



Australian
Competition &
Consumer
Commission

Australian Competition and Consumer
Commission (ACCC) submission
to the
Government's Options Paper:
Approaches to regulating coastal
shipping in Australia

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Summary

The Australian Competition and Consumer Commission (ACCC) welcomes the opportunity to provide a submission to the Australian Government's Options Paper: *Approaches to regulating coastal shipping in Australia* (the Review). The ACCC supports open competition in coastal shipping as the best way to increase efficiency and reduce the cost of freight in Australia.

We recognise the importance of coastal trade to the national economy and the role that coastal shipping plays in the overall transport network. Over the next 20 years, the nation's freight task is expected to double. So, it will be critical to improve freight flows by promoting competitive industry structures that provide signals for efficient investment.

The ACCC's key points are:

- Restrictions on competition in coastal shipping are not having their intended effect of preserving or 'revitalising' domestic shipping.
 - Recent regulatory changes have not made domestic shipping more competitive.
 - Even if such regulations were having their intended effect, the costs imposed by inflating transport costs raise serious questions for a country like Australia which has an enormous freight task.
- Recent regulatory changes have imposed additional burdens on foreign shipping lines providing coastal shipping services.
- Cabotage restrictions that impede foreign shipping lines from competing with Australian lines for domestic trade add to freight costs for Australian businesses.
- It is particularly concerning that a foreign shipping line could be discouraged or prohibited from carrying coastal trade on a coastal journey it is already undertaking as part of an international service.
- Restrictions on competition in coastal shipping are potentially at odds with principles of National Competition Policy (NCP).
 - The Review should assess whether policy objectives about preserving domestic shipping can only be achieved by restricting competition and, if so, whether the costs outweigh the benefits.
- Increased competition in coastal shipping should result in lower freight costs, with flow-on effects of lower prices for manufacturing inputs and consumer goods.
- A more efficient coastal shipping industry will help to relieve pressure on Australia's road and rail networks, lowering transport costs and consequently prices, across the economy.

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The ACCC's role

The ACCC is pleased to provide a submission to the Government's Options Paper: *Approaches to regulating coastal shipping in Australia*.

The scope of the Review covers several aspects of competition and efficiency that impact on overall shipping and freight costs affecting Australian importers, exporters and the broader community. Competition and efficiency in Australian shipping are important to the ACCC given its role to promote competition to make markets work for the benefit of consumers, business and the community. The ACCC has not commented on the detail of the various policy options presented in the Options Paper for reform of coastal shipping regulation.

The ACCC has instead taken a principle-based approach to considering the impact of regulation on coastal shipping services. For the purposes of this Review, the ACCC considers that the following principles are relevant:

- Competitive markets where possible are the best means of achieving efficient outcomes for businesses, and ultimately, consumers.
- Cost reflective pricing will send the appropriate signals to influence supply and demand for coastal shipping services.
- Where regulation is required to address problems of market failure, a principle of NCP is that legislation should not restrict competition unless the benefits outweigh the costs to the community; and the objectives of the legislation can only be achieved by restricting competition.

Coastal shipping and the national freight task

Interstate movement of cargo is a particular challenge for a nation as vast and dispersed as Australia.

While shipping companies are fundamental to international import/export supply chains, coastal shipping plays a far less significant role in the domestic supply chain. Of Australia's domestic freight task, most freight is carried by rail (in 2011-12, rail had a 48.5 per cent share of the task, with road carrying 34.6 per cent and coastal shipping carrying 16.8 per cent of total domestic freight volumes). Coastal shipping can be an alternative to road and rail services, but may not always be available or competitive for Australian domestic routes.

Composition of coastal trade

Coastal cargo represents around 10 per cent of all cargo volumes (by weight) moved across Australian wharves.¹ Maritime statistics published by the Bureau of Infrastructure, Transport and Regional Economics (BITRE) indicate that Weipa, Port Hedland, Gladstone and Melbourne are the four largest ports in terms of total loaded coastal cargo. Weipa, Port Hedland and Gladstone are bulk ports, while Melbourne, Australia's largest container port, is significant as the mainland gateway to sea trade to Tasmania.²

¹ BITRE, *Freightline*, 2 May 2014, p.2.

