

EXECUTIVE SUMMARY

Both government and non-government business activities have always been potentially subject to declaration under Part 5 of the *Queensland Competition Authority Act 1997* (the QCA Act). This Part relates to third party access to the services provided by essential infrastructure.

In addition, government business activities have always been potentially subject to declaration under Part 3 of the QCA Act, which deals with prices oversight of monopoly business activities. The criteria to which the Premier and the Treasurer (the Ministers) must have regard in deciding whether or not to declare a government business activity to be a monopoly business activity were developed by the Authority in 1997.

Recent amendments to the QCA Act make non-government business activities potentially subject to declaration as monopoly business activities. The amendments require the Authority to develop criteria the Ministers must have regard for in deciding whether to declare a non-government business activity to be a monopoly business activity.

The test for identifying non-government monopoly business activities is based upon an assessment of whether these business activities have sufficient market power that they are capable of persistently behaving in a manner different to that which would occur in a competitive market. In competitive markets, sellers increase their prices or reduce the quality of their products or services at their peril, as consumers are able to find alternatives relatively easily.

Where an incumbent possesses substantial market power, the rigours normally provided by competition to protect customers and to innovate are substantially weakened. This is likely to occur where:

- (a) a business activity enjoys a substantial influence in a market;
- (b) a business activity can act to an appreciable degree independently of its competitors¹; or
- (c) a business activity's competitors are unable or unwilling to effectively compete with it.

Figure 1 gives a simplified description of the framework within which the Authority recommends non-government monopoly business activities be identified. Basically, a three-step process is envisaged:

step 1 - determines whether the activity is a non-government business activity;

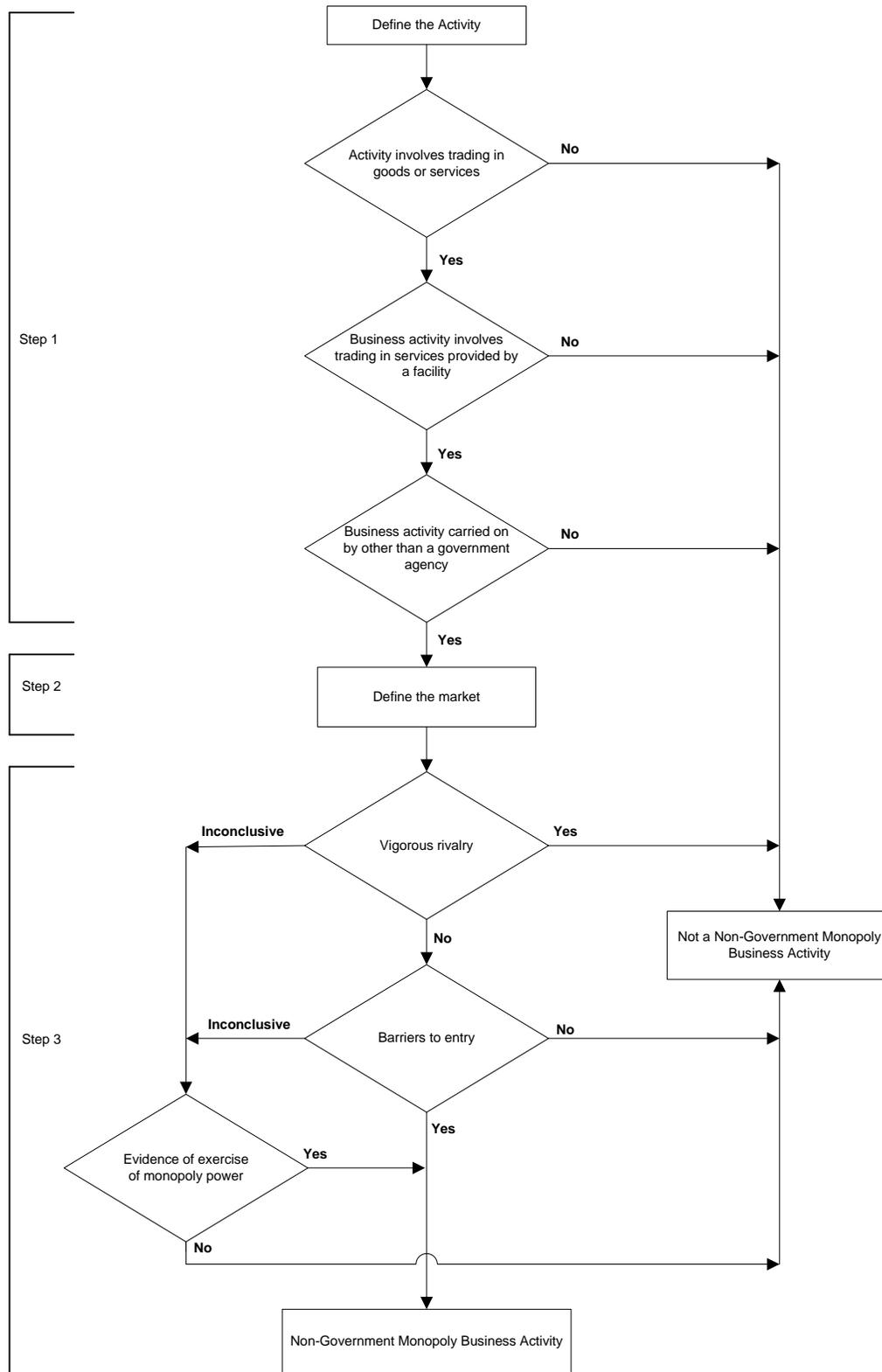
step 2 - defines the markets in which the non-government business activity operates; and

