

The Allen Consulting Group

**Council of Australian Governments
Review of Western Australian Ports**

Final Report

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Report to Department of Planning and Infrastructure

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Executive summary

Introduction

In February 2006, the Council of Australian Governments signed the Competition and Infrastructure Reform Agreement (the CIRA). Clause 4 of the CIRA commits the parties to the agreement (the Australian Commonwealth, State and Territory Governments) to microeconomic reform in the regulation of significant shipping ports (Box ES.1).

Box ES.1

COMPETITION AND INFRASTRUCTURE REFORM AGREEMENT, FEBRUARY 2006

4.1. The Parties agree that:

- (a) ports should only be subject to economic regulation where a clear need for it exists in the promotion of competition in upstream or downstream markets or to prevent the misuse of market power; and
- (b) where a Party decides that economic regulation of significant ports is warranted, it should conform to a consistent national approach based on the following principles:
 - (i) wherever possible, third party access to services provided by means of ports and related infrastructure facilities should be on the basis of terms and conditions agreed between the operator of the facility and the person seeking access;
 - (ii) where possible, commercial outcomes should be promoted by establishing competitive market frameworks that allow competition in and entry to port and related infrastructure services, including stevedoring, in preference to economic regulation;
 - (iii) where regulatory oversight of prices is warranted pursuant to clause 2.3, this should be undertaken by an independent body which publishes relevant information; and
 - (iv) where access regimes are required, and to maximise consistency, those regimes should be certified in accordance with the Trade Practices Act 1974 and the Competition Principles Agreement.

4.2. The Parties agree to allow for competition in the provision of port and related infrastructure facility services, unless a transparent public review by the relevant Party indicates that the benefits of restricting competition outweigh the costs to the community, including through the implementation of the following:

- (a) port planning should, consistent with the efficient use of port infrastructure, facilitate the entry of new suppliers of port and related infrastructure services;
- (b) where third party access to port facilities is provided, that access should be provided on a competitively neutral basis;
- (c) commercial charters for port authorities should include guidance to seek a commercial return while not exploiting monopoly powers; and
- (d) any conflicts of interest between port owners, operators or service providers as a result of vertically integrated structures should be addressed by the relevant Party on a case by case basis with a view to facilitating competition.

4.3. Each Party will review the regulation of ports and port authority, handling and storage facility operations at significant ports within its jurisdiction to ensure they are consistent with the principles set out in clauses 4.1 and 4.2.

- (a) Significant ports include:
 - (i) Major capital city ports and port facilities at these ports;
 - (ii) Major bulk commodity export ports and port facilities, except those considered part of integrated production processes; and
 - (iii) Major regional ports catering to agricultural and other exports.

Under clause 4.3 of the CIRA, the Government of Western Australia is required to review the regulation of ports and port authorities, handling and storage facility operations at significant ports to ensure they are consistent with principles for economic regulation and competition in the provision of port services and infrastructure set out in clauses 4.1 and 4.2.

At a subsequent meeting in April 2007, COAG approved a “CIRA Implementation Plan”, which required the Western Australian Government to review the Port of Esperance, the Port of Fremantle and the Port of Port Hedland to satisfy its review obligations.

The Western Australian Department for Planning and Infrastructure (the Department) engaged the Allen Consulting Group to undertake the review required by clause 4.3 of the CIRA.

This report takes account of the issues raised in submissions from stakeholders in response to an Issues Paper and a Draft Report, and makes findings and recommendations on matters required to be addressed under clauses 4.1 and 4.2 of the CIRA, including:

- under clause 4.1 of the CIRA –
 - whether there is evidence that significant Western Australian ports and/or related infrastructure facilities have market power,
 - where significant Western Australian ports and/or related infrastructure facilities are found to have market power, whether there is evidence this market power has been misused,
 - whether there is evidence that economic regulation of significant Western Australian ports and/or related infrastructure facilities would promote competition in upstream or downstream markets; and
- under clause 4.2 of the CIRA –
 - whether there are restrictions on competition in provision of port and related infrastructure facility services,
 - whether port planning facilitates the entry of new suppliers of port and related infrastructure facility services,
 - whether third party access provided at significant Western Australian ports and related infrastructure facility services is provided on a competitively neutral basis,
 - whether commercial charters for port authorities include guidance to seek a commercial return while not exploiting monopoly power, and
 - whether there are vertically integrated structures that result in conflicts of interest between port owners, port operators or service providers at significant Western Australian ports.

The findings of the Allen Consulting Group on these matters are set out as follows.

CIRA clause 4.1 – Justification for Economic Regulation

Clause 4.1 of the CIRA states that ports should only be subject to economic regulation where a clear need for it exists in the promotion of competition in upstream or downstream markets or to prevent the misuse of market power.

For the purposes of this review, the requirements of the clause 4.1 of the CIRA were considered in terms of two categories of port infrastructure services and their related upstream and downstream markets.

First, the review considered the provision by the Fremantle, Esperance and Port Hedland Port Authorities of “port facilities” that include access to land at ports and the basic infrastructure and facilities of the ports. The relevant markets serviced by the provision of port facilities are the downstream markets for the “port services” that use the basic port facilities. These are the markets for:

- shipping services;
- stevedoring services;
- pilot services;
- tug and towage services; and
- line and mooring services.

For the Fremantle, Port Hedland and Esperance Ports it is concluded in this report there are no instances where economic regulation of providers of port facilities is required to either prevent the misuse of market power in the provision of port facilities by the port authorities or to increase competition in the downstream markets for port services.

Second, the review considered the provision of the port services including:

- stevedoring services;
- pilot services;
- towage services;
- line and mooring services;
- grain bulk-terminal services; and
- iron ore bulk-terminal services.

These services are provided in part by the port authorities and in part by private-sector providers of the services.

The relevant upstream and downstream markets that are likely to be dependent on the provision of port services are broadly categorised as the markets for the products transported as containerised freight, the markets for grains and the market for iron ore.

It is found that regulation of providers of port services would only increase competition in upstream and downstream markets in the case of the bulk export grain terminal services that are provided by Cooperative Bulk Handling Limited (CBH).

Consistent with this finding, the Western Australian *Bulk Handling Act 1967* provides for CBH's facilities at Western Australian ports to be available on a 'common user' basis, although there are no provisions to govern the manner in which terms or prices of access are to be determined. The Commonwealth *Wheat Export Marketing Act 2008* also requires CBH, as an accredited wheat marketer, to pass an 'access test'. The rights of access established under these two Acts are likely to limit the degree to which CBH could misuse its market power and provides other parties with the opportunity to operate their own grain export activities using the facilities of CBH.

A limitation of the *Wheat Export Marketing Act 2008* is that the access test will apply only to export terminals that are operated by an accredited wheat marketer, and only in relation to the export of wheat. Should CBH at some future point not be an accredited wheat marketer, it would no longer be required to meet the access test, although it would still be obliged to allow other parties to use its export terminals under the *Bulk Handling Act 1967*.

It has not been demonstrated that there is a clear need for the Western Australian Government to consider further economic regulation of the grain terminal services for wheat.

While there are access test provisions in place to adequately regulate wheat export grain terminals in Western Australia, these provisions do not extend to the other bulk grains exported from the State (such as barley, lupins and canola). There is the potential for the misuse of market power by operators of the bulk grain terminals for these other bulk grains. While there is no evidence to indicate that misuses of market power have occurred, given that there is potential for misuse of market power, the access provisions for these other grains may need further investigation to create consistency with the existing regulatory arrangements for wheat.

CIRA clause 4.2 – Allowing for Competition

Clause 4.2 of the CIRA requires that competition be allowed in the provision of port and related infrastructure facility services unless it is established that the benefits of restricting competition outweigh the costs to the community.

Consideration was given in this review to the specific aspects of port operations identified in clauses 4.2(a) to (d) of the CIRA and whether these operations are conducted in a manner consistent with allowing competition in the provision of port and related services – except in those circumstances where there is a demonstrated net public benefit in restricting competition.

The findings of the review on each of these matters are as follows.

Port Planning

Clause 4.2(a) of the CIRA requires that port planning should facilitate the entry of new suppliers of port and related infrastructure services consistent with the efficient use of port infrastructure.

There is not a specific planning framework at a state-level that considers future port infrastructure requirements, and options for facilitating the entry of new suppliers of port and related infrastructure services. Rather, planning of ports is undertaken by individual port authorities. Section 30 of the *Port Authorities Act 1999* contains a number of provisions that require port authorities to plan for future growth and generally be responsible for the efficient operation of the port. The port authorities also have specific powers in relation to planning (and undertaking works) at ports that stem from their government ownership.

The statutory requirements for port planning and the responsibility given to the port authorities for planning functions would, of themselves, not impede the entry of new suppliers of port and related infrastructure services. However, there is no statutory requirement for port authorities to pro-actively facilitate the entry of new suppliers of port and related infrastructure services. There exists a potential conflict of interest for the port authorities in that performing the planning role within an existing port could, where it is vertically integrated, affect a port authority's competition position with respect to other suppliers of port and related infrastructure services in the port.

Notwithstanding this, the steering committee for this review has advised the Allen Consulting Group that there is significant evidence that planning by ports has and does facilitate the entry of new suppliers of port and infrastructure services. For example, planning by the Fremantle Port Authority in relation to towage and break-bulk stevedoring services has led to the introduction of arrangements to facilitate competition in the provision of these services. Furthermore, the planning for new container facilities in the Fremantle Outer Harbour is likely to lead to the possible entry of a third container stevedore.

A means available to Government to ensure that port planning promotes the efficient use of infrastructure and facilitates the entry of new suppliers is for the Minister to require that the statement of corporate intent and the strategic development plan of port authorities:

- identify how port planning will facilitate the entry of new suppliers of port and related infrastructure services; and
- where port planning will not facilitate the entry of new suppliers of port and related infrastructure services, demonstrate that:
 - this is consistent with the efficient use of port infrastructure; and/or
 - the benefits from restricting competition outweigh the costs to the community.

Such a requirement may not require legislative amendment as section 51(2)(b) of the *Port Authorities Act 1999* provides a Port Authority Board, in the preparation of a strategic development plan, with the discretion to consider other matters that the Minister and the Board agree should be considered.

Competitive neutrality of third party access

Clause 4.2(b) of the CIRA requires that where third party access to port facilities is provided, that access should be provided on a competitively neutral basis.

Competitive neutrality is a term applied in the Competition Principles Agreement to mean the absence of competitive advantages of government businesses over private-sector businesses as a result of public-sector ownership of the government businesses, and in the case of ports would mean that government businesses do not have access to facilities on more favourable terms than private-sector businesses solely for reason of public-sector ownership. More generally, competitive neutrality may be taken to require that third party access to port facilities is on terms and prices that do not discriminate between any parties except on reasonable commercial grounds.

The Fremantle, Esperance and Port Hedland port authorities provide access to a range of service providers including shipping lines, stevedores, pilot service providers and towage service providers. There is no evidence, from submissions to this review or otherwise, to indicate that third party access to port facilities has been provided on anything other than a competitively neutral basis.

Commercial charters

Clause 4.2(c) of the CIRA requires that port charters should include guidance for ports to seek a commercial return while not exploiting monopoly powers.

The commercial charter of port authorities in Western Australia is established by the *Port Authorities Act 1999*. Section 34 of the Act states that:

A port authority in performing its functions must —

- (a) act in accordance with prudent commercial principles; and
- (b) endeavour to make a profit.

On port charges, section 37(2) of the Act states that:

Port charges are to be determined by the port authority in accordance with prudent commercial principles and may allow for —

- (a) the making of a profit; and
- (b) depreciation of assets.

It is clear that *Port Authorities Act 1999* establishes a commercial charter that includes guidance for the port authorities to seek a commercial return. Requirements of the *Port Authorities Act 1999* that the port authorities ‘endeavour to make a profit’ and impose port charges to allow for ‘the making of a profit’ are considered to be consistent with the requirements clause 4.2(c) of the CIRA.

There is no explicit direction in the *Port Authorities Act 1999* for the port authorities to not exploit monopoly power. However, the functions of port authorities also extend beyond a requirement to earn a commercial rate of return and include functions of facilitating trade and commerce. To the extent that exploitation of monopoly powers would be inconsistent with facilitating trade and commerce, the commercial charter established by the *Port Authorities Act 1999* constrains the commercial charter of the port authorities in a manner consistent with guidance to not exploit monopoly powers.

Taking the above into account, the Allen Consulting Group considers that the commercial charter established for Port Authorities under the *Port Authorities Act 1999* is consistent with the requirements of clause 4.2(c) of the CIRA.

Conflicts of interest through vertical integration

Clause 4.2(d) of the CIRA requires that any conflicts of interest between port owners, operators or service providers that result from vertically integrated structures be addressed on a case by case basis with a view to facilitating competition.

Vertical integration occurs when a single company or entity controls several steps in the production and/or distribution of a product or service. In the context of ports, vertical integration is most likely to arise in relation to two or more aspects of infrastructure services and port services — for example, a single business that includes ownership of terminal infrastructure and the provision of stevedoring services. In this example, a conflict of interest may arise if the owner of the terminal infrastructure had an incentive to restrict access to other stevedoring operations so as to protect its own stevedoring operations.

The port authorities have conflicts of interest where they provide port services in actual or potential competition with other providers of port services. Examples of these conflicts of interest exist for the Fremantle and Esperance ports.

The Fremantle Port Authority provides services to transport pilots to ships. There is no evidence to suggest that this conflict of interest has led the Fremantle Port Authority to engage or attempt to engage in anti-competitive behaviour.

The Esperance Port Authority is a provider of stevedoring services, pilot services and line and mooring services at the Port of Esperance. There are conflicts of interest in the provision of each of these services. However, there is no evidence to indicate that these conflicts of interest have caused the Esperance Port Authority to engage or attempt to engage in anti-competitive behaviour. The Esperance Port Authority has not restricted access to port facilities for the provision of port services for reasons of protecting its own business interests.

It is concluded in this review that there is no need for intervention in the operation of the Port Authorities to address conflicts of interest.

Amongst the private-sector providers of port services, CBH, The Pilbara Infrastructure Pty Ltd and some stevedore operators have vertically integrated businesses.

CBH is a vertically integrated company that provides grain export services at the Ports of Albany, Esperance, Geraldton and Fremantle (Outer Harbour), while also being the dominant operator of grain storage and handling facilities in Western Australia.

There are conflicts of interest for CBH in providing access to the grain handling facilities, arising from the vertical integration of CBH with grain transport and grain trading businesses. These conflicts of interest are addressed by the access test imposed by the *Wheat Export Marketing Act 2008*.

TPI, which provides export iron ore handling services at the Port Hedland Port, is a wholly owned subsidiary of iron ore miner FMG, and is vertically integrated with an iron ore rail business, and an iron ore mining and trading business. This vertical integration would give rise to conflicts of interest in providing access to port facilities to other iron ore miners. This conflict of interest is, however, addressed by requirements under agreement with the Western Australian Government for TPI to provide third-party access to the port facilities and to invest in further capacity at Port Hedland to meet the demands of new customers, if commercially justified and subject to Ministerial approval. The effectiveness of these requirements is possibly evident from FMG having recently negotiated an arrangement for access to the TPI berths with Atlas Iron. In addition, it has also negotiated a memorandum of understanding with BC Iron to negotiate port and rail access.

The providers of container stevedoring businesses are vertically integrated with transport and logistics businesses. In its submission to this review, the Transport Forum also expressed concerns about the potential takeover of the Maersk, Baguleys and Connaus container yards at the Port of Fremantle by P&O. While it does not clearly identify the conflict of interest that it believes would arise from the potential takeovers or mergers, the Transport Forum appears to be generally concerned with issues of market power. The potential for reduced competition in the markets for stevedoring and container services has been addressed by the ACCC with the finding that the merger is unlikely to lessen competition in the relevant market. The ACCC found that competitive providers of the same service would be an effective constraint on the merged firm were it to attempt to use any perceived market power. The ACCC noted that the industry had low barriers to entry, and that shipping lines had sufficient bargaining power to enable them to either switch suppliers and/or sponsor new entry into the relevant market (ACCC, 2008).

In summary, therefore, there are not considered to be conflicts of interest arising through vertical integration amongst providers of port facilities and services that restrict competition or that have not been adequately addressed by existing economic regulation.

