

1 June 2017

Essential Services Commission
GPO Box 2605
Adelaide SA 5001
Via Email: escosa@escosa.sa.gov.au

Attn: Mr Stuart Peevor
Manager Pricing and Access

2017 Ports Access and Pricing Review

I refer to the 2017 Ports Access and Pricing Review Draft Report dated May 2017 (Draft Report) and make the following further submissions on behalf of Flinders Ports Pty Ltd (Flinders Ports).

1. Summary

- a) On the basis of the evidence before the Commission, **the access and pricing regulation regimes are unnecessary and should no longer apply** to the regulated port services:
 - There continues to be no evidence of Flinders Ports exercising any alleged market power that it may have;
 - There have been no access or pricing disputes since the regimes commenced in 2001;
 - Flinders Ports will continue to be constrained by countervailing power exerted by sophisticated port users; and
 - Since the commencement of the regimes, significant investment has been made in port-related infrastructure which has assisted in increasing both cargo trades and vessel calls at South Australian Ports.
- b) To the extent that the Commission considers that some form of access and price regulation is still necessary, **the current regimes are appropriate** as they are relatively low cost, provide regulatory certainty and the Commission has significant institutionalised knowledge about their application.
- c) In such circumstances, Flinders Ports seeks further consultation with Commission with the aim of **simplifying the current regimes** for the benefit of operator, users and the Commission itself.
- d) Further, the Commission should **seek re-certification of the regimes** at least 24 months prior to expiration of the current certification to provide regulatory certainty and avoid additional costs.

Flinders Ports also makes a number of further submissions in response to some of the findings in the Draft Report.

2. Continued regulation is unnecessary

Flinders Ports notes that the Commission's draft recommendations are, based on the evidence available, that:

- The current Access Regime should continue for a further five years; and
- That the current Pricing Regime, which takes the form of monitoring and public reporting, continue for a further five years.

Flinders Ports notes that, in relation to pricing, the Commission concludes that there is no evidence to suggest that port operators are exercising market power. This conclusion is supported by the fact that:

1. The GHD Report highlights that port charges in South Australia are competitive (if not generally lower) in comparison with other Australian ports,
2. There is no evidence that Flinders Ports is earning excessive profits, and
3. Over the current regulatory period a range of new commodities have been traded through South Australian ports in addition to the continued positive trend in other trades, without any access or pricing disputes being raised.

Flinders Ports also notes that the market in which Flinders Ports operates is one which is commercially mature and involves port users that are sophisticated commercial entities. These entities usually operate across different regions (largely with no regulatory regimes in place) and are experienced in commercial negotiations.

Flinders Ports accordingly submits that on the evidence that has been presented, the ability to exercise market power by the port operator is in practical reality limited by the nature of the market itself and prevailing commercial pressures.

In relation to both pricing and access, Flinders Ports notes that since the Regulatory Regime commenced in 2001 (i.e. some 16 years) there have been no access or pricing disputes raised. This is against a background whereby, during the period from 2001 to 2016, cargo trades and vessel calls have both increased.

Given the above, Flinders Ports takes the view that the continuation of the access and price regulation regimes is unnecessary. Hence Flinders Ports would propose that the Commission reconsider its draft recommendation, on the basis of the evidence presented in its own reports.

3. If any form regulation is required, the current regimes are appropriate but should be simplified and re-certified

Should the Commission not change its recommendations then Flinders Ports suggests that the existing regulatory model is appropriate for the market, on the basis of its relatively low cost, the Commission's understanding of local requirements and issues and access to the Commission itself. There is no evidence to suggest that the current regulatory framework is inadequate. On that basis Flinders Ports supports the continuation of the current regimes but it further believes that the regimes should be simplified (if able) for the benefit of operator, users and the Commission itself. In this respect, Flinders Ports welcomes further discussion with the Commission on this matter.

Flinders Ports notes that the existing certification, issued on 9 May 2011 for a period of 10 years, is due to expire during the new five year period. If the regulatory environment is to be retained it is critical that clarity exists as to model being applied and the appropriate party to manage this process. If the regimes are to continue then Flinders Ports would request that the Commission put in place the necessary mechanism to arrange an extension to the existing Certification of the Ports Access Regime at least 24 months prior to the expiry of the existing certification. This will provide regulatory certainty for all parties involved and will continue to ensure efficient investments and negotiated agreements. A change to the regulatory regime however will create uncertainty, additional cost and inefficiency.

