



## Statement of Issues

19 February 2015

### **Sea Swift Pty Ltd – proposed acquisition of Toll Marine Logistics Australia’s NT/ FNQ marine freight business**

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#### **Purpose**

1. This Statement of issues aims to:
  - give the Australian Competition and Consumer Commission’s (**ACCC**) preliminary views on competition issues arising from Sea Swift Pty Ltd’s proposed acquisition of Toll Marine Logistics Australia’s marine freight business in Far North Queensland, the Torres Strait and the Northern Territory;
  - identify areas of further inquiry;
  - give all interested parties an opportunity to comment; and
  - invite interested parties to submit information to assist us in our assessment of the issues.

#### **Overview of ACCC’s preliminary views**

2. The legal test which the ACCC applies in considering the proposed acquisition is in section 50 of the *Competition and Consumer Act 2010* (**Act**). Section 50 prohibits acquisitions that substantially lessen competition in any market, or are likely to do so.
3. The ACCC has received a very large number of submissions expressing concerns about the impact the proposed acquisition will have on competition in the supply of marine freight services, especially scheduled freight services, in far north Queensland, including the Torres Strait (together referred to as **FNQ**) and the Northern Territory (**NT**).
4. Many interested parties are concerned that the proposed acquisition is likely to harm standards of living in remote communities whose residents are dependent on sea freight. These communities are home to many disadvantaged and vulnerable consumers, often with very low incomes.

5. The ACCC divides its preliminary views into three categories, 'issues of concern', 'issues that may raise concerns' and 'issues unlikely to raise concerns'.

### **Issues of concern**

- The ACCC is concerned that the proposed acquisition would be likely to lead to significant price increases and/or service degradation in scheduled marine freight services<sup>1</sup> in the NT and FNQ, due to a reduction in suppliers from two to one on most routes and new entry being unlikely due to high barriers to entry. Market inquiries have indicated that recent competition between Toll Marine and Sea Swift in the NT and FNQ has led to significant price decreases and some service improvements. Many market participants have submitted that prices were significantly higher and service levels were lower when only one of Toll Marine or Sea Swift operated in these regions with no or little competition. Market inquiries indicate that Toll Marine and Sea Swift have competed vigorously and effectively against each other in recent years.

### **Issues that may raise concerns**

- The ACCC is considering whether the proposed acquisition would be likely to lead to significant price increases and/or service degradation in chartered marine freight services in the NT and FNQ.
- The ACCC is considering whether the proposed acquisition would be likely to lead to increased prices for the supply of fuel for vehicles and boats in parts of the NT and FNQ, due to the overlap between Sea Swift and Toll Marine in supplying these fuel products, and the limited number of alternate suppliers in some areas.

## **Making a submission**

6. Detailed discussion of these and other issues, along with specific questions, is contained in this Statement of Issues.
7. Interested parties should provide submissions by no later than 13 March 2015. Responses may be emailed to [mergers@acc.gov.au](mailto:mergers@acc.gov.au) with the title: Submission re: Sea Swift – Toll Marine.
8. The ACCC anticipates making a final decision by 16 April 2015, however, this timeline can change. To keep abreast of possible changes in relation to timing and to find relevant documents, interested parties should visit the Mergers Register on the ACCC's website at [www.accc.gov.au/mergersregister](http://www.accc.gov.au/mergersregister).

### **Confidentiality of submissions**

9. The ACCC will not publish submissions regarding the proposed acquisition. We will not disclose submissions to third parties (except our advisors/consultants) unless compelled by law (for example, under freedom of information legislation or during

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<sup>1</sup>Scheduled marine freight services include the provision of scheduled shipping services to customers on a contracted basis, as well as to a vast number of smaller customers in remote and coastal communities on an uncontracted or more ad hoc basis. This is explained in more detail in paragraphs 41 to 70.

court proceedings) or in accordance with s155AAA of the Act. Where the ACCC is required to disclose confidential information, the ACCC will notify you in advance where possible so that you may have an opportunity to be heard. Therefore, if the information provided to the ACCC is of a confidential nature, please indicate as such. Our [Informal Merger Review Process Guidelines](#) contain more information.

## About ACCC 'Statements of Issues'

10. A Statement of Issues published by the ACCC is not a final decision about a proposed acquisition, but provides the ACCC's preliminary views, drawing attention to particular issues of varying degrees of competition concern, as well as identifying the lines of further inquiry that the ACCC wishes to undertake.
11. A Statement of Issues provides an opportunity for all interested parties (including customers, competitors, shareholders and other stakeholders) to consider the primary issues identified by the ACCC. It is also intended to provide the merger parties and other interested parties with the basis for making further submissions should they consider it necessary.

