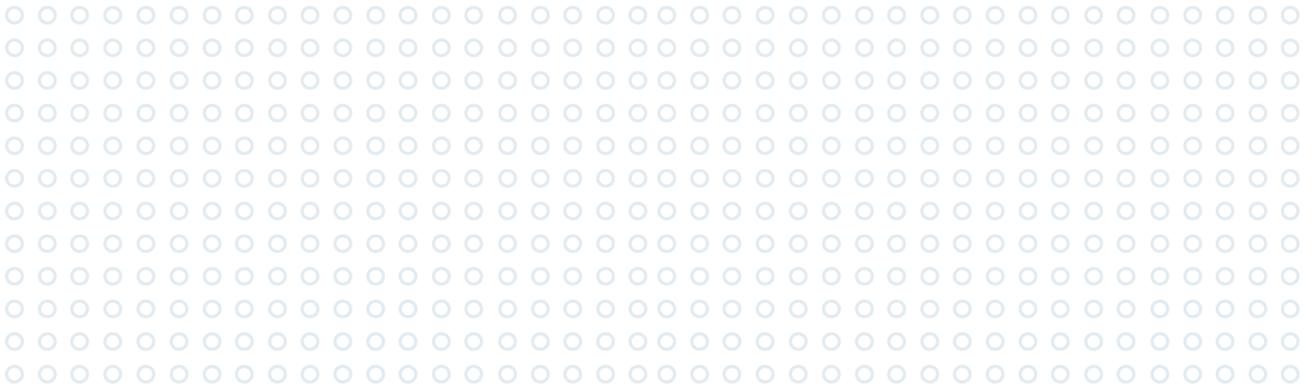


Business  
Council of  
Australia



Submission to the Department of  
Infrastructure and Regional  
Development on the Approaches to  
Regulating Coastal Shipping in  
Australia Options Paper

JUNE 2014

The Business Council of Australia (BCA) brings together the chief executives of more than 100 of Australia's leading companies, whose vision is for Australia to be the best place in the world in which to live, learn, work and do business.

## About this submission

This is the BCA submission to the Department of Infrastructure and Regional Development's *Options Paper: Approaches to regulating coastal shipping in Australia*.

Coastal shipping is the carriage of cargo or passengers from a state or territory to another state or territory via water (it does not include intrastate and international voyages). The Coastal Trading (Revitalising Australian Shipping) Act 2012 (the Act), which regulates the market for coastal trading services, is harming Australia's global competitiveness by imposing substantial costs throughout the economy.

This submission argues for the removal of cabotage restrictions in the Act that give Australian General Licensed ships the right to contest loads carried by a foreign ship under a temporary licence. It argues to move to an open, competitive market, with all other Australian laws continuing to be observed. Removing cabotage restrictions will reduce shipping costs and support investment and employment growth in manufacturing sectors, many of which are located in regional Australia.

## Overview

This review of coastal shipping should recommend legislative reforms that are in Australia's wider national interest. Following the blueprint established by other productivity enhancing reforms over the past three decades, this review should lead to an open, globally competitive coastal shipping sector that contributes to lifting Australia's national economic competitiveness, boosts productivity and jobs, and grows national wealth.

An efficient coastal shipping sector is important for lifting the competitiveness of Australian businesses that use coastal shipping in their supply chains and which employ many Australians right across the country. Around 90,000 Australians are employed in manufacturing sectors that use coastal shipping, including oil refining, cement, steel and aluminium.

At the core of this review is the threshold question of whether Australia should continue to legislate to give Australian General Licensed vessels preferential trading rights over foreign vessels. Currently, Australian General Licensed ships have the right to contest and carry shipments that a shipping user is seeking to have carried by a foreign registered vessel under a temporary licence.

These contestability rights, or cabotage restrictions, are locking in uncompetitive shipping rates and imposing excessively high regulatory costs on business. The impacts on business differ by sector and by whether there is a General Licence vessel available to challenge. The costs to business range from cases where ships are being operated inefficiently in order to comply with complex rules, to other cases where businesses are paying very high rates in the market for shipping services where there is a high chance of a contest to a temporary licence. Cabotage restrictions in these cases mean Australian firms are paying rates that can be up to double the rates offered by foreign ships, adding tens of millions of dollars to their cost base, and making their operations less viable as a result. Australian businesses report that it is cheaper to ship materials from overseas than to move them around the Australian coast.

Current policy objectives attempt to both promote an efficient shipping market and maximise the use of Australian ships. This has led to a set of coastal shipping policies that are confused, costly and counter-productive.

- Confused: the Coastal Trading Act has two inconsistent objectives: to enhance efficiency and competition while also maximising the use of Australian vessels. These objectives clearly come into conflict when a higher-cost Australian ship is given preferential rights over a lower-cost foreign vessel.

- **Costly:** the licensing system put in place to support the conflicting objects of the Act is cumbersome and inflexible and imposes costly red tape on industry. The preferences given to Australian ships leads to higher shipping costs. There is uncertainty around the decision-making framework, adding to business concerns.
- **Counterproductive:** by raising the costs of coastal shipping the current regime puts the long-term viability of coastal shipping and shipping users at risk. Higher costs makes coastal shipping less competitive with road and rail. Higher costs also creates incentives for industry to import product rather than transfer materials around the coast for local manufacture. Under the current regime, which was designed to 'rebuild Australian shipping', shipping rates continue to rise, shipping volumes are falling and the number of Australian ships has not increased.

These impacts work against Australia's national objectives for economic growth and job creation.

There is a simple way forward. Government should prioritise an objective for a competitive and efficient coastal shipping sector, consistent with its wider economic strategy to grow productivity and national wealth. If the government wishes to then provide support to Australian shipping, it should do so via a separate, discrete industry policy, subject to an appropriate evaluation of its costs and benefits. It should not do so by restricting competition in the market and by causing industry to operate inefficiently.

Prioritising an objective for a competitive and efficient coastal shipping market means abolishing the cabotage restrictions in the Act and moving to an open market, as has occurred in New Zealand.

Removing cabotage restrictions will have various benefits. Depending on the particular trade, it will:

- remove excessive and stifling red tape and its associated costs of administration and compliance
- lower shipping costs to users as a result of greater competition
- give users more options in the market for coastal trading services
- give users greater flexibility to manage their businesses efficiently and grow their businesses
- remove the costs of regulatory uncertainty under the present scheme
- provide incentives for the Australian shipping industry to lift productivity and grow sustainably.

These changes can also spur the Australian shipping industry to become more competitive and over time use the advantages of proximity, reliability and service quality to secure shipping business. For the Australian shipping industry to remain viable, it must become globally competitive.