4. Flinders Ports comments on specific sections of Draft Report

(a) Presence and exercise of market power (3.2)

The Draft Report indicates that there is no evidence of market power being exerted and consequently it would be difficult to recommend further protections than those already afforded under the regimes. Flinders Ports agrees with this conclusion and makes the following observations to support it:

- The Commission ‘notes that Flinders Ports is continuing to expand into port logistics, and therefore further increasing its vertical integration, which may limit the bargaining power of customers’. There is no evidence to suggest that the expansion of the logistics services that the Flinders Port Holdings Group (Group) provides has enabled Flinders Ports to gain leverage over port users. The logistics operation competes for the supply of services in an open market place independent of any access or pricing arrangement. There is evidence that a number of contracts have been awarded to other third party operators with no impact on port pricing or access arrangements.
- Recent announcements associated with two potential new port operations (Lucky Bay and Cape Hardy) strengthen the position put by Flinders Ports that alternative ports (unregulated) are available and the potential for new developments to proceed provide incentive within the market place to adopt reasonable and long term commercial solutions. These alternatives also challenge the view that Flinders Ports has market power.
- The trend towards larger and wider vessels is predominantly related to the container and fuel markets. The use of tug and barge operations continues to provide a competitive port and transport solution particularly to the mining and grain industries (as is the case with the Lucky Bay proposal).
- Port users are generally sophisticated commercial corporate entities which transact in a range of markets and across a number of ports both along the Australian coastline and internationally. It is their knowledge of the market and related pricing outcomes which provides them with strong countervailing bargaining power to negotiated pricing and access arrangements. The outcome of this is reflected in the evidence outlined in the Draft Report.
- The Commission acknowledges that there is a limit that Flinders Ports can charge certain access seekers before a transport solution is unviable. The Commission views this as a ‘ceiling’ price that may vary on a case-by-case basis. Flinders Ports submits that, based on the evidence provided over fifteen years, the prices ultimately charged reflect an ‘agreed’ pricing arrangement and one that sustains both the trade for longer term (as reflected in growing trade volumes over time) and availability of the required port infrastructure and services as provided by the port operator. In the same way that there is no ability to charge monopoly prices to customers given their sophistication and buyer power, there is also no incentive for Flinders Ports to charge monopoly prices because it would risk loss of volume that is required to ensure return on investment over the long term.
- The Commission states that the ability of the port operator to charge a price above the efficient price may still exist and hence is a reflection of the potential to exercise market power. Flinders Ports’ view is that this is not supported by the benchmarking study undertaken by GHD.
- The Commission notes that on review of the Regulatory Accounts there is no evidence to suggest that Flinders Ports is earning super profits. Flinders Ports reaffirms its position that, given the investment made over a long period of time in port infrastructure, and which has additional capacity, there is every incentive to maximise throughput to ensure the efficient use of assets and the long term appropriate return for the investments made.

(b) Access Regime (3.3)

The Commission states that the main direct and observable outcome of a successful access regime will be the presence of commercial access agreements reached between the operator and its customer.

Flinders Ports believes that this outcome is reflective of the commercial maturity of the parties operating within the marketplace and the willingness of the parties to achieve long term outcomes that meet each party’s requirements.

There is no incentive for Flinders Ports to restrict access to its port assets. The investment undertaken and need to ensure a long term sustainable and reasonable return on the investment undertaken provides the foundation to build a pricing and access model that meets the objectives of both port user and port operator.

If the Access Regime is to be retained then Flinders Ports believes:

1. The certification of the regime post 2021 should be pursued well before the expiry date so that the regime can continue with the appropriate level of certainty as to effective jurisdiction and process, and
2. There is no evidence or apparent benefit that has been identified, to propose any argument that an alternative regime should be considered.

(c) Pricing Regime (3.4)

The Commission states that the primary purpose of the Pricing Regime is to protect the long-term interests of port customers by ensuring that prices are fair and reasonable.

The Draft Report provides evidence that:

- Pricing arrangements have been successfully negotiated over a long period of time with no disputes being raised,
- Flinders Ports charges are considered reasonable when compared to other ports, and
- Flinders Ports is not earning super profits from its regulated operations.

Flinders Ports would further argue that this outcome would be the same without the Pricing Regime being in place. This position is supported by the large number of port users that have negotiated pricing below scheduled rates and the fact that no evidence of misuse of market power has been provided over the period since the inception of the Regulatory Regimes.

Flinders Ports would also argue that the provision of relevant information to port users is a fundamental requirement in ensuring that an appropriate and negotiated pricing position is achieved. This would be the case irrespective of whether it is a requirement under the regime or not.

The Commission makes a number of observations in relation to achieving the outcome of “fair and reasonable prices”. Despite the absence of evidence to the contrary, the Draft report states:

“The presence of commercial agreements does not indicate whether or not efficient prices are being charged by the operators.”

