

18 May 2018

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Dear Mr Hatfield and Ms Batten

**Gladstone Ports Corporation Limited – exclusive dealing notification**

We act for Gladstone Ports Corporation Limited (**GPC**).

On 13 March 2018, GPC lodged an exclusive dealing notification N10000453 (**Notification**) with the Commission.

**A. GPC's response to submissions from interested parties**

GPC has considered the following submissions in response to the Notification:

- Svitzer Australia Pty Ltd, dated 20 April 2018;
- the Australian Institute of Marine and Power Engineers, dated 13 April 2018;
- the Australian Maritime Officers Union, dated 6 April 2018;
- the Port Authority of New South Wales, dated 6 April 2018;
- Rio Tinto Aluminium Limited, dated 6 April 2018; and
- Smit Lamnalco Towage Australia Pty Ltd, dated 6 April 2018.

GPC wishes to provide the Commission with its response to those submissions in 2 Attachments - **Attachment A** and **Attachment B** to this letter.

Please contact us if the Commission would like any further information.

Thank you for your assistance to date.

Yours sincerely



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## 1 Extension of SMIT's licence

In section 3.1 of Svitzer's submission, Svitzer asserts that, "*if the Notification is not revoked, it will have the effect of extending the current exclusive licence by a further year (to a total of nine years), by effectively preventing entry in advance of the grant of the Exclusive Licence.*"

As set out in GPC's Notification,<sup>1</sup> the conduct described in the Notification will occur for up to eight years, commencing at a date yet to be determined but no later than 1 January 2020 and expiring no later than 31 December 2027.

The conduct described in the Notification does not encompass the possible 12 month period referred to in section 3.1 of Svitzer's submission, for the potential extension by up to 12 months of SMIT's existing licence.

GPC has not sought immunity for the potential extension because the potential extension for up to 12 months will not have the purpose or likely effect of substantially lessening competition in any market for the following reasons.

An extension of SMIT's licence by no more than 12 months will ensure that there will be minimal disruption to the towage services at the Port until the proposed competitive tender process is complete and the new licensee can mobilise to commence its towage operations at the Port. In fact, the rationale for the possible extension of SMIT's licence will aid in creating the opportunity for a new entrant providing towage services at the Port as a result of the competitive tender process. The possible extension will only be utilised should the winner of the competitive tender process require time to transition to the Port, allowing GPC to ensure towage services continue to be provided at the Port during that time.

As explained in GPC's submission in support of the Notification,<sup>2</sup> the timing of the competitive tender process and the award of the new exclusive licence is to allow for the completion of an LNG towage requirement review. That review is underway.

Following the competitive tender process, which is expected to be completed by 10 September 2018 (and subject to receipt of approvals from GPC's Board and GPC's Shareholding Minister), the successful tenderer will need time to adequately prepare to commence providing towage services under the new licence. The amount of time required will depend on the identity of the successful tenderer, which is not yet known.

The successful tenderer could require up to approximately 18 months from the time of winning the tender to adequately prepare to commence operating under the licence.

Having said this, it might not be necessary to extend SMIT's licence for 12 months if the successful tenderer has sufficient liquidity to enable them to commence providing the towage services at the Port an earlier date.

The likely counterfactual scenario to the potential extension of SMIT's licence by up to 12 months would be that, if lead-in time is required for the successful tenderer to begin supplying towage services at the Port, SMIT would continue to be the sole provider of towage services in the Port for up to 12 months because its towage vessels are already deployed in the Port.

<sup>1</sup> GPC Notification Attachment A, section 3.

<sup>2</sup> GPC Submission, section 6.

Consequently, there is no difference between the factual and counterfactual scenarios for the potential 12 extension of SMIT’s existing licence and no detriments to competition or otherwise will arise from it.

## 2 Proposed timeframe for the competitive tender process

The information in the table below describes GPC’s timetable for the procurement process to award the replacement exclusive towage licence. It shows the key milestones commencing with the issue of the Request for Expressions of Interest (“**EOI Request**”) until execution of the licence.

GPC’s timeframe for the procurement process will not commence unless it receives approval from its Shareholding Minister. The approval is pending.

No	Task	Start	Finish
<b>A.</b>	<b>EOI &amp; Tender - Construct &amp; Recommendation</b>	<b>Mon 28/05/18</b>	<b>Mon 10/09/18</b>
<b>1</b>	<b>Procurement Execution - EOI Process</b>	Mon 28/05/18	Wed 20/06/18
	Issue EOI	Mon 28/05/18	Mon 28/05/18
	Place advertisements locally, nationally and internationally	Mon 28/05/18	Fri 1/06/18
	EOI response duration	Mon 4/06/18	Fri 15/06/18
	Open EOIs via QTenders	Mon 18/06/18	Mon 18/06/18
	Select Bidders eligible for ITT <sup>3</sup> process	Tue 19/06/18	Wed 20/06/18
<b>2</b>	<b>Procurement Execution - ITT Process</b>	Thu 21/06/18	Mon 10/09/18
	Issue ITT to selected Bidders	Thu 21/06/18	Thu 21/06/18
	ITT response duration	Fri 22/06/18	Thu 26/07/18
	Open ITTs via QTenders	Fri 27/07/18	Fri 27/07/18
	Initial ITT evaluation and Bidder shortlisting by GPC	Mon 30/07/18	Fri 10/08/18
	Detailed ITT evaluation of Shortlisted Bidders	Tue 14/08/18	Mon 27/08/18
	Negotiations with Shortlisted Bidders	Tue 28/08/18	Mon 10/09/18
	Develop Preferred Bidder recommendation for approval purposes	Tue 28/08/18	Mon 10/09/18
<b>B.</b>	<b>Exclusive Towage Licence - Approvals &amp; Execution</b>	<b>Tue 11/09/18</b>	<b>Mon 3/12/18</b>
	Exclusive Towage Licence – executed by Preferred Bidder	Tue 11/09/18	Tue 11/09/18
	Approval by GPC Board	Tue 11/09/18	Fri 28/09/18
	Approval by Shareholding Ministers	Mon 1/10/18	Fri 30/11/18

<sup>3</sup> ITT means Invitation to Tender.