Summary of findings

- There is no evidence of port and related infrastructure service providers having misused market power and accordingly there are no instances where economic regulation of providers of port facilities is required to either prevent the misuse of market power in the provision of port facilities by the port authorities or to increase competition in the downstream markets for port services.
- Regulation of providers of port services would only increase competition in upstream and downstream markets in the case of the bulk export grain terminal services that are provided by CBH. However, at this time it has not been demonstrated that there is a clear need to consider economic regulation of the grain terminal services for wheat in addition to that imposed by the *Wheat Export Marketing Act 2008*.

- Existing regulatory provisions for wheat do not extend to the other bulk grains exported from the State (such as barley, lupins and canola). There is the potential for the misuse of market power by operators of the bulk grain terminals for these other bulk grains. There is no evidence to indicate that misuses of market power have occurred. However, given that there is potential for misuse of market power, the access provisions for these other grains may need further investigation to create consistency with the existing regulatory arrangements for wheat.
- One means available to Government to ensure that port planning promotes the efficient use of infrastructure and facilitates the entry of new suppliers if the Minister were to require that the statements of corporate intent and the strategic development plans of port authorities:
 - identify how port planning will facilitate the entry of new suppliers of port and related infrastructure services; and
 - where port planning will not facilitate the entry of new suppliers of port and related infrastructure services, demonstrate that this is consistent with the efficient use of port infrastructure; and/or the benefits from restricting competition outweigh the costs to the community.
- There is no evidence to indicate that third party access to port facilities has been provided on anything other than a competitively neutral basis.
- The commercial charter established for Port Authorities under the *Port Authorities Act 1999* is consistent with the requirements of clause 4.2(c) of the CIRA.
- There is no evidence of conflicts of interest arising through vertical integration amongst providers of port facilities and services that restrict competition or that have not been adequately addressed by existing economic regulation.

Chapter 1

Introduction

In February 2006, the Council of Australian Governments signed the Competition and Infrastructure Reform Agreement (the CIRA; COAG, 2006a). Clause 4 of the CIRA commits the parties to the agreement (the Australian Commonwealth, State and Territory Governments) to microeconomic reform in the regulation of significant shipping ports (Box 1.1).

Box 1.1

COMPETITION AND INFRASTRUCTURE REFORM AGREEMENT, FEBRUARY 2006

4.1. The Parties agree that:

- (a) ports should only be subject to economic regulation where a clear need for it exists in the promotion of competition in upstream or downstream markets or to prevent the misuse of market power; and
- (b) where a Party decides that economic regulation of significant ports is warranted, it should conform to a consistent national approach based on the following principles:
 - (i) wherever possible, third party access to services provided by means of ports and related infrastructure facilities should be on the basis of terms and conditions agreed between the operator of the facility and the person seeking access;
 - (ii) where possible, commercial outcomes should be promoted by establishing competitive market frameworks that allow competition in and entry to port and related infrastructure services, including stevedoring, in preference to economic regulation;
 - (iii) where regulatory oversight of prices is warranted pursuant to clause 2.3, this should be undertaken by an independent body which publishes relevant information; and
 - (iv) where access regimes are required, and to maximise consistency, those regimes should be certified in accordance with the Trade Practices Act 1974 and the Competition Principles Agreement.

4.2. The Parties agree to allow for competition in the provision of port and related infrastructure facility services, unless a transparent public review by the relevant Party indicates that the benefits of restricting competition outweigh the costs to the community, including through the implementation of the following:

- (a) port planning should, consistent with the efficient use of port infrastructure, facilitate the entry of new suppliers of port and related infrastructure services;
- (b) where third party access to port facilities is provided, that access should be provided on a competitively neutral basis;
- (c) commercial charters for port authorities should include guidance to seek a commercial return while not exploiting monopoly powers; and
- (d) any conflicts of interest between port owners, operators or service providers as a result of vertically integrated structures should be addressed by the relevant Party on a case by case basis with a view to facilitating competition.

4.3. Each Party will review the regulation of ports and port authority, handling and storage facility operations at significant ports within its jurisdiction to ensure they are consistent with the principles set out in clauses 4.1 and 4.2.

(a) Significant ports include:

- (i) Major capital city ports and port facilities at these ports;
- (ii) Major bulk commodity export ports and port facilities, except those considered part of integrated production processes; and
- (iii) Major regional ports catering to agricultural and other exports.

Under clause 4.3 of the CIRA, the Government of Western Australia is required to review the regulation of ports and port authorities, handling and storage facility operations at significant ports to ensure they are consistent with principles for economic regulation and competition in the provision of port services and infrastructure set out in clauses 4.1 and 4.2.

At a subsequent meeting in April 2007, COAG approved a CIRA Implementation Plan, which required the Western Australian Government to review the Port of Esperance, the Port of Fremantle and the Port of Port Hedland to satisfy its review obligations (COAG, 2007).

The Western Australian Department for Planning and Infrastructure (the Department) engaged the Allen Consulting Group to undertake the review required by clause 4.3 of the CIRA. The terms of reference for this review are provided in Appendix A.

In July 2008, the Allen Consulting Group circulated an Issues Paper inviting submissions on a range of issues to almost 100 stakeholders nominated by the steering committee.

The Department made the Issues Paper available on its website, and notified the public of the review via a notice in *The West Australian* on 16 July 2008.

Submissions were received from the following parties.

- The Fremantle Port Authority.
- James Point Pty Ltd.
- The Transport Forum WA Inc.
- AWB Limited.
- The Department of Environment and Conservation.
- The Sea Freight Council of Western Australia.
- The Port Hedland Port Authority.

A Draft Report was prepared by the Allen Consulting Group that incorporated issues raised in submissions from stakeholders in response to the Issues Paper. In November 2008, this Draft Report was circulated to stakeholders for comment.

Submissions on the Draft Report were received from the following parties.

- CBH.
- The Maritime Union of Australia.
- The Western Australian Farmers Federation.
- James Point Pty Ltd.
- Smithson Planning.
- Premium Grain Handlers Pty Ltd.
- The Department of Agriculture and Food, Western Australia.

- The Department of Environment and Conservation, Western Australia.

This report incorporates issues raised in submissions from stakeholders in response to the Draft Report. This report makes findings and recommendations on matters required to be addressed under clauses 4.1 and 4.2 of the CIRA, including:

- under clause 4.1 of the CIRA –
 - whether there is evidence that significant Western Australian ports and/or related infrastructure facilities have market power,
 - where significant Western Australian ports and/or related infrastructure facilities are found to have market power, whether there is evidence this market power has been misused,
 - whether there is evidence that economic regulation of significant Western Australian ports and/or related infrastructure facilities would promote competition in upstream or downstream markets; and
- under clause 4.2 of the CIRA –
 - whether there are restrictions on competition in the provision of port and related infrastructure facility services,
 - whether port planning facilitates the entry of new suppliers of port and related infrastructure facility services,
 - whether third party access provided at significant Western Australian ports and related infrastructure facility services is provided on a competitively neutral basis,
 - whether commercial charters for port authorities include guidance to seek a commercial return while not exploiting monopoly power, and
 - whether there are vertically integrated structures that result in conflicts of interest between port owners, port operators or service providers at significant Western Australian ports.

Chapter 2

Scope and Conduct of the Review

2.1 Introduction

The review of Western Australian Ports is being undertaken by the Allen Consulting Group for the Department of Planning and Infrastructure, and under the auspices of a steering committee.

In response to the Issues Paper for the review, three parties made submissions addressing the scope and conduct of the review. These submissions are outlined and addressed below.

2.2 Composition of the steering committee

The steering committee for the review comprises representatives from the Department of Planning and Infrastructure, the Department of Treasury and Finance, the Department of Agriculture and Food and the Fremantle Port Authority.

James Point Pty Ltd (James Point) submitted that:

...the composition of the Review steering committee invites criticism in terms of conflicts of interest. Comparable reviews in other jurisdictions have not included port authorities in the management of the reviews, presumably on the grounds that these bodies are the subject of the review and their involvement could compromise the impartiality of the review.

The review should consider whether it would be more appropriate for Fremantle Ports to be a respondent to the Review rather than a representative of Fremantle Ports being a member of the Review steering committee.

The Department of Planning and Infrastructure has advised the Allen Consulting Group that it decided to include port representation on the review steering committee in order to ensure the committee had access to technical, operational and management expertise, but that the port representative would, if necessary, be excluded from any direct presentations.

The Allen Consulting Group expects that the Department's representative, as chair, will act to resolve any actual, perceived or potential conflict of interest within the steering committee in a manner that preserves the integrity of the review process.

2.3 Ports subject to review

The review addresses only the Ports of Fremantle, Esperance and Port Hedland.

AWB Ltd (AWB) submitted that:

...the review will only consider three of sixteen ports in WA. Clause 4.3 of the CIRA commits to the review of the regulation of ports and port authority, handling and storage operations at significant ports and that these are defined in part as major bulk commodity ports not considered to be part of integrated production processes (AWB, 2008: p.1).

AWB appear to contend that clause 4.3 of the CIRA requires that all significant Western Australian ports be reviewed.

Although the Issues Paper did not include a reference to it, COAG agreed in April 2007 that Western Australia's review obligations under clause 4.3 of the CIRA would be met by a review of the Port of Esperance, the Port of Fremantle and the Port of Port Hedland (COAG, 2007: p.44).

2.4 Opportunities to increase competition between ports

The scope of the review was described in the issues paper as addressing the particular requirements of clause 4 of the CIRA, focussing on whether there is justification for economic regulation of port facilities and port services to promote competition in upstream or downstream markets or to prevent a misuse of market power.

James Point submitted that:

[while on]...one level the Review can be seen merely as a compliance exercise to meet the specific CIRA requirement...[a] more expansive view having regard to the underlying philosophy of the CIRA is for the Review to look at the current level of competition within and between ports and at opportunities to foster greater competition.

[James Point believes that] [t]he Review should consider the extent to which there are opportunities and mechanisms to foster increased competition in the provision of port infrastructure and related services in WA, recognising the benefits from this competition, including a reduced need for regulation (James Point, 2008; pp.4 5).

It is not within the scope of the review to consider opportunities for increasing competition between ports and whether such competition is in the public interest. Notwithstanding this, the extent of competition between ports is a factor relevant to analysis of whether there is justification for economic regulation of port facilities and port services.

2.5 Excluded facilities – Fremantle Outer Harbour

James Point submitted that the exclusion of the proposed facilities at the James Point Port, which is to be located adjacent to the Port of Fremantle Outer Harbour, should be reconsidered. Specifically, James Point commented that, from a legal perspective, the James Point Port would:

...operate as a "port within a port". In this sense and as the Issues Paper states "this port would be independent of the existing Port of Fremantle Outer Harbour". However, from an economic perspective the facilities would compromise a significant component of the supply of port and related infrastructure services for the capital city port.

The potential development of the James Point facilities has a significant bearing on some of the issues before the Review. The proposals provide a key example of how new suppliers can contribute to meeting demand. The existence of an Operating Agreement with the WA Government for the development repudiates the notion that Fremantle Ports should remain the monopoly supplier of multi user/multi product berths. The development also has the potential to provide relief from the current shortage of bulk berths in the Outer Harbour and in its second stage, to provide capacity to meet increasing container trade. (And in both cases, a more competitive market would emerge.)

The scope of the review required by Clause 4.3 of the CIRA includes the Port of Fremantle and, hence, the two development options being proposed by the Fremantle Port Authority for the Outer Harbour. It is therefore within the scope of the review to consider whether planning for either of the Fremantle Port Authority's proposed Outer Harbour developments makes adequate provision for the entry of new suppliers of port services.

As the James Point Port proposal is outside of the Port of Fremantle it is not within the scope of the review.

2.6 Excluded facilities – Kwinana Bulk Jetty and Bulk Terminal

James Point submitted that:

...the limit of 1 million tonnes per annum...has no apparent connection with the CIRA. Accordingly, there seems to be no justification in terms of competition principles for the exclusion of "facilities with exports of less than 1 million tonnes per annum".

and:

It is in this area of multi user/multi product bulk berths that the adequacy of supply of port infrastructure at Fremantle has become an issue in recent years...[leading to] interruptions in supply, significant demurrage costs and loss of specific trades.

As acknowledged by James Point, the terms of reference given by the Department for Planning and Infrastructure to the Allen Consulting Group for the review specifically exclude the Kwinana Bulk Jetty and the Kwinana Bulk Terminal facilities. It is understood that these exclusions are on the basis of those facilities not being 'significant' and the fact that other jurisdictions (for example, Queensland) excluded facilities of less than 10Mtpa.

2.7 Functions of port authorities

The Department of Environment and Conservation submitted that:

...the Issues Paper redefines the obligations of port authorities in terms of two primary functions...In referring only to these primary functions, the Issues Paper significantly underestimates the public benefit role that port authorities have in managing the environmental and potential health impacts of ports on the wider community....the public benefit of port authorities having explicit obligations within legislation to plan for their cumulative environmental impacts, and manage the day to day operations to minimise impacts on the environmental values of ports and on the communities adjacent to ports, should not be underestimated.

Clause 4 of the CIRA is concerned with the economic regulation of services provided by ports and related infrastructure facilities. This has been interpreted for the purposes of this review as relating to services of a commercial nature. The scope of the current review does not extend to considering whether there should be any change to the functions of port authorities.

2.8 Length of consultation period

The Issues Paper was distributed to known stakeholders on 11 July 2008, and the consultation period closed on 8 August 2008 — a total of four weeks.

James Point submitted that the period for consultation was too short:

...it is vital that stakeholders have adequate opportunity to provide considered responses to the Issues Paper and Draft Report. The three weeks provided in relation to the Issues Paper does not seem adequate in this regard and a further opportunity for stakeholder input should be provided....The Draft Report should be made available to stakeholders for comment for at least five weeks.

In view of the submission from James Point, the period for submissions on this Draft Report has been set a five weeks, which is longer than the period of four weeks allowed for submissions on the Issues Paper.

2.9 Presentations

James Point submitted that key stakeholders be invited to make oral presentations to elaborate on their submissions and to answer questions.

No formal presentations from stakeholders are intended during the course of the review. Where clarification of issues raised by stakeholders in their respective submission is necessary, this will be followed up on a case-by-case basis.

Chapter 3

Port Descriptions and Operations

3.1 Introduction

Clause 4.3 of the CIRA requires a review of economic regulation of ports and port authority, handling and storage operations at significant ports. Significant ports are defined to include:

- major capital city ports and port facilities at these ports;
- major bulk commodity export ports and port facilities, except those considered to be part of integrated production processes; and
- major regional ports catering to agriculture and other exports.

Seven Western Australian ports meet this definition of significant ports. These are the ports at: Albany, Bunbury, Dampier, Esperance, Fremantle (Inner and Outer Harbours), Geraldton and Port Hedland.

The CIRA Implementation Plan agreed by COAG in April 2007 required that Western Australia review three ports in order to comply with the review requirement imposed by Clause 4.3 (COAG 2007). These three ports are:

- the Port of Fremantle (a major capital city port);
- the Port Hedland Port (a major bulk commodity export port); and
- the Port of Esperance (a major regional port catering for agriculture and other exports).

The remaining significant ports in Western Australia are the ports of Albany, Bunbury and Geraldton, which are all major regional ports (and similar to the Port of Esperance), and the Port of Dampier, which is a major bulk commodity export port (and similar to the Port Hedland Port).

The following sections provide further information on the operations of the Fremantle, Port Hedland and Esperance Ports.

3.2 Port of Fremantle

Operations

The Port of Fremantle comprises two separate operations, the Inner Harbour and the Outer Harbour.

The Inner Harbour handles the majority of Western Australia's container trade. The Inner Harbour also handles break-bulk vessels, livestock exports and motor vehicle imports, and accommodates cruise ships and visiting naval vessels.

The Outer Harbour is situated 15 kilometres south of Fremantle at Kwinana (on the shores of Cockburn Sound). It is one of Australia's major bulk cargo ports handling grain, petroleum, liquid petroleum gas, alumina, mineral sands, fertilisers, sulphur, pig iron and other bulk commodities.