² The ACCC notes that the Productivity Commission (PC) recently conducted an inquiry into Tasmanian Shipping and Freight. The PC's final report was sent to the Government on 7 March 2014 (but has not yet been publicly released).

The majority of coastal trade in Australia is bulk cargo.³ The majority of bulk vessels registered to carry coastal trade are Australian vessels.

Around 10 per cent of coastal trade in Australia is containerised freight. This freight is carried by foreign ships licensed to operate along Australian trade routes.⁴

Coastal shipping is therefore a mostly specialised service; it favours bulk freight (rather than containers) because the market for containerised transport faces strong competition from road and rail. Moving containerised domestic freight by ship takes longer; roughly twice as many hours as road transport. One estimate suggests that containerised coastal shipping is only competitive with land-based transport for distances above 2,200 kilometres.⁵

Cost of running a containerised coastal shipping service

Historically, it has been claimed that it costs Australian operators more to provide a coastal shipping service for containerised trade than foreign vessel competitors.⁶

One reason for the cost disadvantage faced by domestic operators is that foreign vessels can charge coastal freight rates based on the additional costs of the coastal voyage to their international schedule, such as extra fuel used. In contrast, domestic operators are likely to have higher average costs of running and maintaining a vessel (such as depreciation, fuel, labour etc.) that is used purely for domestic trade.

Another possible reason for a cost differential is that a foreign vessel offering a coastal service as part of an international schedule does not have to charge a freight rate that covers the cost of 'backloading', whereas a domestic operator is likely to have to charge a freight rate to cover the return journey. For example, when Australian ships serviced the container trade between south-eastern ports and Fremantle, to be profitable, it is understood that they had to charge a rate per container that covered average cost. Because opportunities to backload cargo from Western Australia to the east coast were limited, the rate had to cover the cost of the round trip.⁷ In contrast, a foreign ship carrying domestic cargo one way as part of a longer international voyage does not have to cover the cost of backloading. The Review should consider whether Australian businesses should benefit from the natural cost advantage of foreign lines providing coastal shipping services or whether existing protections should remain in place.

³ Bulk cargo can be split by dry and liquid cargoes. Dry bulk cargo includes cement, iron ore, manufactured steel, sugar cane, gypsum, alumina/bauxite, soda ash and fertiliser. Liquid bulk cargo includes oil, refined petroleum, liquefied gas and chemicals.

⁴ The exception to this is the Bass Strait freight services whereby containers are transported via domestic vessels. There are no foreign vessels that carry containerised trade between the mainland and Tasmania.

⁵ Parliamentary Research Library, *Research Paper: Coastal shipping: an overview*, May 2004, p.19.

⁶ Shipping Australia Limited, Submission to the coastal shipping policy and regulation inquiry by the Parliament of Australia House of Representatives Standing Committee on Infrastructure, Regional Development and Local Government, April 2008, p.8.

⁷ Parliamentary Research Library, *Research Paper: Coastal shipping: an overview*, May 2004, p.19.

ACCC concerns with restrictions on coastal shipping

The ACCC has several concerns regarding the impact of the current regulations on the supply of coastal shipping services and the effect on domestic freight costs in Australia. These are discussed below.

Restrictions on competition are not having their intended effect of preserving or 'revitalising' domestic shipping

Restrictions on the ability of foreign vessels to compete for domestic coastal trade in Australia have long been in place (since the early 1900s). The coastal shipping regulatory framework was changed between 2010 and 2012 where additional restrictions were imposed on the ability of foreign vessels to compete for domestic sea trade. The changes were aimed at 'revitalising' Australian shipping, facilitating long-term industry growth, enhancing the efficiency and reliability of Australian shipping as part of the national transport system and maximising the use of Australian vessels in coastal trade.⁸

In 2012, the then Government made several statements about the need for reform in response to Australia's declining and ageing coastal fleet, the significant cost disadvantage faced by Australian registered vessels and a widespread skills shortage. The Government also highlighted the need to 'level the playing field'⁹ between domestic ship operators and foreign ship operators while still enabling the participation of foreign operators in the movement of coastal cargo.