No	Task	Start	Finish
	Exclusive Towage Licence – executed (by GPC)	Mon 3/12/18	Mon 3/12/18

The purpose of the EOI Request is to solicit expressions of interest from bidders interested in bidding for an exclusive towage licence in the Port of Gladstone for a period of 5 years (with an option in GPC's favour for a further 3 years).

GPC will utilise responses to the EOI Request to decide who to invite to participate in the tender process. The Invitation to Tender will launch on Thursday 21 June 2018.

It is imperative that GPC know by no later than Friday 15 June 2018 that the ACCC does not intend to revoke the immunity conferred on 13 March 2018.

This is because GPC will be issuing Invitation to Tender documents to selected bidders on the basis they are being offered the opportunity to competitively bid for an exclusive towage licence. The Invitation to Tender will contain the proposed form of towage licence prepared by GPC that is suitable for the grant of an exclusive towage licence.

Certainty of the ACCC's position will similarly be of paramount importance to bidders as they will need to expend considerable executive management time and resources (including advisory and travel costs) in responding to GPC's request for tenders, including by attending site visits at the Port, attending GPC's management presentations and in preparing a conforming tender.

Therefore, in summary, a decision from the ACCC in mid-June 2018 is necessary to allow GPC to proceed with confidence (and bidders to respond in kind) to offer an exclusive towage licence in the Port of Gladstone that may commence with effect from as early as 1 January 2019.

### 3 Employment arrangements under the existing exclusive licence with SMIT

The submissions of the Australian Institute of Marine and Power Engineers (**AIMPE**) and the Australian Maritime Officers Union (**AMOU**) do not provide sufficient evidence to establish that the notified conduct would be likely to give rise to a significant public detriment.

In particular, GPC would like to respond to the following submissions of AIMPE and AMOU, which assert that, under the current exclusive licence:

- (a) there has been a reduction in safety standards;<sup>4</sup> and
- (b) increases in wages and / or employment conditions have been restricted.<sup>5</sup>

In relation to the first point, GPC and SMIT<sup>6</sup> do not agree that the current exclusive licence has reduced safety standards.

The towage industry is, (including SMIT as the existing operator, and the successful bidder for the proposed exclusive licence will be) subject to regulatory audits and strict inspection regimes to ensure the highest standards of safety. These facts are reflected in SMIT's licence to provide towage services at the Port and will, necessarily, be reflected in the new licence which is the subject of the Notification.

<sup>4</sup> AIMPE Submission dated 13 April 2018, page 5; AMOU Submission dated 6 April 2018, [10].

<sup>5</sup> AIMPE Submission dated 13 April 2018, page 4; AMOU Submission dated 6 April 2018, [10].

<sup>6</sup> See Smit Lamnalco Submission dated 6 April 2018, [61] – [62].

The submissions from the AMOU support the proposed exclusive licence on the basis that it provides a secure and productive way in which to assure service levels and the competency of staff.

Regarding the second point, it is not correct – the exclusive licence with SMIT does not restrict or limit wages or employment conditions.

In fact, SMIT's licence allows for an incremental cost for labour. Without divulging SMIT's commercially sensitive information, GPC understands that employees have enjoyed wage growth which has occurred annually.

SMIT's Enterprise Agreements are publicly available via the Fair Work Australia database and clearly show consistent and above national average wage growth over the life of the current licence.

Further, in response to AIMPE's submission<sup>7</sup> that the Notification requires further consideration of changes brought about by LNG towage operational requirements, GPC asks the Commission to note that its submission was based on the operating parameters existing at the time. Operating parameters change from time to time and are publicly available on the websites of both GPC and Marine Safety Queensland.

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<sup>7</sup> AIMPE Submission dated 13 April 2018, page 3.

# Attachment B

Point	What was submitted	GPC's response	Reference in Svitzer's submission
Impact on market and competition	<p>The Exclusive Licence would:</p> <ul style="list-style-type: none"> <li>• Preclude competition between towage operators that takes place at other ports, primarily outside of those owned by the State of Queensland,</li> <li>• Eliminate the competitive constraints by reason of the threat of entry over the term of the Exclusive Licence, and</li> <li>• Stifle the ability of market forces to constantly test and shape market structure, allowing market participants the flexibility adapt to changing market conditions.</li> </ul>	<ul style="list-style-type: none"> <li>• 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 of Gladstone.</li> <li>• Examples were provided in the PwC report as to the Ports of Newcastle and Brisbane where, after relatively short periods of competition, those towage markets were unable to support multiple operators and each of the markets essentially reverted to a single provider arrangement (refer PwC report, page 34).</li> <li>• There is no evidence presented by Svitzer that the threat of future entry by a new competitor presents as a meaningful or effective discipline on the commercial behaviour of the remaining operator. The examples provided in Svitzer's submission are isolated and, in the case of the Ports of Bundaberg and Eden, are not reliable comparators to the significantly larger and more complex Port of Gladstone.</li> <li>• Indeed, any threat of entry becomes less credible in markets where a sole provider is the most efficient means of providing the service, as potential new entrants will be aware that the only prospect of success is to displace completely the incumbent operator.</li> <li>• GPC's position is that intense competition occurs through the tender process which provides competition for entry to the market. The terms and conditions of the new Licence will be designed to ensure that prices and service levels are competitive for the duration of the licence.</li> </ul>	3.2(a), 6.3
Public benefits	<p>Any public benefits are limited or non-existent. In particular:</p> <ul style="list-style-type: none"> <li>• An Exclusive Licence is unlikely to increase competition <i>for</i> the market and increase competitive pressure. The process of transformation of competition between these two states and continued threat of re-entry provides significant competitive tension and public benefit.</li> <li>• An Exclusive Licence is unlikely to decrease prices. Indeed, an Exclusive Licence is more likely to have the opposite effect, as evidenced by Smit's price increase when volume forecasts were not met.</li> <li>• An Exclusive Licence is likely to reduce opportunity and incentive to reduce costs both through innovation and other cost reducing mechanisms such as industrial relations reform. The concern as to the introduction of spare capacity can be resolved by cross hiring.</li> </ul>	<ul style="list-style-type: none"> <li>• GPC's experience in previous tenders for an Exclusive Licence at the Port of Gladstone is that the tender process was keenly contested by alternative providers. This competitive tender process provided the appropriate market competition. In the case of the most recent competitive tender, this process allowed a new entrant to successfully establish itself in Australia.</li> <li>• A competitive tender provides an effective way to establish towage charges which recover the underlying efficient costs of service delivery. Where the service requirement is clearly specified, all providers have the opportunity to compete equally. The parameters of contestability are transparent and well-understood.</li> <li>• There are strong incentives for innovation and for pursuing other cost-savings initiatives. Building the effect of these into the tendered rates allows the tenderer to enhance the likelihood of its bid being selected. The Licence framework can be structured to ensure that costs are managed prudently, and any benefits of future scale efficiencies are passed-through to towage users.</li> </ul>	3.2(a), 6.3