## Timeline

Date	Event
9 December 2014	ACCC commenced review of the proposed acquisition
9 January 2015	Closing date for submissions from interested parties.
19 February 2015	ACCC publication of Statement of Issues
13 March 2015	Deadline for submissions from interested parties in response to this Statement of Issues
16 April 2015	Anticipated date for ACCC final decision

## The parties and the proposed transaction

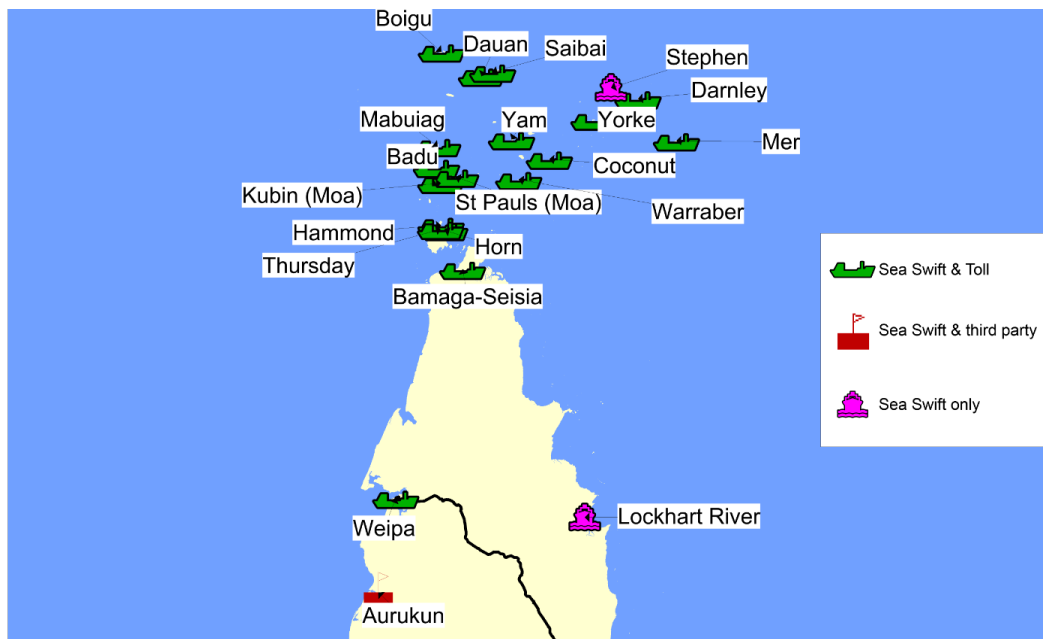
12. Sea Swift Pty Ltd (**Sea Swift**) provides scheduled freight shipping, project logistics, mothershipping and other marine-transport services in northern Australia (motherships deliver supplies to and collect catch from fishing boats at sea). It was established in 1987 and is based in Cairns, Queensland.
13. Sea Swift has three vessels in the NT and a distribution centre in Darwin. It has seven vessels in FNQ and distribution centres at Cairns, Weipa, Seisia-Bamaga and Thursday and Horn Islands (maps below).
14. Toll Marine Logistics Australia (**Toll Marine**) is a division of the Toll transport business owned by Toll Holdings Limited.

15. Toll Marine commenced in 2009 when Toll Holdings acquired the Darwin-based Perkins shipping group. Toll Marine provides scheduled and charter shipping services in the NT and FNQ.
16. In the NT Toll Marine has three vessels, a terminal in Darwin and depots at Gove and Groote Eylandt. In FNQ it has two vessels and depots in Cairns, Weipa, Thursday and Horn islands and Seisia-Bamaga.
17. Sea Swift historically only operated in FNQ and Toll Marine historically only operated in the NT and on the Cairns-Weipa route. However, in 2013 Sea Swift acquired Tiwi Barge Company and began to expand its services in the NT in competition with Toll Marine. The ACCC understands that in late 2013, Toll Marine expanded its FNQ services into the Torres Strait and top of Cape York in competition with Sea Swift.
18. Sea Swift and Toll Marine currently overlap in the provision of scheduled marine shipping and charter shipping services in the NT and FNQ.
19. Scheduled marine services are the provision of regular services to customers on a contracted basis, as well as to a large number of smaller customers in remote and coastal communities on an uncontracted or more ad hoc basis. An example of scheduled shipping on a contracted basis is supply to supermarkets requiring regular deliveries of food. An example of ad-hoc shipping would be an individual requiring a car to be shipped from Cairns to an island in the Torres Strait. Both scheduled and ad-hoc freight may be physically delivered on the same scheduled service.
20. Charter shipping is the provision of services to companies requiring large, sporadic or one off deliveries, for example a mining company requiring the shipment of specific equipment.
21. Sea Swift proposes to acquire from Toll Marine assets associated with Toll Marine's NT and FNQ marine freight business, including four vessels.
22. Sea Swift also proposes to acquire Toll Marine's depots at Gove/Nhulunbuy, Weipa, Horn Island and Cairns. The proposed acquisition does not include Toll Marine's Frances Bay terminal in Darwin or its marine logistics business servicing liquefied natural gas operations in Queensland and Western Australia.
23. The purchase price is \$45 million. Toll would also acquire a 20 per cent holding in Sea Swift.<sup>2</sup>
24. The parties both service the coastal areas of the NT from Darwin and the coastal areas of FNQ from Cairns. The maps below indicate scheduled destinations served by both Sea Swift and Toll Marine, by Sea Swift alongside a provider other than Toll Marine or by Sea Swift alone.

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<sup>2</sup> <http://www.tollgroup.com/asx-announcement/portfolio-changes-driven-by-focus-on-return-on-capital>

**Figure A: scheduled destinations - FNQ**



Not shown: Origin point of Cairns, Mornington Island in the Gulf of Carpentaria (served by Sea Swift and a third party).