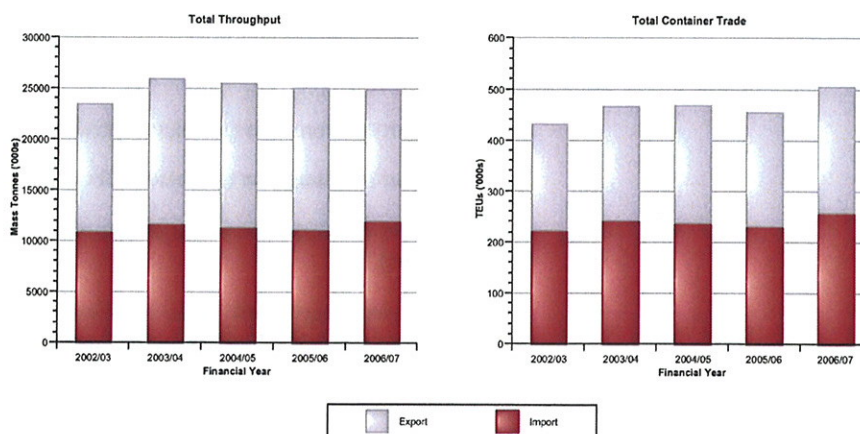
The Port of Fremantle is one of the top ten busiest ports in Australia by throughput. It handles approximately three quarters of Western Australia's imports and 90 per cent of the State's general cargo and containerised trade.

Growth in total throughput at the Port of Fremantle has been relatively stable in recent years – averaging 1.7 per cent per annum over the period from 2002-03 to 2006-07. Growth in containerised trade at the Port of Fremantle has been greater, averaging 4.2 per cent per annum over the past five financial years (Figure 3.1) and 9.5 per cent on average over the past 16 years.

Responsibility for the overall management of the Port of Fremantle lies with the Fremantle Port Authority, which trades as Fremantle Ports. It is a commercialised government owned statutory authority.

Figure 3.1

TRADE STATISTICS, PORT OF FREMANTLE



Source: AAPMA (2008)

Port Infrastructure

The infrastructure of the Inner and Outer Harbours is in part owned and operated by the Fremantle Port Authority and in part owned and operated by private parties.

Inner Harbour

The Inner Harbour facilities are located on the northern side of the Swan River (North Quay) and on the southern side (Victoria Quay) (Figure 3.2).

Figure 3.2

PORT OF FREMANTLE — INNER HARBOUR

Source: Fremantle Port Authority.

North Quay is used for container shipping, with land used for container handling and general stevedoring activities.

DP World and Patrick provide stevedoring services and container terminals at North Quay for the handling and storage of containers. DP World operates a twin lift and two single lift container cranes, each with a lifting capacity of around 65 tonnes. Patrick operates three single and/or twin lift cranes with a lifting capacity of 75 to 80 tonnes. The two container terminals are located at Berths 4-10 and together provide 1,100m of heavy-duty berth for container shipping.

In addition to the container terminals, North Quay provides 811 metres of common user wharf at Berths 1, 2, 11 and 12. The common user wharf is used for the handling of non-containerised and break-bulk trades such as steel products, scrap metal, livestock, machinery and motor vehicles. Berths C to H on Victoria Quay are also common user berths and are used for general cargo (including motor vehicles) cruise ships and naval ships. The lower level of the Fremantle Passenger Terminal and the stacking areas adjacent to Berths E, H and J provide space for importation of motor vehicles. Most of the 100,000 new motor vehicles currently imported through Fremantle each year are handled over Victoria Quay.

While the Common User berths are managed by the Fremantle Port Authority, operations at these berths are conducted by a range of companies. Shipping lines and agents are free to engage any stevedoring company to carry out stevedoring activities at any of the common user berths in the Inner Harbour providing that the stevedoring company has entered into a Common User Stevedoring Agreement with the Fremantle Port Authority. Such agreements set out basic safety, environmental and other operational requirements.

Outer Harbour

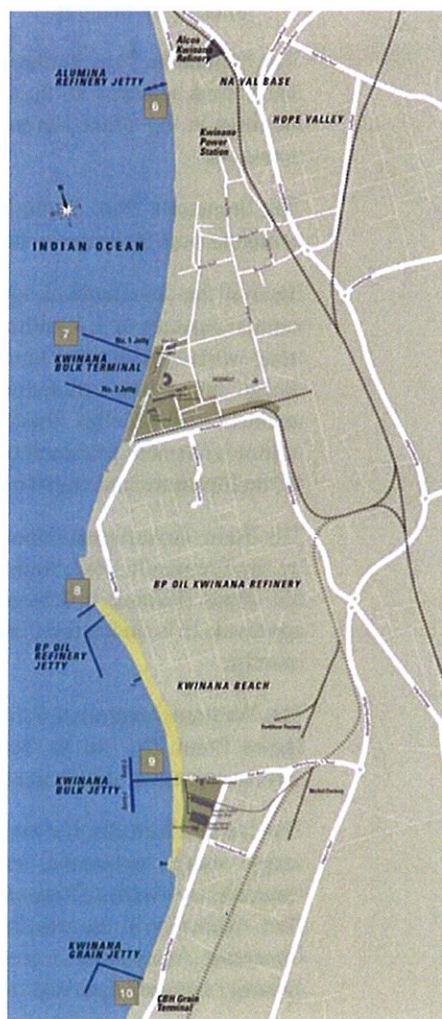
Facilities in the Fremantle Outer Harbour are owned and/or controlled by the Fremantle Port Authority or private sector operators. In both cases, the Fremantle Port Authority is responsible for managing the interface of the facilities with the port waters, which are vested in the Fremantle Port Authority.

The Fremantle Port Authority owns and operates the Kwinana Bulk Jetty and the Kwinana Bulk Terminal in the Outer Harbour (Figure 3.3).

The Kwinana Bulk Jetty has two berths, Kwinana Bulk Berths 3 and 4. The berths are used by ships unloading bulk products such as fertiliser and sulphur, but also provide facilities for various types of liquid bulk commodities, including petroleum. Kwinana Bulk Berth 3 is equipped with a “grab unloader” with a maximum working capacity of 500 tonnes per hour. Kwinana Bulk Berth 4 is equipped with a continuous unloader with a capacity of 17,000 tonnes per normal working day. “Grabs” and “hoppers” are also available for hire for geared vessels.

The Kwinana Bulk Terminal Jetty accommodates ships loading and unloading bulk products such as cement clinker, mineral sands, silica sands and various other commodities. The berth has two unloaders with a combined unloading rate of about 900 tonnes per hour (depending on product type) and a loader with a maximum loading rate of 2300 tonnes per hour.

Figure 3.3

PORT OF FREMANTLE — OUTER HARBOUR

Source: Fremantle Port Authority.

In addition to the facilities provided by the Fremantle Port Authority, the Outer Harbour contains the following private facilities that are included in this review.

- A jetty that is owned and operated by Alcoa World Alumina Australia Limited. This jetty accommodates ships unloading bulk caustic soda and loading refined alumina. The jetty is equipped with a belt conveyor system specially designed for the loading of refined bulk alumina.
- A jetty that is owned and operated by BP Oil and accommodates tankers loading and unloading bulk petroleum products from the adjacent Kwinana refinery.

- A jetty that is owned and operated by CBH and supports the loading of bulk grain. CBH exports an average around 4 million tonnes per annum of bulk grain from this jetty.

The Fremantle Port Authority has a number of tenants in the Outer Harbour that lease areas adjacent to the cargo handling facilities. The Fremantle Port Authority facilities in the Outer Harbour are linked by rail to the interstate and intrastate rail networks.

The Fremantle Port Authority has proposed two options for the building of new container port facilities in the Port of Fremantle Outer Harbour.

Each of the development options proposed by the Fremantle Port Authority has an annual capacity of 1.4 million containers and is designed to handle the overflow of trade when Fremantle's Inner Harbour reaches capacity. The first option is an island design about one kilometre offshore, linked by an open spanned bridge to an extension of Rowley Road (which is north of the Alcoa refinery). The second option is located just south of the Alcoa refinery, and involves both the reclamation of the foreshore and an island component.

The State Government announced in late 2007 that the two options being proposed by the Fremantle Port Authority for the building of new container port facilities in the Outer Harbour had been approved to proceed to planning and environmental approval. It is understood that the statutory approvals process could take about 30 months.

The Western Australian Government has also signed an Operating Agreement with James Point Pty Ltd in December 2000 for the construction and operation of a private container and general cargo port north of James Point, Kwinana.

The James Point Pty Ltd stage 1 port proposal consists of a reclaimed land-backed cargo wharf, associated cargo handling facilities and an off-shore breakwater, immediately north of the existing bulk handling jetties owned by The Fremantle Port Authority in an area known as Barter Road Beach in Cockburn Sound. The Operating Agreement is conditional on, among other things, James Point Pty Ltd gaining relevant approvals including environmental and planning.

Stage 2 of the James Point proposal would be located at the southern end of Cockburn Sound and immediately north of James Point. James Point proposes to reclaim about 100 hectares of seabed and to construct about 1.3 kilometres of berths (including three container berths and one general purpose berth or four container berths).

The James Point port will not be part of the existing Port of Fremantle Outer Harbour, and consequently is not addressed in this review.

Port and related infrastructure services

Vessel movements

Port of Fremantle regulations apply to all waters within the limits of the port; this includes waters of both the Inner and Outer Harbour. The Fremantle Port Authority Harbour Master determines vessel movements into both harbours.

Decisions on vessel movements are made in accordance with the Harbour Masters' Rules, which determine priority generally on a 'first come, first served' basis subject to 'availability and suitability' criteria.

Land management

Land in the Inner Harbour used for port operations at North Quay and Victoria Quay is owned freehold by the Fremantle Port Authority. The container terminal operations of DP World and Patrick are undertaken on land leased from the Fremantle Port Authority under long-term lease arrangements.

Land leasing arrangements in the Inner Harbour provide for rents to be set at current market rental values determined by a licensed valuer. Rental agreements contain clauses that stipulate requirements to undertake regular rental reviews of land values and to make annual adjustments to rental values in accordance with inflation. It is also standard practice for the Fremantle Port Authority to seek expressions of interest through public requests before making a final decision on the successful lessees.

The Fremantle Port Authority provides basic infrastructure on common use land and access to such land is controlled through licences.

Port services

The Fremantle Port Authority is responsible for:

- the maintenance of shipping channels, navigation aids, cargo wharves, road and rail infrastructure within the port area, moles and seawalls, and other port infrastructure;
- port planning, ship scheduling and berth allocation, port communications, pilot transport, mooring, security services and emergency response services; and
- customer information and advice, trade facilitation, port promotion and property services.

The majority of the port and infrastructure facility services in the Port of Fremantle are provided by the private sector. These services include container terminal stevedoring, break bulk and general stevedoring, mooring at some privately owned facilities, towage and pilot services. A number of these services are provided under lease, licence or other contractual arrangements with the Fremantle Port Authority.

3.3 Port of Esperance

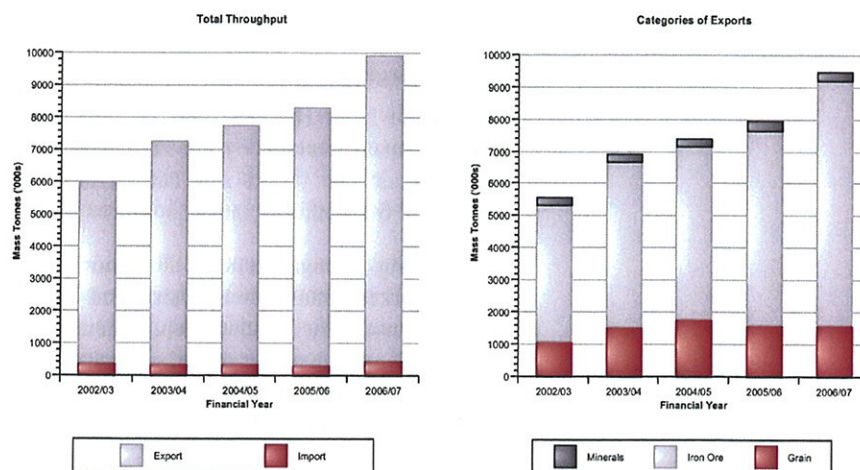
Operations

The Port of Esperance is situated on the south coast of Western Australia, half way between Albany and the South Australian border. It primarily handles bulk cargo, such as iron ore, nickel, grain and fertilisers. The Port of Esperance also has container-handling facilities.

The Port of Esperance is largely an export port, and iron ore accounts for the majority of its exports (Figure 3.4).

Figure 3.4

TRADE STATISTICS, PORT OF ESPERANCE



Source: AAPMA (2008)

Total throughput at the Port of Esperance has increased by an annual average rate of 13.6 per cent from 2002/03 to 2006/07. Containerised trade accounts for a relatively small proportion of total port throughput. However, the Esperance Port Authority forecasts strong growth in containerised trade in the future.

Port Infrastructure

The Port of Esperance consists of two land-backed berths, with a combined berth face of 457 metres. A third berth is located on the main breakwater.

Almost all port-related infrastructure is owned and operated by the Esperance Port Authority, including:

- a bulk ore loader that is situated on the Number 2 Berth;
- a fuel pipeline on the Number 2 Berth;
- a travelling ship loader on the Number 3 dolphin-type Berth; and
- stockpile areas and shed space within the port area that may be made available by the port authority to port users.

The only privately owned and operated infrastructure is a grain loader, which is operated by CBH at Number 1 Berth.

Port and related infrastructure services

Vessel movements

The Esperance Port Authority's Harbour Master is responsible for the management and control of vessels into and out of the harbour. Vessel berth priority is determined in accordance with the Port Information Guide for Ship's Masters, and is generally on a 'first come, first serve' basis as determined at the time that vessels tender their *notice of readiness* to the Harbour Master. Within this framework, priority is also given to vessels that require tide for sailing (EPA, 2007b).

Land management

The land occupied by the Port of Esperance is Crown land vested in the Esperance Port Authority. The Esperance Port Authority currently operates berthing and infrastructure facilities at Berths 2 and 3. Berth 1 is currently leased to CBH.

Port services

All port services are provided by the Esperance Port Authority, with the exception of towage (currently provided by Mackenzies Tug Service under a non-exclusive licence that is regularly put to competitive tender) and the CBH grain loading facility.

3.4 Port Hedland Port

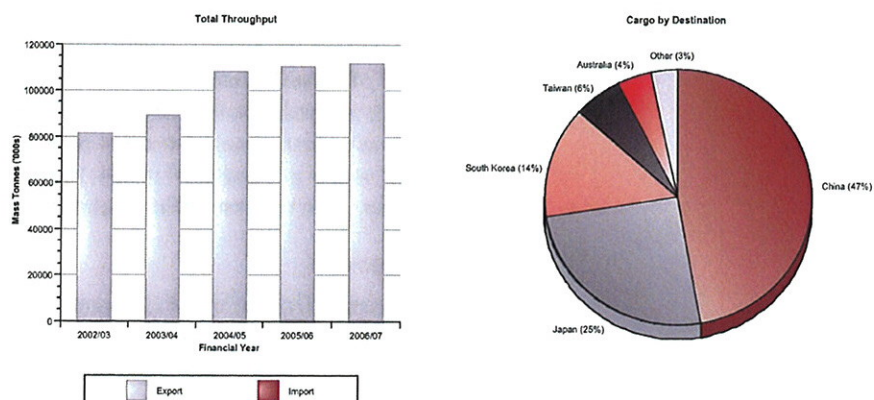
Operations

Port Hedland Port is located on the central north coast of Western Australia, 1,322 kilometres from Perth. It exports high volumes of bulk cargo, including iron ore, salt, manganese, chromite, and copper concentrates. Imports to Port Hedland include fuel oils, sulphuric acid, general cargo and break bulk cargo.

Port Hedland Port is Australia's and Western Australia's second largest individual tonnage port. In 2006-07, total throughput at the port was 112 million mass tonnes; 99 per cent of which were exports (Figure 3.5). Iron ore is the dominant cargo exported (accounting for 95 per cent of total export tonnage). Total throughput has increased by an annual average rate of 8.4 per cent over the period from 2002-03 to 2006-07.

