PRICEWATERHOUSECOOPERS

Productivity Commission

Inquiry into Economic Regulation of Harbour Towage and Related Services

Public Submission by PricewaterhouseCoopers

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Len Gainsford
Partner, Tax and Legal Services
National Leader on Pricing and Competition Policy

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1 Introduction

1.1 Identification

This submission is provided by PricewaterhouseCoopers (PwC) in response to the Productivity Commission's (the Commission) Position Paper on Economic Regulation of Harbour Towage and Related Services. PwC is the world's largest professional advisory firm. We operate in 150 countries and employ over 150,000 people worldwide.

The Commission's 6 June 2002 Circular TOWC4 sets out requirements for interested parties. At Attachment A to that Circular and faxed to the Commission on 18 June 2002, we have advised that Len Gainsford, Partner, Tax and Legal Services and PwC National Leader on Pricing and Competition Policy will present our submission at public hearings in Sydney on Thursday, 11 July 2002. Contact details are as follows:

Len Gainsford
Partner
PricewaterhouseCoopers
215 Spring Street
MELBOURNE VIC 3000

Phone: (613) 8603 3664
Mobile: 0418 978 449
Email: len.gainsford@au.pwcglobal.com

1.2 Background

Since declaration of harbour towage in 1991 under the *Prices Surveillance Act* 1983 ("the Act"), PwC and its predecessor firm, Coopers & Lybrand, have assisted Howard Smith Towage, Adsteam Marine, Brambles Industries, P&O Towage and Shipping Australia in respect of notifications, and at a public inquiry conducted by the Prices Surveillance Authority (PSA), which is the predecessor to the Australian Competition and Consumer Commission (ACCC). There are some issues which emerge from the ACCC's processes and these are addressed in our submission. We are unable to provide details which may be judged "commercially sensitive" or "client confidential" at this Inquiry. Nonetheless, in addressing the Government's 20 February 2002 Terms of Reference, we seek to make a worthwhile contribution to the Commission's consideration of regulation for this sector. There are a number of preliminary recommendations, findings and requests for information in the Position Paper at pages XXXIX to XLII. We are unable to comment on all of them, concentrating instead on preliminary findings 7.1 to 7.3. These findings focus upon an assessment of the price notifications for harbour towage services.

Essentially, we find it difficult to endorse preliminary findings 7.1 to 7.3. Primarily and based on our experience, we do not sufficiently understand the reasons underlying preliminary recommendation 3, for a removal from declaration. In the absence of good argument to the contrary, there should be *no* removal from declaration. We also question whether, instead of failure in the *system* of price notifications, there has been failure in the *administration* of it, by the regulator.

2 Request

At this Inquiry, we note that the Commission has come to a preliminary view (Recommendation 3) that:

> "Declaration of harbour towage services at the ports of Melbourne, Sydney (Port Botany and Port Jackson), Newcastle, Brisbane, Fremantle and Adelaide under S. 21 of the *Prices Surveillance Act* 1983 should not be renewed when the current declaration expires on 19 September 2002."

We invite the Commission to reconsider its view, such that declaration of harbour towage continues for 3 years from 19 September 2002, instead of 3 years of price monitoring suggested by the Commission at Recommendation 4. We note that participants such as Fremantle Port Authority (FPA), CSR Shipping and the Sea Freight Council of Australia have argued in favour of continuing the current declaration of harbour towage services under the Act. The FPA has also argued for an extension of the declaration to include Outer Harbour Fremantle.

3 Reasons for Request

3.1 Public Benefits from the Act

The Act has been in force for almost 20 years, having been created at a time when prices surveillance was required under the Hawke Government's Wages Accord. Successive governments have decided to retain this piece of legislation, notwithstanding the Commission's "*Review of the Prices Surveillance Act 1983*" (2001) findings. The Act contains notification requirements for declared entities. It also has price monitoring and public inquiry provisions which are not present in the ACCC administered *Trade Practices Act 1974* (TPA). It could be argued that the Act serves a useful public purpose, in allowing the ACCC to scrutinise both price increases and changes in terms and conditions of sale, such as the introduction of rebates. Historically, declarations have occurred in relatively concentrated industries. The ultimate objective of any regulatory intervention or policy reform should be to promote the national interest (Position Paper, Appendix B).

