Competition Policy Review
Final Report

Submission to the Treasury

May 2015

Table of Contents

1 EXECUTIVE SUMMARY

The Competition Policy Review Final Report (the "Report") is a detailed and thoughtful piece of work and the Review team should be commended. We believe that a positive response by the Government to the recommendations has the potential to boost Australian productivity growth by improving competition and regulation and thereby increasing efficiency in the investment and operation of infrastructure. We have focussed our comments on areas where we believe our views can add to the debate.

This response is a public document

1.1 Port Privatisations

The Report expresses concern with the current port privatisation processes. Vertical integration, monopoly pricing and restriction on port competition resulting from the privatisation process all have the potential to reduce supply chain efficiency. The Report notes that:

> *"maximising asset sale prices through restricting competition or allowing unregulated monopoly pricing post sale amounts to an inefficient, long-term tax on infrastructure and consumers."* [1]

Recently the Port of Melbourne has proposed a 700%+ rental increase on one of its stevedores DP World. This clearly demonstrates that without appropriate regulation ports are free to charge monopoly prices. These monopoly prices will negatively impact the competitiveness of both Victoria and Australia.

Asciano strongly supports the Report's conclusions on port privatisations and believes that the Federal Government should ensure, as the ACCC has recommended, that appropriate competitive and regulatory arrangements are in place before asset recycling payments are made to the States.

[1] Report p. 196

1.2 Road Reform

Asciano strongly supports the Report's conclusion that road pricing reform should be a priority as it has the potential to deliver significant efficiency improvements. The Government should adopt the recommendation to introduce cost reflective road pricing with pricing subject to independent oversight. The Report's recommendation of the introduction of trials in the near term is a sensible approach to implementation. However, we believe that the implementation of road pricing reform should be limited to heavy vehicles and should not be constrained by requirements for revenue neutrality.

1.3 Single Rail Economic Regulator

The Report correctly concludes that:

> *"policy makers should look to reduce the number of access regimes and regulators in the rail sector as far as possible as excessive complexity imposes costs on users"* [2]

However, Asciano is disappointed that this conclusion did not make it into a specific recommendation. The key benefits of a single economic rail regulator would be:

- reduced duplication of effort;
- economies of scale allowing rail specialisation for regulators;
- reduced likelihood of regulatory capture (for example state based regulators will not be regulating state government owned assets);
- improved regulatory certainty as there would be only one decision maker not six; and
- coordination benefits, for example one approach to technical documents such as network rules right across the country.

We believe the Government should accept the Report's conclusion and move forwards with creating a single national rail economic regulator. The Report's recommended creation of the national Access and Pricing Regulator (APR) provides a great opportunity to create a single national economic rail regulator.

[2] Report p. 212

1.4 Employment Reform

Asciano is supportive of the broad thrust of the changes recommended in the Report on employment matters, in particular:

- Maintaining prohibition on secondary boycotts and recommending a more robust enforcement regime by the ACCC; and
- Removing the limitations on sections 45E and 45EA allowing them to apply to industrial agreements. These provisions prevent agreements with employees from placing restrictions on who the employer can supply or acquire goods from.

The Report's relevance to employment reform is limited and Asciano is actively engaging in the Productivity Commission's Review of the workplace relations framework where we are advocating for reform to improve the efficiency of the bargaining framework set up by the Fair Work Act.

2 PRODUCTIVITY AND IMPROVED REGULATION

Australia has been enjoying one of the highest living standards in the world, but this has been matched by a relatively high cost of living.

The high cost of living has been sustainable while our national income was being supported by strong commodity prices and volumes, but economic conditions are now changing. The prices which Australia receives for our resources have been falling, meaning our national income can no longer support our high cost of labour. Australia risks becoming uncompetitive in a very competitive world.

Often the debate around productivity has been too narrowly focussed on reducing wages. However, if Australia can produce more for the same level of wages and other costs, then our productivity, our competitiveness and our relative standard of living will all rise.

