



PRODUCTIVITY COMMISSION INQUIRY INTO TASMANIAN FREIGHT ASSISTANCE ARRANGEMENTS

Supplementary Submission DEVELOPING A FRAMEWORK FOR ADJUSTING PARAMETERS

3 November 2006



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1. INTRODUCTION

In their joint submission to the Productivity Commission Inquiry into Tasmanian Freight Assistance Arrangements the Tasmanian Farmers and Graziers Association and Tasmanian Chamber of Commerce and Industry submitted that:

“...in consultation with industry, a framework should be developed for the annual adjustment of assistance parameters. This framework would identify and explain the methodology to be employed in adjusting the parameters, the supporting data requirements and how they might be collected and determine the annual date on which the adjustment would be implemented.”¹

The Productivity Commission at its Public Hearings in Launceston and Melbourne invited industry to provide an indication of how such a framework might be developed. To facilitate a response to this request the Major Manufacturers (Figure 1), which ship around half the freight eligible for TFES assistance, have commissioned this supplementary submission.

Figure 1 - Major Tasmanian Manufacturers

Norske Skog
Simplot Australia
Australian Paper
Cadbury Schweppes
McCain Foods (Aust) Pty Ltd
J Boag & Son
Cascade

This supplementary submission is a discussion document which explores the development of a framework for adjusting parameters. The intention is to provide a brief summary of the issues that such a framework needs to address, how it might be developed and thoughts on the supporting administrative arrangements. It is envisaged that the concepts contained herein will provide a basis for more detailed consultation with major shippers/industry, industry representative groups and Government with a view to developing and refining a robust framework prior to implementation.

¹ TFGA & TCCI, Productivity Commission Inquiry into Tasmanian Freight Assistance Arrangements, Submission; June 2006, p. 26

2. THE CONTEXT

Underpinning the content of this supplementary submission is the shared view of Major Manufacturers that **freight equalisation assistance should reflect the actual sea freight cost disadvantage experienced by eligible Bass Strait shippers.**

The Productivity Commission's concerns regarding potential for 'rorting' as a consequence of fraudulent claims is acknowledged. Similarly the potential for maximisation of assistance through claiming on a door-to-door basis and similar rule workarounds which are outside the spirit of the Tasmanian Freight Equalisation Scheme are also recognised. While the incidence, if any, of such behaviour is unknown it is apparent that any refining of parameters for calculating assistance should be considerate of such issues. **Major Manufacturers regard rorting in any form as unacceptable. Measures to ensure adherence to the spirit of TFES will be strongly supported.**

In this regard the benefits of moving to wharf-to-wharf invoicing as the basis of claiming TFES assistance are evident. It would enhance the scheme's robustness and also be consistent with the previously stated view that assistance should reflect the actual sea freight cost disadvantage experienced by shippers. **Major Manufacturers strongly support a process for claiming assistance that is based on wharf-to-wharf freight rates.**

It is recognised that the rigorous implementation of annual adjustments to the door-to-wharf parameter, as provided for in the Ministerial Directions, would deliver a progressive shift to wharf-to-wharf claiming. However, in support of addressing the concerns identified by the Productivity Commission a more expeditious and explicit timeframe for a transition would be supported.

Claiming assistance on a wharf-to-wharf basis also provides scope for ensuring improved compliance with the moral intent of TFES. This could be achieved through shippers signing declarations that relevant wharf-to-wharf freight rates are exclusively limited to the wharfage, stevedoring, container hire and blue water costs associated with shipping across Bass Strait.

Costs associated with other elements of the sea freight cost disadvantage, such as intermodal dislocation², additional dwell time, packaging/deconsolidation of freight, additional equipment and infrastructure requirements etc. are recognised through the Fixed Intermodal Cost component of assistance payments.

² Intermodal dislocation refers to the additional costs imposed on shippers through the inability to operate a typical line-haul operation over the full length of the door-to-door supply chain. In optimising the supply chain to minimise overall costs for a Bass Strait transit shippers will target maximise stowage rate efficiencies in containers. This often imposes reduced efficiencies on the landside components of the freight task in the form of the need to both transport additional 'dead weight' in the form of containers and the inability to maximise vehicle payloads on the door-to-wharf and wharf-to-door legs.

