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Ms Linley Johnson
Executive Director
National Competition Council
GPO Box 250
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By email: pon@ncc.gov.au

Dear Ms Johnson *Lin*

Possible NCC recommendation to revoke declaration at the Port of Newcastle – relevance of ACCC arbitration determination

I am writing to you with an additional ACCC submission to the NCC's consideration of whether to recommend that the designated Minister revoke the declaration of the shipping channel service at the Port of Newcastle (**Revocation Recommendation**).

This letter follows the recent finalisation of the ACCC's arbitration of a dispute between Glencore Coal Assets Australia Pty Ltd (**Glencore**) and Port of Newcastle Operations Pty Ltd (**PNO**) in relation to access to the shipping channel service (**arbitration determination**). I note the NCC's invitation on 15 October for further submissions about whether and how the NCC should have regard to the arbitration determination in considering the Revocation Recommendation.

The ACCC considers that the arbitration determination is relevant to the NCC's considerations. The attached submission accordingly sets out additional points from the ACCC, stemming from the arbitration determination, which the ACCC considers the NCC should take into account in its assessment. Consistent with its earlier submission on 8 August, the ACCC has limited its comments to the interpretation of section 44CA(1)(a) (**criterion (a)**) of the *Competition and Consumer Act 2010* (Cth) (**CCA**).

If you would like to discuss this letter or any issues contained in the attached document, please contact Michael Cosgrave, Executive General Manager, Infrastructure Regulation Division on (03) or Michael Eady on (03)

Yours sincerely

Rod Sims
Chair

ACCC arbitration determination

As the NCC is aware, the ACCC made its final determination on 18 September 2018 and published its arbitration report, final determination and statement of reasons on 8 October. Public versions of those documents are available on the ACCC's website at:

<https://www.accc.gov.au/public-registers/access-to-services-registers/determination-of-the-access-dispute-between-port-of-newcastle-operations-and-glencore-coal-assets-australia>

The history of the Navigation Service Charge in dispute between the parties in the arbitration is that, in January 2015, PNO increased the charge by around 40 per cent to \$0.69 per gross tonnage (GT).

The Australian Competition Tribunal declared the shipping channel service in June 2016. In November 2016, Glencore notified the ACCC of a dispute with PNO about the price increase and requested that the ACCC arbitrate under Part IIIA of the CCA. Since then, PNO has increased the Navigation Service Charge to its current 2018 price of \$0.76 per GT.

In the course of the arbitration, PNO submitted to the ACCC that a Navigation Service Charge of \$1.3643 per GT for Glencore's use of the shipping channel service would be consistent with a proper application of the section 44X factors that the ACCC must have regard to in an arbitration under Part IIIA of the CCA. In contrast, Glencore submitted that a charge of \$0.41 per GT would appropriately reflect the section 44X factors.

Table 1 below (taken from the ACCC's statement of reasons) summarises Glencore and PNO's submitted positions and the ACCC's Determination with respect to resulting prices as at 1 January 2018. For comparison, the table also provides (in \$2018 terms) the prices that PNO currently charges coal users at the Port of Newcastle, and the prices that PNO charged in 2015 that resulted in the price dispute.

Table 1: Prices for coal users at the Port (\$2018)

	Navigation Service Charge \$ per gross tonnage	Wharfage Charge \$ per revenue tonne
PNO 2015 port pricing schedule	0.7286	0.0720
PNO 2018 port pricing schedule	0.7553	0.0746
Arbitration:		
- PNO submitted position	1.3643	0.0746
- Glencore submitted position	0.4139	0.0746
- ACCC's Determination	0.6075	0.0746

The ACCC refers to Table 1 in its comments below. The ACCC also notes that, in addition to the assessment of certain charges, the arbitration determination also includes the ACCC's assessment of the parties' submitted positions in relation to non-price terms and conditions that would be consistent with a proper application of the section 44X factors.

Implications for the NCC's consideration of the Revocation recommendation

Terms of criterion (a)

Declaration criterion (a) states that the NCC must consider whether:

access (or increased access) to the service, on reasonable terms and conditions, as a result of a declaration of the service would promote a material increase in competition in at least one market (whether or not in Australia), other than the market for the service

The ACCC's first submission noted that the 2017 amendment to criterion (a) changed the emphasis in the first part of criterion (a) from assessing the result of *access* to assessing the result of *declaration* in promoting a material increase in competition. This has been referred to as a 'with and without declaration' test as opposed to the previous 'with and without access' test.

As previously submitted, the concept of "promoting" competition in the criterion does not correspond to only measuring quantifiable increases in competition, but expresses a more flexible idea of creating the conditions or environment for improving competition from what it would be otherwise.¹

As also noted, it is especially important that the second part of criterion (a) relating to 'a material increase in competition in at least one market... other than the market for the service' is properly interpreted and applied, having regard to economic principles. This requires a forward looking analysis, over the medium to long term, when considering the conditions or environment for improving competition.

Should the NCC have regard to the arbitration determination?

The ACCC considers that the NCC should have regard to the arbitration determination in considering the Revocation Recommendation. The outcome of the arbitration will inform the NCC's interpretation of the 'with and without declaration' test in considering criterion (a).

An obvious direct consequence of declaration is providing access seekers with potential recourse to arbitration by the ACCC. In the case of the shipping channel service, the ACCC's final determination is an assessment that PNO's current charging is not appropriate or reasonable, having regard to the criteria in Part IIIA of the CCA. It provides the best and most recent independent assessment of what constitutes 'reasonable terms and conditions' of access to the service, as compared with what the service provider considered reasonable.² This includes both price and non-price terms and conditions. As noted in the ACCC's first submission, it is necessary to consider the prices and terms of services, rather than just focusing on the impact of price changes on the level of production in related markets, when considering the economic and competitive outcomes of declaration.

