There are changes that should be made in the energy sector. But the big issues in energy reform are not about institutional arrangements. They are energy pricing, industry structure and retail contestability.

In telecommunications the government has strengthened current regulatory arrangements in a way that should help to promote competition in the industry.

Concerns have been expressed that regulatory error can deter investment by service providers. The presumption seems to be that regulators are going to be biased against regulated businesses. I am sceptical about the reviews, reports and submissions that start from this position. It is supported by neither economic literature nor regulatory experience. To share their concerns and to be convinced by such a case I would need to see solid evidence. There is in fact no evidence of an empirical kind in Australia to support any such case.

The picture I have painted here is mixed. There has been some progress but continued regulatory pressure will be needed for some time.

Australian shipping and best regulatory practice

Following is a summary of a speech given by Commission Chairman, Professor Allan Fels, to Shipping Australia Limited, 14 August 2002.

Professor Fels first discussed the importance of competition. As an example of the value of competition law in the shipping industry he then referred to the Commission action against the Maritime Union of Australia (MUA).

The Commission alleged that the MUA and a number of senior officials breached s. 45DB—the section that deals with boycotts affecting trade or commerce.

We alleged they unlawfully hindered and prevented—or made the attempt to hinder and prevent—vessels from sailing unless the owners/charterers agreed to use the MUA to clean vessels' holds. In effect, the ship did not sail unless it was cleaned by MUA workers. Both shipowners and other workers were subject to harassment and coercion, in breach of s. 60. Workers who considered releasing ships were called 'dogs', 'slimes' and 'scabs'.

These allegations were upheld. The Federal Court ordered the MUA pay penalties and costs totalling $210 000 for breaching the secondary boycott provisions of the Trade Practices Act. The court also made declarations that the union's conduct constituted undue harassment and coercion in breach of the Act.

The fact is that successful action under Part IV of the Act broke a racket that worked to the disadvantage of both shippers and exporters.

Shipping Australia and Part X

There has been a long standing concern by government about the lack of competition in parts of the maritime industries, the consequent lack of efficiency of these industries and the subsequent adverse impact on the Australian economy. In a broad sense these are the issues that have provided the basis for the Commission's involvement in the monitoring and oversight of prices charged by the container stevedoring and harbour towage industries.

For the liner shipping industry, however, the Commission's role is a little more complex and there are various issues that arise as a result of the Commission's engagement with the Part X regime.

Australia's approach to regulating liner shipping services is similar to that adopted in many other developed countries. Part X provides the legislative framework for shipping companies and their exporting customers to negotiate the terms and conditions for providing liner shipping services. Essentially, Part X gives concessions to providers of liner shipping services to allow them to behave in ways that otherwise would not be permitted under the Act. Liner shipping companies are given limited exemptions from trade practices laws to enter into cooperative arrangements in providing shipping services to Australian importers and exporters. Specifically, exemption is provided by applying s. 45 (arrangements restricting dealings or affecting competition) and s. 47 (which deals with exclusive dealing—exemption is not provided for third line forcing).

Part X does not provide exemptions from s. 46 (misuse of market power). The arrangements permitted under Part X include joint provision of services and agreements on capacity, service levels and prices charged. In return for these exemptions, some obligations and requirements on lines have been imposed. These include requirements to negotiate with shipper bodies, and register

agreements with the Department of Transport. Part X also includes provisions to enhance the countervailing power of shippers in their dealings with shipping lines.

The Commission's role under Part X is largely limited to investigating specific agreements with a view to recommending to the minister whether or not there may be grounds for deregistering the agreement and subjecting the lines to the provisions of the Act.

Until recently the Commission could investigate an agreement only after being asked to do so by either the minister or after receiving a complaint from shippers. However, amendments to Part X, introduced in 2000, allow the Commission to be more active in initiating investigations.

To deal with concerns about the operation of agreements that potentially cover much of the nation's trade, increased powers were provided to the minister and Commission—including the power to initiate an investigation with a public benefit test.