The BCA identified the need for removal of restrictions on competition in the coastal shipping sector in our *Action Plan for Enduring Prosperity* (2013). We consistently called upon the previous government to submit its shipping reforms to the Productivity Commission to assess their wider economic impact. More recently, the Productivity Commission has argued for the "removal of any anti-competitive provisions" in legislation governing coastal shipping.

The BCA recommends the removal of the legislated cabotage restrictions in the Coastal Trading Act to move to an open, globally competitive coastal trading sector, with foreign and Australian vessels continuing to be subjected to all other Australian laws.

Of the three options presented by the government we support, in principle, Option 2: Remove all regulation of access to Coastal Trading and enact legislation to deal with the effects of other Australian laws.

The most important effect of Option 2 would be to remove the right of General Licence holders to contest Temporary Licence shipments. However, given the complexities inherent in identifying and amending other legislation under Option 2, such as the Customs Act, there is the potential risk that reform will be difficult and prolonged.

We therefore recommend the government consider a staged approach to Option 2 that can deliver the desired economic benefits quickly and simply. Taking the quickest and simplest path to removing the cabotage restrictions in the Act is needed to boost competitiveness across the Australian economy.

Under a staged approach to Option 2, the government would first simply repeal those sections of the Coastal Trading Act that give rise to the cabotage restrictions. This should not, of itself, require other Acts to be amended. It should be able to be done by the next repeal day, in the second half of 2014.

The repeal of those sections of the Act would leave the licensing system in place but most of the economic costs associated with contestability would be removed. The provision of information by temporary licence applicants would be both drastically reduced and it should no longer be required in advance of the shipment. Minimal voyage information need only be provided after a shipment has been made.

The government could then reassess whether it continue to proceed with full implementation of Option 2, repeal of the Act, or whether the remaining sections of the Coastal Trading Act might remain in place. This will allow more time to consider the complex interactions of the Act with other legislation. Whether the Act remains might depend on an assessment of whether the Act is of use in facilitating the application of other Australian law or is providing the department with basic information about which ships are engaging in coastal trading.

We also urge the government to immediately explore the potential to make greater use of the Exemptions provision in the Act, where feasible, to provide businesses and regions with immediate relief from higher costs.

We recommend that during this review the government should prioritise the resolution of problems experienced by vessels conducting voyages between an offshore facility and Australian ports, due to the interrelationships between the Coastal Trading Act and Customs Act, as discussed in the options paper.

A full Regulatory Impact Statement should be prepared for any legislative changes so the costs and benefits of ending the current regime are properly evaluated and tested.

An additional issue that should be addressed by this review is application of the Fair Work Regulations 2009 to foreign ships which increases payments to foreign crews and are difficult and costly to implement. These regulations have further raised the cost of shipping for benefits to the local economy that are unclear. We recommend a reassessment of whether this policy is working in the national interest.

Our submission also comments on the implications for removing cabotage on skills development and the supply of shipping services.

## **Key recommendations**

### **Recommendation 1**

Remove the legislated cabotage restrictions in the Coastal Trading Act to move to an open, globally competitive coastal trading sector, with foreign and Australian vessels continuing to be subjected to all other Australian laws.

### **Recommendation 2**

Remove cabotage restrictions by implementing Option 2 (i.e. *Remove all regulation of access to Coastal Trading and enact legislation to deal with the effects of other Australian laws*) in a staged approach as follows:

- Immediately explore the feasibility of providing exemptions to businesses (and regions) that seek to make applications to engage temporary licensed vessels (by using the provision in the Act

where the minister may exempt certain vessels or persons from the application of the Act under Part 3, Section 11).

- Repeal or amend the sections of the Coastal Trading Act that give effect to cabotage restrictions. The sections to repeal or amend are the Objects of the Act and the sections that cover the contestability rights of General Licence holders and the associated information obligations of temporary licence applicants. These changes should be introduced to parliament at the next repeal day, in the second half of 2014.
- The department should then continue to assess whether repeal of the remaining parts of the Act following these changes remains warranted, and if so prepare for the full repeal of the Act. The assessment should identify any associated legislation (e.g. the Customs Act) to be amended or overridden (e.g. state legislation) in order to avoid unintended consequences.

### **Recommendation 3**

Remove unnecessary regulatory barriers to the efficient operation of vessels conducting voyages between an offshore facility and Australian ports.

### **Recommendation 4**

Reassess the merits and reduce the costs associated with the current approach to applying the Fair Work Regulations 2009 to foreign-registered vessels under temporary licences.

### **Recommendation 5**

Undertake a long-term skills needs assessment for the shipping sector in Australia and, if necessary, put in place targeted policies to ensure an adequate supply of skilled professionals for onshore positions in future.

### **Recommendation 6**

The Department of Infrastructure and Regional Development should release updated data on the coastal shipping market at regular intervals so that stakeholders can be fully informed as this reform process proceeds. This may require data transfer from other departments.

## 1. Australia's coastal shipping regulations

This section details key features of Australia's coastal shipping market and the current coastal trading regime.

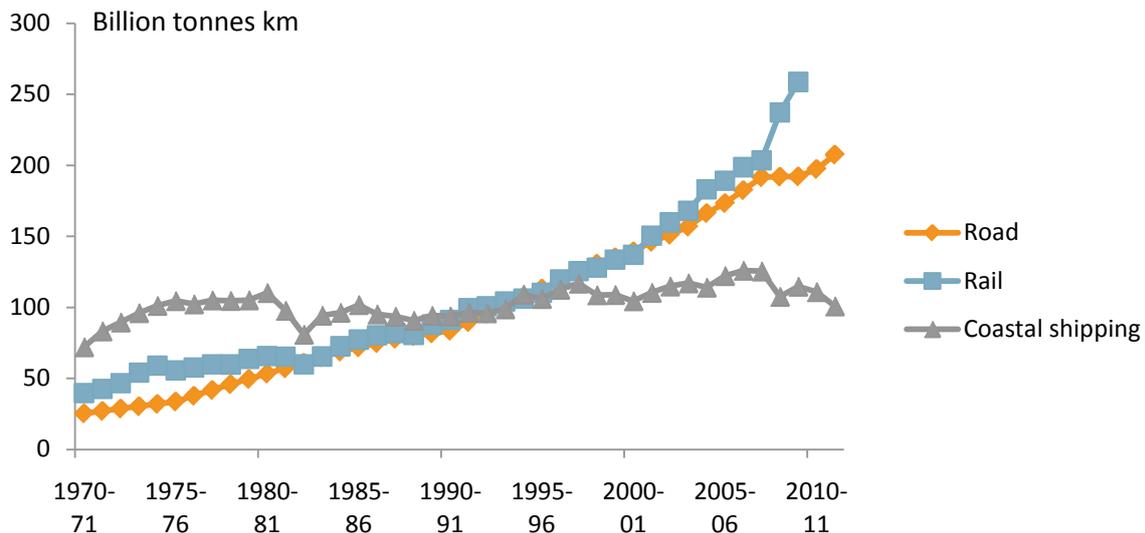
### *The coastal shipping market*

Coastal shipping refers to the interstate carriage of cargo or passengers from a state or territory to another state or territory via water. Intrastate and international voyages are not considered to be coastal trading.

