



**A SUBMISSION TO THE
WORKING GROUP ON COMPETITIVE NEUTRALITY
ADVISING THE
NSW MINISTER FOR TRANSPORT SERVICES**

**COMPETITIVE NEUTRALITY ISSUES
ASSOCIATED WITH THE OPERATIONS OF
SYDNEY FERRIES CORPORATION AND
PROPOSED SOLUTIONS**

PREPARED FOR

**BLUE LINE CRUISES
CAPTAIN COOK CRUISES
AND MATILDA CRUISES**

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1. Executive Summary

This submission represents the views of the three major private cruise operators in Sydney Harbour -Blue Line Cruises, Matilda Cruises and Captain Cook Cruises (the Operators).

All three operators are represented on the NSW Government's working group examining the competitive neutrality issues arising from the corporatisation of Sydney Ferries, which is expected to take effect from 1 July 2004 via the *Transport Administration Amendment (Sydney Ferries) Act 2003*. Sydney Ferries is currently a statutory authority.

The working group was established by the NSW Government in response to Parliamentary concerns about anti-competitive effects in the tourist cruise market arising from the *Transport Administration Amendment (Sydney Ferries) Bill 2003*. Parliament expressed concern that these effects may damage the businesses of private cruise operators.

Parliament was concerned about the possible anti-competitive effects because the private tourist cruise industry represents \$250 million to the NSW economy each year and there are over 200 cruise operators on Sydney Harbour offering a range of charter and other services. The Operators and another company called Vagabond Cruises provide the bulk of scheduled cruises and alone employ over 1500 people.

The NSW Government is corporatising Sydney Ferries primarily to assist the organization reduce debt accumulation by improving its commercial focus and capabilities. The *Transport Administration Amendment (Sydney Ferries) Act 2003* provides that the new Sydney Ferries Corporation (SFC) will inherit the functions and services of the former Sydney Ferries, including any other marine or land based transport services that assist its commerciality.

The Operators are not seeking that SFC be restricted from providing any services.

Rather the Operators have asked the NSW Government to ensure that where SFC uses its services to compete with private cruise operators for the delivery of tourist cruises there is a level playing field consistent with the principles of competitive neutrality. In practical terms this means that where SFC operates services in competition with private operators in the market for tourist cruises:

- Those services should be subject to the same wharf access and use charges and other fees imposed by government on private operators of scheduled and charter cruises;
- Pricing of those services should be transparent and reflect total cost of capital and operating expenses as well as avoidable cost;

- SFC should pay taxes or tax equivalents to which the private operators are subject; and
- Private operators and SFC should have equal opportunities for equal wharf signage and advertising on government owned assets.

The Operators consider that in order for SFC to fully comply with competitive neutrality principles these requirements set out above must apply to SFC services that are:

- Scheduled cruises for sightseeing;
- Charter cruises for events and functions; and
- Any other service provided for and/or promoted to tourists. This includes public transport services to the extent that they are marketed and promoted to tourists.

These requirements could apply through legislation or policy commitments by government.

1.1 Application of Wharf Access Charges, Private Sector Costs and Tax Equivalents to Tourist Cruises

One key way for SFC to reduce debt and improve its commerciality would be to maximize the utilization of its ferry fleet each day. This may mean rationalizing and/or changing the nature of its fleet to provide general purpose vessels and/or increasing tourist services in non-peak commuter times.

Currently Sydney Ferries has about 32 vessels, with most only suitable for operation in harbour areas that match their capability. For example, inner harbour ferries cannot be used in the outer harbour. The bulk of its vessel use occurs in peak morning and evening commuter times. In between these times, much of Sydney Ferries fleet remains idle, although it is still required to pay high wages and other administrative costs for the entire day. This compounds the debt accumulation issues associated with Sydney Ferries services.

Sydney Ferries operates three scheduled sightseeing cruises each day to improve the utilization of its inner harbour vessels. Sydney Ferries is also conducting a review to identify whether it should compete in the market for charter cruises.

Sydney Ferries pays \$250 000 to the NSW Waterways Authority for the lease of wharves 2-5 at Circular Quay from which it operates its ferry services, including its scheduled sightseeing cruises. This fee includes the cost of wharf access, and staff, office and

ticketing facilities. This lease fee was arranged privately between Sydney Ferries and the NSW Waterways Authority and was not market tested.

In comparison the Operators pay the NSW Waterways Authority a combined total of \$1 million for their shared use (on a time slot basis) of wharf 6 at Circular Quay from where they operate their scheduled tourist cruises. This includes the cost of wharf access and ticketing facilities. The access charges which the Operators pay was market tested by the NSW Waterways Authority in 2000 through an Expression of Interest process.

Currently, Sydney Ferries prices its scheduled sightseeing cruises below the market rate and is able to take this approach potentially because of cross-subsidization within the State Transit Authority (between Sydney Ferries and Sydney Buses) and within Sydney Ferries.

1.1.1 Wharf Access Charges and Cost Basis for Pricing

The Operators consider that in order to comply with principles of competitive neutrality, SFC's scheduled sightseeing, charter and any other tourist cruise services must, at a minimum, be subject to the following:

- A market tested and transparent charge for wharf access and use, including fees for ticketing;
- Accounting systems that are ring fenced from public transport services and reported separately within SFC and in annual reports;
- Pricing that is based on avoidable costs if the service was not provided; and
- Pricing that is fully distributed and reflects the total cost of capital and operating expenses of vessels used by SFC for tourist cruise purposes, even though those vessels may not be used for those purposes fulltime.

Pricing employed by the Operators reflects the cost of capital and operating costs required to provide vessels and services for scheduled and charter cruises. SFC may argue that because it is using vessels for both public transport and tourist purposes, its pricing should only reflect the proportion of the cost of capital and operating expenses required to provide a tourist service using its vessels.

The Operators consider that this would enable SFC to price tourist products below the market rate because those prices would not reflect the true cost of capital and operating expenses required to provide those services. A level playing field is not achievable if SFC's pricing for tourist cruises is not based on the total costs that private operators bear in operating their vessels for tourist purposes.

1.1.2 Tax Equivalents

On average the Operators combined tax liability each year is about \$8 million. This includes payroll tax, GST, FBT, superannuation requirements, and group tax. This total figure can be higher depending on the level of profit made by each operator.

Section 35N of the *Transport Administration Amendment (Sydney Ferries) Act 2003* enables the Treasurer to exempt Sydney Ferries from the payment of taxes or tax equivalents. In a letter to the Charter Vessel Association dated 2 December 2003, the Minister for Transport Services confirmed that the intention of the Government was to only exempt SFC from paying tax equivalents in relation to not for profit activities.

While the Operators appreciate the policy reasons for this distinction, they submit that where vessels, crew and other inputs are utilized for public transport and tourist services, tax liabilities should reflect the total use of those inputs, not a proportion that may be considered commercial. This is consistent with the approach taken by the Operators in relation to the cost basis for pricing discussed above.

The Operators have this view particularly because, as discussed below, the *Transport Administration Amendment (Sydney Ferries) Act 2003* provides SFC with the power to market and promote its public transport services to tourists and permits it to enjoy exclusive access to the public transport ticketing arrangements that enable it to attract tourists to its public transport services.

1.2 Application of Wharf Access Charges, Private Sector Costs and Tax Equivalents to Public Transport Services

The application of these requirements to services that are public transport services is a contentious issue because public transport services have historically been operated by Sydney Ferries at a loss. In addition, the ability of SFC to improve the commerciality of public transport services would depend on fare increases being approved by the Independent Pricing and Regulatory Tribunal (IPART), which regulates public transport fares.

The Operators consider that the application of these requirements to SFC's public transport services is relevant to the extent that:

- SFC's public transport services are a product that is substitutable for non-dining scheduled cruises operated by the private sector;
- SFC carries tourists on its public transport services;
- SFC has exclusive access to public transport ticketing arrangements by virtue of its

government ownership that permits it to attract tourists to its public transport services;
and

- SFC markets and promotes its public transport services and public transport ticketing arrangements specifically to the tourist market.

1.2.1 Substitutability of Public Transport and Scheduled Tourist Cruises

The Operators consider that public transport services are substitutable for their non-dining scheduled cruises because public transport services offer the same visual experience on Sydney Harbour, are cheaper, and more easily accessible.

In his second reading speech on the *Transport Administration Amendment (Sydney Ferries) Bill 2003*, the Minister for Transport Services confirmed the view that public transport services are substitutable for non-dining scheduled cruises, particularly in the minds of domestic and international tourists.

1.2.2 Tourists Carried on Public Transport Services

The Ministerial Inquiry into Sustainable Public Transport held in 2003 concluded that 60% of Sydney Ferries passengers are tourists, with at least 25% being non-Sydney residents.

Given that Sydney Ferries only operates three scheduled sightseeing cruises per day, it is clear that the overwhelming majority of tourist users of Sydney Ferries services use public transport services for their harbour experience.

