



Australian
Competition &
Consumer
Commission

Draft Determination

Applications for authorisation

lodged by

Anglo Coal Australia Pty Ltd and others

in respect of

an extension to a queue management system designed to address the imbalance between the demand for coal loading services at the Dalrymple Bay Coal Terminal and the capacity of the Goonyella coal chain

Date: 23 February 2009

Authorisation no.: A91107 -
A91109

Public Register no.: C2008/1863

Commissioners: Samuel
Kell
Schaper
Dimasi
Martin
Willett

Summary

The ACCC proposes to **deny** authorisation to the proposed extension of the queue management at the Dalrymple Bay Coal Terminal.

The ACCC is concerned that the ongoing operation of the QMS has reduced the incentive for a long term solution to be developed and implemented, which has resulted in potentially significant foregone coal export opportunities. As such, it is difficult to see that any extension of the current or a similar QMS, even if world demand were to pick up again, would be in the public interest.

In these circumstances, the ACCC encourages all relevant parties to continue to work together to finalise and implement a long term solution so that future potential queuing issues can be avoided.

The authorisation process

The Australian Competition and Consumer Commission (ACCC) can grant immunity from the application of the competition provisions of the *Trade Practices Act 1974* (the Act) if it is satisfied that the benefit to the public from the conduct outweighs any public detriment. The ACCC conducts a public consultation process to assist it to determine whether a proposed arrangement results in a net public benefit.

The applications for authorisation

The applicants applied for authorisation for the continuation of the Queue Management System (QMS) currently designed to address the imbalance between demand for coal loading services at the Dalrymple Bay Coal Terminal (DBCT) and the capacity of the Goonyella coal chain.

The applicants seek a short-term extension of the QMS for a maximum of 6 months, until 30 June 2009. The applicants propose authorisation being conditional upon them submitting an implementation plan for a long term solution by 31 March 2009.

Background

The ACCC has granted authorisation to the QMS on two previous occasions. These were applications for authorisation:

- A30239 - A30241, which were granted on 15 December 2005.
- A91060 - A91062, which were granted on 29 February 2008.

Public benefit

Due to the global financial crisis and reduced demand, there is currently no queue at DBCT. The applicants have advised the ACCC that as a result of current market conditions it is unlikely that excessive queues will develop within the first half of 2009, the term for which authorisation is sought.

Therefore, the ACCC does not consider that the public benefits claimed by the applicants will be realised during the term for which authorisation is sought. The ACCC does not accept that an extension of the QMS would result in a public benefit in the short term.

Public detriment

The ACCC considers that the continued operation of the QMS has the potential to result in the following detriments:

- reduced incentives for efficient investment in the Goonyella coal chain
- reduced incentive to develop a long-term solution and
- reduced likelihood of competitive entry in above rail haulage services.

Balance of public benefit and detriment

The ACCC considers that in all the circumstances, the proposal is unlikely to generate public benefit. To the extent that any public benefit may result from the arrangements (for example, if a queue were to form during the period for which authorisation has been sought so that the benefits claimed by the applicants, such as demurrage savings, are more likely to occur), the ACCC considers that these benefits will not outweigh the likely public detriments identified by the ACCC.

The next steps

The ACCC will now seek further submissions from the applicants and interested parties in relation to this draft determination prior to making a final decision. The applicants and interested parties may also request that a conference be held to make oral submissions on the draft determination.

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List of abbreviations

ACCC	Australian Competition and Consumer Commission
Babcock and Brown	Babcock and Brown Infrastructure Group
Central Coordinator	Central Coordinator of the Dalrymple Bay Coal Chain
DBCC	Dalrymple Bay Coal Chain
DBCC Leadership Team	Dalrymple Bay Coal Chain Leadership Team
DBCT	Dalrymple Bay Coal Terminal (the terminal)
DBCTPL	Dalrymple Bay Coal Terminal Pty Ltd (operator)
Entitlement	capacity entitlements
Mtpa	Million tonnes per annum
QMS	Queue Management System
QRNational	QRNational Coal
Rio Tinto	Rio Tinto Coal Australia Pty Ltd
System Capacity	Capacity of the Goonyella coal chain, including track, rail and terminal
Supply Chain	Goonyella supply chain, comprising the mines that ship coal through DBCT, the Goonyella rail infrastructure, the rollingstock and DBCT.
TAM	Transitional Allocation Mechanism
the Act	<i>Trade Practices Act 1974 (Cth)</i>
Users / Applicants	Coal mine operators
Working queue	A working queue is a ship queue of sufficient length to enable throughput to be maximised.
Xstrata	Xstrata Coal Queensland Pty Ltd

1. Introduction

Authorisation

- 1.1 The Australian Competition and Consumer Commission (the ACCC) is the independent Australian Government agency responsible for administering the *Trade Practices Act 1974* (the Act). A key objective of the Act is to prevent anti-competitive conduct, thereby encouraging competition and efficiency in business, resulting in a greater choice for consumers in price, quality and service.
- 1.2 The Act, however, allows the ACCC to grant immunity from legal action in certain circumstances for conduct that might otherwise raise concerns under the competition provisions of the Act. One way in which parties may obtain immunity is to apply to the ACCC for what is known as an 'authorisation'.
- 1.3 The ACCC may 'authorise' businesses to engage in anti-competitive conduct where it is satisfied that the public benefit from the conduct outweighs any public detriment.
- 1.4 The ACCC conducts a public consultation process when it receives an application for authorisation. The ACCC invites interested parties to lodge submissions outlining whether they support the application or not, and their reasons for this.
- 1.5 After considering submissions, the ACCC issues a draft determination proposing to either grant the application or deny the application.
- 1.6 Once a draft determination is released, the applicant or any interested party may request that the ACCC hold a conference. A conference provides all parties with the opportunity to put oral submissions to the ACCC in response to the draft determination. The ACCC will also invite the applicant and interested parties to lodge written submissions commenting on the draft.
- 1.7 The ACCC then reconsiders the application taking into account the comments made at the conference (if one is requested) and any further submissions received and issues a final determination. Should the public benefit outweigh the public detriment, the ACCC may grant authorisation. If not, authorisation may be denied. However, in some cases it may still be possible to grant authorisation where conditions can be imposed which sufficiently increase the benefit to the public or reduce the public detriment.

The application for authorisation

- 1.8 On 14 November 2008, eight users of the Dalrymple Bay Coal Terminal (the applicants) lodged applications for authorisation A91107 – A91109 with the ACCC. The users making the applications are:
 - Anglo Coal Australia Pty Ltd

- BHP Billiton Mitsubishi Alliance
 - Isaac Plains Coal Management Pty Ltd
 - Macarthur Coal (C & M Management) Pty Ltd
 - Peabody Pacific Pty Ltd
 - Rio Tinto Coal Australia Pty Ltd
 - Vale Australia Pty Ltd
 - Xstrata Coal Queensland Pty Ltd
- 1.9 The applicants applied for authorisation for the continuation of the Queue Management System (QMS) currently designed to address the imbalance between demand for coal loading services at the Dalrymple Bay Coal Terminal (DBCT) and the capacity of the Goonyella coal chain.
- 1.10 The applicants seek a short-term extension of the QMS for a maximum of 6 months, until 30 June 2009.
- 1.11 The applicants propose authorisation being conditional upon them submitting an implementation plan for a long term solution by 31 March 2009. It is envisaged by the applicants that this long term solution will involve a transition phase.

Interim authorisation

- 1.12 The applicants also requested urgent interim authorisation of the proposed arrangements due to the pending expiration of the current QMS.
- 1.13 On 10 December 2008, the ACCC decided not to grant interim authorisation. The ACCC considered that in the absence of a long term solution having been developed, interim authorisation would not be in the public interest.
- 1.14 In deciding not to grant interim authorisation, the ACCC considered that:
- urgency alone is not a sufficient reason for the granting of interim authorisation, given that the applicants have known of the expiry of the authorisation and the ACCC's views regarding the long term operation of the QMS since at least February 2008.
 - the continued operation of the QMS has the potential to reduce the incentive to develop a long term solution to address the capacity constraints in the coal chain. This has significant flow on effects in terms of lost export revenue. Given the period of sustained high demand, it is likely that had the underlying issues been resolved, the capacity of the Goonyella Coal Chain would be significantly higher than it currently is.

- given recent falls in vessel hire rates and a significant drop in demand for coal, the ACCC considers vessel queues and associated demurrage savings are likely to be lower than at previous times it has considered the QMS. The ACCC acknowledges that if an extensive vessel queue were to form in the first six months of next year, the QMS would lead to a reduction in demurrage costs for the industry, particularly as falls in spot rates for demurrage may not have an immediate impact due to fixed contracted rates. However, the evidence of a drop in demand for coal makes it less certain that an excessive queue will arise in the absence of a QMS.
- the ACCC acknowledges that the QMS could act to reduce the environmental impact of a long vessel queue in the short term and lead to increased short term efficiency and throughput at DBCT.

Chronology

1.15 Table 1.1 provides a chronology of significant dates in the consideration of this application.

Table 1.1: Chronology of application for authorisations A91107-A91109

DATE	ACTION
14 November 2008	Applications for authorisation lodged with the ACCC, including an application for interim authorisation.
28 November 2008	Closing date for submissions from interested parties in relation to the request for interim authorisation.
4 December 2008	Submission received from the applicants in response to interested party submissions on interim authorisation.
10 December 2008	The applicants provides further information regarding the applications for authorisation.
10 December 2008	The ACCC denied the request for interim authorisation.
12 December 2008	Closing date for submissions from interested parties in relation to the substantive application for authorisation.
23 February 2009	Draft determination issued.

