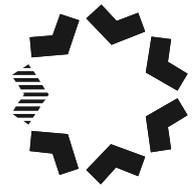


NATIONAL
COMPETITION
COUNCIL



Herbert River cane railway

Application for declaration of a
service provided by the Herbert River
cane railway



Draft Recommendation

1 June 2010

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Abbreviations and Defined Terms

ACCC	Australian Competition and Consumer Commission (www.accc.gov.au)
Act	<i>Trade Practices Act 1974 (Cth)</i>
Applicant / NQBE	North Queensland Bio-Energy Corporation Limited
Application	North Queensland Bio-Energy Corporation Limited, <i>Application under Part IIIA of the Trade Practices Act 1974 for Declaration of the Service provided by CSR's Herbert River Narrow Gauge Tram Network</i> , received by the Council 22 March 2010.
Canegrowers	Queensland Cane Growers Organisation Ltd
CCS	Commercial Cane Sugar – the commercially recoverable sugar content of sugarcane, expressed as a percentage.
Council / NCC	National Competition Council (www.ncc.gov.au)
Declaration Guideline	<i>NCC Declaration of Services – A guide to Declaration under Part IIIA of the Trade Practices Act 1974 (Cth)</i> (2009)
Growers	Landholders in the Herbert River district that grow sugarcane for harvest and sale
National Access Regime	The mechanism established by Part IIIA through which an access seeker can gain access to the service or services provided by a nationally significant infrastructure facility on commercial terms and conditions
NEM	The National Electricity Market – a wholesale electricity market for the supply of electricity to customers in Queensland, New South Wales, the Australian Capital Territory, Victoria, South Australia and Tasmania.
Network Easements	The various arrangements (including informal licenses, permits to pass and easements under sugar industry legislation and general law easements) in place between Sucrogen and the owners of land over which the Network runs.
Part IIIA	Part IIIA of the Act
ROAM Report	Report dated 12 April 2010 by ROAM Consulting, attached as Annexure H to the Sucrogen Submission.
Service	Use of the narrow gauge sugar cane railway in the Herbert River district of North Queensland owned and operated by Sucrogen.
Sucrogen	Sucrogen (Herbert) Pty Ltd (formerly CSR Sugar (Herbert) Pty Ltd)
Sucrogen Submission	Sucrogen (Herbert) Pty Ltd, <i>Submission to the National Competition Council</i> , received by the Council 27 April 2010.
Synergies Report	Report dated April 2010 by Synergies Economic Consulting, attached as Annexure E to the Sucrogen Submission.
Tribunal	Australian Competition Tribunal

1 Draft recommendation

Draft Recommendation

- 1.1 The Council has reached a preliminary view that the Application does not satisfy all of the declaration criteria contained in s 44G(2) of the Act and proposes to recommend to the designated Minister that the Service **not be** declared under Part IIIA .
- 1.2 The Council's reasons for its draft recommendation are set out in this report.

Public consultation on the Draft Recommendation

- 1.3 The Council now seeks submissions from interested parties in response to this draft recommendation and will take these submissions into account in preparing its final recommendation to the designated Minister. The closing date for submissions is **5.00pm on 1 July 2010.**
- 1.4 Submissions should be emailed in soft copy to the Council at hrtramways@ncc.gov.au (in both MS Word and PDF formats), with a hard copy sent to:

HR Tramway
National Competition Council
GPO Box 250
Melbourne VIC 3001
- 1.5 The Council will use its best endeavours to make its final recommendation to the designated Minister by **21 July 2010**. Given this time constraint, all parties are urged to comply with the submission deadline. Extensions to the deadline are unlikely and late submissions will only be considered in exceptional circumstances.

2 Application and process

Application

- 2.1 Sucrogen (Herbert) Pty Ltd (formerly CSR (Herbert) Pty Ltd) (**Sucrogen**) owns and operates a narrow gauge sugarcane railway, comprising at least 500km of track,¹ located in the Herbert River district of North Queensland (**Network**).
- 2.2 During the crushing season, which runs for approximately 22 weeks between June and November, Sucrogen uses the Network to transport sugarcane from Growers' fields to one of its two mills in the Herbert River district – Victoria mill or Macknade mill. Sucrogen also uses the Network to transport raw sugar from both mills to the port facility at Lucinda for export. The facilities at the Port of Lucinda are owned by Sugar Terminals Limited and operated by a subsidiary of Queensland Sugar Limited under a lease agreement.
- 2.3 On 22 March 2010 the Council received an application from North Queensland Bio-Energy Corporation Ltd (**Applicant**) for declaration under Part IIIA of the use of the facility comprising the Network. The Applicant seeks declaration of the service to enable the Applicant to operate its own trains and rolling stock to transport sugarcane and other feedstock harvested within the Herbert River district to the Applicant's proposed new factory near Ingham (**Application**) (see section 4 of this report for more detail on the Service the subject of the Application).

Public consultation on the Application

- 2.4 The public version of the Application (which excludes material identified by the Applicant as confidential) was made available on the Council website and the Council invited written submissions on the Application from interested parties. Submissions closed on 27 April 2010.
- 2.5 The Council received submissions from the following parties:
 - Sucrogen; and
 - Queensland Cane Growers Organisation Ltd (**Canegrowers**).
- 2.6 A late submission was received by the Council on 18 May 2010 from the Queensland Cane Harvesters' association. As the preparation of this draft recommendation was

¹ At [1.2] of Annexure A to the Sucrogen Submission, Sucrogen states that the Network comprises 321.6km of main and branch lines, 141.2km of sidings and 41.8km of yard track and passing loops – a total of 504.6km. However, the Sucrogen Submission refers at [5.3] to 'approximately 550km of tramway' and the Synergies Report at page 53 states: 'It is also noted that Sucrogen estimates the total length of the Tramway Service Network at 550km (as opposed to the 530km stated by NQBE).'

already significantly advanced, the Council was unwilling to formally accept the submission at that time. The Queensland Cane Harvesters' association have a further opportunity to provide a submission in response to this draft recommendation.

- 2.7 In preparing this draft recommendation, the Council has taken into account the submissions received (except as noted in paragraph 2.6), information provided during meetings and discussions with interested and related parties and information obtained from publicly available sources.

3 Declaration under Part IIIA

Objectives and character of Part IIIA (the National Access Regime)

- 3.1 The National Access Regime, established by Part IIIA of the Act, provides a legal mechanism through which an access seeker can gain access to the services provided by an infrastructure facility—such as a railway, port, or other handling, transport or communications facility—on commercial terms and conditions. It is available when attempts at commercially negotiated access are unsuccessful.
- 3.2 The regime provides an important means of promoting competition in markets where the ability to compete effectively is dependent on being able to use monopoly infrastructure. At the same time the regime ensures that infrastructure owners receive a commercial return on investment and that incentives for efficient investment are not adversely affected.
- 3.3 Declaration forms the first stage of the National Access Regime under Part IIIA. It is the mechanism for determining whether the service or services provided by a particular facility should be subject to access regulation and depends on whether six criteria specified in Part IIIA of the Act are satisfied.
- 3.4 Stage 2 of the National Access Regime is the negotiate/arbitrate stage. At this stage, a service provider and access seeker negotiate the terms and conditions upon which access may be granted. Where negotiations are unsuccessful, recourse is available to the Australian Competition and Consumer Commission (**ACCC**) to arbitrate an access dispute.
- 3.5 The High Court discussed the two stage nature of the National Access Regime in *BHP Billiton Iron Ore Pty Ltd v National Competition Council* (2008) HCA 45 at [17]-[18]:²

The consequence of a declaration of a service is that the “third party” ... is given what may be described as an enforceable right to negotiate access to the service. The right may be considered “enforceable” because, subject to the constitutional limits (stated in s 44R), if a third party and a provider are unable to agree upon an arrangement for the third party to have access to the declared service, the third party may notify the ACCC of the dispute (s44S). The ACCC then has the power to arbitrate such an access dispute and, in general, “must make a written determination on access by the third party to the service” (s44(V)(1)).

Access to the declared service is, however, not a necessary or ultimate result of the arbitration (s44V(3)). Further, s44W provides that the ACCC must not make a determination that would have any of the prescribed effects. These include the effect of “preventing an existing user obtaining a sufficient amount of the

² References in original removed.

service to be able to meet the user’s reasonably anticipated requirements, measured at the time when the dispute was notified” (s44W(1)(a)).

- 3.6 A decision by the designated Minister to declare a service neither provides access seekers with an automatic right to use the service nor determines the terms and conditions of any use. If a service is declared, an access seeker has an enforceable right to enter into access negotiations with the provider of the declared service. This is not limited to the particular party that made the application for declaration. Other parties may also negotiate with the service provider for access to the declared service.
- 3.7 The objects of Part IIIA (see paragraph 3.10 below), the provisions governing both declaration recommendations and decisions and also the arbitration of access disputes explicitly recognise the relevant interests of the various parties affected. These interests include the service provider’s legitimate interest in preserving their use of a service and making a commercial return on their investment in infrastructure and other facilities. Part IIIA also allows for a broad consideration of the public interest that encompasses the likely effects of access on investment and economic efficiency. Declaration is only available in limited situations and, even if a service is declared, the specific terms and conditions of access will be determined through subsequent commercial negotiation. Recourse to regulation through the mechanism of ACCC arbitration is only available in the event of an access dispute that the parties cannot resolve through commercial negotiation. Further, the outcome of an ACCC arbitration determination may be that the access seeker does not gain access, notwithstanding that the service has been declared.

Legal requirements for declaration

- 3.8 The Council is responsible for considering applications for declaration. Under s 44G(2) of the Act, the Council cannot recommend that the designated Minister declare the service unless it is satisfied of all of the following matters:
- (a) access (or increased access) to 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 (**criterion (a)**)
 - (b) it would be uneconomical for anyone to develop another facility to provide the service (**criterion (b)**)
 - (c) the facility is of national significance, having regard to:
 - (i) the size of the facility; or
 - (ii) the importance of the facility to constitutional trade or commerce; or
 - (iii) the importance of the facility to the national economy**(criterion (c))**

- (d) access to the service can be provided without undue risk to human health or safety (**criterion (d)**)
- (e) access to the service is not already the subject of an effective access regime (**criterion (e)**)
- (f) access (or increased access) to the service would not be contrary to the public interest (**criterion (f)**).

3.9 Section 44F(4) of the Act requires that the Council also consider whether it would be economical for anyone to develop another facility that could provide *part* of the service. In respect of this Application, the Council's consideration of s 44F(4) is incorporated into its consideration of criterion (b) (see 6.42 to 6.45 below).

3.10 The Council's considerations are also informed by the objects of Part IIIA which are set out in s 44AA of the Act:

The objects of this Part are to:

- (a) promote the economically efficient operation of, use of and investment in the infrastructure by which services are provided, thereby promoting effective competition in upstream and downstream markets; and
- (b) provide a framework and guiding principles to encourage a consistent approach to access regulation in each industry.

3.11 Further information on declaration and the Council's assessment of declaration applications is available in the Council publication *Declaration of Services – A guide to Declaration under Part IIIA of the Trade Practices Act 1974 (Cth) (Declaration Guideline)*.³

³ Available on the Council's website at: www.ncc.gov.au/images/uploads/Declaration_Guide.pdf

4 Definition of Service

The Service sought to be declared

4.1 The Applicant describes the service for which it seeks declaration as follows:

The Service is ... the use of the facility comprising the narrow gauge cane tram network owned and operated by Sucrogen in the Herbert River district and which is approximately 530km in length.

The ... Service would also include the use of all associated infrastructure necessary to allow third party trains and rolling stock to move along the Network between points of interconnection, including, but not limited to:

- (a) tram track, associated track structures over or under track structures, supports (including supports for equipment or items associated with the use of the track);
- (b) bridges
- (c) passing loops
- (d) tram control systems, signalling systems and communication systems
- (e) sidings and refuges to park rolling stock, and
- (f) easements and other facilities which provide access to the tram route

(the **Service**). (Application, [2.6] – [2.7])

4.2 The Network extends throughout the Herbert River district. It is roughly bounded by Crystal Creek to the South, the Cardwell Range to the North, the seaboard to the East and Abergowrie and Upper Stone to the West. A map of the Network was provided as Appendix 1 to the Sucrogen Submission and may be viewed on the Council's website at <http://www.ncc.gov.au/images/uploads/DERaHRSu-009.pdf>.

Proposed use of the Service by the Applicant

4.3 The Applicant seeks access to the Service in order to transport sugarcane and other feedstock harvested within the Herbert River district to NQBE's proposed new factory (Application, [2.8]).

4.4 The Applicant submits that access to the Service is necessary to enable it to:

- (a) transport sugar cane harvested by growers within the Herbert River district from field to the NQBE factory;
- (b) transport other feedstock, such as timber and sorghum to the NQBE factory;

- (c) transport bio-fertilizer from the factory to the field; and
 - (d) transport sugar to the Lucinda bulk sugar terminal for export (Application, [2.10]).
- 4.5 The Applicant intends to acquire and operate its own locomotives and rolling stock to use on the Network (Application, [2.11]).

Service as defined in the Act

- 4.6 The term ‘service’ is defined in s 44B of the Act:

Service means a service provided by means of a facility and includes:

- (a) the use of an infrastructure facility such as a road or railway line;
- (b) handling or transporting things such as goods or people;
- (c) a communication service or similar service;

but does not include:

- (d) the supply of goods; or
- (e) the use of intellectual property; or
- (f) the use of a production process;

except to the extent that is an integral but subsidiary part of the service.

