Pacific Maritime
LAWYERS & CONSULTANTS

Our Ref: JK:AM:2022528

8 August 2023

Sam O'Connor,
Australian Competition & Consumer Commission
23 Marcus Clarke St
Canberra ACT 2601

By email: sam.oconnor@accc.gov.au

Dear Mr O'Connor,

Application For Authorisation AA1000646 – Townsville and FNQ Ports

1 Executive summary

We represent Pacific Tug Group (**Pacific Tug**), a family-owned supplier of tug and towage services on the Eastern Seaboard of Australia with a fleet of 26 vessels including barges and transfer vessels as well as tugs. Pacific Tug is based in Brisbane. Pacific Tug currently provides harbour towage services in 4 ports across the Eastern Seaboard of Australia.

Pacific Tug's position is that, if the application is granted, it will certainly result in a substantial lessening of competition and poorer outcomes for consumers.

In summary, the application rests on outdated or unproven assumptions about the nature of competition if authorisation is not granted. In particular, the application is based on the assumption that without a long term exclusive licence there would be insufficient commercial incentive for towage services to compete to provide services. This is wrong. Pacific Tug is an example of a towage service that seeks to compete to provide towage services at Townsville and FNQ Ports. It does not need an exclusive licence to do so. On the contrary, an exclusive licence will only serve to inhibit the competition that towage service providers such as Pacific Tug seek to provide.

It appears that the application is based on the notion that Ports are a natural monopoly. Innovations mean that this is no longer the case. Pacific Tug has developed a low cost, nimble business model that allows it to operate without the benefits of exclusivity. Pacific Tug is not the only small towage service provider that is seeking to disrupt the larger incumbents. As the ACCC is aware, the Federal Court has recently given judgment in a case involving the attempted entry by Engage

Marine into Tasmanian ports: *ACCC v Tasmanian Ports Corporation Pty Ltd* [2021] FCA 482. The ACCC must take into account these changes in market-dynamics.

If the application is granted, not only will the relevant markets be deprived of the benefits of this competition for an extended period of 13 years, the Ports and users of towage services will be faced with a service provider that has, in the words of the applicants, "considerable countervailing power". This countervailing power, combined with the absence of any threat of entry by a rival, is likely to lead increased prices, or poorer service, or both.

The applicants submit that towage service providers have an opportunity to compete for the market. However, in circumstances where service providers, such as Pacific Tug, wish to compete in the market, there is no justification for granting the authorisation sought.

Similarly, the applicants seek authorisation to be able to run a joint tender process across multiple ports so that towage providers have a greater commercial incentive to bid. Again, however, service providers such as Pacific Tug do not need this aggregated demand to compete. Indeed, if demand is allowed to be aggregated in this way, it is likely to be the detriment of smaller participants such as Pacific Tug who will be unable to offer a service that meets the whole demand, and competition will be restricted to the two largest market participants (Svitzer and Smit Lamnalco).

Much of the application seeks to justify the conduct on the basis that it will assist towage service providers. When a towage service provider such as Pacific Tug says it does not need - or want - this arrangement, that should cause the ACCC to question seriously the claimed benefits of the application.

We expand on these points below.

2 Reduction in competition and public detriment

The effect of the application (if granted) would be to remove all competition for the provision of harbour towage services within four neighbouring ports for (at least) 10 years and possibly 12 years, locking towage to the Port Operator. Plainly, that is a significant step and one that should not be taken without a high-degree of confidence that it will produce a better competitive and consumer outcome than refusing the application.

However, the application fails to meaningfully engage with fundamental concepts and assumptions, such that the ACCC could not obtain the high-degree of confidence necessary to conclude that granting the application would promote a better competitive outcome than refusing the application. To the extent that the application submits that the authorisation would promote competition, the reasons provided are unconvincing.

2.1 Pacific Tug wants to compete

Firstly, it should be stressed that Pacific Tug is able to compete in the relevant ports, and should be considered a likely competitor in a future without the authorised conduct. The applicants submit that the commercial realities of operating in these ports (capital costs etc.) are such that the ports are natural monopolies. For reasons addressed below, that submission should be rejected. However, even assuming those barriers to multiple towage providers, it remains the case that Pacific Tug is undeterred and wants to compete in the relevant ports.

Pacific Tug is an agile operator that moves tugs between ports depending on demand. It utilises a range of infrastructure to operate across multiple ports, such as berths, swing moorings and anchoring, where necessary.

