

Chapter 3

The economic impact on 'downstream' industries

3.1 A number of submitters expressed concern that implementation of the coastal trading bills would have a negative economic impact on industries that are reliant on coastal trading. These arguments consisted of two key elements:

- the temporary licence regime will excessively restrict foreign vessels from accessing the coastline and reduce competition in the freight market; and
- the policy intention for shippers to increase reliance on general licence vessels will increase freight rates due to the higher seafarer rates paid on these vessels.

3.2 This chapter will examine the broader arguments presented to the committee on the economic impact on industries that are reliant on coastal trading. In particular, it will examine arguments pertaining to:

- the objects of the bill;
- the policy intention to encourage the use of general licence (GL) vessels; and
- wages and entitlements of seafarers.

3.3 A detailed examination of the regulatory elements of the reform will be discussed further in chapters four and five, particularly submitters' concerns about the operation of the temporary licences (TLs).

3.4 The majority of submitters' views discussed in this and proceeding chapters relate to the Coastal Trading (Revitalising Australian Shipping) Bill 2012 (CT bill). As such, references to 'the coastal trading bill' or 'CT bill' will refer to this bill.

Coastal trading

3.5 The Australian Dry Bulk Shipping Users provided a broad overview of the current scale of coastal trade in Australia:

It is really important to understand the size and the scale of this market that we are talking about when we are talking about coastal trade. The current market supports 17 Australian vessels that move Australian product around the coast. This is around 70 per cent of the total coastal trading market. So you can see it is quite small. Foreign vessels account for a further 30 per cent of the market, which I assume would be approximately eight shipping vessel equivalents. So we are not talking about a massive market here. It is not the 27,000 international voyages moving product in and out of

Australia. It is a tiny slither of the market of which we are highly dependent on.¹

3.6 The Maritime Union of Australia offered the following explanation on the decline in coastal shipping:

Fifteen years ago, when permits were starting to be abused, we were servicing 95 per cent of our cargo. But then it went to 90, 85 and 80, and now it is 70. What is going to happen if we do not get a curve in that policy and start redirecting back into Australia as a shipping nation and start securing the industry and making fiscal decisions both domestically and internationally is that that 70 per cent will disappear and we will be a country that is completely beholden to an industry that is not Australian. Those percentages are mainly declining because of policy negligence or policy oversight. We believe this suite of legislation addresses that.²

The object of the coastal trading bills

3.7 A number of submitters recommended that clause 3 of the CT bill (Object of Act) should be amended to specifically acknowledge the need to foster the viability of industries reliant on sea freight.³ The Business Council of Australia argued that:

...a key objective of any legislative reform of Australia's shipping industry should be to increase the competitiveness of the coastal shipping market and ensuring globally competitive costs of transporting Australian goods by ship. We have recommended that this objective be made explicit in any legislative reforms being considered.⁴

3.8 CSR Limited, Sucrogen Australia and Sugar Australia argued:

The shipping industry is a service industry to the Australian economy. In the past 30 years the importance of the integrated supply chain has become well understood as part of an internationally competitive environment. Dissecting coastal shipping from the supply chain is likely to lead to a less competitive supply chain for Australian manufacturing or processing industries. It is imperative that...all the ramifications of the Minister's decisions on the supply chain are considered and that this is reflected in the Objects of the Act.

Therefore the Objects should include a clause which reflects the role that the coastal trading framework has in promoting an efficient and effective

1 Ms Margie Thomson, Chief Executive Officer, Cement Industry Federation, *Committee Hansard*, 15 May 2012, p. 24.

2 Mr Paddy Crumlin, National Secretary, Maritime Union of Australia, *Committee Hansard*, 15 May 2012, p. 62.

3 Australian Logistics Council, *Submission 5*, pp 2, 5–7; CSR Limited, *Submission 13*, p. 1; Sucrogen Australia Pty Ltd, *Submission 14*, p. 2; Caltex Australia Limited, *Submission 16*, p. 6; Minerals Council of Australia, *Submission 20*, p. 1; Sugar Australia, *Submission 21*, p. 3.

