



## **Port of Brisbane Corporation**

Productivity Commission  
Discussion Paper

### **Economic Regulation of Harbour Towage & Related Services**

**Public hearing**  
Wednesday 10<sup>th</sup> July 2002  
Brisbane

Presented by  
Greg Smith

Port of Brisbane Corporation

## **Table of Contents**

|   |    |
|---|----|
| 1. Introduction .....                                     | 3  |
| 2. Historic Port Development .....                        | 4  |
| 3. The Changing Marine Environment .....                  | 5  |
| 4. Effects of Price Surveillance on Towage Costs.....     | 7  |
| 5. Dynamics of Control on Towage Pricing .....            | 8  |
| 6. Strategic Equipment in Holistic Towage Provision ..... | 9  |
| 7. Conclusion.....  | 10 |

## 1. Introduction

Due to unsupported price increases in the towage industry, the Productivity Commission has been requested by the Federal Government to inquire into the harbour towage and related service industry in Australia. The Port of Brisbane Corporation sees such an inquiry as an opportunity to probe for any efficiency or productivity gains that structural reforms have delivered to the industry. Following on from this point, if there have been any gains, then why are differing advantages being experienced in various Australian ports? Are there basic impediments to efficiency inherent in the pricing structure of the service or are some of the regulatory measures taken by some port authorities responsible for returning efficiency (measured in dollars) through service requirements and demands (KPI's).

Faced with the same single service provider in most ports, what is stopping the development of a competitive environment considering the incumbent seems to be making reasonable profits covering the cost of the operation, return on capital plus dividends to shareholders? Are there measures that can be adopted to increase competition and is price surveillance a warranted form of review that has protected industry from monopolistic pricing events?

In consideration of the possible effects of a single towage service provider, the Port of Brisbane Corporation has internally debated the role of the Port Corporation in controlling service pricing. The results of the debate are far from conclusive and in fact, the question “does the current cost of the towage service dictate any reaction at all” must be considered in comparison to total port charges. It would be fair to say that our organisation, whilst attempting to increase demand for our port through competitive pricing, is limited in what influence can be placed on third party service providers without any legislative influence.

In attempting to assist the Productivity Commission in this inquiry, we herewith detail some of the concepts of our discussions in the hope that it may provide some explanation and background evidence in consideration of future

recommendations (albeit with a distinct Brisbane focus). Should the Commission require any further advice, we are happy to make ourselves available.

## **2. Historic port development**

We feel that the position paper released by the Productivity Commission adequately explains the corporatisation of most Australian ports. The principal reasons behind the decision are well documented in the position paper. Furthermore, in the case of Queensland, the fundamental design of corporatisation was to improve Queensland's overall economic performance by increasing the effectiveness and efficiency of the Government owned businesses and make them more competitive and like-minded with private industry.

Prior to Corporatisation, Queensland ports were structured as a statutory regulator of port services that mainly controlled safety and protected state assets. As Government departments, the organisations were more administratively focused in monitoring trade. Corporatisation separated port organisations into commercially focused, independent structures charged with developing and enhancing port facilities and services. As such, the original role of the port administration has been removed and replaced with responsibility for increasing the economic performance of the organisation and improving the return on shareholder funds.

Although there are some challenges between the principles of full commercialism and the needs of Government Owned Corporations (GOC) to satisfy their social responsibility, the process has been successful. Corporatisation has enhanced growth by developing port assets to the benefit of both the Government and private sectors. In Queensland, it should be noted that port corporatisation has divorced the regulatory and statutory responsibility for safety from the commercial responsibility of port operation. Safety rests with the Queensland Department of Transport while the GOC Port Administration is responsible for commercial performance and

development. Thus, there is a clear delineation between statutory regulation and commercial development that may not be apparent in the port operations of other states.

In exercising this charter, Queensland ports have adopted a landlord model that maximises the advantages of their physical assets. In most circumstances, this has tended to be based on developing land banks and existing port structures where rental returns give immediate economic benefits. In the past, it would be true to say that ports have been generally slow to capitalise on service enhancement as a viable economic performance driver. This in turn has led to the supply of port related services through third party service organisations in most ports.