In 2002/03 Sydney Ferries carried 13 million people. On the basis of the findings by the Ministerial Inquiry, 8 million of these passengers were tourists, with at least 3.25 million being non-Sydney residents. These figures are relatively constant each year.

In the same period the four major private operators carried about 1.5 million people on their scheduled tourist cruises. These passengers are overwhelmingly non-Sydney residents.

On one construction it is arguable that the market for a tourist cruise on Sydney Harbour is 9.5 million each year, with Sydney Ferries commanding an 84% share of this market.

Government may consider that this approach unreasonably captures Sydney residents choosing a public transport service to travel to Manly or Taronga Zoo for a weekday or weekend outing, and that these users would not normally choose a scheduled cruise offered by a private operator for this purpose.

Leaving aside Sydney residents, another construction may be to combine only non-Sydney residents to identify relative market shares in the tourist cruise market. On this construction the market for tourist cruises is 4.75 million people each year, with Sydney Ferries commanding a 68% market share and the remaining 32% being divided between four major private operators.

In either scenario it is clear that Sydney Ferries public transport services provide it with a significant share of the tourist cruise market.

1.2.3 Public Transport Ticketing Arrangements

Sydney Ferries participates in ticketing arrangements, such as the Sydney Pass, which entitle tourists to combine Sydney Ferries services for a harbour cruise with other public transport travel on State Rail and Sydney Buses services. This kind of tourist pass is distinct from passes available for commuter travel on different public transport modes.

The State Transit Authority (of which Sydney Ferries forms one part) controls access to these ticketing arrangements and has consistently denied the Operators and other private providers, access to the Sydney Pass and similar ticketing arrangements.

The corporatisation of Sydney Ferries will separate SFC from the STA, and potentially import new commercial incentives for STA to provide private operators with access to public transport ticketing arrangements. On the other hand, the *Transport Administration Amendment (Sydney Ferries) Act 2003* permits SFC to inherit all of Sydney Ferries existing ticketing arrangements.

Where government ownership enables SFC to retain exclusive access to public transport ticketing arrangements to promote the tourist use of its public transport and tourist services it is clearly using this access to in compete with the Operators for tourist passengers.

1.2.4 Marketing and Promotion of Public Transport Services to Tourists

Sydney Ferries advertises its public transport and scheduled sightseeing cruises and public transport ticketing arrangements in every major and medium level national and international tourist publication. At working group meetings the Operator have tabled strong evidence that Sydney Ferries marketing is aimed at attracting tourists to its public transport services.

This demonstrates that it is keenly aware of the commercial benefits of advertising its public transport services to tourists.

Where SFC also conducts this kind of advertising it is clearly intending to use its public

transport service to compete in the tourist cruise market.

1.2.5 Possible Solutions

There are various options to ensure that SFC cannot unfairly use its public transport services to compete against the scheduled cruises provided by the Operators.

These include:

- Applying the kind of cost basis pricing to public transport services recommended above for scheduled sightseeing cruises operated by SFC. However, because SFC's fares for public transport services are regulated by IPART, this cannot occur without IPART approval. There are also policy issues, such as the need to maintain the affordability of public transport, to take account of when considering this form of cost basis pricing.

Where cost basis pricing cannot be applied and/or government chooses to not apply general principles of competitive neutrality to SFC's public transport services used to compete in the market for tourist cruises, the Operators consider that at a minimum:

- Private operators and SFC could be afforded equal access on fair commercial terms to public transport ticketing arrangements that enable them to offer to tourists tickets that combine travel on the rail and/or bus network with a scheduled tourist cruise, but not public transport (ferry) services;
- Tickets used by tourists to combine rail and bus travel with scheduled tourist cruises could be prevented from use on public transport services operated by SFC;
- Marketing by SFC in domestic and international tourist publications could be limited to advertising its scheduled cruise, charter or other tourist specific services and related ticketing; and
- Where private operators are not provided equal access to public transport ticketing arrangements available to SFC, then SFC could be prevented from marketing those ticketing arrangements in any domestic or international tourist publication.

1.3 Wharf Signage and Advertising on Government Owned Assets

1.3.1 Wharf Signage

Sydney Ferries is able to advertise its services on all wharves it uses in Sydney Harbour with the use of permanent and attractive signs. This includes promotion of scheduled

sightseeing and public transport services used by Sydney Ferries to compete in the scheduled cruise market.

Private operators are currently only permitted by government agencies owning wharves to advertise their services on these wharves with the use of standard temporary 'A' frame signs that are obviously less elegant and attractive than Sydney Ferries signage.

The operators consider that all competitors in the scheduled cruise market should be governed by the same signage and advertising requirements imposed by government.

1.3.2 Advertising on Government Owned Assets

Sydney Ferries advertises its services on government owned transport and other assets, such as at rail stations and on Sydney Buses. This advertising supports Sydney Ferries promotion of its scheduled cruise and public transport services to national and international tourists in tourism publications discussed above. It also supports its use of its public transport services and related ticketing arrangements discussed above to attract tourists.

Sydney Ferries also advertises its services at bus stops owned and controlled by Sydney Buses in the specific tourist corridors at the Rocks and King Street wharf. These bus stops used by Sydney Buses services such as the Sydney Explorer. Private operators are not permitted to advertise at these stops.

The Operators consider that this kind of advertising may breach competitive neutrality principles where SFC gains access to advertising its services on government assets, particularly public transport assets, without a tender process and the payment of market rates for such advertising.

2. Summary of Recommendations

2.1 Full Compliance with Competitive Neutrality Principles

2.1.1 In order to fully comply with the principles of competitive neutrality Sydney Ferries Corporation should be required to apply to its scheduled cruises for sightseeing, charter cruises and any other cruise service provided for and/or promoted to tourists (including public transport services to the extent they are marketed and promoted to tourists), the following:

- (a) The same rate of wharf access and use charges and other fees imposed by government on private operators of scheduled and charter cruises;
- (b) Pricing of services that is transparent and reflects the total cost of capital and operating expenses for vessel, crew and other inputs;
- (c) Pricing that covers the avoidable cost of those services if they were not provided;
- (d) The same taxes or tax equivalents to which private operators of scheduled and charter cruises are subject.

2.1.2 To ensure a level playing field in the market for tourist cruise services:

- (e) SFC and private operators have equal access to overnight berthing facilities for vessels being used to compete in the scheduled cruise market;
- (f) SFC and any other government agencies with control of wharf signage should be required to provide private operators with equal access to wharf signage used to advertise their tourist cruise services; and
- (g) State Rail, Sydney Buses and any other government agencies with control of assets used for advertising should be required to grant to SFC and private operators equal opportunities, through suitable market mechanisms, to advertise via those assets.

2.1.3 Where the costs of applying the recommendations in 2.1.1 outweigh the benefits, government should at a minimum apply recommendations 2.1.2, 2.2 and 2.3.

2.2 Compliance of Tourist Specific Cruise Services with Competitive Neutrality Principles

In order to comply with the principles of competitive neutrality, Sydney Ferries Corporation should be required to apply to its scheduled sightseeing, charter and any other tourist specific cruise service the following requirements:

- (a) A market tested and transparent charge for wharf access and use, including fees for ticketing facilities;
- (b) Accounting systems that are ring fenced from public transport services and reported separately within SFC and in annual reports;
- (c) Pricing that covers the avoidable cost of those services if they were not provided; and
- (d) Pricing that is fully distributed and reflects the total cost of capital and operating expenses of vessels used by SFC for tourist cruise purposes, even though those vessels are not being used for those purposes fulltime.

2.3 Compliance of Public Transport Services with Competitive Neutrality Principles

In order to minimize the anti-competitive effect of the use by Sydney Ferries Corporation of public transport services to compete in the tourist cruise market the following requirements should be applied:

- (a) Private operators and SFC should be afforded equal access on fair commercial terms to public transport ticketing arrangements that enable them to offer to tourists tickets that combine travel on the rail and/or bus network with a scheduled tourist cruise but not public transport (ferry) services;
- (b) Tickets used by tourists to combine rail and bus travel with scheduled tourist cruises should not be able to be used on public transport services operated by SFC;
- (c) Marketing by SFC in domestic and international tourist publications should be limited to advertising its scheduled cruise, charter or other tourist specific services and related ticketing; and

- (d) Where private operators are not provided equal access to public transport ticketing arrangements available to SFC, then SFC should not be able to market those ticketing arrangements in any domestic or international tourist publication.

3. Background to the Establishment of the Working Group on Competitive Neutrality

3.1 Creation of a New Sydney Ferries Corporation

In early December 2003, the NSW Government introduced into the NSW Parliament the *Transport Administration Amendment (Sydney Ferries) Bill 2003*. The Bill sought to transfer the functions, liabilities and service responsibilities of Sydney Ferries (a division of the State Transit Authority) to a new state owned Sydney Ferries Corporation (SFC).

The Bill was passed by the Parliament before the end of the 2003 without amendment. However parliamentary support for the Bill was subject to the consideration of issues and establishment of processes discussed in section 3.2.