**Figure B: Scheduled destinations - NT**



25. Toll and Sea Swift (the **parties**) provide marine freight services to communities which include settlements adjoining mining projects, such as Gove, Groote Eylandt and Weipa, and communities of largely indigenous Australians. The populations of the destinations can be as low as 70 to 80 people (estimated population of Ugar/Stephen Island in the Outer Torres Strait Islands).
26. Most of the communities served by the parties cannot receive freight by road at all or in any significant volume. This is either because they are located on islands or because the roads to them are routinely not in good enough condition to handle trucks. A small number of the communities are able to receive limited road freight

in drier times of the year. In the NT these include Port Keats/Wadeye, Gove/Nhulunbuy and Numbulwar. In FNQ these include Bamaga-Seisia and Weipa.

27. A small number of the destinations have ports which are capable of receiving 'container vessels', which are small container ships. These destinations are usually the more populous and developed communities, such as those based around the mining projects.
28. Most of the other destinations can only receive flat-bottomed landing barges, which can land on rough concrete ramps or beaches.
29. Sea Swift and Toll Marine operate both container vessels and flat-bottomed landing barges.

## **Market inquiries**

30. On 10 December 2014 the ACCC commenced market inquiries regarding Sea Swift's proposal to buy the Toll Marine assets.
31. The ACCC received a large number of responses to its market inquiries.
32. Many submissions expressed concern about the impact the proposed transaction would have on competition for marine freight services.

## **Future with and without the acquisition**

33. Section 50 of the Act prohibits mergers or acquisitions that would have the effect or be likely to have the effect of substantially lessening competition in a market. In assessing a proposed acquisition pursuant to section 50 of the Act, the ACCC considers the effects of the acquisition by comparing the likely future competitive environment post-acquisition if the acquisition proceeds (the 'with' position) to the likely future competitive environment if the acquisition does not proceed (the 'without' position) to determine whether the proposed acquisition is likely to substantially lessen competition in any relevant market.
34. The ACCC is required to assess whether the state of competition would be substantially less with the proposed acquisition compared to the likely future without. The likely future without the acquisition is not always a continuation of the current conditions.
35. In this matter the ACCC is considering whether or not the future competitive environment without the proposed acquisition is likely to be similar to the current competitive environment.
36. Since at least the 1990s the NT and FNQ have each experienced periods of having only one provider of scheduled freight to many destinations, with periods in-between of competition, during which other companies have offered services until they have decided to leave the market or sell the business.
37. The merger parties have submitted to the ACCC that the relevant markets are only capable of sustaining one full service operator, by reason of:

- the 'base-load' demand required to support and underpin a full service offering;
- the high fixed costs and ongoing capital investment involved in providing a full service offering; and
- the limited and declining demand for scheduled shipping services.

38. The parties submit there is limited demand in each of FNQ and the NT to support the 'base-load' requirement. Furthermore, the parties submit that demand for scheduled shipping services in FNQ and the NT is also declining over time, due to the downturn in mining and project / infrastructure work, and also the changes in federal and state government funding to local councils (putting pressure on council spending).

39. The parties submit, therefore, that given the limited and decreasing demand for scheduled shipping freight services, the returns available in either FNQ or the NT at the prices that customers are willing to pay are not sufficient to sustain the minimum ongoing investment required for two providers to deliver scheduled shipping services on a profitable, sustainable basis.

40. The ACCC continues to assess whether, if the proposed acquisition does not proceed, competition in the relevant markets is likely to be less in the future than it is now. This includes assessing whether:

- market conditions in the future will be conducive to competition, taking into account matters such as demand levels and supply costs
- as an alternative to Sea Swift buying the Toll Marine assets, it is likely to be feasible for Toll Marine to retain its assets and continue to operate in competition with Sea Swift in the NT and/or FNQ
- the assets that Toll Marine currently uses to compete with Sea Swift in the NT or FNQ are likely to be deployed by someone else in competition against Sea Swift if Sea Swift does not acquire them.

### **Questions for interested parties**

The ACCC invites comments on the likely future competitive environment if the acquisition does not proceed.

In particular interested parties may wish to address the following questions:

- Is the future level of demand likely to be enough to support the supply of scheduled marine freight services in the NT and FNQ by more than one provider:
  - across the entire NT and FNQ markets?
  - only on certain shipping routes? or
  - only on certain combinations of shipping routes?

Please provide reasons for your answer.

- Do you agree with the parties' characterisation in paragraph 38 of the changes in

demand for scheduled shipping services in the NT and FNQ? How much has demand for freight changed?

- Is it likely that demand for scheduled marine freight services will increase or decrease in the short or medium term? Why/why not?
- Is it likely that costs for supplying scheduled marine freight services in the NT and FNQ will remain the same? If not, are they likely to decrease or increase?
- How much does the price of freight impact the quantity of products that you purchase? Please indicate if this depends on the types of products that you would have delivered.
- If Toll Marine does not sell its marine freight operations to Sea Swift would there be another likely buyer?

## Market definition

41. The ACCC's purpose in defining relevant markets is to assess the likely competitive effects of a proposed acquisition. The starting point for defining markets involves identifying the products actually or potentially supplied by the merger parties. The ACCC then considers what other products constitute sufficiently close substitutes to provide a significant source of constraint on the merger parties.
42. Based on information received by the ACCC to date, our preliminary view is that the markets relevant for assessing the competition effects of the acquisition are:
- markets for the supply of scheduled marine freight services<sup>3</sup>, in each of:
    - a. the NT; and
    - b. FNQ;
  - markets for the supply of charter marine freight services in each of the NT and FNQ;
  - markets for the supply of vehicle and marine fuel in each of the NT and FNQ.
43. However, as explained below, the ACCC is also considering whether the geographic scope of these markets should be narrower, such as an Outer Torres Strait Islands (**OTSI**) market or even a market confined to a particular route.
44. The ACCC ultimately may not need to reach a final view on the precise product or geographic boundaries of the markets. We consider that at this stage the exact market definitions are not likely to determine the assessment of the competition issues arising from the proposed acquisition.