Point	What was submitted	GPC's response	Reference in Svitzer's submission
		<ul style="list-style-type: none"> <li>• Svitzer's submission misrepresents the pricing framework established in the current Licence, which was described in detail at page 14 of the PwC report. Key characteristics to note include: <ul style="list-style-type: none"> <li>○ The current Licence pricing framework, and the towage pricing framework that applied before that, allows for prospective price adjustments where actual vessel numbers / tug jobs fall short of forecast. This feature was described clearly in the tender documentation, and all respondents (including Svitzer) would have been aware of the way the price adjustment mechanism was intended to operate.</li> <li>○ Over the term of the Exclusive Licence average towage charges have fallen by 14.6 per cent in real terms (see page 9 of the PwC report).</li> <li>○ Service standards under the current Licence are not identical to those under the previous Licence. To the extent that service standards <i>increased</i> (reflecting the requirements of the Safety Regulator (MSQ) and prescribed in the PPM), then the 3 per cent reduction in average towage charges at the commencement of the Licence (see page 9 of the PwC report) understates the true reduction in real towage charges realised under the current Exclusive Licence.</li> </ul> </li> <li>• Cross-hiring matters are considered further below.</li> </ul>	
8,000 threshold	Little reliance should therefore be placed on the "8,000 tug jobs" proposition	<ul style="list-style-type: none"> <li>• The PwC report provides a discussion of the relevance and applicability of the Productivity Commission's 8,000 tug jobs benchmark (see, for instance, page 23 of the PwC report).</li> <li>• GPC agrees that the 8,000 tug jobs is not a definitive trigger threshold. It could be 7,000 or 11,000 and should be regarded as indicative only. Further and specific consideration is required of the different assumptions about particular costs, demand and other characteristics of the Port in question.</li> <li>• PwC's modelling, supported by Aurecon's analysis which is calibrated to the specific tug operating parameters at the Port of Gladstone, found that a sole towage provider would be the most efficient means of servicing towage demand at the Port, despite that demand being above the notional 8,000 tug job benchmark.</li> </ul>	2.2
Competition in/for	Svitzer considers framing the question as a choice between competition <i>for</i> and competition <i>in</i> sets up a false dichotomy. Competition in the market does not preclude competition for the market. In fact, in workably contestable markets, competition in the market often transforms to competition for the market. It is this contest which is the essence of the competitive process.	<ul style="list-style-type: none"> <li>• As noted above, 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 of Gladstone.</li> <li>• 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.</li> <li>• An Exclusive Licence, properly structured and implemented, is an effective way of encouraging competition <i>for</i> the market. This competition is likely to be more effective and more robust than competition in the market, where</li> </ul>	3.2(a)



Point	What was submitted	GPC's response	Reference in Svitzer's submission
		market analysis indicates that a single provider is the least-cost means of meeting demand for towage services.	
Competitive pressures	Many of Svitzer's customers have significant purchasing power and Svitzer is well aware that if prices are not competitive, those customers have the ability and incentive to sponsor entry of a competitor.	<ul style="list-style-type: none"> <li>• It is only in smaller ports, or where there is a single or dominant customer, where customers have encouraged the entry of an alternative towage provider. The entry of RivTow at Hay Point Coal Terminal, which caters exclusively for BMA/BHP coal exports, is a case in point (see PwC report page 35).</li> <li>• PwC's research has otherwise not identified any instances in larger, multi-commodity ports, where a single customer or collective of customers has successfully sponsored the entry of a new towage provider.</li> <li>• Customers of the Port of Gladstone have demonstrated their support for an Exclusive Licence going forward via supporting submissions to GPC and the ACCC. The ACCC's previous decisions relating to the current licence have proven robust, with actual experience validating the cost and service level benefits argued in GPC's submissions of 2009 and 2012.</li> </ul>	3.2(a)
Sustainable competition	The examples of Fremantle and Bundaberg below indicate that competitive entry is possible, and that it may result in either sustained competition or ultimate rationalisation with the survival of the most efficient operator, yet remaining subject to the constant threat of new entry.	<ul style="list-style-type: none"> <li>• Port of Fremantle – with respect to this Port, the towage market is segmented. C Class Tugs service only a segment of the towage market in Fremantle, typically smaller vessels, and cannot effectively compete for other towage services.</li> <li>• Port of Bundaberg – GPC understands that Queensland Sugar was approached by Wide Bay Shipping and reached a direct commercial agreement on more competitive terms than those offered by Svitzer. In effect, this resulted in a single customer contracting on exclusive terms with a single provider. This created a market structure functionally equivalent to an Exclusive Licence, but where this arrangement is organized by a single dominant customer, rather than the Port Authority on behalf of a larger customer base. Further, the Port of Bundaberg has very different characteristics to the Port of Gladstone – the Port of Bundaberg is a very small port and most of its tug jobs only require one tug.</li> <li>• Towage services at the Port of Gladstone are subject to a completely different operational dynamic to those in place at the Port of Fremantle and the Port of Bundaberg.</li> <li>• At the Port of Fremantle, where there are multiple towage providers, the towage providers are likely restricted in that they are likely only able to provide alternate and/or partial services.</li> <li>• Efficient utilisation of Port capacity is paramount to GPC's customers and inefficiency resulting from multiple towage providers poses a significant risk.</li> </ul>	3.2(b)

