SUBMISSION TO THE NATIONAL COMPETITION COUNCIL BY RIO TINTO IRON ORE IN RESPONSE TO THE NATIONAL COMPETITION COUNCIL'S DRAFT RECOMMENDATION DATED NOVEMBER 2005

5 December 2005

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1. INTRODUCTION AND EXECUTIVE SUMMARY

(a) Introduction

1.1 On 6 May 2005, Rio Tinto Iron Ore (***RTIO***) provided a submission (***RTIO's First Submission***) to the National Competition Council (the ***Council***). This responded to the Council's Issues Paper of 11 March 2005, in relation to the application (the ***Application***) by Fortescue Metals Group Limited (***FMG***) for declaration of services provided by BHP Billiton Iron Ore Pty Ltd (***BHPBIO***).

1.2 On 4 November 2005, the Council issued a Draft Recommendation in relation to the Application (the ***Draft Recommendation***), and invited submissions in response to the Draft Recommendation by Monday, 5 December 2005.

1.3 RTIO provides this further Submission in response to the Council's Draft Recommendation. In essence, RTIO strongly contends that:

(a) the Council's process in formulating its Draft Recommendation has been fundamentally flawed in a number of ways, and that those process flaws must be addressed and rectified before the Council can proceed; and

(b) in any event, the Council's analysis in its Draft Recommendation in relation to the six different 'Declaration Criteria' under Part IIIA of the *Trade Practices Act 1974* (Cth) (the ***Criteria*** or the ***Declaration Criteria***) is incorrect — for the reasons set out in this further Submission, the Council cannot be affirmatively satisfied that all of the Criteria are met.

Accordingly, the Council must recommend against declaration of the Mt Newman Service.

(b) Process

1.4 The key process issues identified by RTIO are as follows:

Failure to apply correct onus

1.5 The Council must not recommend declaration except where there is clear and unequivocal information before it upon which the Council can be satisfied that each of the Declaration Criteria is met. Given the weight of material before it, this onus does not appear to have been applied by the Council in this matter.

'Junior explorer' statements

1.6 In reaching its determination, the Council has relied extremely heavily on submissions and statements obtained by it from a small number of unidentified 'junior explorers'. However, the Council has declined to make that information available, in any meaningful form, to RTIO and other third parties for review and scrutiny.

Lack of independent engineering/technical analysis

1.7 The Council has erred in failing to obtain any independent expert technical and engineering advice, to assist it in assessing the relevance and accuracy of the information provided to

it, and to allow it to make a sound assessment (both quantitative and qualitative) for the purposes of Criterion (b) (uneconomical to duplicate) and Criterion (f) (public interest).

1.8 Instead the Council relies extensively on the statements in the Western Australian Government's submission of May 2005 (the ***WA Submission***), which are necessarily qualitative.

Inappropriate reference to the Australian Competition and Consumer Commission

1.9 The Council acted inappropriately in seeking advice from the Australian Competition and Consumer Commission (the ***ACCC***) in the context of the Council's consideration of the Criteria under section 44G of the *Trade Practices Act 1974* (Cth) (the ***TPA***), and then in purporting to rely on the ACCC's response to help to justify its conclusion on Criterion (b).

(c) Declaration Criteria

1.10 As noted in this Submission and previously, the Council must be affirmatively satisfied that all of the Declaration Criteria are met in order to recommend declaration of the Mt Newman Service. RTIO's Submission illustrates that, in fact, the Council cannot be satisfied that any of Criteria (b), (a), (f), (d) or (e) are met.

Criterion (b) — Uneconomical to develop another facility

1.11 RTIO's key points regarding Criterion (b) are as follows:

(a) The Council is in error in seeking to apply a 'social' or 'natural monopoly' test to determine whether Criterion (b) is satisfied.

(b) Even if a natural monopoly test is applied, this test cannot be used when a duplicate facility has either been built or committed to be built.

(c) Accordingly, on this basis alone, Criterion (b) cannot be satisfied to the extent of the duplication of the Mt Newman railway line by FMG's committed railway line from its Chichester Ranges mine sites to Port Hedland (the ***Chichester line***). This conclusion is amplified by the fact that, if Mindy Mindy is developed, the duplicated part of the Service would not be used — FMG and its Mindy Mindy partner would clearly use FMG's Chichester line rather than the 200 kilometres (***km***) of duplicated Mt Newman railway line.

(d) On any proper analysis of the interface costs and diseconomies of scope that would flow from the declaration of the Mt Newman Service, as well as the relative capital and operating costs of duplication compared with access to the Mt Newman Service, it is impossible for the Council to conclude that Criterion (b) is met, even if the natural monopoly test is applied.

Criterion (a) — Promotion of competition in another market

1.12 RTIO strongly disagrees with the Council's analysis in respect of the asserted rail haulage and iron ore tenements markets, and also with the Council's conclusions regarding promotion of competition in those alleged markets.

1.13 RTIO's key conclusions on Criterion (a) are as follows:

(a) The Council's alleged markets for iron ore tenements in the Pilbara and rail haulage in the Pilbara are not separate markets from the global iron ore market.

(b) If the market for iron ore tenements exists separately, it includes both large and small iron ore deposits and is a global market.

(c) If the transport function is in a separate market from the iron ore market, there is no distinction between rail haulage and railway track access. The market is simply the market for the service to move iron ore from mine to port.

(d) There is no basis for the Council's assertion that BHPBIO's Rail Transport Agreement (the ***RTA***) does not constrain BHPBIO's market power, with the result that it must be concluded that access to the Mt Newman Service will not promote competition in any rail haulage or iron ore tenements market (if such markets exist).

(e) There is no basis for the Council to find that competition in the iron ore tenements market (if there is such a market) will be promoted by access to the Mt Newman Service. In fact, all evidence demonstrates that any such market is very competitive.

Accordingly, the Council must conclude that Criterion (a) is not met.

Criterion (f) — Public interest

1.14 In this Application, Criterion (f) is probably the most important of the Declaration Criteria, as it involves issues of national interest that transcend the more competition-focused matters raised by the other Declaration Criteria.

1.15 RTIO's Submission illustrates the likely huge costs to Australia that would flow from declaration of the Mt Newman Facility, including those arising from:

- delayed expansions;
- lost capacity; and
- impaired investment and competitiveness.

1.16 In light of this potentially huge cost to Australia, the Council cannot be satisfied that access to the Mt Newman Service would not be contrary to the public interest. Accordingly, even if it is concluded that the other Declaration Criteria are satisfied, declaration of the Mt Newman Facility should not proceed, on the basis that Criterion (f) is clearly not satisfied.

Other Criteria — Criterion (d) — Health and safety

1.17 In the Draft Recommendation, the Council has failed to properly address this Criterion. In short, the Council cannot be affirmatively satisfied that access can be provided to the Mt Newman Facility without undue risk to human health and safety, because it has not been provided with any evidence to support this conclusion. Accordingly, Criterion (d) is not met.

Other Criteria — Criterion (e) — Effective access regime

1.18 RTIO reiterates its previous submission that the utilisation of BHPBIO's rail haulage service, under the provisions of the Mt Newman State Agreement and the RTA, constitutes an 'effective access regime' for the transport of iron ore from Mindy Mindy to port. Accordingly, Criterion (e) is not satisfied.

2. PROCESS

2.1 RTIO considers that, in a number of fundamental ways, the Council's process in formulating its Draft Recommendation has been flawed. Each of these process issues is further discussed below.

(a) Failure to apply correct onus

2.2 As the Council itself recognised in 'The National Access Regime: A Guide to Part IIIA of the Trade Practices Act 1974, December 2002' (the ***Council's Guidelines***) in relation to 'declaration', the Council must be **affirmatively satisfied** that all of the Declaration Criteria in section 44G of the TPA are met before it can recommend declaration of a service.

2.3 In other words, the Council must not recommend declaration, except where there is clear and unequivocal material before it upon which the Council can be satisfied that each of the Declaration Criteria is met. This 'burden of proof' is consistent with the 'Hilmer Report'[1] (that led to the introduction of Part IIIA of the TPA),[2] various United States authorities relating to the 'essential facilities' doctrine (upon which Part IIIA of the TPA is based),[3] and decisions of the Australian Competition Tribunal (the ***Tribunal***) in relation to third party access.[4]

2.4 RTIO considers that the Council — if it had applied this onus in the process of formulating its Draft Recommendation — could not be satisfied regarding the application of the Criteria so as to enable it to recommend declaration of the Mt Newman Service. In this Submission, RTIO identifies a range of matters and analyses where the Council has ignored the preponderance of material before it or has adopted an inconsistent approach to the analysis of the material. Perhaps the clearest example of this is demonstrated by the inconsistent bases upon which the Council assesses the Criteria. These are highlighted throughout this Submission, but are typified by the assumption that only Mindy Mindy will

[1] National Competition Policy Report by the Independent Committee of Inquiry, August 1993 (the ***Hilmer Report***).

[2] It is noted, at page 248, of the Hilmer Report that:

> The Committee is conscious of the need to carefully limit the circumstances in which one business is required by law to make its facilities available to another. Failure to provide appropriate protection to the owners of such facilities has the potential to undermine incentives for investment.

It is further noted, at page 260, that 'such a regime should be applied sparingly'.

[3] Professor Kalt notes, in his statement annexed to RTIO's First Submission, that 'four criteria must generally be proven in order for a facility to be considered "essential" for antitrust purposes, and for policy to potentially impose rules of mandatory access'.

[4] By way of example, in *Re Duke Eastern Gas Pipeline Pty Limited* (2001) 162 FLR 1 (***Duke EGP***), the Tribunal stated, with respect to the National Third Party Access Code for Natural Gas Pipeline Systems, that:

> …the relevant minister must decide that the pipeline is covered if the relevant minister is satisfied of all of the matters set out in paragraphs (a) – (d) of s1.9, but the minister must decide that the pipeline is not covered if not satisfied of one or more of those matters. (Paragraph 38, page 9)

Moreover, in *Re Sydney Airports Corporation Limited* (2000) 156 FLR 10, the Tribunal stated, with respect to Part IIIA of the TPA, that ' … the Tribunal has to be satisfied affirmatively of each of [the declaration criteria]…' (paragraph 8, page 15).

use the Mt Newman Service, when assessing likely interface costs under Criterion (b), and the assumption that there are numerous potential users when identifying markets and hypothesising on competition effects under Criterion (a).

(b) 'Junior explorer' statements

2.5 The Council's analysis in its Draft Recommendation relies extremely heavily on submissions and statements obtained by it from a small, but unspecified, number of unidentified 'junior explorers'[5] (as defined in paragraphs 4.15 and 4.16 of the Draft Recommendation). For example, the Council's market analysis – in the context of its determination in relation to Criterion (a) – is effectively entirely underpinned by this material and the conclusions that the Council draws from it.

2.6 RTIO has serious concerns about the relevance of these 'junior explorers' – and their statements – to any applicable market analysis. These concerns are addressed in paragraphs 4.23 and 4.24 of this Submission.

2.7 However, given the fundamental importance of the 'junior explorers'' statements to the Council's analysis and Draft Recommendation, RTIO considers that the Council's process for the gathering and reporting of those statements has been entirely inappropriate. Procedural fairness demands that the Council give little or no weight to the material provided by them unless the matters raised below are addressed in relation to these 'junior explorers'.

2.8 RTIO's principal concern is that the statements relied upon by the Council have not been made available for third party review and scrutiny. Instead, for reasons of confidentiality, the Council has elected to simply provide a short summary (at paragraphs 5.12 and 5.13 of the Draft Recommendation) of the Council's factual conclusions drawn from the comments provided by the 'junior explorers'. The approach adopted by the Council is even less defensible, given that it appears that not all 'junior explorers' asked to communicate on a confidential basis.

2.9 All other key proponents in this matter have been required to provide submissions for publication by the Council, in a timeframe allowing scrutiny and analysis by other parties. On any view, the Council's interpretation of, and reliance on, the comments of the 'junior explorers' means that they are also key proponents. However, RTIO and other parties are being given no opportunity to construe or comment upon the 'junior explorers'' statements in the context in which they were provided. Furthermore, having for the first time disclosed the existence and importance of comments by these 'junior explorers', on 4 November 2005, the Council has given all parties only four weeks to respond.

2.10 RTIO has a number of related concerns, all of which pertain to the transparency and fairness of the Council's 'junior explorer' analysis:

(a) First, the identity of the 'junior explorers', and the nature of their projects and tenure (if any), is another critical piece of missing information. In particular, without that

[5] Draft Recommendation, paragraph 4.17.

information, it is impossible for parties to be certain as to the relevant markets in which those 'junior explorers' actually operate.

(b) Secondly, while the Council indicates that it has identified 16 'junior explorers', it is clear that only some of them provided comments to the Council on only some issues (paragraph 4.17 of the Draft Recommendation), with just two providing any written input to the Council. No weight can be given to the material, and yet it is central to the Council's Draft Recommendation.

(c) Thirdly, RTIO is also concerned that much, if not all, of the 'junior explorer' comment was solicited by the Council, after third party submissions were due. In this scenario, particularly given the Council's expressed desire for the 'views of interested parties on matters raised in the draft recommendation' (see paragraph 1.8 of the Draft Recommendation), it is imperative that the 'junior explorers'' comments and submissions be substantiated and made available for review by others.

(d) Lack of independent engineering/technical analysis

2.11 RTIO considers that the Council has erred in failing to commission its own detailed independent technical/engineering advice, particularly as regards expected costings for different possible track construction or expansion scenarios, and also interface and 'diseconomy of scope' costings for the scenario where there is mandated access to the Mt Newman Service. It is inconceivable that the Council could be positively satisfied that each Criterion is met without obtaining such advice, tailored to the specific issues under consideration in this Application. RTIO and BHPBIO are both highly experienced in the matters being analysed, yet chose to obtain independent technical advice. The Council, without any relevant independent technical advice, chose to differ from the positions put by RTIO and BHPBIO and their respective advisers.