- 4.7 Where a service falls within one of the exceptions in the above definition in s 44B, the Council does not have jurisdiction to consider an application for declaration of that service under s 44F(1) of the Act.

Production process

- 4.8 Sucrogen submits that the Service is the use of a production process. It argues that the Service is therefore not a “service” within the definition of s 44B of the Act and cannot be the subject of an application for declaration under s 44F of the Act (Sucrogen Submission, [1.7]; [8.1-8.3]; and Annexure B).
- 4.9 Sucrogen also submits that ‘NQBE proposes to acquire the [Service] as an essential part of NQBE’s production process’ (Sucrogen Submission Annexure B at [7.16]) and that NQBE’s production process ‘amounts to a use of Sucrogen’s production process’ (Sucrogen Submission, Annexure B at [7.17]).
- 4.10 The extent of the production process exception in paragraph (f) of s 44B of the Act has been the subject of judicial consideration by both the High Court of Australia and the Full Court of the Federal Court of Australia. The High Court held in *BHP Billiton*

Iron Ore v NCC [2008] HCA 45 at [38] and [39] that it does not follow that because a service provider uses a service as part of its production process that the use of that service by an access seeker ‘would be excluded from the definition of “service” as being “the use of a production process”.’

4.11 The High Court went on to say (at [41]) that the issue is:

...whether the use of the service, which engages par(a) of the definition, to meet the needs of the access seeker also answers the description of the use by the access seeker of [the provider’s] production process. What Fortescue seeks is the use of a facility that BHPBIO uses for the purpose of its production process. That use does not fall within par (f) and so does not deny the operation of the definition in s 44B and the engagement of Pt IIIA.

4.12 While the High Court did not expressly comment on the earlier decision of the Full Court, it made reference (at [43]) to a production process ‘...involving the use of integers’ and where ‘...an access seeker wishes to utilise [those integers] for its own purpose [that] does not deny compliance with the definition of “service”. In the Full Court decision (*BHP Billiton Iron Ore Pty Ltd v National Competition Council* [2007] FCAFC 157), the majority found (at [175]) that the phrase ‘the use of a production process’ does not include a step in a production process.

4.13 In the Full Court decision, Justice Greenwood (with whom Sundberg J agreed) went on to say (at [175]) that:

...it seems that Parliament’s election not to introduce words of express choice indicate that the production process exclusion is to operate only in circumstances where the service sought by the third party is the use of the integrated sequence of operations comprising the production process as found on the facts and not any one of those steps.

4.14 The Council accepts that the transportation of sugarcane is part of the process for the production of sugar in the Herbert River and in all sugar growing regions.

4.15 In the Council’s view, the circumstances in the present Application are akin to those before the Full Court and the High Court. While Sucrogen’s transportation and crushing of sugarcane is, for a variety of reasons, a highly vertically integrated operation, it is not inevitable that sugarcane transportation and milling be undertaken by a fully integrated entity.⁴ The transportation of sugarcane is an integer or part of the production process employed by Sucrogen and may be provided as a separate and distinct function. The fact that NQBE proposes to use the Service to transport sugarcane for the purpose of crushing such cane in order to produce sugar or other commodities does not amount to use of Sucrogen’s production process.

⁴ Synergies Report (Annexure E to the Sucrogen Submission) states at p 27 – ‘It is therefore considered that it is not strictly necessary for the same entity to perform the sugarcane crushing and transportation functions.’

4.16 The Council considers that it is not prevented from dealing with this application on the grounds that the Service constitutes the use of a production process for the purposes of the exception in paragraph (f) of the definition of 'service' in s 44B of the Act.

5 Criterion (a) – Promotion of competition

Legal requirements

- 5.1 Section 44G(2)(a) (**criterion (a)**) provides that the Council cannot recommend that a service be declared unless it is satisfied that access (or increased access) to the service would promote a material increase in competition in at least one market other than the market for the service (a “dependent market”). An increase in competition will be material if it is not trivial.⁵
- 5.2 The right to access that may result from declaration is not limited to the party which made the application for declaration. Consequently, the assessment of the competitive effects of access is concerned with the process of competition and the effect of access in general. Whether criterion (a) is satisfied does not turn on the commercial interests or pursuits of the particular applicant for declaration or other individual market entrants.
- 5.3 The inquiry for the Council is a comparison of the future state of competition in the dependent market with a right or ability to use the service and the future state of competition in the dependent market without any right or ability to use the service.⁶ The test is not whether *declaration* would promote a material increase in competition, but whether *access*, in the ordinary sense of that word, would promote a material increase in competition.⁷
- 5.4 Accordingly, in assessing whether criterion (a) is satisfied, the Council:
- identifies whether there is one or more dependent (upstream or downstream) markets;
 - considers whether the dependent markets exist separately from the market for the service to which access is sought, and
 - assesses whether access (or increased access) would promote a materially more competitive environment in any dependent market thereby promoting a material increase in competition in that dependent market.

The dependent market(s)

- 5.5 Markets are commonly defined in terms of their product (or service), geographic, functional and temporal dimensions:

⁵ Trade Practices Amendment (National Access Regime) Bill 2005 (Cth), Explanatory Memorandum at item 16, and p 21.

⁶ *Sydney Airport Corporation Ltd v Australian Competition Tribunal* [2006] FCAFC 146, [83].

⁷ *Sydney Airport Corporation Ltd v Australian Competition Tribunal* [2006] FCAFC 146, [81]-[83].

- The *product/service* dimension of a market identifies the set of product(s) and/or service(s) that are sufficiently substitutable to be traded in a relevant market as defined.
- The *geographic* dimension of a market identifies the area within which substitution in demand and supply is sufficient for the product(s)/service(s) traded at different locations to be considered in the same market.
- The *functional* dimensions of a market describe the market in terms of the function being considered (such as manufacturing, distribution, wholesaling or retailing). This is often highly relevant to consideration of declaration applications where the owner of monopoly infrastructure is vertically integrated.
- A *time* related dimension can also be relevant to market definition in some circumstances, although this is less likely in the context of Part IIIA where markets usually involve long lived assets and shorter term market conditions are less likely to be relevant.

5.6 Separate product or service markets exist if their respective products or services are not strongly substitutable for one another. Similarly, separate geographic markets may exist where products or services in one geographic location are not strongly substitutable for those in another location. Where two or more markets are characterised by a common product or service or geographic area, they may still be separate markets where they involve transactions at different functional levels. For markets to be regarded as functionally separate, vertical integration must not be inevitable (the 'economic separability test'). The joint economies of scope and transaction costs involved in the separate provision of the product or service must not be so large as to preclude separate provision. In addition, for functional levels to be distinct, each must involve assets that are sufficiently specific and distinct that assets used to produce an output at one level cannot readily produce an output at another level (the 'asset specificity test').

Application and Submissions

- 5.7 The Applicant submitted that access to the Network would promote a material increase in competition in the following dependent markets:
- (a) the market for processing sugarcane in the Herbert River district
 - (b) the market for growing sugarcane in the Herbert River district
 - (c) the market for ethanol in Australia
 - (d) the market for the supply of electricity in Northern Queensland (Application, [8.11]).
- 5.8 The Applicant argued that the sugarcane processing market is distinct from the market for the Service because the costs of vertically separating the Service from

processing sugar do not preclude a separate market or dictate that the activities must be performed within the same entity. It said that the assets required for processing are distinct from those for providing track services. The Applicant said that the market for processing sugarcane is separate from the market for growing sugarcane and the fact that Sucrogen processes but does not grow sugarcane is evidence that the costs of separation do not preclude the existence of a separate market. It also said the assets required are distinct in each of the processing and growing markets (Application, pp 16–18). The Applicant argued that there is a separate market for ethanol in Australia, evidenced by ethanol mandates and targets imposed by State Governments (Application, [8.55]). It also said that North Queensland is a net importer of electricity from the National Electricity Market (**NEM**) and is a long way from base load generation in the south of the State (Application, [8.79] – [8.81]).

- 5.9 Sucrogen relies on the analysis in the Synergies Report, summarised in 5.10 below, adding that there is a national market for electricity, with a Queensland regional sub-market, assuming the Council is satisfied such a separate market exists.
- 5.10 The Synergies Report states that the relevant dependent markets for assessing potential competitive effects are:
- (a) a sugarcane production and sales market (in the Herbert River district)
 - (b) a sugarcane processing market (in the Herbert River district)
 - (c) a national fuel sales market
 - (d) a national electricity sales market
 - (e) an international sugar sales market
 - (f) a market for sugar terminal services in the Port of Lucinda
 - (g) an international shipping services market (Synergies Report, p 35).
- 5.11 Sucrogen said that the sugarcane production/sales and processing markets are geographically constrained to the Herbert River district because of the costs and CCS losses incurred in the movement of sugarcane between regions (Synergies Report, pp 37 and 42).
- 5.12 The Council does not propose to expound on the structure of and nature of competition in the international sugar sales, Port Lucinda terminal services or international shipping services markets as no competitive effects from access have been asserted in the Application or in submissions. The Council does not consider that it is likely that access to the Service will have any material effect on competition in these markets.
- 5.13 The Canegrowers Submission did not specifically identify a dependent market, but expressed the organisation's support for 'the provision of competition for the

purchase of sugarcane generally, and in the Herbert River specifically.’ It expressed the view that such competition is

...not possible at present because the nearest mill owned by a company other than [Sucrogen] is Tully Mill, which, at 97km distance, is too far away for sugar to be transported economically.

The Council’s view on dependent markets

5.14 The Council considers that the most relevant markets dependent upon the Service are the markets for:

- (a) acquisition and processing of sugarcane in the Herbert River district;
- (b) national supply of ethanol; and
- (c) wholesale supply of electricity across the NEM.

5.15 The market for the Service is the market for the use of the below-rail infrastructure comprising the Network. This market is separate from the three markets listed in 5.14 above.

5.16 The Synergies Report states that:

Despite the magnitude of the complementarities associated with operating a vertically integrated processing and transport operation, it does not appear that these preclude the separation of some of these functions from a management perspective in all circumstances. It is therefore considered that it is not strictly necessary for the same entity to perform the sugarcane crushing and transportation operations (Synergies Report, p 27).

5.17 The Council does not believe that the degree of integration of the Service with the process of milling sugarcane is such that the two must invariably be undertaken by one entity. The Council also notes that the assets required to provide cane railway services (including track, bridges, sidings, passing loops and signalling, communication and control systems) and sugarcane milling (a sugar mill) are distinct. In the Council’s view, the market for the acquisition and processing of sugarcane in the Herbert River district is separate from the market for the Service. As the supply of ethanol and electricity are consequent upon the processing of sugarcane, it follows that the markets for the supply of electricity and ethanol are also separate from the market for the Service.

5.18 The Council considers that the markets for sugarcane growing and sugarcane production and sales, alleged by the Applicant and Sucrogen (via the Synergies Report) respectively, are substantially the same market for the purposes of the Application. Access may affect a grower’s decision to begin or continue growing sugarcane rather than an alternative crop because a miller’s ability and capacity to efficiently process harvested cane can affect a grower’s returns. However, the Council

considers that the relevant market in which to assess the competitive effects of alternative land uses is the market for sugarcane acquisition and processing.

The market for sugarcane acquisition and processing

- 5.19 The Council considers that the product/service dimension of the market is appropriately characterised as a market for the acquisition by millers of sugarcane cut for processing.
- 5.20 The geographic dimension of the market is the Herbert River district. The Application and the Sucrogen Submission (including the Synergies Report) both support this conclusion. The requirement to crush sugar cane as soon as possible after harvesting (within 16-24 hours) in order to minimise loss of CCS content constrains the area available to supply sugarcane to a particular mill, and the Council understands that in any case harvested sugarcane is not transported into or out of the Herbert River district. Further, the Network does not connect with any facilities outside the Herbert River district.

Application and Submissions

- 5.21 The Applicant submits that growers in the Herbert River district have no option but to sell their sugarcane to Sucrogen (Application, [8.37]). It claims that road transportation of sugarcane is not a substitute for transportation using the Service and that access is necessary to make development of a competing mill economic. The Applicant claims that access will enable innovation in processing and in the production of ethanol, co-generation and bio-fertilisers, using sugarcane (including energy canes in 5-10 years), timber and sorghum as feedstocks. The Applicant argues that, unlike its proposal, Sucrogen uses aged equipment and only produces raw sugar and molasses. The Applicant claims that with access it will be able to allow growers to participate in additional revenue streams from electricity, bio-fertilisers and ethanol (Application, [8.24] – [8.32] (referring to [7.32] – [7.41] in respect of road transport)).
- 5.22 Sucrogen submitted that the Application assumes that Sucrogen is not competitively constrained in sugarcane markets. It said that it disagreed with this assumption, and asked the Council to note that there is no material difference in the cane payment formula used by Sucrogen in the Herbert River district and that used in the Plane Creek area where Sucrogen competes for sugarcane with Mackay Sugar. It said that this further demonstrates that the Applicant's underlying premise that more mills in the Herbert River district would lead to more price competition was not well-founded (Sucrogen Submission, [3.33] – [3.36]).
- 5.23 The Synergies Report concedes that a move from a monopsony to a duopsony would appear to increase competition in the sugarcane processing market. However, it argued that, given the short haulage distances in the Herbert River district and as road transport is used by other mills in Queensland and New South Wales, road

transport competes with rail. Access to the Service is, therefore, not necessary to promote competition in the sugarcane processing market (Synergies Report, pp 43–44). The Synergies Report also expressed the view that Sucrogen’s market power is constrained because:

- (a) Growers are not locked into long term agreements with Sucrogen
- (b) returns to Growers are determined by the cane price formula
- (c) Sucrogen has incentives to maximise throughput at its mills, and
- (d) Growers can switch to alternative land uses which risks stranding mills.