The introduction of the *Fair Work Act 2009* imposed Australian labour standards on foreign-registered vessels with foreign crews operating in the Australian coastal trade.¹⁰ At the time, the then Minister for Infrastructure and Transport expressed the view that foreign seafarers on vessels operating in the domestic economy were entitled to be paid Australian wages. He also identified coastal shipping as the only sector of the Australian domestic transport industry where lower paid foreign workers were employed.

On 1 July 2012, the *Coastal Trading (Revitalising Australian Shipping) Act 2012* and associated legislation came into effect. The Explanatory Memorandum states the reforms were aimed at 'revitalising' the Australian shipping industry; facilitating long term industry growth; enhancing the efficiency and reliability of Australian shipping as part of the national system; and maximising the use of Australian vessels in coastal trade.

Central to these changes is a licensing system that grants Australian registered vessels unlimited access to coastal trade for the term of the licence (which can be for a period up to five years), while restricting the ability of foreign vessels to operate within Australian waters through temporary licences with several conditions and reporting requirements. The term of a temporary licence is limited to 12 months. Prior to 2012, foreign vessels were subject to a permit system, with less reporting requirements. Since 2012, under the new temporary licence

⁸ The Minister for Infrastructure and Transport, *Coastal Trading (Revitalising Australian Shipping) Bill 2012*, Explanatory Memorandum, p.6.

⁹ The Minister for Infrastructure and Transport, *Coastal Trading (Revitalising Australian Shipping) Bill 2012*, Second reading speech, 22 March 2012, p.3933.

¹⁰ As of 1 January 2010, the coverage of the *Fair Work Act 2009* (FW Act) was extended to certain permit (i.e. foreign) ships. Ships covered by the FW Act while engaged in coastal trade are also covered by the Seagoing Industry Award 2010 (SIA). While Australian ships covered by the FW Act became covered by Part A of the SIA from 1 January 2010, foreign ships became covered by Part B of the SIA from 1 January 2011.

system, applicants must undertake a minimum of five voyages during the term of the licence. Loading dates, the volume of cargo, ports of loading and unloading are all to be specified at the time when the application is made. This information is published on the Department of Infrastructure and Regional Development's website to allow general licence holders to nominate to carry that cargo instead. The Minister has 15 days to decide whether or not to grant the temporary licence. Should a general licence operator be able to carry the trade on reasonable commercial terms and satisfy the cargo or passenger movement needs of the shipper, the temporary licence could be refused.¹¹

Even where temporary licences are granted, further conditions apply. Should voyages vary (outside existing tolerance thresholds), the temporary licence holder must apply to vary the term of the existing licence prior to handling the cargo. Where much of the containerised coastal trade is incidental trade for a foreign vessel, the administrative burden of complying with these regulations could act as a disincentive to continuing to provide a service. These regulatory changes were intended to maximise the use of Australian ships on coastal trade routes and reduce the cost disadvantage for Australian registered operators.¹² While it is early days since the reforms were implemented, the ACCC is not aware of any clear evidence that would suggest that these objectives are being met.

Based on 2010-11 data, there were 22 Australian vessels registered to carry coastal trade (and over 400 foreign flagged ships under permits). The number of Australian vessels registered to carry coastal trade had fallen to 16 as at December 2013.¹³ Noting the limited data available, early indications are that there has not been a reversal or easing in the long-term decline of Australia's coastal fleet.

Recent regulatory changes have not made domestic shipping more competitive

The ACCC is concerned that existing regulations may discourage or prevent foreign lines from entering the domestic shipping market by increasing the administrative burden and cost of providing these services. An example of this is in relation to the supply of Bass Strait coastal shipping services where no foreign lines currently provide a service.

There has also been a progressive decline in the number of Australian vessels offering coastal shipping services. Over the last decade, the number of Australian registered ships has fallen from 33 ships in 2002–03 to 16 ships as of December 2013.

This longer-term downward trend in the number of Australian vessels could suggest that it is uneconomic for existing suppliers of domestic shipping to expand their fleet and there is no incentive for new players to enter the market.

¹¹ Department of Infrastructure and Transport, *Reforming Australian Shipping, Regulatory Impact Statement*, August 2013, pxxxix.

¹² *ibid.*

¹³ Minister for Infrastructure and Regional Development, Media release, *Shipping to cast off red tape and set sail for productivity boost*, 8 April 2014.