2. Background to the application

The applicant

2.1 This chapter focuses on:

- an overview of the Goonyella coal supply chain
- the ACCC's evaluation of the past authorisations
 - A30239 - A30241 (2005)
 - A91060 - A91062 (2008)
- current issues with the Goonyella coal supply chain

2.2 Further background information on the industry participants and the operation of the Goonyella coal chain is provided in Chapter 2 of the ACCC's determination of 15 December 2005 in relation to authorisations A30239 - A30241.

Goonyella Coal Supply Chain

2.3 The Goonyella coal supply chain rails metallurgical and thermal coal from mines in the central Bowen Basin to two export terminals at the Port of Hay Point, one of which is Dalrymple Bay Coal Terminal (DBCT). Major participants of the Goonyella supply chain include:

- coal mine operators (Users)
- one below-rail track provider in QR Network
- two above-rail haulage operators in QRNational Coal (QRNational) and Pacific National
- two export terminals and two respective port terminal operators
- one port authority in Ports Corporation Queensland
- pilotage provided by Maritime Services Queensland

2.4 In terms of governance frameworks, the Goonyella supply chain is predominantly disaggregated, with contractual arrangements the most important determinant of supply chain performance given there has been no coordination of the whole supply chain up to this point in time.¹

2.5 Recognition of the need for coordination of the whole supply chain has been a relatively new development, stemming from the recent high profile rail and

¹ Supporting Submission to applications for authorisation A91107 - A91109, 14 November 2008, p71

port infrastructure bottlenecks in the Supply Chain, reflected in significant ship queues.²

- 2.6 The capacity of the Goonyella coal chain (System Capacity) is determined by the following components:
- collective capacity of mine load points
 - below rail capacity
 - above rail rolling stock and train scheduling and
 - terminal infrastructure capacity (including inloading and outloading functions).
- 2.7 As submitted by the applicants, the interaction of different elements of the coal supply chain results in capacity losses if the capacity of the system as a whole is not accounted for in both the design of infrastructure and the way in which capacity is sold to coal exporters.³ In other words, the throughput of the Goonyella coal chain, or System Capacity, is likely to be **lower** than:
- the capacity at DBCT
 - the capacity of the rail system or
 - the collective capacity of mine load points.
- 2.8 Until each of the elements of the Supply Chain adopts a common definition of all of the assumptions that are considered when calculating the capacity of the system as a whole, there will continue to be a mismatch between the total capacity that is contracted to the Users, and the capacity of the coal chain as a system to deliver against those contracts.⁴
- 2.9 The System Capacity forecast for the 2008 calendar year was **54.5 million tonnes**.⁵

Dalrymple Bay Coal Terminal

- 2.10 DBCT is located in the Port of Hay Point, 38 kilometres south of Mackay in Queensland. It is a common user terminal leased from the Queensland Government by Babcock and Brown Infrastructure Group (Babcock and Brown)⁶. Dalrymple Bay Coal Terminal Pty Ltd (DBCTPL) is responsible for

² Supporting Submission to applications for authorisation A91107 - A91109, 14 November 2008, p71

³ Supporting Submission to applications for authorisation A91107 - A91109, 14 November 2008, p27

⁴ Supporting Submission to applications for authorisation A91107 - A91109, 14 November 2008, p28

⁵ The Forecast System Capacity for the Goonyella Coal Chain – DBCT Component, Independent Expert – Bruce Martin, November 2007.

⁶ The lease has a 50 year term, with an option to extend this by an additional 49 years

the daily operation and management of the terminal under an operations and management contract with Babcock and Brown⁷.

- 2.11 The major functions performed by DBCTPL are:⁸
- coordinating the railing of coal from the mine sites to DBCT (in conjunction with QRNational)
 - managing and operating train unloading, stockpiling and shiploading activities within DBCT
 - maintenance and minor engineering functions.
- 2.12 DBCT processes three commercial coal types, namely, coking coal (70 per cent), PCI coal and thermal coal, which can be blended into a possible 58 products. Coal processed through the terminal is defined as a homogenous product attracting a single terminal infrastructure charge.
- 2.13 Under their User Agreements, coal producers have agreed annual contract tonnages with Babcock and Brown for a varying number of financial years. Coal producers are required to provide Babcock and Brown with quarterly demand forecasts for terminal coal loading services.

ACCC's evaluation of past authorisations

Authorisations A30239 - A30241

- 2.14 On 15 December 2005, the ACCC granted authorisation to DBCTPL of the QMS until the earlier of:
- 31 December 2008;
 - completion of Phase 1 expansion of DBCT; or
 - when system capacity reaches or exceeds the monthly tonnage of coal that Users wish to ship.
- 2.15 At the time the QMS was expressed to terminate upon completion of Phase One expansion. The ACCC granted authorisation on an understanding that the Phase One expansion would be completed in early 2008.
- 2.16 At the time of granting authorisation, the ACCC stated that it was satisfied that the QMS was likely to result in significant public benefit, particularly by reducing demurrage costs for industry and hence improving economic efficiency relative to a situation where a queue persisted. The ACCC recognised there was no way of accurately predicting the level of the queue going forward if the QMS were not in place. However, the ACCC considered

⁷ The operations and maintenance contract is effective until March 2009, with the capacity for a further extension until 2014. DBCTPL supporting submission, 26 September 2007, p17

⁸ DBCTPL supporting submission to applications A30239-A30241, 5 April 2005, p17

DBCTPL's estimate of \$350 million in demurrage savings for 2005 was not unreasonable.

- 2.17 The ACCC considered that the QMS was a transitional measure which aimed to limit the demurrage costs associated with excessive vessel queues until capacity expansion projects were operational.

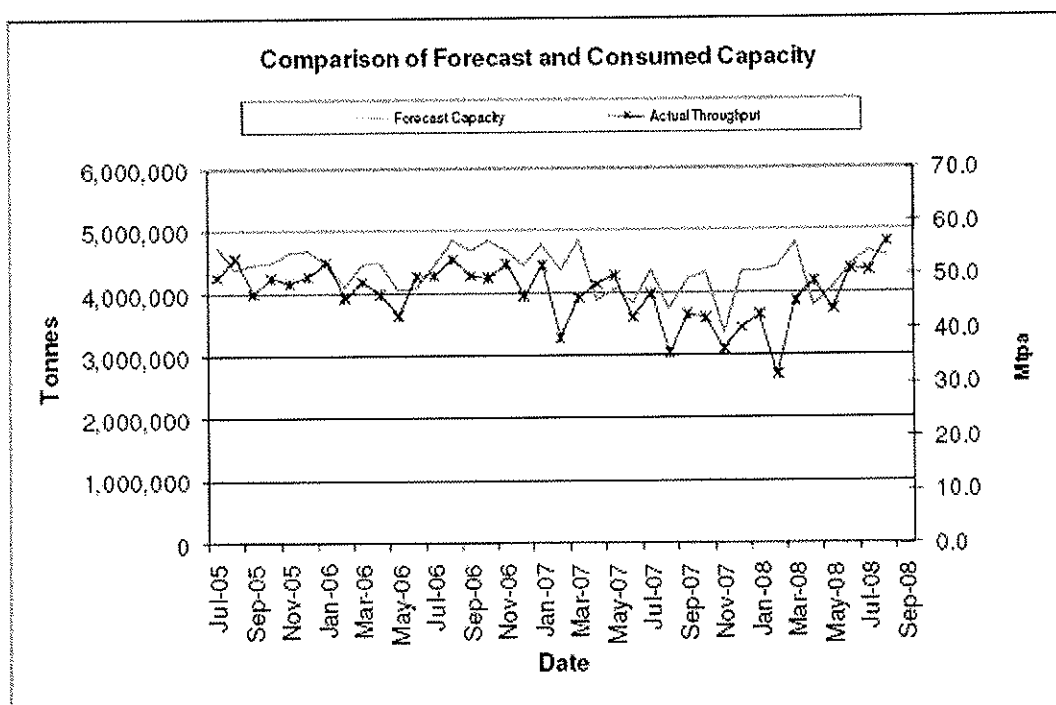
Authorisations A91060 - A91062

- 2.18 On 26 September 2007, DBCTPL sought authorisation to extend the term of their QMS until December 2010 in order to address the imbalance between demand for coal loading services at DBCT and the capacity of the Goonyella coal chain. The ACCC had previously granted authorisation to the QMS until 31 December 2008, however DBCTPL sought an extension due to the fact that its *Dalrymple Bay Coal Terminal Queue Management System Amendments to Terminal Regulations* (Terminal Regulations) were due to expire upon the completion of the phase one expansion in early 2008.
- 2.19 On 29 February 2008 the ACCC decided to grant authorisation to a QMS at DBCT only until 31 December 2008. In granting authorisation, the ACCC noted that without evidence that a long-term solution is being developed, the continued operation of the QMS has the potential to result in significant public detriment in the form of insufficient investment and substantial losses in export revenues.
- 2.20 The ACCC considered that the continued operation of the QMS, in the long-term, has the potential to impact upon investment, delay competitive entry in above rail haulage services, and reduce incentives to develop a long-term solution to contracting and capacity issues in the Goonyella coal chain.
- 2.21 Authorisation was granted only until 31 December 2008 as a transition period to enable a long-term solution to excessive vessel queues to be developed and implemented.