4 Business Council of Australia, *Submission 6*, p. 1.

and competitive supply chain for Australia's internationally trade exposed industries. The welfare of the coastal shipping industry should not be at the expense of the industries it is there to serve.⁵

3.9 Minerals industry suppliers and customers are responsible for up to half of the bulk cargo (other than containers or break bulk) moved around Australia. The Minerals Council of Australia commented:

Our priority, which is lacking in the Object and provisions of the Bills, is a legislative framework that supports the interest of the consumers of shipping services: flexibility and internationally competitive prices.⁶

3.10 Caltex raised similar concerns to other submitters about the object of the CT bill. It argued that the reforms omit consideration of industries reliant on shipping, and in doing so conflict with one of the objects of the CT bill, paragraph 3(1)(c), to enhance 'the efficiency and reliability of Australian shipping as part of the national transport system'. Caltex argued that:

...the objects of the Bill, and reform package as a whole, should include improving the competitiveness of Australian industry in general and through an internationally competitive coastal shipping industry.

The reform package should consider the competitiveness of industry reliant on shipping by providing internationally competitive incentives to invest in the shipping industry thereby developing a market in which there is an economic incentive for shippers to use Australian flag vessels. If the Government wishes to intervene in the shipping market, the costs should be explicit through concessions to Australian flag vessels rather than hidden through regulatory burdens on other Australian industries.⁷

3.11 The Department of Infrastructure and Transport (the department) argued that the objects of the CT bill does consider the broader Australian economy:

The object of the Bill as set out in clause 3 reflects the Government's policy intent and the Department believes addresses the increase in competitiveness and provision of efficient and cost effective freight solutions. In particular, item (a) in the object identifies the importance of shipping being able to contribute positively to the broader Australian economy. The industry will not be able to make a positive economic contribution if it is inefficient.

It should be noted that the object clause was developed in close consultation with the shipping industry – both ship owners/operators and users.⁸

5 CSR Limited, *Submission 13*, p. 1; Sucrogen Australia Pty Ltd, *Submission 14*, p. 2; Sugar Australia, *Submission 21*, p. 3.

6 Minerals Council of Australia, *Submission 20*, p. 1.

7 Caltex Australia Limited, *Submission 16*, p. 6.

8 Department of Infrastructure and Transport, *Submission 2.1 to the House of Representatives Standing Committee on Infrastructure and Communications*, p. 3.

Amendments in House of Representatives

3.12 The object of the Coastal Trading (Revitalising Australian Shipping) Bill 2012 set out in subclause 3(1) originally stated:

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.

3.13 The object clause of the bill has since been amended with government members of the House of Representatives agreeing to the following coalition amendment:

- (1) Clause 3, page 2 (line 11), at the end of subclause 3(1), add:
; and (e) promotes competition in coastal trading; and
- (f) ensures efficient movement of passengers and cargo between Australian ports.⁹

Encouraging the use of general licence vessels

3.14 As discussed in chapter 1, there has been a decline in Australian registered ships. The Explanatory Memorandum (EM) outlined that this decline is due to the failure of Australian shipping policy to compete with international competitors and 'the regulatory and competitive settings faced by the domestic industry'.¹⁰

3.15 A number of tax incentives have been included within the reform package to counteract the decline in Australian-flagged vessels. In addition, regulatory measures have been included in the reforms to ensure that it 'maximises the use of vessels registered in the Australian General Shipping Register'.¹¹

9 Mr Warren Truss MP, 'Non-government amendment no. 1, Coastal Trading (Revitalising Australian Shipping) Bill 2012, http://parlinfo.aph.gov.au/parlInfo/download/legislation/amend/r4784_amend_7d7eac80-0060-43ac-ade0-3918abf6ab56/upload_pdf/12048Truss.pdf;fileType=application%2Fpdf (accessed 6 June 2012); Mr Warren Truss MP, *House of Representatives Hansard*, 31 May 2012, pp 37–39; Votes and Proceedings, House of Representatives, p. 1539.

10 Explanatory Memorandum, Coastal Trading (Revitalising Australian Shipping) Bill 2012, p. 1.

11 Coastal Trading (Revitalising Australian Shipping) Bill 2012, paragraph 3(1)(d) – Object of the Act, p. 2.

3.16 Due to a strong reliance on marine skills and experience, Ports Australia is supportive of the proposed measures to develop Australia's flag fleet. It highlighted that coastal shipping should be encouraged as a viable modal choice and that 'coastal shipping has historically performed about 25 per cent of the total domestic freight task'. It noted therefore, that 'any falling away of this performance could be expected to significantly impact on landside infrastructure, logistics and operations and come at a considerable cost to the economy'.¹²

3.17 It argued, however, that developing Australia's flag fleet should be seen as quite distinct from strengthening the domestic sea freight task:

The objective of strengthening the role of coastal shipping is sometimes perceived as the same as strengthening the role of dedicated national flag shipping in the coastal task. They are distinctly separate issues.