Point	What was submitted	GPC's response	Reference in Svitzer's submission
Principal-Agent problems	Svitzer considers that there is a principal-agent problem in an exclusive licensing process conducted by the port authority	<ul style="list-style-type: none"> <li>The basis of the Exclusive Licence is that GPC, as the Port Authority, is seeking to establish a towage service arrangement which best meets the towage requirements of a large and diverse Port customer base, and which supports the safe, reliable, efficient and integrated functioning of the Port.</li> <li>A principal-agent problem would occur where GPC, as "agent", had an incentive structure which is misaligned to that of its customers (the "principals"). GPC has no financial incentive to seek any standard other than that required to meet the objectives above, which are based on GPC's statutory powers and functions.</li> <li>Under the current Licence (and anticipated new licence), towage costs incurred by the Licensee are recovered directly from Port users, without any connection to GPC. GPC's objectives are aligned to maximizing the throughput of the Port, and it has no interest in seeking to make towage services higher-cost than needed.</li> <li>GPC has sought customer engagement throughout the process, with all major Port users being supportive of the direction GPC is proposing to adopt for the provision of towage services at the Port.</li> <li>It is important to understand the distinction between GPC, as the Port Authority, and Maritime Safety Queensland (MSQ), which is part of the Queensland Department of Transport and Main Roads and which is responsible for maritime safety.</li> <li>MSQ, as the regulator under TOMSA, is the custodian for Vessel Traffic Safety and has a determining input in the way in which vessel traffic is undertaken within the Port.</li> <li>MSQ is also responsible for delivering a range of services on behalf of the national regulator (the Australian Maritime Safety Authority) under the Marine Safety (Domestic Commercial Vessel) National Law Act 2012.</li> </ul>	3.2(e), 5.4
PwC Pricing Analysis	<p>The PwC Report contains a comparison of towage charges at the Port of Gladstone relative to the published pricing of nine other unnamed ports. The PwC Report uses this data to demonstrate that the "total cost per vessel call for cape sized vessel at the Port is approximately 61% cheaper..."</p> <p>This analysis should be given little weight as:</p> <ul style="list-style-type: none"> <li>It is not possible to assess whether the unnamed ports included in the analysis are of a comparable type to the port of Gladstone and whether they have a comparable volume of towage jobs,</li> <li>Each port has individualized factors which may influence cost per tug job including the scale (i.e. number of tug jobs)</li> </ul>	<ul style="list-style-type: none"> <li>The comparison of towage charges in the PwC report uses information from a range of comparable large bulk and commodity ports in Australia. Towage costs were referenced from public information, or information provided to GPC by its customers. The per vessel cost data was normalised, as noted in Figure 6 on page 9 of the PwC report, to account for factors such as time-based charges that might apply in some ports.</li> <li>GPC maintains that the ports included in this comparison are reasonable comparators to the Port of Gladstone, notwithstanding that each port has individual factors which impact the way towage services are provided and the cost to users.</li> <li>PwC's analysis indicates that the current Exclusive Licence arrangement has delivered standard harbour towage services for a Cape-size vessel which are towards the lower end of the range of reported costs at other Ports.</li> </ul>	3.3(a), 6.3

Point	What was submitted	GPC's response	Reference in Svitzer's submission
	<p>and may include other factors such as the geography of the port, remoteness and homogeneity of calling vessel fleet.</p> <ul style="list-style-type: none"> <li>• Reliance on published pricing for actual cost of towage is misleading, as many customers can and do negotiate significant discounts to published prices in ports not subject to exclusive licensing,</li> <li>• More discounting occurs at ports <u>without</u> exclusive licensing.</li> </ul>	<ul style="list-style-type: none"> <li>• The Essential Services Commission of South Australia (ESCOSA) published a <i>Port Price Benchmarking Study</i><sup>1</sup>, in March 2017. Appendix D of this report contains benchmark port costs for different vessels and cargoes at a range of Australian ports, including Gladstone. This analysis indicates that cost of towage at the Port of Gladstone is at the lower end of the range for both Liquid Bulk and Dry Bulk vessels.</li> <li>• GPC is aware that discounting arrangements are used in some other ports for towage services. GPC has engaged with customers in that regard and acknowledges that parent company rebating is known to occur on a more global scale.</li> <li>• The extent to which discounting arrangements may occur is generally commercially sensitive. This adversely impacts the transparency of towage commercial arrangements, and in GPC's view, would make it more difficult for a new entrant to compete with an incumbent towage provider, where the incumbent has established opaque and potentially complex rebate arrangements with customers on a global or other level.</li> <li>• The ESCOSA <i>Port Price Benchmarking Study</i> supports using published rates in benchmarking port costs, noting: <ul style="list-style-type: none"> <li><i>'...the analysis ... is based entirely on published/standard schedules of charges, and does not take into account privately negotiated discounts from these rates. However, as this information is, almost by definition, commercially confidential, it is not possible to obtain reliable information on discounts offered across the wide range of ports required for a satisfactory benchmarking process. Under these circumstances it is better to rely entirely on formal tariffs than to attempt to incorporate information on discounting that is fragmentary and uncertain.'</i></li> </ul> </li> <li>• Absent further information being provided by Svitzer on the extent and value of any discounts, the use of published or contracted towage rates in the pricing comparison included in the PwC report is appropriate for comparative analysis.</li> <li>• GPC also notes that users representing each of the major trades at the Port of Gladstone have provided support for the proposed Exclusive Licence approach. GPC is continuing to engage with its customers as it considers how to define the structure and framework for towage charges in the future, as a key feature of the proposed future Exclusive Licence arrangement.</li> </ul>	
PwC market segmentation	PwC's modelling of options 2, 3 and 4 essentially splits the Port into two or three customer groups and allocates a separate towage provider for each of these groups which has enough tugs to ensure	<ul style="list-style-type: none"> <li>• The towage market options assessed in the PwC report were intended to illustrate the level of fleet redundancy, and associated cost-penalty, were the</li> </ul>	3-3(b), 4.3