There are a number of elements which will contribute to Australia being able to be able to achieve greater production at the same level of wages. These elements include:

- more flexible working arrangements;
- lower and less distortionary taxation;

- more efficient infrastructure; and
- improved regulation.

Successful efforts to address each of these factors will enable Australia to increase its productivity.

Previous reforms to regulation and competition arising from the 1993 Hilmer Report were an important driver of Australian productivity growth in the 1990s and early 2000s. We see the Harper Review as having the potential to similarly contribute to Australian productivity growth by improving regulation and increased efficiency in investment and operation of infrastructure.

.

3 PORT PRIVATISATIONS

The Report expresses clear concern with the current port privatisation processes. It notes:

> *"The issue of how to privatise effectively is demonstrated by port infrastructure, where it is important to ensure that the regulatory regime can sufficiently influence port authority activities to constrain monopoly power. While some ports, particularly bulk ports, may have only a few large customers that can exert countervailing power, others may have significant market power in the absence of effective regulation."*[3]

> *"Where monopoly infrastructure is contracted out or privatised, it should be done in a way that promotes competition and cost-reflective pricing. Maximising asset sale prices through restricting competition or allowing unregulated monopoly pricing post sale amounts to an inefficient, long-term tax on infrastructure and consumers."*[4]

There have been a number of capital city container port privatisations in the recent past where it has seemed that maximisation of the asset sale price has been prioritised over long term competitive effects and efficient market outcomes.

[3] Report p.193

[4] Report p.196

There are two key issues arising from the creation of these private port operator monopolies namely, vertical integration and monopoly pricing. These issues in some circumstances could be partially mitigated if there was competition between ports. However, in recent sales there have been restrictions placed on competition between ports.

The first key issue is vertical integration. Any degree of vertical integration will provide the privatised monopolist port operator with the ability to leverage its power in the markets in which it has a monopoly (port access and port services) into vertically related competitive markets such as stevedoring, terminal operation, rail operations and rail haulage.[5] Whether the port owner has the incentive to leverage this power will depend on the degree of integration and relevant competitive dynamics in the market. A port operator with no downstream stevedore operations would have no commercial incentive to engage in non-price discriminatory practices.

There has been regulatory focus, including from the ACCC, at the time of the port privatisations in an attempt to address vertical integration issues. This interest has often been piqued by comments and interventions from interested parties. With the exception of Flinders Ports which commenced stevedoring post-privatisation, there are currently no capital city container terminal operators who are vertically integrated. However, the concerns regarding vertical integration do not end at privatisation.

Issues can occur post privatisation through the port operator subsequently:

- acquiring an established stevedoring or downstream business;
- entering into a joint venture with an existing stevedore business or other downstream business; or
- commencing its own stevedoring or downstream operation.

Although these subsequent actions may give the ACCC an opportunity to review transactions (e.g. the acquisition of an established stevedoring business) this is not true of them all. In particular, the organic expansion into stevedoring would not be subject to ACCC scrutiny. For example, the decision by Flinders Ports to commence stevedoring noted above would not be subject to ACCC scrutiny.

[5] We will use stevedoring as the most relevant port user service to Asciano. The arguments we make are equally valid for other port uses which are delivered competitively.

The likelihood of a port owner organically growing into stevedoring operations is increased when the owner already operates stevedoring operations elsewhere.

The second key issue is monopoly pricing. Given the monopoly position which the port operator enjoys, Asciano anticipates that the port operator will seek both to increase rentals and to introduce additional charges on port users such as Asciano. A monopoly provider of port services has an incentive to charge monopoly prices for its services, and this incentive is strengthened with a privatised leaseholder seeking to maximise its profits for shareholders.

Rental charges have been significantly increased in the years prior to privatisation, thus maximising the sale price. For example in the three years prior to privatisation rents increased at the Brisbane Container terminal by 128%. Further increases in charges post port privatisation have also occurred. The most recent example is the 700%+ increase in rent proposed by the Port of Melbourne for one of its stevedores, DP World.