It is apparent that in developing the framework for parameter adjustment it is legitimate to consider the potential for refinements such as the move to wharf-to-wharf. However, any such refinements must be consistent with the base position that assistance should reflect the identified sea freight cost disadvantage.

It is observed that because of their position, shippers are often best placed to identify practical enhancements that will deliver outcomes within the spirit of the TFES. Accordingly **it is essential that shippers be an integral part of developing a framework for parameter adjustment and the Major Manufacturers look forward to being involved in such a process.**

3. ISSUES

The current Productivity Commission inquiry has brought to the surface a number of issues which reinforced the view of Major Tasmanian Manufacturers that there is a need for a framework that will ensure a robust process and structure surround to the annual adjustment of assistance parameters. These are:

- Need for a transparent mechanism for updating parameters (to facilitate an understanding of the potential impact of variations and enable appropriate provisions to be made in forward contracts for any envisaged adjustments in assistance levels);
- Desirability of a consistent approach to setting of parameter values (considerable variation has been evident in past parameter reviews³ and this has the potential to introduce uncertainty through fluctuations in assistance levels without commensurate changes in the disadvantage being incurred);
- Ensuring that parameter values reflect actual practice amongst Bass Strait shippers (the closer parameter values are able to be linked to the relevant Bass Strait freight task the less risk that assistance levels will be inconsistent with the disadvantage experienced; either higher or lower);
- Enabling industry to implement a program of consistent data collection that will facilitate regular parameter adjustments; (the current periodic ad hoc collection of data carries risks of inconsistencies in approach by both industry and Government with consequential impacts on parameter adjustments);
- Providing certainty that data collections will be treated with the utmost confidentiality. (Freight costs and related supply chain efficiencies represent a significant contribution to Bass Strait shippers maintaining their competitive position in the

³ Productivity Commission, Tasmanian Freight Subsidy Arrangements – Draft Report, Sept 2006, p. 16

market place. Companies engaged in interstate trade across Bass Strait are concerned that appropriate safeguards be implemented to minimise any risk of exposure of freight rates.)

- Desirability of annual incremental adjustments rather than periodic 'shock' adjustments (The TFES Review Authority recognised that "... By reviewing and updating these key parameters as necessary, the scheme can continue to track sea freight cost disadvantage as it changes over time and thereby maintain its relevance"⁴ and explicitly recommended that "Key parameters of the proposed scheme should be reviewed on an annual basis and updated as required.")
- Defining what constitutes a material change in parameter values to ensure potential adjustments are not deferred unnecessarily (Historically "... the small impact on overall program expenditure was the reason for not adjusting the parameters"⁵ However, deferring adjustment has compromised the effectiveness of some aspects of the assistance mechanism. In particular some measures that would have promoted behavioural changes in how claims are made have not been implemented and in addition to sending the wrong signals to the shipper community it has diminished the integrity of the scheme.)

This list of issues is not exhaustive. However, the issues serve to highlight the importance industry places on having a robust methodology for parameter adjustment. They also serve to indicate some of the process outputs that will be required in addition to revised parameter values plus some of the criteria against which the success of the process can be evaluated.

4. DEVELOPING THE FRAMEWORK

4.1 *Conceptual Parameters*

Industry supports the current approach to delivering freight assistance, i.e. an approach based on calculated disadvantage. Notionally this can be defined as:

- The difference between the actual sea freight incurred and the notional equivalent road freight rate a shipper would have incurred moving an equivalent amount of freight as part of an interstate line-haul operation; combined with

⁴ Tasmanian Freight Equalisation Scheme Review Authority, *Advisory Opinion*, 1998, p.30

⁵ Productivity Commission, *Tasmanian Freight Subsidy Arrangements – Draft Report*, Sept 2006, p. 17

- An allowance for intermodal costs that would not be captured in the freight rate differential including elements such as:
 - intermodal dislocation;⁶
 - additional dwell time costs;
 - additional packaging/deconsolidation costs; and
 - additional equipment, delivery and infrastructure costs etc.

