NET SEA FREIGHT • TASMANIA P/L
'The Logistics Administrative Specialist'

16 June 2006

Mr Andrew Irwin
Australian Government
Productivity Commission
PO Box 80
Belconnen ACT 2616

Ref SJCR 114/06

Submission to the Inquiry into the Subsidisation of Containerised and Bulk Shipping between the Mainland and Tasmania

Dear Mr Irwin

Attached to this covering letter is a submission to the Productivity Commission's Review of the Tasmanian Freight Equalisation Scheme (TFES). The submission concentrates on economic and social factors in addressing points contained within the Issues Paper.

Net Sea Freight - Tasmania Pty Ltd is a freight administration company. A range of services is offered to its clients; from obtaining a simple market freight quote to the provision of comprehensive logistic management reports. From a small beginning in 1992 the company incorporated in 2002 and now services over 100 firms affected by TFES. Many of those firms have been consulted in the preparation of this submission, on whose behalf it is made.

Their unanimous views include that the present system works well, it assists intended recipients, and that the independent assessment process of claim evaluation be retained. It is a commonly held view that TFES forms a relationship between shippers and the Commonwealth Government in which shipping companies and freight forwarders have no place.

It is the strong view of our shipping firm clients that shipping companies should not have freight assistance paid directly to them, and that shipping companies not be the only proclaimer of the costs of shipping. It is further considered that freight forwarders are better positioned than shipping companies to accurately identify the costs of shipping.

Southbound shippers who are also the final users of eligible goods, state a preference for having their freight assistance claims managed in the same manner as this firm's northbound shipper clients.

ABN 97069743264 • ACN 069743264 • 20 BURNS STREET, LAUNCESTON, TASMANIA 7250 • P - (03) 6326 4679 • F - (03) 6326 6882 • E - NSF@netseafreight.com.au

Increased efficiency and potential fraud reduction can both be assisted by recognising a firm's area of competency in such a way that adds to the bargaining position of shippers.

We will be pleased to expand upon views raised in this submission, should the requirement arise.

Yours sincerely

SJC Ralph
State Manager
Net Sea Freight – Tasmania

T: 03 6326 9555
M: 0427 246 469
E: stuart.ralph@netseafreight.com.au

Net Sea Freight – Tasmania Pty Ltd

Submission to the Inquiry into the Subsidisation of Containerised and Bulk Shipping between the Mainland and Tasmania

NET SEA FREIGHT
TASMANIA P/L
'The Logistics Administrative Specialist'

Authors:

Fred Ralph RFD, BBus – 03 6326 6860
Brian East BCom, BEc (Hons), MBA, Dip Ed – 03 6344 4927
Stuart Ralph BCom – 03 6326 9555

16 June 2006

Net Sea Freight – Tasmania Pty Ltd

Submission to the Inquiry into the Subsidisation of Containerised and Bulk Shipping between the Mainland and Tasmania

EXECUTIVE SUMMARY

1. The purpose of this submission is to address the case for continuance of assistance by the Tasmanian Freight Equalisation Scheme (TFES) to shippers of eligible goods to and from Tasmania and to examine the procedures of the present assistance system.

2. The submission proposes economic and social justifications for such assistance. It discusses the processes involved in shipping a typical consignment from Tasmania and attempts to highlight the sources of costs of this activity and cost disadvantages in comparison with land transport.

3. The administration of the current assistance arrangements is reviewed with suggestions for improvement for consideration by the Productivity Commission. A strong recommendation of this submission is that the present manner of assessing and paying subsidies be retained; that is to follow the precedents established by conclusions of previous reviews, whereby shippers should be direct recipients of the assistance.

4. The submission highlights several issues which it is felt are worthy of specific investigation by the Commission, notably including where the present Scheme has anomalies which preclude assistance being paid, either totally or in part.

5. Parameters which are instrumental in the determination of assistance payments are considered in the context of their current validity, having been initially set eight years ago. There is a suggestion that three parameters are due for revision, particularly the intermodal cost allowance.

6. Finally, the submission briefly comments upon several matters raised by the Productivity Commission's Issues Paper. It concludes with a series of specific recommendations for consideration by the Commission.

7. A case study which examines the workings and importance of the TFES to a small regional business is included as Annexure A.

1. INTRODUCTION

1.1 This submission by Net Sea Freight - Tasmania (NSF-T) will refer to and offer comment upon some of the questions posed in the Issues Paper published by the Productivity Commission in April 2006 (5).

1.2 Not all the questions raised for comment in the Issues Paper will be addressed as many are not within the competence of NSF-T to comment upon. NSF-T offers details of operational difficulties faced by one of its clients as an illustrative case study; see Annexure A.

2. ROLE OF NSF-T

The role of NSF-T is to provide an administrative service to shippers of goods to and from Tasmania. Attached at Annexure B is a brief on services provided by NSF-T.

3. AIM OF THIS SUBMISSION

The aim of this response is to support the ongoing operation of the Tasmanian Freight Equalisation Scheme (TFES). We believe there is a case for such assistance, based on:

(a) strict economic grounds

(b) non-economic justifications which are of vital importance to the Tasmanian community

4. ECONOMIC AND SOCIAL RATIONALES

A Consitutional Basis

4.1 We begin with the proposition that a political decision has been made to ensure that Tasmanian importers and exporters do not suffer a cost disadvantage due to the Bass Strait component of the freight task. This can be justified by reference to the fact that the Commonwealth is composed of a federation of States. The citizens of those States should enjoy equal opportunities and benefits of such a union, among which the Constitution in S 92 determined that there should be no impediment to trade flows between States. The matter of equality of opportunity among States was extensively debated in pre-Federation Conventions. One manifestation is a Senate with uniform representation between States, insisted upon as part of the price of Federation. Reference will be made later within this submission to the social and regional development benefits of retaining assistance to the transport activity.

B Economic Case

4.2 A prime economic justification for assistance payments arises from the need to employ sea transport for the transport of most goods, either northbound or southbound, rather than air freight which is obviously appropriate only for very high value and/or very perishable goods, as well as the more obvious inability to use road or rail transport.

4.3 Assessment of the cost disadvantage is presently made by comparing Bass Strait transport of certain defined products with road transport of goods over a comparable land distance between interstate centres. This is based upon a land distance comparable with the shortest sea journey between the Mainland and the North of Tasmania, taken to be 420 kilometres. At present the assistance structure takes into account a difference between a wharf-to-wharf cost and the cost of an equivalent land journey.

4.4 This road freight equivalent (RFE) is currently set at $ 281 per TEU for dry freight and $ 309 per TEU for refrigerated freight, where a TEU (twenty-foot equivalent unit, 6.1 metres) is the standard measurement chosen for computation of assistance; other loads are converted to an equivalent in TEUs. The $ 281 is obtained by applying a value of $ 1.34 per kilometre over the 420 km for a vehicle carrying two TEUs, or $ 0.67 per km per TEU. The RFE specifically excludes load/unload costs. An intermodal fixed amount ($100) is allowed for activities associated with loading and unloading, to which this submission will refer later.

4.5 An excess of the wharf-to-wharf shipping freight charge over the road freight equivalent is a starting point for computation of assistance under the Scheme.

4.6 It is contended that notional private cost of a 420 km land journey, determined as above, may understate the true transport cost, and this needs to be recognised in determining the rate of assistance. The understatement arises because the private cost ignores externalities. Private costs include the operators' capital and current expenses, including road taxes and other road user charges. Externalities arise from a variety of sources, such as congestion and non-charged road damage which it is argued are not reflected in direct charges paid by road users, and result in a less-than-efficient resource allocation on the part of road transport providers.