For example, Pacific Tug has successfully operated in Port Eden, NSW since 2016, where it competes with a much larger operator, Svitzer. At Port Eden, Pacific Tug utilises a combination of non-exclusive berths to provide competition to Svitzer. Last year Pacific Tug completed 25 shipping movements, which represented over half of the market share in Port Eden. Pacific Tug's ability to win half of the movements in the face of a much larger competitor is a testament to its ability to compete and the viability of its nimble business model in other ports.

There are other operators with similar business models, such as Mackenzie Marine, a 4th generation WA provider and also Engage Marine. These two companies, together with Pacific Tug, offer an alternative to the duopoly of Svitzer and Smit Lamnalco in the Australian market. Local and Australian family companies should not be unfairly constrained in favour of multinationals.

If the application is granted, it is highly likely that operators like Pacific Tug will be excluded from operating in the relevant ports. In circumstances where Pacific Tug (and presumably other operators) wishes to compete, and has a demonstrated business model that would allow it to do so, the ACCC should not lightly prevent them from doing so. This is particularly so when other models, such as non-exclusive licensing, would allow Pacific Tug (and others) to compete, while ensuring that towage providers meet a minimum set of standards, so as to mitigate the risk of poor consumer outcomes.

2.2 Assumption of natural monopolies / failure to define market

The thrust of the applicants' submission is that granting exclusive licenses will promote competition *for* the market to provide services in the relevant ports in circumstances where there would not otherwise be competition within those ports. This is made plain in section 10.2, where it is submitted that:

> *Consistent with the ACCC's statement of reasons in respect of the Previous Notification, while granting an exclusive licence would ordinarily reduce competitive pressure to innovate and pass through benefits from cost reductions during the period of the licence, the natural monopolistic characteristics of the towage industry means that the opposite is true…*

This submission rests on the critical assumption that ports are natural monopolies. For the following reasons, that assumption is wrong.

In *Stirling Harbour Services Pty Ltd v Bunbury Port Authority* 2000] FCA 38 (***Bunbury***), French J (as his Honour then was) identified a number of factors that bore upon whether a port was a natural monopoly including: (i) the cost of entry to and operation in the relevant ports;[1] and (ii) whether there is a cluster of ports close to one another such that there is a single geographic market that is capable of supporting more than one operator.[2]

In this case, both of these factors point away from characterising the relevant ports as natural monopolies.

In relation to the first factor, Pacific Tug's business model (as described above) demonstrates that the costs of entering and operating in ports are not prohibitive. For example, it is not the case that service providers require certainty of customers in order to make the necessary financial investments to compete.

In relation to the second factor, the relevant ports are scattered located along a stretch of approximately 300 kilometres of coastline. Those distances are not significant and service providers could readily move between the ports. The application recognises this by its proposal to group multiple ports under single licences. In contrast to the situation in *Bunbury*, the relevant ports are not isolated such that they require a dedicated towage provider.

Further, the applicants themselves note that a range of "physical characteristics of each port determine its towage service needs" such as "[w]eather conditions, ship size and design, port authority regulations, pilotage guidelines and the needs of shipping lines". However, despite identifying these range of variables, no meaningful attempt is made to explain why, in respect of these ports, those factors point towards the conclusion that the ports are natural monopolies.

Moreover, the submission that ports are natural monopolies also rests, at least in part, on the findings of a Productivity Commission report from 2002: see footnote 9 on page 17. That report is now over 20 years' old. A fresh appraisal of the towage market is required in order to account for the business practices of smaller, agile operators, such as Pacific Tug.

In a similar vein, the applicants have not attempted any meaningful determination of the relevant markets for the assessment of competitive effects. The identification of markets is the essential first step in the assessment of likely competitive outcomes: *Re Queensland Co-operative Milling Association Ltd; Re Defiance Holdings Ltd* (1976) 25 FLR 169.

[1] *Bunbury*, [50].
[2] *Bunbury*, [52].

For example, there is no updated economic modelling of the size of a market which might sustain more than one operator; no discussion of the impact of adjacent ports and the potential for smaller, more agile providers (like Pacific Tug) to switch assets between ports depending on predictable patterns of demand. Nor have the applicants considered, as would be appropriate given the proposed length of the exclusive licence regime, how the market might change over the period of the proposed exclusive licenses.

2.3 Exclusive licence is redundant if ports are natural monopolies

Pacific Tug's primary position is that the relevant ports are not natural monopolies and that it would be anti-competitive to countenance a monopoly in those circumstances. However, if it is assumed that the relevant ports are natural monopolies, that very fact renders the proposed exclusive licence unnecessary.