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<sup>3</sup> As noted at paragraph 19, scheduled marine freight services includes services to both contracted and ad-hoc customers.



## **Product dimension for marine freight services**

### **Sea, land or air**

45. Market inquiries indicate that road and air freight are not close substitutes for seaborne-freight for most customers in the areas which the merger parties' marine freight services cover.
46. Air freight is significantly more expensive, even for low-weight, low-volume items. Some market participants have stated that air freight is best reserved for urgent, critical items. One market participant gave an example of an air-freight quote being more than five times the corresponding surface-freight quote.
47. As stated earlier, most of the communities the merger parties service cannot receive freight by road at all or in any significant volume. This is because they are located on islands or because the roads to them are routinely not in good enough condition to handle trucks or carry freight without unacceptable damage. A small number of the communities are able to receive limited road freight in drier times of the year.
48. The ACCC considers that, as a whole for the customers affected by this proposed acquisition, road and air freight do not constitute sufficiently close substitutes for Sea Swift's and Toll Marine's marine freight services to be included within the relevant market.

### **International shipping**

49. Ships travelling on routes between Australia and Asia travel along the NT and FNQ coasts.
50. However, market inquiries indicate that companies operating international shipping services are unlikely to commence providing marine freight services within the relevant geographic areas and therefore would not provide a significant constraint on the merged entity. This is because:
  - there are laws restricting the ability of foreign vessels to compete for domestic coastal trade. While the Australian government is currently reviewing these laws, it is unclear whether any significant reform will be implemented within the next two years; and
  - in any event, international vessels are not suited to servicing most of the destinations that Toll Marine and Sea Swift service. They are generally too big and cannot land at the facilities available at most ports in the relevant geographic markets.

### **Charter freight versus scheduled freight**

51. Customers wishing to receive freight into remote locations in northern Australia and the services they seek are generally categorised by the nature, volume and regularity of the customer's needs:
  - **Charter freight:** Some customers, such as mining, construction and energy-provider businesses require large, sporadic or one-off deliveries of plant, equipment and building materials. For example, island communities

occasionally need new sea walls and periodically there are large housing-construction projects for mining or indigenous communities.

- Scheduled freight:
  - a. **‘Contracted’ customers:** Some customers in the NT and FNQ regions require regular replenishment of basic inputs and supplies, including fuel for generators. Large and small retailers in the regions, ranging from a major supermarket chain to community-owned stores, require regular, reliable deliveries, particularly for perishable food. There is also some ‘back-loading’ of material out of the regions, including waste, vehicles, equipment and some seafood.
  - b. **‘Ad-hoc’ customers:** other customers require occasional freight services of items ranging from vehicles to household items.

52. The ACCC’s inquiries indicate that both customers and suppliers view and approach charter freight differently from scheduled freight.
53. On the customer side, large customers such as a mining company or government authority use scheduled Sea Swift or Toll Marine services to bring in batches of regularly required supplies, often under long-term (multi-year) contracts. The same parties or, for instance, a construction contractor, could charter Sea Swift, Toll Marine or another supplier to provide a dedicated vessel to bring in the materials needed for a defined project. This may be under a separate tender or contracting process to any general freight work done for the same customer.
54. For small or ad hoc shipping customers, chartering an entire vessel on a route from Darwin or Cairns is unlikely to be viable. For these customers the ability to place a consignment on a regular, scheduled shipping service is important.
55. On the supplier side, market inquiries suggest that scheduled freight providers are able to switch quite readily into providing shipping services for charter freight. Toll Marine and Sea Swift bid for and perform charter freight assignments, using owned or leased vessels.
56. However, it appears that businesses equipped for and experienced in providing charter freight may not be able to switch readily into scheduled freight. Relevant factors appear to include that a scheduled freight operator would require additional facilities such as warehouses and food-storage facilities (including refrigeration), different systems and infrastructure to manage more customers and smaller consignments, and more facilities and staff at the cargo’s destination.

### **Geographic dimension for marine freight services**

57. The merger parties both service the NT from Darwin and FNQ from Cairns. Market inquiries indicate that customers in the NT generally use supply chains starting at or passing through Darwin; and that a similar process starts at Cairns for FNQ customers. The ACCC understands that at times vessels have conducted runs crossing the NT/Queensland border but infrequently.
58. Accordingly, the ACCC considers that there are at least separate geographic markets for the supply of marine freight services in:
- the NT; and

- FNQ (which for the purposes of this document includes the Torres Strait).

59. The ACCC is also considering whether it may be appropriate to define geographic markets that are narrower than the NT or FNQ.