4.7 That there are congestion costs is manifest by the increasing prevalence of toll roads within the Australian environment and congestion charges explicitly levied in an attempt to internalise such costs in several overseas countries. Toll roads (sometimes privately provided) and congestion charges attempt to price-discriminate between potential users, such that separate markets are created - one which caters for those prepared to pay for a better service because of the additional utility derived from that market, the other for those not prepared to pay because their perceived marginal benefit does not exceed the marginal cost. By contrast, services provided by private or privatised sources, such as ship owners or railways, are presumably charged at a price intended to cover the full cost of providing these services; this may also be due to the impossibility of shifting part of the overall cost to others. An outcome of having a service available at a less-than full price is that the service is over-used, i.e. there is a resource misallocation (over-allocation) due to the ability of users collectively being able to avoid paying a price which reflects the full social cost.

4.8 Road damage is recognised by the existence of speed and axle-load restrictions imposed by State governments. Efforts to make road transport vehicles more road-friendly include overall load limitations, as well as innovative measures on the part of some operators to spread loads over a larger number of wheels. These have the effect of partially internalising additional costs of road usage.

4.9 Hence the comparison base of a 420 km road journey ($ 281) is likely to understate the cost with which a sea freight charge is to be compared. The cost disadvantage on the sea leg may accordingly be less than the difference between the wharf-to-wharf charge and the notional private cost of a 420 km land journey. The cost understatement is tantamount to assistance being provided on land transport, and can be applied as an additional justification for assistance paid to shippers for Bass Strait freight movements. In addition, railways in Australia have been notoriously

unprofitable; their revenues have failed to cover their costs. To the extent that this circumstance still holds, rail freight is also subject to assistance.

C **Compensation Case**

4.10 Other justifications for assistance to Tasmanian users of Bass Strait shipping services have been proposed by several previous inquiries and commented upon in their published reports. One major Report is that of The Interstate Commission, "An Investigation of the Tasmanian Freight Equalisation Scheme, Volume 1", published in March 1985 (4). This documents several constraints from which Bass Strait shipping is suffering higher costs than would otherwise be the case in a free market economy.

4.11 These include the existence of the Navigation Act, which prohibits foreign shipping from operating around Australia's coastline, unless permission is granted for such services to be used. In itself, it is contended that this is likely to impose cost penalties on users, because of the small number of competitors in the Bass Strait trade. Moreover, because Tasmanian interstate trade is so heavily dependent upon Bass Strait shipping, it can be argued that the burden of this protective measure falls disproportionately heavily upon Tasmanian shippers, to the benefit of the Australian shipping and ship-building industries. Taxpayer-funded assistance on shipping activity between Tasmania and the Mainland is then a case of recovering some of that excess cost.

4.12 Ship operators would also probably claim that a strong Maritime Union increases operating cost penalties by requiring them to provide better pay and conditions than would be on offer in foreign operated and crewed vessels. By their very nature, these alleged cost penalties are not borne by producers using road and rail services in other States.

4.13 In addition, there are notionally restrictions on imports of ships, to encourage the domestic ship-building industry, which ship owners would also contend imposes a cost penalty. However, because of the difficulty of acquiring a ship within Australia, it is usual for cargo vessels to be imported, either new or previously owned. Few ships for commercial use have been built within Australia in recent times.

4.14 These types of policies have made the environment within which Bass Strait shipping operates more expensive than international standards, but have been imposed by a Federal Government and impact on Tasmania as a State in a Federation. This provides a further basis for compensation from general tax revenues.

D **Social Case**

4.15 It is observable that population and economic activity in Tasmania is very decentralised. There is a dispersion of population away from the capital city in a manner which is unmatched by other States of the Commonwealth. This has implications for supply of services and provision of opportunities to residents living in regions often some distance from major cities. These regions are often highly dependent upon a single industry for employment opportunities, usually rural or primary industry based. Output from these activities is usually well in excess of what is needed by the Tasmanian market and exporting becomes essential for continuation of the activity, sawmilling and vegetable production being illustrative industries. Such single industries underpin the social core of the town.

4.16 The outcome on a single industry community is well documented should that community lose a major employer. The domino effect of closures of banks, service station, post office, supermarket

(or smaller grocery store), school, hotel, not necessarily in that order, has been well documented, and replicated, in country Australia over the past century. Ultimately, the town becomes social welfare dependent, with concomitant problems known only too well. It often follows, should there be a drift of the town's population, that concurrently it becomes increasingly difficult for the town's sporting teams to continue to field, particularly the local football team. Indeed, some towns are so small that their main sporting and cultural activities involve even fewer people, such as church-related groups, Country Women's Association, Rural Youth, local fire brigade. Should those go, social cohesiveness becomes even more strained as the facilities supported by these activities, including halls and other community utilities, also tend to become run down.

4.17 It is a fact that there are several smaller Tasmanian towns, and their associated hinterlands, which are largely dependent upon economic activities whose output is subject to freight assistance. So much so that in some cases, termination of this assistance would result in a rapid cessation of the activity, with consequent effects likely to mirror those described above.

E **Economic and Social Synergies**

4.18 There is accordingly a strong case for the continuance of some assistance from the public purse to ensure the maintenance of these types of communities. They are often close to being self-sustaining and capable of functioning with very little support. Failure to extend the required support usually results in a much greater burden on the welfare sector than a specific purpose payment. Assistance paid under the Tasmanian Freight Equalisation Scheme is, in the case of several towns, all that render a particular activity economic. It assists in sustaining production which results in the employment of a significant number of locals directly and with the multiplier effects on the immediate region ensure further indirect employment, with much broader Statewide effects.

4.19 The actual amount of assistance paid may well be less than the annual wage paid to a handful of that firm's employees. However, the regional support directly generated by that relatively small payment can be an order of magnitude greater, in monetary terms, with further trickle-down effects leveraging the outcome to something quite substantial. The non-monetary social dividends for the local region should need no amplification.

4.20 To put some perspective on the quantum of funding which is enjoyed by firms receiving assistance, the 2004-05 expenditure on the assistance was $ 89.1 m, across a population of less than half a million Tasmanians, which converts to about $ 180 per head of population. The community-sustaining value of the assistance is many times greater.

4.21 By comparison, the Alice Springs - Darwin railway has enjoyed federally-funded capital expenditure, and annual operating losses have been met by federal government funds. With a Northern Territory population much less than that of Tasmania, the per-head federal assistance on this transport link exceeds that afforded by the TFES.

F **Second Best Argument**

4.22 This submission also argues that the second-best argument for assistance is still apposite. The theory of the second best suggests that where there are entrenched non-optimal constraints, the system might not be generally moved toward optimality by seeking efficient outcomes in other parts of the system. This means that given a non-optimal constraint, a second-best optimum might be obtained only by departing from all other conditions for optimality. To amplify, because there has been some intervention in the economy, it is possible that in at least one market marginal social

costs are not equal to marginal social benefits; a sign that there is an inefficient allocation of resources. It is not necessarily true that the next best optimum will be attained by policy measures that ensure marginal social costs and marginal social benefits are equal in all other markets.

4.23 Economic theory suggests optimum (efficient) outcomes are more likely when no market intervention occurs. Exceptions do occur when market-based solutions do not produce a socially optimal result, for example when there is market failure for reasons such as the existence of externalities (e.g. marginal social benefit is less than marginal private benefit, instanced by congestion), or if the market is dominated by a single supplier, or few suppliers (e.g. where there is a welfare loss due to underproduction by a monopoly supplier). Given that some remaining intervention is a fact of life, and that it would be difficult to dismantle it to avert continuing market distortions, the case for assistance remains as a means of compensating for these distortions.

4.24 The persistence of institutional constraints, such as land transport users not bearing its full cost (assuming that shipping service users do), continuance of cabotage and restrictions on imports of ships, means that the operating environment is not conducive to optimality. In that case, assistance (whose effect distorts behaviour from what it would be in its absence) will not necessarily make the market outcome less efficient. There is, accordingly, a compensation case for assistance. It is the size of the assistance which needs to be determined.

