

**PRODUCTIVITY COMMISSION
INQUIRY INTO
ECONOMIC REGULATION OF
HARBOUR TOWAGE
AND RELATED SERVICES**

AIMPE SUBMISSION

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CONTENTS

1.	Introduction	3
2.	Port Types	4
3.	Towage Service Providers	4
4.	Towage Ownership – Entry and Exit	5
5.	Competition – A New Player	6
6.	Geography and Centralisation	7
7.	Trading Hours	8
8.	Microeconomic Reform	8
9.	Reliability	9
10.	Port Protection	10
11.	Salvage	11
12.	Conclusions	12

1. INTRODUCTION

Harbour towage is a comparatively small part of the Australian transport and distribution industry. There are relatively few people employed in harbour towage, either directly or indirectly. Revenue for the sector is not officially aggregated anywhere but is likely to be in the vicinity of \$300 million per annum. This is for services delivered in some 42 trading ports where towage services are available.

For such a small sector, harbour towage has been investigated like few other areas. The process goes like this - users complain about the cost of towage and Government sets up another inquiry. This pattern has been seen over many years. Past studies/inquiries include:

- ❖ Harbour Towage Services in Australian Ports, Information Paper no. 27 BTCE 1988;
- ❖ Harbour Towage An Analysis of industry Performance, Occasional Paper 96, BTCE 1989;
- ❖ Inquiry into Harbour Towage Charges, Prices Surveillance Authority, August 1990;
- ❖ Monitoring of Harbour towage Charges, Prices Surveillance Authority, July 1993;
- ❖ Issues Paper for the Inquiry into the Review of Harbour Towage Declaration, Prices surveillance Authority, June 1995;
- ❖ Inquiry into harbour towage declaration, Prices surveillance authority, December 1995;
- ❖ International Benchmarking of the Australian Waterfront, Productivity Commission 1998; and
- ❖ National Competition Policy Review of the Transport Infrastructure Act 1994 Harbour Towage Provisions, Queensland Transport, August 2000.

The current method of *economic* regulation of the harbour towage sector takes the form of surveillance of prices in a limited number of declared ports. These ports are the major metropolitan ports.

Adsteam is the major operator in the sector having bought out Howard Smiths in 2001. Now Adsteam's price rises in several of the declared ports has led to another outcry and another inquiry.

All sorts of bodies that usually support free trade apparently want the principles of free trade *not* to apply to them. Rather they seek government intervention to control prices.

AIMPE by contrast submits that external price surveillance of a limited number of ports has not proved particularly effective. By contrast, the internal process of microeconomic reform has been dramatic in the towage sector and has delivered huge change in almost all ports around the coast. Accordingly the regulators should acknowledge the product of the change process and leave the question of price to the market. This would be consistent with s.8 (1)(b) of the Productivity Commission Act 1998, which requires the Commission to have regard to the need to reduce regulation of industry.

If however, there is to be any further government *economic* regulation in this sector it should be of the nature of *price monitoring* directed to the full range of ports. The

provision of broad information to the public may result in more transparency for those not involved in the business on a day to day basis.

2. PORT TYPES

Towage services are provided in a relatively large number of ports ranging from the capital city multi-faceted ports ('integrated') through significant regional ports ('regional') down to single berth sole user ports ('dedicated').

Capital city ports tend to dominate in the merchandise trades including most container traffic and car imports/exports as well as petroleum trades. Regional ports typically service their hinterland by facilitating exports of mining and agricultural produce and importing requisites for those industries. Single user ports are often privately owned and established by and for a particular company/organisation and usually are for bulk trades.

The current economic regulation therefore only relates to the capital city 'integrated' ports.

3. TOWAGE SERVICE PROVIDERS

The single user ports sometimes have towage services provided on an in-house or vertically integrated basis. Examples of this situation include Gove, Groote Eyland and Cape Flattery. In the past decade other single purpose ports have out-sourced their towage services to independent operators. Examples include Dalrymple Bay, Carnarvon/Cape Cuvier, Port Walcott, and Withnell Bay.

Yet other single purpose ports have services provided by 'second tier' towage operators such as:

Port Lincoln Tugs Pty Ltd (Thevenard, Port Lincoln and Wallaroo)
North Western Shipping and Towage Pty Ltd (Port Latta and Triabunna/Spring Bay)
and
Teekay Shipping Australia Pty Ltd (Hay Point).