Current issues with the Goonyella coal chain

- 2.22 Figure 2.1 below was submitted by the applicants and shows forecasted and actual throughput of the Goonyella supply chain for the period July 2005 – September 2008. The applicants submit that between March and April 2008 actual throughput has averaged 50.9 Mtpa, around 75 per cent of contracted tonnage.

Figure 2.1: Throughput DBCT, forecast and actual capacity⁹



Data source: 2319 Pty Ltd

- 2.23 The applicants note that the figure fails to identify that performance is still below that of capacity contracted across the system as a whole. They state existing contracts provide for 68 Mtpa capacity being delivered, but the system has been unable to demonstrate that it can deliver above levels of 61 Mtpa.¹⁰
- 2.24 As submitted by the applicants, this gap between contracted capacity and system-deliverable capacity is only set to widen unless alignment is sought.

Recent developments in demand

- 2.25 The ACCC understands that the global economic down turn had lead to less construction activity, causing the decline in demand for coking coal.
- 2.26 The applicants submitted to the ACCC on 28 January 2009 that they do not believe the Goonyella coal chain will be constrained in the next six months. It was specifically noted that demand for coal has fallen from a 56 Mtpa in October 2008 to 28 Mtpa in January 2009.
- 2.27 The applicants note that demand is not expected to start recovering until at least the second quarter of 2009, however is not expected to return to original peak levels for at the very least 12 months.
- 2.28 The ACCC understands that contract prices for both thermal and coking coal are expected to fall significantly when contracts are renegotiated come 1 April

⁹ Supporting Submission to applications for authorisation A91107 - A91109, 14 November 2008, p13

¹⁰ Supporting Submission to applications for authorisation A91107 - A91109, 14 November 2008, p13

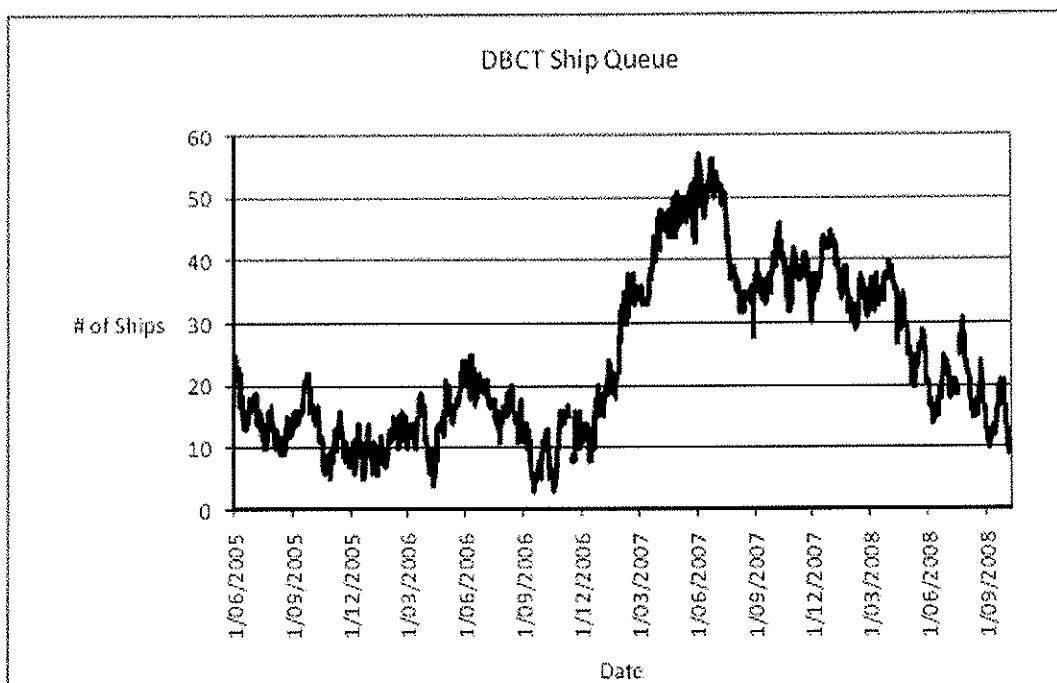
2009. For example a recent press article quotes estimates of a 60 per cent drop in the price of coking coal, from \$US303 to \$US120.¹¹

Ship Queue

2.29 Figure 2.2 below shows the number of ships in the queue from June 2005 to September 2008.

2.30 The applicants submit that the QMS has been successful in reducing the ship queue. The average ship queue during the period in which the QMS was operational was 18 ships.¹² A ship queue between 15 and 20 is considered optimal.¹³

2.31 **Figure 2.2: DBCT shipping queue, June 2005 – September 2008**¹⁴



Data source: DBCTPL

¹¹ 'Coal prices set for massive plunge', Ayesha de Kretser, *Australian Financial Review*, 28 January 2009, p.14

¹² Supporting Submission to applications for authorisation A91107 - A91109, 14 November 2008, p14

¹³ Supporting Submission to applications for authorisation A91107 - A91109, 14 November 2008, p14

¹⁴ Supporting Submission to applications for authorisation A91107 - A91109, 14 November 2008, p15

3. The application for authorisation

- 3.1 On 14 November 2008, eight users of the Dalrymple Bay Coal Terminal (the applicants) applied for authorisation for the continuation of the Queue Management System (QMS).
- 3.2 The QMS is designed to address the imbalance between the demand for coal loading services at DBCT and the capacity of the Goonyella coal chain. The key objectives of the QMS are to:
- maintain a Working Queue¹⁵, so as to minimise deadweight demurrage costs to all users
 - maximise utilisation of capacity and maximise exports from DBCT
 - preserve and enhance the reputation of the Supply Chain as being competitive and reliable and
 - ensure a fair, equitable and transparent system for allocating capacity from time to time between users.
- 3.3 Further information on the QMS can be found in the ACCC's determination dated 29 February 2008 in relation to authorisations A91060-A91062.
- 3.4 This chapter outlines the following:
- the current proposed arrangements and
 - progress towards a long term solution
- 3.5 The continued operation of the QMS potentially raises concerns under the anti-competitive conduct provisions of the Act. Consequently, the applicants have lodged the applications for authorisation with the ACCC.
- 3.6 Under section 88(6) of the Act, any authorisation granted by the ACCC is automatically extended to cover any person named in the authorisation as being a party or proposed party to the conduct. The ACCC notes that the applicants have requested that authorisation apply to all users of DBCT, DBCTPL's shareholders and Babcock and Brown Infrastructure (Babcock and Brown).

Current applications

- 3.7 In making the current applications for authorisation, the applicants note the ACCC's concerns and submit the current applications for authorisation takes into account these concerns, seeking only a limited extension of the QMS to facilitate the development of an agreed long term solution Phase 1.

¹⁵ A working queue is defined as a ship queue of sufficient length to enable throughput to be maximised.

- 3.8 The applicants seek a short-term extension of the QMS for a maximum period of 6 months, until 30 June 2009. The applicants submit that the extension is required to facilitate the time necessary for all users and service providers to reach agreement on the practical terms and mechanics of the long term solution, in particular the alignment of rail and port contracts in Phase 1 until capacity exceeds 85 Mtpa (expected to be 18-24 months).
- 3.9 The applicants propose authorisation be conditional upon them providing a detailed implementation plan to the ACCC by 31 March 2009 which will set out the mechanics and practical steps required in order to achieve the long term solution. The implementation plan will be accompanied by a further application for authorisation.

Progress towards a long-term solution

- 3.10 The applicants note that they are mindful of the concerns expressed by the ACCC in previous decisions in terms of developing a long term solution and submit there has been progress regarding investment in capacity, institutional reform and agreement on long term contractual reform¹⁶.

Recent developments

- 3.11 The applicants submit numerous improvements in the coordination of the Supply Chain have been developed since the previous authorisations and following the completion of the O'Donnell Review, including:
- in March 2008 an MOU was signed and executed establishing a Supply Chain Board comprised of all Goonyella producers and transport service producers. A Supply Chain Leadership Team was established under the MOU and a Central Coordinator was appointed to chair this forum. The Central Coordinator's role is to review coal chain performance and develop recommendations for coal chain improvements. The Central Coordinator reports to both the Dalrymple Bay Coal Chain Board and the Dalrymple Bay Coal Chain Leadership Team (DBCC Leadership Team)
 - the DBCC Leadership Team has agreed to a common demand forecasting process for the Supply Chain which is important for coordinating information for service providers. The Central Coordinator will use this information to establish monthly forecasts and stretch targets.
 - Planning developments to increase capacity including the preparation of a detailed submission for the establishment of a DBCC Management Centre. This proposal comprises various components including:
 - design and construction of a purpose built facility in the Mackay region to house all coal chain planning functions across all supply chain participants to be completed by the end of March 2010

¹⁶ Supporting Submission to applications for authorisation A91107 - A91109, 14 November 2008, pp. 7-8.