“Although a significant number of commercial agreements are negotiated at a price less than the published price it is still possible port operators are earning excessive profits.”

Flinders Ports disagrees with these statements on the basis of the key findings of the GHD Port Price Benchmarking Study as outlined in the Draft Report (Box 3.6) and the review that the Commission undertook of the Regulatory Accounts and outcome reached.

It is noted, therefore, that while the Commission states that the evidence does indicate port charges “appear” to have been fair and reasonable over the current regulatory period, Flinders Ports submits that the evidence strongly supports the position that port charges have **in fact** been fair and reasonable over an extended period of time rather than simply having the appearance of having done so.

The Commission concludes that it is recommending the continuation of a price monitoring regime and requirement of a Price Information Kit.

Flinders Ports proposes that if the regime is to continue, and there are arguments to suggest that it should not, then the existing price monitoring approach is appropriate. Given the on-going relationships that Flinders Ports has with its port user customer base and the access provided to relevant port pricing and services information, the proposal to continue the annual port pricing monitoring reporting is questioned.

Flinders Ports provides supporting documentation to the Commission annually in relation to the proposed price increases and supporting justification. This should be sufficient for the Commission to maintain a “watching brief” over general pricing movements and to monitor the “fairness and reasonableness” of the increases, particularly given that the Commission also has access to the annual Regulatory Accounts. Flinders Ports would therefore contend that the annual review process be extended to five yearly and included within the overall Port Access and Pricing Review process undertaken.

(d) Statewide transport regime (4.1)

The Commission raises the proposal to consider a State-wide transport regime, potentially including the South Australian Rail Access Regime, Tarcoola-Darwin Rail Regime and the Ports Access Regime.

It states that such an approach recognises the fact that many access seekers require access to multiple modes of transport to move their product.

The Commission recommends that the Government examine the costs and benefits of greater integration of transport infrastructure access regimes in South Australia.

The movement of cargo through the port logistics chain include the use of rail, road, intermodal facilities, storage and handling infrastructure and related services. These services and the related infrastructure are provided by a range of providers across both regulated and non-regulated operating environments. In addition with increasing trade volumes there is no evidence of any market failure to suggest that the existing system needs review, or for that matter, any further regulation.

Flinders Ports would not support such a study on the basis that no evidence has been put forward to establish the need for such a study.

(e) Level and type of infrastructure covered by the regimes (4.2)

The Commission states that there is some merit in revisiting the scope of port infrastructure included in the regimes, as supply-chain dynamics and associated infrastructure, change over time.

The port infrastructure, subject to the regimes, has not materially changed over the period that the regimes have been in existence, that is, since 2001. Over this time various upgrades and new developments have been undertaken but the overall port boundaries and land leases have effectively remained the same.

While the wider Group has invested in other port services related assets (such as warehousing facilities, cargo handling equipment, etc.) this investment has been based on specific commercial arrangements agreed with customers or made to ensure that appropriate service levels can be provided and maintained. In many cases this investment has been made on the basis of competitive tender processes and with some element of future risk.

In addition other compliance and regulatory models exist that effectively cover these other services.

Flinders Ports therefore does not support this proposal.

(f) Consistency of services in scope of the regimes (4.3)

Flinders Ports notes the comments made in the Draft Report on this matter.

If the regimes are to continue Flinders Ports would support the notion of maintaining a simplified regime framework moving forward for the benefit of the operator, users and the Commission. It would welcome further discussion with the Commission on this matter to be able to properly assess the likely outcome of this proposed initiative.

5. Conclusion

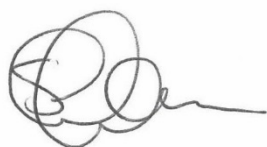
To summarise, Flinders Ports is of the view that:

- (i) There is no evidence of the exercise of market power by the port operator;
- (ii) There are countervailing market forces that diminish the potential to exercise market power outside of or at least in addition to the regulatory regimes;
- (iii) (As has been the case since the commencement of the Access and Pricing Regimes) no disputes have been raised between port user and operator over the current review period;
- (iv) Investment in port-related infrastructure and throughput (cargo trade and vessel calls) have significantly increased since the commencement of the regime; and
- (v) South Australian port charges are fair and reasonable and the port operator has not made super profits over the review period.

In light of the above, Flinders Ports continues to question the on-going need for price regulation and to a large degree the retention of the access regime. If the regimes are retained then these same factors support the position that the regimes should be simplified (if able).

Flinders Ports welcomes the opportunity to respond to the Draft Report and would be happy to further discuss any matters raised in this submission.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Stewart Lammin', with a stylized, circular flourish at the beginning.

Stewart Lammin
General Manager Flinders Ports