5.24 In its analysis of the sugarcane production and sales market, the Synergies Report said that the key factor affecting market entry by growers is the economic returns achieved from sugarcane relative to alternative land uses. It said that access would not be a critical factor. The Synergies Report said that sugar returns are determined by international raw sugar prices in a competitive international market because all Herbert River sugar is exported in raw form. It questioned whether the additional income flowing to growers under the Applicant’s proposal would be either sustainable or large enough to materially increase in competition given that (as the Applicant had effectively acknowledged) entry by the Applicant would simply divide existing sugarcane volumes amongst mills rather than increase production. It concluded that lack of access should not prevent the Applicant from competing in the sugarcane processing market and there are other more important barriers (Synergies Report, pp 36–38).

5.25 In its submission, Canegrowers expressed support for the competitive purchase of cane by millers but noted that this is not currently possible because the nearest mill that could compete with Sucrogen (Tully Mill) is too far away for economical transport. Canegrowers expressed the view that competition must be sustainable, and that it is necessary to understand the Applicant’s financial situation in order to determine the organisation’s overall view.

The Council’s assessment of the sugarcane acquisition and processing market

5.26 The Council is satisfied that access to the Service would promote a material increase in competition in the market for the acquisition and processing of sugarcane in the Herbert River district. Sucrogen is currently the only purchaser of sugarcane in the district, and the Council considers that there is little or no likelihood of competition in the market for sugarcane acquisition and processing without access to the Service.

5.27 Sucrogen argued that the Applicant is already able to compete in the market because road is a viable alternative to the Service. It was noted by the Council that, in Queensland, a number of sugar mills use a combination of rail and road transport and 3 operate road transport only (LRRSA 2009), while in New South Wales (and Western Australia until 2007 when sugar production ceased in that State) all sugarcane is

transported by road (Queensland Sugar Corporation 1998, p 6). The Council understands that a 'greenfield' sugar mill development would be unlikely to be serviced by a new cane railway, and notes that the most recently developed mill—Tableland Mill near Mareeba in Northern Queensland (commissioned in 1998)—is fully serviced by road transport. However, the Council also notes that Tully Sugar Limited (**Tully Sugar**) is planning to extend its cane railway by approximately 6.5km to access new cane areas, displacing existing road transport in the process (Tully Sugar 2009). The Council does not consider that road transport is a viable substitute for rail transport in districts where a rail network already exists. In the Council's view, it is unlikely that the operator of a new sugarcane processing facility could compete effectively in the market for sugarcane acquisition and processing in the Herbert River district using road transport.

- 5.28 The Council notes that access would be unlikely to result in an increase in sugarcane production, at least in the short to medium term. The Applicant claims that access will facilitate the introduction of 'energy canes' in the Herbert River district, leading to increased yields. The Council is of the view that the nature of any increased yields appears uncertain and, in any case, the introduction of 'energy canes' is at least 5 years away. Accordingly, the potential production increase from the introduction of 'energy canes' does not have a substantial effect on the Council's assessment of criterion (a) in relation to the Application.
- 5.29 Sucrogen (through the Synergies Report) argued that its power in the market for the acquisition of sugarcane is constrained by the cane price formula and because there is no 'take or pay' component Sucrogen bears the volume risk with the supply of sugarcane. The incentive to maximise throughput at its mills was said to provide a strong incentive to contract with growers at prices that ensure quantity and quality of production. In addition, as growers are able to switch land uses, Sucrogen has an incentive to maintain volumes to prevent stranding of its mills (Synergies Report, p 43).
- 5.30 The Council understands that the majority of mills throughout Queensland employ substantially the same cane payment formula, which factors in the CCS content of the grower's sugarcane and the international market price for raw sugar and apportions the total approximately one third to the mill and two thirds to the grower.⁸ However, the Council does not consider that the use of the formula is inevitable, notwithstanding its broad industry acceptance. For example, the Council understands that Mackay Sugar Limited employs a formula that provides growers with a share of revenue from sugar, molasses and electricity. Further, the Council understands that since the reform of regulation of the sugar industry, there has been significant

⁸ The Synergies Report at p 38 gives the following formula for the Herbert River district: \$/tonne cane = 0.009 * World sugar price * (CCS - 4) + 0.6353. '0.009' is a factor for the extraction of sugar from the cane. The CCS is the sugar content of the grower's sugarcane, with four units retained by the mill, and the constant is a negotiated amount.

innovation in pricing options for growers, who are now, subject to the terms of their supply agreements with mills, able to participate in a range of pricing options. Sucrogen, for example, has introduced a sophisticated forward pricing system that gives growers some control over the raw sugar price component of the cane payment formula. The Council also understands that 'off-formula' payments, such as bonuses and incentive payments, may be made in response to actual or threatened competition for sugarcane from competing mill operators (in those regions where more than one mill company operates) or from alternative land use by growers.

- 5.31 Although access may not result in a substantial increase in production in the short to medium term, the Council considers that access would create an environment in which the presence of or threat of entry by a competing miller in the Herbert River district would promote competition in the form of innovative sugarcane pricing and in growers receiving a higher proportion of returns from sugarcane.

The market for ethanol

- 5.32 The Council considers that the product dimension of the market is ethanol. Although international ethanol prices affect Australian ethanol prices, the Applicant and Sucrogen (Application, [8.70]; Synergies Report, p 45) agreed that demand is primarily driven by government-mandated fuel content. As ethanol produced in the Herbert River district would most likely be blended with conventional fuel for sale within Australia to meet demand arising from mandated ethanol content, the relevant geographic dimension for present purposes is a national Australian market. The appropriate functional level is the manufacture and supply of ethanol.

Application and Submissions

- 5.33 The Applicant submitted that ethanol is derived from starch-rich feedstocks and molasses and can also be extracted from lignocellulosic materials where the plant matter is first converted to sugars (Application, p 20). It claimed that it plans to invest in 'energy canes' which have the capacity for higher fibre content and higher crop yield that can be used to produce increased volumes of ethanol. The Applicant argued that, as Sucrogen is not planning to invest in 'energy cane' development, without access the amount of ethanol produced in the Herbert River district would remain constant. (Application, p 24)
- 5.34 The Applicant argued that although Brazil is a major ethanol producer, there are barriers to imports due to limited availability of chemical bulk carriers, the large freight costs and rising domestic consumption. It argued that the threat of ethanol imports from Brazil may only act as a ceiling on Australian prices. (Application, p 22) According to the Applicant, Australian potential 2010 capacity of 480ML is below expected demand (for which it gave a combined figure for New South Wales and Queensland of 655ML) and that access will allow the Applicant to produce ethanol in excess of the amounts already produced (Application, p 23).

- 5.35 Sucrogen argued that the ethanol market is currently competitive because there are three domestic ethanol producers, plus imports, and there are low barriers to entry (Synergies Report, pp 45-46). It argued that government policy and competitiveness with Brazil and traditional fuels are more significant factors in the ethanol market than access to the Service and, given the range of potential ethanol feedstock, access itself will not materially increase competition. According to Sucrogen, the major constraint on ethanol production in the Herbert River district is the limited supply of sugarcane. It submitted that 'energy cane' development is contingent on factors unrelated to declaration (Synergies Report, pp 46-48).
- 5.36 In its submission, Canegrowers noted that it is not aware of any contribution by the Applicant to 'energy cane' research and that indications from work done to date are that the increased fibre content of energy canes is likely to lead to a reduction in sugar content.

The Council's assessment of the ethanol market

- 5.37 A key consideration in the assessment of the likely competitive effect of access is the ability and incentive of the owner of the asset to exercise market power. The Council does not consider that Sucrogen is able to exercise market power in the market for ethanol. The market is competitive as there are currently three ethanol producers in Australia (including the Sarina Distillery owned by a related body corporate of Sucrogen) and there are substantial imports of ethanol.⁹ In addition, the principal factors affecting entry into or expansion in the ethanol market are government mandates as to fuel content, the cost of production in Australia relative to ethanol import prices and the relative returns of ethanol and raw sugar.
- 5.38 The Applicant submits that it will produce additional ethanol from sugar by-products, including all of the molasses it produces and lignocellulosic material. It submits that the higher fibre content of 'energy canes' can be used to increase ethanol production. However, the Council is not satisfied, at least in the short to medium term, that any additional ethanol produced from sugar by-products in the Herbert River will be sufficient to have a material impact on the national market for ethanol.
- 5.39 The Council considers that access would not promote a material increase in competition in the ethanol market.

The market for electricity

- 5.40 The Council considers that the relevant market is the national market for the supply of electricity.

⁹ The Synergies Report (at p 47) said that 2008 imports were 49ML. The Application ([8.62], citing the ABS) said imports were 176ML and 205ML in 2007 and 2008 respectively.

- 5.41 The Applicant submitted that its production of electricity will promote competition in the market for the supply of electricity in North Queensland. It argued that North Queensland is a long way from base load generators in the south of the State so prices are materially impacted by transmission loss factors and any new generation in North Queensland will increase supply and potentially lower prices. The Applicant claims that its plant will export 50-55MW to the market over 300 days a year (Application, [8.79] – [8.81]).
- 5.42 Sucrogen argued that the electricity market is national, although there is a Queensland pool price (Sucrogen Submission [3.42]). The report by ROAM Consulting (**ROAM Report**), which was annexed to the Sucrogen Submission, concluded that 50-55MW would generate 360-396GWh per year. The ROAM Report said that the main effect of this generation would be to offset 80% of one year's increase in Marginal Loss Factors in North Queensland, which is not a material effect on North Queensland's supply. According to the ROAM Report, another effect is to offset about 12% of one year's demand growth in Queensland, which is a relatively low level of benefit in the market. It added that connecting 50-55MW at Ingham would require augmentation of the distribution network.

The Council's assessment of the electricity market

- 5.43 The Council is not satisfied that access will promote a material increase in competition in any dependent electricity market.
- 5.44 The Federal Court found that the market for electricity was NEM-wide when it considered the acquisition by AGL of an interest in the Loy Yang A power station.¹⁰ In the NEM, electricity is traded through a central pool, and an additional 50-55MW in North Queensland would have virtually no effect in a market based on the NEM.
- 5.45 Using the purposive approach¹¹ to market definition, the ACCC recently considered the competitive effects of a suite of agreements relating to the Gladstone Power Station in the context of a Queensland based geographic market (ACCC 2010, [4.6] – [4.9]). The ACCC found (at [4.69]) that 810MW of exportable capacity would be unlikely to enable the applicants for authorisation to affect the price of wholesale electricity supply in Queensland. While the ACCC's findings are not determinative in the present matter, they indicate that 50-55MW, which is less than 10% of the capacity of the Gladstone Power Station, would be extremely unlikely to have a material effect on prices or competition in a Queensland-wide electricity market.
- 5.46 The Applicant argued that the relevant market for the Council to consider is a North Queensland market. However, even to the extent that it may offset increases in Marginal Loss Factors or demand growth in North Queensland, the Council considers

¹⁰ *Australian Gas Light Company v ACCC (No 3)* [2003] FCA 1525.

¹¹ See: *Queensland Wire Industries Pty Ltd v BHP* (1989) 167 CLR 177, 195 (Deane J).

that the Applicant's claimed additional generation capacity will not be sufficient to have any material effect on electricity prices in North Queensland.

Other issues raised by Sucrogen

5.47 The Council has considered the extensive submissions by Sucrogen in respect of:

- the viability of the Applicant's proposal to build a sugar mill in the Herbert River district; and
- Sucrogen's inability to provide an integral part of the Service (ie the benefit of the various arrangements by which Sucrogen has access to land over which the Network runs, which, for convenience, will be referred to as **Network Easements**).

Viability of the Applicant

5.48 Sucrogen argues that the Council cannot be satisfied in respect of criterion (a) because the Applicant's enterprise is unlikely to come into existence. In addition to access to the Service, Sucrogen alleges that the Applicant faces the following obstacles to the establishment of its mill:

- (a) the need for development approval from the Hinchinbrook Shire Council;
- (b) the availability of alternative feedstocks;
- (c) the moratorium on water rights for the Wet Tropics catchment area;
- (d) enforceability of cane supply agreements;
- (e) land access (considered further at 5.53 below);
- (f) financing; and
- (g) electricity connection, offtake and other agreements (Sucrogen Submission, pp 10 – 13).

5.49 Sucrogen also asserts that for a project valued at \$400 million (as the Applicant claims for its proposed mill), a bankable feasibility study would require expenditure of around \$20 million (Sucrogen Submission, [3.26]).

5.50 The Council has in previous declaration recommendations expressed the view that it is not necessary for an applicant for declaration to present a detailed business plan as to its proposed use of the relevant service to make out a case for declaration.¹² The task of the Council is not to assess the viability of an applicant's business plan, but to assess whether the service sought meets the criteria for declaration. This has also been consistently held by the Tribunal.¹³ In the Council's view it would frustrate the

¹² See for example NCC 2004 at [10.7]; NCC 2008 at [9.110].

¹³ *Re Sydney International Airport* [2000] ACompT 1 at [19]; *Re Services Sydney Pty Ltd* [2005]

purpose of Part IIIA if an applicant is required to develop a full business model before the availability of access to the service has reached a sufficient level of certainty. Indeed under the provisions of Part IIIA it is entirely possible that a party which ultimately obtains access resulting from a declaration application may not be the Applicant.