Prior to the passage of the Bill, the State Transit Authority (a government statutory authority) was responsible for delivering bus and ferry services.

The new SFC will be a separate entity from the State Transit Authority and have its own management and Board. It is intended that the SFC will commence operations by 1 July 2004. The primary objectives of the NSW Government in creating the SFC are to:¹

- Provide a management environment in which the commercial and public transport revenue opportunities for SFC can be fully exploited;
- Create new opportunities for SFC to reduce the debt likely to be accumulated in relation to ferry services over time and build a profitable enterprise; and
- Permit the managers of bus and ferry services to focus on their distinct market and service responsibilities.

During his second reading speech supporting his Bill, the Hon Michael Costa, Minister for Transport Services stated that:

*“Sydney Ferries faces an increase in accumulated debt attributed to ferry operations from \$89 million to \$219 million by 2008, and \$413 million by 2013. Average patronage on Sydney Ferries during peak periods is 19 per cent of capacity...The change to Sydney Ferries will put in place a management structure which I believe will better focus on the future challenges facing Sydney Ferries”.*²

¹ The Hon Michael Costa, Second Reading Speech, NSW Parliamentary Hansard, December 3, 2003

² Ibid

The Minister also confirmed that:

*“Sydney Ferries will continue to operate Sydney ferry services, which were provided by State Transit immediately before the commencement of this section. Sydney Ferries may also, in connection with its ferry services, operate other transport services, including bus services. This is to ensure that Sydney Ferries is able to fully exploit the public transport potential of ferry services, and can properly plan for and manage all contingencies.”*³

Because of the projected accumulated debt associated with ferry services and the financial problems SFC would be inheriting from Sydney Ferries, the Minister also declared that:

*“There will continue to be government support for Sydney Ferries. Accordingly, the Government does not propose to seek dividends from Sydney Ferries and therefore excludes Sydney Ferries from the operation of section 20S of the State Owned Corporations Act. It will be a non-dividend paying State-owned corporation, as agreed with Treasury”.*⁴

3.2 Parliamentary Concerns with the Operation of the New Sydney Ferries Corporation

During the parliamentary debate on the Bill the Opposition and several Independent Members of Parliament raised a number of significant concerns with the Bill and its potential anti-competitive effect in the tourist cruise market. These concerns were primarily that:⁵

- The Bill (section 35C) would permit Sydney Ferries Corporation (SFC) to inherit the regular passenger services of Sydney Ferries, which were being promoted to and catering for significant numbers of domestic and international tourists.
- The Bill (sections 35C, 35D and 35E) would provide SFC with the power to operate new transport related or ancillary products and services, including those catering to the tourist market, in competition with private providers of tourist cruise services.
- The Government’s objectives driving the creation of SFC confirmed that the intention of the new entity would be to develop new transport products and services, including in the tourist cruise market, to improve asset utilization and reduce debt.

³ Ibid

⁴ Ibid

⁵ Debate on the Bill by the Hon Michael Gallacher, Reverend the Hon Fred Nile, the Hon Dr Arthur Chesterfield Evans, NSW Parliamentary Hansard December 3, 2003

- Although SFC would be able to compete with private operators in the tourist cruise market, the Bill (section 35N) excluded SFC from the responsibility of paying tax equivalents and dividends.
- In circumstances where SFC was competing with private operators, the Bill did not require SFC to pay the market tested fees and charges to which private operators are subject under NSW government policy for access to wharves, ticketing facilities and other infrastructure.
- The Bill would permit SFC to inherit the existing integrated ticketing arrangements, such as the tourist oriented Sydney Pass, which Sydney Ferries provided in tandem with Sydney Buses and State Rail by virtue of its government ownership, while private operators continued to be excluded from those arrangements under government policy.
- Because the pricing of fares on SFC's services are determined by the Independent Pricing and Regulatory Tribunal (IPART) and set at low levels to encourage public transport affordability, SFC would be able to continue to offer services to tourists at prices well below the market rate.

In his second reading speech on the Bill, the Minister confirmed the concerns of parliamentarians and private industry with respect to the current and future presence of SFC in the tourist cruise market. He said:

“Last financial year Sydney Ferries, at a total cost of \$99.9 million, carried just over 13 million passengers, comprising commuters and local, domestic and international tourists.

*Tourists visiting Sydney often include a trip on a Sydney ferry to see our harbour city. People make a day of it, and every night spent in Sydney means other tourism employment opportunities become available. This all comes very cheaply to those who use Sydney ferries: the average cost per person of every ferry trip is \$7.42 but the average fare is \$2.96. This bill is needed to give Sydney Ferries the direction and focus it needs to build revenue and to manage properly a safe and reliable maritime transport service”.*⁶

To address these widespread concerns an independent MP, the Reverend Fred Nile, sponsored a number of amendments to the Bill on behalf of other parliamentarians. The Government opposed the proposed amendments.

In negotiations on the amendments, it was agreed that Parliament would permit the Bill to proceed following an offer by the Minister for Transport Services to establish a working group to advise him on the competitive neutrality issues and solutions arising in relation to the Bill and the operations of SFC. It was implicit in this undertaking that the

⁶ The Hon Michael Costa, Second Reading Speech, NSW Parliamentary Hansard, December 3, 2003

Government would take action to remedy competition issues arising from the Bill and the operations of SFC that were of concern to private operators.

At the same time the Minister for Transport Services also wrote to the Charter Vessel Association indicating that the intention of the Government was that section 35N of the Bill only exempt SFC from the payment of tax equivalents in relation to not for profit activities.⁷ By implication the Minister was referring to public transport services.

3.3 Establishment and Process of the Working Group

The working group was established in early 2004 and consists of representatives from NSW Treasury, Sydney Ferries, Ministry of Transport, NSW Waterways Authority and private cruise operators including the three operators making this submission (the Operators).

The working group intends to prepare a report for the Minister by 31 March 2004 and has asked for submissions to inform the report.

The Ministry of Transport, which is chairing the working group, has indicated that the report may include:

- Recommendations to the Minister on action to be taken by SFC to address issues agreed by the working group.
- Recommendations to the Minister on action to be taken by other agencies and/or government as a whole to address issues agreed by the working group.
- The identification and discussion of issues over which there is disagreement within the working group.

Recommended Approach to Solutions

While the working group is not a formal competition review of the Bill, the Operators making this submission consider that the report of the working group should provide the first step for immediate or longer term remedial action in relation to agreed competition issues.

In relation to competition issues agreed by the working group that can be immediately addressed by SFC by altering its policies or practices, the Operators consider that this should occur before SFC begins operation on 1 July 2004. This would allow the new SFC Board to be aware of the new parameters in which SFC must operate.

⁷ Letter from the Hon Michael Costa dated 2 December 2003.

Ensuing steps for government in relation to agreed competition issues that require remedial action by another agency or at whole of government level should include a rigorous cost/benefit analysis of any restrictions on competition before any decision is made about the public benefit of these anti-competitive effects. These issues should be grouped together for inclusion in a formal competition review by the National Competition Council.

Where the working group does not agree with competition issues raised by industry representatives, the Operators consider that the Minister should refer these issues to the National Competition Council for independent determination. This would provide certainty for industry that there has been transparent consideration of issues by government agencies participating on the working group.

In the event that the Government does not choose to refer these issues to the National Competition Council for review, the Operators may elect to do so.

4. Tourist Cruise Services

4.1 The Market

A comprehensive definition of a market was provided by the Australian Competition Tribunal in *Re QCMA and Defiance Holdings*.⁸ The Tribunal stated that:

“A market is the area of close competition between firms or...the field of rivalry between them. Within the bounds of a market there is substitution – substitution between one product and another and between one source of supply and another – in response to changing prices. So a market is the field of actual and potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long run, if given the sufficient price incentive. Let us suppose that the price of one supplier goes up. Then on the demand side buyers may switch their patronage from this firm’s products to another...”

The market for tourist cruise services can be distinguished between three primary products. The first two are scheduled cruise services and charter services. These are market segments because they represent different customer requirements and cruise operators develop, market and price distinct products and sometimes utilize different vessels to meet each of these requirements. Scheduled cruises, for example, are primarily utilized by tourists, whereas charter services are generally utilized by a mix of tourists as

⁸ (1976) ATPR 40-012. The Tribunal’s view has been confirmed in a number of key cases such as Trade Practice Commission v Nicholas Enterprises Pty Ltd (No 2) (1979) 40 FLR 83; Trade Practices Commission v Australian Meat Holdings Pty Ltd (1988) ATPR 40-876; and Re AGL Cooper Basin Natural Gas Supply Arrangements (1997) ATPR 41-593.

part of a package holiday as well as local persons, corporations or other organizations seeking a function venue.

A third part of the market relates to public transport services used by tourists. A public transport service is a regular passenger or commuter ferry service which connects one point to another and operates on a route licensed by the Ministry for Transport under the Passenger Transport Act. These services can be considered to be part of the tourist cruise market to the extent that a public transport provider intentionally markets and promotes their commuter services to tourists, and because regular passenger services are substitutable for scheduled cruises in the minds of tourists. These issues are discussed in more detail at 4.1.3.