Figure 3.5

TRADE STATISTICS, PORT HEDLAND PORT



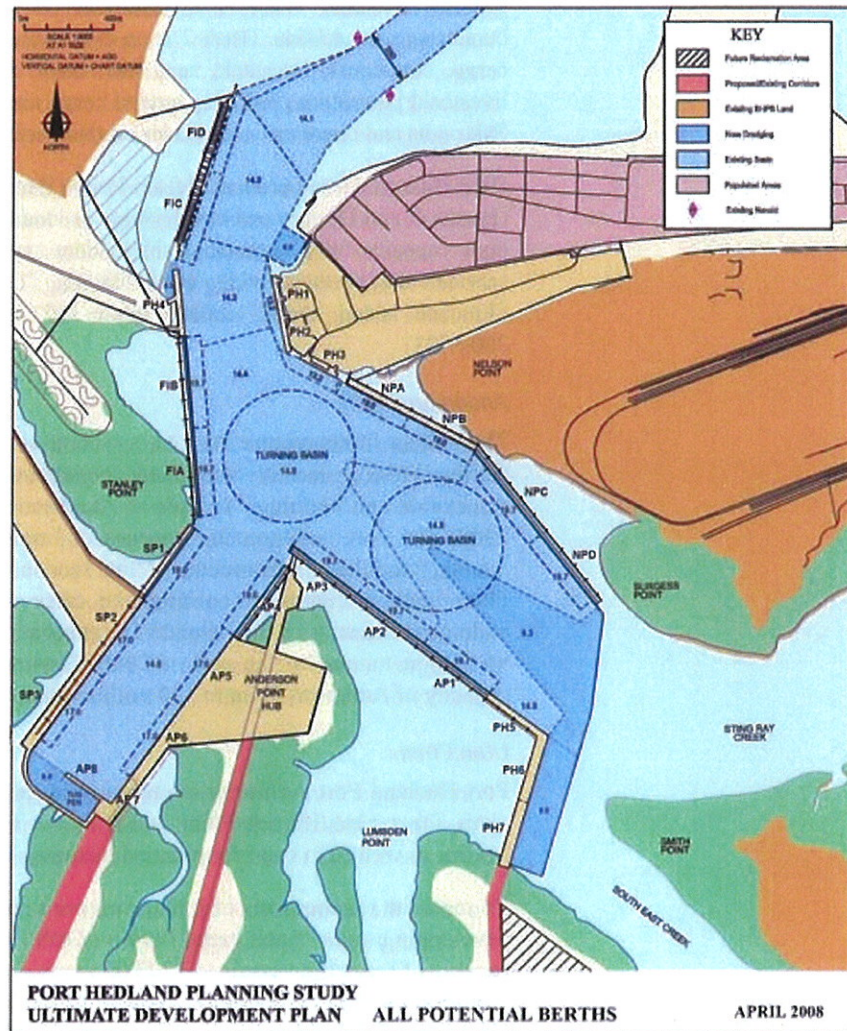
Source: AAPMA (2008)

Port infrastructure

Responsibility for the management of Port Hedland Port lies with the Port Hedland Port Authority. Port Hedland Port consists of separate port infrastructure at the Inner Harbour (owned by Port Hedland Port Authority and BHP Billiton), Anderson Point (owned by The Pilbara Infrastructure Pty Ltd) and Utah Point (owned by the Port Hedland Port Authority) (Figure 3.6).

Figure 3.6

PORT HEDLAND PORT AUTHORITY MAP



Source: Port Hedland Port Authority

Inner Harbour

There are eight berths operating within the Inner Harbour. Three berths are owned and operated by the Port Hedland Port Authority. BHP Billiton Iron Ore owns and operates four berths (two at Nelson Point and two at Finucane Island) and there is a loading berth at Anderson Point that is owned and operated by TPI.¹

¹ There is also a layby berth at Anderson Point.

Port Hedland Port Authority's Berth 1 is used for bulk products such as manganese, copper concentrate, chrome and feldspar, petroleum products, acid, containers and general livestock. There is a shiploader on the berth, and it is equipped with bunkering and utilities. Berth 2 is an extension of Berth 1, and is used for general cargo, containers, livestock, acid and heavy lifts. Berth 3 is used for bulk salt, livestock, petroleum products, general cargo and acid. Rio Tinto Minerals Dampier Salt owns and operates a shiploader on this berth.

BHP Billiton's two berths at Nelson Point (Berths A and B) and at Finucane Island (Berths C and D) are used exclusively for loading iron ore. Two 10,000 tonnes per hour capacity fully retractable shiploaders are located at Nelson Point, and can service either berth allowing double loading. Tonnage through the Nelson Point and Finucane Island berths totalled about 107 million tonnes in 2006-07 (PHPA, 2007:72)

Anderson Point

The Pilbara Infrastructure Pty Ltd, a wholly-owned subsidiary of Fortescue Metals Group (FMG), recently completed construction and commissioning of iron ore stockyards and berthing facilities at Anderson Point. Shipping began on 15 May 2008. The port infrastructure consists of train unloading, ore blending and ship loading facilities. Construction of the second berth is underway. The Anderson Point berth is currently configured to carry 45 million tonnes per year though additional capacity to be installed is expected to bring annual capacity to around 95 million tonnes by the end of 2009. Beyond 2009, TPI plans to increase the capacity of Anderson Point to 120 million tonnes per year.

Utah Point

Port Hedland Port Authority is presently investigating common user development plans for a Utah/Harriet Point wharf to overcome congestion at its 1, 2 and 3 Berths, as well as to cater for planned increases in trade volumes.

To meet the requirements of junior iron ore miners, Port Hedland Port Authority is developing a new "small cape" berth at Utah Point to the western side of the port, capable of servicing vessels to 120,000 tonne deadweight with a capacity of around 18 million tonnes per annum. Dredging of the berth pocket was completed in May 2007. Detailed design and an environmental review processes are in progress and it is envisaged that the berth will be operational during the first half of 2010.

The new Utah Point berth will facilitate exports of junior iron ore miners, and free-up capacity at the existing Port Hedland Port Authority berths allowing for an expansion in general cargo, containers, oil and acid imports, as well as copper and zinc concentrate exports.

Future Outer Harbour development

Demand for Australian iron ore over the next ten to twenty years is predicted to increase. To meet the throughput demand of the iron ore majors, Port Hedland Port Authority is investigating developing an outer harbour offshore from Finucane Island as an alternative to developing a new port at Ronsard Island (85 kilometres from Port Hedland). The new harbour has not yet been approved, but if constructed would have a capacity of around 400 million tonnes per annum.

Port and related infrastructure services*Vessel movements*

Berthing priority is generally given on an order-of-arrival basis. The Port Hedland Harbour Master may vary the berthing sequence in the event of conflicting requirements.

Land management

The bulk of land surrounding the port is Crown land vested in Port Hedland Port Authority, which leases land to other parties. Port Hedland Port Authority indicates that leasing rates for port land are linked to market rates though it may lease land at less than market rates to facilitate trade. Significant leases of areas of abutting the port have been created under State Agreement Acts, with a number also being issued under the *Land Administration Act 1997*.

Port services

Services provided by the Port Hedland Port Authority include:

- maintenance of 'navigational markers and aids, wharves, cargo sheds, roads and all ancillary facilities necessary for the effective operation of the port';
- compulsory pilot services ;
- port planning, ship scheduling and berth allocation, and security services; and
- electricity, fresh water and diesel supply services.

Services provided by the private sector include:

- stevedoring as currently provided by two private parties under non-exclusive licenses;
- tug services as currently provided by Teekay under a non-exclusive licence; and
- line boat services are provided by private contractors under a non-exclusive licence.

The scope of work for the current review includes the regulation of Port of Port Hedland, including the berths of The Pilbara Infrastructure, but excluding the BHP Billiton facilities and the Outer Harbour proposal. The BHP Billiton facilities are excluded as they are currently subject to proceedings to determine whether they are part of an integrated production facility. The Outer Harbour proposal is only at concept planning stage and therefore excluded from this review.

Chapter 4

Current Economic Regulation of Ports and Port Services

4.1 Introduction

The three significant ports in Western Australia that are being reviewed under Clause 4.3 of the CIRA are each operated by a port authority that is commercialised government-owned entity.

The port authorities have functions and powers established under the Western Australian *Port Authorities Act 1999*. The port authorities are also subject to accountability mechanisms established by the Western Australian Government.

Regulation of access to port facilities and port services exists only under the generic access law of Part IIIA of the *Trade Practices Act* (which has not been applied, to date, to ports or port services) and specific access legislation for grain-handling facilities.

4.2 Port Authorities Act 1999

Coverage

Section 24 of the *Port Authorities Act 1999* defines a port as an area or areas described by an order made by the Governor that is published in the Government Gazette. Although infrastructure facilities and/or infrastructure facility services may be provided by a port authority or by another party, section 30 provides for a port authority to have exclusive control of a port, subject to any direction given by the responsible Minister (in this case the Minister for Transport).

Ultimately all activities within a defined port, whether undertaken by a port authority or not, are substantially controlled by the port authority.

Structure, governance and accountability

The *Port Authorities Act 1999* requires that each port authority have a board appointed by the Minister to govern its operations, and perform the functions, determine policies and control the affairs of the port authority. In the case of the Port Hedland Port Authority (and the Dampier Port Authority), the *Port Authorities Act 1999* allows for the boards to include two members nominated by specified resource companies.

Each port authority has a Chief Executive Officer, who, subject to the control of the board, is responsible for, and has all the powers needed to administer, the day-to-day operations of the Port Authority.

Port authorities are required to annually negotiate and agree a statement of corporate intent and a strategic development plan with the Minister. Statements of corporate intent address the port authority's performance objective for a single financial year. Strategic development plans are confidential business planning documents that cover a five year period. Matters that must be addressed in each of these documents are set out in the *Port Authorities Act 1999*. Prior to agreeing to these two documents, the Minister is required to obtain the Treasurer's concurrence.

Port authorities are required to report on their performance on a half-yearly basis to the Minister and the Treasurer so that their performance against targets can be monitored. Port authorities must also prepare an annual report on performance against the targets set out in their statements of corporate intent.

The Minister has the right to access information and to issue directions to a Port Authority, with any Ministerial directions required to be tabled in parliament.

Functions and duties

Section 30 of the *Port Authorities Act 1999* establishes the functions of port authorities as being to:

- facilitate trade within and through the port and plan for future growth and development of the port;
- undertake or arrange for activities that will encourage and facilitate the development of trade and commerce generally for the economic benefit of the State through the use of the port and related facilities;
- control business and other activities in the port or in connection with the operation of the port;
- be responsible for the safe and efficient operation of the port;
- be responsible for the maintenance and preservation of vested property and other property held by it; and
- protect the environment of the port and minimise the impact of port activities on that environment.

Section 33 and 34 of the *Port Authorities Act 1999* require that port authorities, in performing these functions, have a duty to:

- perform their functions in accordance with their strategic development plans and its statements of corporate intent as exist from time to time; and
- act in accordance with prudent commercial principles, and endeavour to make a profit.

Finally, the *Port Authorities Act 1999* requires that duties imposed by strategic development plans and statements of corporate intent prevail in instances where there is conflict between that duty and the duties to act in accordance with prudent commercial principles and to endeavour to make a profit.

Pricing

The *Port Authorities Act 1999* gives port authorities the power to levy fees for licences and approvals (provided for in regulations) and impose port charges as the Port Authority determines.

Government policy introduced in July 2000 requires ports to achieve a return on assets of between five and eight per cent.² Port authorities generally report on the actual rate of return achieved each year in their annual reports.

Access to port facilities and services

The *Port Authorities Act 1999* does not address access to ports or to infrastructure or infrastructure services owned or controlled by the port authority. However, in a number of cases a 'right' to access certain port and port related infrastructure is established under other legislation or agreements. These are as follows.

- General rights of a party to seek access to port facilities or services exist under the generic access regulation laws under Part IIIA of the *Trade Practices Act 1974*. Currently, no Western Australian port, port owned or controlled infrastructure, or infrastructure services provided at a port, is subject to access regulation under Part IIIA.
- The *Western Australian Bulk Handling Act 1967* requires that CBH allow any party to use the bulk handling facilities and equipment controlled by it at ports in the State on the payment of a (prescribed) charge. That is, access to CBH's facilities at Western Australian ports are essentially available on a 'common user' basis, although there are no provisions in the *Bulk Handling Act 1967* that govern the manner in which terms or prices of access are to be determined.
- The Commonwealth *Wheat Export Marketing Act 2008* requires port facilities operated by bulk handling companies, such as CBH, that are also accredited as wheat marketers under the Act to satisfy an 'access test'. A limitation of the *Wheat Export Marketing Act 2008* is that the access test will apply *only* to export terminals that are operated by an accredited wheat marketer, and only in relation to the export of wheat.
- The *Railway and Port (The Pilbara Infrastructure Pty Ltd) Agreement Act 2004* requires TPI, a wholly owned subsidiary of FMG, to have in place an access regime approved by the portfolio Minister that provides for access to TPI's port facilities (and any additional infrastructure) constructed under the Agreement.

The *Port Authorities Act 1999* allows port authorities to issue licences and administer licensing schemes. However, a port authority must obtain the Minister's approval before it can issue an exclusive licence to provide port services, and the Minister may not approve such a licence unless the public benefits exceed the public costs. On approving an exclusive licence, the Minister is also required to table the reasons for approval in Parliament.

² Government policy introduced in July 2000 requires port authorities to report a rate of return on non-current assets that have been valued based on their Deprival Value. This measure quantifies the rate of return earned on average current and non-current assets of a port.

4.3 Port Authority Regulations

The *Port Authorities Regulations 2001* deal with a range of matters including:

- the keeping of records of vessels, goods and cargo;
- the loading and unloading of goods and cargo;
- the conduct of persons within ports;
- the use of vehicles in ports;
- the approval and licensing of pilots, requirements in relation to pilot services, and pilot charges; and
- requirements for licensing of parties (other than the port authorities themselves) undertaking certain activities including towage services, line boat services, bunkering services, stevedoring services and mooring services.

Chapter 5

CIRA clause 4.1 – Justification for Economic Regulation

5.1 Introduction

Clause 4.1 of the CIRA states that ports should only be subject to economic regulation where a clear need for it exists in the promotion of competition in upstream or downstream markets or to prevent the misuse of market power.

In this chapter, consideration is given to whether there is justification for economic regulation of port and port services within the requirements of clause 4.1, and in particular:

- whether economic regulation of port authorities and/or private sector operators of port and related infrastructure facilities would increase competition in upstream and downstream markets; and
- whether regulation is needed to prevent port authorities and/or private sector operators of port and related infrastructure facilities from misusing market power.

5.2 Economic regulation

Economic regulation can be used to establish rights of access to infrastructure or services (access regulation) and to facilitate negotiation of the terms of access including, at an extreme, setting prices that may be charged for goods or services (price regulation).

Access regulation establishes a right of access for prospective users of a facility or service by requiring facility owners (typically owners of monopoly infrastructure) to negotiate access terms and conditions with access seekers. Access regulation typically provides access seekers with a resort to independent arbitration of terms and conditions of access in circumstances where negotiations between access seekers and facility owners fail to reach mutually agreeable outcomes.

Price regulation may form part of a regime for access regulation and can involve a range of levels of intervention from price monitoring to the setting of regulated prices. Price regulation involves governments intervening in markets to influence or establish prices that can be charged for goods, services or access.

5.3 Upstream and downstream markets

There are two sets of markets relevant to a consideration of regulation of ports and port services.

- The first set of markets comprises the downstream market for port services. Parties with access to ports land and the basic infrastructure and facilities of ports are able to provide port services. Port services include stevedoring, pilot services, tug and towage services, and line and mooring services. The providers of these services typically operate from within the port facility and utilise space and basic infrastructure services provided by the port owner.
- The second set of markets comprises the upstream and downstream markets that depend upon the provision of port services. These would include markets for shipping services and the upstream and downstream markets for products that are transported from and to markets via the shipping services. For the ports of Fremantle, Esperance and Port Hedland, the upstream and downstream product markets comprise markets for goods transported by containerised freight, markets for grain and markets for iron ore and other mineral commodities.

There are two ways in which economic regulation may be used to increase competition in the upstream and downstream markets of port and related infrastructure facilities.

