ACCC Responses to Questions Raised by the NCC re Arbitration Under Part IIIA

General

The National Competition Council (NCC) has put a number of questions to the Australian Competition and Consumer Commission (ACCC) in relation to its consideration of an application by Fortescue Metals Group Ltd (FMG) for the declaration of services provided by facilities owned by BHP Billiton Iron Ore Pty Ltd (BHPBIO). While the questions are responded to in detail below, there are a number of general points that can be made:

- Many of the issues raised appear to relate more to the making of an access determination under section 44V of the *Trade Practices Act 1974* (TPA); than to the declaration criteria under s 44G;

- In relation to concerns about additional costs and loss of control and flexibility by an access provider over the services potentially provided by declared infrastructure, there are legislative provisions which limit the determinations that the ACCC can make in arbitration, including section 44W(1)(d), which prevents a determination resulting in a third party becoming the owner of any part of, or an extension of, a facility without the consent of the provider;

- There is wide experience in rail and other complex industries, such as electricity and telecommunications, where facilities have been subject to mandated access and the facility owner has maintained an effective level of control over operational decisions, including scheduling, maintenance and capacity expansion.

Question 1 *Given the matters that the Commission must take into account when making an access determination, and in particular the provider's interests outlined in section 44X(1)(a), can an access determination require an access seeker to invest in whatever infrastructure and mechanisms are necessary to avoid adverse impacts on the provider's operations (as opposed to mechanisms to compensate the provider for the impacts of third party access)?*

To date, the ACCC has not received any access dispute notification under Part IIIA. Question 1 would need to be considered in the context of a particular arbitration after taking into account any submissions provided by the parties concerned.

However, section 44V(2) provides that a determination "may deal with any matter relating to access by the third party of the service". On the face of it, a determination requiring the third party to "invest in … infrastructure and mechanisms … necessary to avoid adverse impacts on the provider's operations" would appear to come within the scope of s 44V(2). Whether such a determination would be made would depend on the matters set out in ss 44W(1) and 44X(1), and the circumstances of the particular arbitration.

Question 2 *In making an access determination under section 44V of the TPA, what mechanisms are available to address future events that cannot be accurately forecast? In particular:*

the need for third parties to implement future technological innovations (such as the introduction of driverless trains) that may be necessary for future compatibility with the facility;

the need for third parties to pay for future capacity expansion of the facility, where that capacity expansion is required because:
the capacity requirements of the third party are absorbing what had been spare capacity but is now required by the provider; or
a general capacity expansion is required due to the increased capacity requirements of both provider and third party?

the need for the provider to temporarily deprive third parties of access due to maintenance or construction requirements (for example: but for third party access, the provider would be free to shut down part or all of its service to allow for unforeseen maintenance, or for construction associated with capacity expansion. How can the flexibility to shut-down be maintained where third parties have capacity requirements?)

Question 3 *To what extent can the above mechanisms be implemented up-front in a way that minimises the risk of future technological advances or capacity expansion being delayed by protracted negotiation and arbitration? In particular, how can the arbitration framework ensure that third parties do not "game" the system by frequent recourse to arbitration over the necessity of expansion/technology investment, cost pass-through, and terms and conditions of payment? (By way of example, a third party using a small percentage of the facility's capacity might have incentives to prolong negotiations because delay costs the provider significantly more dollars per day than the third party, forcing the provider to accept the third party's terms)*

It would be inappropriate for the ACCC to be definitive about mechanisms to deal with risk without considering the facts of an arbitration in detail. However, it can be noted that:

- prior to any arbitration, there would be an opportunity for an access provider to negotiate with an access seeker to attempt to resolve such issues on a commercial basis;

- if the matter proceeded to arbitration, the access provider would be able to put forward its preferred approach to forecasting and controlling for future uncertain events including technological advances or capacity expansion. For example, it is a common characteristic of access arrangements to provide for maintenance or capital works; and to include provisions dealing with: the sharing of costs, emergencies and termination or suspension of obligations (see, for example, the access undertaking

provided by the Australian Rail Track Corporation accepted by the ACCC in May 2002);

- an arbitration determination must not contravene section 44W (which, amongst other things, protects reasonably anticipated requirements); and

- in the event that the parties are unable to agree on a variation[1] to an arbitration determination, a new access dispute can be notified under section 44S (see the note to s 44ZU(1)).

Claims by an access provider that the arbitration provisions are being gamed by an access seeker would need to be considered on a case by case basis. However, it should be noted that:

- under section 44Y, the ACCC may terminate an arbitration (without making a determination) if it considers that notification of the dispute was vexatious; the subject of the dispute is trivial, misconceived or lacking in substance; or the party who notified the dispute has not engaged in negotiations in good faith;

- a determination does not have to require the provider to provide access to the third party (s 44V(3));

- the *Trade Practices Amendment (National Access Regime) Bill 2005* proposes to introduce a target time limit of six months for resolution of access disputes; and

- the Part IIIA arbitration guideline to be published by the ACCC may also impact on the way parties conduct negotiations.