Recent regulatory changes have imposed additional burdens on foreign vessels providing coastal shipping services

Cabotage restrictions that impede foreign shipping lines from competing with Australian vessels for domestic trade add to freight costs for Australian businesses

The 2009 ministerial guidelines on coastal shipping state that the policy objective is to foster a viable coastal shipping industry in a competitive domestic transport sector.¹⁴ Cabotage restrictions form part of these arrangements.

Cabotage is the transport of goods (or passengers) between two locations in the same country by a vessel (or aircraft) registered in another country. Australian shipping is subject to a number of regulations whereby vessels are required to register and obtain licences to operate along Australia's coastline.

The ACCC is concerned that current regulatory arrangements can interfere with market forces by restricting the ability of foreign lines to compete with Australian vessels for coastal trade. For example, under the current licencing arrangements, Australian vessels can lodge a 'notice in response' to a foreign line's application for a temporary licence. While the licence assessment process provides for some discretion in granting a temporary licence, the ACCC considers the current arrangements can restrict competition from foreign lines and therefore result in higher freight costs for Australian businesses.

The ACCC notes reports of a recent example whereby a general licence holder lodged a notice in response to an application for a temporary licence. The pricing of the services quoted by the general licence holder were reportedly higher than those quoted by the temporary licence applicant. The temporary licence was granted. The general licence holder commenced proceedings in the Federal Court of Australia to have that decision overturned.¹⁵ While the temporary licence was granted in this case, this example highlights how current administrative processes act as potential artificial impediments to new entry and competition.

It is particularly concerning where a foreign vessel could be discouraged or prohibited from carrying coastal trade on a coastal journey it is already undertaking as part of an international service. This is because much of the cost of the journey is already covered by the international container trade on board.

For foreign vessels to carry domestic cargo when operating along Australia's coastline, they must adhere to additional regulations prescribed under the *Fair Work Act 2009* (FWA) whereby temporary licence holders (i.e. foreign vessel operators) are required to pay their foreign crews Australian wages and conditions for the duration of their Australian voyage. On 1 January 2010, new remuneration structures for the Seagoing Industry Award (SIA) were put in place to account for award modernisation legislation. Wages on general licenced vessels are determined by Fair Work Australia and registered under the SIA Part A or individually negotiated Enterprise Bargaining Agreements. As of 1 January 2011, wage rates of foreign vessels operating in the coastal trading sector are set according to the FWA; these wage rates are known as SIA (Part B). Previously wage rates for foreign vessels were set by the

¹⁴ Ministerial Guidelines for Granting Licences and Permits to Engage in Australia's Domestic Shipping,

www.infrastructure.gov.au/maritime/freight/licences/ministerial_guidelines.aspx#preamble

¹⁵ HWL Ebsworth; Joe Hurley, Partner and Jesper Martens, Special Counsel; 'Do holders of General Licences for Coastal Trading in Australia receive preferential treatment under new laws?' 19 February 2013

International Transport Federation (ITF) market rate.¹⁶ Foreign ships that were previously operating under permits were exempt from the provisions of Australian legislation, including the wages and conditions which applied to licensed vessels and other domestic crewed and owned vessels.

At the time that the legislation was introduced, then Minister for Infrastructure, the Hon, Anthony Albanese MP, stated that foreign seafarers on vessels operating in the domestic economy should be paid Australian wages.¹⁷ He also identified coastal shipping as the only sector of the Australian domestic transport industry where lower paid foreign workers were employed.¹⁸

The effect of these changes is that higher costs are associated with the movement of domestic trade as opposed to those goods designated for import/export despite there being no difference in the nature of the shipping service being performed. These additional costs result from the costs of complying with the administrative requirements for foreign lines as well as the higher wage and other benefits that must be paid for the coastal journey. The downstream effect is higher freight costs for Australian businesses. In the absence of these reforms, a foreign vessel should be able to charge a lower freight rate for the movement of domestic containers.

Higher costs to foreign shipping lines will influence whether those lines apply to move coastal trade. Where this coastal trade represents a foreign shipping line's incidental business, any additional costs or onerous procedural requirements could act as a disincentive to entering the domestic shipping market. Where the foreign vessel faces a disproportionate effect (where it incurs higher costs across its entire vessel despite carrying only a relatively small percentage of coastal cargo) this could act as a disincentive to engaging in coastal trade. This is particularly concerning where a foreign line is discouraged from carrying coastal trade as part of an international service.