First, economic regulation can be applied to owners of port infrastructure. Regulation would oblige infrastructure owners to provide port-service providers with access to land within the port facility and to the basic infrastructure of the port. The ultimate objective of such a form of regulation would be to increase competition in the market for port services.

Second, economic regulation can be applied to port-service providers. Regulation would be used to require the service providers to provide services to all parties (that may or may not include themselves) in a non-discriminatory manner and to prevent the charging of monopoly prices for the services provided. The ultimate objective of such a form of regulation would be to increase competition in the related markets for shipping services and for the goods transported through the ports.

In each case, economic regulation is only justifiable on economic grounds in particular circumstances where a number of criteria are met.

5.4 Circumstances that might justify economic regulation

Economic regulation may be effective in increasing competition in the market for port services in circumstances where:

- participants in the related market are dependent on access to the facility or service; and
- the provider of the facility or service has market or monopoly power that results from natural monopoly characteristics in the facility or service or barriers to entry to the market for the facility or service; and
- the provider of the facility or service is a vertically integrated business that will benefit from restricting access of other businesses to the facility or service.

These are further described as follows.

Dependence on access to the facility or service

For there to be a case for economic regulation to increase competition in a related market, it needs to first be established that participants in the related market are dependent on access to the facility or service that is the subject of regulation. That is, there are no practical substitutes for the facility or service.

Monopoly position

For the provider of a facility or service to be able to restrict competition in a related market, the provider must necessarily have a degree of market or monopoly power. Economic regulation is not warranted where there is actual or potential competition amongst a number of providers of the facility or service. In such a case, the providers of the facility or service would not hold market power and would have no ability to restrict access or charge monopoly prices.

A position of market power in the market for a facility or service results from either natural monopoly characteristics of the facility or service or the existence of barriers to entry to the market for the facility or service, coupled with an absence of countervailing market power by the user of the facility or service.

A natural monopoly exists where a single facility or service provider is able to service market demand at a lower total cost than two or more facilities or service providers. Where the provision of a facility or services is a natural monopoly, the incumbent provider will typically have a cost advantage over any potential new entrant and is able to exploit this cost advantage to restrict entry to the market for the facility or service and, having done so, exploit a position of market power.

Barriers to entry to the market for provision of a facility or service can comprise physical, legal or financial barriers. Physical barriers to entry typically arise from a lack of space that prevents new players from entering a market. For example, if a port only has sufficient berth and storage space to cater for one stevedore then competition within the stevedore market will be limited by a physical barrier to entry. Legal barriers to entry arise in cases where legislation limits new players from entering a market. For example, Australia Post operates in a market where there are legal barriers to entry as it is the only company that is legally allowed to deliver mail that is below a certain weight or value. Financial barriers to entry exist in circumstances where the upfront costs in getting established in a new market are high enough to deter market entrance. Typically financial barriers to entry occur in industries where upfront capital costs are high and there are significant economies of scale in operations. Existing players in such markets are able to operate effectively at a large scale so that average costs are low.

The existence of a natural monopoly or barriers to entry will translate into market power where there is an absence of countervailing market power on the part of the user of the facility or service. Countervailing market power can be held by users of a natural monopoly facility or service provider and if this is the case then the market power of the natural monopoly facility or service provider will be limited.

Vertical integration

A vertically integrated entity controls several steps in the production or distribution of a product or service. Vertically integrated entities may have an incentive to restrict access to services to third parties so as to protect their own interests in an associated up-stream or down-stream business. Where vertically integrated entities do not exist, there is less possible incentive for infrastructure owners to restrict access to the relevant facility or service.

5.5 Port facilities

In the context of this review, the relevant providers of port facilities are the Fremantle Port Authority, the Esperance Port Authority and the Port Hedland Port Authority. The objective of the review under clause 4.1 of the CIRA is to determine whether the regulation of the providers of port facilities is necessary to either prevent the misuse of market power or promote competition in upstream or downstream markets.

The potential benefits of economic regulation of port facilities are assessed in this review by consideration of the markets for the particular port services for which competition could be increased and noting whether the circumstances exist that suggest that there could be benefits of applying economic regulation to the providers of port facilities. This is undertaken by considering the use of port facilities by participants in the markets for port services that include providers of:

- shipping services;
- stevedoring services;
- pilot services;
- tug and towage services; and
- line and mooring services.

It is found that for the Fremantle, Port Hedland and Esperance Ports that there are no instances where regulation of providers of port facilities is required to either prevent the misuse of market power in the provision by the port authorities of port facilities or to increase competition in the downstream markets for these port services.

The analysis supporting this finding is set out for each of the categories of port services as follows.

The market for shipping services

Across Australia, it is estimated that nearly 100 shipping companies provide scheduled services to Australian ports (PWC, 2007)

A number of different shipping service providers use the ports of Fremantle, Esperance and Port Hedland. Ship timetable information available for the Port of Fremantle shows that between 19 September and 30 September 2008, there were 35 scheduled ship arrivals (excluding cruise ships) from 14 different shipping companies. A large number of different shipping companies also service the ports of Esperance and Port Hedland.

Port infrastructure that is provided to shipping companies includes berth space to allow for the berthing of ships and loading and unloading of freight, as well as navigation infrastructure to provide safe access to berth space. Access to a dredged port channel is also provided to shipping companies as are amenities such as fuel and water.

Dependence on port facilities

Shipping service providers are dependent upon obtaining access to shipping channels, berths and other port infrastructure. However, there is some degree of competition between ports to secure ship visits and this element of competition limits the dependence that providers of shipping services have on the infrastructure of any particular port.

Container importing ships that arrive in Australian waters often have to make several stops to unload cargo at different ports and it can be the case that a scheduled stop at one of Australia's five major container ports (Brisbane, Sydney, Melbourne, Adelaide and Fremantle) is deleted from the ship's schedule in which case any excess cargo can be unloaded at another of the scheduled stops and railed or trucked to the appropriate destination. Improvements in land transport efficiency in recent years have led to a considerable reduction in inland transport costs and increased the potential degree of competition between ports (Essential Services Commission, 2004).

Freight can be railed or trucked between the eastern states and Western Australia at rates that are competitive with transport by sea. It is estimated that approximately 20 per cent of the freight tonnage that is moved between Perth and the eastern states is carried by sea and the remainder of this interstate freight task is serviced by road and rail (Bureau of Transport and Regional Economics, 2001). As such, providers of shipping services are not totally dependent upon the port facilities of any particular port as competitive substitutes are available to transport freight.

Shipping services for bulk commodities are more dependent upon infrastructure at particular ports. Due to ports being integrated with other (land-side) transport and storage infrastructure, ports cannot generally substitute one for another in providing shipping services of these commodities and, at least in reasonable time frames, the shipping services are therefore dependent upon the infrastructure of particular ports.

However, there may be competition between ports at the start of particular projects, where proponents attempt to optimise supply chains and individual port authorities compete to facilitate that outcome through the establishment of dedicated infrastructure or equipment. Under those circumstances, once the port is selected, bulk trades usually become captive to that port. Competition between ports may also occur where the relative location of different ports provides no competitive advantage and the ports have similar necessary infrastructure and equipment or where no specialist infrastructure or equipment is required.

Market power held by providers of port facilities

There is no evidence to indicate that port authorities either hold market power over shipping service companies or have misused market power to the disadvantage of shipping companies.

The Fremantle Port Authority submitted to this review that it actively markets its port facilities to attract new shipping lines and new exports so as to add competition in upstream and downstream markets. The Fremantle Port Authority also submitted that even if it were to hold market power it would have no incentive to exercise market power as it is not required or encouraged to maximise profits but is only required to earn a minimum rate of return on the value of its assets³ (Fremantle Ports submission, 2008).

An exploitation of market power would be contrary to Fremantle Port's statutory functions. Section 30 of the *Port Authorities Act 1999* states that the functions of the port authorities are to, *inter alia*:

- facilitate trade within and through the port and plan for future growth and development of the port; and
- undertake or arrange for activities that will encourage and facilitate the development of trade and commerce generally for the economic benefit of the State through the use of the port and related facilities.

The Fremantle Port Authority also commented on the countervailing market power of shipping lines. Countervailing market power arises where concentration on the supply side of a market (in this context, the market for port facilities) is balanced by concentration on the demand side (in this context, the market for shipping services). Through size and commercial pressures buyers in some markets are able to counter the market power of suppliers. According to the Fremantle Port Authority, the market power that is held by shipping lines ensures that they 'obtain a reasonable price for services provided'. Shipping lines are able to compare prices obtained at other ports and exert pressure on ports to be competitive if they want to retain visits from ships (Fremantle Ports submission, 2008).

There is no reason to expect that the market conditions at the Port of Fremantle for use of port facilities by shipping services would not also hold at Esperance and Port Hedland, and no submissions were provided to this review indicating that this is not the case.

Vertical integration of providers of port facilities

Port authorities in Western Australia do not provide shipping services. With no vertical integration there is no associated incentive for the port authorities to restrict the ability of shipping companies to access port facilities.

Conclusions

There is no *prime facie* evidence to suggest that economic regulation of access to port facilities would increase competition in markets for shipping services or that there is a need for such regulation to prevent misuse of market power by the port authorities.

- Any market power that might be held by the port authorities over providers of shipping services may be limited by countervailing market power of shipping companies and possibly, for container freight, by competition between ports.

³ The Fremantle Port Authority is required to 'endeavour to make a profit' under section 34 of the *Port Authorities Act 1999* but is also subject to current State Government policy that requires port authorities to target a long-term average rate of return of five to eight per cent.

- The port authorities do not provide shipping services and therefore have no incentive by virtue of vertical integration to restrict access of shipping companies to port facilities.
- Existing policy and regulatory requirements encourage the port authorities to facilitate trade and not to maximise profits. Trade facilitation requirements provide a disincentive for port authorities to limit access to ports or to engage in price gouging.

The market for stevedoring services

Container stevedoring services at the Port of Fremantle Inner Harbour are provided by DP World and Patrick. The two service providers operate under long-term lease agreements held with the Fremantle Port Authority. Break bulk and general stevedoring services in the Inner Harbour are provided by private sector companies operating under non-exclusive Common User Agreements issued by the Fremantle Port Authority. Outer Harbour stevedoring services are provided by the private owners of Outer Harbour facilities (Alcoa, BP and CBH). Stevedoring services at the Kwinana Bulk Jetty and Kwinana Bulk Terminal are provided by the Fremantle Port Authority and private sector companies that operate under Common User Agreements.

The majority of stevedoring activities at the Port of Esperance are undertaken by the Esperance Port Authority. The remaining stevedoring task is serviced by two private stevedoring companies each operating under a licence issued by the Esperance Port Authority.

Stevedoring services at the Port Hedland berths that are owned by the Port Hedland Port Authority are provided by P&O Automotive and General Stevedoring, and Patrick. Both company's operate under three-year licences held with the Port Hedland Port Authority. The Pilbara Infrastructure owns the port's Anderson Point facilities and the company operates its own stevedoring services.

Dependence on port facilities

The provision of stevedoring services at all three ports is dependent on having access to port infrastructure. Stevedores need access to berth space to load and unload containers, container storage space and equipment such as cranes to shift containers.

Market power held by providers of port facilities

A degree of market power would likely be held by the providers of port facilities due to the dependence of stevedoring services on the port facilities. It is expected, however, that this market power is limited by countervailing market power held by large and established stevedoring companies.

DP World and Patrick operate as stevedores at the Fremantle Inner Harbour. Both companies are large businesses in the stevedoring industry. DP World is one of the largest marine terminal operators in the world and Patrick has significant port-related operations around Australia.

The Transport Forum of Western Australia submitted to this review that the two stevedoring companies operating at the Fremantle Port Inner Harbour actually hold a degree of power over the Fremantle Port Authority – the contrary circumstance to that being examined in this review. No evidence is provided to support this statement but the notion of the statement reinforces the idea that stevedores do hold a degree of countervailing market power (at least in the Fremantle Inner Harbour).

Stevedoring operations at Port Hedland are provided by P&O Automotive and General Stevedoring, and Patrick, again both of which are large and established stevedore service providers that would be expected to have substantial countervailing market power against the port authorities.

The absence of large stevedoring businesses at the Port of Esperance could confer some market power on the Esperance Port Authority. However, according to the Esperance Port Authority, there is a lack of market demand among new or existing stevedoring companies in providing more stevedoring services at the port.

No submissions have been made to this review indicating that the port authorities hold market power over companies that currently provide stevedoring services at the ports of Fremantle, Esperance and Port Hedland.

Vertical integration of providers of port facilities

The Esperance Port Authority is vertically integrated as it provides the majority of stevedoring services at the Esperance Port. In principle, the Esperance Port Authority has an incentive to prevent new providers of stevedore services from operating at the Esperance Port. However, there is no evidence that indicates that this has been the case. The Esperance Port Authority is willing to provide new stevedores with access so that they can provide stevedoring services but there is a lack of interest among private sector stevedores in operating at the port due to the relatively small scale of its operations and the isolation of the port.⁴

No submissions have been made to this review to indicate that the Esperance Port Authority have restricted access to new stevedores or have misused its market power in this area.

The Fremantle Port Authority provides stevedore services at the Kwinana Bulk Jetty and Terminal, which are excluded from the scope of the review. Nevertheless, the Fremantle Port Authority also allows other parties to provide stevedore services at the Kwinana facilities.

The Port Hedland Port Authority does not provide stevedoring services.

Conclusions

There is no prime facie evidence to suggest that economic regulation of access to port facilities would increase competition in markets for stevedoring services or that there is a need for such regulation to prevent misuse of market power by the port authorities.

⁴ Esperance Port Authority 2008, personal communication.

The market for pilot services

Fremantle Pilots holds an agreement with the Fremantle Port Authority to provide pilot services at the port (including Inner and Outer Harbour facilities and privately owned facilities). At present, Fremantle Pilots is the only company to hold a pilot services agreement at the Port of Fremantle though the agreement does not grant the company any exclusive rights of service provision. The agreement is periodically subject to market testing and a competitive tendering process.

Pilot services at Port Hedland are provided by the Port Hedland Port Authority. The Authority contracts an independent service provider to provide marine pilot, helicopter services and pilot boat services (the pilot licence at the port is held by one service provider). Calls for tender to provide these services are made at regular intervals and pilot contracting arrangements, including contract prices, are gazetted.

Pilot services at the Port of Esperance are provided by the Esperance Port Authority.

Dependence on port facilities

Pilot services are not necessarily dependent upon facilities or infrastructure provided at the port if there are alternative locations from which to operate.

Market power held by providers of port facilities

Providers of pilot services require the approval of the port authorities to provide the service (granted by way of a licence or a contract) and are therefore dependent on a permission to operate issued by the providers of port facilities. It is possible that this could be used by the owner of the port facility to restrict competition in the market for pilot services.

Any potential market power held by port authorities is limited by the countervailing market power held by providers of pilot services. Pilots are highly skilled and their services are in demand. For example, the pilot company used by the Port Hedland Port Authority is in a strong bargaining position as it has expertise in navigating at the port. It can take up to two years to train new pilots and new pilots can cause disruptions to port operations. Prices charged by the current pilot company have increased markedly in recent years as a result of the strong bargaining position that the company is in and the Port Hedland Port Authority is currently in the process of trying to negotiate pilot rates that are more in line with market rates.

Vertical integration of providers of port facilities

As a provider of pilot services and port facilities, the Esperance Port Authority is vertically integrated. The Authority is reluctant to allow private parties to provide pilot services at the Esperance Port, holding the view that it is able to manage risks far more effectively than were services provided by a third party. The Authority contends that in-house provision of pilot services allows the Authority to control aspects of operations such as pilot training and pilot staff selection and also to ensure reliability of supply of pilot services at the port. This argument may not, however, be sustainable. Other Australian port operators have been successfully able to manage safety and risks whilst contracting out pilot services to third parties.

Conclusions

There is no prime facie evidence to suggest that economic regulation of access to port facilities would increase competition in markets for pilot services or that there is a need for such regulation to prevent misuse of market power by the port authorities.

There is no case for economic regulation to be introduced at the ports of Fremantle, and Port Hedland so as to increase competition in the market for pilot services. Both port authorities put pilot contracts to regular tender and are subject to prevailing conditions in the market for pilot services. Neither organisation holds market power over pilot service providers and neither is vertically integrated in the provision of pilot services.