4.25 It is doubtful that it is possible to compensate only for that component of freight cost disadvantage directly attributable to transport-related distortions, because of the complexity of the task of unravelling the cost increases induced by these distortions. Accordingly, we suggest a continuance of the Scheme in order to alleviate some of the cost disadvantages, with modifications proposed later in this Paper.

5. CHARACTERISTICS OF THE FREIGHT TASK

5.1 The TFES defines a TEU to be a 6.1 metre container whose load is 21 tonnes, or 30 cubic metres. The container has an actual volume of 35.28 cubic metres. As containers frequently hold a greater weight than 21 tonnes, or a greater volume than 30 cubic metres, there is some incentive to maximise container capacity to achieve greater efficiencies. The effect of these loadings is to reduce assistance payments, because the assistance relates to the standard TEU of either 21 tonnes or 30 cubic metres.

A A typical freight operation

5.2 Consider the following example of a container's movement between Launceston and Melbourne. A forwarder picks up an empty container. This is then taken to a client's premises and loaded, or is loaded from partial consignments consolidated at the forwarder's premises. The contents of the container must be shored in a manner to render them secure for a sea voyage, as opposed to what might be necessary for a land freighting operation.

5.3 The loaded container is then taken to a wharf, say Launceston - Bell Bay. The journey may be broken by the need to visit a weighbridge, which may involve some waiting time, as well as the diversion from the intended trip. On arrival at the wharf, there will inevitably be a wait before unloading can occur, as well as the time taken to unload.

5.4 At the Melbourne end, the forwarder will almost certainly be subject to a delay before unloading is completed and the container can be accessed by the customer. After delivery of its contents, the container must be taken to its owner's premises and de-hired.

5.5 This example illustrates some of the different aspects of a Tasmanian freighting exercise compared with one wholly on land between, say, regional Victoria and Melbourne. There will probably be less of a problem in most cases in Victoria in arranging use of a container should one be required. In Tasmania, however, containers are often in scarce supply due to the imbalance of trade in each direction. This can cause increases in the overall cost of a shipping exercise as it might be necessary to track one down, or alternatively wait until one becomes available, even by importing one empty, or have one brought as backload freight from another delivery operation. Packing for a land journey does not have to be as robust as for a sea journey. In the case of a land journey, the two wharf visits will not be necessary, and the carrier will not have to allow for demurrage, which can be quite significant as a portion of the land freight cost component of the interstate freight operation.

B **Other freight matters**

5.6 An alternative to use of containers for shipping is to use tautliners and trailers, where a ship is of the roll-on, roll-off type. These are more efficient, are provided by forwarders, and are subject to a hiring charge to the shipper - a common rate is $ 350 per trip. Whether this hiring charge might be classed as an intermodal charge, or whether it might be subsumed in the $230 DW, or WD adjustment is unknown, but the hire of a container owned by a shipping company is included in the wharf-to-wharf charge of a shipowner. The issue of what the intermodal allowance is intended to cover is addressed later in this document. Guidance from a TFES source would be useful.

5.7 The advantages of roll-on, roll-off tautliners and trailers lie in the relative rapidity with which loading and unloading can take place, and the speed of the wharf activity. While trailers have been in vogue for many years, over recent years longer ones are being used. The availability of wheeled-vehicle traffic freight capacity has had a beneficial effect on efficiency with overnight carriage, later loading and earlier access to freight at destination ports. The availability of a TT Line service broadens the variety of choice for shippers as it provides an express service (and a later departure time, especially valuable to shippers from southern Tasmania including for such goods as fresh fish), even if charges are higher to reflect such a service.

5.8 Air freight is suitable for cases where greater rapidity is required. This mode is suitable only for small, high value freight, or where there is some urgency to deliver because the product is perishable. Most of what is sea-freighted to and from Tasmania is unsuitable for air freight. If assistance were not paid on sea freight, it is unlikely that air freight would be used more. A case for air freight assistance is not pursued in this submission.

5.9 The shipper is often required to load the container, which may involve the hire of specialised equipment such as a side loader. This activity imposes additional costs on the shipper as two trips are required - one to drop the container off, one to pick it up.

5.10 There are additional costs of cross-Strait shipping compared with land-based transport between regional and metropolitan centres. In many cases, it may be necessary for freight to be double-handled - packing of containers on-wharf or within freight forwarders' premises are activities associated with ship transport which do not apply in a purely road transport operation. In the latter case, tautliners may be used with minimal packing effort. For sea voyages, spoilage is likely to be more prevalent; packaging and strapping must be more robust.

5.11 One aspect of Bass Strait shipping that is an occasional irritant is the seasonality of demand on facilities, which comes from vegetables, for example, which have to be shipped without delay (usually requiring overnight shipment) and which receive preferential treatment thus occasionally diminishing the quality of service to other shippers. Such seasonal cargo space shortages, as well as capricious availability of containers add to the costs faced by shippers, none of which are recognised in determining assistance under TFES.

6. COST DISADVANTAGES

A Systemic factors

6.1 A major contributor to the cost disadvantage suffered by Tasmanian shippers, in both directions, is the short-haul nature of the task. Shipping becomes more economic as distance increases. There are several factors already mentioned which impose higher costs per kilometre across Bass Strait than on mainland routes, such as rail-road competition which keeps rail charges low, less than full cost recovery from road transport, cabotage regulations which require higher-paid Australian crew on Australian vessels. The latter averts international competition with domestic services. We hasten to add that we do not promote the use of "ships of shame".

6.2 A Senate Standing Committee Inquiry was established in 1970 to investigate the reasonableness of a proposed 12.5 % increase in Australian National Line (ANL) freight rates on Tasmanian services. The ANL was then an Australian Government body, and subject to oversight by the Australian Coastal Shipping Commission. In the Committee's Report delivered in 1971 (6), it noted many aspects of the shipping environment which tended to impose higher costs on Tasmanian shippers than applied to the freighting task in other States. Most of these persist today.

6.3 A fundamental driver of the cost disadvantage is the scale of operations. That is, the relatively high capital costs of shipping assets, compared with the volume of activity means that amortisation charges are necessarily high. At present Tasmania has four major ports – it is likely that none of these is operated at anywhere near their possible capacity on a continuing basis, so that for much of their lives, port assets are idle. An implication of this is that, with permanent dock-side labour, charges for on-wharf activity are likely to be higher per unit (say tonne) shipped. Seasonal highs and lows in shipping, though not as pronounced as in past decades, still exacerbate costs of shippers.

6.4 Ship size is important in determining the cost per TEU. Bass Strait ships are small compared with their international counterparts, which currently are able to load up to 8000 containers, compared with about 300 on the Bass Strait run. Accordingly, the average cost per container on the Bass Strait run is likely to be several times that of a ship with a capacity of 8000 containers freighting, say, from Bell Bay to Antwerp. To illustrate, a blue-water freight quotation from Bell Bay to Ho Chi Minh City for a TEU is $ 985, on a vessel with a capacity of about 1300 containers, while a charge for a Bell Bay to Melbourne shipment on a 300-TEU capacity vessel is about the same.

6.5 Many shippers are too small to be able to utilise available economies of full container loads; consolidation of cargoes of several shippers is necessary to fill containers. This means that freight forwarder charges (arising from fragmented pick up and subsequent delivery) are higher per container shipped than if individual shippers were able to fill their own container.

6.6 The Standing Committee's Report (6) also referred (in Chapter 8) to the problems of provision of adequate capacity in shipping, compared to the situation of land transport. Ships come in significantly greater increments than rail or road trucks. A service may have to persist with growing under-capacity for some period before it becomes economic to add another ship to the trade. Re-scheduling existing ships is often not a satisfactory option to reduce a rising backlog, as it means depriving a lump of capacity from another service. Associated with this dilemma are problems imposed on shippers and other parties in the production chain, of irregular and uncertain service, the need for greater inventories and loss of competitive advantage in markets.

