

**PRODUCTIVITY COMMISSION INQUIRY INTO INTERNATIONAL LINER CARGO  
SHIPPING: A REVIEW OF PART X OF THE *TRADE PRACTICE ACT 1974***

**SUBMISSION BY THE DEPARTMENT OF  
FOREIGN AFFAIRS AND TRADE**

The Department of Foreign Affairs and Trade (DFAT) has an interest in shipping matters, including the Review, given the importance of efficient and reliable liner services for Australia's international competitiveness, its trade performance and national economic welfare. DFAT suggests that key objectives of the Review should be:

- to ensure that Australia's liner shipping legislation provides continuing access to the types and quality of liner services required to maximise export potential at the lowest possible cost; and
- to identify strategic gains to Australian exporters of any proposed changes to Part X of the Trade Practices Act 1974 (TPA).

DFAT notes the following arguments for retaining Part X TPA:

- that the cost of freight for Australian exporters appears to be competitive;
- that there is a general consensus among Australia's exporters that the exemptions granted by Part X TPA from section 45 and section 47 TPA have allowed shipping lines to provide Australia with adequate levels of service;
- that the countervailing powers granted to exporters under Part X have allowed them to negotiate service agreements with liner operators that have ensured adequate levels of services, in terms of frequency and destination, including the servicing of smaller volume ports such as those in South Australian and Western Australia.

However, DFAT notes a widely held view among smaller importers that Part X TPA has not contributed to either stable or competitive freight rates or adequate levels of service.

Whilst supporting the retention of Part X TPA, DFAT recognises that there is a need to ensure that appropriate safeguards are in place to prevent possible abuse of market power arising from the exemptions granted to liner operators from the normal operations of the TPA. In particular, exporters and importers need continuing access to reliable and competitively priced liner services. Refinements in this area should be the focus of any amendments to Part X TPA resulting from this current Review.

DFAT considers that the Review should consider, *inter alia*:

- the implications of any recommendations regarding Part X TPA for the competitiveness of Australia's exporters and in particular, the impact on exporters of access to reliable, regular and competitively priced liner services;
- the economic and regulatory changes that have occurred in the liner industry since the Productivity Commission's last Review of Part X TPA, and the effects on liner services and freight rates for Australia.

In addition to examining these issues, this submission discusses the relevance to the Productivity Commission inquiry of Australia's obligations under the World Trade Organisation (WTO), of negotiations currently occurring in the Doha Development Agenda, and of our commitments under free trade agreements which Australia has negotiated.

## **1. Overview of the Liner Industry**

The liner shipping market has been characterised historically by cooperative behaviour amongst liner operators aimed at setting rates and coordinating the supply and frequency of liner services. This has traditionally occurred in the form of government-sanctioned Conference Agreements, whereby liner operators entered in binding agreements to charge a common freight-rate, manage capacity, revenue and costs. In many countries, such agreements have been allowed exemption from legislation governing anti-competitive behaviour.

The arguments in favour of allowing liner operators to behave in ways that in most cases would contravene State competition laws are partly based on the distinctive nature of the liner industry. There has been a widespread view that a competitive liner market would lead to ‘destructive competition’ and cycles of chronic over and under supply of capacity, leading to large fluctuations in freight rates and inadequate service. Instead, allowing some forms of anti-competitive conduct in the form of Conference Agreements has arguably allowed liner operators to limit freight-rate fluctuations and provide regular services with sufficient capacity, especially to smaller ports.

During the early 1980’s, strong independent shipping lines who were able to compete on price and service with Conference members entered the market. This led to a steady decline in the market share of Conferences Agreements along most trade routes. But other forms of cooperation among carriers have either remained significant or become increasingly important.

Discussion Agreements - non-binding forums where members agree to share information on a relevant route and may reach agreement on issues such as capacity and rates – now cover a significant percentage of liner trade (although their non-binding nature has limited their effectiveness). Consortia Agreements - developed in response to the technical and logistical hurdles of launching a container service – also remain an important means for cooperation amongst liner operators. Under these Agreements, liner operators cooperate on various technical, operational, logistical or commercial aspects. Consortia Agreements are distinct from Conference Agreements in that they are focused only on the operations of liner shipping and do not extend to cooperation on rates.