<sup>1</sup> Available at: <https://www.escosa.sa.gov.au/ArticleDocuments/1024/20170424-PortsPricingAccessReview2017-BenchmarkingStudy-GHD.pdf.aspx?Embed=Y>  
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Point	What was submitted	GPC's response	Reference in Svitzer's submission
	<p>that each group can be immediately serviced when multiple ships in an individual group require towage simultaneously. Svitzer considers that this is unrealistic – not least because cross-hiring arrangements occur in ports with multiple providers.</p>	<p>towage market at the Port of Gladstone to be segmented, based on certain customer/trade groupings.</p> <ul style="list-style-type: none"> <li>• This market structure is not “unrealistic”. Similar “segmented” models operate at some other ports. For instance, the Port of Hay Point has two towage providers, which each service separate user groups at either the Dalrymple Bay Coal Terminal or the Hay Point Coal Terminal. GPC understands there are no cross-hiring or tug sharing arrangements in place at Hay Point.</li> <li>• The PwC report acknowledges that cross-hiring arrangements are used at some Australian ports. Where cross-hiring exists, however, its success is dependent on a high level of cooperation and collaboration between the two (or more) providers, each of whom rely on the other. This cooperative relationship is fundamentally inconsistent with the expectation that the two providers would also vigorously compete with each other, seeking to capture market share through price or non-price rivalry. Thus, while cross-hiring may offer the potential to limit any investment in redundant tug capacity, it does so at the cost of diminishing any expected contestability as might occur between the various operators within that market.</li> <li>• The existence of more than one towage provider, where there is some level of joint reliance, does not in and of itself support a finding of contestability. The Port of Brisbane example noted in the PwC report (see page 34), illustrates that Smit exited the market due to the lack of viability of the Brisbane operation and as a result subcontracted its services to the incumbent Svitzer Australia. In its submission, Svitzer claims (in section 2.1) that despite the subcontracting arrangement with Smit, <i>‘Smit continues to compete on price independently of Svitzer and maintains a direct relationship with those Customers’</i>.</li> <li>• Smit Lamnalco’s submission to the ACCC on this notification process is not consistent with Svitzer’s claim. Smit Lamnalco’s view is that it is not viable for a second operator to compete in most ports (even in large ports) in the Australian market. This evidenced by Smit Lamnalco’s withdrawal from various Australian ports. Smit Lamnalco states <i>“...in September 2015, Smit Lamnalco ceased operating tugs in its own right in the ports of Newcastle, Melbourne and Sydney and in February 2018, Brisbane... the absence of an exclusive licence has also meant that there has been limited competitive tension to constrain the incumbent...”</i>. This demonstrates that the existence of more than one towage provider does not necessarily result in a sustained competitive market for towage services.</li> <li>• The ACCC’s 2012 decision specifically considered the natural monopolistic characteristics of the Port of Gladstone and the public benefits that were being realised in terms of price and service level under the Exclusive Licence. In section 4.39 the ACCC stated the <i>“features of the Port of</i></li> </ul>	

Point	What was submitted	GPC's response	Reference in Svitzer's submission
		<p><i>Gladstone increase the minimum scale for new entry because, in order to maintain acceptable waiting times, an operator would need more tugs to service a given number of vessels during peak periods compared to other ports where trips are shorter, tend to require fewer tugs per vessel call, and are more evenly spread out over the day”.</i></p> <ul style="list-style-type: none"> <li>The Port of Gladstone is not an evenly distributed logistics chain. Shipping is not uniform over any given period as the number of vessels fluctuates on any given day and this results in uneven tug utilisation. GPC considers that the options assessed are the most likely distribution options and note these were developed in consultation with the major customers of the port.</li> <li>Whilst acknowledging that cross-hiring does occur at some other ports, the frequency and predictability of the number and type of tug for any given day cannot be accurately forecasted or arranged without loss of port shipping capacity at the Port of Gladstone.</li> </ul>	
PwC market segmentation	Open competition yields significant benefits to customers, and even if the transformation to competition for the market has not occurred, the continued threat of entry and ability of customers and/or the port to sponsor new entry constraints incumbents.	<ul style="list-style-type: none"> <li>Svitzer has not provided evidence of open competition within the Australian harbour towage market. Rather, it has provided a number of examples that relate to cooperation between competitors within a particular towage market. Svitzer has provided no evidence of vigorous price or non-price contestability. Further, benchmarking towage costs would not support a view that towage rates are lower in such ‘competitive’ markets (refer, for instance, to the port pricing benchmarking undertaken by ESCOSA, and referred to above).</li> <li>As noted above, instances of where a port user has sponsored the entry of a new towage operator are rare. The single example provided by Svitzer relates to a port which is not comparable to the Port of Gladstone.</li> </ul>	3-3(b)
Tug berth assumption	Svitzer notes that the cost of constructing a second berthing facility would be met by a second entrant to the Port, in any event. This occurred in Port Hedland and Svitzer has built or upgraded tug infrastructure in multiple ports where it operates.	<ul style="list-style-type: none"> <li>The PwC report sought to assess the impacts of a future towage market structure that was segmented by major trades / customer groupings. This analysis, informed by harbour modelling undertaken by Aurecon, indicated that in any multi-provider model there would be a need for additional tugs beyond the capacity of the current tug base.</li> <li>The current tug base is owned by GPC and leased to Smit Lamnalco. The tug base would be offered for lease to a future towage licensee.</li> <li>There is sufficient capacity within the existing tug base to meet current (and forecast) demand for tug jobs, based on a single-provider arrangement.</li> <li>PwC’s analysis did not consider matters such as which party would fund or build any additional tug facilities, should these be required (see page 42). Rather, it acknowledged that the cost of expanding the existing tug base to accommodate additional fleet (if required) would reflect an unnecessary duplication of investment. Ultimately the cost of the unnecessary,</li> </ul>	3-4(b)