4.1.1 Scheduled Cruises

4.1.1.1 Private Operators

The market for scheduled cruises can be defined according to those services that are generally marketed to and priced and designed for tourists (whether domestic or international) to enhance their experience in Sydney.

These services are cruises of the harbour that depart and return to the same destination and either do or do not stop at any other wharves during the trip. Scheduled cruises currently include stand alone sightseeing cruises as well as cruises that combine sightseeing with some form of dining experience, such as lunch, coffee or dinner cruises. Other product forms may also be available in the future.

Currently four main private operators provide these kinds of cruises – Blue Line Cruises, Captain Cook Cruises, Matilda Cruises and Vagabond cruises. These operators provide about 20 000 scheduled cruises annually, carrying more than 1.5 million people. Tourism NSW estimates that the value of these services to the NSW economy is about \$250 million each year, depending on international and other events affecting tourism generally.

The scheduled cruises operated by Blue Line Cruises, Captain Cook Cruises, and Matilda Cruises are discussed below to illustrate the dynamics of this market, cruise prices, wharf access fees and other relevant issues.

(a) Blue Line Cruises

Blue Line Cruises operates scheduled cruises that do not stop at any wharves except those from which the cruises depart and return. These wharves are Circular Quay Jetty 6 and King Street wharf for which Blue Line Cruises pays wharf access and ticket license fees to the NSW Waterways Authority. These fees are set at market rates and access to these

wharves is determined by competitive tender amongst private operators. Blue Line Cruises operates five vessels.

<i>Product</i>	<i>Departure/Return Point</i>	<i>Departure Time</i>	<i>Retail Price</i>
Sightseeing	Circular Quay	1000	\$22
Sightseeing	Circular Quay	1100	\$22
Sightseeing	Circular Quay	1200	\$22
Lunch	King Street	1215	\$60 - \$99
Lunch	Circular Quay	1245	\$60 - \$99
Sightseeing	Circular Quay	1300	\$22
Sightseeing	Circular Quay	1400	\$22
Cruise n Cafe	King Street	1430	\$25
Cruise n Cafe	Circular Quay	1445	\$25
Sightseeing	Circular Quay	1500	\$22
Sightseeing	Circular Quay	1600	\$22
Dinner	King Street	1930	\$99 - \$180
Dinner	Circular Quay	2000	\$99 - \$180

(b) Captain Cook Cruises

Captain Cook Cruises operates a mix of sightseeing cruises and dining cruises using nine vessels. Two of its four scheduled sightseeing cruises stop at wharves additional to those from which those cruises depart and return. Two of the seven dining cruises stop at more than one wharf. These wharves, their use and cost of access are described in the table below.

Captain Cook provides the following services:

Sightseeing cruises (15 Departures daily)

<i>Product</i>	<i>Route</i>	<i>Time</i>	<i>Retail Price</i>
Harbour Highlights	Circular Quay (CQ) – Point Piper – Aquarium Wharf - CQ	9.30am, 11.00am, 12.45am, 2.30pm, 4.00pm, 5.45pm, 7.30pm	\$20
Sydney Harbour Explorer	CQ – Watsons Bay – Aquarium Wharf & Cockle Bays - CQ	9.45am, 11.30am, 1.30pm, 3.30pm	\$25
Coffee Cruise	CQ – main harbour - CQ	10.00am, 2.15pm	\$39
2000 Café Cruise	CQ – Shark Island - CQ	10.15am, 3.15pm	\$20

Dining Cruises

<i>Product</i>	<i>Wharves</i>	<i>Time</i>	<i>Retail Price</i>
2000 Buffet Lunch	CQ	12.30pm	\$52-69
2000 Top Deck Lunch	CQ & King Street Wharf	12.30pm	\$52-69
2000 Sunset Dinner	CQ	5pm	\$55-190
2000 Starlight Dinner	CQ	7pm	\$55-190
Sydney 2000 Dinner	CQ	7pm	\$55-190
2000 Sky Deck Gold	CQ	7pm	\$55-190
2000 Opera Dinner	CQ & King Street Wharf	7pm	\$55-190

(c) *Matilda Cruises*

Matilda Cruises operates a range of scheduled and dining cruises using 6 vessels.

Its dining and coffee cruises operate from Circular Quay and King Street Wharf for which it pays wharf access and ticket license fees to the Waterways Authority. These fees are set at market rates and access to these wharves is determined by competitive tender amongst private operators.

Dinning Cruises

<i>Product</i>	<i>Departure/Return Point</i>	<i>Departure Time</i>	<i>Retail Price</i>
Morn Coffee	King Street	1000	\$26
Morn Coffee	Circular Quay	1030	\$26
Lunch	King Street	1215	\$56
Lunch	Circular Quay	1240	\$56
Aftn Coffee	King Street	1500	\$26
Aftn Coffee	Circular Quay	1530	\$26
Cocktail Cruise	Circular Quay	1700	\$25
Cocktail Cruise	King Street	1730	\$25
Cocktail Cruise	Circular Quay	1800	\$25
Cocktail Cruise	King Street	1930	\$25
Dinner	King Street	1930	\$99 - \$125
Dinner	Circular Quay	2000	\$99 - \$125

Other scheduled cruise products are the Rocket Harbour Express Cruise and the Manly Rocket Express Cruise. These scheduled cruises cost an average of \$28 and use a number of wharves, which are subject to varying access fees, although those owned by STA are not subject to any charge.

Sightseeing Cruises

<i>Product</i>	<i>Wharves Used</i>
Rocket Harbour Express Cruise	Sydney Aquarium, Darling Harbour, CQ, Sydney Opera House, Watson's Bay, Taronga Zoo.
Manly Rocket Express Cruise	Sydney Aquarium, Darling Harbour, CQ, Rosebay, Manly East Jetty.

4.1.1.2 Sydney Ferries Corporation

As discussed above, the *Transport Administration Amendment (Sydney Ferries) Act 2003* provides that SFC will inherit the services, fare prices and ticketing arrangements offered and delivered by the former Sydney Ferries.

Currently, Sydney Ferries operates in the scheduled cruise market because it provides dedicated sightseeing cruises in competition with private operators. These cruises operate from wharf 4 at Circular Quay and are described in the table below.⁹

<i>Cruise</i>	<i>Time</i>	<i>Cost</i>
Morning cruise	10.30 am	\$15 per adult and \$7.50 per child
Afternoon cruise	1pm	\$22 per adult and \$11 per child
Evening cruise	8pm	\$19 per adult and \$9.50 per child

Catering, including a bar is provided to passengers on these scheduled cruises and commentary is provided on the harbour sights.

Holders of the Sydney Pass, an integrated public transport ticket available to Sydney Bus and State Rail passengers are entitled to these scheduled cruises operated by Sydney Ferries.

4.1.2 Charter Cruises

Charter cruises are another part of the cruise market. A charter cruise is defined as private vessel hire by a person, corporation, or other organization such as a school. Charters usually cater for specific functions, include catering and extend for about four hours. The pick-up and drops off of passengers usually occurs at the vessel's home berth or a public wharf.

⁹ Sydney Ferries Information Paper considered by the Working Group

As a result there is little opportunity for product substitution between the market for scheduled cruises and charter cruises. That is, a purchaser of a scheduled cruise is generally distinct from a purchaser of a charter cruise.

In this market the four main providers of scheduled cruises compete with about 250 other smaller charter operators.

Sydney Ferries provides charter services and is currently undertaking a review of whether it will increase its charter services in competition with private operators in this market. This review is expected to be complete by 30 June 2004, in time for the commencement of operations by SFC.¹⁰

4.1.3 Public Transport Services

A public transport service is a regular passenger or commuter ferry service which connects one point to another (point to point) and operates on a route licensed by the Ministry for Transport (MOT) under the Passenger Transport Act.

Sydney Ferries is the monopoly provider of regular passenger or ferry services in Sydney Harbour, as part of the State Government's public transport network. Its services are contracted by the MOT.

Matilda Cruises is the only major private ferry operator in Sydney Harbour. It is contracted by the MOT and the National Parks and Wildlife Service to operate the ferry routes discussed in the table below.

<i>Contract Route</i>	<i>Wharves</i>	<i>Times</i>
Darling Harbour - Circular Quay	Pier26 Darling Harbour, Circular Quay West, Casino Wharf, Pyrmont. Harbourside Shopping Center, Darling Harbour.	7 days a week 9.00am to 6.00pm Sun – Thurs 9.00am to 10.00pm Fri – Sat.
Lane Cove - Circular Quay	Circular Quay, North Sydney, Kirribilli, Birchgrove, Greenwich, Northwood, Longueville, Hunters Hill, Lane Cove, Darling Harbour.	5 days a week Mon – Fri, 6.30am to 9.00am, 3.30pm to 7.00pm.
Homebush – Darling Harbour	Homebush, Bayview Park Cape Cabarita, Wosley St, Drummoyne, Darling Harbour.	7.15am and 5.35pm Mon-Fri 5.35pm Sat-Sun.
Shark Island – Circular Quay	Circular Quay Shark Island	All day Saturday & Sunday.