60. Sea Swift and Toll Marine currently overlap in the supply of scheduled marine-freight services to the following destinations in the NT and FNQ:

Table 1: Current overlapping routes for scheduled marine freight

NT	Sea Swift	Toll Marine	Other
Bickerton Island (East Arnhem)	Yes	Yes	
Croker Island / Minjilang (West Arnhem)	Yes	Yes	
Elcho Island (East Arnhem)	Yes	Yes	
Garden Point / Pirlangimpi (Tiwi Islands)	Yes	-	Teras
Goulburn Island / Warruwi (West Arnhem)	Yes	Yes	
Gove / Nhulunbuy (East Arnhem)	Yes	Yes	
Groote Eylandt (East Arnhem)	Yes	Yes	
Lake Evella (East Arnhem)	Yes	Yes	
Maningrida (West Arnhem)	Yes	Yes	
Milikapiti (Tiwi Islands)	Yes	-	Teras
Millingimbi (East Arnhem)	Yes	Yes	
Nguiu	Yes	-	Teras
Numbulwar (Gulf of Carpentaria)	Yes	Yes	
Paru (Tiwi Islands)	Yes	-	Teras
Port Keats / Wadeye (south-west of Darwin)	Yes	-	Teras
Ramingining (East Arnhem)	Yes	Yes	
Umbakumba (Groote Eylandt)	Yes	Yes	

<b>FNQ</b>	<b>Sea Swift</b>	<b>Toll Marine</b>	<b>Other</b>
Aurukun (western Cape York)	Yes	-	Carpentaria Contracting (wet season)
Badu (Outer Torres Strait Islands or OTSI)	Yes	Yes	
Bamaga (Cape York)	Yes	Yes	
Boigu (OTSI)	Yes	Yes	
Coconut (OTSI)	Yes	Yes	
Darnley (OTSI)	Yes	Yes	
Dauan (OTSI)	Yes	Yes	
Hammond (OTSI)	Yes	Yes	
Horn Island (Torres Strait)	Yes	Yes	
Kubin / Moa Island (OTSI)	Yes	Yes	
Lizard Island (eastern Cape York)	Yes	-	Carpentaria Freight
Lockhart River (eastern Cape York)	Yes	-	
Mabuiag (OTSI)	Yes	Yes	
Mornington Island	Yes	-	
Murray (OTSI)	Yes	Yes	
Saibai (OTSI)	Yes	Yes	
St Pauls / Moa Island (OTSI)	Yes	Yes	
Stephen Island / Ugar (OTSI)	Yes	-	
Thursday Island (Torres Strait)	Yes	Yes	
Warraber (OTSI)	Yes	Yes	
Weipa (western Cape York)	Yes	Yes	
Yam (OTSI)	Yes	Yes	
Yorke (OTSI)	Yes	Yes	

61. On the customer side, delivery from Point A to Point B is unlikely to be a close substitute to delivery from Point A to Point C, as the customer would be subject to additional cost and delay in transporting the goods from Point B to Point C. This may suggest that each shipping route should constitute its own geographic market.
62. However, if suppliers of freight services can switch quickly and without significant investment from one route to another, this may suggest that those routes should

be included within the same geographic market. Factors that may limit the ability of shipping providers to switch in this way include:

- sailing time, distance and conditions (including tides). For instance, providers may not be able to add extra destinations to a run or extend it easily if they are to maintain reasonable frequency to each destination and allow for maintenance and turnaround times
- the types of vessels required on different routes
- the number and nature of customers. For example, whether there is a high-volume customer or community on the route such as a mining operation
- ability to access infrastructure such as ramps and obtain landing permissions and suitable berthing time slots.

63. We have also received submissions that the financial viability of servicing the OTSI is dependent on the traffic on the Cairns-Thursday Island-Horn Island-Weipa route and that FNQ should therefore be treated as a single geographic market.

64. The ACCC is considering whether differences between regions and routes in the NT and FNQ limit the ability of suppliers to operate particular routes or switch between them.

### **Charter freight markets**

65. As discussed above, the ACCC considers that there may be separate product markets for the supply of charter freight services to larger customers who require sporadic or once-off deliveries of a size that justifies using a dedicated vessel.

66. The ACCC considers that there are likely to be separate geographic markets for charter marine freight services in each of the NT and FNQ. Currently, companies (other than Sea Swift and Toll Marine) which provide charter freight services tend to service either the NT or FNQ, but not both.

### **Fuel markets**

67. Sea Swift and Toll Marine each deliver fuel to customers on behalf of fuel companies as part of the marine freight services they provide. However, in some cases Sea Swift and Toll Marine actually purchase the fuel (e.g. from the terminal gate) and both transport and sell it to customers.

68. Sea Swift also sells fuel from ships, as part of the mothershipping service it provides in FNQ and from several ports in FNQ. Toll Marine sells fuel direct from the hull of its vessels and also from certain bulk storage facilities at ports in the NT and FNQ.

69. The ACCC therefore considers that Sea Swift and Toll Marine compete in the supply of fuel to fishing vessels and other customers in the NT and FNQ. While Sea Swift may not currently supply fuel in the NT, it appears to be at least a potential supplier in this region, given its existing shipping operations there.

The ACCC considers that there are likely to be separate markets for at least vehicle fuels (unleaded petrol and diesel) and marine fuel, but is seeking further information

about the types of fuel used by customers in these regions, and the suppliers/locations from which fuel is purchased.

### Questions for interested parties

The ACCC invites comments from interested parties on its preliminary views on market definition.