The three main options for moving freight between Australia's states and territories are by road, rail and coastal shipping.

In the early 1970s, over 50 per cent of the domestic freight task was moved by coastal shipping, as measured in billion tonnes kilometres (tonnes loaded multiplied by the kilometres travelled) moved (see Exhibit 1). By 2009–10, due to road and rail freight volumes growing steadily but shipping volumes remaining flat, coastal shipping's share of the total domestic freight task had fallen to around 20 per cent.

### Exhibit 1: Australian Domestic Freight Transport



Source: Bureau of Infrastructure, Transport and Regional Economics, 2013.

In recent years coastal shipping volumes have fallen from a peak of 126 billion tonnes kilometres in 2006–07 to 101 billion tonnes kilometres in 2011–12. For the last year of published data, between 2010–11 and 2011–12, domestic freight moved by coastal shipping in Australia fell by around 10 per cent, or 10 billion tonnes kilometres.

The main commodities carried by coastal shipping are:

- dry bulk freight, such as sugar, cement, fertiliser, alumina, iron ore, bauxite and steel
- liquid bulk freight, such as refined petroleum
- containers and other cargo.

Dry bulk comprises around three-quarters of total coastal shipping freight, up from around 65 per cent 10 years ago. Liquid bulk freight is the next largest commodity, but is in decline. Containers and other cargo make up only a small share of coastal shipping freight as they mainly utilise road and rail transport.

The providers of coastal shipping services are:

- Australian or foreign registered ships that are dedicated to servicing the coastal trading sector (the options paper says that there are currently a total of 45 Australian registered ships that hold general licences and a further 16 foreign registered ships that hold transitional general licences with the same operating rights. At last count in Australia's major coast trading fleet, there were 23 Australia registered vessels (BITRE 2013).
- foreign registered ships visiting Australia on international business that can be available to provide coastal trading services while they are in the region (the options paper says that since the commencement of the Act on 1 July 2012, almost 3,000 voyages have taken place under 86 temporary licences held by 51 organisations).

### ***Australian coastal trading regulations***

Like many other countries, Australia has historically imposed a system of cabotage that provides Australian registered ships with preferential rights to coastal trading services over visiting foreign ships.

In recent years, significant changes have been made to coastal trading regulation in Australia.

- From 1 January 2010, amendments to Fair Work Regulations 2009 extended the application of the Fair Work Act to all workers on foreign vessels operating in Australia's Exclusive Economic Zone.
- The Seagoing Industry Award 2010 replaced the previous award. Part A wages were required to be paid on Australian licensed vessels from 1 January 2010. Part B wages were applied to foreign vessels from 1 January 2011. Previously foreign vessels paid market rates based on International Transport Federation (ITF) wages and conditions.
- In 2012 a new system of regulating access to coastal trading was introduced in the Act 2012 – the main subject of this review.
- An Australian International Shipping Register (AISR) was established and tax concessions introduced to encourage investment in Australian shipping. As with foreign vessels, ships on the AISR do not have preferential rights to coastal trading.

The Coastal Trading (Revitalising Australian Shipping) Act 2012 replaced the previous system for regulating cabotage under the Navigation Act 1912. The old system licensed Australian registered ships to provide coastal trading services. Foreign ships were granted single voyage permit and continuous voyage permits to enable them to also provide coastal shipping services.

The Coastal Trading Act replaced the earlier system with the following licences:

- general licences for Australian registered ships (and Transitional General Licences) that get the rights to carry coastal freight
- temporary licences for AISR and foreign registered vessels to provide services that General Licence holders are unable to fulfil
- emergency licences for AISR and foreign registered vessels to provide services when there are unforeseen events.

The options paper describes the purpose of the licensing system:

A licensing system established by the Coastal Trading Act regulates the activities of Australian and foreign ships and provides an advantage to Australian ships by allowing them unrestricted access to coastal trade along with the opportunity to compete for voyages proposed to be conducted by foreign ships. (Options Paper: Approach to Regulating Coastal Shipping in Australia, p.7.)

**Exhibit 2: Ship Registration and Licensing arrangements under the Coastal Trading Act**

	<b>Australian register</b>	<b>Australian International Shipping Register</b>	<b>Foreign Register*</b>
<b>Licence to allow coastal trading</b>	General licence	Temporary licence	Temporary licence
<b>Restrictions on trading</b>	None	Only if no suitable general licence ship available Licence conditions apply Must be approved by department	Only if no suitable general licence ship available Licence conditions apply Must be approved by department

\*Some foreign registered ships that were licensed to undertake coastal trading under the former regime have a Transitional General Licence. It is expected that these ships will transfer to the Australian General Register.

Foreign vessels visiting Australia, and AISR vessels, must apply to the Department of Infrastructure and Regional Development for a temporary licence to conduct coastal trading. In essence the temporary licensing system works as follows:

- the applicant for a temporary licence provides the department with detailed information on the size of type of freight to be loaded and unloaded at each port on each voyage, with dates
- this information is published on the department's website to give Australian general licensed ships the opportunity to bid for the work
- the minister decides whether to grant the temporary licence taking into account whether or not a General Licence holder can feasibly do the work
- if a temporary licence is granted, then any subsequent variations to the shipping arrangements outside of established parameters must be approved again by the department, with the new information being put back out to the market for a General Licence holder to challenge.

## 2. The problems with Australia's coastal shipping policies

The current licensing system, along with other recent policy changes, imposes costs on shipping users and the wider Australian economy that are reducing the competitiveness of Australian businesses.

Overall, the regime suffers from three key problems.

- Confused objectives: a combination of competition, efficiency and industry development objectives that are in conflict with each other.
- A complex regulatory regime that imposes costs from:
  - higher administration and compliance costs
  - higher shipping costs and rates
  - less supply options
  - inflexibility that doesn't match business needs
  - uncertainty.
- The policy is counterproductive: by making coastal shipping more costly it is less competitive in relation to other transport options. The volume of coastal shipping freight moved continues to fall, as does the number of Australian registered ships engaged in coastal trading.

Examples of the problems with the current regime are provided below based on the experience of businesses using coastal shipping. An assessment of the impacts on the wider coastal shipping market is somewhat limited by the absence of official data from mid-2012 onwards.

### Confused objectives in the Coastal Trading Act

A fundamental problem arises from the confusion between objectives to promote competition and efficiency and objectives to promote industry development. The options paper says that:

The Coastal Trading Act has been drafted to balance the interests of the Australian shipping industry and users of shipping services more broadly.