¹⁰ Ibid

Given that these ferry services are licensed under the Passenger Transport Act, there is an intention in regulation and policy that these services are established for the purpose of providing public transport to those persons wishing to commute from one point to another.

However, it is inevitable that non-commuters (ie. domestic and international tourists) may have the opportunity, and choose to travel on public transport for point to point journeys as part of a tourist experience.

5. Competitive Neutrality Issues

The operators making this submission (the Operators) consider that issues of competitive neutrality can only potentially arise where Sydney Ferries is competing with private operators in any of the markets for cruise services described above. This approach is consistent with National Competition Policy, the Competition Principles Agreement and NSW Treasury's Policy Statement on the Application of Competitive Neutrality 2002.

Unless existing anti-competitive issues are addressed, the Operators consider that the new SFC will be able to exploit these unfair advantages that the *Transport Administration Amendment (Sydney Ferries) Act 2003* permits it to inherit.

5.1 How Sydney Ferries Competes In the Tourist Cruise Market

The Operators consider that Sydney Ferries currently competes with private operators in the market for scheduled cruises. Sydney Ferries competes in this market by offering the following products:

- (a) Specific scheduled cruises for sightseeing; and
- (b) Regular public transport (point to point) services that can substitute for non-dining scheduled cruises because services are frequent, safe, high quality and offer the same visual experience; customers choosing this kind of service do not want a dining experience; and the low cost of services makes customers switch easily from privately operated scheduled cruises to ferry services.

Sydney Ferries also currently competes on a small scale in the market for charter services, although the new SFC may increase its presence in this market subject to a review being finalized before 30 June 2004.

The new Board of the SFC is likely to undertake a review of its asset utilization strategies. This review may conclude that SFC's fleet should be reconfigured to assist it provide commuter services at peak times and increased charter and scheduled tourist services at non-peak times.

All the restrictions on competition discussed below would provide SFC with an advantage by virtue of its government ownership in both the market for scheduled cruises and charter cruises. Unless remedied these restrictions may increase the potential for less competition in these markets, as well as the risk that private operators will be damaged to an extent that they are forced to exit the market, reduce investment and/or employment opportunities for the more than 1,500 people they employ each year. This may consequently threaten the viability of a part of the tourist industry contributing

\$250 million to the NSW economy annually.

5.1.1 Specific Scheduled Cruises

It is expected that SFC will continue the current scheduled cruise services offered by Sydney Ferries and potentially expand these services because doing so would assist to maximize the use of its vessels, crew and related assets during non-peak commuter times. The maximization of asset utilization during non-peak commuter time is likely to be an essential element in SFC's debt reduction program. Sydney Ferries currently operates its three scheduled cruises per day for this specific purpose only.¹¹

Given that Sydney Ferries scheduled cruises are priced lower than its private sector competitors, and because it offers catering and commentary and access to the same harbour experience as a private sector cruise, the current Sydney Ferries and potential SFC scheduled cruise product is substitutable for comparable private sector scheduled cruise services.

5.1.2 Regular Public Transport Services

With respect to regular public transport services the operators understand that it is inevitable that these services will naturally attract tourists even where Sydney Ferries does not promote such services to them. The operators understand that the fact that tourists may use Sydney Ferries regular public transport services does not of itself necessarily create competitive neutrality issues. We consider that the same view can be applied to the services of the new SFC.

However we suggest that where Sydney Ferries, the new SFC or any other government agency or government supported tourism body is intentionally and successfully promoting Sydney Ferries or SFC services to tourists in a way that includes by expression or implication regular public transport services, competitive neutrality issues do arise in relation to these services.

Sydney Ferries reports that in 2002/03 it operated 169,344 timetabled services carrying 13 million people.¹² In his second reading speech on the *Transport Administration Amendment (Sydney Ferries) Bill 2003*, the Minister for Transport Services confirmed this number of passengers carried by Sydney Ferries in 2002/03.

Sydney Ferries also reports that in 2002/03 about 48% of passenger traveled on its Manly services, 42% on its Inner Harbour services and 10% on its Parramatta River services, with little variation of these distributions from year to year.¹³

¹¹ Ibid

¹² Ibid

¹³ Ibid

Sydney Ferries maintains that it is unable to reliably disaggregate its passenger numbers into commuters and tourists. However, the Ministerial Inquiry into Sustainable Transport in NSW found that over 60% of Sydney Ferries passengers are tourists, with at least 25% being non-Sydney residents.¹⁴

On the basis of the findings by the Ministerial Inquiry, 8 million of Sydney Ferries passengers in 2002/03 were tourists, with at least 3.25 million being non-Sydney residents. These figures are relatively constant each year.

In the same period the four major private operators carried about 1.5 million people on their scheduled tourist cruises. These passengers are overwhelmingly non-Sydney residents.

On one construction it is arguable that the market for a tourist cruise on Sydney Harbour is 9.5 million each year, with Sydney Ferries commanding an 84% share of this market. In this context the four major private providers share the remaining 16% of tourists choosing a Sydney Harbour cruise each year.

Government may consider that this approach unreasonably captures Sydney residents choosing a public transport service to travel to Manly or Taronga Zoo for a weekday or weekend outing, and that these users would not normally choose a scheduled cruise offered by a private operator for this purpose.

Leaving aside Sydney residents, another construction may be to combine only non-Sydney residents to identify relative market shares in the tourist cruise market. On this construction the market for tourist cruises is 4.75 million people each year, with Sydney Ferries commanding a 68% market share and the remaining 32% being divided between four major private operators.

In either scenario it is clear that Sydney Ferries is a monopoly provider of tourist cruises delivered via its regular public transport services, not its scheduled sightseeing cruises which represent only three cruises by one vessel per day.

The link between tourism and Sydney Ferries regular public transport services is also evident from the high number of Manly services operated by Sydney Ferries, the significant proportion of total passengers using the Manly commuter services each year (48%), and the iconic value of Manly as a tourist destination.¹⁵

Accordingly there are significant opportunities for product substitution between the market for non-dining scheduled cruises and regular public transport services. That is, a purchaser of a non-dining scheduled cruise may substitute that product for the purchase for a regular public transport service and gain the same experience at a lower price. This

¹⁴ Interim Report, August 2003, page 15.

¹⁵ Sydney Ferries Information Paper considered by the Working Group

is likely to be particularly true for non-Sydney residents seeking a harbour cruise experience.

The Minister for Transport Services has confirmed the link between tourism and Sydney Ferries public transport services as well as the substitutability of regular public transport services offered by Sydney Ferries and scheduled cruises offered by private providers, because the former are a cheap way for tourists to cruise the harbour.

He has said that “*tourists visiting Sydney often include a trip on a Sydney ferry to see our harbour city. People make a day of it, and every night spent in Sydney means other tourism employment opportunities become available. This all comes very cheaply to those who use Sydney ferries: the average cost per person of every ferry trip is \$7.42 but the average fare is \$2.96*”.¹⁶

Product substitution of this kind provides Sydney Ferries and the new SFC with significant opportunities for the bulk of its revenue capture. Sydney Ferries reports that in 2002/03 public transport services accounted for 97.1% of its total revenue.¹⁷ On the basis of findings by the Ministerial Inquiry into Sustainable Transport in NSW discussed above, tourists contribute over 60% of the revenue from public transport services.

Given this ease of product substitution and disparity between Sydney Ferries costs and revenue in operating regular public transport services, the Operators expect that the new SFC is likely to continue and potentially further maximize the opportunities for it to operate in the market for scheduled cruises via its regular public transport services. The explicit intention of the Government in corporatising Sydney Ferries is that SFC should build revenue.¹⁸

The extent that Sydney Ferries markets and promotes its regular public transport services and ticketing to the tourist market demonstrates the value of these passengers to its revenue base, and confirms the potential that SFC is likely to maintain and may increase its competitive activity in the tourist cruise market via regular public transport services.

5.2 Marketing and Promotion by Sydney Ferries to Tourist Market

There is substantial evidence that Sydney Ferries intentionally markets and promotes both its scheduled sightseeing cruises and regular point to point public transport services to tourists, in competition with the scheduled cruise products offered by private operators.

This marketing includes advertising ticketing arrangements, such as the Sydney Pass, which it provides in combination with other government owned public transport providers, Sydney Buses and State Rail. Sydney Ferries has exclusive access to these

¹⁶ The Hon Michael Costa, Second Reading Speech, NSW Parliamentary Hansard, December 3, 2003

¹⁷ Sydney Ferries Information Paper considered by the Working Group

¹⁸ The Hon Michael Costa, Second Reading Speech, NSW Parliamentary Hansard, December 3, 2003

public transport ticketing arrangements by virtue of its government ownership and it is these arrangements that support its ability to attract tourists to its public transport services. These issues are discussed in more detail in 5.3.