Interested parties may wish to address the following questions:

- How readily could charter freight operators switch or expand into providing scheduled freight or otherwise act as a competitive constraint on Sea Swift's scheduled freight operations?
- If a charter freight operator were to expand to provide scheduled freight services, what assets and facilities would they require to provide these services?
- Is the level of competition in the supply of marine freight services likely to vary significantly between different parts of the NT or different parts of FNQ (for example in terms of the types of services demanded by customers or any issues which affect the ability of suppliers to extend services to certain locations)? In answering this question you may wish to consider the following regions:
  - Port Keats / Wadeye
  - the Tiwi Islands
  - Gove
  - Groote Eylandt
  - Arnhem Land communities outside Gove and Groote Eylandt
  - Weipa
  - Thursday and Horn Islands
  - the OTSI, or
  - any other region or route?
- How easy is it for a provider of freight services currently operating in the NT to begin providing services in FNQ (or vice versa)?
- How easy is it for a provider of freight services to switch from providing scheduled shipping services on one route to another (whether within or across the NT or FNQ)?
- How easy is it for a provider of freight services to switch from providing scheduled shipping services on a small number of routes, to an expanded network of destinations?

## **Issue of concern: Likely increase in price and/or decreased service levels in the supply of scheduled marine freight services in the NT and FNQ**

70. The ACCC's preliminary view is that the proposed acquisition is likely to substantially lessen competition in the relevant markets for the supply of scheduled marine freight services. The following section describes the ACCC's preliminary concerns in this regard and provides details of further information that is being sought from interested parties.

### **Market concentration**

71. Currently Sea Swift and Toll Marine are the only providers of scheduled freight services on most routes within the relevant NT and FNQ markets. As noted in the geographic market definition section above, while there are some routes in the NT where another company or other companies are also providing scheduled freight services, these are limited.
72. Accordingly, the proposed acquisition would involve a very significant increase in concentration in the relevant scheduled freight markets, and would result in Sea Swift obtaining a monopoly on many routes.

### **Removal of a vigorous and effective competitor**

73. As noted above, market inquiries have indicated that Sea Swift and Toll Marine have competed strongly with each other in recent years. Sea Swift historically only operated in FNQ and Toll Marine historically only operated in the NT and on the Cairns-Weipa route. However, in 2013 Sea Swift acquired Tiwi Barge Company and began to expand its services in the NT in competition with Toll Marine. The ACCC understands that in late 2013, Toll Marine expanded its FNQ services into the Torres Strait and top of Cape York in competition with Sea Swift.
74. Many market participants submitted that having two operators on routes in the NT and FNQ has led to significant price decreases compared to the previous situation where there was only one operator. Market participants also provided examples of service improvements obtained as a result of competition between Sea Swift and Toll Marine, such as increased frequency of services and better responses when goods have been damaged.

### **Countervailing power**

75. On some of the routes in the relevant markets there are large customers, such as Rio Tinto, GEMCO/BHP Billiton, fuel providers and Woolworths. These customers are important in underpinning 'base-load' volumes on these routes, given the high fixed costs associated with running a shipping service.
76. These large customers may be dissatisfied with having only one marine freight provider to choose from. This may be due in part to the desire for a 'back up' provider in case an unexpected event were to prevent Sea Swift from providing the services, given the heavy reliance of these remote communities on the shipping service.
77. The ACCC is therefore considering whether large customers would have the ability and incentive to sponsor entry by a new provider, and the extent to which this

would be likely to constrain Sea Swift from increasing prices or reducing service levels post-acquisition.

78. There appears to be some potential for major customers to sponsor, or threaten to sponsor, entry of new marine freight providers, particularly on the routes with larger volumes such as Darwin to Gove and Cairns to Weipa. However, market inquiries have suggested that this could take two years or longer, as these large customers may have strict processes for accepting new suppliers.
79. It is also not clear whether this would necessarily flow through to increased competition for ad hoc customers. For example, in the short to medium term a large customer might use a tender process simply to identify potential new suppliers and use this to force the incumbent provider to reduce its prices, without actually awarding the contract to the potential entrant. In this scenario, smaller or ad hoc customers would continue to be reliant on the incumbent (monopoly) provider, notwithstanding the presence of a potential new entrant.

#### **Likelihood of entry or expansion by other marine freight providers**

80. The ACCC considers that there are likely to be barriers to entry to the relevant markets that make it difficult for a new entrant to enter on a small scale and then expand. Substantial investment is required upfront, in ships and/or barges, staff, distribution/warehousing facilities and freight-processing systems.
81. Providers of scheduled marine freight services typically have warehouses/depots, chiller and freezer facilities and open hardstands or 'laydown' areas at their origin points. Some smaller destinations do not require suppliers to have receiving facilities (other than a barge ramp). For example, at small ports the freight provider may just drive a forklift down the landing barge's open ramp onto the beach for customer collection. However, at larger ports, such as trans-shipment or high-volume points, they may require facilities such as warehouses and laydown areas. Some of these assets may be able to be leased, reducing the upfront cost to a new entrant.
82. A significant barrier is the need to obtain a contract with a large customer to underpin volumes. There are a relatively small number of these customers on each route, and they tend to have contracts with marine freight providers that last for several years (although some customers may have 'dual source' contracts which allow them to use multiple providers). Without a commitment from a large customer, a potential new entrant is unlikely to make commitments to lease or purchase the necessary assets. However, a customer may be reluctant to award a contract to a potential new entrant which does not yet have the necessary assets to provide the service.
83. Another potential barrier is access to the relevant ports. The ACCC understands that most of the relevant ports in the NT and FNQ are operated as common user facilities which allow any shipping provider to access them, subject to paying any applicable fees and complying with scheduling and other requirements. An exception is the port of Gove.
84. Toll Marine accesses the port of Gove pursuant to a lease with the Aboriginal Land Trust, which expires 20 November 2024. Toll Marine has exclusive rights to use this port, but makes access available to third parties for a fee. Third party access to the facilities at the port of Gove is governed by a court enforceable undertaking given to the ACCC in 2003 and revised in 2005.