Such concerns are expected to arise only in exceptional circumstances, which were defined in the Second Reading Speech as being:

- an agreement that has the effect of giving its parties a substantial degree of market power
- when the conduct of those shipping lines has led to, or is likely to lead to, an unreasonable increase in freight rates or an unreasonable reduction in services
- when an agreement covers a substantial majority of shipping lines and capacity in a trade
- when the public benefit from the operation of the agreement is outweighed by an anti-competitive detriment.

To meet these new responsibilities under Part X the Commission is implementing an informal monitoring program. We are working to develop an awareness of factors likely to contribute to increased sea cargo freight rate rises—either in the form of rises in blue water freight rates, or in general tariff levels.

I would like to pass on my appreciation to Shipping Australia for their cooperation and assistance in providing information for this.

The Commission's attitude towards Part X is well known. The Commission does not consider that the arrangements permitted under Part X are appropriate for the liner shipping industry or indeed other sectors of the economy. Part X gives concessions to providers of liner shipping services not otherwise permissible under the Act.

It is sometimes argued, in justifying the retention of Part X, that it is warranted by the economics of the liner shipping services industry. The argument continues that it may not be possible for shipping lines to provide Australian exporters with shipping services of an adequate standard without allowing some level of coordination.

The conclusion is then drawn that blanket immunity from the anti-competitive provisions of the Act is needed. But there is no justification whatsoever in providing blanket immunity to all arrangements without a public benefit test. To do so would be to run the risk that arrangements would act against the interests of exporters and, more generally, against domestic producers and consumers.

My view is that the authorisation process is more appropriate for assessing claims for immunity. A move to apply the authorisation process to liner shipping is not intended to result in the dismantling of shipping conferences. Exemptions for most of the conduct prohibited by the Act can be provided through authorisations—if the conduct is likely to result in a benefit to the public that exceeds the associated detriment.

Thus, conduct involved in typical industry agreements (joint venture provisions, price fixing, income pooling, self regulatory schemes and collectives of users to achieve countervailing balance of power) can all be allowed under the authorisation process.

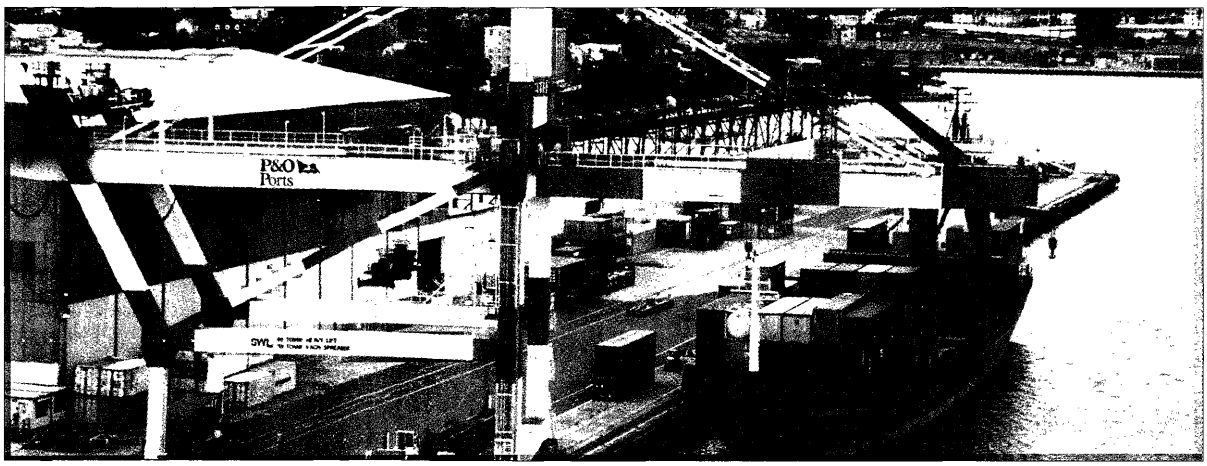
The relevant shipping companies would be required, like any other business, to demonstrate that benefits of the proposed arrangements offset the anti-competitive costs.

Future developments in container stevedoring monitoring

I would now like to move on to another important area of activity for the Commission, which is the oversight of prices in the container stevedoring industry.