2.12 The Council relies very heavily on the WA Submission — this includes no expert costings or analysis to support its conclusions, which are therefore qualitative in nature. Nevertheless, by its own analysis, the Council acknowledges that its conclusion in relation to Criterion (b) must be based on a quantitative exercise, in which it must find that interface costs and diseconomies of scope 'would not outweigh the capital and operating cost savings from access' (paragraph 6.194 of the Draft Recommendation). It is understandable that the WA Submission, on technical matters, was necessarily qualitative, as the Western Australian Government did not have access, at that time, to the detailed technical analyses by TSG Consulting Pty Limited (***TSG Consulting***) and Evans & Peck. RTIO's concern is that reliance has been placed upon the qualitative assertions in the WA Submission, in preference to these detailed analyses.

2.13 RTIO submits that independent advice would both assist the Council in assessing the WA Submission and support the quantitative information provided by RTIO, BHPBIO and the various independent experts commissioned by them. Without such advice, there is no basis upon which the Council could credibly reject the abovementioned costing information provided to it.

2.14 RTIO notes that, in contrast to its approach in this matter, when the Council considered the application by Robe River Iron Associates (***Robe***) for declaration of the rail service provided by the railway line owned by Hamersley Iron Pty Limited in 1998/9, it engaged Rail Management Services Pty Limited (***RMS***) to analyse the costs of various options for the provision of railway line services in the central Pilbara. Indeed, in the Draft Recommendation relating to the Mt Newman Service, the Council refers to the findings of RMS (albeit that they are irrelevant as they are out of date and related to a different railway line). RTIO questions why the Council has failed to seek such independent analysis in this case.

(e) Inappropriate reference to the ACCC

2.15 RTIO objects to the Council seeking an advisory opinion from the ACCC, regarding the possible outcome of arbitral terms and conditions of access should the matter be brought to the ACCC for arbitration. RTIO further objects to the Council's purported reliance on the ACCC's response to help justify its conclusions on Criterion (b).

2.16 The ACCC should play a separate, independent role in Part IIIA access determinations. Once a service is 'declared', parties have the right to seek to negotiate the terms and conditions of access. If terms cannot be agreed, a party may apply to the ACCC to set the terms and conditions in an arbitration, pursuant to section 44S of the TPA. As such, the Council is obliged to make its recommendation without regard to access terms in order to ensure that the two stage process is preserved. This conflict was even acknowledged by the ACCC in its letter to the Council, dated 9 August 2005, which, after acknowledging that the questions raised by the Council are 'not directly related to the NCC's consideration of the criteria under s.44G', then states that '…it would be inappropriate for the ACCC to provide definitive views on these matters without a thorough process'.[6]

2.17 The separate and independent roles that the Council and the ACCC play in access determinations make it impermissible for the Council to effectively seek an advisory opinion from the ACCC, and for the ACCC to give an advisory opinion, regarding the possible outcome of arbitral terms and conditions of access should the matter be brought to the ACCC for arbitration. Consequently, it is also impermissible for the Council to rely on the ACCC's response to help justify its conclusions on Criterion (b).

(f) Conclusion

2.18 RTIO believes that, in order to properly discharge its function, the Council must address and rectify each of these process flaws before it can proceed to finalise and issue any recommendation in relation to the Application.

[6] Letter from Joe Dimasi, acting Chief Executive Officer of the ACCC, to John Feil, Executive Director of the Council, dated 9 August 2005 (www.ncc.gov.au).

3. CRITERION (B) - UNECONOMICAL TO DEVELOP ANOTHER FACILITY

(a) Is a natural monopoly test appropriate?

3.1 RTIO strongly disagrees with the Council's position that a natural monopoly test is to be applied in deciding whether Criterion (b) is satisfied. RTIO repeats paragraphs 7.19 - 7.28 of RTIO's First Submission and reasserts that, for the reasons expressed in those paragraphs (including those espoused by Professors Baumol and Kalt), generally a private investment test should be applied regardless of whether another facility has in fact been constructed or committed.

3.2 However, the Council seems to have misunderstood the thrust of RTIO's First Submission concerning Criterion (b). RTIO maintains that, in circumstances where an alternative facility in fact exists or will be built irrespective of the outcome of the Application, there is no need to apply any *ex ante* test, whether on a private investment or a social cost-benefit basis.

3.3 Even if the Council maintains that a natural monopoly test is to be used for the purposes of Criterion (b) (wrongly in RTIO's view), Professor Ordover, upon whom the Council heavily relies to support the application of the test (and supported by Professor Willig), points out that this test should not be used when another facility has been built or committed. For the reasons outlined in the following paragraphs, the application of a social test is particularly inappropriate in this case and the Council's reasoning in applying a natural monopoly test, so as to justify declaration of the entire section of the Mt Newman railway line to which FMG seeks access, is seriously flawed.

3.4 Further, the nature and ambit of the social test was clarified by the Australian Competition Tribunal (the ***Tribunal***) in *Duke EGP* where the Tribunal stated:

> Rather, "uneconomic" is to be construed in a broader social cost benefit sense, in which the total costs and benefits of developing another facility are brought to account[7] (*our emphasis*).

There is no evidence that the Council has made any attempt to ascertain the social benefits of developing another facility. For example, the Council has not considered:

(a) near term benefits like additional employment; or

(b) longer term strategic benefits such as whether exports would be enhanced by the construction of further railway lines or whether it would be more efficient to increase the utilisation of FMG's Chichester line (as would occur if a spur line to the Chichester line were constructed).

[7] *Duke EGP*, paragraph 59.

(b) Duplicated facilities

No distinction between a constructed facility and a committed facility

3.5 First, there is no valid distinction between a duplicate facility that has, in fact, been constructed and a facility that will be built irrespective of the outcome of the application. In both instances, by the time the access is required, the service will be available on each of the two facilities and the economic analysis must be done on the basis that it is so available. To do otherwise is to ignore reality.

3.6 In fact, in its Draft Recommendation, the Council has in every other instance (including assessment of other aspects of Criterion (b)) conducted its analysis on the basis that the Chichester line will be constructed, thereby duplicating the Mt Newman railway line for over two thirds of the distance in respect of which access is sought. See for example:

- Paragraph 6.72 — 'The Council therefore agrees with RTIO and BHPBIO that the prospective movement of Chichester ores should be excluded from the foreseeable demand for the Mt Newman Service'.
- Paragraph 7.167 — 'FMG's proposals to develop its Cloud Break and Christmas Creek projects in the Chichester Ranges do not rely on the use of the Mt Newman Service'.
- Paragraph 6.172 — 'FMG is likely to require the movement of no more than 10 mtpa…'.

3.7 Contrast this analysis with the Council's comment at paragraph 6.42 of the Draft Recommendation where, in downplaying the commitment that FMG has made to construct the Chichester line, the Council refers to the statement by FMG, in its June 2005 submission, that it might seek to use the Mt Newman railway line for its Chichester deposits if the Service is declared. The Council cannot have it both ways. It must either conduct its analysis on the most likely scenario that FMG's Chichester line will be built as FMG consistently announces, or that it may not be built and FMG will be seeking to rail up to 60 million tonnes per annum (***mtpa***) of ore from Cloud Break and Christmas Creek[8] on the Mt Newman railway line in addition to 10 mtpa from Mindy Mindy.

3.8 Given FMG's advice to the Council that the Chichester line will be built (paragraph 6.43 of the Draft Recommendation) and FMG's announcement, following the release by the Council of its Draft Recommendation, that '[t]he positive recommendation does not affect Fortescue's firm intention to build its own railway from Anderson Point at Port Hedland to its Chichester Range deposits…',[9] there can be no basis for the Council to proceed otherwise than that the railway line will be built as announced, and that it will be operating by the time any access could be achieved through Part IIIA. In fact, on 1 December 2005, FMG and the Western Australian Government entered into a mining State Agreement, the

[8] 'Opening Further the World's Leading Iron Ore Region', FMG presentation to the Asia Pacific Iron Ore Conference, 22 November 2005 (www.fmgl.com.au).

[9] 'Positive NCC Recommendation of Declaration of BHPB Rail Line', announcement by FMG to the ASX, 4 November 2005.

Iron Ore (FMG Chichester Pty Ltd) Agreement (the ***FMG Mining State Agreement***). This Agreement brings into effect the Railway and Port (The Pilbara Infrastructure Pty Ltd) Agreement, providing for the construction of FMG's Chichester line to Port Hedland.[10] This provides further confirmation that the construction of the railway line will occur and that it cannot be described merely as an 'opportunity' (paragraph 6.55 of the Draft Recommendation).

Criterion (b) cannot be satisfied to the extent of the Chichester duplication

3.9 The Council has chosen to rely on Professor Ordover to support its application of the natural monopoly test as a general principle (paragraph 6.3 of the Draft Recommendation), but to ignore Professor Ordover's unequivocal opinion that such a test must not be applied if the facility has been or will be duplicated. Moreover Professor Ordover's opinion was ardently supported by Professor Willig, an equally eminent economist.

3.10 In rejecting the opinions of Professors Ordover and Willig in relation to duplicated facilities, the Council relies, at paragraph 6.12, on a generic statement by Judge Posner as to whether a natural monopoly may in theory exist notwithstanding there being more than one facility. This begs the question. The issue is not whether two natural monopolies can co-exist, but whether a natural monopoly test should be applied in determining whether Criterion (b) is satisfied when the facility is in fact duplicated. The Council decided on a positive answer to this question, notwithstanding the unequivocal opinions to the contrary by Professors Ordover and Willig and without any opinion from any economist supporting the Council's position.

3.11 At paragraph 6.19, the Council also quotes a statement by Judge Posner suggesting the existence of parallel facilities may be a temporary phenomenon that reverts over time to a monopoly configuration. Whilst it may be true that where sunk investment is short-lived, market structure may revert to monopoly quickly, this is not the case in relation to Pilbara railway facilities. As Professor Ordover points out[11], a duplicated facility can remain in the market for a very long time if much of the entry cost is long lived and sunk, as in railroading. The market reality in this case is that, once FMG has constructed its railway line, there is every reason to expect that railway line to remain operational for so long as operating costs can be recovered by selling iron ore in the world market. There is no

[10] 'Signing of State Agreement for Mining', announcement by FMG to the ASX, 2 December 2005.

[11] Statement of Professor Janusz Ordover, Annexure C to RTIO's First Submission, page 11.

market evidence or economic opinion to suggest that, in this case, the existence of the parallel facility would not continue for a very long time indeed.[12]

3.12 A further basis for rejecting the Ordover/Willig position was the Council's view that, even if there are parallel facilities, there could be commercial incentives for both operators to deny access so as to 'extract premiums from a dependant market' (paragraph 6.21 of the Draft Recommendation) and to protect 'Ricardian rents' (paragraphs 6.23 – 6.24 of the Draft Recommendation). These statements again demonstrate the Council's failure to address the facts as they exist in this case. First, the FMG Chichester line has been made an 'open access' line by the relevant State Agreement (see paragraph 2.15 of RTIO's First Submission). It is, therefore, not open to FMG to 'deny access'. Secondly, in paragraphs 7.141 – 7.172 of the Draft Recommendation, the Council finds that access would not promote competition in the iron ore market. As a low cost producer, it is unlikely that sales by BHPBIO would be displaced by sales from Mindy Mindy. In such a situation why would 'Ricardian rents' in the iron ore market (if they exist at all) be threatened by access?

The facts demonstrate that the duplicated part of the Service will not be required

3.13 Not only is the Council's position on duplicated facilities not supported by economic principle in general or economic principle applied to these particular facts, it ignores the reality as to the service that will, in fact, be used in respect of Mindy Mindy ore.

3.14 The application is made by FMG as 'a joint shareholder and operations manager of Pilbara Iron Ore Pty Ltd' (paragraph 3.4 of the Application), Pilbara Iron Ore Pty Limited being the owner of Mindy Mindy. The controlling shareholder of Pilbara Iron Ore Pty Limited, Consolidated Minerals Limited, has made it clear that it proposes to have the ore railed by a third party.[13] This is not surprising, as a mine with maximum forecast production totalling around 60 million tonnes (***mt***) over the life of the mine would be unlikely to have the capital or expertise to purchase, operate, and maintain heavy haul trains, especially if a haulage service is available. This is consistent with the response the Council apparently received from junior explorers, as quoted at paragraph 5.13(a) of the Draft Recommendation.

3.15 Therefore, if Mindy Mindy (assuming it is developed) does not avail itself of BHPBIO's haulage service under the RTA, it will ask FMG to provide this service. In that scenario, it

[12] At paragraph 6.20 the Council suggests that Professor Ordover, at page 11, considers that there will be no competition at the level of services of the facilities. Professor Ordover, at page 11, was making the point that FMG will continue to maintain its railway line in operation, as long as the price it receives for iron ore covers all costs incurred, including the operating costs of the railway. The fact that competition is occurring in relation to the sale of iron ore reduces the chance that FMG would cease to operate its railway line. Professor Ordover is not suggesting, as the Council seems to have assumed, that competition would not also develop in relation to the provision of services. Professor Ordover notes, at page 9 of his paper (Annexure C to RTIO's First Submission), that:

> From a public policy perspective, once a facility has been duplicated or independently committed to be duplicated, there is no need for the regulator to intervene into the unimpeded operation of market forces. Indeed, after entry has occurred, both parties may have a unilateral interest to grant each other access to the facilities in question on mutually agreeable terms: private incentives — and not regulatory fiat — will drive business transactions between the parties.

[13] 'Consmin to approach BHP and Rio for iron ore deal', Metal Bulletin, 9 August 2005.

is highly unlikely that FMG would use the 200 km of duplicated Mt Newman railway line instead of its own under-utilised Chichester line. Not only would FMG unnecessarily incur access fees for more than two thirds of the distance, but operationally FMG would require the flexibility to divert trains from Mindy Mindy to its Chichester mines without having to travel all the way back to Port Hedland. Assume, for example, that there is a breakdown at the Mindy Mindy load out that is not reported until the FMG train is almost at Mindy Mindy. The cost to train cycle time would be about a day compared with perhaps nil if the train could be diverted to Cloud Break.

