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# *A swift authorisation decision in the marine freight industry*

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## ***In brief***

On 28 July 2016, the Australian Competition Tribunal (Tribunal) published the reasons for its decision to authorise the proposed acquisition by Sea Swift Pty Limited (Sea Swift) of certain assets of Toll Marine Logistics' (Toll) marine freight operations in Far North Queensland (FNQ) and Northern Territory (NT).

Authorisation was granted subject to conditions and a section 87B undertaking given by Sea Swift, and commitments given by Toll (together, the Conditions). The Tribunal was of the view that there are likely public benefits that result from the Conditions. The Australian Competition & Consumer Commission (ACCC) opposed the authorisation even with the Conditions on the grounds that the claimed public benefits do not outweigh the anti-competitive detriment. There is unlikely to be an appeal by the ACCC to the Federal Court as no merits appeal is available from the Tribunal's decision to authorise a merger, although there are limited grounds of appeal based on error of law. The key factors in the Tribunal's decision are discussed below. The Tribunal placed considerable weight on the testimonies of the witnesses which included key management of the merger parties, their competitors and consumers.

This is only the second merger authorisation granted by the Tribunal since this regime came into effect in 2007.

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## ***In detail***

### ***Background***

Both Sea Swift and Toll operate marine freight services for delivery of freight by sea to islands and remote coastal communities in FNQ and NT. The cargo included food, fuel, and other goods to businesses, government agencies, and individuals on the remote islands and coastal communities.

Prior to approaching the Tribunal for authorisation, the merger parties had sought informal merger clearance from the ACCC in December 2014. In July 2015, the ACCC announced that it opposed the merger as it was likely to substantially lessen competition in the market by eliminating competition and raising barriers to entry for other freight providers.

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The merger parties applied for authorisation to the Tribunal in April 2016. The merger was considered in the market for scheduled freight services (as opposed to ad hoc or charter services) in FNQ and NT. Sea Swift and Toll are each other's closest competitors in FNQ and NT. There are some smaller operators of freight services, however none operate large full-scale services like the merger parties.

### ***Authorisation Test***

To grant authorisation, the Tribunal applies a 'net public benefit' test. This requires the Tribunal to conduct a balancing exercise to weigh the public benefits likely to result from the proposed acquisition against the anti-competitive detriment arising from any lessening of competition. The Tribunal assessed the net public benefits in the context of the counterfactual which involves an analysis of the future state of competition in the market with and without the proposed acquisition. While the ACCC also assessed the merger in the context of the counterfactual, the Tribunal and the ACCC came to disparate views on the effect on the market without the proposed acquisition. This is discussed further below.

### ***ACCC's Position***

The ACCC in its report to the Tribunal opposed the grant of authorisation on the grounds that the claimed public benefits are minimal and do not outweigh the substantial detriments such that the 'net public benefits' test is not satisfied. The ACCC's concerns were that:

- The merger eliminated competition between the two largest providers (and on many routes they are the only two providers) which would strengthen Sea Swift's position in the market.
- There are high barriers to entry for other providers in competition with a large incumbent.
- While the parties offered undertakings under which Sea Swift would maintain a base level of services and set a cap on price increases, the Conditions have their shortcomings and will not address the advantages of incumbency enjoyed by Sea Swift.

### ***Key factors in Tribunal's decision***

#### ***1. Counterfactual***

Toll stated that due to ongoing losses and insufficiency of volume in the market to service two full-service operators, it would cease providing scheduled services within 60 days if authorisation was not granted and would wind up its operations. While ACCC accepted that Toll would likely exit the market, it disagreed that Toll would exit in 60 days for reasons of profit maximisation and minimising reputational damage caused as a result of disruption to existing large customers. The ACCC was of the view that Toll would likely sell its business as a going-concern or assign its contracts together with selling its vessels along key routes. Further, ACCC was of the view that even if Toll shut down its marine freight business, this would make Toll's assets and customers contestable providing opportunities for new competitors to enter the market.

Based on the testimonies of the witnesses, the Tribunal was of the view that absent the proposed acquisition, Toll would exit in accordance with its intentions and Sea Swift would become the de facto provider in the short-term either by sub-contracting or winning new contracts. This was because the alternate providers had not expressed interest or taken steps to purchase Toll's assets or were not logistically prepared to take on Toll's contracts in the short-term. The Tribunal determined that in the counterfactual, Sea Swift would be the provider to Toll's customers without having any Conditions attached to it.