- centralisation of the planning functions that exist currently within the chain to one temporary location by 30 June 2009, until the purpose built facility can be commissioned and
- transition of Central Coordinator activities into the Management Centre including supply chain performance management and improvement initiatives.
- utilisation of a single asset maintenance plan agreed to by DBCTPL and QRNational to identify system capacity loss due to maintenance activities. An Independent Planner has been engaged to review system loss due to maintenance activities.
- daily operational coordination conferences have been initiated with service providers to establish productive operational dialogue across all service providers with high levels of participation and transparency of information.

3.12 The applicants also submit that there have been a number of contractual reforms including developments to the current access undertaking for DBCT (held by Babcock and Brown). The current access undertaking regulated by the QCA expires on 31 December 2009. In anticipation of this, users have been working with Babcock and Brown to develop a replacement undertaking. Some of the initiatives include:

- the concept of 'Terminal Capacity' to be replaced with 'System Capacity'. System Capacity would refer to the overall capacity of the DBCC and would be determined by reference to Coal Chain Operating Assumptions agreed between users and service providers (including Babcock and Brown, QRNetwork and above-rail operators) and calculated by an independent party.
- users and service providers agree to participate in a collaborative process to determine System Capacity and the underlying Coal Chain Operating Assumptions
- an agreement between all parties to not service any future port contracts (beyond the 85 Mtpa currently contracted from the completion of the Phase 2/3 expansion works) unless there is sufficient System Capacity
- investment at the port should have regard to a 'whole of coal chain' Master Plan – in which all parties within the chain would participate.

3.13 The applicants also submit that users and QRNetwork have been developing the next rail network undertaking to commence on 1 July 2009, containing the following elements:

- contracted rail does not exceed an appropriate measure of rail capacity, with the assessment of rail capacity taking into account all aspects of the Supply Chain

- complete alignment of Coal Chain Operating Assumptions across the coal chain when contracting for capacity
- continued development of a Rail Infrastructure Master Plan which accounts for the expansion of the rail network, within the context of the relevant supply chain. Such a Master Plan should have regard to any broader 'whole of coal chain' Master Plan and
- establishment of an alternate access agreement which would facilitate a more integrated and aligned contracting framework between users, QRNetwork, above-rail operators and the port/terminal.

Phase 1 of the long term solution

- 3.14 Phase 1 of the long term solution is a transitional phase moving towards achieving a long-term sustainable means of operation within a complete contractual framework within the Supply Chain. The applicants submit that a transitional phase is required because reforms to the contractual framework are unlikely to be completed for another 18-24 months; capacity up to 85 Mtpa has already been contracted for; and to incorporate the time taken for reformed access undertakings and access arrangements to be approved.
- 3.15 It is proposed that a transitional allocation mechanism (TAM) will operate until regulatory and contractual reform processes have been completed. The TAM will operate when:
- aggregate forecast coal tonnage demand exceeds the estimated declared System Capacity and
 - aggregate forecast coal production (based on actual throughput and mine stocks as assessed by the independent expert¹⁷) is likely to exceed the declared System Capacity (or is evident due to a vessel queue).
- 3.16 The applicants submit that the TAM aims to put in place an integrated whole-of-system approach which will facilitate rationing of access to capacity in order to align with what the system, as a whole, is capable of delivering. The TAM will not be required to operate when the coal chain as a system is able to meet the ability of the users to produce, sell and export coal.
- 3.17 The applicants submit that Phase 1 of the long term solution and the operation of the TAM represents a principled solution to encourage efficient investment and expansion in the medium term throughout the Supply Chain and enable participants of the Supply Chain to enter into contracts with greater certainty.

¹⁷ The QMS achieves coordination of the supply chain through capacity adjustments being determined by an independent expert. The independent expert has no incentive to reduce queue length above or below efficient levels. Supporting Submission to applications for authorisation A91107 - A91109, 14 November 2008, p 39.

Phase 2 of the long term solution

- 3.18 Phase 2 of the long term solution entails alignment and operation of contracts in accordance with the agreed Coal Chain Principles¹⁸ which will be reflected in the rail and port access undertakings (approved under the *Queensland Competition Authority Act 1997*) and associated contractual framework.
- 3.19 The applicants note that revised access undertakings are being developed and will be submitted to the Queensland Competition Authority for approval (see paragraph 3.12). As part of the reform, the draft of each revised undertaking is incorporating the Coal Chain Principles.
- 3.20 The applicants note that the key to making Phase 2 viable is that contractual alignment will require compromise between users in terms of allocating capacity when the Supply Chain is constrained.

Process for developing the long term solution

- 3.21 On 11 February 2009, the applicants advised the ACCC of the progress being made towards the development of a long term solution. The applicants advise that the process will involve two phases, being:

Phase 1 will result in the establishment of a Memorandum of Understanding (MOU) that will contain the key principles that will underpin coordination in the supply chain going forward. It is intended that this must be concluded by the end of May 2009. An Implementation Plan will also be developed to guide the development of the detailed solution (Phase 2).

Phase 2 will be the development and implementation of the commercial, operational, legal and regulatory frameworks to support the solution embodied in the MOU. This will be concluded in the 12 to 18 months following the execution of the MOU.

18 The objective of the development of the Coal Chain Principles is to maximise the value of the coal export industry by creating a framework to provide certainty of access to supply chain capacity such that: existing mines can rely on their contracted access to system capacity; and new/expanding mines have certainty of being able to contractually trigger and access increased coal chain capacity to meet future demand with reasonable notice. See Attachment C to Supporting Submission for further information.

4. Submissions received by the ACCC

- 4.1 The applicants provided a supporting submission with their applications for authorisation and has since provided further written and oral submissions in support of their applications.
- 4.2 The ACCC also sought submissions from around 35 interested parties potentially affected by the applications, including service providers, port users and relevant government authorities. The ACCC received public submissions from Rio Tinto, Xstrata, Asciano, and QRNational.
- 4.3 Rio Tinto supports the application for interim authorisation and notes that the QMS will assist with short term planning and management to avoid demurrage costs. However, Rio Tinto is of the view that the QMS 'has not been successful in ensuring that sufficient focus is maintained on contractual arrangements that are in place through the coal chain'. For this reason, Rio Tinto also supports the long term principles outlined in the application.
- 4.4 Xstrata also supports a further short extension to the QMS, 'primarily on the basis that progress demonstrated in broadly agreeing a sound set of commercial Coal Chain Principles represents a significant step towards addressing the underlying issues of the coal chain and finally removing the need for any future rationing systems once and for all.' Xstrata submits that an interim form of capacity rationing is required to mitigate against the risk of excess vessel queuing. Xstrata notes in their submission that they support:
- the continued operation of the QMS for only a very short time to enable the industry to finalise the details of the Transitional Allocation Mechanism (TAM). If the details of the TAM and the longer term mechanism are not defined in detail and submitted to the ACCC by 31 March 2009, then the QMS will self-terminate. Xstrata supports this approach which provides incentive for the coal producers to continue their cooperative approach towards addressing the issue of capacity rationing within a short period of time.
- 4.5 Asciano submits that, while it is not strongly opposed to the short term extension of the authorisation of the QMS, the existence of the QMS makes entry into the Queensland rail haulage market significantly more difficult. Asciano submits that this is the result of increased contractual uncertainty and capacity uncertainty under the QMS.
- 4.6 QRNational does not oppose the applications, as the request was for a short term extension of the QMS. QRNational notes that the ACCC should examine whether the claimed public benefits would be realised in the current economic environment. QRNational also advised that it is supportive of the intent to implement a long term solution in the DBCT Coal Chain.
- 4.7 The views of the applicants and interested parties are outlined in the ACCC's evaluation of the QMS in Chapter 6 of this draft determination. Copies of public submissions are available from the ACCC website (www.accc.gov.au) by following the 'Public Registers' and 'Authorisations Public Registers' links.

5. The net public benefit test

- 5.1 The ACCC may only grant authorisation where the relevant test in section 90 of the Act is satisfied.

Application A91107

- 5.2 The applicants lodged application for authorisation A91107 under section 88(1) of the Act to make and give effect to a contract, arrangement or understanding, a provision of which is or may be an exclusionary provision within the meaning of section 45 of the Act.
- 5.3 The relevant test is found in section 90(8) of the Act.
- 5.4 Section 90(8) states that the ACCC shall not authorise a proposed exclusionary provision of a contract, arrangement or understanding, unless it is satisfied in all the circumstances that the proposed provision would result or be likely to result in such a benefit to the public that the proposed contract, arrangement or understanding should be authorised.
- 5.5 The applicants have applied for authorisation that they may, from time to time, make and/or give effect to contracts, arrangements or understandings that contain provisions that are, or may be, exclusionary provisions within the meaning of sections 45 and 4D of the Act in connection with the supply and/or acquisition of coal handling services at DBCT, in particular arising from the proposed queue management system.

Application A91108

- 5.6 The applicants lodged application for authorisation A91108 under section 88(1) of the Act to make and give effect to a contract or arrangement, or arrive at an understanding, a provision of which would have the purpose, or would have or might have the effect, of substantially lessening competition within the meaning of section 45 of the Act. The relevant tests for this application are found in sections 90(6) and 90(7) of the Act.
- 5.7 In respect of the making of and giving effect to the arrangements, sections 90(6) and 90(7) of the Act state that the ACCC shall not authorise a provision of a proposed contract, arrangement or understanding, other than an exclusionary provision, unless it is satisfied in all the circumstances that:
- the provision of the proposed contract, arrangement or understanding would result, or be likely to result, in a benefit to the public and
 - this benefit would outweigh the detriment to the public constituted by any lessening of competition that would result, or be likely to result, if the proposed contract or arrangement was made and the provision concerned was given effect to.