6.7 Refrigerated shipping has scale problems of its own. The existence of less-than-full container loads requires pick-up and delivery strategies which inflates costs. Such cargoes are susceptible to spoilage should shipping delays occur. There is a need for specialised trailers, which can either freeze or chill its contents, but which are not necessarily going to be used all year; shipment of frozen vegetables are obviously of seasonal nature. Some products such as chocolate can be moved in conventional containers in winter, but in summer there will be an increase in demand for refrigerated units. It is possible to raise the utilisation of such containers by loading with dry cargo.

6.8 Competition in the trade by (a now private) ANL has ensured freight rates are lower than an otherwise expected 20% to 30% rise over recent years. Currently the competitive effect of the TT Line with its three ships has also assisted in keeping rates below what otherwise would hold. Bass Strait is over-tonnaged, with freight capacity in excess of what is necessary to service present demand. Advice is that current capacity is about 600 000 TEUs p.a., compared with current demand for about 450 000 TEUs p.a. It is likely that no line is presently making a satisfactory profit, especially with the TT Line losing money. Rationalisation and higher freight rates are likely in the medium term.

6.9 The assertion in the Issues Paper (5), page 15, that freight rates have declined is not consistent with the experience of NSF-T. An examination of a sample of representative rates per TEU, on Bass Strait over the period 1998 to 2005, revealed increases from $1040 to $1387. These indicate a compound increase of 4.2% p.a. This is in excess of the general inflation rate. It may be that rates quoted on a door-to-door basis might show a decline, but these can carry some distortion, depending on the land freight component.

6.10 Freight related costs are significant for some classes of freight, particularly those of low value, for example packaging timber and scrap steel. A product may have a sales value to a shipper of between $120 and $270 per cubic metre, depending upon quality and the degree of processing. The freight cost on this product is about $50 per cubic metre, i.e. varying from about 20% to 40% of the selling price. Higher priced goods with low profits, such as textiles, have significant margin erosion as a result of the high freight costs associated with Bass Strait transport. Without assistance on freight costs these products are uneconomic to ship interstate and production could cease.

B **Market Structure**

6.11 Cost disadvantages to shippers can also arise because shipping companies have significant market power. The shipping market is comprised of a small number (presently four), of Bass Strait shipping companies, an oligopoly. Given this small number relative to the number of shippers, the power imbalance is obvious. The industry is not, in practice, contestable, in the sense that threats of entry would otherwise ensure competitive behaviour on the part of shipping companies. Entry costs are relatively high (due to the difficulty of obtaining tonnage of suitable design) and exit costs (sunk costs in the form of having difficult-to-sell shipping in the event of fire sale market

conditions) would also make potential entrants cautious. The present degree of competition between the shipping companies is unlikely to change in the short run.

6.12 There is a larger number of freight forwarder firms. Some are vertically integrated with shipping companies, some are very small independent operators. Freight forwarders, particularly those which handle large volumes, are able to bargain with shipowners for preferential rates, but except in this instance, the power balance is little different from that between shippers and shipping companies. Vertical integration enhances the ability of a shipping company to hide land transport costs within a wharf-to-wharf rate; this is deleterious to shippers' ability to obtain maximum assistance entitlement.

6.13 There is an even larger number of shippers, some of whom are quite dominant users of shipping services and who receive the bulk of assistance paid. Larger shippers are able to negotiate direct with shipping companies. The importance of large shippers in underpinning regular services is acknowledged as a benefit to smaller shippers. The majority of shippers are medium to small.

6.14 This morphology of the market creates a power imbalance for negotiating rates. To correct this imbalance a hierarchy of bargaining can be instituted. It would be preferable for freight forwarders, who are characteristically larger than the shipper, to negotiate shipping rates with shipping companies. The shipper could then negotiate with the freight forwarder to determine the door-to-door rate, i.e. the freight invoice charge and the wharf-to-wharf rate.

7. CURRENT ASSISTANCE ARRANGEMENTS

A Assistance to be paid to Shippers

7.1 At present, TFES assistance payments are made to shippers directly. This is preferable to any alternative, including paying to shipping companies, as there is no guarantee in the latter case that freight rates will be lowered to reflect the assistance. There is a higher risk that assistance will be appropriated, at least in part, by the service providers if the assistance is paid to them, that is, the benefit of assistance may not be passed on. The present practice of assessment of cost disadvantage by Centrelink and computation of assistance is reasonably transparent.

7.2 This principle of making assistance payments directly to shippers was a recommendation of each of:

(a) the Nimmo Commission Report of 1976 (1) which found that, "(for) maximum effectiveness transport assistance should be paid directly to the persons and firms who suffer the financial disadvantage".

(b) the 1985 Interstate Commission Investigation (4) which proposed that, "compensation shall be paid directly to consignors or consignees", and

(c) the 1998 TFES Review Authority Report, the Nixon Committee, (7) which in enunciating desirable characteristics of an assistance package stated that there should be, "maximum retention of the assistance by producers/shippers. It should not be captured by the carriers, neither freight forwarders nor liner operators, if it is to have the intended effect of correcting for the freight related cost disadvantages experienced by Tasmanian producers."

7.3 This submission proposes most strongly that these precedents not be cast aside in favour of any alternative which might place shippers in a comparatively detrimental situation. It is better that assistance payments be made direct to shippers as this will ensure it is less likely that the assistance will be appropriated by providers of shipping services. While administration of the assistance scheme may be viewed as more simple if assistance payments are made to ship owners, with the wish that freight rates will be decreased to reflect the assistance, there is no guarantee that ship owners will comply.

7.4 Economic theory suggests that a subsidy will in general benefit both buyer and seller in a transaction; that is, the price charged will fall by less than the amount of the subsidy, as some of the benefit of the assistance is claimed by the seller. However, in extreme cases, such as where the demand for the service is highly price-elastic, or where the supply is highly price-inelastic, the majority of the benefit of subsidy will accrue to the seller.

7.5 Therefore, it is likely that shipping companies do appropriate part of the assistance, and that they do take notice of the availability of subsidies when setting rates. Any adverse effect of assistance on shippers' incentives to improve efficiency and innovation would be minimal, as shipping services are not made free by the assistance, and pursuit of profit on the part of market traders should ensure a continued pursuit of efficiency. This has seen increases in cassette and MAFI trailer capacity and development of innovative containers. The present scheme provides incentive for efficiency, as only part of a marginal wharf-to-wharf rate increase is met by the scheme.

7.6 Costs of complying with the requirements of TFES are relatively small for a normally efficient firm. The potential benefits from being able to obtain assistance are greater than costs imposed. Attempts to increase precision of the process of claiming assistance have not increased compliance costs. Computation of assistance is simple if relevant information (i.e. $ wharf-to-wharf/TEU, or $ door-to-door/TEU) is known, due to the short cut formulae developed following the establishment of the methodology for determining assistance by the Nixon Committee in 1998 (7). Calculation over the past four years has been aided by a spreadsheet developed by the TFES office. The Nixon formulae for calculating assistance are far superior in their simplicity to the process which preceded it.