...measures that will unnecessarily restrict the presence of other flags in our coastal trades run the risk of deterring interest from foreign flagged operators shipping freight on the coast where they currently address a significant proportion of the total domestic freight task, while at the same time stimulating little or no Australian flagged presence. What it is imperative to avoid, in our view, is a net effect where the role of coastal shipping in the total domestic freight task diminishes and Australia is left with what amounts to a double policy failure of considerable significance and impact.¹³

The Deloitte report on the economic impacts of the reform

3.18 Shippers of dry bulk commodities have argued that they will be adversely affected by the proposed coastal trading bill on the premise that the use of TL vessels will be phased out entirely over a five year period.

3.19 A number of these organisations formed an informal group, the Australian Dry Bulk Shipping Users (ADBSU), to represent 'industries that are highly dependent on coastal shipping to move dry bulk products'. ADBSU commissioned a report by Deloitte Access Economics (Deloitte) on the *Economic impacts of the proposed Shipping Reform Package*.¹⁴ The key findings of the report was that under the reforms:

- there will be an increase in the cost of coastal shipping, and by extension freight rates of up to 16 per cent;

12 Ports Australia, *Submission 24*, pp 1, 2.

13 Ports Australia, *Submission 24*, p. 3.

14 The companies and industry associations involved include the Cement Industry Federation, CSR, Penrice, Pacific Carbon, the Fertiliser Industry Federation of Australia and the Minerals Council of Australia.

The Business Council of Australia and the National Bulk Commodities Group have also provided in kind support to the Deloitte project.

See Australian Dry Bulk Shipping Users, *Submission 4*, p. 8

- these costs are likely to be borne by the users of coastal sea freight;
- the aggregate impact on Gross Domestic Product (GDP) over the period to 2025 will be between -\$242 million and -\$466 million; and
- an associated loss of employment of up to 200 full time equivalent employees.¹⁵

3.20 While the Deloitte report explored the impacts on the wider dry bulk commodities, it focused particularly on the dry bulk shipping groups that relied heavily on Single Voyage Permit (SVP) and Continuous Voyage Permit (CVP) vessels under the current regime including dry bulk companies that ship soda ash, retort coke, gypsum, fertiliser, cement, clinker and raw sugar.

3.21 The Deloitte report specified that the large majority of Australia's shipping task, the producers of bauxite, alumina, iron ore, steel products and liquid bulks, 'are far less reliant on vessels operating under temporary licences' and as such are not the focus of the Deloitte analysis.¹⁶ The modelling in the Deloitte analysis assumed that TL vessels' coastal access would be 'severely' limited:

It is suggested that there is an intention of government to severely limit access to the Temporary Licences under the new arrangements. If this were to occur, this would reverse the situation that has occurred over the last 15 years where the granting of SVPs and CVP[s] has been accepted as a necessity to ensure dry bulk cargoes are shipped domestically at competitive prices.¹⁷

3.22 The department argued the Deloitte report had demonstrated a 'misunderstanding' that the bills were intended to limit coastal access for foreign-flagged, TL vessels:

The report asserts that it is the intention of the Government to "severely limit" access to the TL under the new arrangements, potentially removing access altogether.

This is incorrect. The Government is not "closing the coast". Foreign flagged vessels will continue to have a role in coastal shipping. It is understood that Deloitte based its modelling on the assumption that TLs would not be issued after five years.¹⁸

15 Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, p. iii.

16 Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, pp 14, 31.

17 Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, p. 9.

18 Department of Infrastructure and Transport, *Submission 2*, p. 27. See Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, p. 7.

3.23 The Deloitte report seems to indicate this and noted in its discussion on modelling for its economy-wide impacts that:

...it should be noted that these estimates relate solely to the impact of the proposed new licensing regime. While the taxation incentives may influence the rate of uptake of vessel registration under the Australian flag, the assumption here is that temporary permits are progressively restricted over the period to 2015 – consistent with the path adopted in the Regulation Impact Statement.¹⁹

3.24 The ADBSU asserted that the '[Deloitte] report makes the assumptions used very clear. They are very similar to the Scenario D assumptions outlined in the Government's Regulation Impact Statement [RIS]'.²⁰ The RIS based its impact analysis on four assumptions in relation to TLs that:

- Scenario A: there is no replacement of foreign TL ships with Australian ships.
- Scenario B: Australian ships gain an additional 10 per cent of total freight tonnage from foreign TL ships after five years.
- Scenario C: As for scenario B but Australian ships gain 20 per cent of the total freight tonnage in the 'other dry bulk', petroleum products and 'other liquid bulk' sectors.
- Scenario D: Use of foreign ships in the 'other dry bulk', petroleum products and 'other liquid bulk' sectors is phased out altogether over the first five years.²¹

3.25 It was outlined in the RIS that the government does have an intention to 'encourage replacement of foreign ships with Australian ships so some substitution can be expected'. It therefore deemed scenarios B and C to be most realistic and scenarios A and D as 'sensitivity tests of more extreme assumptions'.²²

3.26 The department summarised the findings in the RIS that the 'combined net present value of the economic cost of the package under scenarios B and C to be a gain of between \$40 million and \$150 million'.²³

19 Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, p. 37.

20 Australian Dry Bulk Shipping Users, *Submission 4*, p. 4.

21 Department of Infrastructure and Transport, 'Reforming Australia's Shipping: Regulation Impact Statement', August 2011, p. vi.

22 Department of Infrastructure and Transport, 'Reforming Australia's Shipping: Regulation Impact Statement', August 2011, p. vii.

23 Department of Infrastructure and Transport, *Submission 2*, p. 26.

Transitional general licences

3.27 As discussed in chapter 2, TLs are given restricted access to coastal trading and are limited to a 12 month period. In contrast, GLs are issued for up to a five year period and are given unrestricted access to coastal trading.

3.28 A Transitional General Licence (TGL) must adhere to the same conditions imposed on GL vessels, as specified in clause 21 of the CT bill, including that seafarers working on the vessel are Australian citizens or hold permanent or temporary visas with the appropriate working rights. As per GLs, TGLs pay Seagoing Industry Award (SIA) Part A rates and the period of a TGL is determined by the Minister with a limit of five years.²⁴ A TGL vessel must hold a licence under the current regime. It is similar to a GL vessel with two key exceptions:

- it is not listed on the general register (foreign-registered vessels cannot be listed on the general register); and
- it does not have access to the tax incentives.

3.29 Ports Australia argued that developing Australia's flag fleet should not be considered paramount to, or at the expense of, strengthening Australia's coastal trading task. It therefore emphasised the need for sound transitional arrangements for the reforms:

Our view is that there is a strong national interest in the promotion of coastal seaborne freight and there is a strong risk of failure if this goal were to be subsumed to the prospect that at best may bring one or two Australian ships onto the coast. If dedicated coastal shipping were not to be successful, international lines should not be discouraged or prevented from carrying coastal cargo. In this regard we have suggested more consideration of transitional arrangements.

The members of Ports Australia have strong empathy with the idea of a stronger role for Australian vessels and seafarers in the coastal trades but see the answer lying in the delivery of a competitive Australian shipping industry to which there is an enduring commitment, rather than draconian and cumbersome measures applying to the coast that might stifle that trade.²⁵

3.30 The Maritime Union of Australia asserted that TGLs are a fundamental part of the reforms to assist in balancing the use of Australian and foreign vessels on the coastline and to 'make sure we get that right mix':

24 Explanatory Memorandum, Coastal Trading (Revitalising Australian Shipping) (Consequential Amendments and Transitional Provisions) Bill 2012, p. 11.

The provisions of the Transitional general licences are stipulated in Schedule 2, Part 3 of the Coastal Trading (Revitalising Australian Shipping) Bill (Consequential Amendments and Transitional Provisions) Bill 2012.

25 Ports Australia, *Submission 24*, p. 4.

Nothing is going to happen in five years. They are not going to shut down the rollers so the industry is then in the hands of pure Australian operators. The fundamentals of the package are that transitional licences will balance out the economies of that use of Australian ships, and there is a dynamic connection between those two things... And they [TGL vessels] will still be there, as defined by the legislation, but complementing the use of Australian shipping, not undermining it. That is the big difference.²⁶

....

In five years time there are still going to be transitional licences. They will still be operating closer to TCC rates under part B of the Fair Work Act than part A and they will also be used to supplement and support the use of Australian shipping, not to replace it. This whole [Deloitte] predication was based on the doors coming down in five years time, and there is nothing in the legislation to say that is going to happen. In fact, as I said before, the legislation is based on the transitional licences using foreign ships and foreign crews and maybe Australian international ships—our own version of foreign ships, if you like—that are operating to support the Australian content in the domestic area. So they [Deloitte] do not get it right. They were not paid to get it right; they were paid to make the legislation wrong, in my view.²⁷

3.31 The department confirmed that the assumption in the Deloitte model (that TLs will be phased out over five years) was incorrect. It strongly asserted therefore, that Deloitte's findings on increased wages, and by extension freight rates, were inaccurate and built on false assumptions.²⁸ These arguments will be discussed further below.