Powers of the Minister (*Act*, S. 18) requiring the ACCC to hold an inquiry, may also serve a useful purpose for the public to see a matter being dealt with and reported on. On this occasion, the Minister chose not to refer Adsteam's 30 January 2002 price notification to the ACCC for public inquiry. Provisions under S. 24 of the Act allow prices to be "frozen", depending on whether particular persons are named in an Inquiry notice. Members of the public are also able to discover details of declared entities, declared goods or services, the basis for notifications and other details from ACCC records and reports. Importantly, under S. 17(3) of the Act, the ACCC is required to have particular regard, *inter alia*, to "the influence of profitability

on investment" and "(b) the need to discourage a person who is in a position substantially to influence a market for goods or services from taking advantage of that power in setting prices."

3.2 Notification Procedures

Under section 1.2 (Scope of the Inquiry) to the Commission's March 2002 Issues Paper (page 5), it was said "the Commission will not be addressing directly the question whether the price increases are justified". Yet, at page 106 of the Position Paper, the Commission states that "in submitting a price notification, the onus is on the declared company to justify the case for the price increase". From S. 22 of the Act, it is not clear that a declared entity *has* an onus to justify the case. What is clear from S. 22(2)(b) is that there *is* an onus on the ACCC to respond to a S. 22(2)(a) notice from a declared entity. The ACCC's "Draft Statement of Regulatory Approach to Price Notifications" (1998) may assist in understanding how the ACCC approaches its responsibilities under S. 22(2)(b). In the absence of a S. 20 Ministerial Direction, it is difficult to ascertain the legislative basis for the "efficiency of the cost base" or "reasonableness of the rate of return" approaches mentioned at page 107 of the Position Paper. PwC is not aware of any judicial interpretation which might assist the ACCC's discharge of responsibilities under S. 22 of the Act. PwC is aware that under the S. 20 Ministerial "Unit Cost Direction", prices should not generally increase at a rate which exceeds movements in unit costs.

3.3 Notifications by Harbour Towage Operators

In the Commission's chronology of notifications by declared entities, (pages 108-110), what is not explained are the inabilities of the

regulator to deal with aggregated information or information not in an "acceptable" format. This is referred to as "insufficient information to allow the PSA to come to a decision" (Box 7.1). In addition, with Waratah Towage's 1997 notifications (page 109), it was said that the ACCC "was not convinced that the proposed increases were justified". As the Act contemplates that the regulator can only offer non objection under S. 22(2)(b)(ii), or non objection under S. 22(2)(b)(iii) at a price lower than the proposed price, it is difficult to discover the legislative basis for where the ACCC has a right to be convinced. In the past, notifications have been withdrawn after pressure from the regulator. The regulator can rightfully object to a proposed increase if it feels that there is insufficient time, or for any other reason, prior to 21 days having elapsed. The Act does not require the regulator to give reasons for its decisions.

In 2001, Adsteam acquired Howard Smith Towage from Howard Smith Limited. We understand that the ACCC previously considered this under S. 50 TPA and other mergers and asset sales matters linked to Wesfarmers Limited's acquisition of Howard Smith Limited. It is not known whether the Minister under S. 21 of the Act required an updating of the declared person(s) as a result of these mergers and asset sales to Adsteam Marine Limited. The following entities from Attachment A to Adsteam's 30 January 2002 prices notification are noted:

Port	Entity	Declared	Wholly Owned Sub. Of Adsteam Marine Ltd
Adelaide	Adsteam Towage Pty Ltd	No	Yes
Brisbane	Queensland Tug & Salvage Co. Pty Ltd	Yes	Yes
Melbourne	Adsteam Towage Holdings Pty Ltd	No	Yes
Sydney - Port Botany	Waratah Towage Pty Ltd	Yes	Yes
Sydney - Port Jackson	Waratah Towage Pty Ltd	Yes	Yes

3.4 Regulation and Promotion of Efficient Pricing

Regulation can be seen as a surrogate for the pressure that competitive forces would exert to deliver economic efficiency, and, in effect, to mimic the market. As competition strengthens (*Ypsilanti and Xavier*, 1998:645), governments could be expected to lessen regulation. This is based on the view that competition is typically better than regulation because it encourages a firm to allocate resources more efficiently and to experiment in creative and flexible ways to provide new services and entice customers into preferring its services.