It is clear that there is both the ability and an incentive for the privatised capital city container port operator to engage in monopoly pricing as the lessee of an essential facility, in the event that sufficient pricing controls are not imposed on the port operator. Thus a regulatory solution is required to limit this monopoly power.

Asciano welcome the comments in the Report which recognised the issues surrounding port privatisations and highlights the issues of pricing and extraction of monopoly rents. In particular we strongly agree with the Report recommending that a regulatory regime that can sufficiently influence port authority activities to constrain monopoly power should be in place.

We agree with the ACCC who recommended in their submission to a senate enquiry that:

> *"the Commonwealth require the states and territories to demonstrate that the appropriate market structure and/or pricing and access arrangements have been put in place as part of the privatisation process. For example, if the states and territories were required to outline the proposed arrangements up front then the Commonwealth*

could take these factors into consideration when reviewing proposals under the Asset Recycling Initiative. Further, the Commonwealth could hold the states and territories accountable for implementing the accepted arrangements at each of the key payment milestones" [6]

The Federal Government can ensure an appropriate regulatory outcome in state based asset sales through the asset recycling payments.

The proposed ARTC privatization raises similar concerns to those raised by the port privatisations discussed above. These concerns are that ARTC, as a private monopolist, will monopoly price and potentially vertically integrate which will lead to supply chain inefficiencies. Thus prior to privatisation ARTC needs to be subject to a strong regulatory regime that will prevent monopoly pricing and vertical integration. Without this regime, the Harper Committee's concerns will be realized namely that the privatisation process creates unregulated monopoly pricing post sale which amounts to an inefficient, long-term tax on infrastructure and consumers.

4 ROAD REFORM

The Report recognises that road is the least reformed of all infrastructure sectors.[7] As a result Recommendation 3 of the Report states:

"Governments should introduce cost-reflective road pricing with the aid of new technologies, with pricing subject to independent oversight and revenues used for road construction, maintenance and safety.

To avoid imposing higher overall charges on road users, governments should take a cross-jurisdictional approach to road pricing. Indirect charges and taxes on road users should be reduced as direct pricing is introduced. Revenue implications for different levels of government should be managed by adjusting Australian Government grants to the States and Territories.""[8]

[6] ACCC, 29/1/15 "Privatisation of state and territory assets and new infrastructure. Submission to the Senate Economics References Committee"p6

[7] Report p38.

[8] Report p38

Asciano strongly support the intent and direction of Recommendation 3 and the logic behind its implementation, namely that in the absence of reform will result in:

> *"inefficient road investment and distorts choices between transport modes, particularly between road and rail freight"*[9]

However, we believe that the implementation proposed by the Report could be improved in two areas which would ensure that the efficiency benefits sought from the reform are delivered.

Firstly, we believe the priority should be to focus on introducing reforms to road pricing for heavy vehicles, and on road infrastructure where significant volumes of freight are carried by heavy vehicles and there is competition with rail freight. Such an approach aligns with the Report's position that differences in road freight infrastructure pricing and rail freight infrastructure pricing is distorting choices between transport modes and thus impacting on efficiency.[10] Detailed policy and technical work has already been undertaken on the development of potential direct user charging and investment reforms that would apply to heavy vehicles.

Therefore, we believe that the implementation of Recommendation 3 should be specifically focussed on heavy vehicle road pricing reform, linked to the reform of road infrastructure investment.

Secondly, we believe it would be inappropriate to apply a principle of revenue neutrality to the introduction of pricing reforms for heavy vehicles. Reform of heavy vehicle pricing should be based on economic principles of cost reflective pricing. Revenue neutrality would impede the objective of introducing price signals that reflect the full cost of use of road infrastructure attributable to heavy vehicles, and which would provide necessary incentives to drive productivity and efficiency improvements.

