



AUSTRALIAN
COMPETITION
& CONSUMER
COMMISSION

Statement of Reasons

In respect of a notification lodged by
Gladstone Ports Corporation Limited
in respect of
exclusive dealing for towage services
for the Port of Gladstone

Date: 19 July 2018

Notification number: N10000453

Commissioners: Keogh
Rickard
Court
Featherston

Summary

The Australian Competition and Consumer Commission (ACCC) has decided not to take further action at this time in respect of the exclusive dealing notification lodged by Gladstone Ports Corporation Limited in respect of the provision of harbour towage services at the Port of Gladstone in Queensland.

The legal test applied by the ACCC requires an assessment of the effects on competition and the likely public benefits and detriments from these arrangements.

The ACCC may act to remove the protection afforded by the notification at any time if it is satisfied that the conduct is likely to substantially lessen competition and that the likely benefit to the public from the notified conduct will not outweigh the likely detriment.

Gladstone Ports Corporation Limited intends to require all vessels requiring towage services at the Port of Gladstone to use the services of the holder of the exclusive 'tug licence' for the Port of Gladstone for a term of up to eight years, ending on 31 December 2027. The exclusive licence will be granted following a competitive tender process. A similar exclusive licensing arrangement has been in place since 1 January 2011 and expires towards the end of 2018.

Although granting an exclusive licence prevents other towage operators from offering their services at the Port during the exclusive licence period, Gladstone Ports Corporation submits that the greater certainty this licence provides will attract the strongest possible field of potential towage service providers and lead to the best outcome for users.

The alternative to the proposed exclusive licence for the provision for towage services would be for the port operator to grant one or more non-exclusive licences. Both types of arrangements (exclusive or non-exclusive licences) can provide for competition. Which approach is more likely to lead to stronger competition in a particular port will depend on the circumstances of that port and the service providers at that time.

The ACCC has decided not to take further action at this time because the notified conduct is unlikely to result in a substantial lessening of competition and the conduct is unlikely to result in public detriments that outweigh the public benefits.

Introduction

1. On 13 March 2018, Gladstone Ports Corporation Limited (**GPC**) lodged exclusive dealing notification N10000453 with the Australian Competition and Consumer Commission (**ACCC**).¹ GPC intends to conduct a competitive tender process for the provision of harbour towage in the Port of Gladstone (**the Port**). An exclusive licence will be granted to one towage service provider for a period of up to eight years.
2. The ACCC is the Commonwealth agency responsible for enforcing the *Competition and Consumer Act 2010* (**the Act**). A key objective of the Act is preventing anti-competitive arrangements or conduct, thereby encouraging

¹ Businesses can obtain protection from legal action under the *Competition and Consumer Act 2010* for exclusive dealing by lodging a notification with the ACCC.

competition and efficiency in business, resulting in greater choice for consumers in prices, quality and service.

3. Broadly, exclusive dealing occurs when one person trading with another restricts the other's freedom to choose with whom, in what or where it deals.
4. Exclusive dealing is common in many business arrangements. Importantly, changes to the Act on 6 November 2017 mean that all forms of exclusive dealing only breach the Act if the restriction is likely to have the purpose, effect or likely effect of substantially lessening competition.
5. The protection from legal action provided by a notification automatically commences on the day the notification is validly lodged with the ACCC. The protection will continue unless or until the notification is revoked or withdrawn.
6. While a notification is in force, the business is able to engage in the exclusive dealing conduct as described in the notification without the risk of breaching the exclusive dealing provisions of the Act.
7. The ACCC may revoke an exclusive dealing notification at any time if it is satisfied that it has the purpose, effect or likely effect of substantially lessening competition, and that the likely benefit to the public will not outweigh the likely detriment to the public from the conduct.²
8. The ACCC is not required to provide a statement of reasons where it has decided to take no further action in relation to a notification. However where, as in this case, interested parties have made submissions in relation to the proposed conduct, the ACCC will generally prepare a statement of reasons to provide greater transparency regarding its decision-making.

The notification

9. GPC is proposing to:
 - require all vessels requiring towage services at the Port to use the services of the holder of the exclusive 'tug licence' for the Port for the period commencing 1 January 2020 and expiring no later than on 31 December 2027
 - commence engaging in the notified conduct by awarding a new exclusive licence through a competitive tender process to provide harbour towage services at the Port for a term of up to eight years(the **Notified Conduct**).³
10. GPC proposes to grant an exclusive licence for a five-year period with an option to extend the licence for a further three years, exercisable by GPC.

² The ACCC conducts a comprehensive and rigorous public consultation process before making a decision to revoke a notification. In doing so, The ACCC follows the process set out in section 93 of the Act.

³ More information about Gladstone Ports Corporation Limited notification is available on the [ACCC Public Register](#).

11. GPC submits that the Notified Conduct will result in public benefits including:
- Increased competitive pressure – the certainty created by exclusivity will lower the risk premium for tenderers and will allow tenderers to offer lower pricing proposals without compromising service levels.
 - Lower costs and efficiencies for Port users – the competitive pressure generated by a competitive tender process for an exclusive licence will generate lower costs and create efficiencies for Port users for the duration of the licence because:⁴
 - the returns to scale for the towage service providers at the Port would not decrease until the Port achieves substantially greater throughput than it is currently forecast to achieve over the eight year term of the proposed licence
 - the unique characteristics of the Port’s single lane channel and its trade and vessel mix mean it would be inefficient for two towage service providers to operate in the Port without substantial capital expenditure to widen the channel
 - the tender process will require all tenderers to commit to pricing principles for standard harbour and liquefied natural gas (LNG) towage services for the duration of the new exclusive licence.
 - Avoiding costs and inefficiencies arising from the absence of exclusivity – such as the cost of constructing and managing a second berthing facility.
12. GPC also submits that the Port will not support an efficient and successful second towage operator between 1 January 2020 and 31 December 2027. The Notified Conduct will avoid the costs of an unsuccessful second towage operator, and the costs of installing and coordinating a second facility at the Port to berth the tug boats of a second towage operator. Consequently, GPC submits that the Notified Conduct will not have the effect or likely effect of substantially lessening competition in any market or result in any public detriment.
13. GPC engaged PricewaterhouseCoopers Consulting (Australia) Pty Limited (**PwC**) to:⁵
- Assess future towage options as defined by GPC.
 - Identify the towage service option that promotes greatest operational and economic efficiency within the Port while ensuring GPC meets its statutory obligations under the relevant Act.
 - Consider the best mechanism to deliver towage services at the Port to ensure operational and economic efficiency for the period following the current licence, including assessing the likely public benefits and detriments of that approach.

⁴ Gladstone Ports Corporation, *Submission in support of notification for exclusive dealing*, 13 March 2018, (**GPC submission, 13 March 2018**) available: [ACCC Public Register](#).

⁵ PricewaterhouseCoopers Consulting (Australia) Pty Limited (**PwC**), *Future Towage arrangements at the Port of Gladstone*, (**PwC Report**) 13 March 2018, p. 1, available: [ACCC Public Register](#).

14. PwC concluded that:⁶

- The most cost efficient towage option for the Port continues to be a single provider.
- Competition between multiple towage providers is unlikely to be sustainable, nor in the best interests of Port users.
- The factors considered by the ACCC in its previous assessment of the Gladstone towage market still hold.
- Subject to a rigorous competitive tender process, an exclusive licence for towage services is the most effective means of achieving competition in the Port.
- In arriving at these conclusions, PwC considered, amongst other things, five potential options to assess the future towage market configuration at the Port and to test whether the size of the future towage market has reached the point where the economies of scale for a single towage provider are exhausted. These options ranged from one provider servicing all Port users (option 1), two or more providers servicing various market segments (options 2, 3 and 4) and an open market model (option 5).⁷
- PwC submits that a fully contestable market for towage services is unlikely to be feasible, and if implemented, cross-hiring arrangements would likely occur, effectively replicating one of the other towage configuration options. As a result, option 5 was not considered in detail and did not form part of the cost modelling exercise conducted by PwC.⁸

Statutory test for notifications

15. The Act allows a business to obtain legal protection to engage in exclusive dealing conduct that might otherwise breach section 47 of the Act by lodging an exclusive dealing notification or obtaining authorisation for the conduct.
16. Broadly, exclusive dealing occurs when one person trading with another restricts the other's freedom to choose with whom, in what or where it deals.
17. Exclusive dealing is common in many business arrangements. Changes to the Act on 6 November 2017 mean that all forms of exclusive dealing only breach the Act if the restriction is likely to have the purpose, effect or likely effect of substantially lessening competition.
18. The ACCC assesses exclusive dealing notifications by applying the test in section 93(3) of the Act.⁹ The test requires that in order for the ACCC to revoke a notification, it must be satisfied that the notified conduct:
 - has the purpose, effect or likely effect of substantially lessening competition, and

⁶ PwC Report, p. ii-iv, available: [ACCC Public Register](#).