An important question is whether declaration under the Act has provided a surrogate for the pressures that competitive forces would otherwise exert. As the Commission points out in Chapter 6, although barriers to entry at particular ports are not so high as to be prohibitive (due mainly to the mobility of tugs), incumbents probably still earn a moderate margin over "efficient" average costs. The ACCC at page 21 to its submission concedes (in the words of the Commission) that there is some evidence of notification having restricted price increases. The factors limiting the promotion of efficient pricing

listed by the Commission (page 112) indicate regulator failure and not notification system failure.

The Commission (1996:146) has found that irrespective of their institutions or legal frameworks, many countries are experiencing problems with their regulatory activities. The Commission goes on to list:

(a) inflexible regulations which often focus on fixing existing problems and are not adaptable to new situations;

(b) rapid growth in regulation, much of which is not subject to consistent and objective assessment prior to implementation; and

(c) the challenge of balancing a sense of being "over regulated" (or inappropriately regulated) with the support of many citizens for regulations which achieve certain economic and social outcomes.

Whether such difficulties extend to regulatory failure by the ACCC may be a question of degree. The OECD (2000:72) refers to the degree of trust between regulatees and regulators. If regulatees feel that regulators treat them as untrustworthy, then defiance and resistance build up so that inefficiency and non-compliance both increase. This can lead to regulatory failure.

Under conditions of regulatory failure, the introduction of "pre-notification" procedures by the ACCC (Position Paper, page 114) is unlikely to improve the regulator's "snapshot" understanding of industry issues. With issues such as joint and common costs and

"bulking" of price increases, coupled with "infrequent assessment of harbour towage prices" (page 112), it is not surprising that the regulator struggles. In addition, the "lack of regulatory teeth" (page 115) apparently makes it difficult for the ACCC to enforce its decisions. The law however still permits objection by the ACCC and the Minister is able to call a public inquiry and significantly, freeze prices.

3.5 Best Practice Principles for Administering Prices Oversight

The Commission has found that the ACCC appears to have undertaken public consultation on notifications in a transparent manner (page 118). In spite of concerns raised by Adsteam about the risks of commercially sensitive information being released in the consultative process, S. 33(b) of the Act permits the ACCC to disclose relevant information, if the regulator is of the opinion that disclosure is necessary in the public interest.

On accountability, the Commission has found (page 120) that the process (of reviews) may have been weakened by having the regulator undertake reviews of its own decisions and processes. While there is recourse to the Courts (for instance, under the *Administrative Decisions (Judicial Review) Act* 1977), and agencies such as the Commonwealth Ombudsman, there is no real evidence of such external scrutiny being applied.

With timeliness, the Commission recites the legal provisions and describes how parties have administrative procedures available to them. Compared with price notifications 10 years ago, there are now

greater delays (and perhaps higher compliance costs) due to the extra time the regulator takes in analysis and in reaching a decision. This is counter-intuitive to the reduction in the number of declarations, following the PSA's 1995 general review. On compliance costs, the Commission has found (page 122) that "these costs are not insignificant and would seem to exceed the benefits."

4 Conclusions

In this submission, we do not believe that there are sufficient reasons for a September 2002 removal of Adsteam Marine Limited and its various entities from declaration under the Act. Rather than evidence of failure in the system of price notifications, we suggest that there has been failure in the administration of it, by the regulator. It is incorrect to blame the system itself or the law that creates it.

With continuation of the declaration, administrative improvements can be made, without resorting to major amendments to the Act. Such administrative improvements include compelling the regulator to dispense with its "pre-notification" process and provide quicker decisions under S. 22 of the Act. Failure to do so should attract scrutiny from an appropriate Commonwealth agency such as the Ombudsman or the Auditor General. The ACCC should be required to provide details of outside scrutiny in its Annual Report to Parliament.

5 References

Organisation for Economic Cooperation and Development (2000) "Reducing the Risk of Policy Failure: Challenges for Regulatory Compliance"

Productivity Commission (1996) "Stocktake of Progress in Microeconomic Reform" Australian Government Publishing Service, Canberra

Ypsilanti, D. and Xavier, P. (1998) "Towards Next Generation Regulation" Telecommunications Policy, Vol. 22, No. 8