step 3 - assesses the intensity of competition in those markets relevant to the enquiry.

Declaration as a monopoly business activity does not automatically subject the monopoly business activity to a prices oversight investigation by the Authority. This requires a separate decision by the Ministers. In this regard, the Ministers may refer the monopoly business activity to the Authority for an investigation into its pricing practices or for ongoing monitoring of its pricing practices.

¹ The term "competitor" refers to actual or potential competitors.

Figure 1: Simplified Framework for Identifying Non Government Monopoly Business Activities



Step 1 - Determining Whether the Activity is a Non-Government Business Activity?

The first step in the process is to properly define the activity that is to be the subject of the analysis with a view to determining whether it is a non-government business activity. There are two requirements under the QCA Act to be addressed in this context. The first requirement is that the business activity is being carried on by a person other than a government agency.

The second requirement is that the activity must involve trading in services provided by means of a facility. A facility includes: rail transport infrastructure; port infrastructure; electricity, petroleum or gas transmission and distribution infrastructure; and water and sewerage infrastructure, including treatment and distribution infrastructure.

In practical terms, a non-government business activity is:

An activity undertaken by the private sector that involves trading in services provided by means of an infrastructure facility.

It should be noted that:

- (a) 'trading' requires services to be provided to another legal entity;
- (b) 'trading in' requires actual trading as opposed to the mere potential for trading. Therefore, a refusal to supply services to any other legal entity will not constitute a business activity for the purposes of Part 3. [Depending on the circumstances, a refusal to supply services may be able to be addressed under Part 5 or Part 5A of the QCA Act];
- (c) only trading in 'services' is encompassed by the definition. Trading in goods is not; and
- (d) a 'facility' is limited to the infrastructure examples given in the QCA Act or infrastructure of a similar nature to the examples given.

A non-government entity may undertake several distinct business activities. Consequently, precisely defining the service that is the subject of the analysis is essential to correctly identify the business activity and to define the relevant market, which is the next step in the process.

Step 2 - Market Definition

A market is an area of close competition or rivalry. If there is no close competition this can, of course, indicate a monopolistic market. Defining a market involves drawing a line in the chain of substitutes for a service that potentially compete with it. In defining and analysing a market, it is important to consider the purpose of the investigation, which, in the case of identifying non-government monopoly business activities, is to assess the extent of competitive pressure.

The analysis will need to address the service market (alternative services that can be used instead of those provided by the business activity), the geographic market (the geographical region from which alternative sources of supply may be found), the relevant functional level of the market under consideration and the period of time allowed for an effective competitor to enter the market.

Once the relevant market has been defined, the intensity of the competitive pressures can be assessed and other relevant factors, such as the extent of barriers to entry, can be considered.

Step 3 - Assessing the Level of Competition in the Market

The principal factors that assist in determining whether a non-government business activity is not effectively constrained by competitive pressures in a market are:

- (a) the absence of vigorous competition in the market together with barriers to entry for new entrants into the industry (or to the expansion of existing rivals); and
- (b) evidence of the exercise of substantial market power by the business activity (e.g. by way of excessive pricing, inefficient operations or cross-subsidisation).

An absence of vigorous rivalry and the existence of barriers to entry constitute the primary test. If there is an absence of vigorous rivalry and barriers to entry exist then the activity is a monopoly business activity. If there is evidence of vigorous rivalry or if no barriers to entry exist, then the activity is not a monopoly business activity.

Where the primary test is inconclusive or there is insufficient information for it to be applied, the second test relating to evidence of the exercise of substantial market power is applied.