⁷ PwC Report, pp. 29-35, available: [ACCC Public Register](#).

⁸ PwC Report, pp. 29-35, Available: [ACCC Public Register](#).

⁹ See the ACCC's [Exclusive dealing notification guidelines](#) for more information.

- in all the circumstances, will not result in likely public benefit which would outweigh the likely public detriment.

Background

The Port

19. The Port is located approximately 525 kilometres north of Brisbane and is Queensland's largest multi-commodity port, with the world's fourth-largest coal-export terminal. Other products exported from the Port include LNG, alumina, aluminium and bauxite. The Port has 20 wharves.
20. In the 2017 financial year, the Port hosted approximately 1800 vessels and handled approximately 120 million tonnes of cargo. Cargo comprised 57 per cent coal, 16 per cent LNG and about 22 per cent related to the alumina industry.
21. There are currently ten tugs (plus one spare tug held in reserve) providing towage services at the Port. The fleet is divided into an LNG fleet (which primarily services the LNG users) and a standard harbour fleet (which is predominantly used to service the other Port users).
22. Characteristics of the Port include:¹⁰
 - A harbour channel distance of 23.2 nautical miles, with the longest towage task being from the tug base, to the 'LIMA' pilot boarding ground and then to one of the LNG wharves being a distance of 46 nautical miles.
 - Variable duration of tug jobs, from 40 minutes to 9.25 hours, dependent on the vessel type, transit, destination and tidal influence.
 - In comparison to other ports, on average, the number of tug jobs per vessel are higher due to the number of tugs required to safely execute certain manoeuvres. For example, LNG vessel movements require four tugs per vessel movement and Panamax ebb tide arrival movements require three tugs per movement.
23. The Port is managed by GPC, a corporatised government-owned entity with shares held by the Deputy Premier, Treasurer and Minister for Aboriginal and Torres Strait Islander Partnerships and the Minister for Transport and Main Roads on behalf of the Queensland Government. GPC also owns and operates a number of cargo handling facilities in the Port.
24. Under the *Transport Infrastructure Act 1994* (Qld), GPC's approval is required to operate a tug service in the Port.

Exclusive licences for towage services

25. The granting of an exclusive towage service licence results in one provider being granted the right to provide towage services in a port for a specified period. It prevents entry of other service providers for the duration of the licence term. Exclusive licences therefore preserve a monopoly for the incumbent towage provider for the duration of the contract.

¹⁰ PwC Report pp. 26-27, available: [ACCC Public Register](#).

26. In 2002, the Productivity Commission examined the Australian harbour towage industry in its report *Economic Regulation of Harbour Towage and Related Services (the Productivity Commission Report)*.¹¹ The Productivity Commission noted that a competitive tender for an exclusive licence is an alternative means of allocating the towage 'market' to a single provider at a port — and a means by which users potentially can have a greater influence on the choice of supplier. It is an alternative to allocation by virtue of incumbency, by a limited period of head-to-head competition (a price 'war') or by way of a takeover.¹²
27. The Productivity Commission also stated that a potential advantage of a competitive tender for an exclusive licence is that the resource costs of a price war are avoided. For this reason, a competitive tender can extract prices closer to current (and foreseeable) efficient costs — how close will depend largely on the extent of competition between bidders and the rigour of the tender process. The main potential advantage of a contract or licence for a set period is the certainty it provides — which, in particular, allows for specific investments to be recouped.
28. Harbour towage services for the other Queensland Ports of Cairns, Mourilyan, Lucinda, Townsville and Mackay are provided via exclusive licence.

Non-exclusive licences for towage services.

29. A non-exclusive licence allows for multiple service providers to provide towage services to port users. A new entrant could enter a port in competition with the incumbent and provide towage services but with no guarantee of market share unless it entered after agreeing to service a particular port user. Any new entrant would face the prospect of head-to-head competition with the incumbent and over time, with other potential entrants.

Current licensing arrangement at the Port

30. Smit Marine Australia Pty Ltd (**Smit Marine**) was granted the current exclusive licence for the Port.¹³ The Gladstone Harbour Towage Licence, provides that all vessels requiring harbour towage services at the Port use a single towage service provider.
31. When the current exclusive licence arrangement began it was considered 'third line forcing', which was prohibited, regardless of its effects on competition unless the conduct was immunised by the ACCC.
32. GPC notified the ACCC of this conduct in order to obtain legal immunity in 2009 via notification N93770. The ACCC allowed GPC's notification to stand. The exclusive licence commenced on 1 January 2011 for an initial five-year term. The optional extension was exercised by GPC in 2015 and the exclusive licence will expire on 31 December 2018.

¹¹ Productivity Commission, *Inquiry Report No.24, Economic Regulation of Harbour Towage & Related services, (Productivity Commission Report)* 20 August 2002, available: [Productivity Commission Report](#).

¹² Productivity Commission Report, p. XXXV, available: [Productivity Commission Report](#).

¹³ In 2014, Smit Marine became a wholly owned subsidiary of Smit Lamnalco Towage Australia Pty Ltd.

Previous notifications

33. The Port Authority for the Port has lodged several previous exclusive dealing notifications for harbour towage services that were allowed to stand including:
- N93770 – Lodged on 6 February 2009 by GPC.¹⁴
 - N93738 – Lodged on 6 January 2009 – to provide a six-month extension of the arrangements notified in N92443.¹⁵
 - N92443 – Lodged on 21 March 2006 by Central Queensland Ports Authority.¹⁶
 - N90695 – Lodged on 13 July 1999 by Gladstone Port Authority.
34. On 23 November 2011, Svitzer Australia Pty Ltd (**Svitzer**) asked the ACCC to review notification N93770. On 27 June 2012, the ACCC issued a statement of reasons detailing why it was not proposing to take further action in relation to this matter.¹⁷

Consultation

35. The ACCC invited submissions on GPC's notification from a wide range of interested parties. Copies of all public submissions are available on the [ACCC's public register](#).
36. Seven interested parties made public submissions. Two of these interested parties made two submissions.
37. GPC also made submissions responding to interested party submissions.

Submissions in support of the Notified Conduct

38. Smit Lamnalco Towage Australia Pty Ltd (**Smit Lamnalco**) is a towage service provider operating 40 vessels providing harbour and terminal towage services in 10 Australian ports including Gladstone, Mackay, and Townsville as well as subcontract operations with another towage provider in the ports of Brisbane, Sydney, Melbourne and Newcastle. Smit Lamnalco supports the notification in respect of a new exclusive licence for towage services in the Port. Smit Lamnalco submits that the net public benefits of granting a new exclusive licence are likely to be substantial and will clearly outweigh any detriments to the public.¹⁸

¹⁴ Details of [N93770](#) are available on the ACCC public register.

¹⁵ Details of [N93738](#) are available on the ACCC public register.

¹⁶ Details of [N92443](#) are available on the ACCC public register.

¹⁷ See the [ACCC public register](#) for more information.

¹⁸ Smit Lamnalco Towage Australia Pty Ltd, *Public register version submission to the Australian Competition and Consumer Commission regarding exclusive dealing notification N10000453 lodged by Gladstone Ports Corporation Ltd, 6 April 2018 (Smit Lamnalco submission, 6 April 2018)*, available: [ACCC Public Register](#).