The Esperance Port Authority is a vertically integrated monopoly provider of pilot services and therefore could have an incentive to restrict competition in the market for pilot services. There is no evidence, however, to suggest that economic regulation to allow for entry of another provider of pilot services would increase competition in the market for these services. There is no evidence that other providers of pilot services would seek to operate at the Port of Esperance if this was possible, given the relatively small number of ships that visit the port.

The market for towage services

Inner Harbour and Outer Harbour towage services at the Port of Fremantle are provided under non-exclusive licences issued by the Fremantle Port Authority. Current towage providers are Adsteam (recently acquired by Svitzer) and Total Harbour Services. Towage licences provide companies with non-exclusive access to port waters as necessary to provide towage services. Additional licences may be issued provided the applicant is able to meet basic safety, service and capability standards.

Towage services at the Esperance Port Authority are provided by Mackenzies Tug Service under a non-exclusive licence issued by the Esperance Port Authority.

Towage services at Port Hedland are provided by Teekay under a non-exclusive licence issued by the Port Hedland Port Authority.

Dependence on port facilities

Towage services are not necessarily dependent upon facilities or infrastructure provided at the port if there are alternative locations from which to operate.

Market power held by providers of port facilities

Providers of towage services require the approval of the port authorities to provide the service (granted by way of a licence or a contract) and are therefore dependent on a permission to operate issued by the providers of port facilities. It is possible that this could be used by the owner of the port facility to restrict competition in the market for towage services.

Notwithstanding this, no submissions made to the review indicated that the port authorities held market power over providers of towage services or misused any such market power.

Vertical integration of providers of port facilities

None of the port authorities provide towage services.

Conclusions

There is no prime facie evidence to suggest that economic regulation of access to port facilities would increase competition in markets for towage services or that there is a need for such regulation to prevent misuse of market power by the port authorities.

The market for line and mooring services

The Fremantle Port Authority provides mooring services in the Port of Fremantle Inner Harbour and at some Outer Harbour facilities in conjunction with other services such as security. Alcoa and BP provide their own mooring services. Line boat services in the Inner and Outer Harbour are provided by Fremantle Launch Company. There are no licences or contracts in place governing the provision of these services.

The Esperance Port Authority is sole provider of line and mooring services operating at the Port of Esperance.

At Port Hedland, line and mooring services are provided by two line boat service companies operating under non-exclusive licenses.

Dependence on port facilities

Line and mooring services are not necessarily dependent upon facilities or infrastructure provided at the port if there are alternative locations from which to operate.

Market power held by providers of port facilities

Providers of line and mooring services require the approval of the port authorities to provide the service (granted by way of a licence or a contract) and are therefore dependent on a permission to operate issued by the providers of port facilities. It is possible that this could be used by the owner of the port facility to restrict competition in the market for towage services.

Notwithstanding this, no submissions made to the review indicated that the port authorities held market power over providers of line and mooring services or misused any such market power.

Vertical integration of providers of port facilities

As the sole provider of line and mooring services and port facilities, the Esperance Port Authority is vertically integrated in the provision of line and mooring services and would have a potential incentive to restrict competition in the market for these services. However, there is no evidence to suggest that economic regulation to allow for entry of another provider of line and mooring services would increase competition in the market for these services. To the contrary, the Esperance Port Authority has indicated that it would like to be able to contract out the provision of line and mooring services to a third party but is unable to do so because the size of the market is not sufficient to support a stand-alone business operation. With 200 ships visiting the port each year, the Esperance Port Authority estimates that the provision of line and mooring services would equate to only about 600 to 650 hours per year of work.

The Fremantle and Port Hedland port authorities are not vertically integrated in the provision of line and mooring services.

Conclusions

There is no prime facie evidence to suggest that economic regulation of access to port facilities would increase competition in markets for line and mooring services or that there is a need for such regulation to prevent misuse of market power by the port authorities.

5.6 Port services

In the context of this review, the relevant providers of port services are the providers of:

- stevedoring services;
- pilot services;
- towage services;
- line and mooring services;
- grain bulk-terminal services; and
- iron ore bulk-terminal services.

The objective of the review under clause 4.1 of the CIRA is to determine whether the regulation of the providers of these services would be effective in either preventing the misuse of market power or promoting competition in upstream or downstream markets.

The relevant markets that are likely to be dependent on the provision of port services are broadly categorised as the markets for the products transported as containerised freight, the markets for grains and the market for iron ore.

The potential benefits of economic regulation of port facilities are assessed in this review by consideration of the relevant markets for which competition could be increased and noting whether the circumstances exist that suggest that there could be benefits of applying economic regulation to the providers of port services. This is undertaken by considering the use of each of the port services by participants in the various markets for containerised freight, grains and iron ore.

It is found that instances where regulation of providers of port services would increase competition in upstream and downstream markets is limited to economic regulation of grain bulk-terminal services. The analysis supporting this finding is set out for each of the categories of port services as follows.

Stevedoring services

At the Port of Fremantle Inner Harbour, container stevedoring services are provided by DP World and Patrick. The two service providers operate under long-term lease agreements held with the Fremantle Port Authority.⁵ Stevedoring services at common user berths at the Port of Fremantle can be provided by any number of private service providers so long as they hold a licence issued by the Fremantle Port Authority. Outer Harbour stevedoring services are provided by the private owners of Outer Harbour facilities (Alcoa, BP and CBH). Stevedoring services at the Kwinana Bulk Jetty and Kwinana Bulk Terminal are provided by the Fremantle Port Authority and private sector companies that operate under Common User Agreements.

The majority of stevedoring activities at the Port of Esperance are provided by the Esperance Port Authority. However, there are also two private stevedoring companies each operating under a licence issued by the Esperance Port Authority.

Stevedoring services at the Port Hedland berths that are owned by the Port Hedland Port Authority are provided by P&O Automotive and General Stevedoring, and Patrick. Both company's operate under three-year licences held with the Port Hedland Port Authority. The Pilbara Infrastructure owns the port's Anderson Point facilities and the company operates its own stevedoring services.

Dependence on stevedoring services

Markets for goods that are traded by sea are dependent on having access to stevedore services to load and unload cargo from ships. Markets for shipping and land transport services are also dependent on stevedore services as are the markets for containerised and bulk goods. There are no effective substitutes for stevedore services within a port.

Market power held by providers of stevedore services

Stevedores operating at the Port of Fremantle common-user berths do not hold market power. Licences to provide stevedoring services at the common use berths are non-exclusive. Barriers to entry to the market are low as licences are readily obtainable and upfront capital costs are modest.

⁵ The current lease agreements end in 2016.

The degree to which stevedores operating at other port facilities hold market power is unclear. A number of factors work to provide market power, including the following.

- Market concentration is high with only two service providers operating at each port.
- Financial barriers to entry are high in the container stevedoring market. Anecdotal information suggests that the minimum cost to equip a new stevedoring service at a major port is approximately \$200 million.
- Physical barriers to entry exist, such as limits on available berth space exist at most ports, including Fremantle, Esperance and Port Hedland.
- Regulatory barriers to entry such as long term lease arrangements exist at some ports.
- Demand for stevedoring services is considered to be highly inelastic primarily because stevedore charges account for only a small proportion of the value of trade. Demand sensitivity is therefore unlikely to be a constraining factor that would inhibit the exercise of market power (Essential Services Commission, 2007).

Factors that may offset any market power held by stevedoring companies include the competition that does exist by two stevedoring firms operating at the ports of Fremantle, Esperance and Port Hedland and also the countervailing market power that is held by large shipping companies. Shipping companies are the direct customers of stevedoring service providers and, given their scale, they may hold significant bargaining power when negotiating with stevedores (PWC, 2007).

Even were stevedores to hold market power, the CIRA only requires that regulation be implemented only if market power is being misused and regulation would promote competition in upstream or downstream markets.

The Transport Forum submitted to this review that a lack of competition in the stevedoring industry had led to an absence of customer focus by the stevedore companies with resultant adverse implications for the road transport industry. The predominant concern raised by the Transport Forum is the length of time that road transport operators are required to wait before gaining access to stevedore facilities to collect containers.

Such a situation is not unique to the Port of Fremantle. Transport operators in New South Wales expressed similar views in that State's review of port competition and regulation (PWC, 2007). It is possible that stevedores do view their relationships with individual shipping lines as being of commercial importance than their relationship with road and rail operators. However, this is not indicative of a lack of competition in the stevedore market or a misuse of market power.

A recent review by IPART looked specifically at the interface between land transport industries and stevedores at Port Botany. This review did identify a number of interface problems, including:

- road transporters needing to access stevedore terminals to collect a container at a particular point in time could not be sure that they would be granted access;

- waiting time for trucks were often found to be ‘unreasonably long’;
- a lack of clear rules that apply when delays at the terminal mean stevedores are unable to serve trucks in the timeslot that had been booked; and
- a lack of clarity about the obligations that stevedores and road transport operators have to each other.

However, IPART concluded that these problems were not the result of a lack of competition in the stevedore market or a misuse of market power. The main reason for this conclusion was that stevedores had a limited ability to use or misuse market power and that the stevedoring companies had an incentive to move containers on and off their land as quickly as possible so that they could meet the demand from shipping companies. Rather than recommending regulation of stevedoring services, IPART recommended a range of strategies to clarify the roles of stevedores and road transport operators and improve communication between the two parties. A voluntary pricing program for the booking of container pick-up slots was also recommended (IPART, 2007).

Publicly available information on productivity and prices of stevedoring services also support a finding that there is no misuse of market power by stevedores.

Stevedore prices and rates of productivity at Australia’s five major capital city ports are regularly published by the Bureau of Infrastructure, Transport, Regional Development and Local Government in its *Waterline* publication. The returns earned by stevedoring companies and the productivity of stevedores are also monitored by the ACCC in its series of *Container Stevedoring Monitoring* reports. These publicly available comparisons of stevedore performance and prices are likely to limit the inclination of stevedore companies to misuse market power were they to hold market power.

Prices charged by stevedores operating at the port are consistent with those charged at other ports. For each of the five ports that are reviewed in the *Waterline* publication, stevedore charges are equal to \$173 per TEU container. Rates of stevedore productivity at the Port of Fremantle have steadily risen over time as they have done at other Australian ports (Bureau of Infrastructure, Transport, Regional Development and Local Government).

Vertical integration of providers of stevedoring services

Vertical integration is prevalent among providers of stevedoring services. Stevedoring companies operating at the ports of Fremantle, Esperance and Port Hedland include DP World, Patrick and P&O Automotive and General Stevedoring. Vertical integration amongst these national and multinational companies, as reported by PWC in its *Review of Port Competition and Regulation in New South Wales*, includes the following (PWC, 2007).

- DP World has significant interests in a range of transport and storage businesses and offers customers an integrated freight logistics service. DP World also owns shares in P&O Trans Australia and P&O Automotive and General Stevedoring. P&O Trans Australia operates a logistics business, including rail, rail terminals, container parks, container freight stations, warehousing and distribution. P&O Automotive and General Stevedoring provides general stevedoring services.

- Toll recently created a new publicly listed company, Asciano, which encompasses Patrick Stevedoring and Pacific National, a major national rail freight business.
- There is a potential takeover by P&O Trans Australia of the Baguleys container yards at the Port of Fremantle. If it proceeds, the takeover would result in a vertically integrated entity operating in the markets of stevedoring and container storage.

Despite the vertical integration of stevedoring providers with related businesses, there is no evidence of preferential treatment by stevedores to affiliated businesses or restricting access non-affiliated businesses. Submissions to this review have not provided any evidence of preferential access or treatment being provided to businesses affiliated with stevedore companies.

Conclusions

The degree of market power held by stevedores is unclear and vertical integration among stevedore companies does exist. However, there is no evidence that indicates that stevedore companies have misused market power. On balance, there is no prime facie evidence to suggest that economic regulation of access to stevedoring services would increase competition in markets dependent on these services.

Pilot services

Pilot services at the Fremantle Port Inner and Outer Harbours are provided by Fremantle Pilots under a contract arrangement with the Fremantle Port Authority.

Pilot services at Port Hedland are provided by the Port Hedland Port Authority. The Authority contracts an independent service provider to provide marine pilot, helicopter services and pilot boat services (the pilot licence at the port is held by one service provider).

Pilot services at the Port of Esperance are provided by the Esperance Port Authority.

Dependence on pilot services

Container and break bulk ships entering and leaving a port are dependent on pilot services and therefore the markets for containerised and bulk freight are also ultimately dependent on pilot services. In most cases, it is a requirement that a pilot be used to navigate a ship, particularly a large ship, into harbour. There are no effective substitutes for pilot services.

Market power held by providers of pilot services

There is no evidence to indicate that providers of pilot services hold or have misused market power.

The pilot services contract at the Port of Fremantle, which is held by Fremantle Pilots, is periodically subject to market testing and a competitive tendering process. Such market testing places competitive pressures on the provider of pilot services and is effective in limiting the market power of pilot service providers. No submissions were made to this review that indicated that pilot service providers at the Port of Fremantle hold market power.

The Fremantle Port Authority provides pilot transfer services. The provision of these services reduces the potentially financial large barriers to entry, associated with the purchase of pilot transfer boats, and makes the provision of pilot services at the Port of Fremantle a market that is relatively easy to access.

The Port Hedland Port Authority contracts an independent service provider to provide marine pilot, helicopter services and pilot boat services (the pilot licence at the port is held by one service provider). Calls for tender to provide these services are made at regular intervals and pilot contracting arrangements, including contract prices, are gazetted. The market power of the incumbent pilot service provider is limited as the pilot service contract is regularly put to tender. No submissions were made to this review that indicated that pilot service providers at Port Hedland hold market power.

Pilot services at the Port of Esperance are provided by the Esperance Port Authority. Private providers of pilot services are unable to enter the market to provide pilot services at the Port of Esperance. This arrangement does provide the Esperance Port Authority with market power, however, there is no evidence that indicates that this market power has been misused. The service charges for pilot services levied by the Esperance Port Authority is published on its website. There is also no evidence that indicates that were the market open to access by third parties that there would be demand from private sector providers of pilot services. The Port of Esperance services a relatively small volume of ships, about 200 per year, and it is not certain that such a small market could support the operations of an independent provider of pilot services.

Vertical integration of pilot services

There is no vertical integration of pilot-service businesses in upstream or downstream markets at any of the ports addressed in this review.

Conclusions

There is no evidence of the existence or misuse of market power in the provision of pilot services at the ports of Fremantle and Port Hedland.

Esperance Port Authority has potential market power as the sole provider of pilot services. However, there is no evidence that this market power has been misused. Further it is not certain that regulation of pilot services at the Port of Esperance could promote competition in upstream and downstream markets.

Towage services

Inner and Outer Harbour towage services at the Port of Fremantle are provided under non-exclusive licences issued by the Fremantle Port Authority.

Towage services at the Esperance Port Authority are provided by Mackenzies Tug Service under a non-exclusive licence issued by the Esperance Port Authority. Towage services at Port Hedland are provided by Teekay under a non-exclusive licence issued by the Port Hedland Port Authority.

Dependence on towage services

Container and break bulk ships entering and leaving a port are dependent on tug and towage services and therefore the markets for containerised and bulk freight are also ultimately dependent on towage services. Large ships do not have the manoeuvrability to enter and exit a port without the assistance of towage services. There are no effective substitutes for towage services.

Market power held by providers of towage services

Towage licenses issued by the three port authorities are regularly put to competitive tender, limiting the market power held by the incumbent service providers.

Financial barriers to entry do exist in the towage service provision market and these are principally the result of entrants having to own or lease one or more tug boats. According to the Productivity Commission, such barriers are 'not large' (Productivity Commission, 2002). After reviewing the towage services market in Australia, the Productivity Commission found that there is a pool of alternative towage operators that are able to enter the Australian market (Productivity Commission, 2002). Thus, barriers to entry are not considered to be restrictive in terms of limiting competition.

No submissions were made to this review to indicate that towage service providers either hold or have misused market power.

Vertical integration of providers of towage services

There is no vertical integration of towage businesses in upstream or downstream markets at any of the ports addressed in this review.

Conclusions

There is no evidence of the existence or misuse of market power in the provision of towage services at the ports examined in this review.