The economic forces of the Australian shipping industry and shippers do not necessarily align and the current object of the Act has caused uncertainty and confusion about who the Act is supposed to support.

The inconsistency arises particularly where Australian shipping costs and rates are higher than prices charged in the market by foreign ships – yet shipping users can be required to use an Australian vessel.

The six objects in the Act are listed below.

#### Exhibit 3: Objects of the Coastal Trading Act 2012

Section 3(1) of the Coastal Trading Act sets out its objectives:

(1) The object of this Act is to provide a regulatory framework for coastal trading in Australia that:

(a) promotes a viable shipping industry that contributes to the broader Australian economy; and

(b) facilitates the long term growth of the Australian shipping industry; and

(c) enhances the efficiency and reliability of Australian shipping as part of the national transport system; and

(d) maximises the use of vessels registered in the Australian General Shipping Register in coastal trading; and

(e) promotes competition in coastal trading; and

(f) ensures efficient movement of passengers and cargo between Australian ports.

Source: Coastal Trading Act 2012.

To paraphrase the options paper, the conflicts in the objects of the Act are:

- sub-paragraphs 3(1)(a), (e) and (f) have been interpreted as being favourable to shipping users in that they aim to give users access to the most competitive freight rates possible
- sub-paragraphs 3(1)(b), (c) and (d) have been interpreted as being favourable to Australian licensed ships over foreign vessels operating under temporary licences, even if it results in higher costs for shippers.

As discussed earlier, our view is that these conflicts in the Act are the root cause of most of the problems in the licensing regime.

The BCA contends that objectives of the Act should be consistent with Australia's wider national interest. An objective in support of a competitive and efficient market should take primacy over objectives for industry development. Therefore, the cabotage restrictions which give rise to the contestability rights of General Licence holders should be removed from the Act.

If the government wishes to pursue policy objectives in support of Australian shipping, then discrete and transparent policy measures that are subject to a rigorous cost-benefit analysis could be considered. However, industry development objectives should not be pursued by distorting the efficient operation of the coastal trading market.

## Regulation imposes significant costs on the economy

Reflecting the difficulty in framing a regulatory regime to meet two conflicting objectives, the complex rules that sit behind the licensing regime in the Act are imposing significant costs on industry on a number of levels. The feedback from member companies and other stakeholders are that these costs arise from:

- unnecessarily **high regulatory costs** of administration and compliance with regard to temporary licence applications, changes and reporting
- **higher shipping costs** as shipping users either incur additional direct costs themselves, or pay rates in the market for shipping services that are above the efficient cost of service provision, due to the effects of the cabotage regime and the application of the Fair Work Regulations
- **fewer coastal shipping options**, where Australian shippers are unable to access foreign vessels
- **costs associated with inefficient vessel use** due to inflexibilities in the regime that prevent the efficient use of ships in line with business needs
- **costs associated with uncertainty** and delay in the determination of temporary licence applications, because the factors to be taken into account are not settled (in part due again to the conflict in the Act's objectives).

### *Excessive administration costs and red tape*

The temporary licensing reporting and notification requirements, including for licence variances, have created high costs of administration and compliance for business:

- A BCA company estimates that it is incurring over 1,000 extra administration hours a year to comply with the new system.
- Compliance costs for Temporary Licence holders includes the costs of constant monitoring of loading and discharge operations. Higher shipment volumes may require additional person hours to comply with license requirements.
- Businesses are required to comply with temporary licence reporting even if it is clear upfront that there is no Australian registered ship with the capacity to transport the particular freight task.

The application of the Fair Work Regulations to foreign ships is particularly time-consuming and difficult to implement. It is proving to be a complex task to calculate (i.e. base wage including or excluding additional allowances) and monitor the flow of incremental payments to the foreign crew under the regulations. Furthermore, it is unclear if crew members receive the additional pay because payments are made directly to either the shipowner or a third party service provider. The complexities of this regime certainly need to be re-evaluated.

There is unnecessary duplication between Commonwealth and Queensland marine safety laws for intrastate coastal shipping voyages in Queensland. Under Queensland's Transport Operations (Marine Safety) Act 1994, companies compliant with Commonwealth marine safety laws are also required to apply for a Restricted Use Flag licence unless they are covered by the Coastal Trading Act.

### *Coastal shipping costs and market rates have increased*

We are advised of these examples of higher shipping costs due to the current regime:

- Tonnage rates for Australian ships, where there is the right to contest, can be up to double the rates offered by foreign ships for effectively the same service. This can add tens of millions of dollars to the cost base of businesses that use coastal shipping, enough to put the continuing viability of manufacturing activity in Australia at risk. (The rates are commercial in confidence and not able to be published publicly.)
- In one published case, the tonnage rate between Tasmania and Queensland increased from \$18.20 a tonne in 2011 to \$29.70 in 2012, or 63 per cent. This compared with \$17.50 a tonne

being charged by international operators in 2012. Demurrage rates also rose from \$14,000 in 2011 to \$35,000 in 2012.

- One company saw freight charges increase by between \$3,000 to \$3,500 a day up and down the east coast of Australia.
- Some products are more costly to transport around the Australian coast than to transport them from China.
- When challenged by a General Licence holder, one company seeking a temporary licence was faced with a 100 per cent freight cost increase.

There are two key ways the current regime appears to be contributing to these higher shipping costs.

First, the rights of Australian General Licence holders to contest shipments by foreign ships leads to higher costs of Australian shipping being passed through to users and also creates an environment where inflated shipping rates can be charged. The current regime does not create incentives for General Licence holders to reduce costs or to offer competitive rates to shipping users.

Second, higher labour rates on foreign ships apply under the Fair Work Act than was the case several years ago. Foreign vessels are required to pay rates that are above International Transport Federation market rates (Seagoing Industry Award Part B).

In effect, these factors can work in combination. The cabotage arrangements embed higher Australian shipping costs into market shipping rates, with shipping users unable to seek competing offers from lower-cost foreign ships.

In our view overall, the cabotage regime plays the bigger role in raising costs above an efficient rate because it entrenches inefficient work practices and excessive costs of supply and significantly dilutes the incentives for Australian shipping to become more competitive.

The Department of Infrastructure and Regional Development indicates it has rarely disallowed a licence application or variation. However, this should not be taken as a demonstration that the system is in effect 'light-touch' and delivering an open market. For instance, the department is unlikely to be receiving requests for temporary licences where a user knows it will be challenged by a General Licence holder. Some companies paying very high rates report they do not apply for temporary licences under the Act because they would not expect to get approval under the current rules.

#### *Fewer coastal shipping options*

The effect of the right to contest is that Australian coastal trading participants are restricted in their ability to access the wider variety of shipping supply options offered by foreign ships already visiting Australia for other business. In addition, we are advised that some foreign vessels may be deciding not to participate in the Australian coastal trading market due to the complexities of the temporary licensing regime and the application of the Fair Work Regulations.