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## *2. Detriment*

Toll has a lease over wharf facilities on the Gove Peninsula (Gove Lease) which include a public wharf, a heavy-lift wharf and a roll on/roll off landing ramp. Access to the heavy-lift wharf is subject to an existing section 87B undertaking given by Toll.

According to the Tribunal, absent a section 87B undertaking, the Gove Lease would comprise a competitive detriment as Sea Swift would be the only entity able and willing to operate the Gove Lease and would have exclusive control of the roll on/roll off landing ramp. However, as part of its authorisation application, Sea Swift undertook to accept and extend the existing undertaking to the landing ramp with provision for lower prices than currently charged by TML. In light of this, the Tribunal considered that there was no competitive detriment with the proposed acquisition that would not exist without it.

## *3. Public Benefits*

The Tribunal determined that public benefits would accrue from the following Conditions:

- **Transferred Contracts Condition**

This condition prohibits Sea Swift from relying on or giving effect to any exclusivity, rights of first refusal or minimum volume clauses in the contracts transferred to it from Toll.

This condition would make the transferred contracts contestable by Sea Swift's competitors. This benefit would not accrue absent the authorisation as in the counterfactual Sea Swift would enter into contracts with Toll's customers which would likely include terms of exclusivity and rights of first refusal. The testimonies of some customers also indicated that some of the Toll contracts were negotiated after long tender processes and some after a price war between Toll and Sea Swift. This resulted in favourable pricing for the customers. Transferring the existing contracts would maintain the favourable pricing and other terms which these customers wished to retain.

- **Remote Community Service Condition and Price Condition**

Under these conditions, Sea Swift is to maintain minimum level of services and price caps for a period of five (5) years.

The public benefit would be assurance of service and price to the remote communities for five (5) years. While the Tribunal acknowledged that there are limitations to the price cap in that prices can be increased (to take into account CPI and operating costs), this would still provide a degree of price certainty to consumers.

- **Gove Lease**

The Tribunal also determined that the extension of the Gove Lease and lower prices than those currently charged by Toll were benefits which would not accrue without the authorisation.

### ***Role of ACCC***

The decision included some interesting observations on the role of the ACCC in an authorisation proceeding. The Tribunal stated that the role of the ACCC is to 'assist' the Tribunal rather than 'advocating a position'. It also noted that the 'factual findings fatally undermine much of the ACCC's theory of harm'. The Tribunal also noted the difference between 'barriers to entry' and 'costs of entry' stating that 'costs of entry' are those inevitable costs of entry without which entry would not be successful and 'barrier to entry' in one way or another raise rival's costs such that it will be hard to compete. The Tribunal stated that the ACCC had not demonstrated which 'costs of entry' constituted 'barriers to entry'.

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## ***The takeaway***

This authorisation decision is significant for future merger authorisation applications to the Tribunal, and also future merger clearance applications to the ACCC. The Tribunal delivered a decision within three (3) months, whereas the ACCC opposition decision took almost eighteen (18) months under the informal review process. This decision shows the significance and weight put by the Tribunal on fact-finding and testimonies of witnesses representing key parties and stakeholders during the hearing. The Tribunal also challenged the expert reports and evidence where it found that expert reports were guided by the terms of reference and assumptions provided by their engaging party. This case entailed supply of essential commodities to remote areas, and the Tribunal saw public benefit in endeavouring to prevent any disruption arising from Toll's decision to exit the market and to maintain scheduled services to these communities.

This case also shows merit in adopting the Harper Review recommendation of combining the current formal and authorisation merger review processes in order to make consistent the tests applied by both the ACCC and the Tribunal throughout the course of an authorisation application. The ACCC will be able to apply both the SLC and public benefit test in the first instance, and the Tribunal as the appellate body would review the ACCC decision applying the same lens. Under the amended process, the applicant will have the likely benefit of more streamlined and consistent analysis by both the ACCC and the Tribunal, saving the applicant time and costs.

## ***Let's talk***

If you are considering an acquisition, this authorisation decision is a positive step forward, as the Tribunal has shown a willingness to accept public benefit arguments provided they are based on cogent commercial reasons and factual evidence.

At PwC our legal and regulatory team provide stand-alone competition and regulatory advice, and also have the expertise to advise you in all stages of your acquisition. We can advise you on all legal and commercial aspects of your transaction from identifying initial competition issues to obtaining competition approval through to completion not only in Australia, but also in other jurisdictions, particularly in Asia-Pacific.

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