More generally, the ACCC notes that issues related to particular access seekers are matters to be determined in the context of a particular arbitration and not at the stage of declaration.[2] In *Sydney International Airpor*t [2000] ACompT 1 (1 March 2000), the Australian Competition Tribunal concluded (at [232]) that:

> any particular consideration in relation to any particular ramp handler can be addressed by the Commission in any arbitration of an access dispute when it considers, in accordance with s 44X(1), the legitimate business interests of SACL, the interests of all persons who have rights to use the service, the operational and technical requirements necessary for the safe and reliable operation of the facility and the economically efficient operation of the facility.

Question 4 *Does the Commission consider that, notwithstanding the limit on access terms set by section 44W(1)(e), an access determination might nevertheless provide for BHPBIO to undertake the initial cost of expanding the facility to allow*

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[1] The ACCC may vary a determination on the application of any party to the determination if the other party does not object: s 44ZU(1).

[2] See *Sydney International Airpor*t [2000] ACompT 1 (1 March 2000) at [128], [146], [164], [221] and [228]-[230].

access, with the costs to be factored into the access price (such that, in the long term, BHPBIO does not bear the cost of expansion)?

Question 5 *If so, what mechanisms are available to the arbitrator to address the risk to BHPBIO of a third party forfeiting on future payments for capacity expansions? Might the arbitrator prescribe that third parties acquire risk instruments such as bonds or take-or-pay arrangements? How might such instruments work in this case?*

Question 6 *Might such instruments also be used to allow for unforeseeable future costs (as discussed in question (2) above)?*

Section 44W(1)(e) provides that the ACCC must not make a determination that would have the effect of "requiring the provider to bear some or all of the costs of extending the facility or maintaining extensions of the facility". As noted above, it would be necessary to consider the particular terms and conditions that are proposed, and the submissions of the parties to the arbitration including on the issue of mechanisms to address future risks including the financial risk of a party not complying with its obligations.

It should also be noted that, while the financial viability of the access seeker may be relevant to an arbitration determination, it is not relevant to the decision to declare the service.[3] In *Sydney International Airport* [2000] ACompT 1 (1 March 2000), the Australian Competition Tribunal stated:

> 19 The Tribunal is of the view that evidence of the financial viability of a party who desires access to the relevant service is not admissible or relevant on a consideration of what the Tribunal calls the first stage of the access regime provided by Pt IIIA of the Act. The task to be undertaken by the Minister, and on re-consideration by the Tribunal, is to determine whether, in accordance with the statutory criteria in s 44H(4), a service should be declared. If a service is declared then, in the absence of an access regime being put in place in accordance with s 44ZZ of the Act, a party seeking access to the service is to negotiate such access with the provider of the service. If such negotiations are unsuccessful it is open to the party seeking access to have the issue of its access arbitrated by the Commission. It is at that stage of the inquiry that the financial viability of the party seeking access may be relevant.
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> 20 It was put by SACL that, in order to determine whether access or increased access to the service would promote competition in the relevant market, it was necessary to have regard to the financial viability of the party seeking the declaration, as such financial viability would be relevant as to whether or not competition would be promoted in the future in the relevant market. However, the Tribunal thinks this is a misunderstanding of what occurs at the first stage. The declaration of a service pursuant to s 44H of the Act is akin to unlocking the door, but whether or not a particular party can then go through the door depends on the party's ability to negotiate an access agreement with the provider or, in default of an agreement, to have an arbitrated outcome of that situation.

Question 7 *How can arbitration deal with costs to BHPBIO that arise from access but which aren't attached to rail investment, such as:*
third party train breakdowns that interfere with the provider's operations;

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3 See *Sydney International Airpor*t [2000] ACompT 1 (1 March 2000) at [18]-[21].

the need to manage risk (such as the above) through increased stockpiling of ores at the port;
perceptions amongst clients that there is increased risk, and thus less security of supply from BHPBIO?

As stated above, issues of this nature would need to be raised by an access provider in the context of a particular arbitration. More generally, the ACCC notes that:

- section 44V would not restrict a determination to dealing only with "investment" costs arising from access. A determination may deal with any matter relating to access; and

- in making a determination, the ACCC would be required to take into account the "legitimate business interests" of the provider (s 44X(1)(a)) and the "direct costs of providing access to the service" (s 44X(1)(d)). The ACCC may also take into account any other matters that it thinks are relevant (s 44X(2)).