- 5.8 The applicants have sought authorisation that they may, from time to time, make and/or give effect to contracts, arrangements or understandings that contain provisions that may have the purpose, effect or likely effect of substantially lessening competition within the meaning of section 45 of the Act in connection with the supply and/or acquisition of coal handling services at DBCT, in particular arising from the proposed queue management system.

Application A91109

- 5.9 The applicants lodged application A91109 under section 88(7) of the Act to engage in conduct to which sections 45D, 45DA or 45DB of the Act might apply. The relevant test for this application is found in section 90(8) of the Act.
- 5.10 Section 90(8) states that the ACCC shall not authorise the proposed conduct, unless it is satisfied in all the circumstances that such conduct would result or be likely to result in such a benefit to the public that the proposed conduct should be authorised.
- 5.11 The applicants have applied for authorisation to engage in conduct to which sections 45D, 45DA or 45DB of the Act might apply involving Babcock and Brown, DBCTPL and any producer of coal for export through DBCT, or exporter/s of coal through DBCT or any other person, which relates to or is in any way associated with, the proposed queue management system.

Application of the tests

- 5.12 There is some variation in the language in the Act, particularly between the tests in sections 90(6) and 90(8).
- 5.13 The Australian Competition Tribunal (the Tribunal) has found that the tests are not precisely the same. The Tribunal has stated that the test under section 90(6) is limited to a consideration of those detriments arising from a lessening of competition but the test under section 90(8) is not so limited.¹⁹
- 5.14 However, the Tribunal has previously stated that regarding the test under section 90(6):

[the] fact that the only public detriment to be taken into account is lessening of competition does not mean that other detriments are not to be weighed in the balance when a judgment is being made. Something relied upon as a benefit may have a beneficial, and also a detrimental, effect on society. Such detrimental effect as it has must be considered in order to determine the extent of its beneficial effect.²⁰

¹⁹ Australian Association of Pathology Practices Incorporated [2004] ACompT 4; 7 April 2004. This view was supported in VFF Chicken Meat Growers' Boycott Authorisation [2006] ACompT9 at paragraph 67.

²⁰ Re Association of Consulting Engineers, Australia (1981) ATPR 40-2-2 at 42788. See also: Media Council case (1978) ATPR 40-058 at 17606; and Application of Southern Cross Beverages Pty. Ltd., Cadbury Schweppes Pty Ltd and Amatil Ltd for review (1981) ATPR 40-200 at 42,763, 42766.

- 5.15 Consequently, when applying either test, the ACCC can take most, if not all, public detriments likely to result from the relevant conduct into account either by looking at the detriment side of the equation or when assessing the extent of the benefits.
- 5.16 Given the similarity in wording between sections 90(6) and 90(7), the ACCC considers the approach described above in relation to section 90(6) is also applicable to section 90(7).

Definition of public benefit and public detriment

- 5.17 Public benefit is not defined in the Act. However, the Tribunal has stated that the term should be given its widest possible meaning. In particular, it includes:

...anything of value to the community generally, any contribution to the aims pursued by society including as one of its principle elements ... the achievement of the economic goals of efficiency and progress.²¹

- 5.18 Public detriment is also not defined in the Act but the Tribunal has given the concept a wide ambit, including:

...any impairment to the community generally, any harm or damage to the aims pursued by the society including as one of its principal elements the achievement of the goal of economic efficiency.²²

Future with-and-without test

- 5.19 The ACCC applies the 'future with-and-without test' established by the Tribunal to identify and weigh the public benefit and public detriment generated by arrangements for which authorisation has been sought.²³
- 5.20 Under this test, the ACCC compares the public benefit and anti-competitive detriment generated by arrangements in the future if the authorisation is granted with those generated if the authorisation is not granted. This requires the ACCC to predict how the relevant markets will react if authorisation is not granted. This prediction is referred to as the 'counterfactual'.

Length of authorisation

- 5.21 The ACCC can grant authorisation for a limited period of time.²⁴

Conditions

- 5.22 The Act also allows the ACCC to grant authorisation subject to conditions.²⁵

21 Re 7-Eleven Stores (1994) ATPR 41-357 at 42,677. See also Queensland Co-operative Milling Association Ltd (1976) ATPR 40-012 at 17,242.

22 Re 7-Eleven Stores (1994) ATPR 41-357 at 42,683.

23 Australian Performing Rights Association (1999) ATPR 41-701 at 42,936. See also for example: Australian Association of Pathology Practices Incorporated (2004) ATPR 41-985 at 48,556; Re Media Council of Australia (No.2) (1987) ATPR 40-774 at 48,419.

24 Section 91(1).

Future and other parties

5.23 Applications to make or give effect to contracts, arrangements or understandings that might substantially lessen competition or constitute exclusionary provisions may be expressed to extend to:

- persons who become party to the contract, arrangement or understanding at some time in the future²⁶
- persons named in the authorisation as being a party or a proposed party to the contract, arrangement or understanding.²⁷

²⁵ Section 91(3).

²⁶ Section 88(10).

²⁷ Section 88(6).

6. ACCC evaluation

- 6.1 The ACCC's evaluation of the QMS is in accordance with the net public benefit test outlined in Chapter 5 of this draft determination. As required by the test, it is necessary for the ACCC to assess the likely public benefits and detriments flowing from the QMS.

The market

- 6.2 The first step in assessing the effect of the conduct for which authorisation is sought is to consider the relevant market(s) affected by that conduct.
- 6.3 The applicants submit that the relevant area of competition are those identified in the ACCC's determination of 29 February 2008, which are:
- the global market for coal (or at least the Asian coal market)
 - the market for the provision of coal loading services for bulk coal carrying ships in the Bowen Basin and
 - the market for the provision of rail haulage services in the Bowen Basin.
- 6.4 For the purposes of assessing the current applications for authorisation lodged by the applicants, the ACCC's view on market definition is unchanged.
- 6.5 The ACCC notes that each of the markets identified above may be affected by the QMS.

The counterfactual

- 6.6 As noted in Chapter 5 of this draft determination, in order to identify and measure the public benefit and public detriment generated by conduct, the ACCC applies the 'future with-and-without test'.
- 6.7 The applicants submit that the relevant counterfactual is one
- whereby ships are loaded in order of arrival, [and] it is in the interests of an individual user to have a large number of vessels in the queue, as that will maximise the tonnage of coal which that user can ship, so long as the return from that additional tonnage exceeds the cost of demurrage to the particular user. The counterfactual will result in excessive queues forming in the first quarter of 2009 and beyond.
- 6.8 In support of this counterfactual, the applicants note that the regulations that govern the operation of the coal terminal 'only permit the Operator to change the priority or order in which Vessels are berthed at the Terminal. It does not permit the Operator to reduce each user's contract tonnage and does not provide for a capacity balancing system.'
- 6.9 The applicants also submit that, 'it would be unrealistic to assume a counterfactual under which, in the absence of the QMS, the contracts for rail

haulage services would be rapidly brought into alignment with terminal capacity [as] . . . the avoidable costs of a tonne of coal are a small proportion of the current coal price.'

- 6.10 The applicants submitted to the ACCC on 28 January 2009 that they do not believe the Goonyella coal chain will be constrained in the next six months. It was specifically noted that demand for coal has fallen from a 56 Mtpa in October 2008 to 28 Mtpa in January 2009, which is much less than System Capacity.²⁸ As a result, the ACCC understands that the QMS is would not currently be in operation, even if authorised by the ACCC.
- 6.11 The applicants note that demand is not expected to start recovering until at least the second quarter of 2009, however is not expected to return to original peak levels for at the very least 12 months.
- 6.12 Given the current levels of demand for terminal services are much less than the capacity of the Goonyella Coal Chain, it is unlikely a queue larger than a working queue will form in the absence the QMS. This is discussed further below, under 'Public Benefits'.
- 6.13 The ACCC considers that the appropriate counterfactual to apply in these circumstances involves the operation of DBCT without a QMS, where all ships are loaded in order of arrival.

Public benefit

- 6.14 The applicants submit the grant of authorisation would result in a number of public benefits including:
- preventing a large vessel queue re-emerging, reducing the potential for incurring demurrage costs and reducing inefficiencies in the coal supply chain
 - throughput benefits from greater certainty
 - environmental benefits and
 - enhancing the reputation of Australian coal exports.
- 6.15 In considering public benefits - particularly cost savings from increases in productive efficiency from conduct proposed for authorisation - the ACCC applies a public benefit standard when determining the weight to be given to productive efficiency savings. That is, the ACCC will consider how much weight society considers should be attached to a benefit. Of particular interest will be the number and identity of the proposed beneficiaries.
- 6.16 An assessment of the public benefits claimed by the applicants follows.