The level of marketing undertaken by Sydney Ferries reinforces the view of the operators that Sydney Ferries competes in the market for scheduled cruises through its dedicated scheduled cruise services and regular passenger services.

Sydney Ferries markets and promotes its scheduled and regular passenger services in:

- STA specific brochures and material;
- National and international tourism industry publications; and
- Material, publications and guides produced by Sydney tourism bodies to inform domestic and international tourists about experiences in Sydney.

The table below illustrates just some of tourism specific publications in which Sydney Ferries markets and promotes its scheduled cruises and regular passenger services. This is not an exhaustive list but has been compiled in the first instance to inform the working group of the range of promotion by Sydney Ferries to the tourist specific market.

The operators have tabled examples of these publications and others, and the kind of advertising conducted by Sydney Ferries at working group meetings.

<i>Form of Advertising</i>	<i>Publications</i>
Tourist Guides and Maps	<ul style="list-style-type: none"> ▪ This Week In Sydney ▪ Sydney Concierge Map ▪ Tourism NSW Map Guide for Sydney and NSW ▪ Where Magazine ▪ What's On in Sydney ▪ Sydney Cruise Arrivals Guide ▪ Sydney Official Navy Guide ▪ Sydney The Official Guide
Tourism NSW and Tourism Sydney Promotions	<ul style="list-style-type: none"> ▪ "Sydney Uncovered" – Winter Campaign 2003 Magazine included in the Brisbane Sunday Mail and Melbourne Herald Sun. ▪ "G-Rated" Guide included for Foxtel subscribers ▪ Tourism NSW International Travel Planner 2003/04 ▪ Tourism NSW International Airport Postcard Packs for visitor wallets

Advertising in Tourist Specific Brochures Used By Wholesale Inbound Tourist Operators	
<ul style="list-style-type: none"> ▪ Australia Brochures 	<ul style="list-style-type: none"> ▪ Qantas Holidays 2004 ▪ NSW Holidays 2003 ▪ Great Aussie Holidays 2003 ▪ Australian Travel Specialists Explore Sydney ▪ ATS Pacific
<ul style="list-style-type: none"> ▪ New Zealand Brochures 	<ul style="list-style-type: none"> ▪ Air New Zealand Holidays 2004 ▪ Gullivers Holidays 2003 ▪ Go Holidays 2003 ▪ Travelplan Holidays 2003
<ul style="list-style-type: none"> ▪ UK/Europe Brochures 	<ul style="list-style-type: none"> ▪ Australie Tours (French speaking market) ▪ FTI Germany (German speaking market) ▪ Quest Travel UK (UK market)
<ul style="list-style-type: none"> ▪ South Africa 	<ul style="list-style-type: none"> ▪ Go Australia – Holiday Tours ▪ Contiki Holidays
<ul style="list-style-type: none"> ▪ North America 	<ul style="list-style-type: none"> ▪ Newmans Vacations ▪ Qantas Vacations/Jetabout ▪ ATS Tours

5.3 Restrictions on Competition that Support Sydney Ferries Competitive Advantages in the Market for Scheduled Cruise Services

The Operators understand that competitive advantages enjoyed by Sydney Ferries do not contravene competitive neutrality principles unless those advantages arise from restrictions on competition.

In identifying the following restrictions on competition that provide Sydney Ferries with competitive advantages in the market for scheduled cruise services, the Operators have relied on the following assumptions.

- (a) Sydney Ferries competes with private operators in this market because it promotes and operates scheduled sightseeing cruises and public transport services to national and international tourists, and uses ticketing arrangements available to it only as a government owned public transport provider to promote its services to national and international tourists.
- (b) Under the NSW Government's Policy and Guidelines for the Application of Competitive Neutrality:¹⁹
 - The corporatisation of Sydney Ferries requires it to adopt measures that increase the level of competition in the market in which it is operating.
 - The corporatisation of Sydney Ferries requires it to pay the same State and Commonwealth taxes or tax equivalents as its private sector competitors.
 - The corporatisation of Sydney Ferries demands that it is no longer subject to exemptions from any legislation or regulations that it may have enjoyed because of its status as an entity of the Crown or statutory authority.
 - The corporatisation of Sydney Ferries requires it to include in its costs any charges that are applied to private sector organisations providing similar goods and services. Notional costs to be applied by Sydney Ferries Corporation can be generally classed as the cost of capital and taxes and other charges.
 - Competitive neutrality will be achieved if the prices charged by Sydney Ferries for the services used to compete in the market for scheduled cruise services (ie scheduled sightseeing cruises and regular passenger services) at least cover avoidable cost and are consistent with approaches followed by private sector competitors. Avoidable costs are those costs that would be avoided by Sydney Ferries if the good or service were not provided. Competitive Neutrality pricing

¹⁹ NSW Treasury, January 2002

does not have to be applied where Sydney Ferries Corporation can demonstrate that the benefits of introducing competitive neutrality are outweighed by the costs.

- Where Sydney Ferries Corporation prices in the short term at less than fully distributed cost (provided avoidable costs are covered) and engages in loss leader activities, it should only do so in special market circumstances and in a manner that does not contravene Part IV of the Trade Practices Act.

5.3.1 Barriers to Entry

5.3.1.1 Public Transport Ticketing

A key factor in Sydney Ferries ability to attract tourists (domestic and international) to use its scheduled sightseeing and regular public transport services is its access to ticketing arrangements that it shares with State Rail and Sydney Buses as part of the public transport network.

An example of this is the Sydney Pass, which can be purchased at ticketing facilities operated by State Rail, Sydney Buses or Sydney Ferries. The Sydney Pass entitles a passenger on public transport to travel on these three modes for the purposes of commuting to and from work or other purposes.

As part of the Sydney Pass customers can also package the use of Sydney Ferries' scheduled sightseeing cruises, and the Sydney Explorer tourist service operated by Sydney Buses. These features enable Sydney Ferries to use the Sydney Pass to promote its services to tourists.

The Sydney Pass can also be considered a tourist ticket to the extent that it offers tourists with an opportunity to combine public transport travel with a harbour cruise on any of Sydney Ferries regular public transport services.

In the national and international publications in which Sydney Ferries advertises, it promotes the use of the Sydney Pass by visitors wishing to experience a cruise on Sydney Harbour. In these publications the Sydney Pass is linked to Sydney Ferries generic services, which include scheduled sightseeing cruises and regular public transport services. There is no attempt by Sydney Ferries to distinguish between its scheduled tourist cruises and public transport services.

The extent and nature of Sydney Ferries marketing and promotion of the Sydney Pass confirms that Sydney Ferries recognises the commercial value of the Sydney Pass as a tourist ticket used on both its scheduled sightseeing cruises and regular public transport services.

Sydney Ferries only has access to these arrangements because it is a government owned public transport provider. By virtue of its ownership it is able to leverage ticketing arrangements with other government owned monopoly transport providers (eg. State Rail) to promote the use of both its scheduled sightseeing and regular public transport services.

Private cruise operators do not have access to the Sydney Pass or any other combined ticketing arrangement provided by public transport providers. According to government representatives on the working group, the provision of access to the Sydney Pass is the responsibility of the State Transit Authority (STA).

Private cruise operators have previously sought access to the Sydney Pass, which could enable them to offer ticketing products to public transport users seeking a Sydney Harbour cruise. The STA has consistently refused to provide private operators with access to the Sydney Pass or equivalent arrangement.

Accordingly, private providers of scheduled cruises are unable to offer cruise products to public transport users in competition with Sydney Ferries, many of whom as discussed above are national and international tourists.

It is arguable that the STA's previous refusal to grant private providers access to the Sydney Pass was influenced by the fact that Sydney Ferries was an integral part of the STA's business and that private sector access to public transport ticketing arrangements threatened to undermine the commercial benefit to STA and Sydney Ferries arising from such ticketing arrangements. Where STA refused private operators' access to the Sydney Pass because of its commercial value, it is arguable that STA did so because it considered Sydney Ferries a competitor to private cruise operators in the tourist cruise market.

The *Transport Administration Amendment (Sydney Ferries) Act 2003* provides that SFC will automatically inherit these exclusive ticketing arrangements and it is expected that SFC would continue its participation in them because doing so is an integral part of SFC's ability to continue to promote public transport services to commuters as well as tourists. Given the Government's reasons for corporatising Sydney Ferries it is anticipated that an expansion of SFC's presence in the tourist market would be one certain and obvious way for SFC to improve its asset utilization and reduce debt. Existing public transport ticketing arrangements, such as the Sydney Pass, have proven to be successful in attracting a significant proportion of the tourist cruise market to public ferry services.

As a result, the commercial advantages for SFC and STA in monopolizing the Sydney Pass and other similar integrated ticketing arrangements may continue to motivate the exclusion of private operators from access to them. Because the *Transport Administration Amendment (Sydney Ferries) Act 2003* enables SFC to inherit these ticketing

arrangements, there is no policy of legislative imperative for STA to reconsider its previous position with respect to private sector access to these ticketing arrangements.