The Adsteam group provides towage services in several other single purpose ports (Weipa, Mourilyan, Lucinda, Bowen/Abbot Point, Bundaberg and Eden).

Turning to the regional ports some are serviced by independent operators like McKenzies Tugs (Esperance), Riverwijs (Bunbury) and Dampier. Second tier companies are also prominent in the servicing of regional ports for example North Western Shipping & Towage Pty Ltd (Portland, Burnie, Devonport, Launceston and Hobart), Coastal Tug and Barge Pty Ltd (Darwin) and Teekay Shipping Australia Pty Ltd (Port Hedland).

The Adsteam group also has operations in several regional ports including Geraldton, Albany, Whyalla, Geelong, Westernport, Port Kembla, Newcastle, Gladstone, Mackay, Townsville and Cairns.

The major metropolitan ports have their towage services provided by the Adsteam group (including Fremantle, Adelaide, Melbourne, Sydney and Brisbane). This was not the case until 2001 when Adsteam group bought Howard Smith's towage interests. This was not opposed by the ACCC.

4. TOWAGE OWNERSHIP – ENTRY AND EXIT

Entry and exit of operators from the Australian Towage Industry has been quite common over the last decade or more. In Port Hedland Adsteam once operated the tugs, then after the contract expired BHP Transport started running tugs now BHP Billiton has in 2002 outsourced BHP Transport to Teekay Shipping Australia. Several years ago Robe River Iron set up a subsidiary to provide towage in Port Walcott – Cape Lambert Services Pty Ltd, subsequently Cape Lambert Services was liquidated and the towage services contracted out to Westug. For many years Mermaid Sound Port and Marine Services provided towage services to its parent Woodside Energy Limited until in 2001 it outsourced to a new independent operator King Bay Marine Employment Service. Hammersley Iron originally had a subsidiary Pilbara Harbour Services which provided towage services until it outsourced the services.

P&O Towage Services was a provider of towage services in Carnarvon/Cape Cuvier, Geraldton and Kwinana until it was taken over by the Adsteam group. Carnarvon/Cape Cuvier was subsequently outsourced. Towage in the Port of Bunbury was operated by an Adsteam subsidiary for many years until 2000. After a bitterly contested contract tender, the services are provided by Riverwijs. AIMPE rejects the ‘partnership’ model used by Riverwijs because it undermines a range of social norms such as taxation and avoids various employee protection legislation. In the Port of Fremantle a licence tendering process in 2000/2001 saw Adsteam have its licence renewed for 2 1/2 years. In Geraldton and Albany there have been contract/licence renewal processes in recent years.

In Tasmania there was a time when towage services in most ports were provided directly by the local port authority. These were ‘privatised’ or outsourced several years ago. North Western Shipping & Towage gained the work. North Western Shipping & Towage also bought out the southern operator Hobart Towage and Lighterage. Brambles Marine subsequently bought out North Western Shipping & Towage however it has recently sold the business (2002) to an independent consortium and exited towage. NWS&T also operates in Portland Victoria since the Port authority there decided not to provide towage services directly.

Victorian operations have been very stable since the local port authority in Geelong outsourced in the 1980s. Also in the early 1980s McIlwraith McEachern exited the field after competing with the Howard Smith subsidiary for several years. Of course in 2001 Adsteam bought out the Howard Smith operations in Westernport, Melbourne and Geelong.

In Port Kembla the main changes have been in the ownership of the local operator Wallace Tugs. Previously a joint venture operator, Brambles sold out its interest to Adsteam after a failed bid to take over the total ownership of the company. Towage services in the Sydney ports were for many years provided by two operators J. Fenwick & Co and Waratah Towage. Brambles bought Fenwicks in the late 1960s while Waratah was a joint venture between Adsteam and Howard Smith. In 1996 Brambles sold Fenwicks to Adsteam and the operations were integrated. Newcastle reflected the pattern of Sydney with Fenwicks and Waratah providing services for many years. These were provided on a co-operative basis with each company allocating two tugs to the port and jointly servicing 3 and 4 tug work. In 1994 BHP commenced towage operations in competition to the Fenwicks/Waratah operations. The latter were subsequently integrated as per the Sydney takeover of Fenwick. For 5 years the two operations battled for market share with both claiming to have lost

money for the whole period. In 1999 BHP decided to stop losing money and sold out to Adsteam.