²⁸ see paragraph 2.9

Reducing vessel queues and demurrage costs

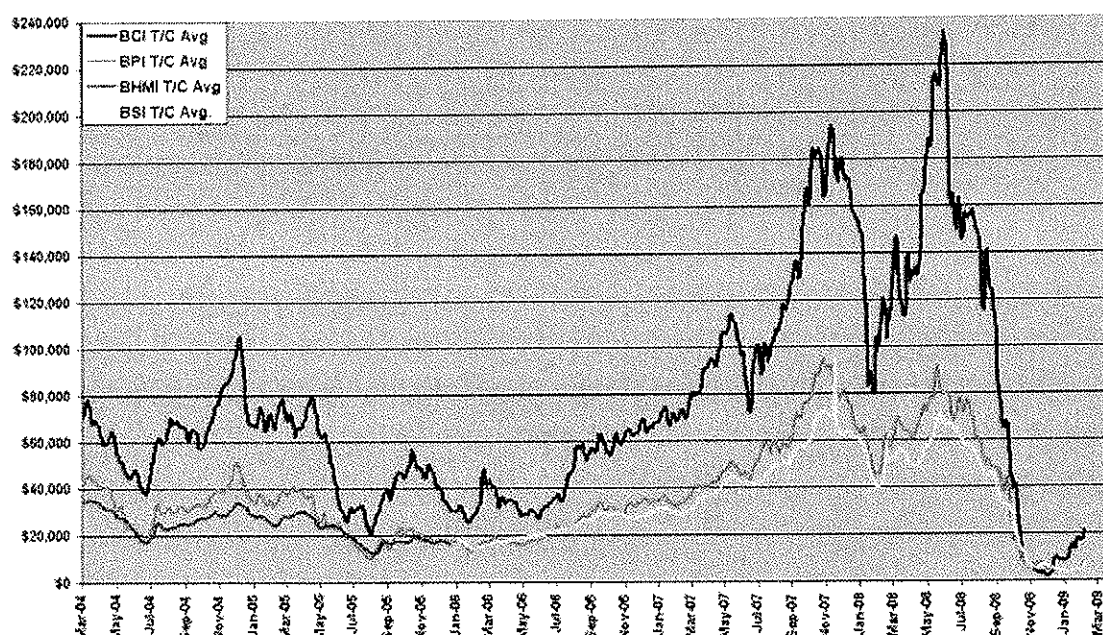
- 6.17 In the applicant's supporting submission, the applicants submit that continuation of the QMS would result in a saving of demurrage costs of approximately \$168 million.
- 6.18 At the time of lodging their applications for authorisation, the applicants submit that with a capacity management system in place for 2009, the ship queue at the end of June 2009 is estimated to be 19 ships with an average wait time of 8 days and a demurrage bill across the year conservatively estimated at \$59 million.
- 6.19 Alternatively, without a capacity management system in place for 2009, the ship queue at the end of June 2009 is estimated to be 109 ships with an average wait time of 41 days and a demurrage bill across the year conservatively estimated to be \$227 million.
- 6.20 On 10 December 2008 the applicants provided further information with respect to the developments regarding demand for coking coal, noting that demand had dropped significantly since late October. The applicants submit that the reduction in demand reduces, but does not eliminate, the likelihood of a lengthy queue at DBCT in the first half of 2009.
- 6.21 As at 6 December 2008, there were 14 vessels in the queue at DBCT. On 28 January 2009 the applicants advised that demand is not expected to start recovering until at least the second quarter of 2009, and is not expected to return to original peak levels for 12 months at the very least.
- 6.22 Xstrata submits that a limited extension of the QMS means that the risk of vessel queuing in the early part of 2009 is mitigated will provide a public benefit.
- 6.23 Asciano accepts that an extension of the QMS will result in fewer vessels in the queue in the factual and this would result in reduced demurrage costs. Asciano further submits that the applicants have overestimated the size of this benefit, submitting that the recent global financial crisis has had a significant impact on demurrage costs. Asciano submits that it understands demurrage has fallen from around US\$20 000 per day to US\$2000 per day. These conditions would be expected to continue over the term of the proposed authorisation. In response, the applicants note that at the time of lodging the applications for authorisation the demurrage estimates were correct, and notes that demurrage costs of the industry are, in the short term, locked in, so the impact of the reductions in demurrage rates paid by the industry will lag movements in the spot rate.
- 6.24 QRNational notes that a six month extension of the QMS may help to minimise the number of vessels in any queue of DBCT and limit demurrage costs as a result.

ACCC's view

- 6.25 The ACCC considers that a reduction in deadweight demurrage payments represents an increase in economic efficiency. That is, the cost of exporting coal is reduced, or alternatively, the amount of time that coal vessels sit unproductively in a queue is reduced.
- 6.26 The applicant's estimate in November 2008 was for a saving in demurrage costs of approximately \$168 million. The ACCC considers this figure now substantially overestimates these costs according to current market conditions.
- 6.27 The ACCC notes that, as at 6 December 2008, there were 14 vessels in the queue at DBCT. With the global financial crisis, there has been an even further downturn in demand at DBCT and as at January 2009, the applicants have advised the ACCC that there was no queue at DBCT.
- 6.28 The independent expert's report provided by the applicants in their supporting submission notes that if the global economic turmoil continues for some period then there is the distinct possibility that demurrage rates will fall below those used in the report. The ACCC notes Asicano's submission that demurrage rates have fallen significantly. The ACCC notes the applicants response that demurrage costs of the industry are, in the short term, locked in, so the impact of the reductions in demurrage rates paid by the industry will lag movements in the spot rate. The ACCC understands that it is expected that such conditions will continue during the first six months of 2009.
- 6.29 The ACCC also notes the significant fall in demand for coal since October 2008, particularly coking coal, consistent with a reduction in demand for steel based products resulting from the current economic environment.
- 6.30 The ACCC further notes that current vessel hire rates have plummeted during the last half of 2008, only making a slight recovery in recent months. Table 6.1 below illustrates the movements in vessel hire rates.

Table 6.1: Movement in vessel hire rates

**Daily Chart For Cape/Panamax/Handy
4 TC AVERAGE Values**



Source: <http://www.dryships.com/pages/report.asp>

- 6.31 Given the reduction in demand and costs for vessels, the applicant's have advised that the current vessel queue has dropped and demurrage costs are not being incurred. Therefore, while the vessel queues and demurrage savings are likely to be lower now than at previous times, they are a result of the drop in demand due to the global financial crisis rather than any QMS in place at the DBCT. The ACCC notes that a benefit in the form of reduced demurrage costs would only result in the instance where an extensive vessel queue would otherwise form in the first six months of 2009. In such circumstances the QMS may lead to a reduction in demurrage costs for the industry, particularly as falls in spot rates for demurrage may not have an immediate impact due to fixed contracted rates.
- 6.32 Overall, the ACCC considers that the reduced demand for coal makes it very unlikely that an excessive queue will arise in the absence of a QMS in the first six months of 2009. Therefore the ACCC does not consider the QMS will result in a public benefit from reduced demurrage costs.

Productivity and throughput increases from greater certainty

- 6.33 The applicants submit there are benefits in terms of productivity gains and throughput increases for all supply chain participants, arising from certainty of terminal capacity allocations offered by the QMS. In particular, the applicants submit this will benefit coal producers because production levels can be aligned to their System Capacity entitlements. The applicants argue that these

productivity gains represent a public benefit to the economy and the Australian public. The applicants submit that a reduction of 1 Mtpa is likely to reduce export earnings by up to \$300 million.

- 6.34 The applicants also submit that there will be productivity benefits for above rail operators. The applicants submit there may be a reasonably significant spot market for above-rail capacity during 2009. Certainty regarding System Capacity entitlements of users will be important for the efficient operation of this spot market.
- 6.35 Asciano submits that it is unclear why some of the certainty that is claimed to be a result of the QMS, eg the efficiency of the above rail spot market, would not be available in the counterfactual. In providing spot tonnes rail haulage, Asciano is indifferent as to whether the QMS is operational or not.

ACCC's view

- 6.36 In the previous decision regarding the QMS, the ACCC considered that the continued operation of the QMS was likely to provide greater certainty to producers as to the available capacity at DBCT, enabling them to more accurately forecast their production levels and maintain optimal stockpiling levels.
- 6.37 The ACCC remains of the view that, in a constrained environment, the QMS is likely to be able to deliver more orderly movement of coal and better coordination across the coal chain, leading to increased throughput by providing certainty as to how much coal a producer can export.
- 6.38 However, the ACCC considers that in the current market where demand for coal has dropped and vessel queues have diminished, this public benefit will not be realised. The ACCC understands that it is unlikely for a queue to develop during the period for which authorisation has been sought.

Reduced environmental risks

- 6.39 DBCT is situated adjacent to the Great Barrier Reef. The applicants note the Great Barrier Reef's importance to Queensland and Australia's tourism industry and the importance of not exposing the reef to negative external impacts.
- 6.40 The applicants also note that following the Pasher Bulker incident in Newcastle in June 2007, the Australian Transport Safety Bureau (ATSB) identified port congestion as a factor which increases the likelihood of ships anchoring in close proximity to each other which, in turn, results in less time to take action if their anchors drag, therefore creating a higher risk of collision. The ATSB also identified a potential for major pollution or the blockage of the port resulting in enormous financial costs.
- 6.41 The applicants submit that the extension of the QMS will reduce the environmental risks associated with a large vessel queue, particularly during the upcoming season which is prone to cyclone activity. The applicants

originally submitted that there was likely to be large queues prior to March 2009 which coincides with the cyclone season.

- 6.42 Asciano accepts there would be some environmental benefits but does not know how significant these benefits would be.