#### *Regime is inflexible and inconsistent with business needs*

There are many ways in which the current temporary licence scheme operates that is inconsistent with the efficient management of the businesses of shipping users, leading to significant costs on shipping users and inhibiting productivity improvement. Flexibility is critical for many industries where shipments can be delayed by factors outside the control of the shipper, such as the weather, and berth availability.

- The minimum five voyage requirement and 12 month maximum licence period are inconsistent with forward planning practices and limit the ability to adapt to unforeseen circumstances.
- Shippers are being granted approval for a temporary licence, but then if they subsequently make changes to shipments due to unforeseen events they are required to notify the market so a general licensed ship can contest the revised shipment. If successfully challenged it can mean

costly changes to shipping arrangements and also a user may have to compensate a foreign ship that was already commissioned to take the load.

- Shipping users may have to charter more than one vessel to perform a shipment where a General Licence holder successfully challenges for some legs of a journey leaving the temporary licence to cover the other legs.
- Unexpected events such as weather, breakdowns and other delays will lead to the loss of the particular voyage under a temporary licence due to the inflexibility of the current system. Shipment delays can have significant consequences for the receiver of the cargo.
- Under the Coastal Trading Act, temporary licences are not available when shipping from offshore installations to Australian ports. This means vessels are can be treated as imported which has significant implications for the efficient operation of these vessels. We support reforms that would enable certain offshore activities not to be treated as imports as long as they do so at the least cost to business (see Exhibit 4).

#### **Exhibit 4: Coastal trading legislation reduces local employment opportunities in downstream industries**

One BCA member company has encountered unintended consequences of importation due to inconsistency between the Coastal Trading Act and the Customs Act 1901. The inconsistency has resulted in locally produced crude oil being exported rather than being sold and refined domestically, due to uncertainty over the consequences for ships engaging in trade between Floating Production, Storage and Offloading (FPSO) facilities and Australian ports to supply domestic oil refineries. This reduces the availability of crude oil sources for local refineries, resulting in less choice of crude oils and potentially increasing their costs.

The coastal trading legislation has also imposed an unnecessary administrative burden on local companies by requiring administrative procedures that have no policy or operational purpose (i.e. where there are no General Licence vessels to contest voyages). This red tape burden occurs as a result of the variation process and minimum voyage requirement. It also limits the ability of companies to optimise their supply chains to ensure they are as competitive and efficient as possible.

The local oil industry operates in a global marketplace where competitiveness against products imported from foreign refineries is critical.

#### *Regulatory uncertainty*

Considerable uncertainty has emerged around how the decision-making criteria should be applied when determining a temporary licence application. There is currently uncertainty over the matters that the regulator (or 'delegate') should take into account when, say, assessing differences in quoted shipping rates between a local and foreign ship. This question is currently subject to a court dispute. Shipping users therefore take a risk that a decision made by the regulator to approve a temporary licence might be challenged in the courts at a later time.

#### **Distorting markets to 'rebuild' Australian shipping is counterproductive**

Australia's cabotage restrictions have been in place for a long time but have not prevented a steady decline in Australia's coastal shipping industry over many years.

As mentioned earlier, the share of the domestic freight task undertaken by coastal shipping has fallen materially over the last four decades, from around 50 per cent in the early 1970s to around 20 per cent by 2009–10. More recently, the volume of domestic freight moved by coastal shipping fell to 101 billion tonnes kilometres in 2011–12, from a peak of 126 billion tonnes kilometres in 2006–07.

The number of Australian registered ships in Australia's major coastal shipping trading fleet fell by 10 over the last decade to 23 ships in 2011–12 (out of a total of 45 General Licence ships of all sizes). These have been offset by increases in the number of foreign registered ships.

As argued previously, in an increasingly competitive global economy, policies that cause higher costs of using Australian coastal shipping are counterproductive. These policies threaten the long-term viability of the coastal shipping industry itself, as well as manufacturing businesses that use coastal shipping.

There are two alternatives to coastal shipping that are relatively more competitive when coastal shipping costs are high:

- Road and rail become relatively more competitive – and many businesses have already chosen to switch to those transport modes.
- Imported products coming to Australia on low-cost international shipping services become relatively more cost competitive against domestic manufactured goods that use coastal shipping services. This leads to a switch from domestic production to imports, which in turn reduces demand for coastal shipping from the current customer base.

It is wrong to think that in the modern global economy the coastal shipping sector can be shielded from international competition and grow within a protective legislative framework. It is becoming relatively cheaper and easier to import dry bulk products such as sugar, cement, fertiliser and steel than to carry the raw product around the coast and incur the high costs of coastal shipping.

Regional centres are particularly badly affected, as jobs and investment in manufacturing that use coastal shipping as an input are often concentrated in regional centres e.g. Tasmania. There are significant implications for community welfare in regional areas where private industry cannot grow and create jobs, as well as potentially large costs to federal and state budgets to mitigate the negative impacts of unemployment and lower business activity.

### **3. The way forward: a single objective for an open, competitive market**

There is a simple way forward. The primary policy objective for the coastal shipping sector should be to promote an open, globally competitive sector that can provide shipping users with globally competitive shipping rates, and thereby boost productivity and competitiveness throughout the rest of the economy.

It is time to remove cabotage restrictions and move to an open market for coastal trading. If the government wishes to continue to support the development of Australian shipping then it should do so via a discrete industry policy, subject to an evaluation of its costs and benefits. It should also be acknowledged that an open coastal trading market will also provide local industry with incentives to lift productivity to compete with visiting foreign vessels.

Removing cabotage restrictions will:

- remove excessive and stifling red tape and its associated costs of administration and compliance
- lower shipping costs to users through greater competition
- give users more shipping supply options and greater flexibility in how they use shipping to sustain and grow their businesses
- remove regulatory uncertainty under the present scheme.

Arguments for using cabotage restrictions to protect Australian shipping are wrong in principle and do not deliver sufficient benefits to warrant the continuation of these costly regulations. As discussed previously, protecting local shipping via cabotage restrictions doesn't work.

In considering the broader strategic context for ending cabotage restrictions on foreign ships in the following section, the BCA makes the following further arguments in support of reform:

- national economic priorities should override sectoral priorities
- regional development opportunities will be enhanced with more competitive shipping
- removing anti-competitive provisions is consistent with broader government policy – National Competition Policy and red tape reduction

We also reassess some of the wider arguments for security, the environment and economic development put forward in the public debate in support of cabotage restrictions. Some of these arguments may be justify further consideration – however none of them in our view justify restricting competition in the coastal shipping market.