Question 8 *How might the arbitrator ensure that BHPBIO retains operational control of its network, including of scheduling, maintenance and capacity expansion decisions?*

Again, in the event that an access dispute was notified, an access provider would have the opportunity to raise operational control issues in its submissions. More generally, the ACCC notes that, under section 44W(1)(d), a determination cannot result in the third party becoming the owner of any part of the facility, or of extensions of the facility, without the consent of the provider. There are examples of railways, including the Australian Rail Track Corporation and Queensland Rail, that are subject to mandated access and yet maintain an effective level of control over operational decisions, including scheduling, maintenance and capacity expansion.

Question 9 *If BHPBIO was to shift from its current timetable system to a run-when-ready system to improve its responsiveness to the market, this would require considerable flexibility, and make the timetabling of third party trains difficult. How might arbitration ensure that the requirements of third parties are met, while not interfering with the way BHPBIO operates its infrastructure? For example, would it be open to the ACCC to determine that BHPBIO may suspend rail services to third parties during periods of capacity expansion, high maintenance or during peak demand?*

It is difficult to provide an answer to question 9 without considering the issue in the context of a particular arbitration. The ACCC would need to consider matters such as:

- the legitimate business interests of the provider, and the provider's investment in the facility (s 44X(1)(a)); the economically efficient operation of the facility

(s 44X(1)(g)); and operational and technical requirements necessary for the safe and reliable operation of the facility (s 44X(1)(g));

- the interests of all persons who have rights to use the service (s 44X(1)(c)) including existing users' reasonably anticipated requirements (s 44W(1)(a)) and the existence of any rights under contracts (s 44W(1)(b) & (c)); and

- the public interest (s 44X(1)(b)).

More generally, the ACCC notes that a type of run-when-ready system has some precedent in the context of mandated rail access. The ACCC understands that, for instance, the scheduling for coal trains in the Hunter Valley rail system operates on a rolling schedule that is dictated by the sequence with which vessels proceed through the queue and are loaded at the Port of Newcastle.

Question 10 *Do issues similar to those outlined above arise in other industries, such as telecommunications? If so:*

How does the arbitration/access framework address these issues?

The arbitration framework in Part XIC of the TPA is similar to Part IIIA:

- an arbitration determination may deal with any matter relating to access by the access seeker to the declared service (s 152CP(2));

- section 152CQ protects reasonably anticipated requirements, contractual rights and ownership of the facility (although, unlike Part IIIA, a determination can require a party other than the access seeker to bear extension costs);

- section 152CR requires the ACCC, when making a determination, to have regard to certain matters including the long-term interests of end-users; the legitimate business interests of the carrier or provider, and the carrier's or provider's investment in facilities used to supply the declared service; the interests of users; the direct costs of supplying access; the value to a party of extensions, or enhancement of capability, whose cost is borne by someone else; and operational and technical requirements.

An access provider can limit uncertainty by proposing an access undertaking. Unlike Part IIIA, Part XIC also provides for anticipatory exemptions (see s 152ATA). An application may be made so that, in the event that a service is declared, the applicant will not be subject to any access obligations. The relevant test – the promotion of the long-term interests of end-users – is set out at s 152ATA(6). A decision by the ACCC to grant such an exemption (in relation to Telstra and Foxtel and digital pay-TV services) was overturned by the Australian Competition Tribunal.

Have the mechanisms developed to deal with these issues in access determinations been effective in avoiding or minimising post-access

disputation?

To what degree does post-access disputation continue to cause delays in investment (in particular capacity expansion and technological advances) notwithstanding the terms of the access determinations?

It is difficult to provide an answer to the question as the issue of disputes arising within the period of operation of an arbitration determination, has not been raised in any of the reviews completed to date of the telecommunications regime. However, as a starting point, the ACCC notes that no party has yet sought to vary an arbitration determination by notifying an access dispute under s 152CM.

Has the Commission received feedback from other industries indicating that third-party access creates disincentives to expand or invest in technology?

The ACCC is aware of arguments made by several operators in the telecommunications industry that the risk of declaration and arbitration leads to uncertainty or otherwise deters investment. The ACCC's view is that these arguments need to be considered in the context in which they are given. There is little evidence of investment being impaired due to the possibility of arbitration of an access dispute. Some perspective is offered in the area of mobile termination services. This area is currently subject to several access disputes. The service has been declared, although described in different ways, since the access regime commenced in 1997. The ACCC arbitrated a series of disputes around the late-'90s early-'00s. There was then a period of quiet, followed by a series of disputes notified over the Dec '04-May '05 period. A key point is that the service description was expanded in June 2004 to include termination provided on 3G mobile networks. In the six months after that, extensive investment plans in 3G networks were announced by Vodafone, Telstra and Optus. The ACCC also approved two 'infrastructure sharing arrangements' in relation to 3G networks in December 2004 that have precipitated extensive network investment during 2005. These observations suggest that declaration of the service has not been associated with the abandonment of investment plans – indeed, quite the contrary appears to have occurred.