ACCC's view

- 6.43 The ACCC considers that reducing the environmental risks associated with a large number of bulk cargo vessels anchored near the Great Barrier Reef is a benefit to the public. The ACCC is not convinced, however, in the relevant period that the QMS mitigates against environmental risk, given that currently there is no queue at DBCT.
- 6.44 The ACCC also notes that the QMS was not developed due to environmental concerns. The ACCC considers that should a vessel queue develop and bring with it significant environmental concerns, it is likely there would be other means used for addressing such risks, for example government intervention. The ACCC notes that government interest has been compounded by the public concern generated by the 2007 Pasha Bulker incident in Newcastle.
- 6.45 Therefore, the ACCC considers that the continuation of the QMS results in limited benefit in the form of reducing environmental damage.

Improved Australian reputation

- 6.46 The applicants submit that the presence of a long vessel queue impacts on the reputation, both nationally and internationally, of coal producers and the Goonyella coal chain. The applicants submit that it impacts on customers' perceptions of price and reliability of the coal supply chain.
- 6.47 The applicants submit that by reducing the queue, the QMS improves the reputation of DBCT and provides a competitive advantage for Australian coal exports.
- 6.48 Asciano does not believe that the enhanced reputation of Australian coal exports would be a material factor in favour of the QMS especially given that the QMS would only be in place for a maximum of six months.

ACCC's view

- 6.49 As noted in the previous decisions regarding the QMS, the ACCC considers that increased certainty with regard to coal deliveries and cost savings as a result of reduced waiting times (in vessel queues) would appear to be factors that influence the purchasing decisions of overseas buyers.
- 6.50 The ACCC therefore considers that a short extension to the QMS may lead to a slight improvement in the reputation of DBCT. Also, given recent events such as the 2007 Pasha Bulker incident, the ACCC considers that the QMS is likely to reduce the risk of an incident occurring that may harm Australia's international reputation.

- 6.51 However, due to the global financial crisis, vessel queues have diminished and excessive queues are unlikely to develop within the first half of 2009. The ACCC notes that queue size is a highly visible issue and there may be potential for harm to our reputation if there is a slow response to global increases in demand for coal.
- 6.52 The ACCC considers that an extension of the QMS may reduce the negative impact generated by an excessive vessel queue to an observer, and therefore may result in limited public benefit.

ACCC conclusion on public benefits

- 6.53 Due to the global financial crisis and reduced demand, there is currently no queue at DBCT. The applicants have advised the ACCC that as a result of current market conditions it is unlikely that excessive queues will develop within the first half of 2009, the term for which authorisation is sought.
- 6.54 Therefore, the ACCC does not consider that the public benefits claimed by the applicants will be realised during the term for which authorisation is sought. The ACCC does not accept that an extension of the QMS would result in a public benefit in the short term.

Public detriment

- 6.55 Following discussions with interested parties, the ACCC has identified the following detriments from the continued operation of the QMS:
- restriction of aggregate coal exports from the Goonyella coal chain
 - reduced likelihood of competitive entry in above rail haulage services
 - impact on investment in the Goonyella coal chain and
 - reduced incentive to develop a long-term solution.
- 6.56 An assessment of these potential public detriments follows.

Potential detriment – restriction of aggregate coal exports from the Goonyella coal chain

- 6.57 Any reduction in the volume of coal moved through the Goonyella coal chain as a result of the QMS would constitute a detriment to the public, in the form of lost coal exports.
- 6.58 The applicants submit that in the short term the QMS maximises efficiency and capacity throughput of the coal chain, given capacity constraints. Throughput is maximised as the QMS rations excess demand to equate System Capacity and allows participants to trade capacity entitlements ('Entitlements').

ACCC's view

- 6.59 In previous decisions, the ACCC recognised one of the key objectives of the QMS is to maximise utilisation of System Capacity, thereby maximising coal exports from DBCT. The ACCC understands that the QMS operates by allocating System Capacity to coal producers based on their contracted tonnages with Babcock and Brown. The QMS also allows for a Working Queue of ships and pooling and/or swapping of Entitlements by producers. The ACCC recognises that in the short term the QMS is indeed successful in ensuring that all available System Capacity is utilised.
- 6.60 Under the QMS, where demand for DBCT services is less than declared System Capacity each coal producer will be provided with an allocation equal to its annual contract tonnage. The ACCC considers this will be the case in the short term.
- 6.61 Given the recent drop in demand for coal loading services at DBCT, the ACCC believes that in the short term the QMS is unlikely to restrict aggregate coal exports.
- 6.62 However, beyond the short term the ACCC is concerned coal export volumes may be affected by an ongoing QMS reducing the incentive for industry participants to develop a long term solution. This issue is discussed further at paragraphs 6.78 to 6.90.

Potential detriment – reduced likelihood of competitive entry in above rail haulage services

- 6.63 The ACCC has previously considered that the operation of the QMS decreases the likelihood of competitive entry in the above rail haulage market.
- 6.64 The applicants submit that the implementation of the long term solution will likely provide certainty to potential new entrants and result in an incentive for entry. They therefore argue the 'Proposed Solution assists competitive entry'.²⁹
- 6.65 Asciano submits that the operation of the QMS has made entry into the rail haulage market difficult, and decreases the potential for meaningful above rail competition. They identify the following two reasons:
- rationing port capacity creates uncertainty about the level of actual verses contracted tonnes that a new entrant will haul and
 - in the early years of a contract, actual tonnes hauled will be less than contracted tonnes/long term haulage levels. Thus entry will be more challenging as assets will have to be acquired that will not initially be fully utilised.

²⁹ The applicants use the term 'Proposed Solution' to incorporate not only the short term extension of the QMS, but also the implementation of Phase 1 of the long term solution (the Transitional Allocation Mechanism) and Phase 2 of the long term solution. Asciano's and the ACCC's concerns relate to the QMS decreasing the likelihood of competitive entry in the above rail haulage market.

- 6.66 Asciano notes the difficulty in getting customers to sign contracts given the capacity uncertainty they face from the operation of the QMS. They also submit that track access is uncertain because producers are rationed at one port (DBCT) but not the other (Hay Point Coal Terminal). They also note that capacity rationing, such as the QMS, creates a barrier for expansion.
- 6.67 The applicants note the following in response to Asciano's concerns:
- Asciano assumes their customers would be prepared to incur more demurrage than other coal producers using the QMS at DBCT.
 - The QMS, if granted authorisation, would only be in operation for a further 3 to 6 months, terminating prior to Asciano's official market entrance.
 - Opportunities for spot-market sales by Asciano will exist under the operation of the QMS between January and June 2009.

ACCC's view

- 6.68 As set out in its determination dated 29 February 2008, the ACCC understands that significant infrastructure costs create high barriers to entry in the provision of above rail haulage services. These barriers become higher if there is uncertainty around the amount of return that new entrants can expect to receive on their assets.
- 6.69 The ACCC notes that the applicants consider that the QMS is unlikely to operate during the period for which authorisation is sought. However, ACCC considers that extending the operation of the QMS has the potential to reduce the likelihood of successful entry by above rail haulage competitors, due to the potential for their customer's capacity to be rationed in the event that a queue were to form.
- 6.70 To the extent that extending the QMS further delays the development of the long term solution, it is likely to result in detriment through delaying competitive entry in above rail.
- 6.71 The ACCC remains of the view that a long term solution that offers long-term certainty over the commercial operations of the coal chain is more likely to give new entrants the opportunity to determine whether it is possible to recover the costs associated with competitive entry.

Potential detriment – impact on investment in the Goonyella coal chain

- 6.72 As stated in the past, the ACCC is satisfied that the QMS had not hindered investment in the Goonyella coal chain, noting significant contributions made by DBCTPL and QRNational.
- 6.73 In January 2008, the second and final O'Donnell Report noted the misalignment in investment in the Goonyella coal chain:

A coordinated approach to master planning of infrastructure is essential. The situation where investments are being made without concurrent investment in other parts of the

supply chain and then additional forecast tonnages are contracted out should never be allowed to happen again. The regulatory frameworks that underpin the governance of the supply chain should support this approach³⁰.

ACCC's view

- 6.74 The ACCC recognises that recent expansion activities in the Goonyella coal chain indicate that the existence of the QMS has not entirely removed the incentive for investment in the Goonyella coal chain. In this regard the ACCC notes the applicants have detailed the investments made and currently in progress in a table 'Capacity expansion in the Goonyella coal chain' in their supporting submission.³¹ In this regard, the ACCC considers the QMS is unlikely to give rise to this public detriment in the short term, particularly as the applicants consider that the QMS is unlikely to operate during the period for which authorisation is sought.
- 6.75 Consistent with its previous decisions, the ACCC is concerned that the QMS, which first started operating in April 2005 and, despite significant investments, there is still an imbalance between the contracted demand for coal loading services and the capacity of the Goonyella coal chain (including DBCT).
- 6.76 The ACCC is concerned that the QMS causes uncertainty around the delivery of tonnage amounts contained in coal producers' contracts with port and rail service providers. This has the potential to distort market signals and affect investment decisions.
- 6.77 The ACCC considers a degree of uncertainty going forward has the real potential to delay long-term investment such as decisions to further increase rail capacity and expand DBCT beyond 85 Mtpa. That said the ACCC considers that investment alone is not enough to address the underlying issues in the Goonyella coal chain.