39. The Australian Maritime Officers Union (**AMOU**) supports allowing the notification to stand provided the tender meets requirements regarding employment, remuneration, safety and operating standards.¹⁹
40. The Port Authority of New South Wales supports the Notified Conduct. The efficiency and safety of port operations is enhanced by the ability of the Port Corporation to mandate towage operators to hold certain minimum capability and commit to levels of responsiveness and service.²⁰
41. Rio Tinto submits that it has no objection to the proposed arrangements on the basis that appropriate governance apply to the tender process, including consultation with all significant Port users and safeguard mechanisms be included to protect the legitimate interests of all Port users.²¹

Submissions opposing the Notified Conduct

42. Svitzer is a subsidiary of AP Moller-Maersk and is a global provider of towage services, salvage and emergency response services terminal towage and salvage. Svitzer opposes the notification because it considers the Notified Conduct is likely to have an anticompetitive effect in the market for towage services in Gladstone. Svitzer engaged Synergies Economic Consulting (**Synergies Consulting**) to conduct economic analysis to support its views.²²
43. Synergies Consulting set out a number of concerns with the assumptions and arguments made in support of continuing the current exclusive licensing arrangement at the Port:²³
 - GPC has not reasonably demonstrated that economies of scale in towage service provision are so large that a single towage operator at the Port is the most efficient market structure.
 - GPC has not given sufficient weight to the effectiveness of potential entry to discipline the market behaviour of an incumbent operator. Sunk costs are not a significant factor in towage service provision, which means that the towage market at a port is contestable, even if it is serviced by a sole provider.
 - GPC has assumed that demand can be reliably predicted at the Port over an eight-year period and that GPC is best placed to determine the towage requirements of Port users. Exclusive licensing eliminates the ability of individual users and groups of users to seek out and negotiate commercial agreements with towage services providers that meet their individual or

¹⁹ The Australian Maritime Officers Union (AMOU), *Submission on the exclusive dealing notification*, 6 April 2018, (**AMOU submission, 6 April 2018**), available: [ACCC Public Register](#).

²⁰ The Port Authority of New South Wales, *Submission on exclusive dealing notification N10000453*, 6 April 2018, available: [ACCC Public Register](#).

²¹ Rio Tinto, *N10000453 – Gladstone Ports Corporation Ltd – Submission*, 6 April 2018, available: [ACCC Public Register](#).

²² Svitzer, *Initial submission in opposition to the notification by Gladstone Ports Corporation Limited for exclusive dealing*, 20 April 2018 (**Svitzer initial submission, 20 April 2018**), available: [ACCC Public Register](#).

²³ Synergies Economic Consulting, *Economic assessment of exclusive licensing of towage services at Port of Gladstone*, June 2018, attached to Svitzer's supplementary submission, (Synergies Report June 2018) p. 3, available: [ACCC Public Register](#).

collective needs, and to renegotiate these agreements as needs change over time.

44. The Australian Institute of Marine and Power Engineers (**AIMPE**) opposes the Notified Conduct and is concerned that another exclusive licence will continue to have a negative impact on its members. The AIMPE is the union representing the industrial and professional interests of marine and power engineers.²⁴

Additional submission

45. Inchcape Shipping Services submits that exclusive licences need to have strict parameters for service, market competitive pricing and safe operation and this needs to be quantified and measured on an ongoing basis by the local port authority to ensure that an exclusive licence enables sustainable operation with control on pricing.²⁵

ACCC's assessment

46. The ACCC has considered the Notified Conduct in accordance with section 93 of the Act.

47. In doing so, the ACCC has taken into account:

- the notification and supporting submissions received from GPC
- submissions received from interested parties
- information independently obtained by the ACCC during the course of its review of this notification and information available to the ACCC from prior similar matters
- the relevant area of competition, as discussed below
- the likely future with and without the Notified Conduct as discussed below
- the proposed duration of the Notified Conduct, being a period not greater than eight years, noting that GPC proposes to grant an exclusive licence for five years with an option to extend the licence for a further three years.²⁶

Relevant area of competition

48. Defining the relevant area of competition affected by the arrangements which have been notified assists in assessing public benefits and detriments including any lessening of competition flowing from the arrangement. However, depending on the circumstances, the ACCC may not need to comprehensively define the relevant market as it may be apparent that a net public benefit and a substantial lessening of competition will or will not arise regardless of this definition.
49. The ACCC considers that the relevant area of competition is narrowly defined, being the provision of harbour towage services at the Port. The nearest ports to

²⁴ The Australian Institute of Marine and Power Engineers (AIMPE), *Submission on the Notification*, 13 April 2018, (**AIMPE submission, 13 April 2018**) available: [ACCC Public Register](#).

²⁵ Inchcape Shipping Services, *Exclusive License – Towage – Port of Gladstone submission*, 31 May 2018, available: [ACCC Public Register](#).

²⁶ GPC proposes to grant a five-year exclusive licence with an option to extend the licence for a further three years.

the Port are Port Alma, near Rockhampton (179 nautical miles to the north) and the Port of Bundaberg (168 nautical miles to the south). The distance between these ports and the Port means that it is appropriate to exclude them from the relevant area of competition.

Future with and without the Notified Conduct

50. The ACCC compares both the effect on competition and the public benefits and detriments likely to arise in the future with the Notified Conduct against the likely future without the Notified Conduct.

Productivity Commission Analysis

51. In 2002, the Productivity Commission found that most, if not all, Australian ports can efficiently support only one towage service provider in the longer term. The provision of towage services in individual ports might therefore be said to exhibit natural monopoly characteristics. The Productivity Commission suggested that the strongest evidence of the natural monopoly characteristics of harbour towage is that even in the large ports where entry is open, only one operator seems to have been able to survive.²⁷
52. The Productivity Commission also found that economies of scale for a (minimum) tug fleet (and one operator) could be exhausted at around 8000 tug jobs per year. However the Productivity Commission found this need not imply that two operators would be efficient at this scale of operation. Returns to scale may not decrease until much higher volumes are reached. The Productivity Commission noted that the Port of Singapore, with around 84 000 tug jobs per year issued six licences, equivalent to 14 000 per licence.²⁸
53. The Productivity Commission considered that in the future, a few Australian ports (Melbourne, Sydney and possibly Brisbane) may be able to accommodate more than one provider.²⁹
54. The Productivity Commission considered that there is little scope for sustainable long-term competition for towage services within most, if not all Australian ports (that is, competition in the market). The Productivity Commission also considered that competitive tendering for the right to provide towage services in a port offers an alternative and potentially more effective mechanism for promoting competition for the towage market in a port, resulting in more efficient pricing and service outcomes.³⁰

Gladstone Ports Corporation

55. GPC submits that the likely counterfactual is one where the Port operates with one towage service provider under a non-exclusive licence.
56. The number of tug jobs at the Port has increased over the term of the current exclusive licence. The PwC report indicates that in 2017 there were 8670 tug jobs in the Port and PwC forecasts that approximately 8928 tug jobs will be

²⁷ Productivity Commission Report, p. 74, available: [Productivity Commission Report](#).

²⁸ Productivity Commission Report, p. XXVI – XXVII, available: [Productivity Commission Report](#).

²⁹ Ibid, p. XXVII, available: [Productivity Commission Report](#).

³⁰ Ibid, p. XLV – XLVI, available: [Productivity Commission Report](#).

required for FY2018, mostly driven by an increase in LNG exports from the Port.³¹

57. GPC forecasts tug jobs in 2019 to be 9099, increasing to 9582 in 2027.³²
58. Nevertheless, GPC submits that the Port has not developed sufficiently to be able to support a second towage operator. PwC's analysis and modelling suggests that a single provider remains the most cost-effective option for towage services in the Port and if there were more than one provider it would be hard for any one towage provider to achieve an efficient level of fleet utilisation.³³

Interested party views

59. Smit Lamnalco submits that most Australian ports have been unable to efficiently support a second towage operator or have only done so temporarily. The likely level of future towage demand in the Port is insufficient to support a second towage operator on an efficient basis.³⁴
60. Smit Lamnalco also submits that the Port could not maintain the current number of 10 tugs with two operators without it leading to slowing shipping movements and reducing the efficiency of the Port.³⁵
61. Svitzer submits that PwC's modelling fails to consider a counterfactual that involves Port customers' work being contestable between multiple towage operators without exclusive licences.³⁶ Svitzer submits that the appropriate counterfactual is more competitive compared with an eight year exclusive licence.³⁷
62. The Synergies Consulting Report, prepared on behalf of Svitzer, states that in the absence of exclusive licensing, the Port would most likely have a non-exclusive licensing regime in place.

ACCC view

63. The ACCC considers that particular features of the harbour towage industry and the Port mean that supply of harbour towage services at the Port is likely to exhibit natural monopoly characteristics. A high proportion of the costs of harbour towage are fixed costs (particularly the upfront capital cost of the tug fleet) – that is they do not vary with the level of utilisation of the services. As the number of tug jobs increases, the average costs of providing towage services decreases.
64. The ACCC notes that the work of the Productivity Commission indicates that in some cases economies of scale in towage services may be exhausted at around

³¹ GPC submission, 13 March 2018, p. 12, available: [ACCC Public Register](#).

³² GPC submission, 13 March 2018, p. 13, available: [ACCC Public Register](#).