Committee view

3.32 The committee considers that the transitional arrangements provided in the coastal trading bills allow for adequate stability during implementation of the shipping reforms. TGLs allow foreign-registered vessels currently engaged in coastal trading to continue to service the industries that are dependent on their services. This approach respects current commercial practices that are in place yet also provides an incentive for these vessels to move to the general register, and full general licences, in order to receive the proposed tax incentives.

3.33 In relation to temporary licences, the committee notes the arguments from the department that the Deloitte report was based on a misunderstanding that temporary licences would not be available after five years. The committee is assured that there is no intention to entirely phase out the use of temporary licences.

26 Mr Paddy Crumlin, National Secretary, Maritime Union of Australia, *Committee Hansard*, 15 May 2012, p. 60.

27 Mr Paddy Crumlin, National Secretary, Maritime Union of Australia, *Committee Hansard*, 15 May 2012, p. 64.

28 Ms Karen Gosling, Executive Director, Surface Transport Policy, Department of Infrastructure and Transport, *Committee Hansard*, 15 May 2012, p. 11.

3.34 The committee recognises that the bills allow for foreign-flagged vessels to have continued access to the coast using temporary licences, albeit restricted access. It notes that vessels using the current permit regime are also subject to certain restrictions, including allowing GLs to nominate for foreign-flagged vessels' trade.

3.35 The committee does acknowledge, however, that submitters deem the proposed regime as more restrictive than the current permit system. These arguments will be discussed further in chapters four and five.

Seafarer wages and entitlements

3.36 The Department of Education, Employment and Workplace Relations (DEEWR) outlined that it had received advice from the Department of Infrastructure and Transport 'that it is not intended that there be any discernable change in the current level of Fair Work coverage under the Bill'.²⁹

3.37 The Department of Infrastructure and Transport (DIT) asserted that the coastal trading bills 'will not change the current coverage of the Fair Work Act' for vessels engaged in coastal trading and 'it is expected that the shipping reform bills will not impact on employment costs for ship owners or operators'.³⁰

3.38 Some submitters were concerned that the policy intention to encourage the use of GL vessels will drive up freight costs due to the higher seafarer rates required on these vessels.³¹

3.39 Under the provisions of the shipping reform package, GL vessels will continue to pay SIA Part A rates, and TL vessels (foreign-registered vessels) will continue to pay SIA Part B rates. Under the current regime permit vessels are also required to pay SIA Part B rates. The Deloitte report outlined the differences in seafarer rates between SIA Parts A and B:

...the Seagoing Industry Award 2010 provides for more generous wages and conditions in Part A than it does in Part B, with this generosity estimated to be in excess of 62%. In light of this, the proposed licensing regime would result in a greater reliance on vessels operating under a General Licence, with associated higher wage costs under Part A of the Award.³²

29 Department of Education, Employment and Workplace Relations, *Submission 3*, p. 3.

30 Department of Infrastructure and Transport, *Submission 2*, p. 16.

31 Shipping Australia, *Supplementary Submission 1*, p. 3; Australian Dry Bulk Shipping Users, *Submission 4*, pp 3, 4; National Bulk Commodities Group, *Submission 10*, pp 8–10; Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, p. 13.

32 Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, p. 9.

3.40 Deloitte stated that seafarers under SIA Part A have more generous entitlements and 'accrue leave at a rate of approximately one day of leave for each day worked in addition to a range of other benefits for eligible employees including handling allowances, disturbance of sleep allowances, meal allowances and study allowances'.³³

3.41 The Deloitte report argued that as a result, vessels operating under SIA Part A have 'operated at some degree of competitive disadvantage to foreign vessels operating on SVPs and CVPs'.³⁴ The RIS acknowledged this disadvantage for Australian-flagged vessels in the current regime:

The current regulatory system requires licensed ships to pay Australian wage rates while carrying coastal cargo. In contrast, ships operating under permit are able to pay their seafarers at international wage rates (consistent with Part B of the Seagoing Industry Award) [with] substantially lower crew costs. The cost differentials can be exacerbated when ships operating on international trading routes, operate incidental Australian coastal voyages, under permit, at marginal cost.³⁵

3.42 The National Bulk Commodities Group (NBCG) provided an example in different rates of pay in a profit and loss statement from one of its members. One line item detailed the four different daily rates paid for employing 12 crew on a particular coastal voyage. An additional line item from the statement projected the adjusted freight costs required (per tonne) in order to 'break-even' under each wage rate paid. These are outlined in Table 3.1 below.