Potential detriment – reduced incentive to develop a long-term solution

- 6.78 The applicants note that 'the ACCC has also stated that it believes the underlying causes of the vessel queue are not being addressed.'
- 6.79 The applicants submit, as noted above, recent investments in both rail and terminal capacity demonstrate that the QMS has not proven to be an impediment to investment incentives. The applicants note that the QMS is not designed to coordinate the investment across the whole supply chain, which the applicants consider to be necessary in order to increase system capacity. The applicants submit that this is a role sought to be performed by the Proposed Solution.
- 6.80 In support of their application for interim authorisation, the applicants submitted that:

30 The Goonyella Coal Chain Capacity Review (second and final report), Stephen O'Donnell, 10 January 2008, p 7.

31 Supporting Submission to applications for authorisation A91107 - A91109, 14 November 2008, 'Table 1: Capacity expansions in the Goonyella coal chain', p25

There is no question as to the determination of the majority of the Applicant Users to agree on a long-term solution for the management of the coal supply chain. However, rejection of an interim authorisation will significantly increase the risk that certain Users will withdraw from the current process. Accordingly, any failure to grant an interim authorisation increases the risk of the current opportunity to develop and implement a long-term solution with unanimous industry support being lost.

- 6.81 The applicants submit that, 'together with the reforms taking place in the industry, the Proposed Solution seeks to address the ACCC's concerns and seeks to result in an efficient and aligned Supply Chain in the long term. Therefore, there are compelling reasons for authorising the implementation of the Proposed Solution.'

ACCC's view

- 6.82 As set out in Chapter 3, the present application under consideration is a 6 month extension to the QMS, which was effectively authorised by the ACCC between April 2005 and 31 December 2008, conditional upon the applicants applying for authorisation for the proposed long term solution by 31 March 2009.

- 6.83 At the time of granting authorisation in 2005, the QMS was proposed as a short term solution while investment and capacity expansions took place.

- 6.84 As noted by the applicants, the ACCC made a number of comments about the underlying issues facing the Goonyella Coal Chain in its determination authorising the QMS on 29 February 2008. In particular, the ACCC considered that:

There are a number of factors that appear to be contributing to coal chain issues including, service providers contracting based on their individual capacities without reference to the coal chain as a whole, and insufficient commercial drivers to provide the required capacity to maximise supply chain throughput. . .

Going forward, the ACCC considers that the contractual framework that underpins the functions of the Goonyella coal chain needs to better reflect the operation realities (i.e. the capacity of each element in the coal chain is reliant upon the others) and provide sufficient certainty to underwrite necessary investment.

- 6.85 The ACCC notes that progress has been made to address the underlying issues facing the Goonyella Coal Chain in the last couple of years. This progress has been discussed in detail in Chapter 3, and includes the O'Donnell review, the establishment of a Supply Chain Board, and the appointment of Ross Dunning AC as the Central Coordinator for the Dalrymple Bay Coal Chain. The ACCC also notes the recent progress towards the establishment of a Memorandum of Understanding containing 'the key principles that will underpin coordination of the supply chain going forward. The applicants advise that this MOU will be finalised in May 2009.
- 6.86 Further steps currently being undertaken by the industry include progress towards contractual alignment through the development of the Babcock and Brown and QRNational access undertakings to introduce concepts of 'System Capacity'.

- 6.87 However, the ACCC considers that granting a further extension to the QMS poses a real risk that some producers will take a short term approach, and that the parties will not be able to reach an agreement on the long term solution by 31 March. Even though the current application is proposed to be 'self terminating', there is nothing stopping the parties coming back at that time with another request for a short term extension of the QMS.
- 6.88 The ACCC is of the view that, while some progress has been made in long-term planning to address contracting issues and capacity constraints, the existence of the QMS may reduce incentives to address the issues.
- 6.89 In the current environment, in which the demand for coal loading services does not exceed system capacity there is unlikely to be any public detriment from lost export revenue in the short term. However, the ACCC remains of the view that the existence of the QMS is likely to reduce the incentive to address underlying issues contributing to capacity constraints. This, in turn, is likely to lead to inefficient investment decisions and reduced export revenue during times when the demand for coal loading services exceeds system capacity.
- 6.90 The ACCC considers that future potential reductions in export revenue will be significantly detrimental to the public, particularly in the current economic climate. The ACCC considers that the QMS is likely to generate significant public detriment for this reason.

ACCC conclusion on public detriments

- 6.91 The ACCC considers that the continued operation of the QMS has the potential to result in the following detriments:
- reduced incentives for efficient investment in the Goonyella coal chain
 - reduced incentive to develop a long-term solution and
 - reduced likelihood of competitive entry in above rail haulage services

Balance of public benefit and detriment

- 6.92 The ACCC may only grant authorisation if it is satisfied that, in all the circumstances, the continued operation of the QMS is likely to result in a public benefit that will outweigh any public detriment.
- 6.93 In the context of applying the net public benefit test at section 90(8)³² of the Act, the Tribunal commented that:

... something more than a negligible benefit is required before the power to grant authorisation can be exercised.³³

32 The test at 90(8) of the Act is in essence that conduct is likely to result in such a benefit to the public that it should be allowed to take place.

33 Re Application by Michael Jools, President of the NSW Taxi Drivers Association [2006] ACompT 5 at paragraph 22.

- 6.94 Due to the global financial crisis and reduced demand, there is currently no queue at DBCT. The applicants have advised the ACCC that as a result of current market conditions it is unlikely that excessive queues will develop within the first half of 2009, the term for which authorisation is sought.
- 6.95 Therefore, the ACCC does not consider that the public benefits claimed by the applicants will be realised during the term for which authorisation is sought. The ACCC does not accept that an extension of the QMS would result in a public benefit in the short term.
- 6.96 The ACCC considers that continued operation of the QMS, in the longer term, has the potential to impact upon investment and reduce the potential for competitive entry in above rail haulage services.
- 6.97 The ACCC is concerned that the ongoing operation of the QMS has reduced the incentive for a long term solution to be developed and implemented, which has resulted in potentially significant foregone coal export opportunities. As such, it is difficult to see that any extension of the current or a similar QMS, even if world demand were to pick up again, would be in the public interest.
- 6.98 In these circumstances, the ACCC encourages all relevant parties to continue to work together to finalise and implement a long term solution so that future potential queuing issues can be avoided.
- 6.99 On balance, the ACCC considers the proposal is unlikely to generate public benefit. To the extent that any public benefit may result from the arrangements (for example, if a queue were to form during the period for which authorisation has been sought so that the benefits claimed by the applicants, such as demurrage savings, are more likely to occur), the ACCC considers that these benefits will not outweigh the likely public detriments. Accordingly, the ACCC proposes to deny authorisation to the extension of the QMS.

7. Draft determination

The application

- 7.1 On 14 November 2008, eight users of the Dalrymple Bay Coal Terminal (the applicants) lodged applications for authorisation A91107 - A91109 with the Australian Competition and Consumer Commission (the ACCC).
- 7.2 Application A91107 was made under subsection 88(1) of the *Trade Practices Act 1974* (the Act) using Form A, Schedule 1 of the Trade Practices Regulations 1974. The application was to make and give effect to a contract, arrangement or understand, where a provision of the proposed contract, arrangement or understand would be, or might be, an exclusionary provision within the meaning of section 45 of the Act.
- 7.3 Application A91108 was made under subsection 88(1) of the Act using Form B Schedule 1 of the Trade Practices Regulations 1974. The application was to make and give effect to a contract or arrangement, or arrive at an understanding, a provision of which would have the purpose, or would have or might have the effect, of substantially lessening competition within the meaning of section 45 of the Act.
- 7.4 Application A91109 was made under subsection 88(7) of the Act using Form D Schedule 1 of the Trade Practices Regulations 1974. The application was to engage, in concert with other persons, in conduct that prevents or substantially hinders, or may prevent or substantially hinder, a third person from engaging in trade or commerce involving the movement of goods between Australia and places outside Australia.
- 7.5 The applications relate to a short-term extension of the Queue Management System (QMS) designed to address the imbalance between the demand for coal loading services at the Dalrymple bay Coal Terminal and the capacity of the Goonyella coal chain.

The net public benefit test

- 7.6 For the reasons outlined in Chapter 6 of this draft determination, the ACCC is not satisfied that the conduct for which authorisation is sought is likely to result in public benefit. To the extent that any public benefit may result from the arrangements, the ACCC is not satisfied that the conduct for which authorisation is sought is likely to result in a public benefit that would outweigh the detriment to the public constituted by any lessening of competition arising from the arrangements.
- 7.7 The ACCC is not satisfied that the arrangements for which authorisation is sought are likely to result in such a benefit to the public that the arrangements should be allowed to take place.

7.8 The ACCC therefore **proposes to deny** authorisation to applications A91107, A91108 and A91109.

7.9 This draft determination is made on 23 February 2009.

Interim authorisation

7.10 At the time of lodging the application the applicants requested interim authorisation to for the extension of the QMS. On 10 December 2008 the ACCC denied the request for interim authorisation. In denying interim authorisation, the ACCC considered that in the absence of a long term solution having been developed, interim authorisation would not be in the public interest.

7.11 The ACCC has reconsidered the request for interim authorisation and has decided to deny the request, given the applicants have not provided any further information supporting their request.

Further submissions

7.12 The ACCC will now seek further submissions from interested parties. In addition, the applicant or any interested party may request that the ACCC hold a conference to discuss the draft determination, pursuant to section 90A of the Act.