincentives that would arise from interference in a firm's production process through third party use of that infrastructure.

57 The High Court's interpretation of the production process exception means that the exception is unlikely to ever apply. This means that facility owners using infrastructure as part of their own integrated business operations are at risk of third party interference even where the facility is

acknowledged to be used as an integral part of the owner's production process. This defeats the purpose of having the exception and does not align with the 'efficiency' objective identified in section 44AA of the CCA.

58 The Productivity Commission's view that amendment to the exception is unnecessary because coordination costs can be assessed under criterion (b) assumes that the Commission's proposed amendments to criterion (b) are adopted. RTIO submits that this is not a sufficient reason not to amend the exception so that it achieves what was originally intended. Regardless of whether criterion (b) is amended or how it is interpreted by the courts, it is important that the production process exception acts as an effective gatekeeper to exclude inappropriate applications at the outset and to avoid wasted time and resources arising from unnecessary consideration of the declaration criteria.

59 Accordingly, RTIO submits that the exception should be amended to make it clear that 'service' excludes the use of infrastructure, or a significant part of infrastructure, which is '*used as an integral part of a production process by the facility owner or access provider*.' RTIO considers that such an amendment would ensure that the production process exception is able to operate as originally intended to effectively filter out inappropriate declaration applications.