The BCA identified the need for the repeal of restrictions on competition in the coastal shipping sector in our *Action Plan for Enduring Prosperity* (2013) and consistently called upon the previous government to submit its shipping reforms to the Productivity Commission to assess their impact in the national economic interest. More recently the Productivity Commission has argued for the “removal of any anti-competitive provisions” in legislation governing coastal shipping.

We also recommend the government should resolve current problems experienced by vessels conducting voyages between an offshore facility and Australian ports, as discussed in the options paper. The government should consider options not to treat vessels that conduct voyages between ports and certain offshore activities, e.g. crude oil tankers, as imported. Consideration should also be given to developing policy guidelines that would clearly explain what types of vessels and goods are not intended to be imported and so not be treated as imported under Section 68 of the Customs Act 1901.

The practical problems with the application of the Fair Work Regulations which have been discussed earlier should also be addressed by the review. As well as imposing considerable administration costs, there is a widespread view that the current approach is not working in local interests. Moreover, ‘levelling the playing field’ should not be achieved by increasing the costs of foreign ships, but by making Australian ships more competitive. This review should reassess the merits of the current approach and whether it is working in Australia’s interest.

### Exhibit 5: What do independent observers say?

A number of independent observers have looked at this issue from the perspective of community welfare, rather an industry perspective, and have argued for more competition in the coastal shipping sector. The Productivity Commission Inquiry into Tasmanian Shipping and Freight draft report in contemplating the potential benefits from this current review said that:

It is important that this work be expedited with the objective of increasing the competitiveness of Australia's coastal shipping. At a minimum, the review should recommend the removal of any anti-competitive provisions from relevant legislation, unless a clear case publicly demonstrates that there is a net benefit to the community as a whole.

Productivity Commission, *Tasmanian Shipping and Freight, Draft Report*, 2014, p. 20.

Chairman of the Australian Competition and Consumer Commission, Rod Sims, has said recently that:

We need to ask whether the existing protections, involving the need for permits and licences to carry domestic goods between Australian cities and the requirement to pay their crew Australian wages, are worth the cost. This is an even more pressing question when it does not seem economic for Australian shipping even with the current protections in place.

Comments by Rod Sims to the SMART Infrastructure Symposium for Next Generation Infrastructure, 30 September, 2013

The government's Commission of Audit noted that:

Cabotage rules – that preserve freight routes from one Australian port to another for Australian-flagged ships – are effectively industry assistance, increasing costs and reducing competition.

Commission of Audit, *The Report of the National Commission of Audit Phase Two*, March 2013, p. 28.

### The wider strategic case for an open, globally competitive coastal shipping sector

The removal of cabotage restrictions on foreign ships is consistent with the broader national strategic case for economic growth because:

- national economic competitiveness should be the priority
- regional development can be supported
- it is consistent with government policy – National Competition Policy and red tape reduction.

### National economic competitiveness is the priority

Australia's socio-economic goals for increasing national welfare will be best achieved by prioritising policies that lift our competitiveness, creating opportunities for investment, jobs and exports. Economic policies that promote the national interest are preferred over policies that may protect specific sectors of the economy but at the cost to national productivity or the competitiveness of other businesses in the supply chain.

The importance of policy settings that support a competitive, productive national economy and increased income has been highlighted by the OECD, IMF and in the 2014–15 Budget Papers.

- The OECD (2008) noted that Australia is the OECD country most disadvantaged by its distance from world markets...estimating that our relative distance to world markets contributed to a decline in GDP per capita of 10.6 per cent on average between 2000 and 2004 relative to the average OECD country. It found that 'good economic policy will facilitate the adaptation of firms to Australia's geographic advantages and disadvantages.'<sup>1</sup>

1. Treasury, Economic Geography and Economic Performance in Australia, *Economic Roundup*, Issue 3, 2008.

- In its recent statement on Australia, the IMF said that ‘renewed efforts to strengthen competition in labour and product markets as well as to address infrastructure bottlenecks are critical to increase productivity and further diversify the sources of growth.’<sup>2</sup>
- The IMF in its advice to the G20 also highlights that ‘the majority of G20 countries face challenges to varying degrees to open markets, increase competition through less restrictive regulation, and develop support for more efficient long-term investment... Competition in many markets, notably in the services sector, is held back by regulations that restrict activities to the detriment of consumers, users of intermediate products and new innovative firms.’<sup>3</sup>
- The 2014–15 Budget Papers identify the need for faster productivity growth to offset the impacts on income growth from the decline in Australia’s terms of trade and lower labour force participation as a result of an ageing population.<sup>4</sup>

Open competitive markets are the best way to lift efficiency in the coastal shipping sector and reduce input costs to other trade-exposed sectors of the Australian economy. A competitive shipping sector means that, as with any other industry, the main purpose of the sector is to serve the needs of its customers, rather than customers serving the needs of the shipping sector.

A more competitive coastal shipping sector will contribute to achieving Australia’s national economic goals by making other parts of the economy more competitive. Lower shipping costs will make value-adding manufacturing activity more viable in Australia and manufacturing products more competitive on global markets.

Around 90,000 Australians are employed in manufacturing sectors that use coastal shipping, including oil refining and manufacturing, cement manufacturing, steel and aluminium manufacturing.

Australia’s value-adding sectors already face many other substantial cost imposts that put them at a disadvantage relative to their international competitors (e.g. a carbon tax, high \$A, labour rates and conditions) and cannot afford to absorb uncompetitive coastal shipping rates.

Indeed, the long-term sustainability of Australian shipping itself has a better chance of being secured where businesses that use coastal shipping services are themselves viable over time.

### **Regional development can flourish**

Coastal shipping services are mostly used by manufacturing businesses centred in regional centres. The top coastal trading routes are:

- Weipa to Gladstone
- Port Headland to Port Kembla
- Klein Point to Adelaide
- Devonport to Melbourne (BITRE 2013).

The Productivity Commission report on Tasmanian shipping, notes that as an island state, Tasmania’s economy is particularly vulnerable to regulatory changes that increase the cost of engaging in coastal trade. As the government develops its Northern Australia White Paper, the opportunities for a more competitive coastal shipping sector to support growth in Northern Australia should be assessed and promoted.

---

2. IMF Executive Board Concludes 2013 Article IV Consultation with Australia, Press Release No. 14/53, February 12, 2014.

3. IMF, *Macroeconomic and Reform Priorities*, 2014 Paper prepared by IMF Staff with inputs from the OECD and the World Bank, for the February 2014 Meetings of G-20 Finance Ministers and Central Bank Governors.

4. Budget Overview Statement 1, pp. 1–6.

### **Removal of cabotage restrictions is consistent with other government policy**

The removal of cabotage restrictions is consistent with economy-wide policies designed to lift productivity and grow national income.