(c) Conclusion on duplicated facilities

3.16 The Council must confine its analysis to the Mt Newman Spur Portion, as defined in paragraph 7.36 of RTIO's First Submission. To do otherwise is to ignore:

- The consistent announcements by FMG that its Chichester line will be built, supported by the recent signing of the FMG Mining State Agreement.
- The assumptions made by the Council throughout the remainder of its analysis that the Mt Newman Service will not be required for FMG's Cloud Break and Christmas Creek ore.
- Unchallenged economic opinion from some of the world's most eminent economists, including the economist that the Council relies on for the application of the natural monopoly test as a general principle.
- The fact that it will be impossible for FMG to deny access because its line has been declared an 'open access' line by the Western Australian Government.
- The fact that, regardless of what is declared, in reality only the Mt Newman Spur Portion will be used by FMG's trains servicing Mindy Mindy.

(d) Demand and costs

3.17 A number of very important assertions and assumptions are made by the Council as regards foreseeable demand and costs, without any supporting technical or engineering analysis. One of these assertions is at footnote 20 of the Draft Recommendation, where the comment is made that 'there are significant capital efficiencies in double tracking over independent duplication', and paragraph 6.127 of the Draft Recommendation is quoted as the authority for this proposition. However, this paragraph does no more than refer to the WA Submission which is quoted as saying that 'the costs of double tracking would lie in a similar range, but that there would be capital savings from existing looped sections of track…'.

3.18 This raises two points. First, it demonstrates the error in relying on unsubstantiated assertions about costs. RTIO has found that when disruption costs are taken into account, it is generally less expensive to by-pass existing loops when dual tracking than to suffer the disruption costs of incorporating a loop into the dual track. Therefore the statement about capital savings is incorrect and is certainly not backed up by any engineering estimates.

3.19 Secondly, based on this assumption and the Western Australian Government's assertion that dual tracking the Mt Newman railway line would increase capacity to 400 mt (a figure

that RTIO very much doubts and, in any event, much of this could not be used because of physical constraints at the port), the Council adopts the Western Australian Government's conclusion that 'double tracking of the existing facility would be a substantially more efficient outcome than the construction of multiple railways' (paragraph 6.132 of the Draft Recommendation). The Council then concludes that 'it would be uneconomical (at least in terms of capital and operating costs) to develop another facility to provide the Mt Newman Service' (paragraph 6.138 of the Draft Recommendation).

3.20 This analysis, which led to the conclusion in paragraph 6.138 of the Draft Recommendation, is the wrong analysis. Even if the Council's natural monopoly test is applied in accordance with the Council's Guidelines, the test is whether 'over the relevant range of demand, it is cheaper for a single facility rather than multiple facilities to provide the service' (paragraph 6.11 of the Draft Recommendation, which is in similar terms to paragraph 4.21 of the Council's Guidelines). In this case the Council has decided that the relevant or foreseeable range of demand is between 160 mtpa and 200 mtpa (paragraph 6.78 of the Draft Recommendation), not 400 mtpa. Therefore the Western Australian Government's assertion that 'double tracking would expand rail capacity significantly more than the construction of a separate stand-alone facility' is irrelevant to a Criterion (b) analysis. The only question that is relevant is whether it would be cheaper to have separate facilities for the foreseeable range of demand (160 mtpa – 200 mtpa). Neither the Council nor any engineering expert retained by the Council has conducted the analysis to answer this question. Instead, the Council has relied on assertions by the Western Australian Government that address a different and irrelevant question (ie, whether more capacity could be achieved from a dual tracked facility than from two facilities) and apply costings that, in RTIO's experience, are incorrect.

(e) Conclusion on demand and costs

3.21 In light of the above, before turning to the results that would have followed if the analysis had been confined to the Mt Newman Spur Portion (as it should have been – see paragraphs 3.5 — 3.16 above), the Council has not established that 'it would be uneconomical (at least in terms of capital and operating costs) to develop another facility to provide the Mt Newman Service' (paragraph 6.138 of the Draft Recommendation).

(f) The Mt Newman Spur Portion

3.22 For the reasons set out in paragraphs 3.5 — 3.15 above, the only analysis that can be undertaken legitimately, in relation to Criterion (b), is that posited at paragraph 7.38 of RTIO's First Submission and referred to in paragraphs 6.109 and 6.110 of the Draft Recommendation, namely, 'whether it would be uneconomical for anyone to develop another facility to provide the same "Service" as would be provided by the Mt Newman Spur Portion'.

3.23 It is noted that the Council does not consider a spur-line linking Mindy Mindy to FMG's Chichester line because, without any economic analysis, FMG asserts in its June 2005 submission that it would not be 'commercially justif[ied]' (paragraph 6.60 of the Draft Recommendation). Apart from the fact that this assertion is totally unsubstantiated, the Council's approach is at odds with its rejection of a private investment test as the relevant

test for Criterion (b). If the cost of building and operating that part of the spur line that would duplicate the Mt Newman Spur Portion is less than the cost of sharing the Mt Newman Spur Portion, according to the Council's Guidelines, that is the end of the matter. Criterion (b) is not met, whether the cost of building the spur is commercially justified or not.

3.24 When the analysis is confined to the Mt Newman Spur Portion, it is even more demonstrable that the Council cannot be satisfied that Criterion (b) has been satisfied. There has been only one engineering study produced in respect of this section of the track and that was the Evans & Peck study attached to RTIO's First Submission. Notwithstanding the Council's decision to escalate the capital estimates of FMG without escalating the estimates of Evans & Peck, the Council still found, at paragraph 6.119 of the Draft Recommendation, that the escalated cost estimates for FMG's rail spur were 'broadly compatible' with Evans & Peck's un-escalated estimates.

3.25 However, the Council then chose to effectively disregard the Evans & Peck estimates in paragraphs 6.120 and 6.121 of the Draft Recommendation. The Council did so without any apparent reliance on expert engineering or other technical input. Further, the Council had raised the issues addressed in both paragraphs with RTIO, after it had lodged RTIO's First Submission, and Evans & Peck provided a Supplementary Report addressing the issues on 27 June 2005. However the Council did not take this reply into account. Turning to the specific issues raised:

- Paragraph 6.120 — As Evans & Peck advised in both their original report and their Supplementary Report, it is legitimate to take into account the present cost of incremental (ie, additional) operating costs that are incurred as a result of sharing facilities. Without access, these costs would not be incurred by either the service provider or the access seeker. It is therefore essential that they are included in a comparative analysis. The analysis does not include base operating costs that will be incurred irrespective of whether Mindy Mindy product was railed on a separate spur line or on the Mt Newman Spur Portion.
- Paragraph 6.121 — As Evans & Peck advised in their Supplementary Report, the extra 80% of a train cannot be used by BHPBIO unless it incurs additional cost to increase capacity at its mines and port. Further, it is considered by Evans & Peck that, because of the extremely tight maintenance windows, congestion will be greater than the modelling implies and this may be addressed by the unutilised portion of one train.

(g) Conclusion on Mt Newman Spur Portion

3.26 The Council cannot legitimately find that the costs of constructing that part of the Mindy Mindy spur line that would duplicate the Mt Newman Spur Portion 'would exceed the capital, operating, interruption and congestion costs of providing access by a clear margin' (paragraph 6.122 of the Draft Recommendation). This is contradicted by the only engineering report available and the Council's criticisms of it have been answered and are unsustainable. These costs (which the Council acknowledges at paragraph 6.119 of the Draft Recommendation are 'broadly compatible') do not include the very considerable

interface costs and diseconomies of scope, which the Council acknowledges, at paragraph 6.189 of the Draft Recommendation, must be taken into account. These are addressed below, but when added to the estimates provided by Evans & Peck, it is impossible to conclude that the cost of sharing the Mt Newman Service is less expensive than building and operating a spur line that duplicates the Mt Newman Spur Portion.

(h) Diseconomies of scope

3.27 It is noted that the Council, whilst accepting that interface costs must be taken into account in applying Criterion (b) (paragraph 6.189 of the Draft Recommendation), attributes little if any weight to these costs in reaching its conclusion, at paragraph 6.194 of the Draft Recommendation, that 'interface costs would not outweigh the capital and operating costs of access'. RTIO strongly disagrees with this conclusion and believes that, when the true extent of these costs is taken into account, the result will inevitably be that it is cheaper to construct and operate a separate facility rather than convert the highly efficient and responsive Mt Newman Facility into a multi-user facility.

3.28 First, it is important to dispel the notion, expressed in paragraph 6.165 of the Draft Recommendation, that these diseconomies are addressed in the TSG Consulting and Evans & Peck modelling work. They are not. This work simply tries to address, through modelling, the impact on capacity that a third party might have on the system and estimates the additional engineering and operating costs that access would entail, including proposals to try to address the capacity impacts. As pointed out in paragraph 7.43 of RTIO's First Submission, there are 'inestimable' costs that are additional to these costs. These are addressed in Section 11 of RTIO's First Submission and at paragraphs 85 — 108 of BHPBIO's June 2005 submission.

3.29 Since RTIO lodged its First Submission in May 2005, the Report to the Prime Minister by the Exports and Infrastructure Taskforce (the ***Taskforce***) has been released (the ***Taskforce Report***). Extracts from this report are quoted in paragraphs 198 to 203 of BHPBIO's June 2005 submission. The essence of the Taskforce Report is that the multi-user facilities that service the coal industry on the east coast of Australia have not responded to the surge in demand triggered by China's growth, whereas the integrated and dedicated facilities in the Pilbara have responded admirably. The Taskforce Report amplifies and undeniably demonstrates the points made in paragraphs 11.6 and 11.24 — 11.31 of RTIO's First Submission.

3.30 In short, since 2002 when the extent of demand from China began to become apparent, the Pilbara producers have undertaken significant capacity expansions. By 2006 the additional capacity installed and commissioned will be 75 mt (an increase of 35%). At today's prices the extra revenue is worth $3.75 billion per annum. By contrast, since 2002 export capacity for coal (for which demand has increased as much as for iron ore) at the two main multi-user facilities has been as follows:

- Port Waratah Coal Services — no additional capacity. An increase from 89 mtpa to 102 mtpa is expected to come on stream by end 2007.

- Dalrymple Bay Coal Terminal (the ***DBCT***) — an increase from 45 mtpa to 54.5 mtpa to cater for the new Hail Creek coking mine project came on stream in June 2003 (with the expansion committed to in 2001). Thereafter no new capacity has been added (in fact a down-rating occurred in February 2004 following the collapse of a major reclaimer). In March 2006 an additional 5.5 mtpa is scheduled to come on stream through relatively modest changes to the system, following the commissioning of a replacement reclaimer and a series of small de-bottlenecking projects. The next substantial capacity increase (8 mtpa) is scheduled to come on stream in the second half of 2007.

3.31 Thus, excluding the DBCT expansion that was committed to before the surge in demand from China became apparent, coal export capacity at these multi-user facilities will have increased by 6 mtpa or 4% between 2002 and 2006 compared with a lift in Pilbara export capacity of 75 mtpa or 35%. Even taking the DBCT Hail Creek inspired expansion into account, only changes the increase in coal export capacity from 6 mtpa (4%) to 15 mtpa (11%).

3.32 The Council argues that the experience at the coal facilities should not be extrapolated to a declared Mt Newman Facility (paragraph 6.173 of the Draft Recommendation). RTIO disagrees with this conclusion (as does the Taskforce). This is discussed further in paragraphs 3.33 — 3.37 below.

3.33 First, the Council bases this finding on the fact that Mindy Mindy is likely to be the only user of the Mt Newman railway line (paragraph 6.172 of the Draft Recommendation), whereas the coal facilities have a large number of users. This is another example of the Council making inconsistent findings throughout the Draft Recommendation. As mentioned in paragraph 3.8 above, this is inconsistent with the Council's view that FMG's Chichester line may not be built. Whilst RTIO is critical of this finding, if the Council is to maintain such a position it must accept that the Mt Newman railway line could be used to rail up to an additional 60 mtpa of ore from FMG's Cloud Break and Christmas Creek deposits. In addition, in other parts of the Draft Recommendation, the Council's conclusions depend on there being several potential users other than Mindy Mindy. Examples are as follows:

- Paragraph 6.74 — 'The movement of ores from these sites is therefore likely to generate demand for the Mt Newman Facility'.
- Paragraph 6.76 — '…demand arising from the development of new tenements in the vicinity of the Mt Newman Facility, including Mindy Mindy and tenements held by junior explorers'.
- Paragraph 7.183 — 'Many potential entrants to the iron ore market – including Iron Ore Holdings Limited, Aquila/API Group, Poondano Exploration Pty Ltd and Ausi Iron Pty NL – will still be reliant on BHPBIO or RTIO's infrastructure to get their iron ore to market'.
- Paragraph 7.190 — 'Accordingly even if the FMG railway is built, there will remain a large number of iron ore tenements south of the Chichester ranges which, absent

declaration, will continue to rely on access to the rail infrastructure of RTIO and BHPBIO'.

- Paragraph 7.194 — 'Declaration would expand the pool of potential purchasers to include "group (b) participants"'.
- Paragraph 7.208 — 'Potential entrants to the iron ore market have indicated to the Council that access to haulage services is pivotal to their ability to export iron ore'.
- Paragraph 7.209 — 'A third party could gain access to the Mt Newman Service and use its own trains to provide haulage services to other parties'.
- Paragraph 11.26 — 'The Council notes, however, that should declaration occur, it would 'open the door' to any party that wished to negotiate access to the Mt Newman Service. The implications of declaration would therefore extend more widely than Mindy Mindy'.
- Paragraph 11.27 — 'Western Australia, FMG and junior explorers consider that the availability of this service would encourage new entry in the Pilbara iron ore industry'.

3.34 Again the Council must decide on a consistent scenario against which it analyses the Criteria. Either:

- the only likely user is Mindy Mindy for up to 10 mtpa (in which case the Council must assume the FMG duplicate line will be built and its findings in relation to the so called rail haulage and tenements markets cannot rely on other potential users); or
- the likely users include FMG for up to 60 mtpa and several other potential users (whose potential usage could be up to 40 mtpa – paragraph 6.78 of the Draft Recommendation) as well as Mindy Mindy (in which case the Council's basis for downplaying interface costs and distinguishing Dalrymple Bay and Hunter Valley is flawed).