The Commission monitors prices, costs and profits of container stevedoring operators in the ports of Adelaide, Brisbane, Burnie, Fremantle, Melbourne and Sydney under s. 27A of the Prices Surveillance Act.

This monitoring informs the Government and wider community about the progress of waterfront reform at Australia's major container terminals. It also



informs the community about the absorption of the stevedoring levy by the stevedores.

As part of its monitoring role the Commission uses revenue and cost information from stevedores to calculate a proxy price at the industry level, that is, average revenue per TEU (twenty-foot equivalent unit). This information is published in the Commission's *Container stevedoring monitoring report*.

However, the Commission has heard the concerns of users of the report, including Shipping Australia, that it should also be providing information on a trend away from twenty-foot containers (representing one TEU) and towards forty-foot containers (representing two TEUs).

The reason for this concern is that, as stevedoring charges per TEU are lower for forty-foot containers than for twenty-foot containers, a trend to forty-foot containers may be contributing to a lowering of average stevedoring revenue on a per TEU basis.

The Commission has therefore sought additional revenue and container volume information from stevedores. We constructed a new time series (from July 2001) to provide information on average revenue per TEU on both twenty-foot and forty-foot containers. This allows the Commission to analyse the effect of the increased use of forty-foot containers on movements in total average revenue per TEU over time more effectively. We can now also compare the stevedoring price trends of both container types.

The Commission is aware that there are several factors that need to be taken into account when comparing differences in average revenue generated from twenty and forty-foot containers. In particular the Commission has information that indicates there are higher costs in handling forty-foot containers. In addition it has also been claimed that the expected mix of twenty-foot and forty-foot containers will be a significant factor for stevedoring companies when they are determining the stevedoring rate to be charged to a shipping line.

Users of the Commission's *Container stevedoring monitoring report* also need to recognise that even with this additional information, average unit stevedoring rates only approximate actual rates and that movements in average rates may not necessarily reflect those in specific stevedoring rates.

Future regulation of harbour towage services

The Commission's role in the harbour towage industry dates back to 1991—when harbour towage services were first declared for prices oversight purposes under the Prices Surveillance Act. Under this Act the Commission is charged with the responsibility of regulating price setting by harbour towage operators in Sydney (Port Botany and Port Jackson), Melbourne, Brisbane, Adelaide, Fremantle and Newcastle.

Given industry rationalisation, the declaration now applies solely to the towage subsidiary companies of Adsteam Marine.

I feel I should make some brief comment on the decision by the Commission in February this year to object under the Prices Surveillance Act to price rises sought by Adsteam for harbour towage services. Adsteam subsequently chose to ignore the Commission's decision and implemented all its proposed increases.

Under the Prices Surveillance Act the Commission can object to, but can not prevent price increases of 'declared services'. The Commission also has to assess, among other things, whether a 'declared' company may be using its monopoly position to set monopoly prices.

The Commission decided that the price increases proposed by Adsteam, which ranged between 11 per cent (in Brisbane) and 27 per cent (in Port Jackson), would have generated excessive rates of return. (I note that after Adsteam's decision to implement price increases, a new harbour towage firm, Australian Maritime Services, has entered the Port of Melbourne and has announced plans to operate in other Australian ports.)

The Commission therefore welcomes the current inquiry into economic regulation of harbour towage by the Productivity Commission. We believe it to be timely.

I believe the declaration needs to be reviewed publicly and transparently before it expires in September 2002, and that harbour towage industry structure and performance should also be investigated in a thorough and detailed way.

The Commission argued to the Productivity Commission that the regulation of prices set by towage operators in declared major ports should be continued.

This is on the grounds that the Australian towage market is characterised as a natural monopoly, with single providers in all declared ports (until the recent entry of Australian Maritime Services into the Port of Melbourne). There is very little scope for inter-port competition, weak contestability and little opportunity for users to substitute away from towage usage. In technical words the own price demand for towage services is inelastic.

There is little evidence to suggest that the single towage operator, Adsteam Marine, which operates in 32 ports around Australia, is subject to any competitive discipline on pricing—either from existing competitors or from potential entrants. This is a market therefore where the incumbent wields considerable power.