Accordingly, Port Corporations are therefore limited in the express controls that they can impose on these service organisations. Provided the service is within the expectations of the customer, it is a challenge to see what improvement the Port Administrator can actually have on the service provider. In fact, the Port Corporation can actually have a detrimental cost impact through charging commercial rates for land rentals. As land users, rents charged for waterfront land add to the operating costs of the towage operator which is then recovered through the service provider's tariff charges. This is the case in the Port of Brisbane where the ability of the Port Administrator to influence the pricing of the towage service is convoluted, as the service provider is a customer of the port. To this extent, it would appear that the shipping market itself should have the greatest ability to exercise some degree of price influence as the end user of the service.

### **3. The Changing Marine Environment**

The advent of globalisation has altered the traditional historic evolution of ports. Economies of scale have forced owners to progress to larger and larger vessels. This has changed the dynamics of port distribution in that increasing vessel dimensions have precluded some medium sized ports due

to their physical limitations. Cargo distribution and population dynamics have also influenced the growth in Australia's ports.

The advent of the hub and spoke principle in vessel routing has certainly increased the prosperity of a few large Australian ports with the cascading effect of displaced tonnage entering into our trading routes. It would be a reasonable assessment to say that the age profile of these vessels sees the incorporation of more modern technological benefits that reduce the risk associated with close manoeuvring operations. Although the vessels have increased in size, the ability of the on-board systems to assist in close hauled manoeuvring has seen a reduction in the assistance required by tugs.

Although we do not think that safety has been compromised, there has been a trend in ports to minimise tug involvement when berthing and sailing ships. This has been encouraged by ports in order to increase the commercial appeal of their port.

However, this must also be viewed with the reality that due to the dynamics of port development in Australia (based on population distribution), it is doubtful that competing ports could take advantage of this phenomenon as a sole reason to entice shipping companies from existing port rotations. As such, the towing industry would appear to have a stable platform for operation.

Both the Productivity Commission discussion paper and the ACCC report have saturated the question of whether the market is large enough for more than one operator. The question seems more of the existence of a natural monopoly in the towing industry in Australian ports. The ability of competitors to enter the market place hinges on the degree of the sunk costs to establish the operation with two streams of thought. One is that there is a high sunk cost precluding new players due to the danger in failing to win sufficient market share to recover start up costs. The second is that due to a reasonable second hand market, a prudent operator could contain sunk costs and redistribute or redeliver the assets in the event of failure. The second premise

is closely affiliated with the theory of ship chartering and is used by new players to cap start up costs when entering a new market.

Whether two or more players can economically survive is well investigated and will not be discussed in this paper. Furthermore, the Port of Brisbane Corporation cannot see how we can influence the market place without licensing authority given our own demands for commercial success. This is of course unless the port itself feels that a competitive venture in towing is warranted and would provide commercial returns to its shareholders, thus stimulating competition in the market. As an option the Port of Brisbane Corporation is currently investigating this, although we take note that only a few Port Authorities in Australia have taken this route.

#### **4. Effects of Price Surveillance on Towing Costs**

We think that it is fair to say that price surveillance has been a practical deterrent to monopolistic pricing over the years leading up to the takeover of Howard Smith's towing interests by Adsteam Marine in Australian ports. Although there have been recorded price increases, they have been limited to specific situations and have followed acceptance by the ACCC. Only when Adsteam Marine became a sole operator has the industry witnessed broader price increases which have not been approved by the ACCC.

We see this as a dangerous precedent and one that is potentially in tune with monopolistic pricing. Considering the publicised finding of the ACCC that no price increases were justified, we feel that the action of Adsteam is contrary to any organisation that is concerned about a potential loss of market due to price increases. Either the operator is totally comfortable with the potential entry of market competition, knowing that the market can bear another entrant or, is totally confident that such competition is now and in the future, non-existent.