3.35 In any event, the experiences at Dalrymple Bay and Port Waratah cannot be distinguished from the situation that would prevail in respect of the Mt Newman Facility if it were declared, irrespective of whether Mindy Mindy is the only user or there are several others. If a third party is granted rights to use the Mt Newman Facility, it is inconceivable that those rights will not include some basic guarantees such as the right to rail a certain tonnage per week, the right to use equipment of certain specification, and the right to enjoy system improvements (possibly with a corresponding obligation to contribute towards the cost of those improvements). Any decision by the facility owner to achieve significant extra rail capacity through major capital works (eg, dual tracking) or technological change (eg, new trains, such as driverless trains, to reduce cycle times) will interfere with these rights (eg, through disruptions to schedules, changes in equipment and/or changes in user charges or entitlements). Further, any decision involving substantial capital expenditure will only be made if the party incurring the expenditure reaps all of the reward. Otherwise alternative (and from a system perspective, sub-optimal) decisions will be made.

3.36 In sum, major decisions involving the above factors always require negotiation between users to reach consensus on the system improvements to be adopted and an agreed mechanism to apportion the benefits amongst those users who incur the expenditure. If one or more users do not agree (whether for genuine reasons or for gaming purposes), delay is inevitable and arbitration/regulation is required. Neither the Council, nor the ACCC (improper though it was to seek an opinion from the ACCC — see paragraphs 2.15 – 2.17 above), could propose terms whereby these issues could be resolved without the delay of negotiation and possible arbitration/regulation. This is not surprising. Such terms do not exist. If they did, multi-user facilities would not exhibit the problems that they, in fact, exhibit and the Taskforce would not have suggested that efficient single user facilities be protected from access under Part IIIA of the TPA so as to maximise efficiency.[14]

3.37 The inability of the users to agree on the need for, and type of, capacity expansions and on the sharing of the costs and rewards from such expansions are the fundamental reasons that, in the four years since the China-led surge in demand for commodities became apparent, the expansion of multi-user coal facilities has lagged so far behind the Pilbara producers. The Pilbara producers are not constrained by a similar need for consultation and agreement with co-users in order to decide to expand — hence the 75 mtpa increase in capacity so far and the recent announcements by BHPBIO and RTIO of further expansions totalling 35 mtpa. These expansions are worth over $5.5 billion annually to Australia. Delay each of them by only six months and the cumulative cost is $2.75 billion. However, a delay to an expansion at the end of an upward cycle may result in the opportunity being lost for decades (it being no longer available due to other markets capitalising on the demand surge, when the disagreement that led to the delay has been resolved). The cost would then be the present value of the revenue stream from that expansion for the decade or more before the opportunity reappears. To demonstrate how significant this could be, the present value of the expected revenue from the most recent expansions that have been announced (ie, 35 mtpa) over a decade is over $12 billion.

(i) Conclusion on diseconomies of scope

3.38 The interface costs/diseconomies of scope that would inevitably be incurred as a result of declaration of the Mt Newman Service are therefore immense. The figures outlined above relate to the facilities of both BHPBIO and RTIO. However, the position is equally stark if the position is confined to BHPBIO. BHPBIO will have expanded its export capacity by about 30 mtpa between 2002 and 2006, representing extra sales revenue of $1.5 billion per annum. This will be increased by a further 11 mtpa according to BHPBIO's most recent expansion announcement, meaning that the extra revenue from BHPBIO's committed expansions will be over $2 billion per annum.[15]

3.39 In light of the above there can be no basis for the Council's conclusion that it is 'satisfied that the interface costs would not outweigh the capital and operating costs savings from

[14] Taskforce Report, pages 39 and 40.

[15] 'BHP Billiton To Increase Capacity At Western Australian Iron Ore Operations', BHP Billiton Press Release, 20 October 2005 (www.bhpbilliton.com).

access'. Just the cost of relatively modest delays to expansion to meet surges in export demand (much more modest than the two years that have occurred already at Dalrymple Bay) far outweigh any savings that the Council might perceive to be achievable through declaration of the Mt Newman Facility. As RTIO has pointed out, it disagrees that there are any such savings before diseconomies are even considered, especially when the analysis is confined (as it should be) to the Mt Newman Spur Portion.

3.40 Accordingly, the Council cannot be affirmatively satisfied that Criterion (b) is met.

4. CRITERION (A) – PROMOTION OF COMPETITION IN ANOTHER MARKET

(a) Background

4.1 A number of preliminary matters are relevant to the Council's analysis of Criterion (a). At the outset the Council must identify the true operational purpose of the 'service' for which access is sought. It is not bound by the applicant's description of the Service. The Council should approach the task of identifying the true nature of the 'service' that is the subject of an access declaration in the same way as it conducts its analysis to identify relevant markets.

4.2 In this case, the relevant operational ends for the Service sought by FMG is the transportation of ore from Mindy Mindy to Nelson Point. The means by which this is to occur — or FMG's preferences as to how this should occur — are subsidiary to the definition of the Service.

4.3 It is also relevant to note the factual basis for the Council's analysis of Criterion (a) depends, to a large extent, upon undisclosed material obtained from unidentified 'junior explorers'. For the reasons set out in paragraphs 2.5 — 2.10 inclusive of this Submission, this is wholly unsatisfactory. As the Council's analysis and findings on Criterion (a), in relation to the asserted rail haulage and iron ore tenements markets, are almost entirely dependent on this material, the findings are unsafe and should not be maintained unless and until this material and the identity of the companies are disclosed, and various interested parties are given an opportunity to comment.

4.4 Further comment regarding the views expressed by the junior explorers (to the extent they have been reported by the Council) will be made in the context of the market analysis below.

(b) The Council's market analysis

4.5 In its Draft Recommendation (paragraph 7.106), the Council has determined that the following markets are separate from the market in which the Mt Newman Service is provided:

- the global market for iron ore;
- the market for iron ore tenements in the Pilbara; and
- the market for haulage services in the Pilbara.

4.6 Of these markets, the Council has determined that access to the Mt Newman Service will promote competition in the market for rail haulage services in the Pilbara and the market for iron ore tenements in the Pilbara (paragraph 7.212 of the Draft Recommendation). Access will not promote competition in the market for iron ore (paragraph 7.213 of the Draft Recommendation).

4.7 RTIO makes the following submissions regarding the Council's analysis of Criterion (a):

- the market for the Service is not separate from the market for iron ore;
- the asserted markets for rail haulage services and iron ore tenements are not separate from the market for iron ore;
- the market for the Service is not separate from the asserted rail haulage market;
- there is no evidence to conclude that any separate market for iron ore tenements exists;
- in any event, BHPBIO does not possess any significant degree of market power in either of the identified Pilbara markets for rail haulage or iron ore tenements; and
- there is no basis upon which the Council could conclude that access to the Mt Newman Service will promote competition in either of the identified markets for rail haulage or iron ore tenements.

(c) Market for iron ore

4.8 RTIO agrees with the Council's analysis of the market for iron ore as expressed at paragraphs 7.21—7.27 of the Draft Recommendation. RTIO disagrees, however, that the Mt Newman Service is separate from the market for iron ore. For the reasons set out at paragraphs 8.17—8.26 of RTIO's First Submission, RTIO reiterates its view that the hypothetical market for railway track services in the Pilbara is part of the iron ore market identified by the Council in its Draft Recommendation.

4.9 In this regard, it is relevant to note that the Council has rejected the notion that there exists any separate market for 'other mineral ores' or 'other products' (paragraphs 7.13 and 7.15 of the Draft Recommendation). Nor are there separate markets for iron ore production and iron ore marketing since 'there is no evidence of any functional separation of production and marketing in the iron ore market' (paragraph 7.26 of the Draft Recommendation). Since all functions involved in the production and sale of iron ore are in the same market, railing is one of those. Accordingly, for the purposes of this application, it follows from the Council's analysis that the Mt Newman Service is part of the iron ore market.

4.10 The Council has nevertheless concluded (at paragraph 7.32 of the Draft Recommendation) that the vertical integration of iron ore production and the rail function 'is not inevitable' and that 'separate provision of iron ore and track services is economically feasible'. The Council has also concluded that iron ore production and railway assets are 'economically distinct' ie, assets used to mine and process iron ore are functionally separate from assets used to rail iron ore from mine to port (paragraph 7.35 of the Draft Recommendation). The Council observed: 'Put simply, one cannot use a train to dig holes'.

4.11 The Council's application of the asset specificity test to identify assets 'specific to their functional layer' is misconceived. The Council is confusing the task of identifying a service, or identifying different stages of a production process, with the task of identifying separate markets. One cannot use trucks or crushers to dig holes, yet these items are unquestionably integral to iron ore production to enable participation in the iron ore market.

Conversely, conveyors (also regarded as being integral to production) perform no different function to rail.

4.12 It is clear beyond doubt that FMG seeks access to the Mt Newman Service for the purpose of participating in the iron ore market (a notion that supports a finding that the Mt Newman Service is part of a production process – see section 4 of RTIO's First Submission). By excluding the notional markets for iron ore marketing, other minerals and other products, the Council has conceded that the railing of iron ore is inextricably linked with participation in the iron ore market. This is entirely consistent with FMG's claims that 'the development of the Mindy Mindy mine is currently wholly reliant on accessing the facility' (the Application, paragraph 4.20, *our emphasis*). As FMG concedes, the railing of ore is central to its participation in the market for iron ore.

4.13 The Council is referred to the memorandum prepared by Mr Stephen King and Mr Rodney Maddock and provided to the Council in the context of the access application pursued by Robe in 1998. After making reference to the decision of Justice Nicholson in *Regents Pty Ltd v Subaru (Aust) Pty Ltd*[16] (in which His Honour considered markets in the context of a vertical production chain), Messrs King and Maddock observed that:

> Simply because a transaction occurs at a different vertical stage of the production process compared with another transaction does not imply that the transactions are in different markets (page 8 of memorandum).

They concluded that:

> Even if it is decided that the use of the rail service is not part of a single production process, it may be the case that the proposed market is simply a sub market of a broader market for the mining, processing and export of iron ore (page 9 of memorandum).

(d) Market for rail haulage services

4.14 RTIO considers that the Council is in error in determining that the rail haulage market is separate from the market for railway track services. The Council could not point to any substantive difference in the product, geographical or time dimensions of the putative markets for railway track services and rail haulage. However, the Council has concluded that railway track services and rail haulage services are functionally distinct. The Council therefore relies solely upon asserted differences in the functional dimensions of each market in support of its conclusion that separate markets exist.

4.15 In reaching this position, the Council has made findings that:

- scheduling control and operational flexibility are 'not necessarily inconsistent with functional separation' as it assumes that these matters could be addressed by the ACCC in making an access determination (paragraph 7.91(a) of the Draft Recommendation);
- management costs would not be high enough to make vertical integration inevitable (paragraph 7.92 of the Draft Recommendation);

[16] (1998) ATPR 41-647.

- there is a price for track services which is greater than the 'interface cost' of separating track and haulage services, yet less than the capital and additional operating costs of duplicating the facility, such that vertical integration is not inevitable (paragraph 7.93 of the Draft Recommendation); and
- in applying the 'asset specificity' test, the bundle of assets required to provide track services is distinct from those required to provide haulage services (paragraph 7.101 of the Draft Recommendation).

4.16 The Draft Recommendation provides no basis upon which the Council could make any of the costs assumptions referred to in paragraphs 7.91 and 7.93 of the Draft Recommendation for the purpose of its Criterion (a) analysis. While acknowledging the existence of these costs of separation, neither the Council, nor any technical expert on behalf of the Council, has apparently undertaken any analysis of these costs which would enable the Council to be affirmatively satisfied that a haulage service is in fact economically separable from a track service. Nor is it open to the Council to avoid undertaking any such analysis by simply assuming that the matter will be dealt with by the ACCC as part of an access determination. In these circumstances, having accepted that both management costs and interface costs would constitute an additional cost of separation of track and haulage services, the Council should have concluded that the existence of these costs support the submissions of RTIO and BHPBIO that railway track services and rail haulage form part of the same market.

4.17 The asset specificity test, relied upon by the Council at paragraph 7.101 of the Draft Recommendation to support its finding that the markets for rail haulage and railway track are economically distinct, is arbitrary and artificial. The Council applies this test to distinguish between the assets used to provide track services from those used to provide haulage services. How is ore haulage to be provided without a railway track and associated infrastructure? How is the track service to be utilised without rolling stock? It is clear that this same bundle of assets provides the service to transport ore from mine to port.

4.18 The Application (at paragraph 7.1) reaffirms that rail haulage of iron ore is not functionally distinct from railway track services for the transport of iron ore. The sole reason for seeking access to the service is to transport iron ore from Mindy Mindy to Port Hedland. At Part 8 of its Application, FMG details 'prior negotiations' over access. These negotiations are set out in a detailed chronology which is annexure 3 to the Application, and relate entirely to the haulage of iron ore. There is no reference to any prior negotiation whereby FMG sought railway track access. It is thus clear that FMG does not regard rail haulage as functionally distinct from the railway track service; either will result in FMG meeting its objective of having ore transported from Mindy Mindy to port. In fact, as pointed out at paragraphs 3.14 – 3.15 of this Submission, Mindy Mindy will use a rail haulage service rather than a railway track service, whether that service is provided by BHPBIO or FMG. Mindy Mindy will be indifferent to the means by which the 'service' is provided. From Mindy Mindy's perspective, getting its ore to port will be all that matters.

4.19 Further, in its submission to the Council dated 6 May 2005 (***FMG's Submission***), FMG does not seriously contend that there is any separate market for railway track services. Instead, BHPBIO's alleged market power is expressed in terms of the ability of BHPBIO to prevent competition in 'moving iron ore' from mine to port (FMG's Submission, paragraph 4.7).