5.51 Sucrogen acknowledged that if the Service is declared, it is declared for all access seekers and not just the Applicant, but argued that it was appropriate for the Council to focus on the Application because:

- (a) the issues facing the Applicant would be faced by any access seeker;
- (b) no other party has sought access to the Service and the Applicant is likely to be the only access seeker; and
- (c) due to the constraints on the supply of land suitable for sugarcane in the Herbert River district, a third mill is not economically viable (Sucrogen Submission, [2.6] – [2.11]).

5.52 In *Re Sydney International Airport* [2000] ACompT 1 at [19], the Tribunal found that the financial viability of an access seeker is not relevant to declaration (the ‘first stage’ of the National Access Regime) but may become relevant at the stage where a party is negotiating access or seeking to have the issue of its access arbitrated by the ACCC. The Tribunal also found (at [21]) that the analysis of the promotion of competition

is not made by reference to any particular applicant seeking to have a service declared. At the point of time at which a decision is to be made as to whether or not to declare a service under s 44H,¹⁴ it may not be known who will be seeking access if the relevant service is declared.

5.53 Accordingly, the Council is of the view that the financial viability of the Applicant is not relevant to its consideration of the Application.

Network Easements

5.54 The Applicant defined the Service to include (among other things) ‘easements and other facilities which provide access to the tram route’ (Application, [2.7]). Sucrogen submitted (Sucrogen Submission, p 18) that without the benefit of the Network Easements, the Applicant could not legally operate trams on the Network. It argued that:

ACompT 7 at [136].

¹⁴ The criteria under s 44H are expressed in the same terms as s 44G, but apply to the decision by the designated Minister, following receipt of the Council’s recommendation, whether or not to declare a service (footnote not in original).

- (a) Sucrogen neither owns nor operates the Network Easements and does not have the right to permit the Applicant to have the benefit of the Network Easements; and
- (b) it is beyond the power of the Council to recommend declaration of, and beyond the power of the Minister to declare, the Service including the benefit of the Network Easements because an easement is not a 'facility' and the benefit of an easement is therefore not a 'service' within the meaning in Part IIIA.

5.55 The Council does not consider that point (a) is an impediment to declaration. Third party rights and regulatory requirements may be relevant to the Council's consideration of criterion (a) where they present an insurmountable obstacle to or effective prohibition on access.¹⁵ In the *Lakes R Us* final recommendation, for example, the Council's view was that for declaration to have any practical effect fundamental changes to the nature and scope of property rights relating to water were necessary, and there would need to be renegotiation of, and unanimous agreement between, three States and the Commonwealth on the modification of the Murray-Darling Basin Agreement. The Council doubted that such changes would be made and concluded that there was unlikely to be any practical effect on competition following declaration (NCC 2005 at [6.9]-[6.11]). In contrast, changing the identity of the owner of the trains using the land pursuant to a Network Easement and the mill to and from which those trains travel (assuming that such changes are in fact necessary) cannot be said to amount to fundamental changes to the nature and scope of the land owners' property rights. The Council considers that the specifics of access may be addressed through negotiation between the parties or arbitration by the ACCC.¹⁶ If necessary, recourse may also be had to the *Sugar Industry Act 1999* (Qld) which provides for the granting to mill owners¹⁷ of permits to pass or easements 'to facilitate harvest of cane and supply of cane to any mill or between any mills.'¹⁸ The Council considers that to find that the terms of the Network Easements are an insurmountable obstacle to or effective prohibition on access would risk frustrating the purposes of Part IIIA as it would allow infrastructure owners to avoid declaration by contractual agreement.

5.56 The Council does not accept Sucrogen's argument in respect of point (b) at 5.54 above. The term 'facility' is not defined for the purposes of Part IIIA, but was considered by the Tribunal in *Re Sydney International Airport*[2000] ACompT 1. The Tribunal said (at [82]) that:

¹⁵ See eg: *Re Services Sydney Pty Ltd* [2005] ACompT 7 at [136] and [158].

¹⁶ Section 44W(1)(c) prevents the ACCC from making a determination that would deprive any person of a protected contractual right.

¹⁷ The Council notes that the relevant provisions refer to 'mill owners' rather than owners or operators of cane railways.

¹⁸ *Sugar Industry Act 1999* (Qld), ss 63(2)(b) and 63(5).

a facility for the purposes of the Act is a physical asset (or set of assets) essential for service provision

and (at [192]) that

[a] key issue is the minimum bundle of assets required to provide the relevant services subject to declaration.¹⁹

5.57 Sucrogen submitted that the term ‘facility’ should be understood as being synonymous with physical infrastructure and that, being interests in land, the Network Easements cannot be declared (Sucrogen Submission, [4.20] – [4.28]). The Council considers that the Network Easements need not themselves constitute a facility. To the extent that they are relevant to the Council’s consideration of the present Application, they may be characterised as part of the ‘bundle of assets’ required for provision of the Service. As noted at 5.55 above, the Council considers that the negotiation or arbitration of the specific terms of access is the domain of the second stage of the National Access Regime.

Preliminary conclusion on criterion (a)

5.58 The Council is satisfied that access to the service will promote a material increase in competition in at least one market other than the market for the Service, being the market for the acquisition of sugarcane in the Herbert River district.

¹⁹ See also: *Re Services Sydney Pty Ltd* [2005] ACompT 7 at [12].

6 Criterion (b) – Uneconomical to develop another facility

Legal requirements

- 6.1 Section 44G(2)(b) of the Act (**criterion (b)**) requires the Council to be satisfied that ‘it would be uneconomical for anyone to develop another facility to provide the service’ sought to be declared. This criterion seeks to ensure that declaration is limited to situations where the development of additional facilities would increase costs, waste resources and generally be contrary to Australia’s national interest.
- 6.2 Criterion (b) is concerned with Australia’s national interest not the private interests of any particular party or parties. To date the Council and the Tribunal have consistently found that the appropriate test for assessing whether criterion (b) is met is a social test. That is to say that the term ‘uneconomical’ should be construed in a social cost benefit sense rather than in terms of private commercial interests. In *Re Sydney International Airport* [2000] ACompT 1 at [205] the Tribunal explained that:

If ‘uneconomical’ is interpreted in a private sense then the practical effect would often be to frustrate the underlying intent of the Act. This is because economies of scope may allow an incumbent, seeking to deny access to a potential entrant, to develop another facility while raising an insuperable barrier to entry to new players (a defining feature of a bottleneck). The use of the calculus of social cost benefit, however, ameliorates this problem by ensuring the total costs and benefits of developing another facility are brought to account.

Natural monopoly

- 6.3 The assessment of criterion (b) centres on identifying whether a facility exhibits natural monopoly characteristics such that a single facility is capable of meeting likely demand at lower cost than two or more facilities. In such circumstances it is uneconomical to duplicate the facility and society’s resources are most efficiently used and costs minimised if additional facilities are not developed. In *Re Duke Eastern Gas Pipeline Pty Ltd* [2001] ACompT 2 the Tribunal stated at [137] that:

[the] test is whether for a likely range of reasonably foreseeable demand for the services provided by means of the pipeline, it would be more efficient, in terms of costs and benefits to the community as a whole, for one pipeline to provide those services rather than more than one.

- 6.4 In this way, criterion (b) limits declaration to the services of facilities with natural monopoly characteristics. The key characteristics of a natural monopoly relate to the nature of costs and investments. Facilities that exhibit natural monopoly characteristics will involve large and lumpy investment costs and the presence of significant economies of scale and/or economies of scope. It is generally accepted

that a natural monopoly is more likely to exist where capital costs are large relative to variable costs (implying high average costs compared with marginal costs).

Application and submissions

The Application

- 6.5 The Applicant submitted that the Service satisfies criterion (b) because it is capable of meeting likely foreseeable demand and the costs and other barriers to constructing a duplicate facility to provide the Service are prohibitive (Application, [7.5]).
- 6.6 The Applicant submitted that the costs involved in duplicating the facility are substantial. Construction costs alone per kilometre of rail could be expected to fall within the range \$145,000-\$315,000. The Applicant's estimate for duplicating the Network was in excess of \$77 million. This estimate was based on the lower figure in the range of construction costs and the Applicant noted the estimate was not all-inclusive (Application, [7.7]-[7.10]).
- 6.7 There exist other barriers to the construction of a duplicate facility. The Applicant submitted that a duplicate facility could not be constructed without first obtaining access to appropriate land via the creation of easements or some other means to facilitate passage. Environmental considerations and compensation for the landholders could also reasonably be anticipated in reserving land for the future construction of all or part of the Network.

Sucrogen Submission

- 6.8 Sucrogen submits that criterion (b) is not satisfied. In support of this Sucrogen relies on the Synergies Report that identifies road transport as a source of supply-side substitution for sugarcane and raw sugar transport in the Herbert River district. It submits that it is therefore economic to duplicate the service by using road transport. Sucrogen notes further that road transport is the sole source of cane transport in 24% of Australian sugar mills and the sole source of transport in other sugar producing countries, notably Brazil (Sucrogen Submission, [6.4]-[6.6]).
- 6.9 The Synergies Report argues that road is a substitute for use of the Network, and that road haulage of sugarcane can be achieved efficiently at a lower cost per tonne than haulage by rail (Synergies Report, pp 24-25,27, 30 and 33).

Alternative facilities that could provide the Service

- 6.10 The Council is of the view that Sucrogen's submissions on the substitutability of road for rail in the context of criterion (b) are misconceived.

- 6.11 The Network is the only railway in the Herbert River district transporting sugarcane from Growers to the two existing Sucrogen mills. In considering whether there exist alternative facilities that could provide the Service, it is important to focus on the Service that has been applied for. The Application is for a below rail service upon which, if declared, the Applicant will seek to run its own rolling stock.
- 6.12 While other facilities, such as road, may exist and be capable of transporting sugarcane, such facilities are not the Service for which declaration is sought. The only possible alternative facility that could provide a part of the Service is part of the railway line of Queensland Rail which runs in a north/south direction, through the township of Ingham in close proximity to the Bruce Highway. While the below rail infrastructure of the Queensland Rail line could potentially be used to run the Applicant's rolling stock, it does not provide the network to access Growers fields and harvest points required in the Application for an all-points service and is, therefore, not an alternative facility that could provide the Service.
- 6.13 The Council considers that road transportation of sugarcane at best serves as a complement for areas that are within a short distance of the mill or factory and for areas remote from rail sidings or that are otherwise unsuitable for rail.

Foreseeable demand for the Service

Transportation of sugarcane

- 6.14 Demand for the service is currently driven by both the capacity of the two mills presently served by the Network (Victoria and Macknade mills, both owned and operated by Sucrogen) and the quantum of sugarcane produced in the Herbert River region. Demand for the service is seasonal, with the peak utilisation period occurring during the sugarcane harvest, which runs from around June to November each year. Depending on seasonal conditions, the Network currently transports approximately 4-4.5 million tonnes of sugar cane from harvest collection points to one of the two Sucrogen mills.
- 6.15 The Applicant submits that there is unlikely to be an increase in the amount of cane transported on the Network if the service is declared and access obtained. The Applicant's business proposal involves competing with Sucrogen for the purchase of the current annual tonnage of sugarcane produced in the Herbert River district. The Applicant intends to purchase approximately 2.1 million tonnes of sugarcane from Growers and transport that cane on the Network from a harvest collection point to the Applicant's mill, which is to be constructed at a designated site near Ingham, approximately 2 kilometres from a point on the Network.²⁰ As this tonnage will be at

²⁰ Should declaration occur and access be obtained the Applicant will need to construct a spur line to connect its mill to a point on the Network, the exact location of the interconnection to be determined as one of the terms and conditions of access.

the direct expense of the amount of sugarcane Sucrogen currently acquires and transports on the Network, the total amount of cane to be transported on the Network by both the Applicant and Sucrogen will remain unchanged and is expected to reflect historical levels, subject to seasonal variations.²¹

Transportation of other crops

- 6.16 The Applicant submits that in addition to the transportation of sugarcane on the Network it intends to use the Service outside of the harvest season to 'haul other feedstock such as woodchip and sorghum' (Application, [7.23]). The Council understands that the Network is largely unutilised from December to May, save for maintenance, repairs and upgrades by Sucrogen. While the ability to source and transport other feedstock on the Network may be open to question, it would appear that there may be sufficient capacity outside of the harvest season for other crops to be transported on the Network and such arrangements may be negotiated in response to any specific request for access should the Service be declared.
- 6.17 The Council is of the view that the transportation of other crops should not be a factor in the consideration of the foreseeable demand for the Service because any such demand is likely to be at the periphery of the foreseeable demand for the service which is for the transportation of sugarcane during the June – November sugarcane season.

Energy canes

- 6.18 The Applicant provided information to suggest that Growers may be able to diversify their crops using 'energy canes'.²² It argues that, if energy canes were introduced, sugarcane production in the Herbert River district could expand from 4-4.5mtpa to about 6-7mtpa. Any introduction of energy canes is said to be 5-10 years away
- 6.19 Canegrowers submitted that it is unaware of the Applicant's involvement with research into the development of energy canes, but that any involvement is not exclusive. Canegrowers also noted that the viability of energy canes is still being studied.

²¹ There are indications that some land previously used for growing sugarcane and currently utilised as timber plantations may return to sugarcane production in the future. The additional quantity of sugarcane produced is likely to be minimal in the overall scheme and is not expected to significantly increase the foreseeable demand for the Network.

²² Energy canes are said to increase the sugar cane yield per hectare. The Applicant advised that currently *'sugarcane produced in the Herbert River district has an average fibre content of about 14% and yields on average 87 tonnes per hectare. Energy canes have the capacity to produce a higher cane fibre content in the range of 18-22% and a much larger crop yield, in the vicinity of 120-160 tonnes per hectare'*. (Application, [7.25]).