In determining assistance payments the current TFES methodology makes use of 6 parameters. These are notionally used to establish the sea freight cost disadvantage incurred and subsequently determine the proportion of this disadvantage that is to be met with an assistance payment.

These parameters and notional data sources are tabulated below; Table 1

Table 1 - Assistance Parameters, Purpose and Data Sources

Parameter	Purpose	Data Source
1. Road Freight Equivalent	Defining disadvantage	Industry
2. Door-to-Wharf and W-D adjustment	Defining disadvantage	TFES database
3. Route Scaling Factors	Defining disadvantage	TFES database
4. Intermodal Cost Adjustment	Defining disadvantage	Industry
5. Median Wharf-to-Wharf Disadvantage	Determining % of disadvantage to be paid	TFES database
6. Heavy Weight Adjustment	Determining % of disadvantage to be paid	Industry

The basis for the conceptual parameters will be heavily influenced by the nature of data that is available and/or readily collected plus the ability to verify its accuracy.

Indicatively the Road Freight Equivalent might reasonably be based on a sampling of Bass Strait shippers who have relevant mainland interstate line-haul operations. The shippers would be able to provide indicative freight rates (with accompanying declarations) across a range of distances. From these, indicative marginal rates could be readily derived for different vehicle x product configurations and subsequently transformed into road freight equivalent measures

⁶ See footnote 2 for term explanation

that distinguish on the basis of how freight is transported across Bass Strait (containerised vs. vehicle), product type (if relevant) and even inform the calculation of the heavy weight adjustment.

The desire for simplification of the conceptual parameters must be balanced against the desire to accurately identify the sea freight cost disadvantage incurred by shippers. Similarly the complexity and cost of data collection must be balanced against the additional value contributed. It is essential that industry be involved in the defining of conceptual parameters and identifying the supporting data requirements as this will form the basis for assessing the practicalities of data collection and minimising any costs associated with future adjustment.

4.2 Methodology

Development of a framework for adjusting these assistance parameters will require 6 distinct groups of activities:

1. Examination of parameters to determine the basis on which appropriate values might be developed and/or derived. This would include identification of relevant data and its potential sources.

It is observed that since the current parameter values were set there have been significant changes in transport and supply chain operations. These changes are as diverse as shippers obtaining improved stowage rates for container movements through to the emergence of high-productivity vehicles on interstate line haul routes.

The examination of parameters should include an assessment of the appropriateness of the current two tier (non-refrigerated/refrigerated) approach to the Road Freight Equivalent parameter. Preliminary indications are that a differential Road Freight Equivalent based on the differences between containerised and vehicle (tautliner/pantechicon trucks) may be more significant.

2. Documenting the methodology to be employed in updating the parameters, including how collected data is to be used and the rationale behind its application. Documenting the methodology will ensure future parameter adjustments can be undertaken in a robust manner with consistency of approach and understanding.
3. Developing data collection mechanisms that will enable efficient gathering of relevant⁷ data on an annual basis. This is expected to entail:
 - a. Data collection templates (e.g. spreadsheets) for industry to complete. These would provide statements of practice regarding comparable

⁷ It is understood that in some instances the carrying forward of major claims into a subsequent financial year has resulted in significant year-on-year fluctuations in assistance payments that are unrelated to any movement in freight rates.

- mainland interstate line haul operations and characteristics of respective Bass Strait freight tasks (with attendant agreement to provide the data on a recurring basis); and
- b. Specifications of the information to be provided by claimants to Centrelink. This would be complemented by a specification for information to be provided by Centrelink in support of the annual adjustment of parameters;
4. Establish protocols for the treatment of commercial-in-confidence data to safeguard shippers' interests.
 5. Developing a timetable for the annual/cyclical application of the Parameter Review Mechanism. This would have regard for the time taken for data collection, validation and analysis. The timetable would be prepared with a view to ensuring an advisory opinion and attendant recommendations are provided to the Minister in a timely and consistent manner from year to year.
 6. Preparing proposed amendments to the Ministerial Directions governing the Scheme's operation to give effect to any data collection requirements, changes in parameter values etc.