Point	What was submitted	GPC's response	Reference in Svitzer's submission
		<p>duplicated investment would need to be recovered in some way from users of towage services.</p> <ul style="list-style-type: none"> <li>• Svitzer's submission implies that these additional costs would be absorbed by a towage operator without necessarily recovering the investment. A more realistic assessment would be that any such costs would form part of the operator's cost structure and ultimately would need to be recovered in some way.</li> <li>• For the purposes of the PwC analysis, GPC estimated the cost of expanding the tug base facility based on the most relevant capital benchmark - the cost of constructing the existing tug facility in 2012.</li> </ul>	
Vessels passing in the Channel	Vessels pass through the channel one after another – widening would only be required if GPC wanted to bring in larger vessels, which has no relevance to the number of towage providers.	<ul style="list-style-type: none"> <li>• To avoid the need for costly channel expansion developments, utilisation of all available water space is required to maximise the shipping capacity at the Port to meet demand.</li> <li>• Unpredictable and fluctuating presentation of vessels at the Port, combined with channel geography and the configuration of the Port, introduces scheduling and prioritisation complexities not seen at many other ports.</li> <li>• A well-organised and aligned towage service is critical in maximising shipping capacity at the Port. Inefficiency in the delivery of towage services, or inappropriateness or incompatibility of towage service delivery to other aspects of the Port's operations, presents as a risk of lost channel capacity.</li> <li>• GPC also notes that the single towage operator option considered in the PwC report, and validated by the Aurecon shipping capacity modelling for the range of plausible scheduling scenarios, is the most cost efficient towage option for the Port.</li> </ul>	3.4(b)
Precluding smaller competitors	The EL and TLF would also prevent smaller competitors from being able to enter and compete at Port of Gladstone, to compete for a limited number or type of tug jobs, or to enter into alliances and joint ventures that enable them to compete on a larger scale.	<ul style="list-style-type: none"> <li>• GPC intends that, for a future Exclusive Licence, tenders would open to joint ventures/alliances, provided they satisfy towage safety and operational standards as required under the Licence and offer the most competitive towage charges for Port users.</li> <li>• The Port of Gladstone is one of the largest multi commodity ports in Australia. The towage task is significant in comparison to the majority of other ports, and distributed across a large geographic area. Although acknowledging a proportion of vessel calls require two or fewer tugs for entry/departure from the Port, the share of the market addressable by a single provider is considerably smaller, once complexities such as concurrent vessel movements, steaming time and crewing and tug re-provisioning, etc are accounted for.</li> <li>• The frequency and predictability of tug jobs necessary to satisfy a minor service provider is unlikely to be experienced at the Port due to uneven and ad hoc shipping.</li> </ul>	4.1

Point	What was submitted	GPC's response	Reference in Svitzer's submission
		<ul style="list-style-type: none"> <li>• In 2012, the ACCC determined that, due to the characteristics of the Port of Gladstone and the minimum scale of entry for towage services at the Port, which have not materially changed, a second towage operator would require more tugs to service peak periods than ordinarily required if shipping presented evenly and consistently. The ACCC considered that: <ul style="list-style-type: none"> <li><i>“these features of the Port of Gladstone increase the minimum scale for new entry because, in order to maintain acceptable waiting times, an operator would need more tugs to service a given number of vessels during peak periods compared to other ports where trips are shorter, tend to require fewer tugs per vessel call, and are more evenly spread out over the day.”</i></li> </ul> </li> <li>• Further, this market structure would contemplate either: <ul style="list-style-type: none"> <li>○ segmenting the market into a notional small/large vessel strata (similar in some respects to the market analysis in the PwC report), such that the smaller operator did not readily compete with the larger provider, and where the larger provider would still need to hold a sufficiently large tug fleet to meet demand from the dominant coal, alumina and LNG trades, necessarily requiring investment in redundant tug capacity, or</li> <li>○ cooperative arrangements as between the smaller/larger providers, in which case there would be no meaningful competition between the providers.</li> </ul> </li> <li>• GPC contends that any alliances or cross hiring arrangements between operators potentially increases the risk of lost shipping capacity due to the inability to cater for every shipping requirement scenario.</li> </ul>	
Open market	The simultaneous operation of competing towage operators, which has been and is taking place in several ports – other than Queensland – over substantial periods is effectively precluded.	<ul style="list-style-type: none"> <li>• Svitzer's submission appears to equate <i>multiple</i> providers with <i>competing</i> providers. In the case studies provided in the Svitzer submission cross-hiring arrangements typically prevail. GPC maintains its view that cross-hiring arrangements require a level of collaboration and cooperation that is inconsistent with an expectation of the providers then competing in the same market.</li> </ul>	4.1
Open market	A fundamental flaw with [PwC's] approach is that it overlooks one of the main advantages of the open market: that market structures can readily adapt to changes in conditions to supply and demand... This judgement is inevitably made in the context of imperfect information about consumer preferences, supplier costs and the structure of future demand.	<ul style="list-style-type: none"> <li>• An Exclusive Licence arrangement can be structured to allow for flexibility in adapting to changes in market conditions, and most particularly to changes in demand.</li> <li>• For example, under the current Licence: <ul style="list-style-type: none"> <li>Harbour towage rates increased in FY14, as a result of a downturn in vessel arrivals and tug demand. However, over the term of the Licence standard harbour towage charges have reduced by 14.6 per cent in real</li> </ul> </li> </ul>	4.4