The applicants' submit that, even in ports where non-exclusive licences are issued that "[t]owage services are generally provided by a single Service Provider even where there is a non-exclusive licensing arrangement in place…" If this is the case, then it emphasises that there is no need for exclusive licencing.

Further, the fact that towage services are provided by a single Service Provider even where there is a non-exclusive licensing arrangement in place does not demonstrate that Ports are natural monopolies. The ACCC would need to look more closely at the tender processes run for those arrangements. Pacific Tug has direct experience in one instance. In 2021, North Queensland Bulk Ports issued a tender. North Queensland Bulk Ports issued a single licence, notwithstanding that there were several compliant tender bids, including from Pacific Tug. The fact of several compliant bid for a non-exclusive licence supports Pacific Tug's contention that ports should not be considered natural monopolies, that require exclusive licences to attract competition.

2.4 Proposed exclusive licence length and conditions

Pacific Tug accepts that, in circumstances where a natural monopoly exists (which is a matter that must be proven, not assumed) it is acceptable to use a tender process to create competition *for* a market (i.e. a port) rather than *within* a port. However, that general position is subject to the requirement that the tender process and licensing regime must not itself be anti-competitive.

In this case, the proposed exclusive licence length is, at least, 10 years and possibly up to 12 years. On any view, that is a significant period of time and, for the following reasons, is anti-competitive:

- Firstly, the proposed minimum term (10 years) is twice as long as the current minimum licence in effect at the ports. It is said that the extended term will "facilitate a competitive tender process and attract more innovative solutions". Those are bare assertions. Further, there is reason to think that a

longer term would tend to stifle innovation, as a licence holder would have a reduced competitive incentive to innovate over the period of the licence.

- Secondly, the rationale that a towage service provider needs to recoup their capital investment is overstated and unsubstantiated. It is said that capital investment in the region of $7.5 million per tug is required and "total investment of $30 million would not be unreasonable to supply towage services to the ports of Cairns and Mourilyan". No explanation is provided as to the investments required at Cairns and Mourilyan nor why, assuming that such investment is required, why shorter licence terms could not be adopted for Townsville and Lucinda. Further, it should be noted that these figures are not large. At the Port of Lucinda, Svitzer's published rates are a mobilisation charge of $8915 per tug, and then an amount ranging from $20,000 to $35,000 per vessel movement. Given the ability to generate such revenues, an investment of $7.5 million, or even $30 million, is not so large as to justify competitive protection for the operator.

- Thirdly, and relatedly, this rationale for the licence length (i.e. the need to recoup capital costs) fails to recognise that operators, such as Pacific Tug, are utilising cheaper business models. The investment required to "swing in" to a port with a vessel which intends to "swing out" again is inevitably going to be much less than $7.5 million dollars.

- Fourthly, the applicants have not provided any indication of whether and, if so, what key performance indicators would be applied under the licences. Given the proposed length of licence, it will be necessary for the licence to contain key performance indicators and conditions that maintain competitive pressure on the licensee throughout the term of the licence. At this stage, the ACCC cannot be comfortable that will occur.

Finally, the current application gives no details about how a tender process would be conducted, and what measures would be proposed to ensure that the process is conducted fairly. Under such circumstances, and absent such detail, the approval ought not to be granted.

2.5 Additional market participants / reduced barriers to smaller providers

At section 3.4 of the application, the applicants submit that the proposed conduct will "provide the potential for aggregated demand for towage services so as to attract a wider possible group of potential service providers." That submission should not be accepted.

Firstly, it has not been demonstrated that the absence of aggregated demand has presented, or contributed towards, a barrier to entry for new market participants.

Secondly, and more importantly, the aggregation of demand (and the issuing of exclusive licences to service that demand) will actually reduce the number of potential service providers. This is because only larger service providers will have the capacity to (exclusively) service that aggregated demand. The proposal will almost

certainly result in two companies – Svitzer and Smit Lamnalco – being the only two market participants in the market.

Furthermore, there is no need for a towage provider to be able to service all vessels in a port (or broader geographical port). The market for tug and towage services is infinitely severable. For example, there is no reason why, if eight vessels arrive in Port of Cairns on a particular day, four of them might not engage one company, three of them a second company, and one of them engage a third. Each vessel movement is completely independent on each other.