¹ *Re Sydney Airports Corporation Ltd* (2000) 156 FLR 10 at [106]-[107]; *Re Duke Eastern Gas Pipeline Pty Ltd* (2001) 162 FLR 1 at [75]; *Re Services Sydney Pty Ltd* (2005) 227 ALR 140 at [132]; *Re Virgin Blue Airlines Pty Ltd* (2005) 195 FLR 242 at [146]; *Telstra Corporation Ltd v. Australian Competition Tribunal* (2009) 175 FCR 201 at [224]-[225]; *Re Fortescue Metals Group Ltd* (2010) 242 FLR 136 at [1060].

² As noted above, the arbitration determination reflects the ACCC's assessment of what constitutes reasonable terms and conditions having regard to the section 44X factors set out in Part IIIA. In the course of the arbitration, the ACCC took into account areas of agreement between the parties as a relevant consideration for the section 44X factors. For example, the parties agreed to use a particular asset valuation methodology and pricing model methodology for the arbitration, which ultimately influenced the exact level of the Navigation Service Charge that the ACCC assessed. For this reason, the arbitration determination is not the only possible set of terms and conditions that might be determined by arbitration, nor does it necessarily reflect the same outcome that would occur were the shipping channel service be subject to price regulation to begin with.

The arbitration determination is currently subject to appeal to the Australian Competition Tribunal by both parties, meaning that the terms could change on appeal in favour of either the access seeker or access provider. Whilst the circumstances of an individual access seeker at a point in time are separate from the benefits for the broader market in the long run as a result of declaration, the ACCC's determination as it stands provides the clearest picture of how the conditions or environment for competition may be promoted by declaration – most directly in the specific example of charges paid by Glencore, but also in potential outcomes for all access seekers.³

The arbitration determination is accordingly a real-life example relevant to the NCC's assessment of whether declaration affects the terms and conditions for a service, and accordingly in turn promotes a material increase in competition in dependent markets. The specific terms determined by the ACCC assist the NCC with conducting a forward-looking analysis, over the medium to long term, of whether declaration creates the conditions or environment for improving competition from what it would be otherwise. This is true despite the uncertainties of the effect of the appeals and lack of clarity about how the determination will affect prices for other users.

Specific points

Further to its high level submission, the ACCC expands on several specific points below.

Materiality and the scale of the competition effect in dependant markets

As indicated above in Table 1, there were significant differences between the parties in the arbitration on the appropriate level of the Navigation Service Charge. The ACCC ultimately decided on a charge between the two submitted positions, and below both the 2015 and 2018 PNO scheduled prices.

It is reasonable to expect that PNO would have, in the absence of declaration, continued to charge at least its scheduled price of \$0.7553 per GT, and potentially higher, given that a facility owner with market power can determine the terms and conditions of access with little constraint.

Significantly, criterion (a) requires that any effect of declaration in dependent markets must be a material one. Consideration of the magnitude of the difference between the arbitrated charge on one hand, and the charges actually or potentially charged by the access provider on the other, should inform the NCC's assessment of the effect of declaration on competition in related markets such as the market for the export of coal from the Hunter Valley.

Forward-looking assessment over the medium to long run

A proper consideration of whether declaration would promote competition in a dependent market requires a forward-looking consideration over the medium to long run.

As noted above, PNO submitted that a Navigation Service Charge significantly above its current scheduled price would be consistent with the section 44X factors. It is reasonable then to expect that, absent declaration, further price increases would be likely to follow in the medium to long term. The NCC should consider the potential evidence from the arbitration determination on its assessment of the effects of such price increases in a forward-looking

³ Other access seekers may refer to the arbitration determination in their own negotiations with PNO and may seek arbitration themselves, or PNO may adopt lower charges or alter terms and conditions for users more generally in reflection of the arbitration determination.

sense. In doing so, it must look at the potential implications of not just price increases that have happened, but also that may happen in the future.

Effects on competition – production levels and potential hold-up

The ACCC's first submission identified two main potential effects on competition of the ability to impose unreasonable price and non-price terms and conditions, absent declaration. The first is the effect of cost increases on production in dependent markets in both the short and long term. The second and broader potential effect on competition of a lack of pricing restraint relates to the potential quantitative and qualitative impacts of dampened incentives to invest in the medium to long term.

The arbitration determination suggests that, if unconstrained, PNO's Navigation Service Charge, having increased by 40 per cent initially, and by a further 4 per cent to 2018, still has significant potential for further price increases. This means that potential effects on production in dependent markets may continue into the medium and long term. This could occur as firms are unable to absorb increases in the costs of using the shipping service, and ultimately may exit the market.

Absent declaration, any investments by customers also face the potential effects of a threat of hold-up. That is, customers will be reluctant to invest, or will make less desirable investments, due to the threat that once an investment is made, the monopoly service provider will seek to change the terms and conditions of use in its favour. This dampening effect on future investment can harm the competitive environment in the dependent markets.

Again, comparing the price ultimately determined by the ACCC to PNO's scheduled and submitted price provides information on the likely scale of the hold-up problem, absent declaration, and the resulting effect on the conditions and environment for competition in dependent markets.

The effect of declaration is to limit the potential scale of both the production impacts and the hold-up problem. As noted in the ACCC's first submission, declaration will require a monopoly service provider to behave more like it would as if its activities were carried out in a competitive marketplace, and will limit its ability to impose terms and conditions that are not reasonable.