Point	What was submitted	GPC's response	Reference in Svitzer's submission
		<p>terms, largely a result of the Licence's pricing framework building in an expectation of costs reducing due to economies of scale.</p> <ul style="list-style-type: none"> <li>Open market structures may be able to change in conditions in supply/demand, but this does make such adjustments costless. To the extent there are fixed costs, lumpy investments, and sunk costs with market entry/exit, then costs associated with future uncertainty will still arise.</li> </ul>	
Natural monopoly	The assumption that the existence of a natural monopoly makes the use of exclusive licensing desirable permeates the PwC Report.	<ul style="list-style-type: none"> <li>PwC's modelling considers whether a single provider is the least cost means of delivering towage services over the proposed licensing term, given alternative ways in which the towage market might be structured.</li> <li>PwC's modelling does not "assume" the existence of natural monopoly conditions. Rather, it uses market information and other benchmarked cost and performance data, to seek to identify whether there is a cost advantage or penalty associated with having one or multiple towage providers in the Port of Gladstone. The modelling indicates that, for the scale and distribution of towage demand over the proposed Licence term, a single provider is the least-cost configuration.</li> </ul>	4.4
Natural monopoly	<p>Svitzer considers that harbor towage is not a natural monopoly; while competition in the market may transform to competition for the market, absent exclusivity, the threat of entry provides a powerful competitive constraint, restricting the ability of any sole operator in a port to behave as a monopolist.</p> <p>However, Svitzer considers that, even if towage services were a monopoly, it does not follow that bidding for an exclusive licence would be an appropriate solution.</p>	<ul style="list-style-type: none"> <li>Svitzer has provided no tangible evidence of the extent to which the threat of market entry is credible or meaningful in constraining the commercial behaviour of an incumbent towage provider.</li> <li>GPC's view is that the threat of market entry is less credible in markets where 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.</li> <li>The PwC report (see page 50) outlines the advantages of an Exclusive Licence, including as a mechanism to secure the orderly provision of towage services, and to minimize the risk of disruption to services were a potential towage competitor to enter and then exit the market.</li> <li>An Exclusive Licence also offers the opportunity to focus competitive rivalry in a way which meets port user's operational requirements with the most competitive charges.</li> </ul>	4.4
Future demand assumptions	Svitzer considers that it is exceptionally difficult to forecast what the structure and level of demand will look like today until the end of the proposed EL period. Markets may be extremely volatile for the next 9 years and potentially unforeseen technological changes will affect tugs and vessels.	<ul style="list-style-type: none"> <li>GPC's submission and the PwC report both provide a detailed analysis of the way the Port's trades have developed over the term of the current Licence, and how they are forecast to develop over the term of the proposed new Licence. GPC acknowledges that all forecasts carry a level of uncertainty.</li> <li>GPC has developed its demand forecasts based on a range of data sources including: <ul style="list-style-type: none"> <li>Trade customer submissions</li> </ul> </li> </ul>	5.1



Point	What was submitted	GPC's response	Reference in Svitzer's submission
		<ul style="list-style-type: none"> <li>○ GPC's historical validations and projections</li> <li>○ Macro and microeconomic forecasts from various sources</li> <li>○ Market intelligence sought from export and import buyers</li> <li>• There are various mechanisms available to GPC to manage uncertainty and to ensure that attendant risks are allocated to the party best able to manage them. Specifically, with respect to demand for towage services: <ul style="list-style-type: none"> <li>○ in the short term, this risk cannot be managed by a towage provider, which needs to ensure that it has sufficient tugs and crews available to meet anticipated demand. Within the current Licence, to the extent that actual tug job numbers differed from forecasts, this was managed through price adjustment mechanisms, as summarised above and described in detail in the Licence.</li> <li>○ over the medium term, there are more management options available, including options to mobilise or demobilise hulls or change crewing rosters. GPC intends that each of these options would be accommodated within the proposed new Licence, with clear triggers and decision-making rules for any amendments in the services required of the Licensee.</li> </ul> </li> <li>• GPC's will engage with towage providers, port users and key stakeholders such as MSQ, to ensure that sufficient flexibility is included within the new Licence to allow for the adoption of new technologies and other service innovations, where these benefit users and maintain or improve Port safety and/or would allow the Port to be operated more efficiently and effectively.</li> <li>• GPC believes that advances in technology, as these relate to the commercial provision of towage services, are able to be anticipated in the design of the Exclusive Licence. For instance, the mechanics of the Exclusive Licence will be able anticipate changes in towage demand brought about by changes in technology.</li> </ul>	
LNG	It is also clear from the PwC Report that there was (and in Svitzer's view continues to be) considerable uncertainty as to both whether and when demand from LNG vessels will increase	<ul style="list-style-type: none"> <li>• The PwC report (see page 13) acknowledges that, at the time of the tender for the current Licence, there was significant uncertainty regarding the timing and scale of any demand for LNG towage services.</li> <li>• Each of the three LNG consortia have now reached operational production. Vessel arrivals and the demand for LNG towage services has stabilised. Only limited further growth is anticipated over the proposed new Licence term.</li> <li>• Although LNG vessels are expected to continue to require a higher standard of towage service (including potentially higher power-rated tugs), GPC intends to seek as part of the new Licence a more integrated pricing framework for LNG towage services in the expectation that this will allow for an efficient configuration and utilisation of the new Licensee's fleet of tugs.</li> </ul>	5.1