B **The Nixon Formulae further simplified**

7.7 The Nixon Review, in developing a new framework for determining assistance, divided shippers into four classes, depending upon what was termed their "notional wharf-to-wharf disadvantage" and proposed a calculation to assess assistance due to shippers in each class. These expressions, when couched in terms of wharf-to-wharf costs, either notional or actual, may be simplified as follows, where NE refers to notional entitlement:

(a) Class 1 : NE = WW – 181, for WW <= $616.50

(b) Class 2 : NE = 0.75WW – 26.875, for $616.50 < WW <= $ 952

(c) Class 3 : NE = 211.125 + 0.5WW, for $952 < WW <= $ 1287.50

(d) Class 4 : NE = 854.875, for WW >$ 1287

7.8 These formulae permit calculation of assistance given an actual or notional wharf-to-wharf charge. The proportion of wharf-to-wharf cost paid as assistance is relatively constant over a range, until the assistance amount tops out at $ 855 per TEU, for wharf-to-wharf costs of $ 1287 per TEU and above, as follows:

WW ($/TEU)	Assistance ($/TEU)	Assistance as % WW
650	461	70.9
700	498	71.1
750	536	71.5
800	573	71.6
850	611	71.9
900	648	72.0
950	686	72.2
1000	711	71.1
1050	736	70.1
1100	761	69.2
1150	786	68.3
1200	811	67.6
1250	836	66.9
1287	855	66.4

7.9 The linearity of the relation between the two measures (which can be observed by graphing them) suggests that the formulae could be replaced by a simpler equation derived from regressing the assistance payment against the wharf-to-wharf costs.

7.10 To do this, a regression exercise was completed for the above range of wharf-to-wharf values from $650 to $1250, and the corresponding assistance values. The calculated linear relationship between the two variables is $Y = 71.4725 + 0.6255X$, where the independent variable, X, is *the notional wharf-to-wharf cost*, and the dependent variable, Y, is *the notional assistance entitlement*, the dimension of both variables being dollars per TEU. It should be stressed that this relationship is valid only over the range of wharf-to-wharf costs from $650 to $1250 per TEU.

7.11 The interpretation of the regression equation is that within the sampled range of the two variables, the increase at the margin in assistance payable is about $0.62 for each dollar increase in wharf-to-wharf cost. Thus the intent of the Nixon Committee, to design an assistance framework which would give incentive to shippers to obtain the lowest shipping charge, is still met.

7.12 This relation has a very low standard error, which means its predictability is good, and the correlation between the two variables is very high, with a correlation coefficient of 0.9950, indicative of a very good fit between observed pairs of the variables. That these properties hold is to be expected, as the calculated assistance is functionally dependent on the wharf-to-wharf cost in the Nixon three-stage model.

7.13 It is suggested that this regression equation might be used to calculate the expected assistance directly, once given the actual or notional wharf-to-wharf costs, as it is rather simpler to use. The procedure developed by the Nixon Committee is cumbersome, and to a layperson could not be described as the apogee of clarity. The verbal description of the rationale behind the derivation of each of the expressions does not fit with the expressed formulae. However, the simplified expressions shown in 7.7 above make the Nixon process more user-friendly.

7.14 An advantage of the single regression formula is that it can be arbitrarily varied by either a shift (change in the constant term) or a tilt (change in the slope coefficient) to reflect changed circumstances or policy objectives. The equation would prove more useful if reviews become more frequent.

7.15 It is clear that the Nixon Committee formulae have built in to them an incentive for the shipper to obtain a minimum wharf-to-wharf rate, as the assistance determined in each of the intermediate range cases has a marginal value of less than one dollar for each one dollar increase in wharf-to-wharf rate. There is always an incentive for a shipper to negotiate a lower wharf-to-wharf rate if possible, as the assistance is always less than 100% of the wharf-to-wharf rate.

7.16 We can observe a simplified expression for the entitlement at each end of the Nixon distribution. Within the first tranche NE = WW - 181, which means that the assistance is zero when the wharf-to-wharf rate is $181. The assistance remains constant at $855 per TEU from a wharf-to-wharf rate of $1287 per TEU, which means a shipper is liable for all of any wharf-to-wharf charge in excess of $1287.

C **Capping assistance**

7.17 It is the opinion of NSF-T that there should be no capping of TFES subsidies. It would not be within the intent of TFES for assistance expenditures to be capped; its purpose was to compensate for freight cost disadvantages for sea freighting of certain goods to and from Tasmania. Capping total assistance to a budgeted annual value would retard growth of Tasmanian industry and introduce uncertainty to freight costs and sale price of goods. Administrative difficulties would arise in determining how to distribute a capped budget assistance value and would delay assistance payments to recipients, with consequent liquidity effects.

7.18 With a cap on expenditures, shippers would have less certainty as to the degree of assistance they would receive. It would be difficult to establish selling prices of goods into mainland markets, as well as inducing more risk into producing in Tasmania. There is no virtue in reduced certainty. Any capping would also have social repercussions; as noted earlier, several Tasmanian communities depend upon assistance rendered by the Scheme to sustain their continuance.

7.19 Information from an informed source is that Bass Strait freight volume has over recent years experienced growth rates of approximately 8% p.a. Reported aggregate TFES payments (northbound and southbound) since the Scheme's inception in 1976 grew fairly slowly until 1998-99, but have since then grown at a more rapid rate. Data published by DOTARS in 2006 (3) indicates the movement in TFES claims since 1997-98 as follows:

Year	**TFES Payments, $m**	**Annual Growth,** %
1997-98	41.4	0.5
1998-99	41.8	1.0
1999-00	59.4	42.1
2000-01	67.0	12.8
2001-02	72.0	7.5
2002-03	77.2	7.2
2003-04	83.0	7.5
2004-05	89.1	7.3

7.20 The rather dramatic growth in assistance in 1999-00, was due essentially to a lifting of the cap on the maximum amount of assistance from $590 per TEU (for the maximum wharf-to-wharf cost disadvantage), pre Nixon Review, to $855 per TEU after the revision of the structure of the Scheme. This is a growth of about 45% in itself.

7.21 It is suggested that the growth in assistance payments from 1999-00 was compounded by an increase in the number of claimants among whom were some who had previously been eligible to claim, but had not. Hence what looks like an aberration is essentially the result of a revision of the Scheme's structure. The growth in assistance in 2000-01 is similarly due to this influence, as the higher scale did not come into effect until late in the previous financial year.

7.22 Since then, the annual growth in assistance virtually matches the observed rate of growth of Bass Strait tonnage. For the years 1999-00 to 2004-05, the growth rate is about 8.4% p.a. compound, more in keeping with the reported recent growth rate in cross-Strait shipping volume.

7.23 The Scheme's cost continues to grow because of a growth in Bass Strait freight volumes. Growth is also occurring because some eligible shippers that were previously either not claiming assistance, or were under-claiming, are now tending to do so. This growth should be welcomed as a measure of how assistance is promoting economic activity in Tasmania.

8. PROPOSALS TO VARY CURRENT ARRANGEMENTS - EXTENSIONS OF TFES COVERAGE

A Assistance to Government Business Enterprises

8.1 Since the 1998 Review some Tasmanian Government businesses have had their status changed from a department or a commission to a government business enterprise under the control of a board of directors, and are required to operate in a competitive business world with market reach beyond Tasmania. With the status of ‘government’, such organisations were specifically excluded from entitlement to TFES assistance. Their current status should render them eligible for assistance as is the case for their privately-owned counterparts. Being unable to access assistance disadvantages them vis–a-vis their competitors.

B Freighting from King Island and Flinders Island

8.2 There is a problem relating to the collection and retrieval of scrap metal from these islands. It is at present uneconomic to collect the substantial amounts of scrap that have accumulated on both islands. The Commission may wish to investigate the issue with a view to assisting the Bass Strait Islands in being environmentally compliant.

C Extension of Scheme to cover imported goods

8.3 The Scheme does not permit assistance to be paid on "goods imported into the mainland of Australia from overseas which have not undergone a manufacturing process on the mainland prior to their shipment to Tasmania" (Ministerial Directions Paper, Clause 10. (2)). It is submitted that this is not in the spirit of the Scheme, and is using Bass Strait freight cost disadvantage as a de facto import duty; an equivalent Australian-made item will obtain a protective cost advantage solely because of freight cost assistance across Bass Strait.