First, all governments agreed at COAG under the National Competition Policy principles that restrictions on competition must be justified by a net benefit. Indeed, cabotage restrictions should already have been reviewed for their economic impact under National Competition Policy. However, in 2005 the National Competition Council reported that the federal government had not met its competition policy agreement obligations in the area of coastal shipping. This review is a belated opportunity to ensure the principles of national competition policy are applied.

Second, the government's red tape reduction program aims to reduce the costs of red tape by \$1 billion per annum. The removal of cabotage restrictions will mean the end of costly administration and compliance associated with the current scheme and can make a significant contribution to the red tape reduction target.

### **Review of broader arguments for protecting Australian shipping using economic regulation**

A number of broader arguments have been put forward by stakeholders in the general debate for retaining Australia's system of cabotage, so that it is used to grow or retain a considerable Australian shipping industry. The merits of some of these arguments warrant further consideration. Some of the arguments do raise important policy considerations for government and there may be implications for the economy and society that need to be managed should cabotage restrictions be lifted following this review.

Fundamentally, however, we argue that none of these arguments justifies the ongoing preferential trading rights given to Australian ships by law. Where there is a genuine concern that requires a policy response, then the problem should first be made clear. The objectives of government policy should then be designed to address the problem at hand but not create new problems by distorting efficient markets for coastal shipping.

#### *We should leverage our large shipping task to grow a large local industry*

It is argued that some 10 per cent of world shipping freight involves Australia and we should leverage this task to grow our local industry. Strategic objectives to develop specific Australian industries where we may have a comparative advantage can be appropriate, but our industries have to be globally competitive to be sustainable in the long term. A House of Representatives report in 2008 agreed that the Australian shipping sector in the long run must be competitive:

Coastal shipping's competitiveness will then have a direct impact on its sustainability. While initial support might be required to rejuvenate the industry, over the long term coastal shipping services will have to offer available, reliable, timely service with competitive pricing if the sector is to be sustained.

House of Representatives report, p. 11.

The way to do this is through implementing national competition policy, and efficient regulation and taxation coupled with appropriate skills development and infrastructure investment. Removing cabotage restrictions will create the incentives for the local industry to lift productivity and use the advantages of proximity to offer high-quality, reliable services to shipping users. Other natural advantages of Australian shipping may reveal themselves in a more competitive environment.

#### *No other country has opened the coast*

New Zealand has a more liberal regime than Australia, which appears to be working well (see Exhibit 7). The New Zealand experience tells us that cabotage restrictions can be significantly lifted successfully, leading to:

- lower cost shipping
- the ongoing presence of a local shipping industry.

Nevertheless, irrespective of what other countries have done, in principle, the actions by other countries should not be a reason for Australia to withhold important economic reform that improves our competitiveness. This is particularly the case given the competitive challenges we face as a medium-sized economy that is geographically remote from major global markets.

### **Exhibit 7: The New Zealand coastal shipping reforms**

New Zealand partially removed cabotage and deregulated its coastal shipping industry in the 1990s. Under section 198 of New Zealand's Maritime Act 1994, international operators are able to compete with domestic operators on coastal shipping routes as long as they:

- move cargo between New Zealand ports as part of an international journey
- exit New Zealand waters with their crew within 28 days, in compliance with immigration laws
- comply with any other conditions that the minister considers appropriate, such as occupational health and safety.

Since the deregulation of the coastal shipping industry and the simultaneous introduction of labour market reforms:

- coastal shipping freight prices fell dramatically in the 1990s by up to 40 per cent
- New Zealand domestic coastal shipping container rates are cheaper than comparable rail and road rates, although coastal shipping services are slower
- New Zealand's coastal shipping freight task (in billion tonne kilometres) fell by less than a fifth between 1989–90 and 2006–07; over the same period, Australian coastal shipping volumes fell by around a quarter.

While total New Zealand coastal shipping business fell, some domestic operators experienced an increase in their business, in part because of a continuing trend towards 'hubbing'. This is where large international carriers only call at a small number of ports and rely on feeder services to carry cargo to other parts of New Zealand. Also, foreign vessels are unable to provide sufficiently regular local services, especially where links with other transport modes are required.

Source: New Zealand Productivity Commission 2013, Australia's Bureau of Infrastructure, Transport and Regional Economics 2013, Cavana et al 1997.

### *Environmental arguments*

There are claims that foreign ships are more risky to Australia's environment. However, the vast majority of ships plying Australian waters are foreign ships taking goods in and out of Australia. Clearly, these ships need to be regulated to protect the environment, as should any ship that is carrying domestic cargo. So long as appropriate environmental protections are in place that apply to all ships then we do not see that there is an argument for using cabotage restrictions to achieve environmental objectives. The majority of shippers utilising the services of foreign-flagged vessels would also have strict vetting protocols that are adhered to prior to utilising a vessel (i.e. for insurance purposes).

There are also environmental arguments running in favour of removing cabotage restrictions. A more efficient market can lead to lower emissions overall. More optimal utilisation of foreign and local vessels to service Australia's shipping needs means local ships are not required to spend as much time in ballast to reposition around the coast.<sup>5</sup>

5. Submission from the Australian Maritime College to the Department of Infrastructure and Transport, January 2011.

### *Skills development needed for onshore roles*

A reduction in Australian coastal trading ships and crews, should that occur, may reduce the number of Australian sailors who could take up on shore positions such as harbourmasters and pilots, although Australian sailors may also be employed by overseas-flagged ships. This is an issue that will require careful consideration. There are a range of options for ensuring that Australia continues to have access to the necessary skills and experience for both onshore roles, and other shipping-related occupations such as masters of tugs and as pilots.

The review should recommend a long-term skills needs assessment for maritime skills and, should future skills shortages be identified as a problem, recommend targeted policies to ensure a long-term sustainable skilled workforce. Policies may include targeted skills training or changes to temporary and permanent skilled migration policies.

### *Government needs to track foreign ships*

The options paper raised the potential problem that lack of oversight of coastal trading activities would also result in the Australian Government losing visibility of the domestic coastal trade, and could present a challenge to the collection of taxation and other levies. Retaining a light-touch licensing system, as would occur under the staged approach to Option 2 in this submission that includes minimal reporting requirements, may be all that is needed to address this problem. Where shipment information is requested by the department, the reasons should be made clear and the information should generally be collected after the shipping has occurred.

### *There will be risks to supply if we rely too heavily on foreign shipping providers*

We have discussed with BCA members their level of concern on the security of supply following the removal of cabotage restrictions. Those discussions plus other comments made by stakeholders during the forums conducted by the department for this review indicate that this is not expected to be a problem in an open market demand where large numbers of visiting foreign vessels are expected to underpin sufficient supply. Quite possibly reform will lead to an increase in supply options. Furthermore, Australian companies that know their forward tonnage schedules will continue to be able to write long-term contracts with Australian or foreign ships. Nevertheless, to be prudent the department, in collaboration with other government agencies, should monitor availability of supply of shipping in the period following the removal of cabotage restrictions to be sure there are no unintended consequences.

