Economuse, 19 January 2007

TPA Part IIIA – What price access?

The access arrangements under Part IIIA of the Trade Practices Act are causing the same angst among minerals and energy companies as Telstra faces. Pricing can resolve the current issues for all concerned.

The Minerals Council of Australia is seeking "reforms to competition laws governing access regimes to export corridors (rail and port infrastructure) to complement significant increased industry investment". This follows Fortescue Metals' win against BHP Billiton in the Federal Court on 18 December where the court ruled that BHP's railways in the Pilbara could be subject to declaration[1]. The decision has major implications for other network industries including electricity and gas transmission lines.

Oops – carved up not carved out

The Hilmer Report[2] that led to the Part IIIA access regime expresses the intention that "products, production processes or most other commercial facilities" (page 251) should fall outside the access regime. This is reflected in Part IIIA of the Trade Practices Act (TPA) introduced by the Competition Policy Reform Act 1995.

Private infrastructure owners have relied on their infrastructure being considered an integral part of the production or transformation process and hence carved-out of Part IIIA. The Federal Court found that BHP's rail network "represents the provision of a transport service, just as the use of a gas pipeline is a conveyance or transport service used to move gas from one place to another, or an airport runway is a landing strip used to ensure airplanes can take-off or touch down. In none of these cases does the infrastructure facility itself involve a process of transformation"[3].

Pricing is the real issue

The desperate attempts to avoid declaration reflect the state of the access pricing principles which permit the access price to be based only the direct costs of providing access.

The Hilmer report flagged concerns about the impact of access pricing on investment incentives and innovation. We are now seeing those concerns come home to roost (eg with Telstra's capital strikes over the FTTN network). The Federal Court's decision on the Pilbara railway, and access pricing hang over the $300 billion of infrastructure projects expected over the next decade.

We need fair and reasonable access prices that do not chill investment and innovation. Direct costs do not cut it. The proper benchmark is the pricing that would apply in a competitive market or, in the more general and practical case, a contestable market. The pricing principles for this have already been developed: "In competitive markets no firm will offer to supply any of its products on a continuing basis at any price that does not

fully cover the incremental cost entailed in the supply process, and that incremental floor price must include all the incremental opportunity costs that the supply process generates. I know no economist who disputes this conclusion that follows so clearly from the logic of economic decisions." [4]

Ironically, an early example of this approach is for railways. Let's say BHP has two sections of track A to B then C and the marginal cost of carrying ore over each section is $3/tonne and the price at the terminal is $10/tonne with a margin of $4/tonne for other costs and profit. What is the fair and efficient price it should charge Fortescue for running its own trains over the section B to C? Assuming that every tonne of Fortescue's product displaces a tonne of BHP's at the terminal, the correct access price is $7 ($4 plus $3). Of course, if it was not Fortescue but a tourist train operation, the opportunity cost is zero and the access price $3.

Opportunity cost is a real marginal cost that applies in competitive markets. But the inclusion of opportunity cost is explicitly ruled-out by the Explanatory Memorandum to the TPA. This is economically illiterate and inimical to investment. Rather than seeking "an efficiency over-ride" from the Treasurer to exempt key transport infrastructure owned by private sector exporters (AFR, 3 January 2007), the Minerals Council should seek to make the TPA less prescriptive about the pricing principles that should apply.

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[1] Fortescue applied in June 2004 to the National Competition Council which recommended declaration to the Treasurer in March 2006. During that process, both BHP and Fortescue applied to the Federal Court to decide whether or not the private rail tracks could be subject to declaration.
[2] See chapter 11 of the 'National Competition Policy Report by the Independent Committee of Inquiry, August 1993' by F Hilmer, M Rayner & G Taperell.
[3] Judge Middleton quoted in the AFR, 19 December 2006 with judgement at http://www.austlii.edu.au/au/cases/cth/federal_ct/2006/1764.html
[4] Professors Baumol and Willig's joint evidence in Clear Communications vs. Telecom NZ Case, 1991.