Change in towage operators in Queensland towage has been most significant in the bulk ports of Weipa, Hay Point and Dalrymple. Weipa was serviced by McIlwraith McEachern until 1995 when that company exited. Howard Smith took over operations until it was in turn bought out by Adsteam in 2001. Hay Point was managed by J. Fenwick until it was in-housed by the BHP group and BHP Transport became the operator. As of 2002 Teekay Shipping Australia is the operator having taken over from BHP Billiton in an out-sourcing exercise. McIlwraith McEachern was the service provider in Dalrymple Bay until the coal consortium in-housed to a newly formed subsidiary Dalrymple Marine Services. Subsequently in 1998 an independent Daltug Pty Ltd took over the operations.

In Cairns, Mourilyan, Lucinda, Townsville and Mackay towage services are provided by Adsteam group subsidiary North Queensland Marine Towage. The only change in ownership here has been the buy-out by Adsteam of joint venture partner Howard Smith in 2001. There have been suggestions by a major user Queensland Sugar that alternative providers could be entertained however this has not come to pass. Adsteam group's Queensland Tug & Salvage Pty Ltd have provided services in Brisbane, Bundaberg, Gladstone and Bowen. Apart from the buy-out of the Howard Smith 50% share by Adsteam, there has been no operator change in these ports in recent years. In Gladstone however there was a strong tendering process in 2000 which was won by QT&S against several contenders.

In South Australia and the Northern Territory there have been no major changes in towage operators or their ownership in recent years.

The overall picture of ownership in the Australian towage industry has been one of much coming and going of operators and of ownership but limited head to head competition. The most recent example of serious two party competition was in the Port of Newcastle between 1994 and 1999. Changes in operators over time has sometimes been as a result of transparent competitive processes and at other times simply the result of commercial decision making.

5. COMPETITION - A NEW PLAYER

AIMPE has in recent times become aware of a major development in Australian harbour towage. A new operator – Australian Maritime Services Pty Ltd (A C N 099 760 380) has decided to set up operations in the Port of Melbourne initially and subsequently in Sydney, Brisbane and Fremantle.

AMS is using a business plan that is quite different from that which was used by BHP in Newcastle in 1994. BHP bought 3 large Voith Schneider tugs from the Middle East and then purchased another Voith Schneider from Singapore which it had to re-fit. The total capital cost was in the order of \$35 million which was to be serviced by the throughput of just one port. In addition to the capital cost, the operating costs of the Voith Schneider vessels were high due to their extra fuel consumption when compared to the pre-existing z-pellers in Newcastle.

(Adsteam's 2000/2001 new-building program has seen it take delivery of some 6 new tugs at a total cost of around \$45 million. But this expense has been spread over six ports.)

AMS however are in the process of chartering their tugs from an overseas source with an option to buy. These 'second-hand' tugs are z-pellers that will be more fuel-efficient than the BHP Voith Schneider models yet highly maneuverable and powerful enough to perform most functions normally required in harbour operations.

The impending start-up of this new operation in several of the major metropolitan ports gives the lie to the notion that there are insuperable barriers to entry in the Australian towage industry. AMS has clearly sourced a supply of vessels from overseas on a cost effective basis (i.e. without having to purchase immediately) and must be confident of securing at least a part of the market in each of the ports it has targeted.

AIMPE infers from the proposed rollout of the AMS operations that its intended customers are the main container/liner trades that visit a series of major ports during each voyage. AMS would appear intent on providing a package service to these major port customers. This may be analogous to the entry of Virgin Airlines into the aviation industry in 2001 – concentrating on servicing the major metropolitan ports in competition with the major national (and international) operator.

If greater competition is the pre-determined philosophical objective of this inquiry then it is submitted that the Commission should ascertain for itself the veracity of the above information. If correct it supports AIMPE's view that the Commission need not and should not intervene in the economic regulation of harbour towage. Consistent with s.8(1)(b) the Commission should then reduce the regulation of the towage industry by recommending that price surveillance cease at the expiration of the current extension of the declaration.

6. GEOGRAPHY AND CENTRALIZATION

Australia's vast coastline dictates the need for a multiplicity of ports. For a population of around 20 million people to maintain and operate over 40 international trading ports is a huge infrastructural effort. On one view of economic modeling it may reflect a major misallocation of infrastructure resources. Countries with much larger economies and far bigger population bases trade very successfully with a fraction of the number of ports.