Liner operators have also increasingly formed Global Strategic Alliances in order to share space and services and thereby capture additional efficiencies on a global basis. These cover the use by various liner operators of many carriers over different trade routes. These Alliances are therefore operationalized through route agreements which cover the entire operation of the liner trade, and involve close cooperation on matters such as the employment and utilization of vessels, itineraries, sailing schedules, the type and size of vessel to be employed, port rotations and use of terminal facilities. Global Strategic Alliances are distinct from Conference Agreements in that their members do not engage in common marketing, establish common tariffs or share

profits and losses. However, the close cooperation entailed by these Alliances usually limits competition on freight rates.<sup>1</sup>

## **2. Developments in the Liner Industry**

### **2.1 Recent Economic Developments**

In 1999, the Productivity Commission produced an Inquiry Report (the 1999 Report) on Part X of the TPA, and concluded, inter alia, that “given competition and market contestability, the benefits to Australian shippers (and hence the community overall) of allowing conferences and other cooperative arrangements to operate exceed any costs.”<sup>2</sup>

Since the completion of the 1999 Report, the liner shipping industry has undergone further changes, driven by the globalisation of the world economy, technological innovations, and the demand for integrated transportation services. In particular, global manufacturing has increased the demand for the provision of just-in-time comprehensive supply chain services.

In response to the deregulation of the liner industry and the changing economic conditions, the industry has also undergone increasing consolidation. For example, in the year ending 30<sup>th</sup> September 2002, the top 20 liner operators controlled 62 per cent of world total container carrying capacity, up from 53 per cent in 1998.<sup>3</sup> This trend towards greater concentration in liner shipping has nevertheless been slowed by the use of Strategic Global Alliances, which have been able to provide many of the benefits associated with mergers, while limiting their members’ exposure to investment risk.<sup>4</sup>

Further, in order to take advantage of economies of scale, liner operators have continued to order an increasing number of larger vessels. For example, at the beginning of 2003, there was a 4.9 per cent increase in the number of ships over the previous year but a 10.1 per cent increase in TEU capacity, with the average carrying capacity of ships growing from 1824 TEUs<sup>5</sup> in 2001 to 2040 TEUs in 2003.<sup>6</sup>

This shift towards larger ships has also coincided with significant growth in transshipment services through hubs such as Singapore, Hong Kong and Busan. This has allowed liners to operate larger ships on the major East-West trade routes, and to use smaller ships to service countries like Australia on the smaller North-South trade routes.

---

<sup>1</sup> OECD, *Competition Policy In Liner Shipping*, Paris, DSTI/DOT(2002)2, 16<sup>th</sup> April 2002, p. 27.

<sup>2</sup> Productivity Commission Inquiry Report, *International Liner Cargo Shipping: A Review of Part X of the Trade Practices Act 1974*, Canberra, 15<sup>th</sup> September 1999, p. xxxix.

<sup>3</sup> UNCTAD, *Review of Maritime Transport 2003*, United Nations, New York and Geneva, 2003, p. 62.

<sup>4</sup> United States Federal Maritime Commission, *The Impact of the Ocean Shipping Reform Act of 1998*, Washington D.C., September 2001, p. 15.

<sup>5</sup> Twenty foot equivalent container units

<sup>6</sup> UNCTAD, *op. cit.*, p. 19.

## 2.2 Changing Views on Regulation

In 1998, the United States amended the 1984 Shipping Act with the Ocean Shipping Reform Act (OSRA). One of the main objectives of the OSRA was to deregulate the liner industry and encourage greater intra and inter competition amongst Conference and other Agreements. The OSRA achieved this by retaining the antitrust exemptions, while prohibiting any Agreement from penalising members that entered into confidential service contracts with shippers. The OSRA also abolished the ‘me-too’ rule, where members had previously been required to offer the same rates or conditions to other similarly situated customers.

As a result of these amendments, in the first two years of the operation of the OSRA, there was a 200 per cent increase in service contracts between liners and shippers.<sup>7</sup> The flexibility of individual service contracts has also allowed liner operators to add value to their services by offering more complete supply-chain management. This increase in individual contracting undermined the viability of many Conference Agreements and led to a corresponding increase in the use of Discussion Agreements.<sup>8</sup> In November 2001, Canada adopted similar regulations to the OSRA with the introduction of the Shipping Conference Exemption Act 2001.

The OECD issued a report in 2002 which concluded, inter alia, that “anti-trust exemptions for conference price-fixing no longer serve their stated purpose (if they ever did) and are no longer relevant...by extension, voluntary and non-binding rate agreements and discussions would seem to fall under the same category.”<sup>9</sup> In 2003, the European Commission produced a discussion paper regarding the Review of Regulation 4056/86, which Regulation grants a Block Exemption to liner shipping from Articles 81 and 82 of the Treaty. The discussion paper concluded, inter alia, that “the conditions for an exemption would appear to be no longer fulfilled.”<sup>10</sup> It remains to be seen what the implications for the Review will be for liner operators in Europe.

As a result of the OSRA and changes in the competition laws in other States, there appears to be a shift towards deregulation of the international liner market. However, given Australia’s size and distance from the major trade routes, it is unclear whether deregulation of the liner shipping market in Australia would produce similar results.