Table 3.1: Example of wage and freight rate assumptions for July 2012

	ITF Market Rates	Aus Part B	Aus Part A	Typical EBA rates
Crew daily rate - Total 12 crew	\$1,494	\$2,764.60	\$4,450.00	\$8,939
Freight rate increase/decrease to break-even	-\$1.75	\$1.05	\$4.76	–

Source: Extract from National Bulk Commodities Group, *Submission 10, attachment 2*, p. 1.

33 Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, pp 7–8.

34 Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, p. 8.

35 Department of Infrastructure and Transport, 'Reforming Australia's Shipping: Regulation Impact Statement', August 2011, p. 19.

The impact of increased seafarer rates

3.43 The Deloitte analysis projected that freight rates could increase as much as 16 per cent under the reforms.³⁶ Some submitters, and Deloitte, outlined some of the options shippers have if faced with increased freight costs including:

- withdrawal of services;
- using alternative modal options;
- import substitution;
- passing costs on to consumers; and / or
- industry absorbing the costs.

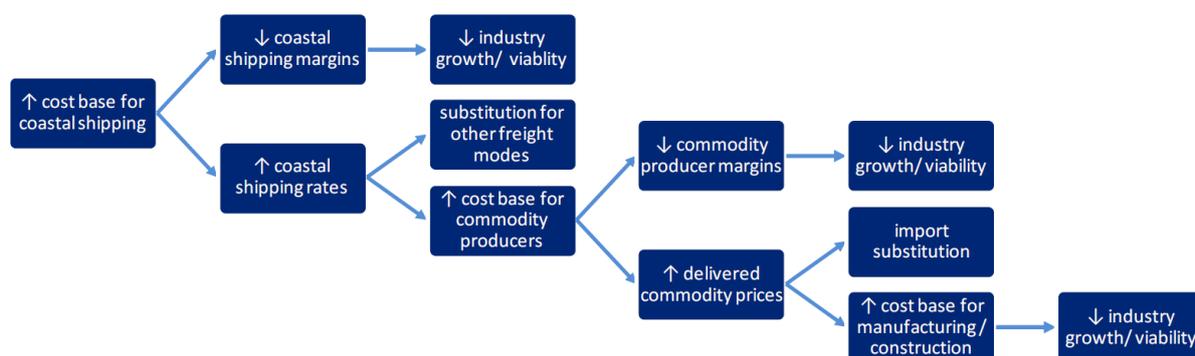
3.44 Shipping Australia specified that the introduction of SIA Part B rates in January 2011 resulted in a substantial increase in the cost of carriage of cargo, and in some cases the withdrawal of services.³⁷ The NBCG foreshadowed the impact of any further increases:

The increases in wage rates (ITF market rates to SIA Part B) resulted in permit vessels increasing their freight rates by approximately A\$5.00 per tonne for a shipper chartering a mini bulker and A\$2.00 per tonne for a shipper chartering a handy size bulker on known domestic voyages of known duration.

The reality of increasing freight rates results in either import substitution becoming more commercially attractive or the gap between seagoing freight rates and road haulage closing – in some cases significantly.³⁸

3.45 Diagram 3.2, taken from the Deloitte report, outlined the potential economic impacts that Deloitte suggests could flow-on to the dry bulk shipping industry as a result of an increased 'cost base for coastal shipping'.

Diagram 3.2: Overview of the economic flow-on



36 Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, pp iii, 13.

37 Shipping Australia, *Supplementary Submission 1*, p. 3.

38 National Bulk Commodities Group, *Submission 10*, p. 8.

Source: Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, p. 30.