To this extent, it seems a reasonable assumption that some form of pricing control is required in order to at least act as a deterrent. Surveillance in its

past form has obviously not decreased charges in the industry, however we do believe that it has maintained price stability. In fact, it could be argued that the past methodology never could provide the vehicle for price decreases. Instead, this pressure surely would have been better applied by the shipping industry being the direct customer base of the service provider. Due to the acknowledged problems associated with this suggestion, we feel that some other mechanism must be developed.

## **5. Dynamics of Control in Towing Pricing**

The Commission has suggested through preliminary recommendation 2 that the ability of Port Administrations to exercise discretion in towing licensing may limit price increases and even force a reduction in service charges. The obvious results from port sponsored towing tenders certainly give credence to this argument. Gladstone, Bunbury and Fremantle are all good examples. However, there are some questions as to if this is the most efficient and productive methodology.

Surely the most influential party able to influence pricing would be the end user. While the Port is expected to control the tender for third party service provision, some states will need changes to legislation plus there will be administration expenses that must be passed on through increased port charges. In plain language, we are expecting prices to be lowered or at least be maintained by such intervention but surely the most efficient action with the greatest scope to maximise any reduction sits with the shipping industry itself.

The industry has good representation in the form of Shipping Australia Ltd (SAL) which has the means to act on behalf of the shipping industry to negotiate contracts for the provision of towing services in Australian ports. In stating this, we do acknowledge comments made by SAL. Fundamentally though, the question that still needs to be addressed is whether this form of control will in fact be more beneficial than the constant threat of entry.



From the material that has been assessed by the ACCC, Productivity Commission and various industry reports, it would appear that the market is only large enough in at least two, may be three East Coast capital city ports to realise this threat. Melbourne has already seen a new entrant competing against Adsteam, and Brisbane and Sydney are rumoured to be under consideration by new towing service providers. In these major ports, it would seem that an exclusive licence might inhibit future benefits. This could have the effect of constraining any future technological benefits to the term of the licence. However, it is acknowledged that in place of no price surveillance, the ability of the Port Administration to issue exclusive licences at their discretion adds in the effective control of unwarranted price increases.

## **6. Strategic Equipment in Holistic Towing Provision**

There is obviously a large price disadvantage in the capital cost of equipment that can service the blue water salvage industry as compared to harbour tugs. Most port towing requirements occur in the protection of sheltered waterways and the need for salvage capability is definitely not a requirement when smaller, cheaper tugs can offer the same towing requirements. The basic question then becomes, should the port industry have to carry the burden of the greater salvage requirement.

This Port Administration (and for that matter, any port administration), would never suggest that the pristine environment and unique nature of the Australian coastal environment should ever be compromised. However, it may well be time to consider a means of affording dedicated salvage capability in areas where the threat is most prevalent. Should such capacity be based on the return from salvage acts rather than subsidised through harbour tariffs? This is a question that needs government consideration and hopefully, a more equitable distribution of costs back to the parties requiring the service. Furthermore, a dedicated service would not impinge on the physical port towing fleet and place the salvage resource at the closest point to potential

problems, thus mitigating the propensity for large-scale environmental degradation.

## **7. Conclusion**

Although the standing of the legislation in Queensland (Transport Infrastructure (Ports) Regulation 1994) governing the right of ports to license towage operators is under review, Brisbane does not have the power to license. It is also under debate within the Corporation that changing the legislation to allow licensing will afford the maximum price pressure in light of other price containment paradigms. Rather, it could be argued that the shipping industry should be pressing for the ability to negotiate mid-term contracts for the provision of harbour towage services. Furthermore and in order to reduce the capital outlay for equipment, it may be prudent for the government to consider the most appropriate means of offering salvage capability.

The Corporation hopes that the above may increase the lateral scope of this inquiry to consider a solution to the question of pricing and service provision in the harbour towage industry. We do acknowledge however, the distinct Queensland tone attached to our paper and realise that other Australian Port Authorities may not share these concepts.