85. Even at ports where access is theoretically available, market inquiries have indicated that there may be practical limitations which make it difficult for a new entrant to gain suitable port access. For example, on small islands where there is limited space for ramps or storage, a new entrant may be forced to accept less favourable berthing timeslots or limited storage space at the wharf. Lack of access to appropriate berthing timeslots can be compounded by the large tidal variations in the relevant regions, which create a narrow window for access to some ports. These factors may limit the ability of a new entrant to provide a service that is competitive with Sea Swift's.
86. In relation to the NT, the ACCC's market inquiries to date have suggested that there is some potential for entry or expansion of other scheduled freight providers within the next two years. However, it is not clear whether this would be sufficient to constrain Sea Swift from raising prices or decreasing service levels. For example, a new entrant might only service the major ports such as Gove and Groote Eylandt, leaving customers at smaller destinations in Arnhem Land reliant on Sea Swift.
87. In relation to FNQ, the ACCC's market inquiries to date have not indicated that there is likely to be, within the next two years, entry or expansion of other scheduled freight providers on any significant scale. Therefore the threat of entry in FNQ appears unlikely to constrain Sea Swift post-acquisition.
88. The ACCC is also considering the minimum scale needed to commence operating a scheduled shipping service in either the NT or FNQ markets and whether this may be a barrier to entry. Some information received by the ACCC has indicated that in order to recover the fixed costs associated with operating scheduled services it is unviable for a new competitor to only enter a single route. Instead entry may require the new competitor to service multiple destinations.

#### **Preliminary conclusion – supply of scheduled freight services in the NT and FNQ**

89. The ACCC is concerned that the proposed acquisition is likely to substantially lessen competition in the supply of marine scheduled freight services in the relevant NT and FNQ markets. There do not appear to be effective competitive constraints, or a credible threat of new entry or expansion, that would prevent Sea Swift from increasing prices post-acquisition. Although some large customers may have a degree of countervailing power, this will not necessarily lead to competition that will benefit smaller ad hoc customers in the communities.
90. Market participants have stated that because most of the communities in the relevant markets are heavily reliant on the scheduled marine freight services that the parties provide, an increase in prices or deterioration in services levels could have a significant impact on these communities' standard of living. Some market participants suggested that an increase in shipping rates could force the local authorities to scale back some of the services that they provide to their communities.

#### **Questions for interested parties**

The ACCC invites comments from interested parties on its preliminary concerns.

Interested parties may wish to address the following questions:

- Do you consider that the proposed acquisition is likely to lead to higher prices or lower service levels for scheduled marine freight services in the NT or FNQ? Why/why not?
- Please provide any examples of where competition between Sea Swift and Toll Marine has led to decreased prices or increased service levels.
- To what extent do existing operators such as Carpentaria Contracting, Carpentaria Freight and Ezion/Teras act as a constraint on Sea Swift and Toll Marine? Are there any other operators that may act as a constraint on Sea Swift and Toll Marine's scheduled freight services?
- How likely is it that large customers in the relevant areas would award a contract to a new company to facilitate competition on the routes where Sea Swift already operates?
- How significant are the upfront costs that would be faced by a potential new entrant? Are there ways of reducing these costs, such as leasing assets instead of purchasing them?
- How difficult is it for a new entrant to gain access to the relevant ports? Please identify any ports where there may be access difficulties and explain why the difficulties arise.
- Has it been difficult for third parties to gain access to the port of Gove? Has the 2003 undertaking been effective in providing access to third parties at the port of Gove?
- What ports or landing facilities may be used as an alternative to the Toll Marine facility at the port of Gove? If there are alternatives, are there any limitations on their suitability for serving certain types of customers? For example, are they suitable for supplying large customers? Please provide any examples of the ease or difficulty of negotiating price and non-price terms of access to the port of Gove.
- What is the minimum amount of resources needed for a competitor to commence offering scheduled services in the NT or FNQ? What vessels, port side equipment and customers would be required?
- What is the minimum level of shipping services and destinations that a new entrant would need to offer to customers for new entry to be viable?

### **Issue that may raise concerns: Potential increase in price and/or decreased service levels in the supply of chartered marine freight services in the NT and FNQ**

91. The ACCC is considering whether the proposed acquisition is likely lead to increased prices or decreased service levels in the supply of charter marine freight services in the NT and/or FNQ.
92. The charter services markets in the NT and FNQ are less concentrated than the scheduled freight markets. While Sea Swift and Toll Marine appear to be the major providers of charter services in the relevant geographic areas, there are

other providers such as (in the NT) Teras (Ezion), Bhagwan Marine and Sealink Barges; and (in FNQ) Carpentaria Contracting and Pacific Marine Group.

93. However, some market participants suggested that these other providers may not impose a strong competitive constraint on Sea Swift post-acquisition. Some of these other providers may not presently be in a position to meet the requirements of all customers for charter freight services. For example, they may be too small and not have a sufficient number of barges.
94. The ACCC's preliminary view is that entry or expansion in the charter freight markets is more likely than in the scheduled freight markets. The infrastructure that a new charter freight provider would require is not as extensive as a scheduled freight service provider would require. However, as with scheduled freight services, market participants have suggested that practical issues with accessing the relevant ports may limit entry or expansion in these markets

### **Questions for interested parties**

The ACCC invites comments from market participants on its preliminary views on the potential impact of the proposed acquisition on competition for the supply of charter freight services.