Point	What was submitted	GPC's response	Reference in Svitzer's submission
Upgrading tugs	In the absence of exclusive licensing, upgraded tugs would instead have been provided in stages, as and when upgraded tugs were necessary for the proper operation of the Port in response to actual demand volumes.	<ul style="list-style-type: none"> <li>• With respect to LNG towage services, the timing of the mobilisation of new LNG tugs, and the size and configuration of those vessels, was determined by LNG users and MSQ. This was informed by the LNG users' own schedules for construction of their Curtis Island facilities, their expected ramp-up in LNG production and vessel arrivals. In fact, the LNG industry instructed GPC and subsequently, the towage provider regarding the type, timing and provision of tugs for their industry.</li> <li>• Although tugs can readily be moved between ports, the particular tug specification required by LNG users/MSQ (and including the requirement for five, equivalent standard tugs) meant that there was a significant lead-time for tug procurement and mobilisation.</li> <li>• GPC does not agree with Svitzer's claim of efficiency benefits being "eroded". The pricing framework for LNG services allows Smit to recover all prudent and efficient incremental costs associated with LNG towage services, from LNG towage users. To the extent that LNG users required new tug capacity to be brought to the Port of Gladstone in turn requiring fixed costs to be incurred in mobilising the new tugs, the recovery of those fixed costs from LNG users is not an "erosion" of any efficiency benefit.</li> </ul>	5.1(a)
Upgrading tugs	While the later purchase of LNG tugs demonstrates that the tender process for EL does not necessarily prevent further and/or upgraded tugs being purchased during the licence period, it does demonstrate how this can significantly erode the supposed efficiency benefits for the fixed EL allowing providers to spread the fixed costs over the EL period.		
Technology	Svitzer considers that it is certain that technological advances will lead to unanticipated developments both in terms of tugs and vessels. For example, more advanced tugs and vessels may reduce the number of tugs required for certain vessel movements before the end of 2027. Technology may provide for significant economies of scale which could be spread amongst ports.	<ul style="list-style-type: none"> <li>• GPC considers the mostly likely technology benefits to be related to automation and fuelling developments.</li> <li>• The proposed Exclusive Licence tender process will allow bidders to offer a number of proposals, thereby encouraging them to engage in innovation, including through considering future technology benefits.</li> <li>• The tender process will not restrict technology benefits. Rather, it will provide competitive tension for bidders to identify potential value opportunities within their offers.</li> <li>• The Exclusive Licence can be structured to accommodate factors such as a change in tug or vessel technology. As noted above, GPC intends that the proposed Licence will provide a pathway for both the increase in tug numbers and crews, if required, as well as the potential for rationalisation in tug numbers, if required.</li> </ul>	5.2, 6.3
Sunk costs and entry costs	Although entry costs are not trivial, many of these costs can be recovered on exit. The sunk cost problem is much less significant in the case of towage. Irrecoverable costs are small relative to the revenue from towage operations in a substantial port.	<ul style="list-style-type: none"> <li>• Tug vessels are mobile assets which can be readily relocated to other ports.</li> <li>• There is an established market in second-hand vessels, as well as an active market for wet- and dry-leasing of tugs (primarily for offshore oil and gas rigs, more so than for major ports).</li> <li>• Sunk costs relate more to the costs of mobilising vessels for entry to a particular market (physical relocation, configuration to meet local conditions, etc), establishing a presence in that market (including supply chains, and access to crews etc), and the costs of having tug capacity available to meet demand.</li> </ul>	5.2, 5.3

Point	What was submitted	GPC's response	Reference in Svitzer's submission
		<ul style="list-style-type: none"> <li>It is unclear how these costs could be recovered upon exit, as claimed by Svitzer. They would not be sunk costs if they could be recovered on exit.</li> </ul>	
GPC has different priorities to its customers	<p>GPC has different priorities to its customers, as demonstrated by the imposition of the “gold standard” and the fact weight has been given to the “administrative benefits” of having a single operator and the complaint that “multiple towage operators would require the development of priority systems and other processes”. Svitzer notes that “the Port of Gladstone must already consider a wide variety of factors when scheduling each vessel arriving or departing the Port and the addition of a second towage provider is, relative to all of the other factors, not remotely material.”</p>	<ul style="list-style-type: none"> <li>GPC accepts that where shipping is stable with little variation, towage services may potentially be able to be provided by more than one towage operator with minimal effect. However, a single operator is more likely to be able to respond to the variability of shipping at the Port of Gladstone, without impacting scheduling and channel capacity.</li> <li>GPC's customers require and expect a towage operator to be able to respond to the variable and unpredictable shipping dynamic. Therefore, an operator must be able to service a shipping schedule that deals with variability without compromising channel capacity.</li> <li>Were there redundant channel capacity at the Port, vessels could be scheduled according to tug availability or a minimalistic towage service. Given this is not the case, GPC is seeking to meet its customer's priorities and expectations through a single towage operator model at the Port.</li> </ul>	5.4
LNG towage pricing framework	<p>There is uncertainty around the end of the exclusive licence period, which Svitzer considers fed directly through to the prices charged to LNG customers when Smit agreed to invest huge sums in these tugs several years into the current exclusive licence.</p> <p>Smit was able to (and in fact did) charge uncompetitive prices to LNG users when asked to purchase further LNG tugs. Svitzer considers that this results in LNG users effectively cross subsidizing other port users at the Port of Gladstone</p>	<ul style="list-style-type: none"> <li>The LNG pricing framework is described in the PwC report (see page 14) and in further detail above. Importantly, the LNG pricing framework is transparent to LNG customers. Each year, GPC has provided information to each LNG customer explaining how price adjustments under the Licence framework have been made.</li> <li>GPC disputes Svitzer's claim that LNG towage charges were “uncompetitive”. The charges reflected the costs of the LNG tugs as required by LNG users and MSQ. To the extent that “per tug job” costs were high, this reflected the delay in the arrival of the LNG vessels compared to the schedule originally advised by each LNG user.</li> <li>Analysis by PwC for GPC, undertaken at the time the LNG tugs were being mobilised into the Port of Gladstone, indicated that when converted to a “per day” equivalent charter rate, Smit's LNG towage charges were comparable to published charter rates for short-term hire of towage vessels.</li> <li>Svitzer's claim of cross-subsidisation by LNG users to other port users is incorrect. LNG towage charges reflect the incremental prudent and efficient costs of providing LNG towage services. A proportion of LNG vessels are supported by standard harbour tugs, for which LNG users pay the applicable standard harbour rate (and that rate is set anticipating demand from LNG vessels, meaning that it is lower than would otherwise be the case, such that other port users benefit from LNG users sharing part of the costs attributable to the standard harbour towage fleet).</li> <li>GPC has commissioned cost audits, as allowed for in the current Licence, to verify Smit's costs and confirm the appropriate allocation of these costs</li> </ul>	6.1, 6.2

Point	What was submitted	GPC's response	Reference in Svitzer's submission
		<p>between the Standard and LNG users. GPC has not identified any material issues through these audits.</p> <ul style="list-style-type: none"> <li>Appendix A of the PwC Report contains an analysis illustrating the current number of LNG tugs not able to service the LNG industry demand without affecting service levels. To provide the current level of service, the LNG industry requires periodic access to the Standard Harbour tugs. Conversely, the analysis also shows that the Standard Harbour tugs are able to service non-LNG demand without relying on the LNG tugs. This combined with the result of cost audits demonstrates that there is no cross-subsidisation by LNG users to other port users.</li> </ul>	