Accordingly the *Transport Administration Amendment (Sydney Ferries) Act 2003* retains existing barriers to entry that provide SFC with exclusive access to tourists choosing to combine a harbour cruise and public transport use while preventing the access of private cruise operators to these consumers.

Barriers to entry are also created where Sydney Ferries controls or influences access to the Sydney Pass by its competitors in the scheduled cruise market. This control or influence can occur because of the relationship between Sydney Ferries, the STA and State Rail. Currently all these agencies operate under the Minister for Transport Services and therefore may be subject to similar and consistent policy direction. The SFC will also operate within this portfolio and may share similar relationships with the STA and State Rail irrespective of corporatisation.

Options

In order to minimize the anti-competitive effect SFC's use of its public transport services to compete in the tourist cruise market the following requirements could be applied:

- (a) Private operators and SFC could be afforded equal access on fair commercial terms to public transport ticketing arrangements that enable them to offer to tourists tickets that combine travel on the rail and/or bus network with a scheduled tourist cruise, but not public transport (ferry) services;
- (b) Tickets used by tourists to combine rail and bus travel with scheduled tourist cruises could be prevented from use on public transport services operated by SFC;
- (c) Marketing by SFC in domestic and international tourist publications could be limited to advertising its scheduled cruise, charter or other tourist specific services and related ticketing; and
- (d) Where private operators are not provided equal access to public transport ticketing arrangements available to SFC, then SFC could be prevented from marketing those ticketing arrangements in any domestic or international tourist publication.

Recommendation

That these options be recommended to the Minister by the Working Group where cost basis pricing and full competitive neutrality principles are not applied to SFC's public transport services used to compete in the market for tourist cruises.

5.3.2 Discriminatory Cost Inputs

5.3.2.1 Access Charges for Wharf Use, Ticketing and Overnight Berthing

Government policy and regulation requires private operators in the scheduled cruise market to pay for access to government owned wharves that they may need in order to provide scheduled cruises. Access leases cover the use of wharves to provide cruise services, the capacity to establish ticketing facilities and the right to berth vessels overnight.

Under various pieces of legislation these charges are generally levied by the NSW Waterways Authority and Sydney Harbour Foreshores Authority because they are the agencies administering wharf assets on behalf of the NSW Government.

Wharf access charges reflect market rates for premium government assets, such as wharves at Circular Quay, King Street Wharf and Darling Harbour, required by private operators to compete in the market for scheduled cruise services.

In 2000, the Waterways Authority sought bids from the private sector under an Expression of Interest (EOI) process for access to wharf 6 at Circular Quay. The three operators making this submission were successful in their bids for access. Access to wharf 6 at Circular Quay was granted to them on a shared time slot basis based on lease payments offered under the competitive EOI process.

The annual combined total lease payment for the three operators to access wharf 6 is about \$1 million. Because of the commercial in confidence provisions attaching to the EOI process the operators are unable to detail their individual lease payments in this submission.

This combined total lease payment includes access to the wharf to operate services and ticketing facilities required to offer and sell cruises at the Circular Quay precinct. It does not include overnight berthing fees as private operators are not permitted to berth their vessels at Circular Quay.

The three operators also lease access to wharves at the other major tourist cruise precincts at King Street and Darling Harbour. The annual combined total lease payment for the three operators to access wharves at King Street and Darling Harbour is about \$1.5 million. This includes access to wharves to operate services, ticketing, staff and office facilities, and overnight berthing.

In comparison Sydney Ferries has advised the Working Group that it pays an annual lease fee of \$250 000 to the Waterways Authority for use of wharves 2-5 at Circular Quay

(four wharves), which is the primary area where it offers services in competition with private operators. It suggests that its lease is for use of the wharves to operate services as well as offices, staff and ticketing facilities and overnight berthing.²⁰

Sydney Ferries apparently does not pay lease fees for use of other wharves at the tourist precincts at King Street and Darling Harbour, where it operates services in competition with private operators.²¹

It has not been clearly established by government that the lease fee paid by Sydney Ferries for use of the four Circular Quay wharves reflects or has been tested against the market rate for access to these wharves, which are a premium tourist precinct and the primary point of embarkation and disembarkation for tourists wishing to cruise Sydney Harbour.

Given the low access fee paid by Sydney Ferries for its access to four wharves at Circular Quay compared to the high costs charged to the three operators to share one wharf in the same precinct it would appear that the wharf access fees paid by Sydney Ferries do not represent the market rate for access to the area. It should be noted that the NSW Waterways Authority controls and levies the wharf access fees for both private operators and Sydney Ferries.

One argument put forward by government to support the low non-market tested lease fees paid by Sydney Ferries for access to four wharves at Circular Quay is that Sydney Ferries is using these wharves to provide public transport services, rather than to compete with private providers in the tourist cruise market.

The operators do not accept this view because it is clear that Sydney Ferries uses the Circular Quay, King Street and Darling Harbour wharves, to which it has access, to compete in the tourist cruise market primarily via its regular public transport services. As noted above Sydney Ferries scheduled sightseeing cruises represent only 3 cruises per day by one vessel.

Sydney Ferries also markets and promotes its regular public transport services to tourists through significant national and international advertising in tourist specific publications and via its exclusive access to the Sydney Pass and other public transport ticketing arrangements. This kind of promotion assists it to retain its current dominant share of the market for scheduled cruise services on any of the constructions discussed at 5.1.2.

Given that Sydney Ferries uses its scheduled sightseeing cruises and regular public transport services to compete in the scheduled cruise market, market determined access fees should be applied to its use of wharves at Circular Quay, King Street and Darling

²⁰ Sydney Ferries Information Paper considered by the Working Group

²¹ Ibid

Harbour from which it operates and enjoys scheduled sightseeing cruises, regular public transport services, and related ticketing, staff, office and overnight berthing facilities.

The operators consider that these market tested lease fees for wharf access should be determined and applied before SFC commences operation in July 2004. To address the anti-competitive effects of the current discriminatory cost inputs managed by the NSW Waterways Authority, these costs could be benchmarked and applied to SFC.

In circumstances where SFC chooses to expand its presence in the market for scheduled cruise services either via its scheduled sightseeing or regular public transport services, the current inequity in wharf access charges may provide it with an advantage that could either threaten or actually lessen competition in breach of Part IV of the Trade Practices Act. This may particularly be the case where the financial viability of private operators is threatened by SFC's ability to take advantage of the current discriminatory treatment of wharf access charges.

To enforce these obligations on SFC, the *Transport Administration Amendment (Sydney Ferries) Act 2003* (which is currently silent on this issue) should be amended to reflect cost input equity between SFC and the private providers with whom it competes in the tourist cruise and potentially the public ferry markets.

Options

- (a) SFC is required to pay market tested wharf access fees for leasing wharves it uses for scheduled sightseeing cruises. Lease fees should include the use of the wharves to operate services, as well as ticketing, staff, office and overnight berthing facilities related to the provision of scheduled sightseeing cruises.

This option should apply where SFC competes in the market for scheduled cruises through the use of its scheduled sightseeing cruises. Alternatively it may be considered suitable if the bulk of SFC's market share in the market for scheduled cruise services is provided through the operation of scheduled sightseeing cruises.

However based on the discussion above it is clear that Sydney Ferries only operates three scheduled sightseeing cruises each day using one primary vessel. In reality these cruises do not represent Sydney Ferries share in the market for scheduled cruises.

Accordingly, applying market tested access fees to these services and related uses alone will have little to no effect in addressing the anti-competitive effect of discriminatory cost inputs applying to wharf access fees applied to private providers.

Nevertheless market tested access fees for wharf use for services and related functions should apply to SFC's scheduled sightseeing cruises to ensure that any future expansion of these services meets competitive neutrality principles with respect to cost input equity.

- (b) SFC is required to pay market tested wharf access fees for leasing wharves it uses for all public transport services and scheduled sightseeing cruises. Lease fees should include the use of the wharves to operate services, as well as ticketing, staff, office and overnight berthing facilities related to the provision of public transport services and scheduled sightseeing cruises.

This option is suitable if it is considered that SFC would compete in the market for scheduled cruise services via its public transport services. It is evident that the vast majority of tourists using Sydney Ferries services travel on its public transport services.

As discussed above this occurs because the pricing, visual experience, frequency and other factors make Sydney Ferries public transport services substitutable for scheduled cruises offered by private providers. It also occurs because Sydney Ferries markets and promotes its public transport services to the tourist market via specific advertising and exclusive ticketing arrangements it shares with other public transport providers by virtue of its government ownership.

The *Transport Administration Amendment (Sydney Ferries) Act* 2003 permits the new SFC to take advantage of these existing arrangements and it is expected that SFC would do so given that the Government explicitly wants it to build revenue.

While this option can effectively address the current discriminatory cost inputs with respect to wharf access fees and the competitive neutrality issues that flow from that, it also raises a number of issues for the provision of public transport services.