Withdrawal of services

3.46 Deloitte noted that the impacts of the reforms 'rest heavily on the commercial decisions of a range of industry players' which makes precise determinations difficult.³⁹ However, the committee has received some early indication from Sucrogen Australia Limited that the molasses market may be forced to export offshore under the reforms:

The balance of north Queensland molasses is sold and exported through a single desk entity, Australian Molasses Trading which is managed under contract by Sucrogen. The molasses business is highly trade exposed. A Bill which has the effect of driving up the cost of coastal shipping will force a potential re think of where this product is sold. All Australian molasses could be exported into existing global markets in preference to supplying domestic markets. This could cause the Australian market to import molasses in cheaper international vessels. There is no benefit to the shipping industry from this legislation if higher coastal shipping costs encourage a change in trade flows from domestic to international.⁴⁰

Alternative modes of transport

3.47 The Australian Logistics Council (ALC) submission cited government figures that around 25 per cent of the domestic freight task (on a per kilometre basis) is carried by ships. ALC highlighted that choice of transport mode within the freight sector is dependent on a number of factors:

...including price, timeliness and reliability, availability (frequency) and flexibility of service, suitability of mode for product and pick-up and delivery times falling within preferred windows of time for transport customers.⁴¹

3.48 Taking this into consideration, the Deloitte report acknowledged that 'it is unclear to what degree these modes of transport [rail and road freight] provide a competitive and practical alternative to coastal bulk freight'.⁴²

For each of the commodities and freight routes included in the analysis, the cost of road or rail freight was higher than the cost of shipping – even after the 10 to 16 per cent increase – or was not an option due to location etc (e.g. for those freighting commodity out of Tasmania to other states). As

39 Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, p. v.

40 Sucrogen Australia Pty Ltd, *Submission 14*, p. 1; see also Sugar Australia, *Submission 21*, p. 1.

41 Australian Logistics Council, *Submission 5*, p. 5.

42 Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, p. 5.

such, intermodal substitution is not regarded as an option for managing the freight cost increase for these commodity producers.⁴³

Import substitution, cost absorption or costs passed on

3.49 Deloitte predicted that should an increase in freight rates occur, due to the rising value of the Australian dollar, a switch to imports was highly likely. It noted that due to thin margins within industry the scope to absorb costs is limited and 'if they are passed through, competitiveness will be diminished'.⁴⁴

For many of the commodities and freight routes included [in] the analysis, the delivered price of competing imports was comparable even before the increase in the delivered price of locally produced product. This is mainly due to the current high exchange rate, which makes imports cheaper, and the current low international shipping rates, which makes the cost of importing goods cheaper. In light of this, the potential for these commodity producers to pass on the cost of the increased freight rate is regarded as minimal and the likelihood of substitution to imports high.

That said, in many cases, the industries' thin margins mean the scope to absorb a cost increase is limited. The ultimate outcome therefore is one where either

- (i) producers absorb cost increases and reduce output (partially or wholly) as production becomes unviable; or
- (ii) increase prices (pass on the cost impacts) to maintain margins.

In the case of the latter, an increase in the domestic prices raises the probability that these intermediate commodities will be imported rather than supplied domestically. As the discussion throughout other parts of this report notes, the scope of import substitution is in many instances high.⁴⁵

3.50 The NBCG commented on the impact of a potential wage increases, and by extension freight rate increases. It emphasised the potential impact on smaller dry bulk shipping users and further highlighted the likelihood of import substitution under the reforms:

These increases would flow-through to freight rates with the knock-on effect of making import substitution competitive leading to an outcome of fewer Australian registered ships undertaking coastal transport tasks and a significant loss of jobs in dry bulk manufacturing sites and within locally based ship-management offices, which employ administrative and technical personnel...

43 Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, p. 34.

44 Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, pp iv–v.

45 Deloitte Access Economics, 'Economic impacts of the proposed Shipping Reform Package', February 2012, pp 34–35.

The progression from the use of temporary licensed vessels to general licensed vessels is unacceptable to smaller dry bulk shipping users, because the freight rate adjustment (to accommodate the ship operator's increased crew costs – SIA Part B to SIA Part A) would render their product uncompetitive when benchmarked against their international competitors.⁴⁶

3.51 Mr David Trebeck, Chairman of Penrice Holdings, provided an example of where imports or alternative modes of freight may be considered a preferred, and more economical, option:

Penrice is an Adelaide based company which ships soda ash to other destinations around Australia. We have a preference for using coastal shipping where we can. The economic break-even is at about Newcastle. In other words, if we tried to use coastal shipping to take product up to Queensland it would get knocked off by imports of soda ash from the US, which predominantly fill the Queensland market. The potential development of coal seam gas and the extraction of soda ash out of the water stream is an interesting variant on that, but that is outside today's activities. We can just get product to Newcastle competitively. In fact, we are a bit less than competitive with imports at Newcastle but our customers stay with us because of other aspects of the service, such as reliability.

...

