



4 July 2002

Ms Lisa Gropp
Assistant Commissioner
Productivity Commission
Harbour Tower Inquiry
LB2, Collins Street
East Melbourne Vic 8003

Dear Ms. Gropp

**The Productivity Commission's Position Paper regarding the Economic Regulation of
Harbour Towing and Related Services**

Shipping Australia Ltd (SAL) congratulates the Commission for the production of a very comprehensive and thoughtful position paper which, with some exceptions which are commented upon below, is in line with many of the arguments and recommendations of the submissions previously made by SAL.

Before commenting on a number of the preliminary recommendations and findings, we understand that the Commission is seeking further information on recent movements in towing prices for the bulk shipping industry and that information will be provided to the Commission.

Preliminary Recommendation 1

This recommendation relates to encouraging a better provision of required levels of service at minimum cost and the harmonisation of regulations between relevant jurisdictions. SAL strongly supports this recommendation.

Preliminary Recommendation 2

This preliminary recommendation urges the relevant jurisdiction to grant port authority's discretion to licensed towing operators on an exclusive or non-exclusive basis if that discretion is not currently available. It goes on to say that when exercising such discretion, port authorities should demonstrate the net benefits of the proposed licensing arrangements, formally consult with towing users in a transparent manner prior to changing existing arrangements and the conditions that attach to any licences and implement arms-length, transparent competitive tendering processes.

SAL is strongly supportive of this recommendation but recommends that towing users or representatives of major users where there are a large number of users in a particular port, should be actually part of the tendering process and formally incorporated into it. Not only will such a mechanism achieve a more desirable outcome but will ensure that the port authority fully understands the requirements of those users for ancillary services as well such as fire-fighting, salvage or emergency response and mooring/un-mooring services. We would urge the Commission to strengthen this recommendation in that manner. We agree that it is very important that the tendering process is as transparent as possible and adequately reflects the views of all interested parties.

Preliminary Recommendation 3

This recommendation relates to the declaration of harbour towage services under the Prices Surveillance Act, 1983 in recommending that declaration of specific main ports should not be renewed when the current declaration expires on 19 September 2002.

SAL agrees with this preliminary recommendation but is concerned that if a port has not exercised its discretion to issue an exclusive or non-exclusive licence for whatever reason, which could well be practical, then there is, in our view, the potential for a natural monopoly provider of towage services in that port to unduly exercise its market power. We would urge the Commission to recommend that further potential remedies under the Trade Practices Act be examined. This situation should be brought to the attention of the current committee reviewing the relevant provisions of the Trade Practices Act in order to highlight the potential problem without necessarily making any firm recommendations as to potential solutions at this point in time.

Preliminary Recommendation 4

Limited monitoring of prices by the ACCC for a three year period is recommended as a transitional measure and that price data should be published annually. Whilst generally supportive of this recommendation, SAL would urge that such monitoring be on the same basis as that which applies to the major stevedores in Australia i.e. monitoring of costs, prices and profits in order to give interested parties the most complete picture possible of what is occurring within the transitional period. This is particularly important bearing in mind the comments above regarding recommendation 3.

We strongly urge the Commission to extend monitoring to all major ports in Australia, both declared and non-declared at the present time. SAL would also recommend that there be on-going monitoring of the selected ports if no competitive tendering is introduced in those ports and that it not be limited to a 3-year period. There have been recommendations previously to extend the number of declared ports and SAL could provide the Commission with a list of ports which should be subject to monitoring over and above the declared ports which, with the exception of Newcastle, have a strong container or liner shipping usage compared to bulk.

Preliminary Findings

We would like to comment on the preliminary findings. SAL fully agrees with preliminary finding 6.1 that at most Australian ports they are only likely to be able to sustain one operator but that these natural monopoly characteristics do not extend to one operator providing towage at all ports in Australia or even at all of the major container ports.

Preliminary finding 6.2 suggests that potential barriers to entry into the towage market, while not insignificant, are not large. SAL would emphasise the point that in the view of members, the contestability of the harbour towage market in Australia is weak. There are significant costs in transporting tugs to Australia to compete with an incumbent operator and for resale or redelivery such tugs would either need to be transported back to ports distant from Australia or would be discounted if sold in Australian ports if the buyers require those tugs again in ports distant from Australia. In addition, contestability is weakened where the incumbent does have a degree of market power by having such a large share of the Australian towage market and being a major towage operator internationally, as well as with the existence of loyalty rebates, could well apply significant pressure on a new entrant by lowering prices significantly e.g. below marginal cost and threatening existing users with withdrawal of loyalty rebates.

We would request that the Commission examines the degree of contestability further when preparing the final report.

We agree with preliminary finding 6.3 that the overall demand for towage at a particular port is not very responsive to price changes in the short to medium term. However it should be pointed out that existing margins for many ship operators and their agents are also very low. We will provide the Commission with a graph produced by Drewry Shipping Consultants which adds considerable weight to that observation. Even a \$1/TEU increase as a result of towage cost increases can have a significant impact. Preliminary finding 6.4 states that at ports where there are a large number of users, the cost and complexity of organising them to negotiate as a group will limit their countervailing power. SAL supports those findings and notes that the Commission requests comments or information from participants relating to the feasibility of users at multi-user ports contracting directly with harbour towage providers. It is considered that many users in this connection will be wary of entering into medium to long-term contracts with towage providers if there was the likelihood of lower prices over that time period. Presumably competitive tendering by a port authority that results in an exclusive or non-exclusive licence would make such contracts redundant. Effectively given the history of towage operation in Australia, it is considered that many users would be wary of entering into such contracts.