4.20 As noted by Messrs King and Maddock in their 1998 memorandum:

> …under the approach to market definition that has been adopted by the Australian courts,… there are no separate markets for 'the use of rail infrastructure for the transportation by train of iron ore or other minerals from mine sites to ports or processing facilities within the central Pilbara region of Western Australia' and the 'market for rail haulage in the central Pilbara'. Rather with regards to the service in which access is sought, these are part of the single market. Consequently it is our view that the claimed 'rail haulage' market is not a market 'other than the market for the service' (page 10 of memorandum).

(e) The market for iron ore tenements

4.21 The Council has also determined that there exists in the Pilbara a market for iron ore tenements. It has made this determination notwithstanding that, in the published submissions responding to the Council's issues paper, no party has made reference to the existence of any separate tenements market in its Criterion (a) analysis. Further, in reaching this conclusion, the Council acknowledges that:

> There is no such thing as an iron ore tenement per se (paragraph 7.54 of the Draft Recommendation).

4.22 Ultimately the Council concludes that the relevant product market is the 'market for rights to mine specific iron ore deposits' (paragraph 7.62 of the Draft Recommendation, *our emphasis*). In other words, the market that the Council defines is a narrow market where there is a **right to mine** (ie, a mining tenement as distinct from an exploration tenement) and where there is a **specific iron ore deposit**. This definition appears to be deliberately narrow as it is similarly described in paragraph 7.63 of the Draft Recommendation as 'mineral tenements containing proven iron ore deposits' (*our emphasis)*.[17] Irrespective of whether it was intended that the market be defined as narrowly as this, the Council does not establish that the asserted market (whatever it may be) is confined to the Pilbara, or even Australia, or that access would have any impact on competition in the asserted market.

4.23 In the context of the Council's definition of this market, it is relevant to note that the Mindy Mindy deposit is not in this market since the Mindy Mindy tenement does not include 'rights to mine' and, if a JORC compliant resource is necessary, then Mindy Mindy also fails in this respect. Moreover, the junior explorers with whom the Council made contact are apparently not participants in this market, since they have not 'prove[d] up' resources in their tenements (paragraph 7.177(b) of the Draft Recommendation). According to publicly

[17] It is left unsaid whether the identified, or proven, iron ore deposit must be an Australasian Code of Reporting of Exploration Results, Mineral Resources and Ore Reserves (***JORC***) compliant resource, but if it is not, it is questionable whether one could claim to hold a 'specific' or 'proven' 'iron ore deposit'.

available information, the companies listed at paragraph 7.183 of the Draft Recommendation have not reached this stage. Those companies are all at the early stages of exploration, some have not yet commenced drilling, some have not even obtained exploration tenements (ie, they are still at the application stage), and none has a proven iron ore deposit. Even if the Council contends that Mindy Mindy and the junior explorers it contacted are potential participants in the Council's asserted market, it is inappropriate for the Council to base its findings wholly on discussions with these potential participants rather than on actual participants in the asserted market.

4.24 It is perplexing why the Council chose to define the iron ore tenements market so narrowly. Perhaps this was to confine the product market to iron ore tenements in the Pilbara rather than exploration tenements for all minerals over a wider geographic area. If any separate market for tenements exists then, as RTIO pointed out in RTIO's First Submission, it is a market for exploration tenements for all minerals and is not confined to the Pilbara or, for that matter, Australia. It seems to RTIO that the junior explorers contacted by the Council may be in this market (if it exists). As the Council notes, at paragraph 7.175 of the Draft Recommendation, the increased interest in iron ore exploration tenements is a direct result of the improvement in iron ore prices. One would expect that either the companies referred to or the promoters of those companies would have had or potentially will have an equally passionate interest in tenements for other minerals in other areas when the prices for those other minerals are attractive. In other words, to the extent that such a market exists, it is the speculative international market for exploration tenements.

4.25 Be that as it may, the problem the Council has created by defining the market so narrowly is that it has not referred to one participant in this market other than BHPBIO and RTIO. As the Council notes at paragraph 7.76 of the Draft Recommendation, the market in which these companies operate is not confined to the Pilbara. The deposits 'at the other end of the spectrum' (paragraph 7.77 of the Draft Recommendation), if they are part of the narrow market defined by the Council, have not been identified. The Council cannot make any findings on either the existence of this market or the effect of access on competition, unless and until it has identified participants in this market and analysed transactions in that market. It has not done so.

4.26 In the access application pursued by Robe, there was no assertion of any independent iron ore tenements market either by Robe or the Council. Rather, Robe identified the iron ore product market to embrace 'iron ore development, mining, processing and sales markets'. RTIO submits, again, that this is the relevant market, especially when the market is confined to specific proven deposits of iron ore. Once a deposit has reached this stage, entry into the iron ore market is the objective.

4.27 FMG complains, in the Application, that 'independent prospecting for iron ore in the Pilbara' is limited by BHPBIO's asserted market power (paragraphs 7.51 and 7.52 of the Draft Recommendation). For the reasons outlined above (ie, no identified deposit and no right to mine), this activity is not part of the market defined by the Council. It is also a misstatement as there have been many iron ore deposits discovered and proved up by parties that did not have their own infrastructure (both in the Pilbara and elsewhere). This

is dealt with in paragraphs 4.63 — 4.72 below when examining Council's findings in relation to promotion of competition. Suffice to say at this point that in finding that this narrow market exists, the Council has not examined the position in respect of these deposits, but appears instead to have relied solely on statements by parties that are apparently not in the alleged market.

4.28 RTIO maintains that the market for rights to mine a specific proven iron ore deposit is not separate from the iron ore market; indeed, it is integral to that market. RTIO reiterates the matters set out in paragraphs 8.6—8.71 of RTIO's First Submission. Having regard to the Council's findings that the tenements market is limited to a market for rights to mine specific proven iron ore deposits, those matters — and particularly the views of Mr Williams[18] — are even more apposite since Mr Williams based his views on the assumption that the iron ore tenements market embraced wider rights of exploration, prospecting and development.

4.29 The Council confuses rights relating to exploration and prospecting with rights to mine a specific proven iron ore deposit in its analysis of the functional and geographic dimensions of the iron ore tenements market. To illustrate the Council's confused approach to its analysis of the functional dimension of the iron ore tenements market, we refer to paragraph 7.70 of the Draft Recommendation. In this paragraph the Council expresses its conclusion that 'it is not inevitable that exploration and mining activities are vertically integrated'. What is the relevance of exploration activities in this context, given their deliberate exclusion from the definition of the iron ore tenements market adopted by Council? Rather, adopting the Council's own assumption, the issue is whether rights to mine or exploit specific proven deposits of iron ore are functionally separate from the iron ore market. Clearly they are not. Indeed, the 'right to mine' is perhaps the most fundamental pre-requisite for participation in the iron ore market.

4.30 In response to the analysis by Mr Williams that the market for iron ore tenements is not separate from the iron ore market, the Council asserts that:

> It is sufficient that there are companies which, whatever their intentions, will either choose or be obliged to sell part or all of their "find" due to a lack of funding to exploit a deposit and/or a lack of access to the necessary rail infrastructure (paragraph 7.67 of the Draft Recommendation).

This statement does not establish the existence of a separate market. All that it demonstrates is that, when deposits are proven, development is the objective and to achieve development, transactions of this nature often take place. But this activity is simply part of the 'iron ore development, mining, processing and sales market' that was the subject of analysis in the Robe application, and is the market that should properly be the subject of analysis here.

4.31 The Council's findings regarding the geographic dimension of the market for iron ore tenements are set out in paragraphs 7.71—7.81 of the Draft Recommendation. RTIO

[18] Report by Frontier Economics Pty Limited, Annexure F to RTIO's First Submission, paragraph 117.

reiterates its previous submission that the evidence demonstrates that, if any separate iron ore tenements market exists, it is a global market. As mentioned above, the Council acknowledges that this might be so for deposits of a 'significant size', but does not identify or analyse any of the smaller deposits that the Council assumes to exist but which do not form part of the global market. The Council has no basis to find that the geographic dimension of the rights to mine specific proven iron ore deposits is confined to the Pilbara.

4.32 It is implicit in the Council's reasoning that the product dimension of the tenements market as defined by the Council is the market for tenements containing deposits of 'very small size and marginal economic viability' (paragraph 7.77 of the Draft Recommendation) (presumably embracing a 'right to mine' and being a 'specific' 'proven' deposit rather than just a conceptual exploration target so as to fall within the definition adopted by the Council at paragraphs 7.62 and 7.63 of the Draft Recommendation). Further, the market for tenements containing specific proven 'deposits of very small size and marginal economic viability', on the Council's reasoning, must be within proximity of the BHPBIO Mt Newman railway line for the purpose of assuming BHPBIO can exercise market power (paragraph 7.190 of the Draft Recommendation). Such a market definition is not supported by fact or any economic analysis. It is far too narrow. If there is a market for proven iron ore deposits, that is separate from the global iron ore market, there is no basis for the Council to conclude that this is not part of the global market for iron ore deposits generally (both large and small).

(f) Conclusion on market definition

4.33 By reason of the matters above, it is clear that the market for the Service is not separate from the global iron ore market and, even on the assumptions adopted by the Council, is not separate from any putative rail haulage market. Further, the asserted rail haulage and tenements markets are not separate from the global market for iron ore. In addition, there is no basis for the Council to conclude that the alleged iron ore tenements market, as defined by the Council, exists or if it does, that its geographic dimension is anything other than worldwide.

(g) Promotion of competition

4.34 Irrespective of the market analysis adopted by the Council, RTIO maintains that the Council cannot be satisfied that access will lead to a promotion of competition in any of those markets. This is because:

(a) BHPBIO's Protected Contractual Rights (***PCRs***) will preclude access to the Mt Newman Service;

(b) as the Council has determined, access would not cause a material increase in competition in the market for iron ore;

(c) BHPBIO's haulage obligations under the Mt Newman State Agreement constrain BHPBIO in the exercise of any market power in any putative separate markets for iron ore tenements or haulage services;

(d) BHPBIO would also be constrained by the presence of FMG's open access Chichester line. Accordingly, there is no basis for the Council to find that access

would promote competition in any rail haulage market. This conclusion is reinforced by the fact that no prospective provider of rail haulage services to third parties has been identified by the Council; and

(e) there is no evidence to support the Council's findings that access will promote competition in any iron ore tenements market. In fact, the evidence which exists, and which the Council did not consider, leads to the contrary conclusion.

Protected contractual rights

4.35 The Council has determined under Criterion (a) that access to the Mt Newman Service will promote competition in the markets for rail haulage services and iron ore tenements in the Pilbara.

4.36 In undertaking its analysis of Criterion (a) the fundamental assumption adopted by the Council is that BHPBIO possesses relevant rights to exclude FMG (and other parties seeking to compete with BHPBIO) from its railway assets which are the subject of this application. Properly understood, it is these rights of exclusion which the Council relies upon as the basis for its finding that BHPBIO is able to exercise 'market power' in these markets.

4.37 BHPBIO's rights regarding its Mount Newman rail assets are entirely derived from the Mt Newman State Agreement. As a consequence, any analysis of BHPBIO's 'market power' in the asserted Pilbara tenements and rail haulage markets inevitably involves consideration of the contractual rights arising under the Mt Newman State Agreement. Because of the unusual circumstance that the entirety of BHPBIO's operations are conducted pursuant to and in accordance with the Mt Newman State Agreement, the Council must analyse the nature and extent of these contractual rights as part of the process of satisfying itself regarding Criterion (a). In this instance, this is not a task that the Council can defer to the ACCC.

The test adopted by the Council

4.38 At paragraph 7.115 of the Draft Recommendation the Council acknowledges that, in appropriate cases, it may have regard to the effect of section 44W(1)(c) of the TPA in considering Criterion (a). The Council has formulated its own 'test' to the effect that PCRs should be considered where 'there is a very high likelihood that the right in question would constitute an absolute barrier to the promotion of competition' and has concluded that:

- it is not clear to what degree, if any, the alleged PCRs are necessarily inconsistent with the Mt Newman Service (paragraph 7.126 of the Draft Recommendation);
- any 'exclusive possession' right appears to expire in 2009 (paragraph 7.126 of the Draft Recommendation);
- the Council is not satisfied that there is a 'very high likelihood' that the alleged protected contractual rights would constitute 'an absolute barrier to the promotion of competition' (paragraph 7.127 of the Draft Recommendation); and
- the rights in question are 'not relevant' to the Council's consideration of Criterion (a) (paragraph 7.128 of the Draft Recommendation).

For the reasons set out below, each of these conclusions is erroneous.

Inconsistency between the PCRs and access to the Service

4.39 The PCRs asserted by BHPBIO are more fully described in Annexure 13 to BHPBIO's submission dated 3 June 2005 (***BHPBIO's Submission***). They are said to arise by reason of the Mt Newman State Agreement, the ancillary RTA, and the special lease (Port Hedland to Mount Newman (Lease No. 3116/3687) (the ***Special Lease***) relating to the Mt Newman railway line. BHPBIO summarises its PCRs as:

- a right to exclusive possession of the land on which the Mount Newman rail assets are constructed; and
- a right to exclusive use of the Mt Newman Facility and associated infrastructure (subject to the conditional obligation under the RTA for third party carriage).

4.40 Each of the PCRs asserted by BHPBIO existed as at 30 March 1995 and remains in existence. Further, each of these rights ultimately is sourced to the Mt Newman State Agreement which, in relevant part, operates and takes effect notwithstanding the provisions of any other Act or law. As the Western Australian Government noted in its 1998 submission filed with the Council in connection with the Robe access application:

> An important feature of State Agreements is that, unlike other statutes which perform regulatory functions of one sort or another, they are facilitating documents. Whereas other statutes are able to be changed at will, the provisions of the State Agreements are only able to be changed by mutual agreement in writing between the parties to each Agreement. State Agreements therefore provide certainty that ground rules for the life of each Agreement project cannot be changed unilaterally.
>
> Agreement holders are not required to allow third parties to operate their own rolling stock and associated ancilliary services on the agreement holder's railway, although they may choose to do so.