Market participants may wish to address the following questions:

- Are there charter freight service providers in the NT or FNQ which provide an acceptable alternative to Sea Swift/Toll Marine? Please identify any such providers.
- Do you consider that the proposed acquisition is likely to lead to increased prices or decreased service levels for charter freight services in the NT or FNQ? Why/why not?
- How easy would it be for a new charter freight provider to enter the market, or an existing small provider to expand their services? What resources would they need in order to do so?

### **Issue that may raise concerns: Potential increase in the price of fuels in the NT and FNQ**

95. As noted in the market definition section above, Swift and Toll Marine each supply fuel to customers in FNQ.
96. Some market participants noted that the price of fuel has decreased significantly since Toll Marine began selling fuel in competition with Sea Swift.
97. The ACCC understands that the supply of fuel is a vital input for coastal communities, and that the number of suppliers varies between regions.
98. The ACCC understands that there are other suppliers of fuel in most parts of the NT and FNQ which the parties service, although in locations such as the OTSI the options appear to be limited. Further, to the extent that competing fuel suppliers would be reliant on Sea Swift to transport their fuel to the retail locations post acquisition, they may be limited in their ability to compete with Sea Swift, because

Sea Swift would have the ability (and potentially the incentive) to increase the delivery costs for competing fuel suppliers to a level which makes competition unviable.

99. The ACCC requires more information in order to make a full assessment of the competitive effects of the proposed acquisition on the supply of fuel.

The ACCC invites comments from market participants on its preliminary views on the potential impact of the proposed acquisition on competition for the supply of fuel.

Interested parties may wish to address the following questions:

- What type of fuel do you buy? How do you use the fuel? Would other types of fuel be suitable for your requirements?
- From which locations do you buy the fuel? Why?
- Besides Sea Swift and Toll Marine, what are your other options for fuel supply?

## **Proposed undertaking by Sea Swift to address competition concerns**

100. The merger parties have offered a court-enforceable undertaking to the ACCC in relation to the proposed acquisition. Broadly, the undertaking offered comprises three components:

- Access commitments which require Sea Swift to provide access to port facilities at the port of Gove in the NT to third parties and to ensure that access is provided on commercially reasonable, non-discriminatory terms;<sup>4</sup>
- Service commitments which require Sea Swift to maintain a base level of frequency of its scheduled services. This base level is set below the current combined offering of the parties; and
- Price commitments which set a base price cap for freight charges, plus variable costs (e.g. fuel, port charges). The price commitments are designed to be adjusted by CPI each year. In addition the parties would commit to not increase prices 'unreasonably' and may increase the base price if there is 'reasonable evidence' that there has been an increase in unit costs.

101. The Parties state that they have proposed the undertaking to provide public assurance, particularly to smaller / ad hoc customers, that regular, committed,

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<sup>4</sup> The ACCC notes that there is currently an undertaking in place for the Port of Gove. In 2003, the ACCC decided not to oppose, subject to undertakings, the acquisition by Toll Marine's predecessor, Perkins shipping group, of northern-Australian marine freight provider Gulf Freight Services. The ACCC had concerns about the acquisition and accepted from Perkins a court-enforceable undertaking requiring Perkins to provide access to the Gove/Nhulunbuy wharf and to publicise its service charter and dispute resolution processes to remote communities. When Toll Marine acquired Perkins in 2009 it assumed responsibility for the 2003 undertaking.

reasonably priced and reliable coastal and community shipping services will continue to be provided to remote and indigenous communities in the NT and FNQ.

102. In deciding whether to accept an undertaking, the ACCC needs to consider whether the proposed undertaking will be effective in addressing the competition concerns raised. The ACCC also considers a range of other factors including whether the undertaking imposes clear and unambiguous obligations on the party giving the undertaking, the difficulties in fulfilling the proposed obligations, monitoring and compliance costs, and the risk of non-compliance.
103. The ACCC's preliminary view is that the price and service commitments in the proposed undertaking are likely to be complex to implement, monitor and enforce. Assessing the reasonableness of the minimum levels of prices and services and any changes to these will require substantial and ongoing information gathering and processing. The ACCC is concerned that this would limit the effectiveness of the proposed undertaking for addressing the competition issues raised by the proposed acquisition. More generally, the ACCC is concerned that any price or service commitments may have distortive effects on the relevant markets. If the undertaking sets price levels too high or service levels too low, it will not address the potential competition concerns raised by the proposed acquisition. Conversely, if the undertaking sets the level of service too high or the price levels too low it will cause economic waste by requiring the inefficient deployment of capacity on the routes, and may deter other providers from entering the market.

## ACCC's future steps

104. The ACCC will finalise its view on this matter after it considers submissions invited by this Statement of Issues.
105. The ACCC now seeks submissions from market participants on each of the issues identified in this Statement of Issues and on any other issue that may be relevant to the ACCC's assessment of this matter.
106. As noted above, submissions are to be received by the ACCC no later than **13 March 2015** (send to [mergers@acc.gov.au](mailto:mergers@acc.gov.au)).
107. The ACCC intends to publicly announce its final view by 16 April 2015. However the anticipated timeline may change in line with the Merger Review Process Guidelines. A Public Competition Assessment for the purpose of explaining the ACCC's final view may be published following the ACCC's public announcement.