³³ GPC submission, 13 March 2018, pp. 14-15, available: [ACCC Public Register](#).

³⁴ Smit Lamnalco, *Submission regarding exclusive dealing notification N10000453 lodged by Gladstone Ports Corporation Ltd*, 6 April 2018, (**Smit Lamnalco submission, 6 April 2018**) available: [ACCC Public Register](#).

³⁵ Smit Lamnalco submission, 6 April 2018, p. 6, available: [ACCC Public Register](#).

³⁶ Svitzer Australia Pty Ltd, *Supplementary submission in opposition to Gladstone Ports Corporation exclusive dealing notification*, 11 June 2018, (**Svitzer supplementary submission, 11 June 2018**) p. 12, available: [ACCC Public Register](#).

³⁷ Svitzer supplementary submission, 11 June 2018, p. 1, available: [ACCC Public Register](#).

8000 towage jobs per year and that this need not imply that two operators would be efficient at and above this scale of operation. Returns to scale may not decrease until much higher volumes are reached. The ACCC acknowledges that the Productivity Commission Report was released in 2002 but considers that the economic principles underpinning the Productivity Commission's analysis remain relevant.

65. In 2009, when assessing notification N93770, the ACCC concluded that the most appropriate counterfactual was where the port operates with a single harbour towage operator via a non-exclusive licence.³⁸ The ACCC formed a similar view during its 2012 review of N93770.
66. The ACCC notes the forecast increased demand for tug jobs over the eight-year period for the Notified Conduct and the views of GPC, Smit Lamnalco and Svitzer in relation to the appropriate counterfactual. The ACCC considers that in a future without the notified conduct, it is most likely that harbour towage services in the Port would be provided under non-exclusive licensing arrangements.
67. In the short term, and in the absence of an exclusive licence, it is likely that Smit Lamnalco would continue to provide harbour towage services to all Port users. Port users would be free to negotiate with alternative harbour towage providers (that had been issued a non-exclusive licence by GPC) and in these circumstances, it is possible that more than one provider could operate in the port. However, over the longer term it is likely that harbour towage services would be provided by one entity, which would face some risk that a competitor would enter if its price/service were well outside reasonable levels.

Assessment of public benefits and detriments

68. The ACCC conducts an assessment of both any likely substantial lessening of competition and the benefits and detriments of the Notified Conduct. An examination of the likely benefits and likely detriments informs the discussion and conclusion regarding any likely substantial lessening of competition.

Public Benefits

Increasing competition for the market and competitive pressure

GPC submissions

69. GPC submits that a competitive tender for an exclusive licence, compared to other arrangements including a non-exclusive licence has the potential to increase competition for the provision of towage services.
70. An exclusive licence provides certainty for the successful tenderer insofar as it knows that it will supply towage services to all the Port users for the length of the licence period. Certainty is particularly important where it is unclear whether the particular market can sustain two operators, because the risk of entering and remaining in the market is much higher in these circumstances.
71. GPC contrasts this with the counterfactual where potential applicants for a non-exclusive licence need to factor into their business cases the risk that they will

³⁸ Australian Competition and Consumer Commission, *Decision in respect of a notification lodged by Gladstone Ports Corporation Limited regarding towage services at the Port of Gladstone*, 1 May 2009, available: [N93770](#).

only be able to supply services to a subset of the Port users, rather than all users. This uncertainty, combined with lumpy investments (due to a minimum number of tugs required to offer appropriate services to users) and economies of scale mean that more towage operators are likely to tender for an exclusive licence where they may not be prepared to compete in the market or tender for a non-exclusive licence.³⁹

72. GPC submits that the outcomes of previous competitive tender processes support its position. GPC's last competitive tender process resulted in Smit Marine being awarded the exclusive licence instead of the incumbent at the time, Svitzer. This provided Smit Marine with the opportunity to enter the Australian market.⁴⁰
73. GPC submits that a competitive tender process for an exclusive licence is likely to subject prospective towage service providers to a higher degree of competitive pressure than a tender for a non-exclusive licence because:⁴¹
- The higher certainty provided by an exclusive licence means that more towage operators are likely to submit responses to the request for tender. Therefore a tender process for an exclusive licence encourages new entry and increases the number of competitors in the tender process.
 - In a process for a non-exclusive licence, tenderers will consider the risk that they will not be able to achieve the number of towage jobs required to recoup their investment in tug boats, as a result they are likely to include a risk premium in their pricing. However, this risk is lower in a tender for an exclusive licence because an exclusive licence guarantees that the successful tender will supply harbour towage services to all users of the Port. Therefore, a tenderer for an exclusive licence will allow tenderers to factor a lower risk premium into their pricing proposals than a tender for a non-exclusive licence. This means that a competitive tender for an exclusive licence should lead to lower costs for Port users and increased efficiencies when compared to a tender for a non-exclusive licence.
 - The increased certainty provided by an exclusive licence provides a greater incentive for tenderers to agree to invest in tug boats, as they would have greater certainty of recouping the costs of their investment.
74. An exclusive licence also offers the opportunity to focus competitive rivalry in a way which meets port users operational requirements with the most competitive service charges.⁴²

Interested party submissions

75. Svitzer submits that an exclusive licence is unlikely to result in public benefits. Many of the benefits cited in favour of the exclusive licence (such as the determination of safety, service and operational standards) can be obtained under other, procompetitive, models of service provision. It is clear that the vast

³⁹ GPC submission, 13 March 2018, pp. 17 – 20, available: [ACCC Public Register](#).

⁴⁰ GPC submission, 13 March 2018, p. 20, available: [ACCC Public Register](#).

⁴¹ GPC submission, 13 March 2018, p. 21, available: [ACCC Public Register](#).

⁴² GPC Attachment B, 18 May, p. 10, available: [ACCC Public Register](#).

majority of ports do not grant exclusive licences and yet they achieve high safety, service and operational standards.⁴³

76. Svitzer submits that an exclusive licence is unlikely to increase competition for the market and increase competitive pressure. The process of transformation between competition for the market and competition in the market and continued threat of re-entry provides significant competitive tension and public benefit.⁴⁴
77. Svitzer submits that any certainty created by an exclusive licence is offset by uncertainty at the end of the exclusive licence period. Svitzer notes that the incumbent, aware that it may not win the future exclusive licence, may seek to recover the costs of significant investments made several years into an exclusive licence period. Svitzer submits this was the case when Smit Lamnalco increased prices charged to LNG customers following the purchase of five LNG tugs.⁴⁵
78. An exclusive licence is likely to reduce the opportunity and incentive to reduce costs both through innovation and other cost reducing mechanisms such as industrial relations reforms.⁴⁶
79. Svitzer considers that it is exceptionally difficult to forecast what the structure and level of demand will be in the period to 2027. Markets may be extremely volatile for the next nine years and potentially unforeseen technological changes will affect both tugs and vessels.⁴⁷
80. Synergies Consulting submits that an exclusive licensing arrangement does not adapt as efficiently as a market environment to variability in demand. Accordingly, the benefits claimed by GPC assume that demand can be reliably predicted for the duration of the franchise period. However, experience over the period of the current licence clearly shows that it is extremely difficult to predict demand for towage services, especially in a location like the Port, which is heavily reliant on resource exports.⁴⁸ Synergies Consulting submits that the forecast demand for tug jobs for the current exclusive licence period significantly overstated the level of tug jobs and it is possible that the current forecasts for the next period understates demand.⁴⁹
81. Smit Lamnalco submits that an exclusive licence is likely to be the best means to ensure a competitive outcome for the rates and terms offered for towage services at the Port because of the substantial economies of the scale and scope in providing harbour towage services.⁵⁰
82. Smit Lamnalco also submits that in the absence of the security offered via an exclusive licence, Smit Marine would not have bid for the Port licence in 2009 in the same manner as it did. The security of the exclusive licence allowed Smit Marine to focus on competition in the delivery of a high quality, efficient service against the lowest possible cost, rather than focus on mitigating the risk of insufficient cost recovery. Smit Lamnalco submits that without that security, Smit

⁴³ Svitzer initial submission, 20 April 2018, p. 1 and p. 6, available: [ACCC Public Register](#).

⁴⁴ Svitzer initial submission, 20 April 2018, p. 1, available: [ACCC Public Register](#).

⁴⁵ Svitzer initial submission, 20 April 2018, p. 13, available: [ACCC Public Register](#).

⁴⁶ Svitzer initial submission, 20 April 2018, p. 2, available: [ACCC Public Register](#).