A more efficient use of port facilities and of port related services (including towage) could be achieved by the rationalization of the number of ports around the Australian coast (refer s.8 (1)(c) Productivity Commission Act 1998).

But the huge distances around the world's largest island (30,000 kilometres of coastline) mean that it is not feasible to rely on centralizing all trade through a handful of ports. The land transport costs of transporting goods to and from a limited number of centralized ports would far exceed the savings in port costs. Furthermore, closure of any ports may have significant adverse impacts for regional economies.

The Productivity Commission is charged with promoting regional development. Rationalisation of the number of ports around Australia could lead to reduced towage costs but at the expense of regional employment and regional development. This would be contrary to s.8 (1)(f) and s.8(1)(g) of the Productivity Commission Act 1998.

7. TRADING HOURS

Shipping globally is a 24 hour /365 day industry with ships traversing the world's oceans in every direction at every hour of the day and night, every day of the year. The need for towage to be available 24 hours per day to service shipping arrivals and departures means that tugs and tug crews have to be available 24 hours per day.

In some ports around the world lack of throughput or inadequate resources means that ports are not open for business 24 hours per day. This provides a lower cost structure for the providers of towage and other marine services because they do not need to employ labour for all hours of the day and night.

If all Australian ports were to have limited trading hours, then towage costs could be reduced to the extent that a lesser labour component would be required. Of course the capital component would not be reduced, as there would still be the same need for a given number of tugs.

AIMPE suspects however that Australian port users would be strongly opposed to restrictions on the hours of operation of trading ports as this would add to the voyage duration of some vessels and perhaps impact on the frequency of their services. In a period of increasing globalisation, limited hours would also reflect poorly on Australia in the eyes of our trading partners. AIMPE would oppose the restriction of hours of operation of ports.

N.B. Some dangerous berthing operations in certain Australian ports are only permitted in daylight hours on safety grounds. AIMPE's submission does not include any reduction in safety regulation of tug operations.

8. MICROECONOMIC REFORM

Direct employment in harbour towage in Australia is limited to less than 1000 people. This is significantly lower than the employment levels of the 1980's. The reduction in employment is due to 3 rounds of reductions in the size of each tug crew – first from 6-8 in some ports down to a standard of 5 persons. Then in the Towage Industry Reform Implementation Committee (TIRIC) process in 1990-91 crew size went down to a standard of 4 persons. Most recently the vast majority of tugs have had their standard crew size reduced to 3 persons.

Moving to crews of 3 necessitated the installation of visible and audible deck alarms, provision of new 'man-overboard' retrieval systems and utilization of two way communications by all personnel. Tugs were also required to have adequate towing winches to facilitate the reduction.

For tug engineers in particular there has been a significant requirement to adapt to the changed crewing arrangements. Tug engineers no longer have a dedicated engineroom assistant as applied in crews of 5, 6, 7 & 8 persons.

Furthermore in tugs with three person crews the tug engineer is now required to assist on deck with the tying up and letting go of the tug and with the berthing and unberthing of the ships. This has necessitated additional training of tug engineers in deck safety operations

In addition, in many ports the numbers of crews have also been reduced. This has led to a reduction in the ratio of tug crews to tugs. By way of generalization, in the busier ports the crew to tug ratio is higher than in the less busy ports. In the least busy ports the ratios can only be sustained by the agreement of the employees to accept unpredictable leave patterns. This is something of an impost on personnel in a sector which already exhibits irregular, unsociable hours and days of work, however it has been accepted to ensure the delivery of a viable towage service in low volume ports.

A separate development has been the modification of port practices to provide more flexibility of service to the end users. This has required much greater availability of crews via pagers and/or mobile phones outside of ordinary hours. Unfortunately some other participants in the transport chain are not as diligent as they could be. This leads to multiple changes of orders and exacerbates the disruptive patterns of work inherent in 24-hour towage services.

One way of minimizing the adverse effects of these patterns of work has been the introduction of 12 hour shift systems (in Melbourne, Brisbane and Gladstone) and quasi-shift systems elsewhere (e.g. Fremantle, Sydney and Newcastle). These developments have been driven by occupational health and safety concerns about the effects of fatigue on work performance.