Preliminary finding 6.5 states that available evidence indicates that towage prices in some Australian ports have been above efficient levels but the margin has not been large. SAL would question that conclusion in relation to the potential pricing effects of an exclusive licence at a particular port that, from experience, indicates it could be up to 30% lower than prices that were charged prior to the recent increases. It is appreciated that such deductions could well relate to greater cost-effectiveness in terms of the provision of towage services, nevertheless it indicates to us that the margin is not insignificant.

Preliminary finding 6.6 suggests that non-regulatory entry barriers to the provision of mooring services are negligible and SAL would agree with that conclusion. Table 2.16 on page 34 of the report examines mooring charges per TEU exchanged at major container ports. SAL suggests that this is not an accurate way of measuring relativity of mooring charges which should be on an average-sized per ship visit irrespective of the TEUs exchanged. The competitiveness of an individual port in this area is measured on that basis by the users of the ports. It is suggested that mooring charges per TEU distorts such comparison.

SAL supports the preliminary findings by the Commission regarding the assessment of price notification of harbour towage services and also the general thrust of the findings under the assessment of alternative arrangements. We do question whether there is potential, for example, for the unconscionable conduct provisions of the Trade Practices Act to be employed as a back-up mechanism to reduce the potential for abuse of any market power, particularly in those cases where, for one reason or another, a port does not enter into a competitive tendering situation and monitoring indicates excessive profits are being earned.

As mentioned above, SAL would urge that the Commission discuss this matter with the Committee currently reviewing the Trade Practices Act. SAL is particularly supportive of preliminary finding 8.7 that exclusive licences for the provision of towage services have the potential to generate greater benefits for towage users than non-exclusive licences.

Other Comments

We draw the Commission's attention to a number of specific points raised in the Position Paper.

On page xxiii, reference is made in Table 4 to "Towage charges for TEU exchanged at major Australian container ports at current prices" but we question whether this is really a valid measurement of cost effectiveness compared to average towage costs per port visit by vessels over typical size ranges over a reasonable time period.

In the penultimate paragraph on page xxvi, reference is made to volume rebates offered by Adsteam overseas ports to shipping lines but no mention is made of the fact that such rebates are not offered, or at least available, to all shipping lines.

In the penultimate paragraph on page 11 it is correct to point out that towage costs are ultimately borne. Ship operators and their agents are not interested in simply passing on such costs even when they can in a timely manner, and are keen to reduce such a cost burden, particularly where they are seen not to be internationally competitive.

We note that Adsteam Marine has also made a submission, dated 24 June 2002, regarding what they perceive to be a threat to a national salvage and coastal protection capability if exclusive towage licences were introduced.

Despite the assertion made on that submission that ship operators, amongst others, are either dismissive or ignorant of such costs, there is a more fundamental objection to the central point. The issue of an emergency response including a fire-fighting capability would in our view, be one of those essential points to be covered in an exclusive licence contract including the need for adequate back-up in times of mechanical failure of the other tugs in the port and to provide the necessary flexibility to meet all types of possible operating conditions. This reinforces the points made strongly by our members that they must be part of the tendering process and very closely involved in the granting of the licence.

It is stated in the Adsteam submission that the capability of United Salvage is borne by the company with no cost to Government, port authorities or the shipping industry. This appears to conflict with the main proposition in that submission that exclusive towage licences, because of their port-specific focus, pose a serious threat to the on-going viability of Australia's existing national salvage and coastal protection capability. In particular, we would have thought that the capital costs of the tug would be recovered from harbour towage users even if the additional extra off-shore operating costs are recovered from the salvage reward.

In debating this issue it could be valuable to differentiate between the provision of salvage services and emergency responses; particularly given the need for on-going towage services within a particular port. It should also be noted that many parties are currently considering Australia's salvage capability at the present time and it would be useful for the Commission to be brought up-to-date with those deliberations.

The Australian salvage capabilities is compared to that in the United Kingdom but there is a considerably higher risk factor in that part of the world because of a much higher traffic level. It is also interesting to observe that a number of the incident reports in the Australian area of operations are breakdowns in harbours and harbour tugs were employed to render assistance. There are now 14 salvage capable tugs in Australia compared to 5 such tugs in the not too distant past but it does not appear that the level of vessels in distress has gone up significantly over the same period.

On page 9 of the Adsteam submission, there is a list of the key features of the services provided that an Arbitrator under Lloyds Open Form would take into account. This list ignores the key "Principles of salvage" which we will send to the Commission.

Finally, SAL appreciates the opportunity of commenting on the position paper and looks forward to the opportunity at the public hearings to elaborate upon these views and to respond to questions from the Commission.

Yours sincerely

Llew Russell
Chief Executive Officer