6.20 The Council considers that, should energy canes be a viable crop, then they will be adopted by Growers in due course and the adoption is unlikely to be linked with the success or failure of the Applicant. Any adopted of energy canes by Growers is expected to impact on the demand for the Service from both Sucrogen and the Applicant. While, on the information provided by the Applicant, it appears that the introduction of energy canes has some potential to increase the foreseeable demand for the Network, the Council is unable to assess the likely success of energy canes in the short to medium term and has therefore not included any potential increased tonnage from energy cane production in its consideration of the foreseeable demand for the Service.

Capacity of the Network

6.21 The Applicant argued that the capacity of the Network ‘...is fairly large, particularly during December to May.’ While Sucrogen agreed with the Applicant’s assessment in this regard, it argued that the appropriate assessment of capacity of the Network is in terms of daily capacity during the harvesting season (Sucrogen Submission, [7.24] – [7.26]). The Council agrees with Sucrogen on this point and considers that an assessment of capacity outside of the June to November sugarcane season is likely to be misleading.

6.22 The Applicant further informed the Council that:

Careful planning of the current use of any particular rail line or spur would allow for a number of other operators to use the existing Tram Network and not interfere with or impact on [Sucrogen’s] own milling operations. The capacity of the Tram Network can be increased by scheduling trains effectively so that the transportation configuration and assignment of trains to a particular pathway or spur can be controlled, monitored and efficiently co-ordinated. Therefore access would not require an expansion of the existing Tram Network. (Application, [7.22])

6.23 Sucrogen submits that there is ‘no available spare capacity during the cane season [which is] when both Sucrogen and NQBE require access’ (Sucrogen Submission, [7.16]). It is estimated that the capacity of the Network to transport sugarcane is in the vicinity of 5.5 mtpa and in the current single-user environment, there is sufficient capacity to meet reasonably foreseeable demand over a 5-10 year period (Synergies Report, p 32). While the Applicant has focused on the fact that its business will displace sugarcane currently acquired and transported by Sucrogen with a consequential zero net effect, Sucrogen states that capacity considerations must have regard to the daily capacity of the Network during the sugarcane season (Sucrogen Submission, [7.24]). As Sucrogen operates a 24 hour a day, 7 day a week operation during the sugarcane season, if Sucrogen lost 50% of the currently available sugarcane it would reduce the length of its crushing season rather than crush the

smaller quantity of available sugarcane over the current 5 month season (Sucrogen Submission, [7.24]).²³

- 6.24 Sucrogen further submit that if access were to occur that would require the capacity of the Network to be increased by an estimated 45% in order to cater for the shared and concurrent use by both the Applicant and Sucrogen (Sucrogen Submission, [7.29]). Sucrogen also state that access would require the construction of a significant number of passing loops, new sidings and new signalling and communication systems (Sucrogen Submission, [7.30-7.31]).
- 6.25 The submission from Canegrowers broadly questioned the ability of the Network to accommodate more than one operator, indicating that there may be issues with capacity.

Presence of natural monopoly characteristics

- 6.26 A natural monopoly is said to exist if, given the level of demand for a good, service or facility within a market, one facility can produce the required outputs at lower cost than two or more facilities.
- 6.27 The basic conditions for natural monopoly generally relate to the nature of costs and investment—such as the ‘lumpiness’ of investment and related economies of scale and/or economies of scope. It is generally accepted that a natural monopoly is more likely to exist where capital costs are large relative to variable costs (thereby implying high average costs compared with marginal costs).
- 6.28 Provision of the Service would require:
- (a) construction of the rail infrastructure, including the acquisition of land or access rights to do so
 - (b) earthworks, track construction and installation of signalling equipment
 - (c) maintenance and renewal of the rail infrastructure, including repairs and replacement of track, signals and platforms, and
 - (d) coordination and management of traffic on the rail infrastructure, including train control and the implementation of safe working procedures.
- 6.29 The provision of this infrastructure requires a significant capital investment in below rail infrastructure, which Sucrogen estimates would cost about \$258 million to replace. While ongoing maintenance costs and other operational costs associated with the Service are significant, they are relatively small compared to the capital costs incurred in developing the Network.

²³ 45% is calculated on the basis that NQBE would seek to transport 15,000 tonnes of cane per day, which would be additional to Sucrogen’s daily transport requirements of 35,000 tonnes per day.

6.30 Once committed, much of the infrastructure costs of a railway, such as the cost of earthworks and track formation, are sunk (unrecoverable). While rails, sleepers and ballast could potentially be moved from one rail corridor to another, the expense involved effectively precludes this.

6.31 In addition, the capacity of a railway can often be expanded significantly at a relatively low incremental cost through discrete additions of capacity in the form of passing loops, sidings and upgraded signalling. Once incremental expansion options are exhausted the track must be duplicated or multiple tracked. This involves a much more substantial investment, but delivers a disproportionately large increase in capacity compared to the construction of a similar length of track on a stand-alone basis. The OECD reported, for example, that expanding from single to double track roughly quadruples capacity at less than double the costs (OECD 2001). That is, the relative costs of constructing new rail facilities compared to expanding existing facilities do not depend on whether a railway is dedicated to passenger traffic, freight traffic or used to accommodate a range of transport tasks including passenger, freight and bulk commodities. Nor is it likely that the relationship is significantly affected by whether or not a rail operation is linked to other upstream or downstream operations. Such features may, however, affect the timing of particular investment choices and the absolute cost of implementing any particular expansion option.

6.32 Sucrogen submitted in the Synergies Report that:

Sucrogen's cost structure is predominantly fixed, with relatively low below rail operating costs. The fixed costs represent Sucrogen's sunk and ongoing investment in tramway. The largest component of operating costs is maintenance of the tramway.

Given this cost structure, Sucrogen's Tramway Service Network is characterised by economies of scale. As the throughput of the Tramway Service Network increases, Sucrogen's average unit costs could be expected to decline up to the point where available tramway capacity becomes constrained. Reasonably foreseeable demand provides an indication of the likely timing of any capacity constraints emerging on the Tramway Service Network. (Synergies Report, pp 31-32)

6.33 These features of railways suggest that the Network is likely to be a natural monopoly—such that a single below rail provider is likely to be able to deliver services at lower cost than two or more below rail providers over a wide range of demand levels and that it is only when the use of a railway approaches the maximum scope of its potential capacity that it would become economical to develop another facility.

Is it uneconomic to develop another railway to transport sugarcane?

6.34 The Council considers that the foreseeable demand for the Network to haul sugarcane is unlikely to change, even in the medium to long term. While there may be some additional demand arising from energy canes, other crops and outside of sugarcane season, the likelihood of such demand cannot be tested and so it is considered inappropriate to consider it at this point in time.

6.35 As foreseeable demand is likely to remain constant and to reflect historical levels (seasonal fluctuations aside), it would appear that there is sufficient capacity on the Network to accommodate that demand. In the event that capacity becomes stretched from the extra complexity and/or disruption caused by having an additional operator on the Network it appears that such inadequacy can be addressed via Network extensions such as extra passing loops, sidings, track duplication and updated communication systems and/or enhanced management and scheduling of the rail operations. The Network appears capable of being extended, however, the Council accepts Sucrogen's submission via the Synergies Report that:

While it is considered that the costs associated with those expansion requirements would be significant, it is difficult to obtain a reliable estimate. This is attributable to the uncertainty associated with the exact magnitude of the works that would be required. This would depend on the new above rail operator's demand for below rail services, which is subject to the number and location of the cane growers with which it contracts. (Synergies Report, p 33)

6.36 The question is then the type of extension required and who will bear such costs. Where extensions are necessary to accommodate access then, broadly speaking, those costs are to be borne by the access seeker and will form part of the terms and conditions of access. This is a matter for the second stage of the National Access Regime.

6.37 As railways generally exhibit natural monopoly characteristics, across a range of demand levels continued extension of an existing facility will involve less cost than constructing a new facility. This is because extending a railway will generally involve construction of additional sidings or passing loops, or in some cases double tracking of discrete and potentially short sections of track. It is unlikely that the size and costs of an extension project will approach those involved in constructing a new railway to provide the Service. As some of the major construction costs of a railway, such as earthworks, construction of bridges and signalling infrastructure are avoided or at least minimised when extending an existing railway, it is likely that extension will almost always be cheaper than duplicating a facility.

6.38 The Applicant submitted that the replacement cost (i.e. the duplication cost) of the Network would be approximately \$258 million. While the costs of extending the Network may be substantial depending on the number and type of extensions

required, it is reasonable to expect such costs to be less than the replacement cost of the entire Network.

- 6.39 There may, however, be some costs associated with the sharing of services, such as the Network, that will offset some of the expected cost savings from access. The National Access Regime contemplates that in negotiating the terms and conditions of access compensation may need to be provided to a service provider for any loss of efficiency that results from third party access. The potential for such diseconomies is discussed in relation to criterion (f) in section 10 below.

Preliminary conclusion on criterion (b)

- 6.40 The Council considers that there is sufficient capacity to meet the likely demand for the Service and that should capacity become constrained the capacity can be augmented at less cost than duplicating the Network.
- 6.41 The Council is satisfied that it would be uneconomical to develop another facility to provide the Service. The Application satisfies criterion (b).

Section 44F(4) - Economical to develop another facility to provide part of the Service?

- 6.42 Section 44F(4) of the Act provides that in deciding what recommendation to make, the Council must consider whether it would be economical for anyone to develop another facility that could provide part of the service.
- 6.43 The Council considers that road transportation of sugarcane is, at best, a complement to the Service for limited tonnage either close to the mill or within areas not serviced by rail.
- 6.44 There is an inherent difficulty in considering whether it is economical to develop another facility to provide part of the Service because of the undefined “all points” nature of the Service applied for. The Applicant potentially seeks access to any Grower location in the Herbert River district to and from the Applicant’s proposed mill. The Council concluded at 6.35 above that the Network is a natural monopoly and, as such, extending the Network is likely to be more efficient and less costly than duplication. The Council considers that the same reasoning applies to the prospect of developing another facility to provide part of the Service. As with criterion (b), ‘economical’ needs to be considered in a social cost benefit context. There is no indication that any party intends to do so, but should a commercial party find it viable to develop a facility to provide part of the service in a particular situation does not necessarily mean it is economical from a national interest view point.

Preliminary conclusion on s 44F(4)

6.45 The Council does not consider that it is economical for anyone to develop another facility to provide part of the Service.

7 Criterion (c) – National significance

Legal requirements

7.1 Section 44G(2)(c) (criterion (c)) provides that the Council cannot recommend that a service be declared unless it is satisfied that the facility is of national significance, having regard to:

- (i) the size of the facility;
- (ii) the importance of the facility to constitutional trade or commerce; or
- (iii) the importance of the facility to the national economy.

7.2 Criterion (c) is intended to ensure that only facilities that play a significant role in the national economy fall within Part IIIA. While declaration is concerned with access to services, criterion (c) relates to the national significance of the facility providing the service. Given that s 44G(2)(c) specifies ‘or’ after each of the factors, a facility need only satisfy one of the three for criterion (c) to be met,²⁴ although there is considerable overlap between the importance of a facility to constitutional trade or commerce and its importance to the national economy.

Size of the facility

7.3 The physical dimensions of a facility may provide guidance on its national significance. Indicators of size for the purposes of criterion(c) include:

- (a) the facility’s physical dimensions;
- (b) the throughput of goods on the facility; and
- (c) the replacement cost of the facility.

Application and submissions

7.4 NQBE asserts that the Network satisfies criterion (c) on size alone because it:

- (a) is 530km long;
- (b) would cost \$77 million to replace; and
- (c) generates revenues of \$180 million to \$210 million a year (Application, [9.2] and [9.5]).

7.5 Sucrogen submitted that the Council is not obliged to declare the Service simply because it has previously declared shorter railways (Sucrogen Submission, [5.3]).²⁵

²⁴ See *Re Services Sydney Pty Limited* [2005] ACompT 7 at [180].

²⁵ The lengths of the Robe, Goldsworthy and Mt Newman railways are included in Figure 1

Sucrogen adopts the reasoning in section 7 of the Synergies Report (see 7.6 to 7.7 below), and summarises its arguments in respect of criterion (c) (Sucrogen Submission, p 5), stating that:

- (a) although the true replacement cost of the Network is in the order of \$258 million²⁶ (rather than the Applicant's estimate of \$77 million), this is at the lower end of the range of estimates for replacement costs of railways previously considered by the Council;
- (b) the length of the Network is not itself determinative of size – the physical characteristics of the Network are markedly different to rail networks where size was a factor considered by the Council, including that the Network is within a single local government area and is radial rather than a point to point network; and
- (c) the throughput and capacity of the Network (3.9mtpa and 5.5mtpa respectively) are well below volumes for railways previously satisfying the criterion.

7.6 The Synergies Report:

- (a) argues that there is a material difference between the radial, single user, fit for purpose nature of the Network and previously declared railways which were either principally mine to port railways, or general freight/passenger networks of much greater length;
- (b) points out that the Network is wholly within Hinchinbrook Shire and accounts for only 13% of all cane railways in Queensland; and
- (c) expresses concerns that if a regional tramway in a small geographic area could meet the size criterion a large number of regional infrastructure facilities could be declarable. (Synergies Report, pp 56 – 57)

7.7 The Synergies Report lists the replacement costs of railways previously considered to have satisfied criterion (c). At the bottom end of the range of figures provided are the Mt Newman railway and the Hunter Valley network with estimated replacement costs of \$400 – \$1,020 million and \$400 – \$825 million respectively. The Synergies Report also includes a table summarising the characteristics of facilities previously considered by the Council to have satisfied criterion (c) in terms of size. That table is reproduced below as Figure 1.

below.