Additionally, Howard Smiths in Melbourne and Brisbane conducted customer surveys which told them that immediate availability was vital on a 24 hour basis for their (i.e. the customers') operations. The only practical way for this to be guaranteed is for crews to be on board 24 hours per day. This is analogous to the fire brigades, ambulance services, power stations and other 24-hour industries.

The Commission should recognize the major changes that have been undertaken in the towage industry including the changes through negotiation between the companies and the unions. This has led to higher labour productivity with tugs previously operated by crews of 5 or more now operated with crews of 3 persons (refer s. 8(1)(a) Productivity Commission Act 1998). Also the Commission should recognize the social and economic hardships that have already been borne by the workforce in the towage industry (refer s.8 (1)(d) Productivity Commission Act 1998).

9. RELIABILITY

Harbour towage reliability is extremely high in Australian ports generally and in the declared ports in particular.

The most recent edition of Waterline published by the BTRE stated that the proportion of ship movements where towage services were available to the ship within one hour of the confirmed ship arrival/departure time was 100% for the December quarter 2001, the same as in the September quarter 2001. Performance has been at similar levels since the first data (covering the March quarter 1997) were published in Waterline. This measurement is based on sampling of movements in the five major metropolitan ports (Brisbane, Sydney, Melbourne, Adelaide and Fremantle).

Reliability of harbour towage is a product of many factors. These include the mechanical soundness of the tugs, the organization of personnel, communication systems and the provision of contingency plans in the event of any problem with any

of these requirements. These problems can be as diverse as mechanical breakdown, illness or injury of personnel or a clash of jobs. For each type of problem, the operator must have solutions available at short notice.

To achieve a 100% reliability assessment over five consecutive years in any part of the transport chain is indeed remarkable and stands as a tribute to workers in the tug industry.

It is tempting to hark back to the familiar refrain "if it ain't broke, don't fix it".

From the tenor of the submissions to the ACCC of various parties price is now seen as an over-riding factor and Adsteam should not be allowed to increase its prices. The risk with this approach is that the desire to hold prices down may lead to deterioration in the quality of the service. There is a cost to delivering a 100% reliable service. But in the words of another song "you don't know what you've got 'til its gone".

The Commission should take care that any recommended change to economic regulation of harbour towage does not lead to a reduction in the outstanding reliability currently enjoyed by towage users. Paradoxically this could even lead to a reduced competitiveness of Australia's export industries.

10. PORT PROTECTION

Many users resent the fees that they have to pay to towage operators feeling that they operate good ships, have good safety records and already get slugged for various State and Federal Government charges. Why should they also have to pay so much for towage?

One answer that should be made absolutely clear is because the protection of the port, its infrastructure and the other users of the port demand it.

The collision of the M.V. *Amarantos* at Wallaroo on 10 April 2000 is a classic example of what can happen;

"At a time logged by the ship's crew as 0720, *Amarantos* made contact with the Wallaroo jetty causing substantial damage to the jetty deck timbers, piles, and the grain loader and its supporting superstructure mounted on the jetty. The vessel struck the jetty almost at right angles and continued on into the jetty for a distance of 3.5 - 4 m." Australian Transport Safety Bureau, Marine Safety Investigation Report 157.

Towage in Wallaroo was provided by the *Kalanbi* (11.5 tonnes bollard pull) and the *Ungarra* (13 Tonnes from Port Pirie). The ATSB concluded among other things that the tugs lacked both the maneuverability and power to either arrest the ship's forward momentum and/or swing the ship off the jetty in time to avert the incident.

Subsequently Port Lincoln Tugs has acquired a larger tug for Wallaroo.

An incident in the Port of Newcastle on 31 May 1995 involving the grounding of the *River Torrens* in the main entrance channel also demonstrated how critical are the processes of berthing large ships. On that occasion two large tugs, *Walana* and *Iron Cove* were able to free the grounded vessel within 30 minutes of the incident. The *River Torrens* sustained severe damage to the rudder and propeller and damage to

the crankshaft. The consequences would have been far worse for the Port if it had not been possible to free the ship as quickly as did occur. Blockage of the main channel would have led to the closing of the port to shipping and a major disruption to trade through the port.