## 3. Part X TPA and the interests of Exporters and Importers

### 3.1 Australia’s Liner Trade

Australia’s main destinations for liner freight are North and South East Asia, North America, Europe and New Zealand. In the 2003 calendar year, approximately \$87 billion or 80 per cent of Australia’s exports were transported by sea. Of this amount, \$41.3 billion or 47 per cent was carried as freight aboard liners, up from \$39 billion or 43 per cent during the 2000 calendar year. With regard to imports in the 2003 calendar year, approximately \$92 billion or 71 per cent of Australia’s imports were

---

<sup>7</sup> United States Federal Maritime Commission, *op. cit.*, p. 17.

<sup>8</sup> *Ibid.*, p. 17.

<sup>9</sup> OECD, *op. cit.*, p. 77.

<sup>10</sup> European Union Competition Directorate General, *Review 4056/86 – discussion paper*, 2003, p 37.

transported by sea. Of this amount, \$74 billion or 81 per cent was carried as freight aboard liners. This contrasts with \$54 billion or 67 per cent during the 2000 calendar year.<sup>11</sup>

Australia's liner trades with the rest-of-the-world are relatively low in value from the perspective of the larger shipping lines. For example, at the end of 2002, Australia's total maritime trade constituted 1.1 per cent of the value of total maritime trade.<sup>12</sup> These trade routes are also long, due to the distance of Australia from the world's major trading routes. Further, because Australia's exports tend to be denser and heavier than its imports, liners carry large numbers of empty containers on the export legs compared with the import legs. For example, in 2000-2001 16 per cent of all TEUs imported were empty compared with 24 per cent of all exported TEUs.<sup>13</sup>

### 3.2 Part X TPA

The definition of a "conference" in Part X Section 10.02 TPA extends the coverage of Part X TPA to Conference Agreements, Discussion Agreements, Consortium and Global Strategic Alliances. Part X allows liner operators who register their Agreements to engage in conduct that would otherwise be prohibited under Part IV TPA. The TPA balances this exemption granted to liners with an obligation to negotiate with designated shipper bodies and to provide all reasonably necessary information. Under the TPA, the Australian Peak Shippers Association (APSA) has been designated as an outwards peak shipper body and the Importers Association of Australia (IAA) has been designated as an inwards peak shipper body. The ACCC also has the power to review whether a registered Agreement has breached a Part X TPA condition. A review is usually conducted by the ACCC at the request of the Minister or a party affected by a registered Agreement, but in exceptional circumstances may be initiated by the ACCC on its own accord. Where a breach is discovered, the Minister may deregister the offending Agreement.

DFAT notes that the APSA is of the opinion that, as a result of Part X TPA, liners service Australian ports with the necessary regularity and capacity to satisfy exporters' demands. Freight rates are also considered internationally competitive, notwithstanding recent rate increases, especially along the Australia-China route, because these rates are seen as coming off a low base. In contrast, DFAT also notes that the IAA has had difficulty negotiating freight rates, and their claims that service levels are generally inadequate.

## 4. Changes to Part X TPA

### 4.1 International Practice

Any recommendations to retain, amend or abolish Part X TPA will need to take into account how liner operators are regulated in other States. For example, should Australia decide to regulate liner operators differently than occurs overseas, the Productivity Commission will need to consider whether this could lead liners to

---

<sup>11</sup> Data sourced from the DFAT Stars Database and the Bureau of Transport and Regional Economics Database.

<sup>12</sup> UNCTAD, *op. cit.*, p. 51.

<sup>13</sup> Data sourced from the Bureau of Transport and Regional Economics Database.

registering in third countries in order to avoid the jurisdiction of Australian law and the implications of this for Australia's exporters and importers. Alternatively and in light of developments with other state's competition laws, the Productivity Commission should also consider the implications for Australia should its regulatory regime be more accommodating of anti-competitive behaviour than occurs overseas.

#### 4.2 Service Quality and Freight Rates

Access by exporters to competitively priced freight rates and to regular departures from all of Australia's ports is an important factor that influences Australia's export competitiveness overseas. Competitive freight rates for Australia's importers will also influence the competitiveness of imports in Australia. Competitively priced imports leads to increased consumer welfare and when used as inputs in the production process, will also affect the competitiveness of Australian produced goods domestically and overseas.

Exporters are concerned that limiting the exemptions granted to liners under Part X TPA will lead to a decline in the servicing of Australian ports. They also argue that a reduction in the countervailing powers granted to exporters under Part X will reduce the ability to negotiate service levels and rates, which will also impact adversely on Australia's trading interests. As a result, DFAT is concerned to ensure that the Productivity Commission carefully considers the effect on freight rates and service levels that would follow from any changes to Part X TPA.