The target in establishing a framework for adjusting parameters should be maximum accuracy while having regard for the practicalities and cost-effectiveness of data collection.

4.3 Administration

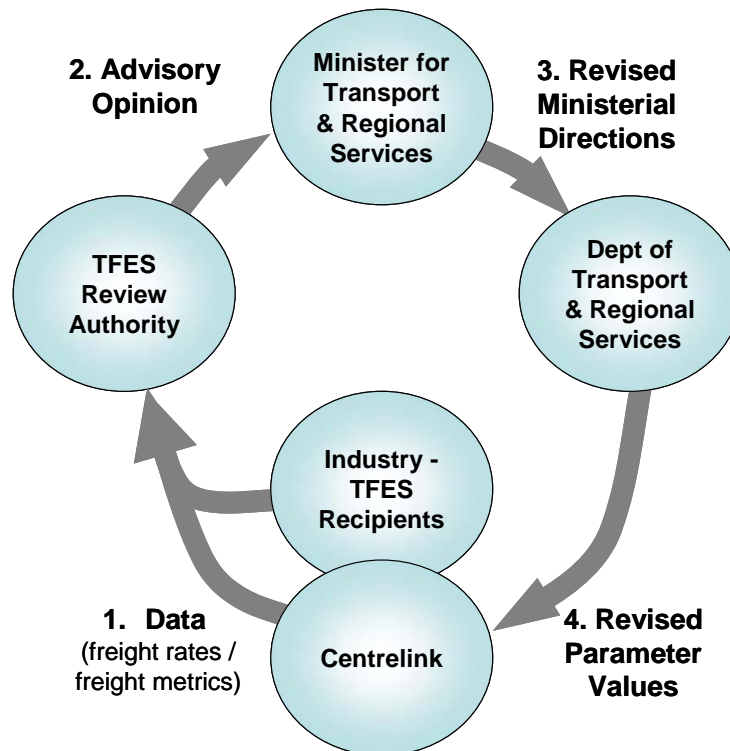
The development of framework for adjusting parameters should have as its objectives:

- Improving scheme accuracy; and
- Enhancing the ability of TFES to deliver on its stated objective of alleviating the comparative interstate freight cost disadvantage.

The Ministerial Directions governing the operation of the TFES provide for the establishment of a Review Authority which may be tasked to provide "...an advisory opinion on any matter or question relating to the administration of the Tasmanian Freight Equalisation Scheme or the interpretation of the Directions..."⁸ The relationship of the TFES Review Authority to other relevant parties is shown in Figure 2.

⁸ Directions by the Minister for Transport and Regional Services for the Operation of the Tasmanian Freight Equalisation Scheme, Section 25.19, April 2002 (updated August 2003) p.16

Figure 2 - TFES Review Authority, Administrative Relationships for undertaking parameter adjustment.



Industry regards the TFES Review Authority as being an appropriate body for both undertaking/oversighting the development of a parameter adjustment mechanism and effecting the annual adjustment process. A crucial determinant of success will be to ensure the engagement and participation of industry in this process. In this regard the Terms of Reference provided for this purpose will be a vital first step and industry is keen to work with Government to ensure that effective consultation is an integral component from inception.

Accordingly industry would welcome the opportunity to work with the TFES Review Authority in developing a framework for adjusting parameters and with Government in ensuring the Terms of Reference are appropriately focused while providing sufficient flexibility.

5. CONCLUSION

A documented methodology for updating parameters is regarded as an essential requirement if the Tasmanian Freight Equalisation Scheme is to continue to deliver on its stated objective of alleviating Bass Strait shippers sea freight cost disadvantage.

The absence of such a methodology has compromised the implementation of an annual adjustment process as recommended by the TFES Review Authority in its 1998 Advisory Opinion.

Industry is now seeking the urgent development and implementation of such a methodology as a way of:

- Improving scheme integrity including administrative oversight, reducing the potential for rorting and enhancing transparency/understanding etc. and
- Calibrating the scheme to ensure assistance levels reflect the actual sea freight cost disadvantage incurred by shippers;

Industry looks forward to assisting Government and the TFES Review Authority through being an active and involved participant in the development of a framework for adjusting parameters and its subsequent implementation.