4.41 Irrespective of the characterisation of the PCRs asserted by BHPBIO, it is common ground between the Council, FMG and BHPBIO that BHPBIO possesses the right to exclude FMG (and other potential producers) from the Mount Newman railway track assets. As stated above, this is the fundamental assumption which underpins the Council's finding that BHPBIO is able to exercise 'market power'.

The Special Lease

4.42 At paragraph 7.118 of the Draft Recommendation the Council places reliance upon clause 3(1) of the Special Lease for asserting that:

- the Western Australian Government could allow third party access to the Mt Newman Service; and
- clause 3.1 of the Special Lease is inconsistent with the right of exclusive possession.

4.43 These assumptions are inconsistent with the Council's 'market power' analysis and ignore the operation of the proviso to clause 3.1 of the Special Lease which protects BHPBIO from any undue prejudice or interference with its operations under the Mt Newman State

Agreement. They are also contradicted by the Western Australian Government's submission in 1998 which reaffirmed that 'Agreement holders' cannot be obliged to allow third parties to operate rolling stock on railway the subject of State Agreements. As a consequence, there is no basis upon which the Council can be affirmatively satisfied that a grant of access (rather than mere declaration) would not have the effect of depriving BHPBIO of its PCRs under the Mt Newman State Agreement.

Expiry of rights

4.44 The Council's reasoning appears to be:

- the right of exclusive possession entirely relies upon the Special Lease (paragraph 7.112 of the Draft Recommendation);
- the right of exclusive use in part relies upon the Special Lease (paragraph 7.112 of the Draft Recommendation); and
- the Special Lease is due to expire on 7 April 2009 (paragraph 7.121 of the Draft Recommendation).

4.45 However, the Council concedes that the Mt Newman State Agreement is not subject to any expiry date and that there is no suggestion that the parties to the Mt Newman State Agreement will seek to terminate or significantly amend it (paragraph 7.119 of the Draft Recommendation). Clause 8 of the Mt Newman State Agreement guarantees to BHPBIO ongoing renewal of the Special Lease for the term of the State Agreement. Rather than assuming the expiry of the Special Lease, the Council must recognise continuation of the Special Lease in accordance with the terms of the Mt Newman State Agreement and must therefore find that the right to exclusive possession will continue for the life of the Mt Newman State Agreement.

Waiver of PCRs

4.46 The Council, at paragraph 7.123 of the Draft Recommendation, states that:

> There is no evidence to suggest whether the Mount Newman Participants might waive their protected contractual rights during any post-declaration access negotiations with FMG or other parties.

In the absence of evidence to the contrary, the Council should act on the basis that BHPBIO will not waive any relevant PCR. No such contrary evidence is before the Council and there is no conceivable basis upon which the Council could conclude that waiver might occur. In fact, in its submission, BHPBIO confirms its intention to rely upon – and not waive – those rights.[19]

4.47 In any event, any potential willingness on the part of BHPBIO to waive its PCRs for commercial or other reasons is not in itself a proper basis for disregarding the existence of PCRs as part of the Council's consideration of Criterion (a). More importantly, the declaration process cannot be used as a means of procuring the waiver of those rights.

[19] BHPBIO's Submission, paragraphs 147 and 148.

4.48 BHPBIO's protected contractual rights mean that, with or without declaration, BHPBIO cannot be required to provide access under Part IIIA. Accordingly, declaration could not promote competition in any relevant market. Therefore Criterion (a) cannot be satisfied. Notwithstanding this conclusion, we consider below the specific findings the Council went on to make in relation to the asserted markets for rail haulage and iron ore tenements.

(h) Promotion of competition – haulage services

4.49 The Council concludes in its Draft Recommendation that BHPBIO has the ability to exercise market power so as to adversely affect competition in any asserted market for rail haulage services and that access would therefore promote competition in that market.

4.50 For the reasons given below (and previously discussed at paragraphs 8.62 — 8.67 of RTIO's First Submission):

- BHPBIO does not have the ability to exercise market power to inhibit competition in any asserted rail haulage market; and
- access will not promote competition in that market.

Market Power – Constrained by State Agreement and RTA

4.51 At paragraph 7.198 of the Draft Recommendation, the Council (in RTIO's view, correctly) identifies BHPBIO's obligations to provide haulage services as a potential constraint on its ability to exercise market power in the hypothetical haulage services market. The Council has concluded, however (paragraph 7.199 of the Draft Recommendation) that it is 'unlikely' that the Mt Newman State Agreement and RTA significantly constrain BHPBIO's ability to exercise market power as the RTA does not satisfy several of the Criteria needed to identify effective access regimes and has not, in fact, resulted in access to haulage services.

4.52 For the purpose of assessing whether BHPBIO has market power, the issue is not whether the RTA is an 'effective access regime'. Rather it is whether the RTA creates an effective means whereby third parties can obtain rail haulage. The RTA clearly does, as it gives any potential iron ore producer a legally enforceable right to negotiate access to haulage services, with any dispute about the terms and conditions of access being referable to an independent expert. The RTA establishes a negotiate/arbitrate regime similar in structure to the regime that would apply under Part IIIA of the TPA if declaration were made. In RTIO's view, the matters raised by the Council at paragraph 10.26 do not detract from the fact that the RTA creates an effective means whereby third parties can obtain rail haulage, for the reasons set out below.

- The Council states that the Western Australian Court of Appeal (***WA Court of Appeal***) has found that a third party's project must be 'well advanced' before it has a right to negotiate with BHPBIO under the RTA.[20] What Justice Templeman in fact said was '…I do not see how the "detailed contractual arrangements" contemplated by CL 2 of the schedule to the Rail Transport Agreement could be

[20] *Hancock Prospecting Pty Ltd v BHP Minerals Pty Ltd* [2003] WASCA 259 (***Hancock Prospecting***).

established except by a person whose plans for mining were well advanced'.[21] All that Justice Templeman is saying, is that as a practical matter anyone who wishes to negotiate a detailed rail haulage agreement is likely to have plans for mining that are well advanced. The ultimate finding of the Court was that Hancock Prospecting (the owner of an undeveloped deposit) had the right to seek services under the RTA. The Court stated that it would prefer a construction 'which leads to a commercially sensible result, having regard to the objective of the agreement'.[22] On the basis of the decision, and the reasoning that underpins it, the owner of a deposit with a genuine need to obtain haulage services can do so under the RTA. The knowledge that this right exists, when a deposit reaches the development phase, is all that is required to constrain BHPBIO's asserted market power.

- The RTA clearly establishes a right to negotiate, with disputes referable to an independent expert. Given the clear right established, on any view resort to Court enforcement is unlikely to be necessary. Even if Court action became necessary, there is no basis for assuming that the Court process would take longer than the Part IIIA process, which requires negotiation, followed by ACCC arbitration, followed potentially by an appeal to the Tribunal. In contrast, under the RTA once a dispute is referred to an independent expert the decision of that independent expert is final and binding.
- Resolution of disputes by independent experts or arbitrators is a commonly used and often very effective means of dispute resolution. It is wrong for the Council to assume that an access regime using an independent expert rather than a regulator as the dispute resolution forum will be less effective in practice.

The matters mentioned by the Council at paragraph 10.26(e) of the Draft Recommendation, whilst relevant to Criterion (e), do not detract from the practical effectiveness of the RTA and are not relevant to the issue of whether the RTA constrains BHPBIO's alleged market power in relation to rail haulage services. It quite plainly does have this effect.

4.53 In addition to its comments on effectiveness, the Council also asserts that, 'on a practical level', BHPBIO's haulage obligations have not resulted in any party gaining access to haulage services. The Council points to 'an absence of transactions for haulage services', other than those occurring between related parties, as evidencing a lack of competition in the market for haulage services. These conclusions, however, ignore the facts that:

- the nature and extent of BHPBIO's obligations to provide an iron ore haulage service were not resolved until November 2003;
- Mindy Mindy has taken no action since the WA Court of Appeal decision to pursue its rights to avail itself of haulage services under the Mt Newman State Agreement;

[21] *Hancock Prospecting,* paragraph 33.

[22] *Hancock Prospecting*, paragraph 34.

- none of the junior explorers contacted by the Council are quoted as having made any assertion to the effect that BHPBIO has refused any requests to haul ore; and
- to the contrary, a number of the junior explorers contacted by the Council in fact contemplate requesting BHPBIO to provide a haulage service in the near future (see, for example, paragraph 7.208 of the Draft Recommendation).

4.54 Stated simply, the underlying assumption made by the Council is that BHPBIO is unconstrained in its exercise of market power by reason of its ability to withhold haulage services. This assumption is directly contrary to the decision of the WA Court of Appeal and contrary to the expressed intentions of junior explorers to utilise those haulage services in the appropriate circumstances. It is clear that any market power BHPBIO may be thought to have would be constrained by the RTA.

Market Power – Constrained by FMG's Chichester line

4.55 The Council also recognises at paragraph 7.198 of the Draft Recommendation the fact that another party may construct a railway from the Pilbara to a port facility may also constrain BHPBIO's exercise of market power.

4.56 As discussed above, it is abundantly clear that FMG will construct an open access railway line from Cloud Break to Port Hedland in the near future. The Council, however, dismisses the relevance of this line because the Council asserts the line could only service the northern part of the Pilbara. RTIO notes however:

- it is unclear how many (if any) of the '16 junior explorers' hold tenements in areas that could be serviced by the Mt Newman railway line but not by the FMG Chichester line; and
- as demonstrated above it will be more economical for Mindy Mindy to build a spur line to FMG's Chichester line than to access BHPBIO's line based on the Evans & Peck analysis of direct costs (without even taking into the account the significant potential interface costs and diseconomies of scope that access would cause). It is likely that this would also be the case for other parties with a potential mine in the vicinity of the Mt Newman railway line (they would also have the option to build a spur line to FMG's Chichester line – or share such a spur line were it constructed to service Mindy Mindy).

4.57 The existence of the open access (and probably lightly used) FMG Chichester line would therefore in all likelihood provide a real opportunity for any company that wished to provide rail haulage services in the Pilbara.

4.58 The practical effectiveness of the RTA, and the presence of the open access FMG Chichester line, mean that BHPBIO has no ability to exercise market power to inhibit the development of competition in any asserted rail haulage market.

Access would not promote competition

4.59 The absence of any ability to exercise market power to distort rail haulage competition means access could not promote competition in the asserted rail haulage services market.

4.60 Even if this were not the case access would still not promote competition in any meaningful sense. There is no practical likelihood of a new provider of rail haulage services emerging even if the Mt Newman line were declared since:

- FMG's access request is focused solely on transport of ore from Mindy Mindy to Port Hedland; and
- the prospect of a third party rail haulage provider is very remote. It should be noted that the Council received no submission from any entity that intends to conduct business as a haulage provider. The costs — of purchasing trains and locomotives, shipping them to the Pilbara, establishing the necessary maintenance facilities and hiring and retaining a crew of skilled drivers and other staff — are likely to be prohibitively expensive. It seems unlikely that any company would be prepared to incur such expenses given the significant uncertainty about whether any of the junior explorers' potential deposits will ever be developed. As the Council mentioned at paragraph 7.208(b) of its Draft Recommendation, junior explorers are more interested in rail haulage than track access. This is because of the cost of purchasing and operating trains. If a potential developer cannot justify this, it is unlikely that an independent haulier would be able to do so.

Conclusion on promotion of competition haulage services

4.61 As a result there is no basis on which the Council could conclude that access would promote competition in the alleged rail haulage market.

(h) Promotion of competition — tenements market

4.62 If BHPBIO is constrained from exercising market power in the asserted rail haulage market, it is similarly constrained in the exercise of market power in any asserted tenements market.

4.63 In its analysis of competition in the iron ore tenements market, the Council asserts that a company in BHPBIO's position (ie, a provider of track services) might have several incentives to exercise its market power. These are set out in paragraph 7.177 of the Draft Recommendation. With regard to these 'incentives', RTIO points out the following:

- There is no evidence proffered by the Council or any party making submissions to the Council to the effect that BHPBIO in fact has pursued these 'incentives' in the iron ore tenements market. The Council cannot rely on comments by junior explorers on this subject as they are not in the market defined by the Council and have not yet reached the point of having a deposit that might enable them to consider development options, including transport options. In fact, most entities that participate in the narrow market defined by the Council (ie, those with a 'right to mine') will have advanced to firm mining proposals, and have in place the transport arrangements they intend to rely upon, before they enter this market.
- More particularly, the analysis is inconsistent with the Council's geographic dimension of the tenements market as Pilbara wide. Based on the analysis of incentives, it would be more accurate to describe the geographical dimensions of the tenements market assumed by the Council for its market power analysis as 'the

market for very small and marginally economic iron ore tenements adjacent to or in the proximity of the BHPBIO railway track'.

4.64 The Council then proceeds to assess whether BHPBIO has the ability to exercise its market power. The Council has noted RTIO's obligations to provide rail haulage and FMG's proposal to construct its Chichester line. Those matters, in addition to BHPBIO's haulage obligations, are dismissed as constraints on the exercise of market power by BHPBIO, because:

- no third party has been able to negotiate access arrangements with RTIO (paragraph 7.181 of the Draft Recommendation);
- the Chichester line is not planned to commence operation until late 2007 (indeed, the Council has suggested that it is 'uncertain to proceed') and as such its effective constraint is 'diluted' (paragraph 7.182 of the Draft Recommendation); and
- many 'potential entrants' to 'the iron ore market' (**not the tenements market**) are located in proximity to the BHPBIO and RTIO railway lines (paragraph 7.183 of the Draft Recommendation).

4.65 The Council understandably confuses potential entrants into the 'iron ore market' with participants in the asserted Pilbara tenements market: as explained in paragraph 4.30, these form part of the same market. In addition, the Council refers to the absence of 'access' (ie, haulage) arrangements with RTIO. The absence of haulage arrangements with RTIO under its State Agreement is equally explained by the absence of requests for haulage services.

4.66 At paragraphs 7.89-7.194 of the Draft Recommendation, the Council sets out its findings as to whether access would promote competition in any tenements market. The Council concludes that 'declaration' (access) would expand the pool of potential purchasers to include 'group (b)' participants. 'Group (b)' participants are defined to be:

> …those entities which have an enforceable right to — or reasonable prospects of being able to negotiate — access to rail and port infrastructure in the Pilbara (paragraph 7.192 of the Draft Recommendation).