²⁶ Sucrogen Submission, p 5. The figure on p 53 of the Synergies Report is \$255m.

Figure 1: Table 4 from Synergies Report**Table 4: Facilities considered nationally significant by the NCC based on size**

Facility	Considerations relating to size of facility
Robe Railway	<ul style="list-style-type: none"> • 210km in length • Duplication cost of \$735m - \$945m
Hamersley Railway	<ul style="list-style-type: none"> • 625km in length • Duplication cost of \$2.19b - \$2.81b
Goldsworthy Railway	<ul style="list-style-type: none"> • 210km in length • Duplication cost of \$750m
Water storage and transport facilities owned by Snowy Hydro Ltd & State Water Corporation	<ul style="list-style-type: none"> • Catchment area of 5,124 square km • 7 power stations • 16 major dams • 80km of aqueducts • 145km of interconnected tunnels • A pumping station
Mt Newman Railway	<ul style="list-style-type: none"> • 295km in length • Reported capacity of 100Mtpa
Sydney Sewerage Network	<ul style="list-style-type: none"> • Total service area of 111,900ha • Total network length of 13,999km • Total DORC value of \$5,382.9m^a
Victoria's intrastate rail network	<ul style="list-style-type: none"> • Total network length of 3,600km
Westrail's Kalgoorlie-Perth rail line	<ul style="list-style-type: none"> • 655km in length • Duplication cost of \$655m - \$982.5m^b
Hunter Valley rail network	<ul style="list-style-type: none"> • Duplication cost of \$400m - \$825m
Sydney to Broken Hill rail line	<ul style="list-style-type: none"> • Two rail lines^c • Track lengths of 1,332km and 1,697km respectively • Annual tonnages of 4.9Mtpa and 6.2Mtpa respectively • Duplication costs of over \$1,998m and \$2,545.5m respectively^d
Queensland rail facilities (track infrastructure)	<ul style="list-style-type: none"> • 1,700km in length

^a Combined information for three reticulation networks – North Head, Bondi, and Malabar.

^b Based on reported estimated duplication cost of \$1m - \$1.5m per km.

^c Sydney-Lithgow-Parkes-Broken Hill and Sydney-Cootamundra-Parkes-Broken Hill.

^d Based on a reported duplication cost of over \$1.5m per km.

Source: All of the estimates provided in this table were taken from NCC final recommendations regarding declaration applications for the relevant facilities.

The Council's preliminary view on the size of the facility

7.8 The figures relating to facilities considered by the Council in previous recommendations and provided in the Synergies Report support Sucrogen's submission that the Network is considerably smaller than any rail facility previously considered by the Council to have satisfied criterion (c) based on size. However, it is important to note that in the Services Sydney matter, for which the Synergies Report provides consolidated figures, the Council considered that each of the North Head, Bondi and Malabar networks constituted relevant facilities and assessed each network individually. The Services Sydney Final Recommendation (NCC 2004 at [7.6]) includes the following figures for each network:²⁷

²⁷ The Tribunal did not consider size in detail, but restated the data in the Final Recommendation: *Re Services Sydney Pty Limited* [2005] ACompT 7, [182]. The Tribunal observed at [181] that, 'there was no dispute between the parties before the Tribunal that the three sewerage reticulation networks are of national significance, although this had previously

- (a) North Head Reticulation Network – Services a population of 1.106 million people and an area of 42,000 hectares.
- (b) Bondi Reticulation Network – Services a population of 258,252 people and an area of 3,900 hectares.
- (c) Malabar Reticulation Network – Services a population of 1.695 million people and an area of 66,000 hectares.

The Final Recommendation continues (at [7.7] – [7.8]):²⁸

Sydney Water argued that the three facilities, examined separately, are unlikely to satisfy the national significance test. It did, however, acknowledge that on the basis of size each of the three facilities may satisfy criterion (c). Sydney Water nonetheless argued that:

Given the limited geographic scope of each of the three networks, serving distinct population groupings within particular regions of Sydney, whilst significant to Sydney, they could not be said to be of national significance.

There is little question that each of the three facilities are substantial in terms of size. Sydney Water provided the following information on the size of each of the three facilities:

	Length	Sewage throughput (average dry- weather flows)	Depreciated optimised replacement cost
North Head Reticulation Network	6,083 km	313 ML/day	\$2,243.6 million
Bondi Reticulation Network	762 km	130 ML/day	\$260.5 million
Malabar Reticulation Network	7,154 km	480 ML/day	\$2,878.8 million

On criterion (c), the Final Recommendation concluded (at [7.11]):

The Council is satisfied that on the basis of size and importance to the national economy in particular, each of the North Head, Bondi and Malabar Reticulation Networks are nationally significant and satisfy criterion (c).

7.9 While the Services Sydney Final Recommendation is instructive, the Council does not consider that it indicates that any single characteristic of a facility will be

been a matter of contention before the NCC’.

²⁸ References in original removed.

determinative in terms of its size. The Council's assessment of the size factor of criterion (c) requires consideration of all the various indicators of size. The Council is of the view that the category of such indicators is not closed.

- 7.10 The Council notes that the nature of the Bondi Reticulation Network, being reticulated, may be considered to be closer to that of a radial network like a cane railway than the point to point networks considered in the various Pilbara rail matters. Assuming that the relevant measure of the Network is total track length (somewhere between 504km and 550km), and the replacement cost is \$255 million, there is a rough correlation with these characteristics of the Bondi Reticulation Network. However, although the Council does not think it is appropriate to determine an arbitrary length to delimit nationally significant size, it notes that the Bondi Reticulation Network was approximately 210 – 260km longer than the Herbert River Network. Regarding replacement cost, the Council notes that the higher estimate given by Sucrogen of \$255 million, while not an inconsequential amount and similar to the replacement cost of the Bondi Reticulation Network, is comparable to (for example) the value of a sizable but not necessarily nationally significant property development. (An example is the development of 141 Queen Street in Brisbane, which is valued at approximately \$250 million.)²⁹ The Council also notes that, while the Network services a large area, the population of the Hinchinbrook Shire (within which the Network is fully contained) is 12,513.³⁰ The Network thus serves and has a material impact on far fewer people than the Bondi Reticulation Network.
- 7.11 The Council must be affirmatively satisfied that each criterion is met. In light of its analysis set out in 7.10 above, the Council does not consider that it can be satisfied that the Network is nationally significant on the basis of size.

Importance to constitutional trade or commerce

- 7.12 Section 44B of the Act defines 'constitutional trade or commerce' to mean any of the following:
- (a) trade or commerce among the States
 - (b) trade or commerce between Australia and places outside Australia, or
 - (c) trade or commerce between a State and a Territory, or between two Territories.
- 7.13 As all raw sugar currently produced in the Herbert River district is exported, and ethanol and electricity production are unlikely to materially contribute to interstate markets (see 5.38 and 5.44 above), the Council considers that the relevant definition

²⁹ www.realcommercial.com.au/commercial-real-estate/5378615

³⁰ www.hinchinbrooknq.com.au/

for assessment of the Network's importance to constitutional trade or commerce is 'trade or commerce between Australia and places outside Australia'.

Application and submissions

- 7.14 The Applicant estimated that the Herbert River district generates total average revenues of \$180 – \$210 million. It said that, as the expected price for the 2009 and 2010 crops are in the order of \$465/tonne, the level of export income to Australia from the Herbert River is 'quite significant' (Application, [9.5]). The Applicant does not provide any comparison with other exports.
- 7.15 The Synergies Report states (at pp 58 – 60) that sugar is a relatively minor export compared with other nationally significant commodities. It said that over the 3 years between 2007/08 and 2009/10 the average value of sugar exports was \$1.4 billion, whereas iron ore was \$28.6 billion, metallurgical coal was \$26 billion, gold \$14.2 billion and thermal coal \$12.8 billion. The Synergies Report also compared sugar exports with other agricultural commodities and argued that sugar is one of the least significant of Australia's agricultural exports. It noted that the Australian sugar industry accounted for approximately 2.9% of global sugar production over the same period. It said that the sugar industry is nationally significant in terms of constitutional trade or commerce, although it is one of the least nationally significant commodity sectors.
- 7.16 The Synergies Report drew a distinction between the nationally significant Australian sugar industry and the Herbert River sugar industry. It said that the Herbert River district exports of around 600,000 tonnes of raw sugar account for around 13% of total Australian raw sugar production and 18% of exports. The Synergies Report estimated that the Herbert River district will contribute around 15% of total raw sugar export revenue in 2009/10. It said that the Herbert River district accounts for 0.4% of total world production (Synergies Report, p 60).

Herbert River sugar's place in constitutional trade or commerce

- 7.17 According to figures from Australia's Department of Foreign Affairs and Trade (**DFAT**), total Australian merchandise exports in 2008-09 were valued at \$230,511 million and sugar comprised 0.4% of that (\$1,030 million) (DFAT 2009, Table 14, page 40; and Table 19, p 57). Sugar does not appear on the DFAT list of Australia's top exports, but, with exports of \$1,030 million, it is approximately Australia's 24th-largest export.³¹ According to the Australian Bureau of Agricultural and Resource Economics (**ABARE**), sugar was outside the top 5 non-mineral exports in 2008-09, which were beef & veal, wheat, wine, wool and dairy (ABARE 2010, p 591).

³¹ DFAT's Table 14 sets out Australia's major merchandise exports, but does not include sugar. This is the Council's own estimate based on the data in DFAT 2009.

7.18 Table 1 below summarises the sugar cane statistics for Queensland and the Herbert River district between 2006 and 2008. Table 2 summarises Australia's national sugar production and exports for the years 2006-07 to 2008-09. Table 3 summarises the value of Australia's commodity exports between 2004-05 and (forecast) 2009-10

Table 1: Herbert River/Queensland cane and sugar production 2006-8:

	HR cane harvest (t)	Qld cane harvest (t)	HR cane area (ha)	Qld cane area (ha)	HR raw sugar (t)	Qld raw sugar (t)
2006	4,794,546	33,023,609	56,331	378,046	619,986	4,506,703
2007	4,287,010	32,622,201	57,159	371,116	593,851	4,533,773
2008	4,688,596	30,177,369	55,061	355,814	632,091	4,384,424

Source: CANEGROWERS, 2008 Annual Report and 2009 data on website.³²

Table 2: National sugar harvest and production:

	Harvest area (ha)	Cane crush (t)	Sugar produced (t)	No 1 pool price (A\$/t)	Sugar Exports (t)
2006-07	409,000	36,397,000	5,026,000	368.0	3,719,000
2007-08	381,000	32,621,000	4,763,000	275.8	3,493,000
2008-09	367,000	30,284,000	4 634,000	331.0	3,244,000

Source: ABARE Summary of Australian Statistics for Sugar.

Table 3: Value of Australian commodity exports (A\$m)

	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10 (forecast)	% change from previous year	
							08-09	09-10
Farm	27 901	27 824	27 900	27 530	32 038	29 982	16.4	- 6.4
– crops	13 679	13 996	13 086	13 027	16 872	16 042	29.5	- 4.9
– livestock	14 222	13 828	14 815	14 503	15 166	13 939	4.6	- 8.1
Forest & fisheries	3 660	3 687	3 849	3 813	3 872	3 611	1.5	- 6.7
Minerals	69 511	92 616	107 976	117 635	161 526	128 964	37.3	- 20.2
Total commodities	101 072	124 127	139 725	148 978	197 435	162 557	32.5	- 17.7

Source: ABARE Australian Commodities, December Quarter, Volume 16 Number 4

7.19 Based on the figures included in Tables 1,2 and 3 and on DFAT 2009:

- (a) Herbert River sugar contributed around 0.09% of total Australian merchandise exports in 2008-09.

³² www.canegrowers.com.au/page/Industry_Centre/about-the-australian-sugarcane-industry/Facts_figures/

- (b) In the same year, the Herbert River district contributed 15.6% of national sugar exports, 0.6% of national farm exports and 0.5% of national non-mineral exports.

The Council's preliminary view on the importance of the facility to constitutional trade or commerce

7.20 The Council considers that the data extracted in 1.17 to 1.19 above supports the view that sugar is an industry of national significance, albeit not in the order of Australia's mineral exports: 2008–09 exports of coal, iron ore or gold were valued at \$54,590 million, \$34,249 million and \$17,509 million respectively (DFAT 2009, Table 14, p 40). The Council considers that it is less clear that sugar exports originating in the Herbert River district, let alone the Network itself, is of national significance in terms of constitutional trade or commerce. A 15.6% share of the sugar export market, while sizable, may not necessarily be characterised as significant. Such a market share would not, for example, trigger the ACCC's notification thresholds in a merger situation.³³ The Council also notes that, although road transportation of sugarcane is not a substitute for the use of an existing rail network, the possibility of using road transport means that the complete loss of the Network (such as through natural disaster) would be unlikely to result in total loss of Herbert River sugar exports. The true measure of the Network's importance to trade with countries outside Australia therefore appears likely to be somewhat less than the Herbert River district's 15.6% share of national raw sugar exports. In addition, as all Herbert River sugar is exported into a global market, and because of the very small share the Herbert River district has in that market, the Network is unlikely to have any material bearing on prices or demand for sugar from other Australian regions.

7.21 As noted at 7.11, the Council must be affirmatively satisfied that each criterion is met. On its current assessment, the Council's view is that it cannot be satisfied that the Network is nationally significant in terms of constitutional trade or commerce.