The case for whether or not coastal shipping should be regulated in this way is an issue about the justification of ongoing industry protection. In most cases, restrictions on competition drive higher prices for customers - in this case, Australian businesses, in the form of higher freight rates. The Review should consider whether the benefits of current protections outweigh the costs they impose on Australian businesses and the wider community.

Domestic freight services available to Australian businesses could be cheaper and more frequent if foreign lines could more easily transport domestic cargo. This could be particularly important in re-establishing a service by a foreign shipping line to Tasmania.

Restrictions on competition in coastal shipping are potentially at odds with National Competition Policy

National Competition Policy was intended to promote a consistent national approach to fostering greater competition in the Australian economy in the interests of higher economic growth and enhanced community well-being.

¹⁶ The Senate Economics Legislation Committee, *Coastal Trading (Revitalising Australian Shipping) Bill 2012 [Provisions] and related bills*, final report, June 2012, p.6.

¹⁷ A Albanese, Second reading speech, *Coastal Trading (Revitalising Australian Shipping) Bill 2012*, House of Representatives, Debates, 22 March 2012, p.3933.

¹⁸ The Minister for Infrastructure and Transport, *Coastal Trading (Revitalising Australian Shipping) Bill 2012*, Explanatory Memorandum, p.1.

The Hilmer report¹⁹ found that regulatory restrictions were a significant restriction on competition in the Australian economy. In order to reduce unwarranted regulatory restrictions on competition, governments agreed to adopt the following guiding legislative principles:

Legislation (including Act, enactments, Ordinance or regulations) should not restrict competition unless it can be demonstrated that:

- The benefits of the restriction to the community as a whole outweigh the costs; and
- The objectives of the legislation can only be achieved by restricting competition.²⁰

Having regard to this principle and its universal coverage of the markets for goods and services in the Australian economy, it is not clear to the ACCC why restrictions on competition should persist in the coastal shipping sector. In accordance with NCP, the review should assess whether policy objectives of coastal shipping arrangements including cabotage can only be achieved by restricting competition and if so, whether the costs outweigh the benefits.

Potential benefits of promoting competition in coastal shipping

More competition in coastal shipping should result in lower freight costs, with flow-on effects of lower prices for manufacturing inputs and consumer goods

Promoting competition through low barriers to entry is important in driving efficiency and keeping freight costs down.

Competition pushes businesses to improve their performance by innovating and investing in new services and technologies. Competition benefits consumers with greater choice and better products and services. Competition helps to ensure that prices will be lower and quality higher than would be the case if there were no or little competition. By driving firms towards greater efficiency, competition provides for higher levels of economic growth, increased employment and higher living standards. As such, competition is not a goal of itself, but a means of achieving higher living standards for the community.

In the ACCC's experience, industries that are protected from competition are less likely to face appropriate incentives to minimise costs and invest efficiently in a better service or offer their customers the most attractive terms and conditions of service.

A more efficient coastal shipping industry will help to relieve pressure on Australia's road and rail networks, lowering transport costs and consequently prices, across the economy

With an expected doubling in Australia's freight transport task over the next twenty years, Australia's road and rail networks will need to be well equipped to handle the future freight task. In many cases, such as the current road funding and charging arrangements, significant reform will be required to ensure supply of freight transport infrastructure is able to meet expected demand.

Any action to make coastal shipping services more competitive, such that domestic shippers have access to a more efficient coastal shipping service (e.g. lower cost / higher frequency),

¹⁹ Prof. Frederick G Hilmer, *Inquiry Report to the National Competition Policy Review*, August 1993.

²⁰ Sourced from Clause 5 (1) of the Competition Principles Agreement. A copy is available at <http://ncp.ncc.gov.au/pages/legislation>

should increase the extent to which shipping is substitutable for road and rail and assist governments and industry address the growing transport challenge. Lower transport costs can ultimately flow to consumers in the form of lower prices with the benefits spread more broadly throughout the domestic economy.

For these reasons, the ACCC considers that competition in coastal shipping services should be promoted wherever possible.

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