⁴⁷ Svitzer initial submission, 20 April 2018, p. 11, available: [ACCC Public Register](#).

⁴⁸ Synergies Report June 2018, p. 7, available: [ACCC Public Register](#).

⁴⁹ Synergies Report June 2018, p. 23, available: [ACCC Public Register](#).

⁵⁰ Smit Lamnalco submission, 6 April 2018, p. 12, available: [ACCC Public Register](#).

Marine would likely have considered including a premium in the towage rates quoted in the bid for the current licence to account for the higher risk of not fully recovering its establishment and operating costs. At the time, Smit Marine believed it was likely that the other (new entrant) bidders for the Port tender would have done the same or not have bid for the licence, if it was not exclusive.⁵¹

83. Smit Lamnalco submits that the current exclusive licence has resulted in increased competitive pressure on it in relation to towage rates and service levels.⁵²
84. Smit Lamnalco submits that competition for an exclusive licence is likely to be more fierce than for a non-exclusive licence. In 2001, when the Port authorities for the Ports of Fremantle and Kwinana offered towage service providers the opportunity to bid for either an exclusive or a non-exclusive licence, all but one provider chose to bid for an exclusive licence. When the port authorities later decided to limit the tender to a non-exclusive licence, these bidders chose to withdraw from the tender rather than tender for a non-exclusive licence.⁵³

ACCC view

85. Compared to the counterfactual, the ACCC considers that the Notified Conduct is likely to result in increased competition for the provision of towage services.
86. The notified conduct is likely to increase competition for the provision of harbour towage services at the Port by providing an incentive for competitors of the incumbent to tender for the market where they may not be prepared to compete in the market (under the counterfactual). The ACCC accepts that the Notified Conduct is likely to create greater certainty for bidders. Towage service providers will have the opportunity to develop tenders in the knowledge that if they are successful, they will be entitled to provide all towage services for the licence period. This is likely to result in more providers tendering for the licence compared to the counterfactual.
87. Competitive tendering for one Australian port can also lead to greater competition for towage services across Australia. The ACCC notes that, as a result of being awarded the current exclusive licence, Smit Marine entered the Australian market. A competitive process for a new exclusive licence creates an opportunity for other towage service providers to enter the Australian market or for existing providers to expand their existing Australian operations.
88. Applicants for a non-exclusive licence will factor into their bids that they may not be able to supply services to all harbour users. This combined with the fact that a minimum number of tugs are needed to offer appropriate service levels and capture economies of scale, mean that more towage operators are likely to tender for an exclusive licence than tender for a non-exclusive licence or compete in an open market for towage services.
89. As a result, the ACCC considers that GPC's competitive tender process is likely to result in benefit by subjecting prospective towage providers to a higher degree of competitive pressure compared to the counterfactual. Greater

⁵¹ Smit Lamnalco submission, 6 April 2018, p. 8, available: [ACCC Public Register](#).

⁵² Smit Lamnalco submission, 6 April 2018, p. 1, available: [ACCC Public Register](#).

⁵³ Smit Lamnalco submission, 6 April 2018, pp. 8-9, available: [ACCC Public Register](#).

competition for the market creates an opportunity for better price/service levels for users.

90. The ACCC acknowledges Svitzer's submissions that an exclusive licence removes the opportunity for ongoing competition in the market. However the guarantee of demand provided by an exclusive licence in ports that are unable to efficiently sustain more than one operator is likely to lead to the effects of economies of scale being incorporated into prices offered by tenderers. Given the greater certainty from winning an exclusive licence, the ACCC considers that competition for the market is likely to be stronger for an exclusive licence, and therefore deliver greater benefits to port users compared to a non-exclusive licence.
91. The ACCC notes Svitzer's concerns that the incumbent may seek to recover the costs of significant investments made several years into an exclusive licence period, before the period ends. The PWC report notes that the only costs which are being amortised over an accelerated period are the costs of mobilising the five new LNG tugs into the Gladstone market and the costs of acquiring the new tugs is being amortised over the life of the vessels, based on industry standards.⁵⁴ The ACCC accepts that recovery of the costs associated with mobilising the new LNG tugs may have created a temporary increase in prices in the short term.
92. The ACCC accepts that an exclusive licence can result in delays to the adoption of efficiency-enhancing technologies or other innovations (not foreseen at the time of the tender). Reductions in the efficient cost due to innovation during the contract period may not be incorporated during the contract period. These might be incorporated during a subsequent tender period or at the end of the initial five year licence period. The rate of innovation in towage services might not be high enough for this to be a major concern over that time period.
93. Accordingly, the ACCC considers that the Notified Conduct is likely to result in sufficient competition and competitive pressure to result in public benefit.

Benefits from efficient prices and appropriate service levels

GPC submissions

94. GPC submits that competitive tendering for an exclusive licence can lead to price reductions without compromising service levels when compared to competitive tendering for a non-exclusive licence. This is due to the increased competitive pressure involved, the higher number of participants likely to be interested in competing for an exclusive licence and the decrease in the risk premium associated with an exclusive licence compared to a non-exclusive licence.⁵⁵
95. GPC submits that this view is supported by the analysis in the PwC report, which indicates that GPC's previous competitive tender for an exclusive licence resulted in towage charges falling by approximately three per cent with the commencement of the exclusive licence with Smit Marine.⁵⁶

⁵⁴ See PwC Report p. 6, available: [ACCC Public Register](#).

⁵⁵ GPC submission, 13 March 2018, p. 21, available: [ACCC Public Register](#).

⁵⁶ GPC submission, 13 March 2018, pp. 22-23, available: [ACCC Public Register](#).

96. GPC submits that the specific licence agreement between GPC and the new licence-holder will provide for prices to be set annually based on costs. Consequently, the provider of harbour towage services will be required to pass through any cost reductions.⁵⁷

Interested party submissions

97. Svitzer submits that the public benefits of the Notified Conduct are highly contingent on GPC setting competitive prices and service levels.⁵⁸
98. Svitzer submits that the exclusive licence would build rigidity into the system in the long term, which prevents the fluid negotiation of prices based on any changes arising from different operating environments and technological change.⁵⁹
99. Svitzer submits that prices are set during the tender process and the holder of an exclusive licence is not subject to any competitive pressure. Therefore it has few incentives to offer further or larger discounts to customers.⁶⁰
100. Svitzer submits that customers' countervailing power adds an important dynamic to competitive dynamics in the market for towage services. In the case of the Port, LNG producers such as Santos are likely to be able to exert countervailing power to obtain better price and non-price terms from towage providers or to bypass towage providers completely through self-supply. However, the notified conduct means that these customers will no longer have these options as they will be locked into a single provider, with prices and terms dictated by GPC, for eight years.⁶¹
101. Svitzer responds to GPC's claim that towage charges fell by three per cent at the commencement of the current exclusive licence, submitting that shortly after the grant of the current exclusive licence, Smit was able to raise prices when forecast demand was not met for harbour towage users. Further, it was able to charge uncompetitive prices to LNG users when asked to purchase further LNG tugs. Svitzer considers that this resulted in LNG users effectively cross-subsidising other port users at the Port.⁶²
102. PwC responds to Svitzer's views described in the preceding paragraph, submitting that GPC's objective is to provide a transparent, predictable and auditable framework for the adjustment of towage charges over the next exclusive licence period, which dynamically adjusts for any variation in demand from that originally forecast and where that demand risk is shared between Port users and the towage licensee.⁶³
103. Smit Lamnalco confirms the accuracy of PwC's explanation of the pricing frameworks under the current exclusive licence and that these pricing frameworks have been effective in ensuring that there is strong incentive for Smit to control its costs to ensure efficiency under the pricing mechanisms.

⁵⁷ GPC submission, 13 March 2018, p. 25, available: [ACCC Public Register](#).

⁵⁸ Svitzer supplementary submission, 11 June 2018, p. 2, available: [ACCC Public Register](#).

⁵⁹ Svitzer initial submission, 20 April 2018, p. 14, available: [ACCC Public Register](#).

⁶⁰ Svitzer initial submission, 20 April 2018, p. 7, available: [ACCC Public Register](#).

⁶¹ Svitzer supplementary submission, 11 June 2018, p. 7, available: [ACCC Public Register](#).

⁶² Svitzer initial submission, 20 April 2018, pp. 13-14, available: [ACCC Public Register](#).

⁶³ PwC Report, pp. 4-5, available: [ACCC Public Register](#).