8.4 A Tasmanian manufacturing firm may have the choice of two similar machine tools, one Australian-made the other imported, both on sale by a Melbourne supplier. If the imported one is preferred, freight cost assistance is not available. If the Australian-made item is bought, assistance is forthcoming. In both cases, the tool will have to be sea-freighted across Bass Strait, but if the imported item is chosen the manufacturer will be at a competitive disadvantage relative to Mainland producers. Similarly, an imported good not manufactured in Australia and for which no Australian equivalent exists, is ineligible for TFES assistance.

8.5 Enquiries made on this point have usually evinced the response that assistance paid on imported goods would be at variance with international obligations. The payment of assistance on northbound international exports may violate World Trade Organisation principles but we do not understand why this should apply to imported goods shipped from mainland suppliers to Tasmanian manufacturers. This does not seem congruent with the intent of the TFES.

D **Shipments of Pallet Timber**

8.6 Using conventional timber industry measurement, a cubic metre of timber weighs about 1.1 tonnes. Thus a 26 cu m container loaded to its volume capacity with pallet timber, given the pack configuration of 1.58 cu m per pack, and 16 packs per load, weighs 27.81 tonnes. This is an example of an overweight container, where the standard limits are 30 cu m or 21 tonnes. Also pallet timber is always packed on new or repaired pallets (each of about 40 kg), and along with the container (about three tonnes), the overall weight of a load is close to 31 tonnes.

8.7 Whilst the average weight in a container crossing Bass Strait is 15 tonnes, pallet timber is in the order of twice the average. The amount of assistance attracted, being based on a 21 tonne load, is less than the standard per tonne.

E **High Density Cargo**

8.8 High density cargo is defined as that which measures (has a stowage factor of) 1.1 cubic metres or less per tonne. A container will thus be less than full for a maximum allowable weight. Shipping companies would regard such a container as a FCL for the purpose of freight charges, because volume is the apposite measure in sea freighting.

8.9 The present scheme discounts assistance to 60% of that which would normally be received. The rationale for the 40% deduction in the amount of assistance per FCL of high density cargo is not clear. Inquiries on this matter have failed to shed any light upon the dilemma.

8.10 Shipping costs are based on volume, rather than weight. In principle, once a container has reached its maximum weight limit, there should be no differentiation in the amount of assistance paid on its contents. The volume on a ship taken up by a container which is less than full is the same as that taken up by a full one.

8.11 There was some equivocation on this matter expressed in the 1998 Nixon Review, which also noted that high density goods, which receive arbitrarily lower assistance, appear to be discriminated against. It is suggested that if no cogent reasons can be provided to explain this conundrum, the restriction be abolished.

9. REVIEWS AND PARAMETER CHANGES

9.1 The present scheme has five parameters whose values affect the rate of assistance to be granted to shippers. These are the road freight equivalent cost, the door-to-door adjustment, the fixed intermodal cost, the route scaling factor adjustment and the median notional wharf-to-wharf freight cost disadvantage. These have not changed since the Nixon Review, in spite of it recommending that there be annual reviews and updates as required, which has not occurred.

9.2 Annual reviews and annual indexation are seen as not essential. A higher frequency of changes could lead to possible confusion and uncertainty to claimants. It is suggested that a three year interval between reviews and possible parameter changes would be preferable.

9.3 It is suggested that at least three of the TFES parameter values have become obsolete since 1998 and should be varied to reflect current cost levels. These are discussed below in more detail. The route scaling factors, insofar as they attempt to strike relativities for shipping on routes other than the 420 kilometre Bass Strait run, are likely to remain relevant at their present values unless some tectonic acceleration occurs. Moreover, the door-to-door adjustment to obtain a notional wharf-to-wharf rate is seen to be about right as a system average. Its realism is apt to be clouded by whether backloading occurs. We offer comments upon the remaining three parameters we believe need reviewing.

A Road Freight Equivalent

9.4 The validity of the road freight equivalent of $281 per TEU for a 420 km journey is questionable, as it is artificial both in concept as a fully-costed figure (does not take into account all road user costs), and as a currently reliable indicator of costs applying today. The Nixon Review determined the RFE as an average from advice sought for costs of operating a two-TEU vehicle, e.g. 40 ft trailer. The representative cost the Review arrived at was $1.34 per km, in 1998 costs, or $0.67 per TEU per kilometre. A per kilometre rate of $0.67 per TEU may be unrealistic in today's conditions, given an estimated 50%-plus increase in fuel costs over the past eight years. Advice from road operators is that, currently, a cost of around $1.60 per km per truck for a two-TEU load, is closer to the mark, or $0.80 per TEU.

9.5 We are advised that this $0.80 per km per TEU is what the road transport industry uses as an estimated cost, derived by assuming that the representative truck is carting two TEUs. That this is realistic (rather than being higher) is because trucks are being used more intensively (a higher number of kilometres per year) and because the national truck fleet is younger and more efficient.

B The Intermodal Allowance

9.6 This is set at a flat $50 per TEU at each end of the shipping journey. It is unclear what the inter-modal allowance is designed to cover, but it can be completely exhausted by pre-wharf activities. For many shippers, the allowance is too low in comparison with costs they incur. There needs to be recognition that some “ship-ready” activities may not necessarily always occur on wharf. These include loading at shippers' door, for which a cost is incurred but which is not reflected on an invoice, and thus not recognised as a cost for which assistance could be paid. These costs are not applicable to mainland land-freighting activities, where a container is not necessary.

9.7 Often there are off-wharf expenses, such as those associated with obtaining a container, cleaning it, loading it, discharging it and returning for de-hire. In addition there are shipping-associated costs that do not apply to land-based transport, such as the need to pack more robustly,

strap or shrink-wrap container contents. Thus the allowance is insufficient for the majority of small-to-medium shippers.

9.8 One option with deceptive simplicity is to increase the intermodal allowance by an arbitrary amount. We believe this is workable, but lacks precision.

9.9 An alternative remedy is that some flexibility be introduced to reflect variations in actual costs from the flat $ 100 allowance, whereby it should be possible to identify relatively common intermodal tasks, specify those that are compensated for, and provide a residual inter-modal allowance covering those items not disaggregated. This implies an allowance greater than $100 for a given Bass Strait journey would be easily justified.

9.10 Note that the Nixon Committee concluded (p 12) that while the costs of intermodal transfer should be addressed, there should be "no attempt to list specific eligible 'other' wharf gate to wharf gate costs", on the grounds that to do so may influence shippers as to which tasks should be undertaken inside and outside the wharf gates. The Committee supported this proposal by noting that the audit trail for verifying claims could become more difficult if a list of other eligible costs were made explicit. However, a refusal to accept that intermodal costs could be disaggregated and identified makes the cost-determining process less transparent and defeats the purpose of shippers seeking to reduce freight costs.

9.11 The blue water rate as provided by some shipping companies does not capture all the costs of shipping when it is expressed as a wharf-to-wharf rate. The term "wharf-to-wharf rate" could be dispensed with in favour of a "cost of shipping rate".

9.12 It seems, based upon the costs experienced outside wharf gates by many shippers, that the parameter most in need of revision is the intermodal allowance. Its value may have been adequate as compensation when first determined, but has since been eroded. It is argued above that for many shippers the $100 allowance is grossly inadequate.

C **The median notional wharf-to-wharf freight cost disadvantage**

9.13 This is the basis of the assistance calculation formulae, and was determined by the Nixon Committee at $671 per TEU, from a distribution of notional wharf-to-wharf cost disadvantages, found by subtracting the RFE from wharf-to-wharf rates of a large number of Bass Strait shipments, northbound and southbound, of FCLs, presumably in 1996-97. The median is a positional value such that 50% of the items in an array of the distribution lie on either side of the median.