These incidents are reminders of the need for towage services and the potential consequences of the lack of adequate towage capacity in a major port. Experience has exposed those locations where inadequate towage capacity has been available to the (inevitable) adverse consequences. Recommendations from the safety regulator have underpinned the upgrading of capacity where that has been necessary. Economic regulatory measures must not be permitted to undermine the requirements of the safety regulators.

11. SALVAGE

Harbour towage in Australia has over the last few decades provided the mainstay of marine salvage capacity throughout the waters of Australasia. United Towage & Salvage Pty Ltd was a joint venture between Howard Smiths and Adsteam Marine until Adsteam's takeover of Smiths.

UT&S continues to maintain salvage class tugs at strategic points around the Australian coast in order to have the capacity to respond to any marine salvage requirement. These locations include Brisbane, Sydney, Melbourne and Fremantle.

When the *Bunga Teratai Satu* grounded on the Great Barrier Reef south of Cairns on 2 November 2000, it was UT&S that was called out and eventually succeeded in removing the vessel from the Reef.

More recently in January 2002 the *Jody F Millenium* was grounded off Gisborne New Zealand during a major storm. The local tugs were unable to pull the ship off the bank. UT&S sent a tug from Melbourne to do the job.

Local port authorities often lack the foresight to consider the need for salvage capacity when assessing the towage requirements for a port. They take a limited, indeed blinkered, view that ordinary day to day harbour ship-handling operations is all that is required. Needless to say, if all ports took the same approach and ignored the broader need for a salvage capacity for a maritime dependent nation then the consequences could be dire. This is what has happened in New Zealand – they now have to call on Australian salvage capacity to get them out of trouble.

Salvage is an unpredictable highly sporadic service. Sometimes there is no salvage work for months or years anywhere in Australian waters and then there can be a spate of jobs. To be able to afford the investment in salvage capacity, UT&S utilizes the salvage tugs to carry out harbour towage operations. Otherwise the salvage tugs would remain idle for long periods of time.

The building, equipping and maintaining of salvage tugs is an additional capital cost for UT&S (Adsteam). Without this privately provided capacity Australia would probably have to consider the provision of a publicly provided emergency and salvage system (as operates for instance in the United Kingdom). Because emergencies are unpredictable, this requires fully manned vessels on standby in strategic locations around the coast. As shipping is the beneficiary of this service,

Government would probably have to levy shipping one way or another to pay for this service.

The salvage capability of the towage industry helps protect the marine environment of Australia's vast Exclusive Economic Zone and hence guarantee the ecological sustainability of maritime transport in Australian waters. Any recommendations of the Commission which impact on the current salvage capacity will need to address the question of ecologically sustainable development of the maritime industry (refer s.8(1)(l) Productivity Commission Act 1998).

12. CONCLUSIONS

The current form of economic regulation of the towage industry relates to a limited number of ports and has not achieved any major positive impacts. By contrast the micro-economic reform of the industry has been dramatic but little understood by outside observers.

A new operator, Australian Maritime Services, is about to set up operations in competition with Adsteam providing direct competition in major metropolitan ports. Although previous recent competition has not succeeded, the AMS model is arguably more likely to prove sustainable. This situation may provide a real choice for towage users in the major ports. The Commission should not make long-term recommendations before having a chance to evaluate the effects of this new development.

Notwithstanding the new competitor, Australia's vast coastline means that we have far more ports than similar sized economies. The corollary of low shipping levels in our ports means that we have low levels of tug utilization when compared to many overseas economies. This means costs per job will be higher than such overseas economies. However local ports are vital to Australia's many regional economies. Inability to ship out of a local port could damage many regional economies.

Alternative methods of reducing costs e.g. by operating for limited times each day are not acceptable to the shipping industry which operates around the clock.

Microeconomic reform of the towage industry has been significant and on-going from the early 1990s through to 2001, although not understood or acknowledged by many observers.

Throughout this period of change the reliability of the towage industry has been exemplary. In addition to which the infrastructure of Australia's ports has been protected by the harbour tugs. And the harbour towage sector has fulfilled a critical role in marine salvage in Australia's Exclusive Economic Zone.

Heavy-handed economic regulation of the harbour towage industry could pose a threat to these outcomes and should not be recommended. Instead economic regulation should be lighter; the new phase of competition should be permitted to demonstrate its effectiveness in meeting the needs of the users.

In no way should safety regulation be compromised by the impact of economic regulation.