## **Conclusion**

The objective of coastal shipping policy should be for a globally competitive market with no cabotage restrictions in place for any ship that complies with general Australian law – that is, move to an 'open coast'.

The options paper provides stakeholders with three options. We support, in principle, Option 2, which is for the repeal of the Coastal Trading Act. However, given repeal of the Act is potentially complicated and requires other legislation to be amended, a simpler and faster way to deliver the desired benefits of reform may be to adopt a staged approach to Option 2 where repeal of the sections of the Act that give rise to cabotage restrictions is implemented in the second half of 2014.

The impact of the current regime on some businesses is substantial. We urge the government to act quickly to make changes to the Act that will create an open, competitive market for coastal shipping services.

## **Key recommendations**

### **Recommendation 1**

Remove the legislated cabotage restrictions in the Coastal Trading Act to move to an open, globally competitive coastal trading sector, with foreign and Australian vessels continuing to be subjected to all other Australian laws.

**Recommendation 2**

Remove cabotage restrictions by implementing Option 2 (i.e. *Remove all regulation of access to Coastal Trading and enact legislation to deal with the effects of other Australian laws*) in a staged approach as follows:

- Immediately explore the feasibility of providing exemptions to businesses (and regions) that seek to make applications to engage temporary licensed vessels (by using the provision in the Act where the minister may exempt certain vessels or persons from the application of the Act under Part 3, Section 11).
- Repeal or amend the sections of the Coastal Trading Act that give effect to cabotage restrictions. The sections to repeal or amend are the Objects of the Act and the sections that cover the contestability rights of General Licence holders and the associated information obligations of temporary licence applicants. These changes should be introduced to parliament at the next repeal day, in the second half of 2014.
- The department should then continue to assess whether repeal of the remaining parts of the Act following these changes remains warranted, and if so prepare for the full repeal of the Act. The assessment should identify any associated legislation (e.g. the Customs Act) to be amended or overridden (e.g. state legislation) in order to avoid unintended consequences.

**Recommendation 3**

Remove unnecessary regulatory barriers to the efficient operation of vessels conducting voyages between an offshore facility and Australian ports.

**Recommendation 4**

Reassess the merits and reduce the costs associated with the current approach to applying the Fair Work Regulations 2009 to foreign-registered vessels under temporary licences.

**Recommendation 5**

Undertake a long-term skills needs assessment for the shipping sector in Australia and, if necessary, put in place targeted policies to ensure an adequate supply of skilled professionals for onshore positions in future.

**Recommendation 6**

The Department of Infrastructure and Regional Development should release updated data on the coastal shipping market at regular intervals so that stakeholders can be fully informed as this reform process proceeds. This may require data transfer from other departments.

## Appendix A

### Estimates of total ship costs for select voyages

Voyage	Vessel	Total cost for temporary licensed vessels	Total cost for general licence vessels	% difference in crew costs	% difference in total costs
Adelaide to Newcastle	Mini Bulker	\$187,746	\$206,286	61%	10%
Portland to Newcastle	Handysize	\$232,748	\$270,314	99%	16%
Gladstone to Brisbane	Handysize	\$122,480	\$136,529	96%	11%
Birkenhead to Brisbane	Handysize	\$267,782	\$299,894	96%	12%
Mackay to Melbourne	Handysize	\$294,688	\$328,080	99%	11%
Thevenard to Brisbane	Handysize	\$277,691	\$311,083	99%	12%
Newcastle to Bell Bay	Mini Bulker	\$87,389	\$95,816	61%	10%

Source: DAE 2012

## References

- ABS (Australian Bureau of Statistics) 2011, Census of Population and Housing
- Australian Government 2014a, The National Commission of Audit, Phase two, Commonwealth of Australia, March
- Australian Government 2014b, Options Paper: Approaches to regulation coastal shipping in Australia, Commonwealth of Australia, April
- Australian Government 2014c, Budget 2014-15 Overview, Commonwealth of Australia, 13 May
- AMC (Australian Maritime College) 2011, Reforming Australia's shipping – a discussion paper for stakeholder consultation, 17 January
- BCA (Business Council of Australia) 2013, Action Plan for Enduring Prosperity, BCA, July
- Berg C and Lane A, Coastal Shipping Reform: Industry Saviour or Regulatory Nightmare? Institute of Public Affairs, December
- BITRE (Bureau of Infrastructure, Transport and Regional Economics) 2013, Australian Sea Freight 2011-12, August
- Cavana R, Harrison I, Heffernan F and Kissling C 1997, Freight Transport Industry in New Zealand, The Graduate School of Business and Management, Working Paper 2/97, Victoria University of Wellington, New Zealand, April
- DAE (Deloitte Access Economics) 2012, Economic Impacts of the Proposed Shipping Reform Package, February
- House of Representatives Standing Committee on Infrastructure, Transport, Regional Development and Local Government 2008, Rebuilding Australia's Coastal Shipping Industry, October, Canberra
- IMF (International Monetary Fund) 2014a, 2013 Article IV Consultation –Press Release No 14/53, February
- IMF 2014b, Macroeconomic Reform Priorities, Prepared by IMF staff with inputs from the OECD and the World Bank for the February 2014 Meetings of the G-20 Finance Ministers and Central Bank Governors, February 22-23, Sydney Australia
- NCC (National Competition Council) 2005, Assessment of governments' progress in implementing the National Competition Policy and related reforms, 2005, Commonwealth of Australia, October
- New Zealand Productivity Commission 2012, International Freight Transport Services Inquiry, April
- PC (Productivity Commission) 2014, Tasmanian Shipping and Freight, Draft Inquiry Report, Canberra
- Wilkie J and McDonald T 2008, Economic Geography and Economic Performance in Australia, Economic Roundup, Issue 3, Commonwealth of Australia

BUSINESS COUNCIL OF AUSTRALIA

42/120 Collins Street Melbourne 3000 T 03 8664 2664 F 03 8664 2666 [www.bca.com.au](http://www.bca.com.au)

© Copyright June 2014 Business Council of Australia ABN 75 008 483 216

All rights reserved. No part of this publication may be reproduced or used in any way without acknowledgement to the Business Council of Australia.

The Business Council of Australia has taken reasonable care in publishing the information contained in this publication but does not guarantee that the information is complete, accurate or current. In particular, the BCA is not responsible for the accuracy of information that has been provided by other parties. The information in this publication is not intended to be used as the basis for making any investment decision and must not be relied upon as investment advice. To the maximum extent permitted by law, the BCA disclaims all liability (including liability in negligence) to any person arising out of use or reliance on the information contained in this publication including for loss or damage which you or anyone else might suffer as a result of that use or reliance.