Imposing revenue neutrality would also constrain the ability of road agencies to invest in infrastructure that would deliver productivity benefits to heavy vehicle operators but would require increased revenue to fund the infrastructure.

[9] Report p 38

[10] Report p213

We support the specific proposal in the Report[11] that the Australian Government and state and territory governments develop pilots and trials of the proposed reforms. As discussed above the trials should only involve heavy vehicles. The development and commencement of trials or demonstration projects, which demonstrate how, under the proposed new pricing model, heavy vehicle access prices would be calculated and charged, should be a high priority for governments over the next six to twelve months. Ideally such trials should result in a consistent approach to road pricing reform being adopted across all states.

In developing the detail around implementation of Recommendation 3 we would recommend that road transport reforms should be focussed on maximising the efficiency of Australia's major freight routes by ensuring competitively neutral price regulation of land freight infrastructure; i.e., competitive neutrality between road and rail. In order to achieve these policy objectives the reforms should:

- Be restricted to areas that directly compete with rail freight transport or are otherwise major arterial roads which primarily serve heavy vehicles i.e., national highways and state arterial roads, and roads into Australia's major ports; and
- Only apply to heavy vehicles that weigh 4.5 tonnes or more.

Overall, Asciano strongly supports the intent and direction of Recommendation 3 of the Report, but believe that the implementation of road pricing reform should be limited to heavy vehicles and should not be constrained by requirements for revenue neutrality.[12]

[11] Report p216

[12] Asciano is party to a joint industry submission on Road reform with the ARTC and Aurzion which provides more detail on our views on road reform.

5 SINGLE ECONOMIC RAIL REGULATOR

The Report correctly concludes that:

> *"policy makers should look to reduce the number of access regimes and regulators in the rail sector as far as possible as excessive complexity imposes costs on users"* [13]

Asciano along with other industry participants sees rail as an industry which could significantly benefit from national access regulation. Many rail freight activities involve interstate haulage, but much of the rail infrastructure continues to be regulated by state regulators.

For example, Asciano operates its above rail operations under six different access regimes with multiple access providers and multiple access regulators. This multiplicity of regimes adds costs and complexity to rail access for no benefit, particularly as many of the access regulation functions are duplicated across states. Given this Asciano strongly supports a national rail access regulator.

Asciano does not advocate a one size fits all approach to rail regulation. For example, you would not expect that the appropriate access regime in a government owned and operated regional grain network would be the same regime required to regulate a vertically integrated monopolist track provider such as Aurizon in Queensland. However, having a single national regulator would have a number of advantages:

- *Reduced duplication of effort* – even with a number of tailored regimes (for example a regional network regime plus an interstate network regime) the number of regimes in operation would be significantly less than the current situation. In addition with one regulator making decisions some key features of the regime would be common across networks. For example, the approach to calculating the cost of capital or the approach to liabilities and indemnities which can currently vary significantly via jurisdiction, would be common. Having a single regulator would significantly reduce the regulatory resources required, saving both industry and Government significant

[13] Report p212

resources. This proposal is consistent with the current Government's priority to reduce unnecessary red tape and cost.

- *Increased specialisation* – some regulators only deal with rail access issues intermittently, usually at the time an access undertaking comes up for renewal. Access undertakings are typically reviewed on a 5 or 10 year cycle. Thus it is difficult for these regulators to retain in house knowledge on rail issues. A national regulator with dedicated specialised rail staff would be more likely to have the appropriate expertise and as such be more likely to come to efficient decisions.
- *Regulatory capture and independence* – the potential for regulatory capture will be reduced with a national regulator. Where a state based regulator, part of the state government bureaucracy, regulates a private company which is a significant contributor to state finances or even a state government owned entity, the commitment to independence and efficient regulatory decision making may be tested. These close relationships would be more arms length with a national regulator.
- *Improved regulatory certainty* – having a single regulator which as noted above would allow specialisation and also would implement decision consistently across networks would increase regulatory certainty compared with the status quo of multiple regulators and multiple access undertaking. The increase in regulatory certainly would reduce investment risk and all other things being equal expect to encourage more efficient investment decisions.
- *Co-ordination benefits* – having a single regulator approve technical rail documents such as network rules will increase consistently between network owners thereby reducing operators' costs. For example, rules regarding rolling stock approval or track possession planning (i.e. maintenance planning) would likely become more consistent thereby reducing co-ordination and regulatory compliance costs of dealing with multiple regimes.