Licenses to provide towage services at the ports of Fremantle, Esperance and Port Hedland are non-exclusive and are subject to regular market tendering thus imposing a discipline on incumbent service providers. Barriers to entry to the towage market do exist but are not so large so as to prevent new towage service providers from entering the market. There is no vertical integration among towage service providers and no evidence to demonstrate that towage service providers have misused market power.

Line and mooring services

Line and mooring service providers are responsible for securing ships to berths while they are staying at port.

The Fremantle Port Authority provides mooring services in the Port of Fremantle Inner Harbour and at some Outer Harbour facilities in conjunction with other services such as security. Alcoa and BP provide their own mooring services. Line boat services in the Inner and Outer Harbour are provided by Fremantle Launch Company. There are no licences or contracts in place governing the provision of these services.

The Esperance Port Authority is sole provider of line and mooring services operating at the Port of Esperance.

At Port Hedland, line and mooring services are provided by two line boat service companies operating under non-exclusive licenses.

Dependence on line and mooring services

Container and break bulk ships that berth at a port are dependent on line and mooring services and therefore the markets for containerised and bulk freight are also ultimately dependent on line and mooring services. There are no effective substitutes for line and mooring services.

Market power held by providers of line and mooring services

Line and mooring services at the Port of Fremantle are provided by Fremantle Launch Company operating under a non-exclusive licence. Two line boat service companies operate under non-exclusive licenses at Port Hedland. Line and mooring service contracts at Fremantle and Port Hedland are non-exclusive and subject to a regular tendering process and this limits the market power of the incumbent service providers.

No submissions were provided to this review to indicate that line and mooring service providers at the ports of Fremantle and Port Hedland hold market power or have misused market power.

The Esperance Port Authority is sole provider of line and mooring services operating at the Port of Esperance. This arrangement potentially provides the Esperance Port Authority with market power, however, there is no evidence that indicates that this market power has been misused. Line and mooring charges levied by the Esperance Port Authority are available on its website.

Vertical integration of line and mooring service providers

There is no vertical integration of line and mooring-service businesses in upstream or downstream markets at any of the ports addressed in this review.

Conclusions

There is no evidence of the existence or misuse of market power in the provision of line and mooring services at the ports examined in this review.

Market power held by the Esperance Port Authority as the sole provider of line and mooring services has not been misused. Further, there is also no evidence that indicates that were the market open to access by third parties that there would be demand from private sector providers of line and mooring services. The Port of Esperance services a relatively small volume of ships, about 200 per year, and it is not certain that such a small market could support the operations of an independent line service provider. The Esperance Port Authority has indicated that it would like to be able to contract out line and mooring services but the market at the port is not big enough to attract interest from the private sector.

Grain terminals at the ports of Fremantle and Esperance

There are four export grain terminals in Western Australia, located at the ports of Fremantle, Esperance, Albany and Geraldton. Each of the terminals is owned and operated by CBH — a standard set of charges is applied across terminals. CBH is the dominant grain storage and handling company operating in Western Australia (CBH 2008a).

Dependence on grain terminals

CBH is the sole provider of export bulk grain terminal facilities in Western Australia and therefore grain exporters are highly dependent on CBH's export grain terminals. Grain may also be exported in bags or containers.

Market power held by the provider of grain-terminal services

CBH holds market power as a result of it being the sole owner and operator of bulk grain export facilities at ports in Western Australia.

AWB's submission to this review referred to the Grain Licensing Authority's 2005—06 Annual Report to Minister and the Western Australian Chamber of Commerce and Industry report titled *Implications of Wheat Marketing Deregulation*. Each report is cited as containing evidence of market power and conflicts of interest held by CBH.

In its Annual Report, the Grain Licensing Authority stated that CBH 'holds natural monopoly on storage and handling in Western Australia, principally through its control of facilities at the four ports' (Grain Licensing Authority, 2006).

The report into the implications of wheat marketing deregulation prepared by the Chamber of Commerce and Industry stated that CBH's ownership of four port terminals and its strong linkages to the rail network has placed the company in a very strong position of supply chain control (Chamber of Commerce and Industry, 2007).

There are high barriers to entry to the provision of grain handling services at ports. Financial barriers to entry include the significant upfront capital costs required to construct grain export facilities. Physical barriers to entry resulting from limited port space are also likely to be a factor limiting the ability of new parties from entering the market.

Vertical integration of the provider of grain-terminal services

CBH is a vertically integrated entity. The company owns significant grain storage and handling infrastructure, including 200 grain receipt points, and is the sole owner of bulk grain export facilities at four ports in Western Australia. CBH has operations in numerous steps of the grain export supply chain, including grain receipt, handling, storage and export.

CBH is also a major trader in grain markets, being a buyer of grain from growers and a seller of grain in international markets. In these upstream and downstream markets, CBH competes with other grain traders.

Conclusions

Conditions for regulation to be potentially effective in preventing the misuse of market power or increasing competition in upstream and downstream markets appear to be satisfied in the case of grain terminals.

- Grain traders who choose to export bulk grain from a port in Western Australia are dependent on CBH's port infrastructure.
- CBH holds market power by virtue of it being the sole owner of bulk grain export facilities and the high barriers to entry into the grain export industry.
- CBH is vertically integrated having operations in numerous steps of the grain export supply chain, and upstream and downstream grain markets.

Accordingly, there is a prima facie case that access regulation to CBH's port infrastructure would increase competition in upstream and downstream markets for grain products.

Consistent with this finding, the Western Australian *Bulk Handling Act 1967* provides for CBH's facilities at Western Australian ports to be available on a 'common user' basis. Although there are no provisions to govern the manner in which terms or prices of access are to be determined, in its 2003 assessment of government progress in implementing National Competition Policy reforms, the National Competition Council determined that the *Bulk Handling Act 1967* was consistent with the State's obligations under the Competition Policy Agreement (National Competition Council, 2003).

In addition to the access provisions of the *Bulk Handling Act 1967*, the recently enacted Commonwealth *Wheat Export Marketing Act 2008* requires that where a party applying for accreditation as a wheat marketer also operates an export grain terminal, it must satisfy an 'access test' in relation to the relevant terminals.

The access test required under the provisions of the *Wheat Export Marketing Act 2008* will, from October 2009, require CBH to:

- comply with continuous disclosure rules (which are intended to eliminate the information asymmetries between parties); and
- provide an access undertaking under Division 6 of Part IIIA of the *Trade Practices Act 1974* to enable accredited wheat exporters to access the port terminal services; or
- provide access to accredited wheat exporters to the port terminal services under an access regime established by a State or Territory that has been found to be an effective regime under Division 2A of Part IIIA of the *Trade Practices Act 1974*.

Although an ‘access’ requirement of sorts exists under the Western Australian *Bulk Handling Act 1967*, it appears unlikely that the Act would lend itself to the establishment of a State-based access regime that is capable of being certified as being effective.⁶ Consequently, in order to meet the port infrastructure access test imposed by the *Wheat Export Marketing Act 2008*, CBH would be required to develop a voluntary access undertaking for acceptance by the ACCC. Such an outcome would also be consistent with the desire in the CIRA for a consistent national approach to the regulation of ports.

A limitation of the *Wheat Export Marketing Act 2008* is that the access test will apply *only* to export grain terminals that are operated by an accredited wheat marketer, and only in relation to the export of wheat. Should CBH at some future point not be an accredited wheat marketer, it would no longer be required to meet the access test, although it would still be obliged to allow other parties to use its export grain terminals under the *Bulk Handling Act 1967*.

A limitation of the *Wheat Export Marketing Act 2008* is that the access test will apply *only* to export grain terminals that are operated by an accredited wheat marketer. Consequently, should CBH (and associated entities) at some future point not be an accredited wheat marketer, it would no longer be required to meet the access test (although CBH would still be obliged to allow other parties to use its export grain terminals under the *Bulk Handling Act 1967*).

On balance, the access test provisions of the *Wheat Export Marketing Act 2008* are considered likely to adequately regulate export terminals in Western Australia to prevent the potential misuse of market power by the operators of these terminals. For this reason, there is no clear need for further economic regulation of wheat export grain terminals in Western Australia.

While there are access test provisions in place to adequately regulate wheat export grain terminals in Western Australia, these provisions do not extend to the other bulk grains exported from the State (such as barley, lupins and canola). There is the potential for the misuse of market power by operators of the bulk grain terminals for these other bulk grains. There is no evidence to indicate that misuses of market power have occurred. However, given that there is potential for misuse of market power, the access provisions for these other grains may need further investigation to create consistency with the existing regulatory arrangements for wheat.

Iron ore facilities at Port Hedland

The Pilbara Infrastructure Pty Ltd (TPI) controls iron ore export infrastructure (berth space and ship loading infrastructure) at Anderson Point located within Port Hedland. TPI is a wholly-owned subsidiary of iron ore miner Fortescue Metals Group (FMG).

Dependence on TPI iron ore facilities

Actual or potential iron ore miners are not dependent on the TPI port facilities at Anderson Point.

⁶ Clause 6 of the Competition Principles Agreement provides that a state based access regime may be established under legislation that is specific to particular types of infrastructure services. The regime would then need to be certified as being effective by the relevant Commonwealth Minister on advice of the National Competition Council (NCC).

Other than TPI, there are two iron ore producers that are based in the Pilbara and are currently exporting iron ore, these are BHP Billiton and Rio Tinto. BHP Billiton (at Port Hedland) and Rio Tinto (at Dampier and Cape Lambert) operate their own port infrastructure and neither company is dependent on the export infrastructure that is owned by TPI.

There are several junior iron ore companies seeking to commence iron ore production and export from Pilbara mines in coming years. At Port Hedland, these companies will be able to export from common-user facilities the Utah Point berth, which is being developed by the Port Hedland Port Authority. The common user berth, which is scheduled for completion during the first half of 2010, will have facilities capable of servicing the needs of junior iron ore miners. At Port Hedland, Junior iron ore miners also have the option of seeking to negotiate access to the port facilities owned and operated by BHP Billiton.

Market power held by TPI

TPI is not considered to hold significant market power by virtue of its ownership of the iron ore export infrastructure at Anderson Point.

Market power is limited by the fact that other iron ore export infrastructure will soon be available to iron ore exporters through the development of the Utah Point facilities.

Market power is also limited by Government-imposed requirements on TPI to provide third party access to its port facilities, as detailed below.

Vertical integration of TPI

TPI provides export iron ore handling services at the Port Hedland Port and is a wholly owned subsidiary of iron ore miner FMG, and therefore is vertically integrated with an iron ore rail business, and an iron ore mining and trading business. This vertical integration would give rise to conflicts of interest in providing access to port facilities to other iron ore miners.

This conflict of interest is, however, addressed by requirements under agreement with the Western Australian Government for TPI to provide third-party access to the port facilities and to invest in further capacity at Port Hedland to meet the demands of new customers, if commercially justified and subject to Ministerial approval. The effectiveness of these requirements is possibly evident from TPI having recently negotiated an arrangement for access to the TPI berths with Atlas Iron. In addition, TPI has also negotiated a memorandum of understanding with BC Iron to negotiate port and rail access.

Conclusions

Conditions for regulation to be potentially effective in preventing the misuse of market power or increasing competition in upstream and downstream markets are not satisfied in the case of TPI iron ore facilities at Port Hedland.

While TPI is vertically integrated in iron ore markets, existing iron ore exporters are not completely dependent on TPI's export facilities to get their product to market. Junior iron ore miners that are projected to start exporting iron ore in the near future will have options other than the use of TPI's export infrastructure available to them to allow them to export their product. Further limiting any market power that could be held by TPI are existing requirements, written into an agreement held by TPI and the Western Australian Government, that require the company to provide third party access to its facilities.

Chapter 6

CIRA clause 4.2 – Allowing for Competition

6.1 Introduction

Clause 4.2 of the CIRA requires that competition be allowed in the provision of port and related infrastructure facility services unless it is established that the benefits of restricting competition outweigh the costs to the community.

Clause 4.2 further identifies four specific aspects of port operations that should be implemented in a manner that allows for competition. Specifically, these are indicated in clauses 4.2(a) to (d) to be:

- (a) port planning should, consistent with the efficient use of port infrastructure, facilitate the entry of new suppliers of port and related infrastructure services;
- (b) where third party access to port facilities is provided, that access is provided on a competitively neutral basis;
- (c) commercial charters for port authorities should include guidance to seek a commercial return while not exploiting monopoly powers;
- (d) any conflicts of interest between port owners, operators or service providers as a result of vertically integrated structures should be addressed by the relevant Party on a case by case basis with a view to facilitating competition.

Consideration is given in this chapter to the specific aspects of port operations identified in clauses 4.2(a) to (d) and whether these operations are conducted in a manner consistent with allowing competition in the provision of port and related services – except in those circumstances where there is a demonstrated net public benefit in restricting competition.

6.2 Port planning

CIRA requirements

Clause 4.2(a) of the CIRA requires that port planning should facilitate the entry of new suppliers of port and related infrastructure services consistent with the efficient use of port infrastructure.

Current regulations

Section 30 of the *Port Authorities Act 1999* contains a number of provisions that require port authorities to plan for future growth and generally be responsible for the efficient operation of the port. Specifically, sections 30(1) (a) (b) and (d) state that the functions of port authorities are:

- (a) to facilitate trade within and through the port and plan for future growth and development of the port;
- (b) to undertake or arrange for activities that will encourage and facilitate the development of trade and commerce generally for the economic benefit of the State through the use of port and related facilities; and

(d) to be responsible for the safe and efficient operation of the port.

The port authorities have specific powers in relation to planning (and undertaking works) at ports that stem from their government ownership. Section 38(2) of the *Port Authorities Act 1999* establishes port works and port facilities as 'public works' and thus exempt port authorities from controls that may otherwise be imposed under the *Planning and Development Act 2005*. The *Planning and Development Act 2005*, does require that port authorities consult the responsible authority at the time of proposal of any public work or the taking of land for public work is being formulated so as to ensure that:

- (a) the purpose and intent of any planning scheme that has effect in the locality where, and at a time when, the right is exercised; and
- (b) the orderly and proper planning, and the preservation of the amenity, of that locality at that time. (*Planning and Development Act 2005*, section 6)

The result of the status of port authorities in respect of planning requirements is that the port authorities have wide powers to undertaking planning and development of the port facilities.

Strategic development plans, which are required to be produced by each port authority and agreed to by the Minister under sections 49 to 57 of the *Port Authorities Act 1999*, are required to cover a forecast period of five years (unless otherwise agreed to by the Minister) and must set out:

- the medium to long-term objectives and how those objectives and targets will be achieved; and
- an environmental management plan.

In preparing strategic development plans, the boards of port authorities are required to consider matters including strategies for land use, trade projections, capital expenditure, relevant government policy, trade facilitation and environmental management (*Port Authorities Act 1999*, sections 49-51).

Port authorities are also exempt from many of the requirements of the *Local Government (Miscellaneous Provisions) Act 1960*. For example, port authorities are not required to get local government approval for building plans nor are they required to hold a building licence to undertake building works. Provisions in the *Local Government (Miscellaneous Provisions) Act 1960* around how buildings are to be constructed also do not apply to port authorities.

However, port authorities are required to comply with the requirements of the Building Code and are also required to consult with the relevant local government before the carrying out of building work to ensure that the performance requirements of the Building Code are applied. Disputes between port authorities and local governments can be referred to the Minister for final decision (*Port Authorities Act 1999*, section 38).

Implications of port planning for competition

Clause 4.2(a) of the CIRA requires that port planning should, consistent with the efficient use of port infrastructure, facilitate the entry of new suppliers of port and related infrastructure services.

It would appear that the statutory requirements for port planning and the responsibility given to the port authorities for planning functions would, of themselves, not impede the entry of new suppliers of port and related infrastructure services. However, there is no statutory requirement for port authorities to proactively facilitate the entry of new suppliers of port and related infrastructure services. In fact, there exists a potential conflict of interest for the port authorities in that performing the planning role within an existing port could, where it is vertically integrated, affect a port authority's competition position with respect to other suppliers of port and related infrastructure services in the port.

Moreover, it appears there is not a specific planning framework at a state-level that considers future port infrastructure requirements, and options for facilitating the entry of new suppliers of port and related infrastructure services.