ACCC view

104. As outlined previously, the ACCC agrees that granting an exclusive licence following a competitive tender process for towage services in the Port is likely to provide the successful towage service provider with greater certainty regarding the volume of work. This is likely to result in vigorous competition for the market resulting in efficiencies, which are likely to result in competitive prices and service levels for Port users. The ACCC notes Smit Lamnalco's submission that if it were bidding for a non-exclusive licence, it would have added a risk premium to its prices.
105. However, investment in a harbour towage operation involves significant upfront capital costs. A provider of harbour towage will generally require multiple tugs to be able to meet the needs of shipping customers. The high cost of delays from waiting for tug jobs (relative to the costs of idle capacity for tugs) mean that most shipping customers are likely to be willing to pay prices which include a provision for the idle capacity of an operator's tugs, rather than accept long delays in receiving towage services which may delay ships' port arrival and departure. In short, while prices are likely to be important to users, service levels may be more important.
106. The ACCC considers that the Notified Conduct is likely to result in benefits via competitive prices and service levels.

Avoidance of costs

GPC submissions

107. Having more than one towage service provider at the Port would result in increased costs and reduced efficiencies:⁶⁴
- increased administration and double handling costs for GPC and the Harbour Master, the latter of which would have to co-ordinate with multiple tug boat operators and these costs are likely to be material
 - the costs of constructing and maintaining duplicate berthing facilities, including the costs of an additional lease and its administration
 - the resource costs associated with any price war
 - increased costs and inefficiencies for Port users.
108. GPC submits that if more than one towage operator services the Port, more tugs will be required to service the same level of demand. This is likely to result in spare capacity resulting in additional costs for the towage service providers because fixed costs are incurred even if tugs are not fully utilised and it would result in duplication of fixed operating costs such as berth leasing and administration costs and crew wages.⁶⁵
109. GPC submits that these additional costs will be avoided under an exclusive licence.

⁶⁴ GPC submission, 13 March 2018, p. 23, available: [ACCC Public Register](#).

⁶⁵ GPC submission, 13 March 2018, p. 24, available: [ACCC Public Register](#).

Interested party submissions

110. Svitzer submits that the cost of constructing a second berthing facility would be met by a second entrant to the port.⁶⁶
111. Smit submits that allowing another exclusive licence provides benefits due to avoiding the costs associated with establishment of additional towage providers, such as the duplication of operating systems and the on boarding of additional crew.⁶⁷

ACCC view

112. In the long term, the most appropriate counterfactual is one where one towage service operator provides services at the Port via a non-exclusive licence. However, in the short term it is possible that more than one operator may provide these services. This short-term outcome is likely to result in increased costs for stakeholders of the kind submitted by GPC, including the costs associated with establishing an additional berth for a new entrant.
113. The ACCC notes the Productivity Commission's view that during the period when two operators are competing to win the market, the war of attrition involves real resource costs to the community. More capital equipment in the form of tugs and landside facilities and labour are used in the provision of towage services in that port than are efficient.⁶⁸ Vigorous competition typically leads to greater efficiency and benefits to the community. However, appropriate levels of competition can be achieved in different ways. In this case, the costs identified above can largely be avoided by conducting a competitive tender for an exclusive licence.
114. Accordingly, the ACCC considers that the Notified Conduct is likely to result in benefit by avoiding costs.

Public Detriment

The Notified Conduct precludes competition *in* the market

Interested party submissions

Svitzer's submissions

115. Svitzer submits that an exclusive licence will result in a substantial lessening of competition for a substantial period of time by precluding competition for the provision of towage services in the Port for the duration of the exclusive licence period, during which demand for tug jobs is expected to increase.⁶⁹
116. Svitzer submits that the Notified Conduct will prevent smaller competitors from entering the market to compete for a limited number or type of jobs or to enter into alliances and joint ventures with other towage service providers. Smaller towage service providers will not have the scale to compete for all towage jobs in the port. Svitzer claims the anticompetitive effects are significant, compared to

⁶⁶ Svitzer initial submission, 20 April 2018, p. 9, available: [ACCC Public Register](#).

⁶⁷ Smit Lamnalco submission, 6 April 2018, available: [ACCC Public Register](#).

⁶⁸ Productivity Commission Report, p. 151, available: [Productivity Commission Report](#).

⁶⁹ Svitzer initial submission, 20 April 2018, p. 9, available: [ACCC Public Register](#).

the scenario where there is no exclusivity, noting there has been no sufficient justification offered by GPC for departing from an open market.⁷⁰

117. Svitzer submits that the pressure and benefits arising from the threat of competitive entry are eliminated by an exclusive licence. The ability of market forces to continually test and shape the appropriate market structure in the face of evolving market conditions is removed.⁷¹
118. Svitzer submits that contrasting competition *in* the market, with competition *for* the market is a false dichotomy. The process of transformation of competition between these two states and continued threat of re-entry provides significant competitive tension and public benefit. The ability to enter into joint ventures, seek customer sponsorship and cross-hire provides a new entrant the capacity to gain a foothold in the market, without depriving customers of the benefit of competition.⁷²
119. Entry and exit costs are not sunk costs and while they are not insignificant, they are not prohibitive for the major operators. Sunk costs are likely to represent one to two per cent of revenue over five years under some entry strategies.⁷³
120. Svitzer submits that prices are set during the tender process and the holder of an exclusive licence is not subject to any competitive pressure. Therefore, it has few incentives to offer further or larger discounts to customers.⁷⁴
121. Svitzer submits that it has repeatedly been forced to reduce its costs, innovate and improve its service and prices as a result of the competitive pressure caused by the actual and/or potential entry of competitors at ports in which it operates. Svitzer notes that its customers have significant purchasing power and Svitzer is well aware that if its prices are not competitive, those customers have the ability and the incentive to sponsor entry of a competitor.⁷⁵

Smit Lamnalco's submissions

122. Smit Lamnalco submits that the "open competition" and "non-exclusive" two-operator model for towage services has largely proven unsuccessful in most Australian ports. Smit Lamnalco has observed that most Australian ports have not been able to efficiently support a second towage operator, or have only done so temporarily.⁷⁶ Smit Lamnalco had been one of the two physical operators in the ports of Botany, Brisbane, Melbourne and Newcastle. However, this proved to be unsustainable. In September 2015, Smit Lamnalco ceased operating tugs in its own right in the ports of Botany, Melbourne and Newcastle, and in February 2018, Brisbane.⁷⁷
123. Smit Lamnalco submits that it agreed to subcontract towage jobs to Svitzer in the Ports of Botany, Brisbane, Melbourne, and Newcastle as a means to maintain a presence in those ports and continue servicing its network customers. The decision was taken because demand in these ports did not

⁷⁰ Svitzer initial submission, 20 April 2018, p. 9, available: [ACCC Public Register](#).

⁷¹ Svitzer initial submission, 20 April 2018, p. 10, available: [ACCC Public Register](#).

⁷² Svitzer initial submission, 20 April 2018, p. 1, available: [ACCC Public Register](#).

⁷³ Svitzer supplementary submission, 11 June 2018, p. 5, available: [ACCC Public Register](#).

⁷⁴ Svitzer initial submission, 20 April 2018, p. 7, available: [ACCC Public Register](#).

⁷⁵ Svitzer initial submission, 20 April 2018, p. 4, available: [ACCC Public Register](#).

⁷⁶ Smit Lamnalco submission, 6 April 2018, p. 2, available: [ACCC Public Register](#).