### 5. Part X TPA and Australia's WTO and FTA obligations

DFAT is responsible for co-ordinating Australia's participation in international trade agreements, such as World Trade Organization agreements and bilateral Free Trade Agreements (FTAs) such as those recently concluded with the US, Thailand and Singapore. As is discussed below, elements of Part X of the TPA have resulted in reservations to existing commitments in bilateral Free Trade Agreements and in the General Agreement on Trade in Services in the WTO.

#### WTO Doha Round negotiations

Maritime transport services are seen by a number of WTO Members, including Australia, as an important part of the Doha Round of multilateral trade negotiations which were launched in November 2001. However, little progress has been made since the breakdown of sector-specific maritime negotiations in 1996. Australia, like other advocates of relatively open markets for international maritime services, has an offer of new commitments on the table in the Doha Round. We also have standing requests of key trading partners to make similar offers of new commitments, but the response has been disappointing to date.

By the time that the Doha Round was launched, WTO Members recognised the need for a multilateral framework to enhance the contribution of competition policy to international trade and development. It was labelled as one of the four Singapore issues (together with investment, transparency in government procurement and trade facilitation). Members agreed that negotiations on these issues would take place in the Doha Round after the Fifth Ministerial Conference (held in Cancún, Mexico in

September 2003). However, opposition from mostly developing countries to the Singapore issues resulted in the issues, with the exception of trade facilitation, being dropped from the Round. Competition policy has now been relegated to the WTO's work program, and no negotiations will take place during this current Round.

### **References to Part X in trade agreements**

Competition policy is covered by Australia's FTAs with the US, Singapore and Thailand. However, the competition chapters of these agreements would allow either continuation or removal of the exemptions from competition policy created by Part X of the TPA.

In contrast, the services and investment chapters of these FTAs and Australia's WTO GATS schedule, include reservations/limitations relating to elements of Part X. While the provisions of these agreements differ somewhat, they generally contain a reference to Part X within Australia's list of non-conforming measures, or as a limitation on commitments (collectively referred to as "reservations" hereafter), depending on the structure of each agreement.

The reservations relate primarily to market access (including local presence) and/or national treatment in the services and investment sections of trade agreements. Specifically, Australia has reservations covering the elements of Part X that provide:

- for international liner operators to be represented by a person who is resident in Australia, and who will act as an agent for the purposes of the TPA
- that only Australian flag operators may apply to the ACCC to examine whether conference members, and non-conference operators with substantial market power, are hindering other shipping operators from engaging efficiently in the provision of outward line cargo services to an extent that is reasonable.

If Australia were to remove the measures that give rise to reservations outlined above, this would be treated as a liberalising step, although probably of quite modest value from a negotiating perspective.

However, if we were to contemplate replacing these measures with different measures as part of a package of changes to the treatment of liner shipping in the TPA, significant care would be needed to ensure that the new measures accord with Australia's trade obligations. This would require analysis of the consistency of any specific measures proposed with existing obligations including, particularly, the fact that:

- (i) under the AUSFTA and SAFTA, the reservations regarding TPA provisions for shipping services cannot be made more restrictive under the terms of the respective FTAs;
- (ii) under the AUSFTA, parties are subject to a ratchet mechanism. This means that if Australia liberalizes a measure described in a reservation, it is bound by the change and cannot subsequently make the measure more restrictive.



## **6. Conclusion**

Since the Productivity Commission's 1999 Report, the international liner shipping industry has responded to the further globalisation of the world economy by cooperating on an increasingly global scale, usually in the form of Discussion Agreements and Global Strategic Alliances and at the expense of the role of Conference Agreements. The liner industry has also engaged in further rationalisation of the industry through mergers and acquisitions.

Major trading nations such as the United States and Europe have also either introduced laws that have encouraged greater deregulation and competition amongst liner operators or undertaken reviews of their laws. In this regard, DFAT welcomes this opportunity for the Productivity Commission to review the costs and benefits to Australia of Part X TPA, and to determine whether the objectives of Part X TPA can be achieved using more efficient means. In particular, DFAT would expect that any amendments to Part X TPA would be in accordance with the Government's competition policy principles and be aimed at increasing competition in the international liner shipping market, where this leads to improved levels of service at lower freight rates for Australia's exporters and importers.

However, the Department also notes the general consensus among Australia's exporters that the exemptions granted by Part X TPA from section 45 and section 47 TPA have allowed liners to provide Australia with adequate levels of service. The cost of freight to Australian exporters also appears to be competitive. The countervailing powers granted to exporters under Part X have allowed them to negotiate service agreements with liner operators that have ensured adequate levels of services, in terms of frequency and destination, including the servicing of smaller volume ports. The Productivity Commission could consider whether greater flexibility for exporters to negotiate confidential service agreements with liner operators would introduce greater competition on freight rates without sacrificing levels of service.