The Council incorrectly states that '[a]t present, there are no entities in group (b)'.

4.67 It was affirmed by the WA Court of Appeal in late 2003 that the Hope Downs Iron Ore Project (***Hope Downs***) was such an entity. It appears that many of the junior explorers (who, as pointed out, do not appear to participate in the tenements market defined by the Council) believe that they are in group (b), since they have foreshadowed their intention to negotiate rail haulage arrangements. Again, this is consistent with the findings of the WA Court of Appeal that third parties have an enforceable right to seek access to haulage services under the RTA prior to the time when iron ore products are to be carried. Finally, for some reason which is not apparent, the Council appears to regard haulage of ore of 'related or integrated' third parties as irrelevant to its analysis of access to rail haulage.

4.68 In addition to the above comments refuting the Council's assertions that BHPBIO has market power to exercise incentives so as to restrict activity in the alleged iron ore

tenements market, the Council provides no evidence whatsoever of activity in fact being restricted. The Council has relied on statements that it claims were made by junior explorers who are not in the market defined by the Council and, given the fact that exploration has a high failure rate, are quite likely never to be in the market. More importantly, the Council has not analysed deposits that are, or have been, in this alleged market to see whether the assertions it makes are justified. The assertions include the following:

- 'not invest[ing] the resources necessary to 'prove up' iron resources … unless and until [there are] some prospects of gaining access to rail transport' (paragraph 7.177(b) of the Draft Recommendation); and
- 'the price of these tenements is maintained at a low level (because they are under-developed and, in the absence of rail transport, unattractive to other investors)' (paragraph 7.177(c) of the Draft Recommendation).

4.69 If one looks at exploration generically, it is axiomatic that explorers prove up deposits before addressing infrastructure availability. If this did not happen then there would be no mines in remote parts of the world. For example, the mines in the Pilbara would not exist, those at Weipa would not exist, Escondida in the Andes would not exist, and Grasberg in Irian Jaya would not exist. RTIO is currently spending millions of dollars on exploration in Guinea in the search for iron ore, notwithstanding the fact that there is no infrastructure and it will be necessary to rail the ore up to 2000 km, if a deposit is proved up and developed.

4.70 Turning specifically to the Pilbara, post the 1970s after infrastructure had been built, there has been very significant expenditure on exploration and proving up resources by parties that did not have access to nearby infrastructure beyond the third party carriage provisions in State Agreements. Probably the best example of this is FMG itself, which is not only proving up, but developing, its Cloud Break and Christmas Creek deposits. Other examples include Hope Downs, West Angelas, Yandicoogina, McCamey's Monster and Marandoo. At the time these deposits were discovered, and proved up to the point of identifying an iron ore resource, the holders of the tenements did not have any particular transport arrangements in place. This did not inhibit the tenement holders from proving the deposits up as they knew that if the resources were sufficiently attractive they would be developed, either using their own infrastructure or the infrastructure of others. If this involved a cooperative arrangement with an existing infrastructure provider then so be it. The value obtained by the tenement holder far exceeded the cost of proving the deposit up.

4.71 It is therefore wrong to say that explorers are reluctant to prove up deposits because of lack of rail access. Apart from the fact that rail haulage rights in fact exist, the empirical evidence, both in the Pilbara and elsewhere, demonstrates that the pattern is to find and prove up deposits and then address infrastructure options as part of development scenarios.

4.72 The second assertion is that the price of tenements is kept artificially low. Talking to junior explorers about their experience in trying to sell tenements which have not been 'proved up' provides no basis for the Council to find that prices of tenements that contain proved iron ore deposits are depressed. In fact, the Pilbara is a very competitive environment for

the sale of interests in proven deposits. This was most recently demonstrated when bidders (both incumbents and new entrants) competed fiercely with each other to acquire a stake in Hope Downs. It is also demonstrated by the market capitalisation of companies such as FMG, demonstrating that investors are prepared to pay substantial sums for a stake in a company that has a Pilbara resource, notwithstanding that it does not yet have its own infrastructure. Doubtless the capitalisation of many of the junior explorers contacted by the Council will also be high considering the early stage their exploration tenements (or applications) are at.

(i) Conclusion on Criterion (a)

4.73 In light of the above, RTIO is strongly of the view that:

- The alleged markets for iron ore tenements in the Pilbara and rail haulage in the Pilbara are not separate markets from the global iron ore market.
- If a market for iron ore tenements exists separately, it includes both large and small iron ore deposits and is a global market.
- If the transport function is in a separate market from the iron ore market, there is no distinction between rail haulage and railway track access. The market is simply the market for the service to move iron ore from mine to port.
- There is no basis for asserting that the RTA does not constrain BHPBIO's market power and this plus other options (including FMG's open access line) mean that access to the Mt Newman Service will not promote competition in any rail haulage or iron ore tenements market (if such markets exist).
- There is no basis for the Council to find that competition in the iron ore tenements market (if there is such a market) will be promoted by access to the Mt Newman Service. In fact, all evidence demonstrates that any such market is very competitive.

5. CRITERION (F) — PUBLIC INTEREST

(a) Importance of Criterion (f)

5.1 Criterion (f) is probably the most important of the criteria against which an access application is assessed as it involves issues of national interest that transcend the competition focused issues in Criteria (a) to (e). Merely because a service satisfies Criteria (a) to (e) does not mean that it is in the public interest that the service be declared. There are numerous instances where one could postulate that a declaration could be harmful to Australia's economic or strategic interests, even though technically Criteria (a) to (e) may have been satisfied.

5.2 It is, therefore, disturbing to note the Council's position that '[w]here Criteria (a)-(e) are met, there is a presumption that declaration would promote the public interest by promoting competition in dependant markets and by avoiding wasteful duplication of infrastructure' (paragraph 11.2 of the Draft Recommendation). Not only is this alarming from a policy perspective, as public interest considerations extend well beyond the prism of competition focused criteria, but it is a misapplication of the law as enunciated by the Tribunal in *Duke EGP*. There the Tribunal found at paragraphs 145 and 146:

> … [the public interest criterion] does not constitute an additional positive requirement which can be used to call into question the result obtained by the application of [the other criteria]. [The public interest criterion] accepts the results derived from the application of [the other criteria] but enquires whether there are any other matters which lead to the conclusion that coverage would be contrary to the public interest.
>
> As the Tribunal is not satisfied that criterion (a) has been met, it is not necessary for us to give independent consideration to [the public interest criterion][23] (*our emphasis).*

5.3 Thus the Tribunal found that public interest was a separate criterion. All that the Tribunal said about Criterion (f)'s relationship with the other criteria was that it could not be used to call into question the result obtained by the application of the earlier criteria. Accordingly the Tribunal found that, because Criterion (a) was not met in that case, it did not then have to consider the public interest criterion at all. The Tribunal simply did not consider the reverse situation where Criteria (a) to (e) are met and Criterion (f) must then be considered. There is nothing in either the Tribunal's decision or the clear language of section 44G(2)(f) of the TPA to suggest any 'presumption' that Criterion (f) is satisfied if the other Criteria are satisfied.

5.4 The Council has therefore made a critical error of law by beginning its enquiry in relation to Criterion (f) with a presumption that Criterion (f) is satisfied if Criteria (a) to (e) are satisfied. The Council must consider as a separate matter whether access or increased access to the Service would not be contrary to the public interest and must not bring to that inquiry any 'presumption'.

[23] *Duke EGP,* paragraphs 145 and 146.

5.5 In fact, in relation to the Application, RTIO is of the strong view that at least Criteria (a) and (b) are not met and, therefore, the 'presumption' inappropriately applied by the Council should not matter. There is also an overlap between the issues that must be considered by the Council in relation to, at least, Criterion (b) and Criterion (f). Whilst RTIO does not suggest that the analysis under Criterion (f) should call into question the Council's conclusions under Criterion (b) (as the Tribunal observed in *Duke EGP* was not permissible), the same considerations should demonstrate to the Council that both Criterion (b) and Criterion (f) are not satisfied.

(b) Australia's economy will be damaged

Expansions will be delayed

5.6 The principal concern in declaring the Mt Newman Facility is that third party access will impede its efficiency and, especially, its ability to respond to surges in demand for iron ore, such as has been recently experienced as a result of China's growth. The Council is referred to paragraphs 3.26 — 3.39 above, all of which demonstrate the inevitable cost to export revenue that will be occasioned if the Mt Newman Facility is converted from a dedicated integrated facility to a multi-user facility. BHPBIO and RTIO have expanded export capacity by 75 mt, between 2002 and 2006, and have recently announced a further expansion of 35 mtpa. This 75 mt expansion has happened when multi-user coal facilities have barely increased capacity at all. The extra export revenue to Australia from the 75 mt expansion is about $3.75 billion each year and when the further 35 mtpa recently announced expansions are added, this will increase to approximately $5.5 billion, based on current prices. This rapid growth provides a significant benefit to the Australian public in a number of respects:

- It improves Australia's trade balance. The contribution from iron ore to Australia's improved trade performance was noted by the Australian Treasurer in August 2005.[24]
- It provides revenue to the Australian Government by way of increased taxation and to the Western Australian Government by way of increased royalty receipts.
- It contributes significantly to employment growth both within BHPBIO and outside BHPBIO (eg, construction contractors, service providers and the wider community due to the flow-on effect).
- It contributes to the development of communities, including remote townships and aboriginal communities.

5.7 The difference in performance of multi-user facility and a single-user facility has recently been demonstrated in the coal industry, and this experience has caused loss of export revenue to Australia. According to the latest forecasts by the Australian Bureau of Agricultural and Resource Economics (***ABARE***) and coal analysts, Barlow Jonker, steaming coal exports from Indonesia will exceed those from Australia for the first time in

[24] 'Balance of payments – June quarter 2005', Press Release by the Treasurer, 31 August 2005.

2005.[25] This has been attributed to the fact that Australia's coal export infrastructure has not been able to expand to meet demand.

5.8 There is no doubt that BHPBIO's ability to respond to surges in demand will be adversely affected by third party access. Two recent independent reports (by the Taskforce and the Reserve Bank of Australia (***RBA***)[26]) have attributed the quick response of the Pilbara producers to their dedicated and integrated infrastructure and attributed the slow response of the east coast coal producers to their multi-user infrastructure. What is unknown is whether the impact will only delay the expansions that would have taken place or whether the 'lowest common denominator' effect, that is an inevitable consequence of multi-usage, will have the effect of permanently curtailing some expansion programs. In addition, by the time users agree on an expansion the opportunity may have been lost and the expansion may be delayed indefinitely. In an internationally competitive market, upswings in demand drive opportunities for those suppliers who can respond the fastest to the increased demand. Those unable to respond quickly risk missing the opportunity. The opportunity may not present itself again for a decade or more (if at all). It does not matter which of these effects materialises. The cost is measured in billions of dollars and is manifestly against the public interest. For example, if the most recently announced expansions of 35 mtpa were delayed for a decade, based on current prices the present value of the $1.75 billion in export revenues lost each year is in excess of $12 billion.

5.9 It is noted that the Council seeks to distinguish the multi-user coal facilities from the position that would pertain at the Mt Newman Facility if it were declared (paragraph 6.172 of the Draft Recommendation) and that the Council believes the concerns expressed by BHPBIO and RTIO 'may be overstated' (paragraph 11.31 of the Draft Recommendation). As demonstrated at paragraphs 3.32 — 3.37, the basis for the Council distinguishing the coal facilities is flawed. Further, two independent reports have drawn the same conclusions as RTIO and BHPBIO. It is, therefore, unjustified and unsafe for the Council to say that the impact is not sufficiently significant as to 'outweigh the capital and operating cost savings from access' (paragraph 6.194 of the Draft Recommendation).

5.10 Turning to the position that the Council takes, that the experience at the coal facilities will not, or need not, translate to a declared Pilbara rail facility, it is worth analysing some of the fundamental issues that arise at multi-user facilities and asking why these will not manifest themselves in the Pilbara. At both Port Waratah and Dalrymple Bay there has been no uniformity of views on whether and when to expand. If a user wants more capacity the first step is to look at how the allocation of capacity amongst users might be revised so as to give that user more capacity. This is referred to in the Taskforce Report, at page 2: 'users and regulators focus more on shifting slices of the pie than on ensuring that the pie expands to meet competing demands'.

[25] 'Bottlenecks drive Hunter down the coal ladder – Rival on top of exports', Newcastle Herald, 18 November 2005, page 15.

[26] The RBA's Statement on Monetary Policy, 7 February 2005.

5.11 When users finally get to the realisation that capacity needs to be expanded as a whole, rather than simply reallocated (a situation that appears not to have been reached until 2004 at the coal terminals), the issues to address are:

- What is required?
- How will the expanded capacity be allocated?
- How will the costs be shared?

5.12 These are the fundamental issues that have been, and are still being, wrestled with at Dalrymple Bay and Port Waratah. Different users have different interests that affect the position they take on such matters. For example, at Port Waratah some users wish to participate in a new independent port that is due to come on stream in 2009 and, consequently, will not agree to any commitment or protocol in respect of Port Waratah that impedes such participation. At Dalrymple Bay there is currently a difference of view on what the scope of the expansion capacity ultimately required is and how capacity from the 8 mtpa expansion due to come on stream in 2007 is to be allocated. This has the potential to impede the implementation of the expansion if it is not resolved. Such differences of view are commonplace. At the Mt Newman Facility, if there are multiple users, similar issues will arise and this is likely to lead to a delay while the differences are resolved. If the usage is as the Council projects at paragraph 6.172 of the Draft Recommendation (ie, Mindy Mindy only up to a maximum of 10 mtpa for six years), the scope for dispute is high as this mine will have an entirely different perspective from BHPBIO's. Based on current information, Mindy Mindy will be resource constrained and will not be interested in any change to the initial terms of access. Further, its short mine life will mean that it is unlikely to fully utilise capital initially spent to service its needs, let alone expansion capital. It is likely BHPBIO will be at the other end of the spectrum and constantly looking for any means available to change the system so as to improve efficiency and expand capacity. If the optimal means of achieving this involves a change to the above or below rail components of the Mount Newman rail system it will impact on Mindy Mindy (whether the impact be disruption to schedules, change in above rail equipment, change in operating practices or a combination of these). It is not realistic to expect that the applicable access terms would permit BHPBIO to impose these changes unilaterally (some of which could be quite expensive, such as a change to above rail equipment). There will need to be a negotiation and, ultimately, arbitration or regulation.