⁷⁷ Smit Lamnalco submission, 6 April 2018, p. 6, available: [ACCC Public Register](#).

support two operators on a sustainable basis. Svitzer's use of multi-port rebates for major customers made it extremely difficult for a new towage operator to successfully compete on rates at any single port. As result, after acquiring PB Towage, Smit Lamnalco ceased all physical operations in those ports and leased its tugs to Svitzer. While the sub-contracting arrangement has proven beneficial to support the continuing participation of two established operators in these four harbour ports, Smit Lamnalco is not aware of any towage operator who would be likely to enter a port similar to the Port, based on securing a sub-contract arrangement with a competing towage operator at the port.⁷⁸

124. Based on its experience with sub-contracting arrangements, Smit Lamnalco considers it highly unlikely that the prospect of entering into a sub-contracting arrangement with another operator at a port would encourage a bidder for a non-exclusive licence.⁷⁹
125. Smit Lamnalco submits that it is unaware of any cross-hiring arrangements that have been agreed or are in place at any Australian ports in recent memory. It submits that Svitzer confuses cross-hiring arrangements with sub-contracting arrangements. Sub-contracting arrangements have emerged in the Ports of Brisbane, Botany, Melbourne and Newcastle because the model whereby two towage service providers competing for physical jobs was unsustainable.⁸⁰
126. Demand for towage services at the Port is based on expected shipping volumes from the various industries at the Port, including coal, LNG, resources, and general cargo. Demand for towage services increases as the number of calls made by commercial vessels increases. However, the number of vessel calls cannot be relied upon alone, as the size of the vessels entering and exiting the port impacts on the number and size of tugs needed to service those vessels.⁸¹
127. Based on the forecast provided in the PwC Report attached to the Notification, the expected demand for towage services in the Port would not be sufficient to support a second towage operator at the Port.⁸²

GPC's submissions

128. GPC submits that PwC's research indicates that competition between towage providers has not been sustainable in most Australian ports, and particularly those with comparable characteristics to the Port. In markets where a period of competition has resulted in the exit of one provider, the threat of future entry is diminished and provides only a weak discipline on the incumbent and remaining provider.⁸³
129. An exclusive licence, properly structured and implemented, is an effective way of encouraging competition for the market. This competition is likely to be more effective and more robust than competition in the market, where market analysis indicates that a single provider is the least-cost means of meeting demand for

⁷⁸ Smit Lamnalco Towage Australia Pty Ltd, *Response to Svitzer Australia Pty Ltd's supplementary submission of 11 June 2018*, 22 June 2018 (**Smit Lamnalco supplementary submission 22 June 2018**), p. 4, available: [ACCC Public Register](#).

⁷⁹ Smit Lamnalco supplementary submission 22 June 2018, p. 4, available: [ACCC Public Register](#).

⁸⁰ Smit Lamnalco supplementary submission 22 June 2018, p. 3, available: [ACCC Public Register](#).

⁸¹ Smit Lamnalco submission, 6 April 2018, p. 13, available: [ACCC Public Register](#).

⁸² Smit Lamnalco submission, 6 April 2018, p. 13, available: [ACCC Public Register](#).

⁸³ Gladstone Ports Corporation Limited, Supplementary submission, Attachment B, 18 May 2018, (**GPC supplementary submission, 18 May 2018**) pp. 2-3, available: [ACCC Public Register](#).

towage services. GPC's view is that the threat of market entry is less credible in markets where a sole provider is the most efficient means of delivering services. In such markets, both the incumbent and any new entrant know that the costs of market entry, and the risks to a new entrant, are significantly higher. The informational advantages held by the incumbent, in particular, are more pronounced as a smaller-scale entry strategy, designed to allow the new entrant to learn more about the market, is less feasible.⁸⁴

ACCC view

130. The ACCC acknowledges Svitzer's submissions that an exclusive licence removes the opportunity for competition in the market during the licence period. However, as noted above, the guarantee of demand provided by an exclusive licence in ports that are unable to efficiently sustain more than one operator is likely to lead to economies of scale being reflected in prices offered by tenderers. Given the greater certainty in winning an exclusive licence, the ACCC considers that competition for the market is likely to be stronger for an exclusive licence, and therefore deliver greater benefits to port users compared to a non-exclusive licence.
131. A substantial proportion of the capital costs of entry into harbour towage are generally recoverable upon exit (that is, they are not sunk). This is because tugs are a mobile asset and therefore can be moved to or sold into other markets. Nonetheless, there are a range of costs associated with towage operations that cannot be recouped on exit, these include crew training costs, modifications to tugs to meet Australian requirements, costs of tug demobilisations and crew redundancy payments. The risk of incurring these costs is likely to result in fewer towage providers entering a port to compete with the incumbent under a non-exclusive licence.
132. The ACCC notes Svitzer's submissions that a non-exclusive licence provides the opportunity for smaller towage operators to provide services to some Port users and therefore compete with the incumbent. Svitzer provided examples of ports where this has occurred, such as the Ports of Eden and Fremantle. The ACCC also notes Smit Lamnalco's submissions in relation to the Ports of Botany, Brisbane, Melbourne and Newcastle where Smit Lamnalco and Svitzer compete for customers and Svitzer performs all the towage operations. The ACCC understands this arrangement developed because demand at these ports did not support two operators. Based on these examples, opening a port to ongoing competition may be efficient and sustainable in some circumstances and less so in others. However, even in the examples of the Ports of Eden and Fremantle, the sustainability of multiple operators over the long term is uncertain.
133. An exclusive licence removes the opportunity for competition in the market for the duration of the licence period. However this is offset by the competitive tender process conducted before an exclusive licence is granted. Accordingly, the ACCC considers that, in these circumstances, an exclusive licence providing for vigorous competition at a point in time (via competitive tender) rather than the possibility of ongoing competition in the market for towage service is unlikely to result in significant, if any, public detriment.

⁸⁴ GPC supplementary submission, 18 May 2018, p. 10, available: [ACCC Public Register](#).

Term of licence

Interested party submissions

134. Svitzer submits that the Notified Conduct means that customers will be locked into a single provider, with prices and terms dictated by GPC, for eight years.⁸⁵ The benefits claimed by GPC assume that demand can be reliably predicted for the duration of the franchise period, in this case up to eight years.⁸⁶
135. The calculated efficiencies occur only in a static world and the current period of exclusive licensing has demonstrated that the market is not static and market conditions will continue to develop and change, undermining any assumptions made for a lengthy exclusive licence period.⁸⁷
136. Svitzer submits that the length of the exclusive licence period reduces the opportunity for cost reduction due to innovation.

GPC submissions

137. GPC submits that the potential public detriments associated with excluding competition during the term of an exclusive licence can be significantly mitigated by requiring tenderers to compete on price and quality and requiring key aspects of the tenders to be agreed upfront for the duration of the licence.⁸⁸
138. During the competitive tender process for the new exclusive licence, tenderers will be required to compete on both price and quality and key aspects of the tenders will be agreed upfront for the duration of the licence. The licensee will be bound to its tendered rate of return/gross margin and price increases if they are approved by GPC in accordance with a defined framework. This will allow competitive pressures, which operate during the tender process, to be enjoyed for the eight year duration of the licence.⁸⁹

ACCC view

139. GPC intends to grant an exclusive licence for a period of up to eight years. GPC will grant an exclusive licence for a period of five years with an option to extend the period by three years, exercisable only by GPC. This is similar to the exclusive licensing arrangement in the current exclusive licence.
140. The longer the period of an exclusive licence, the greater the risk of detriment from not immediately having cost savings, such as from innovation and better utilisation of labour and resources, passed through to customers. The shorter the period the less benefit to prospective tenderers of certainty and the less time under that certainty to recover costs of entry. An exclusive licence period of five years, with an optional three year extension, strikes a reasonable balance. The ACCC notes that the licence agreement will provide for prices to be set annually based on costs, and the exclusive licence holder will be required to pass through any cost reductions.⁹⁰

⁸⁵ Svitzer supplementary submission, 11 June 2018, available: [ACCC Public Register](#).

⁸⁶ Synergies Report June 2018, p. 86, available: [ACCC Public Register](#).

⁸⁷ Svitzer initial submission, 20 April 2018, p. 14, available: [ACCC Public Register](#).

⁸⁸ GPC submission, 13 March 2018, p. 26, available: [ACCC Public Register](#).

⁸⁹ GPC submission, 13 March 2018, p. 26, available: [ACCC Public Register](#).

⁹⁰ GPC submission, 13 March 2018, p. 25, available: [ACCC Public Register](#).

141. Accordingly, the ACCC considers that the Notified Conduct is unlikely to result in significant public detriment due to the length of the exclusive licence term.

Potential for uncompetitive service levels

Interested party submissions

142. Svitzer submits that foreclosing customers and/or competitors from supplying their own towage services is likely to result in detriment from reduced choice and service levels to customers compared to the counterfactual.⁹¹
143. Svitzer submits that it has repeatedly been forced to reduce its costs, innovate and improve its service and prices as a result of the competitive pressure caused by the actual and/or potential entry of competitors at ports in which it operates.⁹²
144. Smit Lamnalco submits:⁹³
- The current licence places stringent conditions on Smit Lamnalco for, amongst other things, service levels and GPC has formulated key performance indicators to assess performance against these conditions.
 - the offer of an exclusive licence, in any port which cannot viably support more than one operator, is likely to deliver a competitive level of tug rates without compromising the quality of service, due to competitive tension in the tender process. The high barriers to entering the market for towage services reduce the scope for the same level of competitive tension to be achieved without exclusivity.
 - To maintain the current high level of efficiency in the Port via a non-exclusive licence, all towage operators would be required to hold sufficient tugs and crews to cater for demand from vessels. As the towage demand conditions are unlikely to change materially prior to 2028, this will likely result in inefficient overcapacity at the Port.