Further south than Sydney, it is cheaper now to send the product by road. From an environmental viewpoint and other factors there are advantages in sending it by ship, we all understand that, but road wins out to Melbourne, for example. That is why the company has a relatively small geographical area that it services by ship, and any action that results in extra costs being loaded onto our coastal shipping providers, existing or new, will reduce that window to the point where we will lose the market. It is as simple as that.⁴⁷

Proposed wage rates maintain existing regime

3.52 The Maritime Union of Australia asserted that the High Court has already found that the shipping industry 'is within the domestic remit of labour regulation and the Fair Work Act'. It highlighted that that this 'was in no way determined by this set of bills... and was put in place by the Fair Work Act and previously the Work Choices act':

There was some confusion about the Deloitte report. They are obviously a very important and pervasively influential group but they do not understand shipping. Some of the things that they were commenting on, in terms of the juxtaposition of costs, had nothing to do with this set of bills. It is

46 National Bulk Commodities Group, *Submission 10*, pp 8–9.

47 *Committee Hansard*, 15 May 2012, p. 29.

something that had previously been determined in labour law in this country.⁴⁸

3.53 The Hon. Anthony Albanese, MP, Minister for Infrastructure and Transport, in an earlier media release, asserted that:

Foreign ships operating on the Australian coast are already required to pay Australian wages and our reforms make no change to this.

It appears the Deloitte modelling commissioned and released today by the Australian Dry Bulk Shipping Users is based on the assumption that this is not currently the case.⁴⁹

3.54 In response to the Minister's statement, the ADBSU emphasised that the Deloitte report does use Australian wages in its modelling and that these wages include higher crewing costs for Australian flagged vessels due to seafarer entitlements:

Following the public release of the DAE report, the Australian Government has incorrectly claimed that the report compares international wages with domestic wages. The Minister has used this incorrect claim as a basis for the Government to dismiss consideration of the DAE report findings.

The Australian wages of the Seagoing Industry Award have been payable to employees operating a coastal voyage under permit since 2011 under the Fair Work Act. As per the Government's Regulation Impact Statement, Australian wages are also used in the modelling of the DAE report.

However, The Government must acknowledge that Australian flagged vessels do face higher crewing costs than international vessels operating on the coast as a result of the 'conditions' outlined in the Seagoing Industry Award that do not apply to foreign vessels.

These conditions include some very generous elements including:

- Approximately one day off for every day worked (including travel from home to port); and
- An additional five weeks annual leave.

These conditions represent expenses that are faced by Australian Flagged vessels only.⁵⁰

3.55 The department reiterated that the modelling for the Deloitte analysis was based on an assumption that access to TL vessels would be phased out over a five year period (forcing a total reliance on vessels paying SIA Part A rates), and that this was

48 Mr Paddy Crumlin, National Secretary, Maritime Union of Australia, *Committee Hansard*, 15 May 2012, p. 57.

49 The Hon. Anthony Albanese, MP, Minister for Infrastructure and Transport, 'Shipping Reforms Will Rebuild Australian Industry', Media release AA033/2012, 14 March 2012.

50 Australian Dry Bulk Shipping Users, *Submission 4*, p. 4.

incorrect. The department informed the committee that the government had no intention to entirely phase out the use of TL vessels:

...there is, as I mentioned before, an assumption that the government intends to phase out temporary licences after a period of five years—that is, arrangements for access for foreign vessels to the coast. This is not correct. There is nothing in the legislation and there has never been anything in the government's policy to that end.

...

Given that the underpinning assumption is that temporary licences will be phased out, the modelling is predicated on the idea that wages will increase between 60 and 100 per cent, which is based on moving from part B of the Seagoing Industry Award to part A. That seems to underpin a number of the cost assumptions. We would argue that that starting assumption is incorrect.⁵¹

Committee view

3.56 The committee questions the findings of the Deloitte analysis on increased freight rates and the reduction in competition for industries reliant on coastal trading. The modelling used in the Deloitte analysis is based on a flawed assumption that temporary licences will be entirely phased out within five years. This is incorrect. Under the reforms, coastal trading will remain open to Temporary Licensed vessels.

3.57 The committee emphasises the interlocking nature of the package of bills. It highlights that any economic analysis of the reforms should consider the full suite of bills, including the tax incentives in the package. The Deloitte analysis fails to do this.

51 Ms Karen Gosling, Executive Director, Surface Transport Policy, Department of Infrastructure and Transport, *Committee Hansard*, p. 11.