Importance to the national economy

7.22 The Council focuses its assessment of importance to the national economy on the markets in which access would materially promote competition. The Council has stated that it generally considers national significance to be established if the dependent market provides substantial annual sales revenue to participating businesses (NCC 2009 at [5.9]). In *Re Sydney International Airport* [2000] ACompT 1 at [208], the Tribunal emphasised the importance of the airport to 'Australia's commercial links with the rest of the world'. In the Carpentaria Transport Final Recommendation, the Council considered the rail track to be nationally significant in terms of the national economy 'due to the importance of the ports serviced [and

³³ ACCC *Merger Guidelines 2008*, 9. (Notification is recommended where the merged firm will have a post-merger market share of greater than 20%).

because] the Brisbane-Cairns corridor is the main trunk line which is essential to the efficient operation of all of Queensland's rail system' (NCC 1997, p 59).

Application and submissions

7.23 The Applicant did not raise discrete points regarding importance to the national economy, but the Council has considered the information the Applicant provided and summarised at 7.14 above.

7.24 The Synergies Report noted that the Network:

- (a) is self contained;
- (b) affects no participants outside the Herbert River region; and
- (c) connects to only 2 of 25 sugar mills in Australia. (Synergies Report, p 61)

7.25 The Synergies Report submitted that the importance of the Network should be considered in the context of its contribution to the Australian sugar industry and the economy as a whole and that there are no other factors relevant in the consideration of national importance. (Synergies Report, pp 61 – 62)

Herbert River sugar's place in the Australian economy

7.26 To a large extent, the analysis of importance to the national economy draws upon substantially the same information as that for constitutional trade or commerce provided at 7.17 to 7.19 above. The following additional information casts additional light upon the sugar industry's size relative to other agricultural industries (all figures are as at 30 June 2009):

- (a) The value of all Australian crops was \$4,692 million. The largest contribution was 'other fruit and nuts' (\$1,010 million) followed by 'sugar cane cut for crushing' (\$916 million) and 'other vegetables' (\$727 million). (ABS 2010)
- (b) Based on figures provided by Sucrogen, in the Herbert River around 575 farmers harvested approximately 3.9 million tonnes of cane from 55,000 hectares, yielding 575,000 tonnes of raw sugar (Synergies Report, p 36).

The Council's preliminary view on the importance of the facility to the national economy

7.27 As already noted in respect of constitutional trade or commerce, the sugar industry as a whole is of considerable importance to the Australian economy. It would be overly simplistic to seek to determine importance to the national economy by dividing total economic production, whether in terms of total GDP or of some sector of the economy such as agricultural produce or crops, by the contribution of the facility. Rather, the Council accepts that, the Network is an important element in the production of raw sugar in the Herbert River district, and the sugar industry is of

importance to the national economy. However, it does not follow that the Network is nationally significant in terms of importance to the national economy. The Network is limited to the transportation of sugarcane within the Herbert River district (and of raw sugar to the Port of Lucinda). It does not affect Australia's broader commercial links with the rest of the world.³⁴ Nor does it service a port or form a corridor other than for the transportation of Herbert River district sugarcane and raw sugar.³⁵

7.28 The Council is of the view that it cannot be affirmatively satisfied that the Network is nationally significant in terms of its importance to the national economy.

Preliminary conclusion on criterion (c)

7.29 The Council is not satisfied that the Network, being the facility providing the Service for which declaration is sought, is of national significance.

³⁴ Cf: *Re Sydney International Airport* [2000] ACompT 1, [208].

³⁵ Cf: NCC, *Application for Declaration by Carpentaria Transport of Queensland rail freight services, Final Recommendation* (June 1997), 59.

8 Criterion (d) – Health and safety

- 8.1 Section 44G(2)(d) (Criterion (d)) requires that the Council be satisfied that access to the service can be provided without undue risk to human health or safety.

Application and submissions

- 8.2 The Applicant submitted that access to the Service can be provided safely because:
- (a) the operations of the Service come under the jurisdiction of the Queensland Workplace Health and Safety Department;
 - (b) the Applicant's operations will accord with best practice and comply with all relevant legislation and with Sucrogen's own safe work policies and procedures; and
 - (c) the terms of access will address any risks that might arise from the presence of third party trains on the Network.
- 8.3 Sucrogen accepted that health and safety issues do not of themselves prevent declaration of the Service, provided appropriate investment is made in sidings, passing loops, signalling, control and communication systems to address the increased risks of simultaneous use by more than one user. Sucrogen submitted that although the matters can be dealt with in an access arrangement between Sucrogen and NQBE or determination by the ACCC, they are relevant to the Council's consideration of the Application. (Sucrogen Submission, [9.2] – [9.4])
- 8.4 Canegrowers submitted that safe operation of the Network will be a major issue for operators, harvesting personnel and growers. Access by more than one operator would require improved and coordinated management and would require detailed analysis.

Council's assessment

- 8.5 The Council accepts that some additional coordination and management of safety issues may be required if multiple operators run trains on the Network, and that these may impose some additional costs. However, the Council considers that access to the Service can be provided without undue risk to human health or safety and any issues arising from use of the Service by more than one operator can be addressed through the negotiation of an access arrangement or arbitration by the ACCC.

Preliminary conclusion on criterion (d)

- 8.6 The Council is satisfied that access to the Service can be provided without undue risk to human health or safety.

9 Criterion (e) – Effective access regime

- 9.1 Criterion (e) requires that the Council be satisfied that access to the service is not already the subject of an effective access regime.
- 9.2 Under s 44G(3), in deciding whether a regime established by a State or Territory constitutes an effective access regime, the Council must:
- (a) apply the ‘clause 6 principles’;³⁶
 - (b) have regard to the objects of Part IIIA;³⁷ and
 - (c) subject to s 44DA (which requires the Council to treat the clause 6 principles as guidelines rather than binding rules), not consider any other matter.
- 9.3 Where a service is the subject of an access regime that has been certified by the relevant Commonwealth Minister under Part IIIA, the Council must follow that decision unless it believes that, since certification, there have been substantial modifications to the access regime or the clause 6 principles.

Application and submissions

- 9.4 The Applicant submitted that access to the Service is not already the subject of an effective access regime because the access regime in the *Queensland Competition Authority Act 1997*:
- (a) has not been certified and may not be an effective access regime; and
 - (b) the Network is neither a public facility nor has it been declared under regulation to be a candidate service.
- 9.5 Sucrogen accepted that the Service is not already the subject of an effective access regime (Sucrogen Submission, [9.6]).

Council’s assessment

- 9.6 The Council considers that the Service is not the subject of an effective access regime. Part V of the *Queensland Competition Authority Act 1997* does not apply to the Service because the Service is provided by a facility (ie the Network) that is not a public facility and has not been declared by regulation to be a candidate service.

Preliminary conclusion on criterion (e)

- 9.7 The Council is satisfied that the Service is not subject to an effective access regime.

³⁶ The ‘clause 6 principles’ are set out in clause 6 of the Competition Principles Agreement between the Commonwealth and all the States and Territories of Australia.

³⁷ The objects of Part IIIA are set out in s 44AA of the Act; see 3.10 above.

10 Criterion (f) – Not contrary to the public interest

Legal requirements

10.1 Section 44G(2)(f) of the Act (criterion (f)) provides that the Council cannot recommend that a service be declared unless it is satisfied ‘that access (or increased access) to the service would not be contrary to the public interest’.

10.2 When applying the equivalent test in s 44H(4)(f) of the Act, the Tribunal stated *in Re Services Sydney Pty Ltd* [2005] at [192]:

This criterion does not require the Tribunal to be affirmatively satisfied that declaration would be in the public interest. Rather it requires that it be satisfied that declaration is not contrary to the public interest. It enables consideration of the overall costs and benefits likely to result from declaration and the consideration of other public interest issues which do not fall within criteria (a)-(e).

10.3 The term ‘public interest’ is not defined in the Act but the Council considers that this term allows consideration of a broad range of issues, including but not limited to:

- (a) ecologically sustainable development
- (b) social welfare and equity considerations, including community service obligations³⁸
- (c) government legislation and policies relating to matters such as occupational health and safety, industrial relations, and access and equity
- (d) economic and regional development, including employment and investment growth
- (e) the interests of consumers generally or of a class of consumers
- (f) the competitiveness of Australian businesses, and
- (g) the efficient allocation of resources.

10.4 Consideration of criterion (f) does not revisit the issues considered under the other declaration criteria. Rather it draws on the Council’s conclusions in relation to those criteria. For example, where the Council has concluded that access will promote a material increase in competition in one or more dependent markets, this will usually give rise to benefits that should be included in the assessment of criterion (f). Similarly, where access will aid in avoiding duplication of a facility that exhibits natural monopoly characteristics, this too will lead to benefits that are appropriately considered under criterion (f).

³⁸ Community service obligations are common in relation to the supply of infrastructure services especially to consumers, although there are no explicit community service obligations applying to cane railways.

- 10.5 The Council considers that in answering criterion (f) it is required to be satisfied that the overall costs to the Australian public that arise from access to the Service do not exceed the overall benefits.
- 10.6 If the likely costs exceed the likely benefits then access would be contrary to the public interest, so criterion (f) is not satisfied and the Council would be required to recommend against declaration. This assessment is necessarily on the basis of 'likely' costs and benefits, as the access (or increased access) is prospective. The assessment also involves consideration of likelihood in the sense that the Council must consider the chance that certain outcomes (and associated costs or benefits) will occur. For example, a very costly outcome with a low chance of occurring may not outweigh a smaller benefit which is more certain.

Application and submissions

The Applicant

- 10.7 In support of its Application, the Applicant submitted that there is no reason why access to the Service would be contrary to the public interest and to the extent that it may be possible to find otherwise, any negative impacts arising from access could be addressed by fair and reasonable terms of access. (Application, [12.5])
- 10.8 The Applicant submitted that the following public benefits would arise from access and that they should be favourably weighed against any perceived public detriments (of which the Applicant identified none):
- (a) access will promote a material increase in competition in the market for processing sugar cane in the Herbert River district;
 - (b) access will promote a material increase in competition in the market for growing sugar cane in the Herbert River district;
 - (c) access will promote a material increase in competition in the market for ethanol;
 - (d) access will promote a material increase in competition in the market for the supply of electricity in Northern Queensland;
 - (e) access will avoid the uneconomic duplication of the Network, therefore avoiding inefficient and wasteful investment in unnecessary track infrastructure. It will also avoid the environmentally damaging impact of building an alternative railway or transporting sugarcane by road;
 - (f) public safety is better managed by continuing to direct cane transport to the present rail network which has a proven capacity and safety record, than have NQBE utilise the road network and consequently increase traffic and safety risks to the general public that use it.

Submissions

Sucrogen

10.9 Sucrogen submit that access would be contrary to the public interest because:

- (a) Sucrogen would be exposed to increased costs, including scheduling costs and the cost of negotiating and arbitrating access arrangements which are likely to be significant because of the difficult issues involved. Sucrogen submits that the Council should have regard to these costs given the modest benefits that the Applicant submits would flow from access. (Sucrogen Submission, [7.51-7.52]; and Synergies Report, chapter 10 pp 66-69)
- (b) Sucrogen would incur efficiency losses were there to be two operators on the Network because it would likely result in disruption to the sugar supply chain in the Herbert River district which will adversely affect the crushing of sugarcane and CCS obtained. (Synergies Report, chapter 10 pp 65-67)
- (c) it would expose Sucrogen to significant regulatory burdens and a loss of statutory exemptions because Sucrogen would no longer have the benefit of current exemptions from the *Transport Infrastructure Act 1994* (Qld). This increased regulation would result in significantly greater costs, capital expenditure requirements and increased legal obligations and liability as compared to Sucrogen's current exempt operations. (Sucrogen Submission, [7.41]; and Synergies Report, chapter 10 p 73-76)
- (d) the Service is unlikely to be used by NQBE or any other party and so a declaration would be futile. Further, this would cause unnecessary regulatory uncertainty and inefficiency with no discernable benefit. (Sucrogen Submission, [7.4]; and Synergies Report, chapter 10 p 71) In this regard, Sucrogen identify the following:
 - (i) NQBE's project is highly speculative;
 - (ii) there is insufficient capacity to accommodate an access seeker;
 - (iii) there is a lack of daily capacity during the sugarcane season given the logistical constraints inherent in collection, transportation and crushing of cane;
 - (iv) NQBE may not be able to fund the significant costs of access, including the acquisition of the required rolling stock.
- (e) an access seeker cannot obtain the benefit of the Network Easements, so it is not in the public interest for the Council to recommend the declaration of a service that will never be acquired.

Canegrowers

10.10 Canegrowers' submission indicates that its position was formed on the basis of an incomplete picture as it stated that it needs more detailed information and understanding of the Applicant's business proposal to make a full assessment. Canegrowers state their concern that the Network is not designed for two users and a second user³⁹ may:

- (a) adversely affect access to the line and the operational reliability,
- (b) create safety issues, and
- (c) require the adoption of improved and coordinated management.

10.11 However, Canegrowers also stated that access may result in increased revenue for Sucrogen which may then feed into an improved capital and maintenance commitment.

Assessment

Benefits from access

10.12 From its consideration of criteria (a) and (b) in this draft recommendation, the Council has reached the preliminary conclusion that access to the Network would promote a material increase in the market for the acquisition and processing of sugarcane in the Herbert River district and that it is uneconomical to develop another facility to provide the Service. Usually these conclusions would of themselves give rise to significant benefits to the public. The increased competition in a dependent market could be expected to result in beneficial price changes, additional output and greater innovation. The fact that uneconomic duplication may be avoided by access is also in the public interest and is relevant to the Council's consideration of criterion (f).