9.14 Over time the distribution of freight rates will have risen (or shifted to the right), consequently shifting the distribution's median, a positional average, upwards. As such, the median wharf-to-wharf disadvantage should rise too.

10. **SPECIFIC TOPICS**

A **Single dollar rate of assistance per container**

10.1 A single dollar rate of assistance per container would result in a greater under-compensation of some shippers, and a greater over-compensation of others. It is common for shipped goods in a TEU to weigh more than 21 tonnes, e.g. 30 tonnes. If shipowners permitted only 21 tonnes to be carried per container, they would then require two containers to be used, with a consequent effect

that a greater aggregate subsidy would be paid for the same volume shipped. There would then be a higher annual cost of the Scheme because there is less incentive to load more than 21 tonnes per container.

B **Would the Scheme's effectiveness improve if all bills were submitted on wharf-to-wharf basis?**

10.2 If freight forwarders charged shippers on a wharf-to-wharf basis, it would not be practical for LCL shipments, as paperwork would have to be supplied breaking down costs among shippers, and would increase the complexity of administering the scheme. There is not a problem with FCL shipments, but the option to lodge assistance claims for LCL shipments on a door-to-door basis should be retained.

C **Is the present system efficient?**

10.3 It is submitted that the present manner in which assistance payments are made should be preserved, i.e. all payments should be made to shippers in the case of Northbound freight, and end users in the case of southbound freight. Assistance benefits go to those intended to receive them. This was a conclusion reached by the 1998 Enquiry Report (7). The administrative process required for claim preparation is within the capacity of an efficient firm; it is simple, procedural, mechanical and straightforward, and is amenable to computer processing.

10.4 It is a strong recommendation of this submission that the assessment process be maintained, that is claims for assistance be submitted to a central office, with supporting documentation for evaluation to include a freight forwarder's invoice, for independent assessment and payment. This firm's experience with Centrelink (as the operating agent for the TFES) over many years has been entirely satisfactory. They are a most competent and helpful source of advice.

D **Southbound freight claims**

10.5 Claims for assistance on eligible northbound freight may only be made by the shipper, the party that pays the freight invoice. By contrast, southbound assistance may only be received for eligible goods by the end user of the products shipped. To our knowledge, because of the perceived complication of the claim process compared to the expected benefits, many eligible claims are not submitted.

10.6 While the format of southbound claims does not require revision, the process can be simplified by allowing agents to make claims on behalf of users of all eligible goods in a manner similar to that which prevails for the P scheme on southbound freight.

E **Potential opportunity for fraud**

10.7 The potential opportunity for fraud increases where claims are prepared by shipping companies, freight forwarders, or agents of these two parties, on behalf of eligible claimants or in fact themselves. Fraud is possible where the one entity sets, or contributes to, the freight rate, validates this rate in writing to the TFES, and prepares and submits the claim.

10.8 For example, fraud could be perpetrated by determining a sea freight rate by deducting as little as $1 from the door-to-door rate, i.e. a shipper could be quoted a door-to-door rate with a very small invoiced road freight rate, so that the blue water charge becomes very high, on the basis that part of this can be claimed back under the assistance process. Alternatively, a shipping company

could supply a shipper with on-site plant and equipment the cost of which is incorporated into the cost of shipping. Again, a shipping company or freight forwarder could maintain an inflated freight rate and offset this expense by provision of, say, a suite of computers to a client. Such largesse is unlikely to be declared as a freight rebate in the required statutory declaration.

F **Shippers' preference for a WW rate to be supplied by a forwarder**

10.9 To compare pricing behaviour of shipping companies, we consider the following three (actual) quotes for the same task of shipping a TEU across Bass Strait, with road haulage of 130 km. To enable comparisons of these quotes to be made more easily, they have been tabulated.

Source of Quote	DD $	WW $	Road Charge $	Road Charge $/km	Assistance Payable $
Shipping Company, K	1275	650	625	4.81	461
Integrated Forwarder, L	1588	1290	298	2.29	855
Integrated Forwarder, M	1228	1070	158	1.22	746

From Firm K

10.10 Shipping company K has offered a door-to-door rate of $1275, inclusive of a stated wharf-to-wharf of $650. This implies a road freight charge of $625. Then assistance of $461 is due, as the given wharf-to-wharf must be used as the basis of a claim for assistance. Alternatively, if the door-to-door rate was $1275 and no wharf-to-wharf is given, the notional wharf-to-wharf rate is $1275 - $460 = $815. Assistance of $584 is due. To achieve the same $584 assistance, a wharf-to-wharf charge of $806 is required. Thus it is better for the shipper to be quoted a higher wharf-to-wharf rate, which more accurately reflects shipping costs, as is recognised within the TFES formula for a door-to-door claim.

10.11 In this case, the shipping company has provided a wharf-to-wharf quote which attracts a lesser assistance than does a door-to-door formula. It is submitted that the difference in assistance outcome is not due to the road freight allowance, $460 as per the formula, being unrealistically high. Considered opinion is that the $460 is already too high. In Company K's quote the road freight charge for a 130 km trip is about $4.81 per km. A more realistic road charge should be about $1.60 per km per TEU, or about $208. This high road freight charge represents $417 of uncompensated shipping expense and non-transparent costs.

From Firm L

10.12 A quote for the same task by a freight forwarder integrated with a second shipping company, L, offered an invoice price for door-to-door service of $1588. A road freight charge was given at $298, meaning the wharf-to-wharf charge was $1290. The road freight charge is $2.29 per km per TEU. The assistance payable is $855.

10.13 The higher assistance is due to the involvement of a freight forwarder who is more aware of costs associated with shipping and quoting more realistic price components. There may still be a

hidden cost in this $1588 quote because of the $2.29 per km road freight charge - the sea leg may be cross-subsidised from land transport revenue.

From Firm M

10.14 Another integrated freight forwarder, M, quoted a door-to-door charge of $1228 for the task. This quote included a road freight component of $158, which implies a wharf-to-wharf charge of $1070. The road freight is $1.22 per km per TEU. The assistance on the sea leg is $746.

10.15 In this case, the road freight charge may be too low, in comparison with the proposed $1.60 per km per TEU. The underpricing of the road component has possibly led to a higher sea freight charge, with consequently higher assistance.

10.16 Comments on these quotations (Firms K, L and M):

(a) The quote from K clearly understates the shipping cost and appears to focus only on a blue water cost. The consequence of this is that shippers are under-compensated with a resulting non-competitiveness penalty on Mainland markets, denying the TFES its aim. The non-subsidised component of the charge is high relative to that part for which assistance is available. A shipper would reject this quote. This indicates the inappropriateness of shipping companies being the authority to issue certificates attesting to the wharf-to-wharf rate which forms the basis for assistance claims.

(b) The quote from L indicates an almost doubled wharf-to-wharf rate, from $650 to $1290, which results in a higher assistance to the shipper. The wharf-to-wharf rate recognises some road freight expenses but still indicates undisclosed shipping charges via a higher-than-justified road charge, by about $0.69 per km.

(c) The quote offered by M is the closest to recognising the cost of shipping, with a wharf-to-wharf charge of $1070, but appears to have shifted some of the road freight cost to sea freight, because the road rate is now $1.22 per km per TEU. This quote is the most acceptable of the three.

10.17 To summarise, the three quotes are indicative of the lack of competence of shipping companies in providing wharf-to-wharf shipping rates, because they are not cognisant of all shipping costs that accrue to shippers. Both the freight forwarder quotes are closer to recognising shipping costs. It is recommended that either the road freight charge or the sea freight charge form an explicit part of the freight forwarder's invoice in the case of shipping FCLs. For LCL shipping, the only feasible charge should be the door-to-door rate.