5.13 If the situation is as the Council contemplates in other parts of the Draft Recommendation, where there are several other users including FMG in respect of its Chichester deposits (see paragraph 3.32 above), then there will be an even greater diversity of views and a greater likelihood of the parties taking positions to try to 'shift … slices of the pie' as between the users.

Capacity will be lost

5.14 In addition to the cost to Australia from lost export opportunities, there will be a permanent loss of capacity arising as a result of third party access. This was referred to in paragraphs 11.7 — 11.12 of RTIO's First Submission where examples of the clashes that have occurred through multiple usage of the Hunter Valley line were provided. It has been

estimated that even the relatively limited multi-usage by coal hauliers on the Hunter Valley railway accounted for an 8% capacity loss over the entire system. As the losses are primarily a function of the 'human factor', they cannot easily be engineered out of the system and do not show up by modelling, such as that undertaken by Evans & Peck and TSG Consulting. It is also not simply a case of building into a system 8% extra capacity, as one cannot identify where the problem will arise and, therefore, cannot know where the work should be done (and, even if this were possible, the cost of an 8% increase in capacity 'across the board' would be very high and would be unlikely to be able to be borne by a new entrant). Therefore when addressing the public interest, as well as Criterion (b), the cost of this lost capacity must be factored in on top of the capital and operating costs of the type estimated by Evans & Peck that address congestion and items that can be identified.

5.15 There must be no confusion between the lost capacity costs referred to above and the costs of delays to expansion as referred to in paragraphs 5.6 – 5.12 above. They are additive, not inclusive. They can both be substantial because they involve the present value of lost exports. If there is a delay to an expansion (as distinct from a permanent loss) then the cost may be very large for the period of the delay (eg, $3.75 billion for every year of delay for the 75 mtpa expansions by BHPBIO and RTIO between 2002 and 2006). If, however, there is a permanent downgrading of the system, then the loss over what otherwise could be achieved is a smaller figure each year, but an even larger number on a present value basis (eg, 8% of BHPBIO's and RTIO's combined capacity in 2006 of 293 mtpa, is 24 mt amounting to $1.2 billion per annum which, if it continues for 20 years, has a present value of almost $17 billion).

Investment will be affected

5.16 In addition to the chilling effect on investment addressed, at length, in paragraphs 11.13 — 11.23 of RTIO's First Submission, there is a further impact on investment that will result from third party access. If BHPBIO intends to expand its rail capacity, but there is no immediate agreement by the users on the proposed expansion, BHPBIO will look at options other than rail to try to increase capacity, notwithstanding that a rail expansion may be the optimal means of expanding capacity. Apart from the delay that this would entail, it would have one of two outcomes, both of which would affect efficiency and BHPBIO's competitiveness in the international iron ore market. These are:

- there may be no decision to expand because the sub-optimal route does not pass BHPBIO's investment criteria; or
- there may be a decision to invest in the sub-optimal route, thereby incurring a waste of resources and damaging BHPBIO's competitiveness in the international iron ore market.

5.17 Each of the above outcomes is against the public interest as it will involve a loss of revenue and, if the second option is taken, a waste of resources and a reduction in competitiveness (which ultimately will cause a loss of revenue).

(c) Benefits of access are overwhelmed by the detriments

5.18 Against each of the very substantial detriments to Australia that would flow from third party access to the Mt Newman Facility, there are few countervailing benefits. As in other sections of the Draft Recommendation, the Council relies (when assessing Criterion (f)) on qualitative assessments made by the Western Australian Government about the benefits that it perceives would flow from access. The Council's position is summarised at the end of paragraph 11.35 of the Draft Recommendation as follows:

> While there are mixed views as to whether the shared use of railways, or the construction of multiple railways would better support growth in iron ore exports, the Council is not persuaded that declaration would have a negative impact on the industry's performance. In the view of the Western Australian Government, declaration would indeed bring developmental benefits for the industry and iron ore exports.

5.19 The thrust of the benefits postulated is that a declared Mt Newman Facility will provide an avenue for third parties to rail their ore to port. As the Council acknowledges, by excluding FMG's Chichester ore from the likely demand, the FMG 'open access' Chichester line will be built. In addition, there is BHPBIO's RTA which has only recently been held by the WA Court of Appeal to be effective and enforceable for a potential entrant. There are also the rail carriage obligations of RTIO under its various State Agreements. These issues are discussed in greater detail in paragraphs 4.51 to 4.54 above.

5.20 The issue to examine under Criterion (f) is, regardless of whether the Council agrees with RTIO's views that these potential entrants already have a means to get their iron ore to port if they have a viable deposit, whether the very substantial public detriment is worth it? The Council states, at paragraph 6.172 of the Draft Recommendation, that it is likely that the only user will be Mindy Mindy with maximum demand of 10 mtpa. Whether it is only Mindy Mindy, or it is the much higher usage that the Council contemplates elsewhere in the Draft Recommendation, the message is clear. It is much better from the perspective of Western Australia and Australia not to interfere with the infrastructure that is working so efficiently in its current configuration. If it is considered that more options than currently exist need to be provided to potential users, then it would be much more preferable, from the public interest perspective, for Government to support the construction of an independent rail line. When the FMG open access railway line is built, this would only entail support for a spur line to connect with FMG's Chichester line if the existence of that spur were the difference between a deposit being developed or being left undeveloped.

(d) The risk is too high

5.21 In light of the potentially huge cost to Australia, declaration of the Mt Newman Facility should not proceed on the basis that Criterion (f) is not satisfied, even if the Council believes (wrongly in RTIO's view) that the other Criteria are satisfied. The Council may believe that the views of BHPBIO, RTIO, the Taskforce, and the RBA are overstated, but the chance that they are not overstated is substantial. The damage that will flow will be immediate and irreversible. In one stroke, Australia's most competitive industry will have been deprived of a key ingredient that accounts for its efficiency and resultant competitive edge.

6. OTHER CRITERIA

(a) Criterion (d) — Health and safety

6.1 Section 44G(2)(d) of the TPA requires the Council to be satisfied that access to the Service can be provided without undue risk to human health and safety. In its Draft Recommendation, the Council stated that it was satisfied that access to the Mt Newman Service can be provided without undue risk to human health and safety on the grounds that:

- use of the Service will be regulated by relevant Western Australian rail safety legislation;
- access terms can impose minimum standards for skills, training, maintenance and communication;
- access terms can allow for BHPBIO (or a similarly qualified provider) to provide the control function in respect of the Mt Newman Facility; and
- access seekers can gain access to essential rail safety technology – including intellectual property where necessary – under Part IIIA of the TPA.

RTIO strongly disagrees with this finding and asserts that the Council cannot, on the evidence before it, be satisfied that Criterion (d) has been made out.

6.2 In the Application, FMG attempted to assure the Council that access to the Service can be provided without undue risk to human health and safety, by stating that its operations on, or utilising, the Facility will be 'in accordance with best principle' and will 'comply with all relevant…legislation'. Further, in its submission, dated 6 May 2005, FMG simply stated that Criterion (d) is made out because 'there are [not] any health or safety matters that could not be dealt with through the terms and conditions of access'. FMG has, however, made no attempt, in either the Application or its submissions, to describe the manner in which its operations can be integrated without undue risk to human health and safety. Consequently, the Council cannot be affirmatively satisfied that access can be provided without undue risk to human health and safety as it has not been provided with any evidence to support this conclusion.

6.3 RTIO has raised legitimate arguments, in its Submissions, in support of the Council finding that it is not satisfied that Criterion (d) has been made out. In particular, RTIO reiterates its key argument, set out in paragraph 9.4 of RTIO's First Submission, that:

> Until arrangements concerning safety issues in respect of the Applicant's operation on BHPBIO's railway track are put in place and capable of analysis, it is not possible for the Council to be satisfied that the access sought in the Application can be provided 'without undue risk to human health and safety'.

Having read the submissions proffered by BHPBIO to the Council, RTIO also supports the arguments, set out in BHPBIO's Submission, in relation to Criterion (d). RTIO emphasises that the Council should not underestimate the health and safety issues that **will** arise as a result of access.

6.4 RTIO is of the view that, in its Draft Recommendation, the Council dealt with the submissions made by RTIO and BHPBIO in a perfunctory manner and failed to adequately analyse the specific issues raised by RTIO and BHPBIO. The Council deferred consideration of the key issues raised in these submissions by stating, consistent with FMG's Submission, that these issues will be dealt with through the terms and conditions of access. RTIO maintains that this approach is inconsistent with the wording and intent of the legislation and is, therefore, unacceptable. The Council must properly address this Criterion and, if it is not completely satisfied that access to the Service can be provided without undue risk to human health and safety, then it cannot recommend declaration of the Service.

(b) Criterion (e) — Effective access regime

6.5 The Council reduces its consideration of Criterion (e) in effect to three issues (paragraph 10.16 of the Draft Recommendation):

(A) Does the existence of an effective access regime for a service which is a substitute for the Mount Newman Service mean that the application fails to meet Criterion (e)?

(B) If so, is the third party haulage service provided for by the State Agreement and the RTA a substitute for the Mount Newman Service?

(C) If so, is the access regime established by the State Agreement and the RTA an effective access regime for the purpose of Criterion (e)?

6.6 RTIO does not consider that these 'questions' are properly formulated or dispositive of Criterion (e). Rather, the sole question is whether FMG is able to effectively access infrastructure which would enable transportation of iron ore from Mindy Mindy to port. Utilisation of BHPBIO's rail haulage service under the provisions of the RTA undoubtedly results in an affirmative answer.

6.7 Nevertheless, adopting the Council's own questions as set out in paragraph 10.16 of the Draft Recommendation, RTIO makes the submissions set out below.

Question A — Effective access for a substitute service

6.8 The Council has determined that an effective access regime for a 'substitute' service which in fact is not **the** service cannot satisfy Criterion (e). However, it appears that the Council misconceives the nature of RTIO's First Submission regarding Criterion (e). RTIO is not contending that rail haulage is a substitute service, but in fact that it relevantly provides the same service sought by FMG for Mindy Mindy: the use of BHPBIO's infrastructure to transport ore from Mindy Mindy to port. Understood in this context, question A is not relevant.

Question B — Is rail haulage a substitute service?

6.9 For the reasons set out in paragraphs 4.14 — 4.20 and as stated in response to question A, question B is similarly irrelevant. The service that FMG seeks is movement of its ore. Rail haulage is not a 'substitute' service.

Question C — Compliance with Competition Principles

6.10 The Council has determined that the State Agreement and the RTA might not comply with certain sub-clauses of clause 6.4 of the Competition Principles, namely:

- the RTA 'might not' satisfy sub-clause 6.4(b) because it is not clear when third parties have a right to negotiate access (paragraph 10.26 of the Draft Recommendation);
- it is 'unlikely' that the State Agreement and RTA would satisfy sub-clause 6.4(c) because there is no mechanism other than the court process by which a third party can enforce rights under those agreements;
- it is 'unlikely' that the State Agreement and the RTA would satisfy sub-clause 6.4(g) or (o) because of asserted limitations of the resources and powers of the 'independent expert' to gather financial information or determine inequitable outcomes; and
- the RTA does not address some elements of sub-clause 6.4(i) 'including':
  - the economic value to the owner of additional investment in the facility;
  - economically efficient operation of the facility; and
  - the benefit to the public of having competitive markets.

6.11 There is a question as to whether the State Agreement and the RTA must comply with the Competition Principles in order to be an 'effective access regime' for the purposes of Criterion (e). Section 44(G)(3) of the TPA only applies to a regime established by a State or Territory Government, not to a regime arising from commercial agreement covering private assets. Section 44DA, in any event, makes it clear that the Competition Principles should be regarded as 'guidelines' only. The Council, instead, has approached its analysis of Criterion (e) on the basis that it is bound by the Competition Principles.

6.12 Leaving aside these matters, RTIO responds to the Council's determinations in relation to question C as follows:

(a) No clear right to negotiate access – While the Council acknowledges the WA Court of Appeal decision in *Hancock Prospecting*, it is implicit in the Council's finding that it believes that the Court of Appeal has failed to give the RTA commercial efficacy. It appears the Council misconceives the effect of that decision. Specifically, it is not, as the Council asserts, a matter for 'BHPBIO discretion' as to when a party has a right to negotiate (paragraph 10.26 of the Draft Recommendation). The Court of Appeal has given the RTA commercial efficacy and it is clear that the right to negotiate will arise well before a project comes into production.

(b) Mechanism for enforcing rights – The dispute resolution processes under the RTA and the State Agreement are perfectly satisfactory mechanisms for parties to enforce rights. It is no less satisfactory than the corresponding procedures in Part IIIA of the TPA.

(c) Resources of independent expert – There is no foundation for the criticism made of the independent expert procedure under the RTA. There is no reason to think that the process will not produce an equitable outcome or that the independent expert cannot request (or will not be provided with) 'financial information' to enable him to discharge his duties under the RTA.

(d) Other matters – There is no reason why any of the matters referred to by the Council in paragraph 10.26(e) of the Draft Recommendation would not be taken into account by a court, or another body, in resolving access disputes, whether under the RTA or in respect of BHPBIO's wider carriage obligations under the State Agreement.

Criterion (e) — Conclusion

6.13 As set out in RTIO's First Submission, RTIO believes that the utilisation of BHPBIO's rail haulage service, under the provisions of the Mt Newman State Agreement and the RTA, constitutes an 'effective access regime' for the transport of iron ore from Mindy Mindy to port. For this reason, Criterion (e) is not satisfied.

5 December 2005