GPC submissions

145. Tenderers will be required to compete on quality as well as on price. Further, the tender specifications for the new exclusive licence (including the tug specifications) will reflect the statutory obligations on GPC to maintain a safe and secure operating environment in the Port and deliver against service levels (i.e. key performance indicators). Consequently, the notified conduct will not result in any detriment in the form of uncompetitive service levels.⁹⁴

ACCC view

146. The ACCC did not receive any submissions from Port users raising concerns about service levels during the current exclusive licence period.

⁹¹ Svitzer initial submission, 20 April 2018, p. 1, available: [ACCC Public Register](#).

⁹² Svitzer initial submission, 20 April 2018, p. 4, available: [ACCC Public Register](#).

⁹³ Smit Lamnalco submission, 6 April 2018, available: [ACCC Public Register](#).

⁹⁴ GPC submission, 13 March 2018, p. 26, available: [ACCC Public Register](#).

147. In its confidential attachment to the Notification, GPC provided the ACCC with letters between GPC and the LNG terminal users, setting out GPC's proposal for future towage licence arrangements at the Port.⁹⁵
148. Based on the information provided to the ACCC, GPC is aware of the need to maintain high service levels and this will be one of the areas of focus during the competitive tender process.
149. Accordingly, the ACCC considers that the Notified Conduct is unlikely to result in significant, if any, public detriment due to uncompetitive service levels at the Port.

Impact on employment and safety standards

Interested party submissions

150. The AMOU submits that during the current exclusive licence period there has been a reduction of employment conditions, permanency of employment and safety standards at the Port.⁹⁶
151. The AMOU submits that the tender needs to meet certain requirements regarding the employment and remuneration of tug masters, flexibility to increase the number of tugs operating in the Port and the successful tenderer has a proven track record of establishing, maintaining and encouraging the highest possible safety and operational standards.⁹⁷
152. The AIMPE is concerned that an exclusive licence reduces the opportunity for crews to negotiate higher wages (and better working conditions), limits expansion of towage assets and crews and can result in structures that expose crews to the risk of liability for accidents and environmental damage.⁹⁸
153. The AIMPE submits that an exclusive licence will have a detrimental effect on employment and crews and the subsequent contractual relationship created by the exclusive licence because it:
- Restricts and impedes rights and freedoms to bargain with the incumbent employer under the *Fair Work Act 2009* and international conventions on collective bargaining and rights of workers.
 - Encourages corporate schemes of employment avoidance to win tenders.
 - Stonewalls any increases to towage assets and crews to address growth and safety in a port.
 - Negates free collective bargaining arrangements and rights to maintain legacy conditions achieved fairly because the incumbent is continually threatened to reduce or restrict employment entitlements or else the contract will be lost to a lower employment cost operator.
154. The AIMPE submits that port corporations and authorities should either issue conditional non-exclusive licences or allow open port arrangements that are

⁹⁵ GPC referred to these letters in its public notification, see p. 4 of GPC's notification, available: [ACCC Public Register](#).

⁹⁶ AMOU submission, 6 April 2018, p. 2, available: [ACCC Public Register](#).

⁹⁷ AMOU submission, 6 April 2018, available: [ACCC Public Register](#).

⁹⁸ AIMPE submission, 13 April 2018, available: [ACCC Public Register](#).

subject to demonstrated compliance with stringent safety and operational standards/parameters to ensure the safety of vessels, crews, cargo, port and the marine environment.⁹⁹

GPC submissions

155. GPC submits that it will specify the crewing requirements, including minimum personnel to crew each tug under the new exclusive licence, which will require approval from the Queensland Government.¹⁰⁰
156. The crewing requirements will require the new exclusive licence holder to comply with various Commonwealth and State Acts and Gladstone Port Rules.¹⁰¹
157. Given that the Queensland Government would not approve any specifications that compromise its policy of promoting employment in regional Queensland or which would lead to non-compliance with any applicable laws (e.g. employment laws), the Notified Conduct will not result in any adverse effects on employment in regional Queensland.¹⁰²
158. GPC responded to the submissions from the AMOU and AIMPE stating:¹⁰³
 - GPC does not agree that the current exclusive licence has reduced safety standards. The towage industry is subject to regulatory audits and strict inspection regimes to ensure the highest of safety standards. These requirements are reflected in the current licence and will be reflected in the new licence.
 - The exclusive licence with Smit Marine does not restrict or limit wages or employment conditions and Smit Marine's licence allows for the incremental cost of labour.

ACCC view

159. The ACCC notes the submissions of the AMOU and AIMPE regarding concerns about potential detrimental impact on employment for tug crews and Port safety.
160. The ACCC also notes GPC's responses to those concerns, that the existing licence does not limit or restrict employment and working conditions. Further GPC will specify the crewing requirements and the Queensland Government will not approve specifications that compromise its policy of promoting employment in regional Queensland.
161. GPC's notification and supporting submissions refer to mandatory safety requirements, highlighting that Port safety is one of the key aspects it will consider during the tender process.
162. Any impact on employment and safety standards seems to be an issue that would arise both with and without the Notified Conduct.

⁹⁹ AIMPE submission, 13 April 2018, available: [ACCC Public Register](#).

¹⁰⁰ GPC submission, 13 March 2018, p. 27, available: [ACCC Public Register](#).

¹⁰¹ GPC submission, 13 March 2018, p. 27, available: [ACCC Public Register](#).

¹⁰² GPC submission, 13 March 2018, p. 27, available: [ACCC Public Register](#).

¹⁰³ Gladstone Ports Corporation Limited, Supplementary submission, Attachment A, 18 May 2018, p. 4, available: [ACCC Public Register](#).

163. Accordingly, the ACCC considers that potential employment and safety issues are unlikely to lead to significant, if any public detriment as a result of the Notified Conduct.

Balance of public benefit and public detriment

164. The ACCC accepts that the Notified Conduct is likely to result in some public benefits, compared to the counterfactual, including:
- Increasing competition for the market and increasing competitive pressure.
 - More efficient prices and appropriate service levels.
 - Avoiding costs.
165. The ACCC considers the Notified Conduct is unlikely to result in significant public detriment.
166. Accordingly, the ACCC is satisfied that the likely benefits of the Notified Conduct outweigh the likely detriment.

Assessment of the impact on competition

167. Before revoking an exclusive dealing notification, the ACCC must be satisfied that the notified conduct has the purpose, effect or likely effect of substantially lessening competition.
168. There is no definition in the Act of '*substantially lessening competition*'. The ACCC generally takes it to mean where the competitive process has been compromised or impacted in a meaningful way, usually by deterring, hindering or preventing competition.
169. The precise threshold between a lessening of competition and a substantial lessening of competition is a matter of judgement and will depend on the facts.
170. The ACCC notes Svitzer's opposition to an exclusive licence and its claims that a non-exclusive licence will be more competitive than an exclusive licence.
171. In assessing the Notified Conduct and the counterfactual, the ACCC is comparing two different approaches that seek to promote competition in the provision of towage services. One model may be more competitive than the other depending on the circumstances. While one competitive model seems to serve some ports well, it may not necessarily be suitable for all ports.
172. Taking into account the discussion of, and the conclusion on, the public benefits and detriments above, the ACCC considers that the Notified Conduct is unlikely to substantially lessen competition for the following reasons:
- An exclusive licence will be awarded following an extensive competitive tendering process.
 - Bidders will be able to assess the scale and scope of the work and lodge their most competitive bid for the work.
 - The tendering process is likely to result in robust competition for the market resulting in competitive pressure on the tenderers to offer competitive prices and high levels of service.

- The licence awarded will be for a reasonable period of five years with the option to extend the licence for three years.

Decision

173. Having considered the matters referred to in this Statement of Reasons, the ACCC considers that the Notified Conduct is unlikely to have the effect of substantially lessening competition, and the Notified Conduct is unlikely to result in public detriment which outweighs the public benefit.
174. Accordingly, the ACCC does not intend to take action to revoke the notification at this time. As with any notification, in accordance with section 93(3) of the Act, the ACCC may act to remove the protection afforded by the notification at a later stage if it is satisfied that the Notified Conduct is likely to have the effect of substantially lessening competition and the likely benefit to the public from the Notified Conduct will not outweigh the likely detriment to the public from the Notified Conduct.