We believe the Government should accept the Report's conclusion and move forwards with creating a single national rail economic regulator. The recommended creation of the national Access and Pricing Regulator (APR) provides a great opportunity to create a single national economic rail regulator.

6 EMPLOYMENT RELATED MATTERS

6.1 Secondary Boycotts

In Recommendation 36 the Report concludes that:[14]

- prohibitions on secondary boycotts should be maintained
- the ACCC should pursue secondary boycott cases with increased vigour
- the ACCC should publish details on secondary complaints;
- secondary boycott fines should be in line with other fines for breaching competition law.

Asciano strongly agrees with recommendation 36 as secondary boycotts are harmful to trading freedom, and the secondary boycott provisions in the CCA have played an important role in deterring behaviour that has the potential to inflict significant harm on Australian business.

A particularly important part of the recommendation is that that the ACCC must play a stronger role in education and investigation, as a means of ensuring that these provisions continue to have efficacy as a deterrent to secondary boycotts.

Asciano welcomes the requirement on the ACCC to disclose more information on complaints and investigations. However, in addition to publishing the number of matters investigated and resolved each year, the ACCC should release further information (presented in such a way as to retain confidentiality). The method adopted by the Australian Human Rights Commission reporting on conciliated matters could be considered as a model. This would provide an important educative function in respect of the operation and effect of these important legislative provisions.

6.2 Trading Restrictions in Industrial Agreements

Recommendation 37 states that 45E and 45EA of the CCA should be amended so they apply to awards and industrial agreements and that the restrictions around being “accustomed” are removed. These are very positive changes and Asciano fully supports them. Asciano also support the penalties for breach of 45E and 45EA being brought into line with penalties for breaches of other provisions of the CCA.

[14] Report p 392

The Reports notes that there is a conflict between the legislative purpose of the CCA and the Fair Work Act. Recommendation 37 also includes a procedural right for the ACCC to be notified and intervene in Fair Work Commission proceedings of Enterprise Agreements which contain potential restrictions of the kind referred to in sections 45E and 45EA. This would serve a valuable purpose in highlighting and gaining a better understanding of the extent of the apparent conflict between the purposes of the CCA and the operation of the FWA. However, Asciano is concerned that, without legislative change, this requirement would not in fact address or resolve the conflict. Further, Asciano would also be concerned if such a process caused delay to the approval process undertaken by the Fair Work Commission of Enterprise Agreements due to the additional administration and procedural steps involved.

7 CONCLUSION

The Competition Policy Review Final Report is a detailed and thoughtful piece of work and a positive response by the Government to the recommendations has the potential to boost Australian productivity growth.

Asciano strongly supports the Report's conclusions on port privatisations and believes that the Federal Government should ensure, as the ACCC has recommended, that appropriate competitive and regulatory arrangements are in place before asset recycling payments are made to the States.

Asciano supports the Report's conclusion that road pricing reform should be a priority as it has the potential to deliver significant efficiency improvements. The Government should adopt the recommendation to introduce cost reflective road pricing with pricing subject to independent oversight.

We believe the Government should accept the Report's conclusion on moving towards a single national rail economic regulator. The Report's recommended creation of the national Access and Pricing Regulator (APR) provides a great opportunity to create a single national economic rail regulator.

Asciano is supportive of the broad thrust of the changes recommended in the Report on employment matters, in particular maintaining prohibition on secondary boycotts and removing the limitations on sections 45E and 45EA.