Because of this the Commission believes that if there is a demonstrated case for economic regulation of towage, then we should be able to effectively implement decisions.

On two separate occasions Adsteam Marine has increased its towage rates—in spite of the Commission's assessments that rises were not justified. This represents not only ineffective regulation of towage rates, but also imposes costs both upon the company (Adsteam) and the regulator (Commission). This is because, under the Prices Surveillance Act, the company is obliged to submit a price notification for the Commission to assess.

These events demonstrate the weakness of the Prices Surveillance Act, which the Commission has argued should also be strengthened as a regulatory tool.

In general, the Commission supports the policy directions that have been identified in the Productivity Commission's position paper on harbour towage services.

However, the Commission has argued that before competitive tendering is widely adopted the potential costs and risks associated with this solution need to be examined more closely. The Commission also considers that the Productivity Commission should explore other regulatory safeguards to ensure that exclusive licensing operates effectively in practice. In particular, the Commission is concerned that port authorities need sufficient incentive to implement a tender process that will provide users of harbour towage services, such as shipping lines, quality at the right price.

The Commission has also sought clarification from the Productivity Commission on two other matters. The Productivity Commission has made a finding 'that towage prices in some Australian ports have been above efficient levels but the margin has not been large'.

We take a different view. In general, margins in the harbour towage industry as they relate to declared ports have been large and above the levels that would be expected in competitive industries operating under similar levels of risk.

The Productivity Commission has also recommended limited monitoring of prices by the Commission for a three-year period. We do not consider monitoring an optimal regulatory option in this industry. However, as a second-best option, the Commission considers monitoring could be a more effective regulatory tool than the current price notification regime.

Unfortunately, the Productivity Commission position paper does not provide sufficient detail for the Commission to assess whether the Productivity Commission's proposed monitoring regime would be effective.

On a final note on price monitoring, the Commission believes that mechanisms should be established to ascertain if monitoring should continue beyond the proposed three-year timeframe that is currently proposed by the Productivity Commission.

Review of the competition provisions of the Trade Practices Act

Effects test

The Commission has proposed that an effects test in s. 46 be introduced. This is something that I see Shipping Australia opposes.

'Effects' has long been, and still is, the normal, uncontroversial test in other countries.

I believe that if a firm with substantial market power takes advantage of that power and causes anti-competitive effects—or damages competition—then such behaviour should be prohibited. It is difficult to see why the section of the Act should be limited to conduct that has an anti-competitive purpose. Overseas jurisdictions in Europe and in the United States, generally use an effects test. The rest of the Act is concerned with the purpose or effect of behaviour.

Section 46 gives legitimate protection to new entrants into industries dominated by major businesses. Moreover, in my view, such protection is legitimate and appropriate since it is limited to anti-competitive behaviour.

What are the arguments against this proposal? The first is that the introduction of an effects test will dull competition.

Nearly everyone accepts that the law should not be taken too far or it will diminish competition rather than protect it.

Section 46 is written with ample safeguards to protect legitimate competitive conduct. Indeed, it has been designed to avoid going too far. For any breach of s. 46 to be substantiated in court, it has to be proved that a firm has substantial market power.

Importantly, it has to be shown in court that the firm has 'taken advantage' of its power—a requirement that distinguishes between legitimate and illegitimate anti-competitive behaviour. Finally, the proscribed behaviour must be shown to have occurred. Safeguards therefore are already embedded in s. 46.

Is hard and aggressive competition a breach of s. 46? Generally not—the courts have usually focused on the effect on competition, not on competitors. Even if competition causes damage to one firm, through lost sales and profit (even if this results, in some sense, in less competition thereafter) this is generally not in itself an issue under the Act.

If this is the result of the action of a firm that by its own effort, increased efficiency and reduced costs, and if the behaviour was of the normal commercial kind that would occur in a competitive market, there is no problem. Moreover, this would generally be the case whether or not there is a purpose test, or an effects test.

It is only when business oversteps the mark of normal tough competition that there is a problem. If the law incorporated an effects test, the key economic issue of whether or not the behaviour was anti-competitive would be considered in the context of the meaning of the words 'take advantage'—not in the context of the impact of the introduction of the words concerning effect.