Both of these potential deficiencies in planning arrangements for port infrastructure in Western Australia have been raised in a submission to this review from James Point with reference to the proposals by the Fremantle Port Authority and James Point for developments in, or adjacent to, the Fremantle Outer Harbour:⁷

- planning for its Outer Harbour developments being undertaken by the Fremantle Port Authority without consideration of potential contributions from other parties; and
- excessive delays in the planning process for James Point's port, creating uncertainty and generally not being conducive to the facilitation of new entrants.

The first matter raised by James Point is that planning undertaken by the Fremantle Port Authority, in particular the planning of the two developments in the Outer Harbour, has focused almost exclusively on planning for facilities that the Authority itself will 'own and operate'. According to James Point, this aspect of the planning process has not facilitated the entry of new suppliers of port and related infrastructure services.

The steering committee advises that the planning being undertaken by the Fremantle Port Authority and other government agencies for additional container facilities in the Outer Harbour to supplement facilities in the Inner Harbour is consistent with its statutory role. Regarding issues of ownership and operating arrangements in relation to the new facilities, no decisions have been taken by the State Government as to how the facilities would be funded, delivered or operated. In any event, whatever delivery and funding model is chosen, it is likely to involve significant private sector funding in the super-structure at least. Operational arrangements for the new facilities are most likely to be determined through an expression of interest process and are most likely to be focused on facilitating the entry of new suppliers of port services.

⁷ There have been no submissions indicating that planning processes at either Esperance Port or Port Hedland have failed to facilitate the entry of new suppliers.

According to James Point, the required approvals and licences for its proposed development have been obtained from the Environmental Protection Authority, the Minister for the Environment and the Department of Environment and Conservation. It has taken 43 months from the time of the release of the relevant Public Environmental Review of the James Point proposal until James Point was granted approval from the Minister for the Environment. James Point noted that 43 months is a significant period of time even for complex projects and puts into question whether planning processes are facilitating new entrants.

In addition to the delays in obtaining Ministerial Approval, James Point indicates that a necessary amendment to the Metropolitan Region Scheme (required to transfer an area of Waterways reservation in Cockburn Sound to Industrial Zone to facilitate the construction and operation of the proposed port facility) has yet to be finalised owing to the potential affects of the Kwinana Quay proposal put forward by the Fremantle Port Authority. There are overlaps in the space required by each of the two proposals. Public hearings on the Amendment to the Metropolitan Region Scheme were conducted in December 2005. In July 2007, the Minister advised that the Amendment would be delayed two years to allow for the Fremantle Port Authority to complete the statutory processes required for its two port development options (James Point submission, 2008).

According to the steering committee, the delays experienced by James Point in relation to environmental and planning approvals are matters for the relevant Ministers and the Fremantle Port Authority or any other port facility developer would experience similar environmental and planning approval processes.

The steering committee also advises that there is significant evidence that planning by ports has and does facilitate the entry of new suppliers of port and infrastructure services. For example, planning by the Fremantle Port Authority in relation to towage and break-bulk stevedoring services has led to the introduction of arrangements to facilitate competition in the provision of these services. Furthermore, the planning for new container facilities in the Outer Harbour is likely to lead to the possible entry of a third container stevedore.

Nevertheless, a means available to Government to ensure that port planning promotes the efficient use of infrastructure and facilitates the entry of new suppliers is for the Minister to require that the statement of corporate intent and the strategic development plan of port authorities:

- identify how port planning will facilitate the entry of new suppliers of port and related infrastructure services; and
- where port planning will not facilitate the entry of new suppliers of port and related infrastructure services, demonstrate that:
 - this is consistent with the efficient use of port infrastructure; and/or
 - the benefits from restricting competition outweigh the costs to the community.

Such a requirement may not require legislative amendment as section 51(2)(b) of the *Port Authorities Act 1999* provides a Port Authority Board, in the preparation of a strategic development plan, with the discretion to consider other matters that the Minister and the Board agree should be considered.

6.3 Competitive neutrality of third party access

CIRA requirements

Clause 4.2(b) of the CIRA requires that where third party access to port facilities is provided, that access should be provided on a competitively neutral basis.

Competitive neutrality is a term applied in the Competition Principles Agreement to mean the absence of competitive advantages of government businesses over private-sector businesses as a result of public-sector ownership of the government businesses (National Competition Council, 1998 p 5) and in the case of ports would mean that government businesses do not have access to facilities on more favourable terms than private-sector businesses solely for reason of public-sector ownership. More generally, competitive neutrality may be taken to mean third party access to port facilities on terms and prices that do not discriminate between any parties except on reasonable commercial grounds.

Port facilities subject to third party access

Port facilities that are (or potentially are) subject to third party access include:

- actual port facilities that are owned and operated by the Fremantle, Esperance and Port Hedland port authorities;
- TPI's port infrastructure at Port Hedland; and
- CBH's export facilities at the ports of Fremantle and Esperance.

Evidence of discrimination between access seekers

The Fremantle, Esperance and Port Hedland port authorities provide access to a range of service providers including shipping lines, stevedores, pilot service providers and towage service providers. There is no evidence, from submissions to this review or otherwise, to indicate that third party access to port facilities has been provided on anything other than a competitively neutral basis.

In its submission to the review, the Transport Forum expressed concerns about a subsidy paid by the Western Australian Government to rail freight service providers at the Port of Fremantle. The Transport Forum indicated that subsidy provides Intermodal Link Services, the entity receiving the subsidy, with what amounts to an unfair competitive advantage over road freight transport service providers at the port.

The rail subsidy is not related to access to port facilities and hence is not a matter within the scope of this review.

6.4 Commercial charters

CIRA requirements

Clause 4.2(c) of the CIRA requires that port charters should include guidance for ports to seek a commercial return while not exploiting monopoly powers.

Current charters of the port authorities

The commercial charter of port authorities in Western Australia is established by the *Port Authorities Act 1999*. Section 34 of the Act states that:

A port authority in performing its functions must —

- (a) act in accordance with prudent commercial principles; and
- (b) endeavour to make a profit.

On port charges, section 37(2) of the Act states that:

Port charges are to be determined by the port authority in accordance with prudent commercial principles and may allow for —

- (a) the making of a profit; and
- (b) depreciation of assets.

The term ‘prudent commercial principles’ is not defined in the Act.

In addition to the requirements of the *Port Authorities Act 1999*, current State Government policy requires that port authorities target a long-term average rate of return of five to eight per cent. Port authorities are able to address the need for variations in rate of return targets in their strategic development plans and statements of corporate intent. While there is no explicit requirement for port authorities to report actual rates of return, the Fremantle, Esperance and Port Hedland port authorities all report actual rates of return in their annual reports.

It is clear that *Port Authorities Act 1999* establishes a commercial charter that includes guidance for the port authorities to seek a commercial return. Requirements of the *Port Authorities Act 1999* the port authorities ‘endeavour to make a profit’ and impose port charges to allow for ‘the making of a profit’ are considered to be consistent with the requirements clause 4.2(c) of the CIRA.

Clause 4.2(c) of the CIRA also requires that the commercial charter of port authorities constrain the guidance of seeking a commercial return by also requiring guidance that the authorities not exploit monopoly powers. The *Port Authorities Act 1999* does not explicitly include such guidance.

The absence of guidance for port authorities to not exploit monopoly powers was identified in a submission from James Point. However, James Point also stated that it is undecided as to whether there needs to be specific provisions in the commercial charters of the port authorities to deal with the exercise of monopoly powers in the areas of access and pricing.

The Fremantle Port Authority submitted that it is not required, or encouraged, to maximise profits, but is required to earn a minimum rate of return on the value of its assets. the Fremantle Port Authority also submitted that there are checks and balances that restrict its ability to misuse monopoly or market powers. These include requirements to produce statements of corporate intent and strategic development plans, which must be approved by Ministers before they can be finalised.

Further to the submission from the Fremantle Port Authority, the functions of port authorities also extend beyond a requirement to earn a commercial rate of return and include functions of facilitating trade and commerce (*Port Authorities Act 1999*, section 30).

To the extent that exploitation of monopoly powers would be inconsistent with facilitating trade and commerce, the commercial charter established by the *Port Authorities Act 1999* constrains the commercial charter of the port authorities in a manner consistent with guidance to not exploit monopoly powers.

Taking the above into account, the Allen Consulting Group considers that the commercial charter established for Port Authorities under the *Port Authorities Act 1999* is consistent with the requirements of clause 4.2(c) of the CIRA.

6.5 Conflicts of interest through vertical integration

CIRA requirements

Clause 4.2(d) of the CIRA requires that any conflicts of interest between port owners, operators or service providers that result from vertically integrated structures be addressed on a case-by-case basis with a view to facilitating competition.

Clause 4.2(d) of the CIRA does not prohibit the existence of vertically integrated structures in the provision of port and related infrastructure services, but only requires that any conflicts of interest be identified and resolved on a case-by-case basis.

Vertical integration in the provision of port facilities and services

Vertical integration occurs when a single company or entity controls several steps in the production and/or distribution of a product or service. In the context of ports, vertical integration is most likely to arise in relation to two or more aspects of infrastructure services and port services — for example, a single business that includes ownership of terminal infrastructure and the provision of stevedoring services. In this example, a conflict of interest may arise if the owner of the terminal infrastructure had an incentive were to restrict access to other stevedoring operations so as to protect its own stevedoring operations.

The following assessment of vertical integration considers vertical integration and conflicts of interest as applying to port authorities and then does the same for private sector providers of port services. In all cases, instances of vertical integration and associated conflicts of interest are found to either not warrant Government intervention at the current time, due to an absence of effects on competition, or to be adequately addressed by existing interventions in the markets for the relevant services.

Port Authorities

The port authorities have conflicts of interest where they provide port services in actual or potential competition with other providers of port services. Examples of these conflicts of interest exist for the Fremantle and Esperance ports.

The Fremantle Port Authority provides services to transport pilots to ships. There is no evidence to suggest that this conflict of interest has led the Fremantle Port Authority to engage or attempt to engage in anti-competitive behaviour.

The Esperance Port Authority is a provider of stevedoring services, pilot services and line and mooring services at the Port of Esperance. There are conflicts of interest in the provision of each of these services however there is no evidence to indicate that these conflicts of interest have caused the Esperance Port Authority to engage or attempt to engage in anti-competitive behaviour. The Esperance Port Authority has not restricted access to the provision of the above port services for reasons of protecting its own business interests.

There is no need for intervention in the operation of the Port Authorities to address conflicts of interest.

Private sector providers of port services

CBH, TPI and some stevedore operators have vertically integrated businesses.

CBH is a vertically integrated company that provides grain export services at the Ports of Albany, Esperance, Geraldton and Fremantle (Outer Harbour), while also being the dominant operator of grain storage and handling facilities in Western Australia.

There are conflicts of interest for CBH in providing access to the grain handling facilities, arising from the vertical integration of CBH with grain transport and grain trading businesses. These conflicts of interest, where relevant to exports of wheat, have been addressed by the access requirements imposed by the *Wheat Export Marketing Act 2008*. There is the potential for conflicts of interest by operators of bulk grain terminals for grains other than wheat. There is no evidence to indicate that misuses of market power have occurred. However, given that there is potential for misuse of market power, the access provisions for these other grains may need further investigation to create consistency with the existing regulatory arrangements for wheat.

TPI, which provides export iron ore handling services at the Port Hedland Port, is a wholly owned subsidiary of iron ore miner FMG, and therefore is vertically integrated with an iron ore rail business, and an iron ore mining and trading business. This vertical integration would give rise to conflicts of interest in providing access to port facilities to other iron ore miners. This conflict of interest is, however, addressed by requirements under agreement with the western Australian Government for TPI to provide third-party access to the port facilities and to invest in further capacity at Port Hedland to meet the demands of new customers, if commercially justified and subject to Ministerial approval. The effectiveness of these requirements is possibly evident from TPI having recently negotiated an arrangement for access to the TPI berths with Atlas Iron. In addition, it has also negotiated a memorandum of understanding with BC Iron to negotiate port and rail access (WA Business News, 2008).

The providers of container stevedoring businesses are vertically integrated with transport and logistics businesses. In its submission to this review, the Transport Forum also expressed concerns about the potential takeover of the Maersk, Baguleys and Connaus container yards at the Port of Fremantle by P&O. While it does not clearly identify the conflict of interest that it believes would arise from the potential takeovers or mergers, the Transport Forum appears to be generally concerned with issues of market power. The potential for reduced competition in the markets for stevedoring and container services has, however, been addressed by the ACCC with the finding that the merger is unlikely to lessen competition in the relevant market. The ACCC found that competitive providers of the same service would be an effective constraint on the merged firm were it to attempt to use any perceived market power. It also noted that the industry had low barriers to entry, and that shipping lines had sufficient bargaining power to enable them to either switch suppliers and/or sponsor new entry into the relevant market (ACCC, 2008).

In summary, therefore, there are not considered to be conflicts of interest arising through vertical integration amongst providers of port facilities and services that restrict competition or that have not been adequately addressed by existing economic regulation.

Appendix A

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Appendix B

Scope of work

Review objectives

The objectives of the review are to develop findings and recommendations on two main issues.

- To determine whether there is a demonstrated case for economic regulation of port and related infrastructure at the facilities nominated for review (refer to Clause 4.1 of the Competition and Infrastructure Reform Agreement [CIRA]).
- To determine whether the supply of port and related infrastructure services, at the nominated ports and port facilities in Western Australia, is consistent with principles contained in Clause 4.2 of the CIRA.

Scope of services

The review will be conducted of a representative range of Western Australian port and related infrastructure facilities to fulfil the objectives outlined in section 0.

The Western Australian port and related infrastructure facilities to be included in the review are:

- Fremantle Port Inner Harbour;
- Fremantle Port Outer Harbour, including the proposed Outer Harbour developments but excluding facilities with exports of less than 1 million tonnes per annum, such as the Kwinana Bulk Jetty and the Kwinana Bulk Terminal;
- Port of Esperance; and
- Port Hedland, including the FMG development but excluding the BHP Billiton facilities and the outer harbour proposal, which is at concept stage only.

Determining if there is a case for economic regulation

To determine if there is a 'clear need' for economic regulation, the review will need to include consideration of the following in the review:

- The structure of the market for port and related infrastructure services, to identify any ports or port-related infrastructure with market power;
- Any evidence of the misuse of market power or the potential for misuse of market power and whether misuse has occurred, which may require examination of the:
- Pricing arrangements and commercial returns for port and related infrastructure services; and
- Access conditions to port and related infrastructure services;
- The consequences, or potential consequences, of any misuse of market power, including in upstream and downstream markets;

- The appropriateness and effectiveness of the existing regulatory and commercial environment in limiting the misuse, or potential misuse, of market power; and
- The case for the introduction of economic regulation of port and related infrastructure based on the likely costs and benefits from such regulation.

If economic regulation is recommended, the review would be required to ensure that any proposed regime is consistent with the principles contained in clause 4.1 of the CIRA, regarding the application of economic regulation to port and related infrastructure.

Determining if port and related infrastructure services are consistent with CIRA Clause 4.2

The review will determine whether the supply of port and related infrastructure services at the nominated ports and port facilities is consistent with principles of CIRA Clause 4.2. The intent of this clause is to allow for competition in the provision of port and related infrastructure services unless it can be demonstrated that the restriction of competition is in the public interest. It is noted in Clause 4.2 of the CIRA, that port planning should facilitate the entry of new suppliers of port and related infrastructure services.

To determine if the supply of port and related infrastructure services at the nominated ports and port facilities is consistent with principles of CIRA Clause 4.2, the review will need to:

- identify any restrictions in the port planning process on the entry of new suppliers of port and related infrastructure;
- where third-party access to port facilities is provided, identify any circumstances where access is not provided on a competitively neutral basis;
- review the commercial charters for port authorities, including port authority legislation, to determine whether guidance is included for authorities to pursue a commercial return while not exploiting monopoly powers; and
- identify any conflict of interests between port owners, operators or service providers that exist because of vertically integrated structures and whether these have impacted on competition in up stream or down stream markets.

The review will also:

- support any recommendations to maintain restrictions, or regulations or arrangements inconsistent with the CIRA, with evidence that the measure is in the public interest; and
- determine whether issues identified by the review have application to other Western Australian ports or port related infrastructure facilities not included in the review.