2.6 Anti-competitive protection of market share

In section 10.1(b) of the application, the applicants submit that, because the ACCC previously considered that economies of scale would be exhausted by a service provider at 8000 movements a year, each market should remain, or will remain, a monopoly until there are more than 8000 movements per year. That submission should not be accepted. Pacific Tug operates in open competition in Port Eden, where it completes 25 ship movements per annum. This is comparable to the number of movements that takes place in half of the ports that are the subject of this application. Thus, the submission that the volume of movements in the relevant ports would not entice competition should be rejected – Pacific Tug has competed profitably (in Port Eden) for comparable numbers of movements and would similarly compete in the ports that are the subject of this application.

Firstly, no operator in any market for any goods or services is entitled to have the market to themselves until they *exhaust* their economies of scale.

Secondly, this submission conflates the minimum required demand to sustain a new entrant with the figure at which economies of scale are exhausted by an incumbent service provider. These are not the same figure. For example, the business models of certain providers (such as Pacific Tug) may permit them to compete in certain markets despite providing a smaller number of movements. In this case, the key matter to be considered is whether there is a sufficient number of movements such that new entrants may compete in the market Pacific Tug operates in Eden, Bundaberg and Port Alma with volumes around 25 vessels per port per year. The fleet utilised varies in age and is both rotated between ports and replaced as the needs of the ports vary.

If the application is not granted, it will be for each non-exclusive licence holder to determine, in relation to each port, how much work they can obtain, and how much revenue they can obtain from that work, and then it will be for each non-exclusive licence holder to determine whether their business models support operation, or continued operation, in that market. These are typical business decisions that must be made by businesses operating in a range of competitive markets. No reason has been advanced that towage providers should be sheltered from such competitive pressures.

2.7 More efficient use of tugs

At section 9.1(c), it is submitted that by allowing for exclusive licences to cover more than one port, the efficiency of the use of the tugs will be increased. Pacific Tug accepts that a multi-port market definition would likely promote more efficient use of tugs.

However, what is not considered by the applicants (in this regard or more generally) is whether the outcome under the application would be more efficient than the outcome arising from a more competitive market. Indeed, this is the fundamental deficiency that permeates the application – no meaningful consideration is given to the counterfactual in which exclusive licences are not granted.

2.8 Costs of procurement

At section 9.1, it is generally submitted that a joint procurement process will deliver material cost savings to the applicants and prospective tenderers.

This submission ignores that there is a readily available alternative to a competitive tender process. Namely, the applicants could grant non-exclusive licences to towage providers that comply with conditions necessary to obtain a licence, such as proving that a prospective licensee has sufficient vessels and the personnel to provide the services safely and competently. That being the case, the cost of conducting a competitive procurement process would be avoided altogether.

2.9 Third line forcing

A corollary of exclusive licenses is that port users will be forced to acquire towage services from the exclusive licensees.

The application does not provide any explanation of what conditions would be imposed on the licensees to protect the users of towage services. For example, there is no explanation of pricing controls that would be placed on the exclusive licensees.

The dangers of this situation are further exacerbated by the fact that the relevant ports are not substitutable. For example, sugar and molasses can only be loaded in Mourilyan, and there is no way for transport providers to (for instance) select another port at which to be loaded.

3 Conclusion

This application asks the ACCC to make a number of fundamental assumptions about the relevant ports in order to justify a regime, exclusive licensing, which is recognised as being *prima facie* anti-competitive. Such assumptions include that the relevant ports are natural monopolies.

The application either fails entirely or meaningfully to attempt to prove the assumptions that the ACCC is asked to adopt. It is respectfully submitted that the

ACCC would be acting contrary to its statutory function if it granted the approval on the basis of the information contained in the application.

Little evidence has been put forward that a more "open" market in the relevant ports would produce poor outcomes for consumers. Rather, the thrust of the application is that other towage providers will not compete in the relevant ports unless they are guaranteed an exclusive licence.

However, Pacific Tug is willing and able to compete without an exclusive licence. It seeks an opportunity to do so. Pacific Tug is willing to stand or fall in any market on the basis of the efficiency and professionalism of its seafarers; the quality of its service; and the cost it charges. All Pacific Tug seeks is a level playing field. The current application would effectively shut out Pacific Tug, and similar operators, from providing services north of Gladstone, Qld.

All Australians who rely on the movement of goods and commodities through Australian ports – which means all Australians – will suffer if enterprises like Pacific Tug are forced from the market, and the market ultimately settles upon one or two players.

The current application must be refused.

Yours faithfully,
Pacific Maritime Lawyers

John Kavanagh
Principal Lawyer, Master Mariner