10.18 It is contended that the wharf-to-wharf rate is more accurately determined by deduction of the actual land transport rate from the gross rate, in the same manner as the current door-to-door formula allows. Short haul cargo tends to be disadvantaged on door-to-door claims, because the arbitrary land transport allowance of $460 can exceed the actual land transport cost. Establishing a sea freight rate by deduction of the road freight rate from the gross invoice, may eliminate potential fraud opportunities.

10.19 It is preferable for a wharf-to-wharf rate be struck by bargaining between a shipping company and a freight forwarder, as the latter is likely to have a better understanding of shipping costs than a small-to-medium shipper. Similarly, a shipper should negotiate with a freight forwarder for the land transport component as the shipper may have some familiarity with land transport costs.

Shippers could be encouraged to seek a fair land transport cost whose amount varies with the land transport task, and have this cost stated on the freight invoice.

11. **RECOMENDATIONS**

The major recommendations in this submission may be summarised.

11.1 The freight assistance scheme should continue.

11.2 The assistance should continue to be paid to shippers and not shipping companies or freight forwarders.

11.3 Shipping companies are not an appropriate source of wharf-to-wharf rates as they are not aware of all costs associated with shipping.

11.4 The Productivity Commission should review the appropriateness of at least three of the parameters applied in determining the rate of assistance to be paid.

11.5 The independent assessment process in evaluating claims for assistance should be retained.

11.6 The Productivity Commission should consider the use of a single equation to determine assistance to be paid.

11.7 The Productivity Commission should evaluate the case for extending the availability of assistance to some shippers currently not eligible.

11.8 The Productivity Commission should extend assistance to its full value on high density cargo.

11.9 Assistance should be paid on all Southbound cargoes shipped across Bass Strait regardless of country of origin, provided these goods are used in a manufacturing process in Tasmania.

REFERENCES

1. Commission of Inquiry into Transport to and from Tasmania, 1976: (Report, J F Nimmo, Commissioner), AGPS, Canberra

2. Department of Transport and Regional Services, 2002: Directions by the Minister for the Operation of the TFES, Canberra

3. Department of Transport and Regional Services, 2005: TFES Statistics, 12 months ending June 30, 2005, Canberra

4. Interstate Commission, 1985: An Investigation of the Tasmanian Freight Equalisation Scheme, Volume 1, AGPS , Canberra

5. Productivity Commission, 2006: Tasmanian Freight Assistance Arrangements, Issues Paper, Canberra

6. Senate Select Committee on Primary and Secondary Industry and Trade, 1971: Freight Rates on Australian National Line Shipping Services to and from Tasmania, AGPS, Canberra

7. Tasmanian Freight Equalisation Scheme Review Authority, 1998: (Nixon Review) Advisory Opinion, Review of TFES Rates of Assistance

ANNEXURE A
TO NET SEA FREIGHT - TASMANIA PTY LTD
SUBMISSION TO THE INQUIRY INTO THE SUBSIDISATION
OF CONTAINERISED AND BULK SHIPPING
16 JUNE 2006

SAWMILL CASE STUDY

This mill is a small operator in a regional town in northern Tasmania and accounts for a significant share of that town's economic activity.

Its bush operations involve the supply of about 75 000 tonnes of logs per year and employ about eight harvesting contractors. The mill's feedstock is low grade logs which are otherwise suitable for chips, but are instead used in a value-adding process in supplying pallet timber. The selling price of these logs for chipping is about $80 per tonne, but as packaging timber they are worth more than three times this amount. These logs are transported to the mill on its own trucks, employing three drivers the year around.

In the mill, a variety of activities is carried out by semi-skilled labour. About 30 mill operators work at breaking down logs, producing boards, and dock these to 1165 mm length planks suitable for pallet timber. These planks are graded into first and second grade, then packed, strapped and placed on pallets for loading on to containers. The packs are of different width depending on the destination. The product is used for the repair or manufacture of pallets in Victoria and Western Australia.

The shipping task is firstly to procure an empty container. Often this involves a truck trip to Bell Bay wharf, which sometimes has led to a promised container not being available, translating into a $150 per trip wasted outlay and delay. Should one not be at hand (a frequent occurrence because of the imbalance between import and export volumes between Tasmania and interstate, approximately 60-40 northbound- southbound), one must be freighted in empty, at a shipping-related cost. The product is shipped, always in a container, to Melbourne or to WA via Melbourne. All Melbourne-bound containers are loaded at the mill.

Timber shipped to Melbourne is arranged in 1165 mm packs, fitting into an Australian-standard size 6.1 metre container, loaded in a side-opening container. Timber shipped to WA is stacked in packs of width 1100 mm to fit international-sized containers, with a width limitation of 2.3 metres. These are loaded from the rear by stevedores at Bell Bay, from packs trucked from the mill. A special type of fork lift is required for the height-constrained container loading operation.

The sawmill has designed a trailer system to freight one standard-sized container of 30 tonnes from the mill to the Bell Bay wharf, and still fall within the permitted axle loading limit. The weight limit in Tasmania is 30 tonnes. If a conventional truck and trailer rig was hired from a sub-contractor, or freight forwarder, the load would be one or two containers, per run. In Victoria, road freight regulations of 25 tonnes on a standard trailer restrict the load to one container by weight.

This has implications for an intermodal cost, as trans-shipment is necessary. Loads of 16 packs have to be broken down into 13-pack loads, weighing around 25 tonnes, which means that about for every six loads leaving Tasmania, seven have to be made up for road transport in Victoria. Alternatively, four containers of 30 tonnes are about the equivalent of five containers of 25 tonnes.

A2

A cheaper alternative to the shipper, or the road freight operator, is to pay a road fine for excess loading. The transporting system adopted by the sawmill is a very proficient way of shipping its product. It is more efficient in terms of weight, freight costs and assistance, in that it saves about 20% of TEU use, of freight cost, and thus of assistance claimed.

Problems faced by the mill include the non-availability of containers, which impose shipping delays, and add to inventory holding problems. Their wharf-side problems include restricted sailing times from Bell Bay by ANL, and the times the firm is able to drop cargo off. The wharf is open to receive goods from 7.30 am to 4 pm on three days per week, and from 8 am to 5 pm on two days per week. Sailing days are Tuesday, Thursday and Saturday, but shippers must deliver freight on Fridays for Saturday sailings.

That the mill and the region are heavily dependent upon the continuance of assistance may be deduced from its financial outcome in 2004-05. The mill received assistance of about 3.3 times its reported profit. That is, without the assistance, the mill would suffer a six-figure loss and would be forced to exit the industry. The regional impact of such an occurrence needs no spelling-out.

ANNEXURE B
TO NET SEA FREIGHT - TASMANIA PTY LTD
SUBMISSION TO THE INQUIRY INTO THE SUBSIDISATION
OF CONTAINERISED AND BULK SHIPPING
16 JUNE 2006

BRIEF INTRODUCTION TO NET SEA FREIGHT – TASMANIA PTY LTD

Net Sea Freight – Tasmania is a freight administration company. We are not a freight forwarder, nor a competitor of either freight forwarders or shipping companies. Net Sea Freight - Tasmania provides a service to firms involved in shipping goods. The service offered removes clients' necessity to claim freight assistance directly. This results in a number of advantages including:

- The client maintains independence in selecting their chosen freight forwarder/s.
- The client pays the net freight cost, northbound only, thereby providing a firm with additional working capital and relieving month-by-month cash flow pressures.
- With no requirement to claim assistance, administrative time and costs are eliminated.
- The client captures the freight assistance benefit when paying a net freight invoice.
- The client is provided with either generic or custom made management reports of a financial and/or operational nature.
- Management reports include analysis data which details specifics of every shipment, including commodity, date of movement, reference numbers, quantities, net costs, GST and total cost and a reports showing sea freight, interstate and intrastate road freight.

The Net Sea Freight – Tasmania process is accepted by both Centrelink and the Australian Taxation Office and is compliant with the intent and rules of the TFES and Federal Taxation Laws governing GST.