10.13 However, the Council considers that the principal effect of an increase in competition in the relevant dependent market (higher cane prices flowing to Growers) appears, at least in the short to medium term, to be largely derived from a transfer of income from millers to Growers rather than from significantly increased output. Such transfers do not represent a net benefit to the public which should be considered in assessing whether criterion (f) is satisfied. While in the longer term output may increase—were for example energy canes to be adopted by Growers—that effect is less certain, some time off and is not necessarily attributable to access. As a result it needs to be significantly discounted in the Council's assessment.

10.14 In addition to the benefits deriving from the satisfaction of criteria (a) and (b), the Council considers that access will also produce benefits to the public in terms of

³⁹ Canegrowers rightly noted that declaration means anyone could seek access to the Service as so the potential exists for there to be more than two users.

minimising the use of relatively costly and inefficient road transport and in terms of the associated reduction in the adverse environmental and social consequences of road transport compared to rail. Rail transport of sugarcane is more efficient than road haulage in almost all circumstances. Similarly rail transport is environmentally and socially preferable to road transport for sugarcane. Use of rail transport will reduce the comparatively greater environmental impact of road transport, the impact of increased traffic congestion from trucks and the attendant road safety and risk to other road users and the township and citizens of Ingham, particularly given the proximity of the Applicant's proposed factory to Ingham.

10.15 Assuming the Applicant's business plan proceeds, benefits may also flow from the construction of the Applicant's proposed new factory/mill. As the factory is to be a newly constructed, purpose built facility it could reasonably be expected to be developed with the latest technology thereby maximising its economic efficiency. The Applicant has also indicated that it intends to construct a factory that can use feedstocks additional to sugarcane. This may give rise to additional output which will result in net public benefits.

10.16 The Council rejects Sucrogen's suggestion that an adverse inference may be drawn from the fact that the Applicant did not provide its feasibility study to the Council and that cane supply agreements the Applicant has secured with Growers are conditional upon access (amongst other things). In association, Sucrogen submit that declaration is futile because the Applicant's business proposal is speculative and there is no certainty that the Applicant could fund or source funding for its proposal. Furthermore, Sucrogen state that there is no other prospective user of the Service. As noted earlier in respect of the consideration of criterion (a), the Council takes the view that it is not necessary for an applicant for declaration to present a detailed business plan as to its proposed use of the relevant service in order to make out a case for declaration. The Council's task is not to assess the viability of an applicant's business proposal, but to assess whether the service sought meets the criteria for declaration in s 44G(2) of the Act (see 5.50 above).

Costs from access

10.17 Sucrogen has detailed a range of consequences arising from access that will generate costs that Sucrogen submits make access contrary to the public interest.

10.18 The costs Sucrogen claims will arise from access are broadly categorised as follows:

- (a) coordination costs, the disruption effect, loss of system capacity and consequential efficiency losses to the operation of the Network and to the production of sugar
- (b) regulatory costs, including the costs of negotiating access arrangements and increased regulatory burdens such as the loss of exemptions under the *Transport Infrastructure Act*, and

- (c) expansion costs to meet the demand of an access seeker(s).

Coordination costs, potential efficiency losses and diseconomies

10.19 The Council accepts that the acquisition of sugarcane is linked with the time of harvest and speed with which the sugarcane needs to be processed following harvest. The terms and conditions of access will need to have regard to the harvest schedules and processing requirements and it may be that access to a cane railway demands greater coordination, control and logistical considerations than other railways where stockpiling is available.

10.20 Sucrogen needs to use the Network in a manner that coordinates both the harvest and its processing of sugarcane, with transportation of the sugarcane providing the crucial link. Sharing the Network with an access seeker is likely to result in some costs to Sucrogen in the form of coordination/scheduling costs, potential lost capacity and other diseconomies. The Council considers that such costs can generally be anticipated and Sucrogen can be compensated through access pricing and other terms and conditions of access. It also appears that, as there is a genuine need for the timely transport of sugarcane it may reasonably be expected that an access seeker will take all steps necessary to minimise disruption to the Network as disruption could result in a loss of capacity that is likely to adversely impact its business as well as Sucrogen. For this reason, the Council queries the extent of Sucrogen's claims about the disruption effect and the magnitude of its potential consequences as it would be in all parties interests to maximise the efficiency and throughput of the Network. Furthermore, there is also scope within access pricing to provide for penalties that are designed to foster cooperative sharing of the Network (for example, providing that penalties are incurred when a train breaks down that blocks or otherwise disrupts a line for a specified period of time).

10.21 Sucrogen has highlighted that it considers there is insufficient capacity on the Network to accommodate the demand of another user and that should Sucrogen be required to provide access then Sucrogen's operations will suffer. The Council notes that Part IIIA provides, in the arbitration of an access dispute by the ACCC, that the ACCC is prohibited from making a determination that prevents an existing user (in this case Sucrogen) from obtaining a sufficient amount of the declared service to meet its current and reasonably anticipated future requirements. If an access seeker seeks access to a declared service that would have the effect of displacing Sucrogen, then presumably Sucrogen would not agree. The access seeker may then exercise its rights to have the matter arbitrated by the ACCC. If Sucrogen establishes that access would prevent it obtaining sufficient access for itself, then access by an access seeker could not be determined by the ACCC. This is a matter to be determined in the circumstances of a particular request for access and based on the facts of that access request.

Regulatory costs and regulatory error

- 10.22 The Council accepts that declaration and access pursuant to Part IIIA creates regulatory costs that must be considered under criterion (f). These are the costs that service providers may incur in conducting negotiations with access seekers and responding to the arbitration of access disputes. They also include the costs of the ACCC and other public bodies in carrying out their functions in relation to a declared service.
- 10.23 Sucrogen submit that the costs arising from disputes are likely to be significant because the integrated nature of the harvest, transport and processing operations is likely to trigger a number of disputes. As noted above, the Council anticipates that because the need to maximise throughput and minimise delivery time on the Network is shared by Sucrogen and the Applicant, the parties should have an incentive to minimise disputes and disruption to the Network's operation. The Council accepts that because of the coordination and logistics inherent in the Network's operations, formulating any initial terms and conditions of access may be more complex than for other railways where there is minimal likelihood of crop deterioration, but the issues peculiar here to a cane railway do not appear to be insurmountable.
- 10.24 In addition, Sucrogen has stated that access will expose it to a significant regulatory burden because it will lose the benefit of current exemptions afforded to it under the *Transport Infrastructure Act 1994* (Qld) because the Service extends to carrying feedstock other than sugarcane. The Council accepts that if the Network does transport anything other than sugarcane it appears that Sucrogen's current operations will lose exemptions available to them under that legislation. The Council accepts that declaration and access may expose Sucrogen to increased costs and compliance should a request for access be made to transport anything other than sugarcane. However, if this occurs the Council considers that it is something that Sucrogen may be compensated for in the access pricing. The regulatory burden thereby being passed onto the access seeker.
- 10.25 Sucrogen submit that access is accompanied by the potential for regulatory error largely as a result of information asymmetry. Sucrogen further submits that access would result in regulatory uncertainty which would have adverse consequences for investment and, importantly, the incentive to invest. The Council accepts that there may be a cost arising from the risk of regulatory failure and, in particular, the risk that arbitrated access prices or terms may give rise to inefficient outcomes. However, in the Council's view the quite specific provisions that govern access determinations, and in particular those that establish specific requirements regarding the interests of service providers, and the review and oversight arrangements in relation to these determinations are such that the risk of regulatory error is small.

Expansion costs to meet NQBE's demand

10.26 Sucrogen suggests that the costs of any expansion to the Network to meet the needs of the Applicant should be considered a cost in assessing criterion (f). While these are costs that might flow from access, in the circumstances where declaration might be available these costs will be less than the costs of building an alternative railway facility and, as such the avoidance of the costs of the alternative is a benefit as described at 10.12 above.

Other cost considerations

10.27 The Council is of the view that in considering the likely costs of access consideration needs to also be given to the number of mills or processing facilities that can reasonably be expected to operate economically and efficiently in the Herbert River district. In this regard it is important to note that it appears without contention that in the event of declaration and subsequent access to the Service, the output of sugarcane is unlikely to increase, at least in the short to medium term. As such, the volume of sugarcane currently processed by two mills will be spread over three mills which is likely to result in the inefficient operation of at least one of those mills and a reduction in the overall efficiency of sugarcane processing in the region. It is unlikely that this arrangement would be sustainable in the medium to long term.⁴⁰

10.28 Following a transition period, competitive forces would be expected to impact and determine the success or failure of the three mills. However, during the transition period, there will be a cost to society, and in all likelihood the environment, from the economically inefficient operation of one or more of the mills.

Preliminary conclusion on criterion (f)

10.29 Access to the Service will generate costs. Many of the costs could be apportioned and compensated for in the terms and conditions of access, including access pricing. However, the Council is concerned that the costs of access, including any increased regulatory burden and regulatory risk, may be relatively large when compared to the benefits which appear likely to result. It is not apparent that the costs are sufficiently addressed given the benefits appear unlikely to include any short to medium term increase in output from sugarcane production. The sugarcane volumes in the Herbert River district are likely to remain at historical levels and be spread across both Sucrogen and the Applicant, should the Applicant's business proposal proceed and access occur.

⁴⁰ See also Attachment 3 to the Application which states – 'The loss of 2.3 million tonne of cane to these mills from a total cane supply of 3 to 5 million tones would have an unacceptable material impact on our business. A permanent closure of at least one of CSR's two sugar mills is the likely result.'

10.30 As noted above in respect of criterion (f), the Council must be affirmatively satisfied that access would not be contrary to the public interest. The Council's present view is that the likely benefits of access to the Service will not outweigh the costs. Therefore the Council is not satisfied that access is not contrary to the public interest and considers that the Application does not satisfy criterion (f).

10.31 In response to this draft recommendation the Council specifically seeks additional information as to:

- (a) the level, timing and likelihood of additional output from the processing of sugarcane in the Herbert River district; and
- (b) the magnitude and frequency of the likely costs,

to enable it to reach a firmer conclusion in relation to this criterion.

11 Duration of Declaration

11.1 Although the Council's preliminary conclusion is that it should recommend that the Service not be declared, consideration has been given to the duration for which the Service should be declared, in the event that the Council's position changes in light of submissions in response to this draft recommendation.

Legal requirements

11.2 Section 44H(8) of the Act requires that if the designated Minister declares the service, the declaration must specify the expiry date of the declaration. The expiry date determines the duration of declaration, which can vary according to the circumstances of each application. Further, s 44I(1) of the Act states that a declaration begins to operate at a time specified in the declaration. The specified time cannot be earlier than 21 days after the declaration is published. Pursuant to s 44I(2), if an application for review of a declaration is made to the Tribunal, the declaration does not begin to operate until the Tribunal makes its decision on the review.

11.3 In considering the appropriate duration of declaration, the Council has regard to the importance of long term certainty for business — including access seekers, service providers and other affected parties. It also considers that declaration should apply for long enough to ensure that the benefits expected from access are able to be realised. This requires that the rights granted by declaration be in place long enough to influence the pattern of competition in relevant dependent markets.

11.4 Against these considerations must be balanced the potential for technological development, reform initiatives (such as changes in legislation governing access to the relevant service) and future market evolution. Further, the Council considers that access regulation governing services, including the right granted by declaration, should be reviewed periodically. The expiry of a declaration provides such an opportunity. The Council notes that any declaration can be revoked on the recommendation of the Council (s 44J of the Act). The Council may make such a recommendation if it considers that the declaration criteria are no longer met. This would allow the Council to reconsider a declaration recommendation in the event of a significant development that impacted on the basis for its recommendation.

Application and submissions

11.5 The Applicant seeks declaration for 30 years. (Application, [13.1]) It argues that this period is necessary to enable investment and the implementation of decisions responding to declaration and to enable the benefits of declaration to be realised.

11.6 Sucrogen submitted that the Applicant gave no reasons for requesting a 30-year declaration period and noted that the declarations sought for the Pilbara railways were for only 20 years. It argued that in the absence of evidence from the Applicant

going to the period of declaration, the Service should be declared for only a modest period (Sucrogen Submission, [10.2] – [10.3]).

The Council's assessment

- 11.7 Should the Council's final recommendation be to declare the Service, access may result in the entry of a new sugar mill operator in the Herbert River district. The commitments required to establish a new mill can be accommodated in a relatively short timeframe, compared to the equivalent commitments in the Pilbara rail matters, for example. However, unlike in the Pilbara matters, the Council has not been provided with any basis on which to assess the appropriate duration of declaration other than the Applicant's assertion that 30 years is 'necessary'.
- 11.8 As noted at 11.4 above, the Council considers that access rights granted by declaration should be reviewed periodically and expiry of a declaration provides an opportunity for such a review, but also notes that any party can apply to the Council for a recommendation that declaration be revoked. In the absence of specific evidence from the parties, the Council considers that a period of 20 years would provide certainty for parties and be sufficient to allow access seekers to realise the benefits of declaration. It would also be a sufficient period for declaration to influence the pattern of competition in dependent markets. Should circumstances change during the 20-year period, such that a person considers that declaration is no longer appropriate, an application may be made to the Council for a recommendation for revocation.

Preliminary conclusion on s 44H(8)

- 11.9 The Council considers that, in the event that its final recommendation is to recommend declaration of the Service, the period of declaration should be 20 years.

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