Arguably, where SFC is required to pay market tested wharf access fees for its public transport services because those services are used by tourists, these fees may add to its operating costs, and in the absence of public transport fare increases granted by IPART, serve to only increase the debt burden of SFC. Equally there are a range of public policy reasons why public transport users should not be charged higher fares simply because SFC services are used by tourists in competition with private providers.

Different pricing regimes for tourist and non-tourist users of public transport services would be one way to address these potential effects. Differential pricing does not need to rely on the ability of SFC to technically distinguish between public transport users and tourists.

In reality regular public transport users are likely to prefer to purchase weekly, monthly or annual tickets, compared to domestic and international tourists who are likely to purchase only one single or return journey. Because of these distinct travel patterns, SFC could encourage public transport use by providing discounts for regular passengers (likely to be commuters) and increase its revenue by charging higher fares for one off journeys (likely to be tourists).

SFC has more capacity to implement greater differential pricing than rail or bus services because ferry services are more boutique and likely to be minimally used for one off journeys by commuters seeking to travel between A and B. This is particularly because there are alternative modes of transport better placed for speedy travel between A and B, such as rail, bus, taxi and private vehicle.

In this sense, SFC services are more akin to the boutique Monorail or Light Rail services, used by a significant proportion of tourists. For example one off journeys on the Monorail and Light Rail cost up to 200% more than tickets for regular travel. This approach rewards commuters using these modes for public transport purposes, but provides flexibility for operators to charge tourists higher prices that better reflect their capacity to pay.

One possible argument against this approach is that it may make SFC's public transport services more expensive for NSW or Sydney based residents seeking a one off tourist experience on Sydney Harbour on the weekend or other times. While this would be the

likely result, the Government needs to consider whether its role is to provide greater welfare to the regular public transport user or the NSW or Sydney resident who chooses to travel on a public transport ferry service for a tourist experience infrequently in any one year or more.

The view of the Operators is that government should ensure that welfare be transferred to the commuter whose disposable income is influenced by regular transport costs, rather than the Sydney, NSW or international resident whose disposable income would be unaffected by the cost of a one off journey on a SFC public transport service at infrequent times during one or more years.

- (c) SFC is required to pay market tested wharf access fees for leasing wharves it uses for scheduled sightseeing cruises and only those public transport services heavily used by tourists. Lease fees should include the use of the wharves to operate services, as well as ticketing, staff, office and berthing facilities related to the provision of public transport services and scheduled sightseeing cruises.

This approach would need to identify specific public transport services which are heavily or primarily used by tourists, such as the Manly services, and apply market tested wharf access fees to the wharf and related facility use of these services.

Market tested or benchmarked lease fees would need to be determined for the proportion of use these services made of wharves and related facilities, particularly where these services were not allocated specific wharf space at Circular Quay or other precincts. This may be complicated and difficult to administer, especially if the need for operational adjustments resulted in different wharf use by these services on a fairly regular basis.

The kind of differential pricing discussed under option (b) could also be applied here. However this option may raise a number of equity issues if only certain services were subject to discounts for regular public transport usage and higher fares for one off tickets.

Recommendation

That option (b) is recommended to the Minister by the Working Group.

Where the costs of option (b) outweigh the benefits, the Working Group recommends to the Minister that, at a minimum, option (a) should be adopted by government.

5.3.2.2 Tax Equivalents

The State Owned Corporations Act requires that government corporations pay taxes or tax equivalents. This is also a requirement of competitive neutrality requirements in the Competition Principles Agreement.

Section 35N of the *Transport Administration Amendment (Sydney Ferries) Act 2003* provides the Treasurer with discretion to exempt SFC from the payment of taxes and tax equivalents on the basis that SFC needs to address the problems with accumulated debt over the next few years. The Minister for Transport Services has indicated to the Charter Vessels Association that the intention of government is to only apply this exemption to not for profit activities of SFC (ie. public transport services).

On average the three operators combined tax liability each year is about \$8 million. This includes payroll tax, GST, FBT, superannuation requirements, and group tax. This total figure can be higher depending on the level of profit made by each operator.

Where SFC competes with the operators in the market for scheduled cruises using its public transport services it is a discriminatory cost input if SFC is exempt from the normal tax liabilities to which the operators are subject. While the profitability of public transport services may affect the payment of corporate taxes, it would not generally effect liabilities for GST, FBT, superannuation, payroll tax and alike.

Recommendation

That the Working Group recommends to the Minister that all of SFC's services used to compete in the market for scheduled cruises should be subject to tax equivalent obligations.

Where the costs of this approach outweigh the benefits, the Working Group recommends to the Minister that, at a minimum, tax equivalents should be applied to SFC's commercial activities.

5.3.3 Price Controls

5.3.3.1 Scheduled Cruise Pricing

We understand that the fares Sydney Ferries applies to its scheduled sightseeing services are not regulated. However based on our expertise of the tourist market, and advice from Sydney Ferries we consider that Sydney Ferries does not price these services at market

rates.

Pricing employed by the Operators reflects the cost of capital and operating costs required to provide vessels and services for scheduled and charter cruises. SFC may argue that because it is using vessels for both public transport and tourist purposes, its pricing should only reflect the proportion of the cost of capital and operating expenses required to provide a tourist service using its vessels.

The Operators consider that this would enable SFC to price tourist products below the market rate because those prices would not reflect the true cost of capital and operating expenses required to provide those services. A level playing field is not achievable if SFC's pricing for tourist cruises is not based on the total costs that private operators bear in operating their vessels for tourist purposes.

The Operators consider that in order to comply with principles of competitive neutrality, SFC's scheduled sightseeing, charter and any other tourist cruise services must be subject to the following:

- Accounting systems that are ring fenced from public transport services and reported separately within SFC and in annual reports;
- Pricing that is based on avoidable costs if the service was not provided; and
- Pricing that is fully distributed and reflects the total cost of capital and operating expenses of vessels used by SFC for tourist cruise purposes, even though those vessels may not be used for those purposes fulltime.

Recommendation

That the working group recommends to the Minister that SFC's scheduled sightseeing, charter and any other tourist services should be subject to:

- (a) Accounting systems that are ring fenced from public transport services and reported separately within SFC and in annual reports;
- (b) Pricing that is based on avoidable costs if the service was not provided; and
- (c) Pricing that is fully distributed and reflects the total cost of capital and operating expenses of vessels used by SFC for tourist cruise purposes, even though those vessels may not be used for those purposes fulltime.

5.3.3.2 Regular Public Transport Fare Regulation

We understand that the fares Sydney Ferries applies to its regular passenger services are regulated by the Independent Pricing and Regulatory Tribunal (IPART). We understand that IPART regulates Sydney Ferries fares because it is a public monopoly and that one of the primary objectives of IPART in determining fares is to maintain the affordability and accessibility of public transport.

Whilst we support these objectives with respect to public transport, we consider that current fare regulation also means that where Sydney Ferries uses its regular passenger services to compete in the market for scheduled cruises there are limits on the ability of Sydney Ferries to price its tourist services consistent with market benchmarks.

Where Sydney Ferries is pricing its regular passenger services used by tourists below market price, private operators (who are subject to regulatory charges and possibly taxes that Sydney Ferries does not pay) are forced to also price below market rates in order to compete. This situation is exacerbated by Sydney Ferries sole access through the Sydney Pass and other arrangements to the tourist market wishing to combine a public transport and cruise ticket.

One option to address this is applying the kind of cost basis pricing to public transport services recommended above for scheduled sightseeing cruises operated by SFC. However, because SFC's fares for public transport services are regulated by IPART, this cannot occur without IPART approval. There are also policy issues, such as the need to maintain the affordability of public transport, to take account of when considering this form of cost basis pricing.

5.3.4 Restrictions on Access to Infrastructure

5.3.4.1 Overnight Berthing For Vessels

Currently the operators of scheduled cruises berth their vessels overnight at King Street Wharf and Pier 26 at Darling Harbour under access arrangements with the NSW Waterways Authority and Sydney Harbour Foreshores Authority. Access arrangements for overnight berthing are determined by competitive tender and charges reflect market rates for premium harbour assets owned by government. Private operators are not permitted to berth their vessels overnight at Circular Quay.

Sydney Ferries berths its vessels (which it uses to deliver its services and products in the scheduled cruise market) overnight at Circular Quay and Balmain shipyards. The lease fee paid by Sydney Ferries to the NSW Waterways Authority for the use of jetties 2-5 at Circular Quay includes access to overnight berthing. The Government has not established that this fee was determined by market testing as discussed above. Sydney Ferries owns

and therefore controls the Balmain Shipyards.

The unequal treatment of berthing access adds costs to private operators in the scheduled cruise market, but not Sydney Ferries. It also obliges private operators, but not Sydney Ferries, to consider overnight berthing restrictions and charges when planning vessel and product growth. This can act to lessen competition in the market for scheduled cruises by dissuading private sector investment in new vessels, services or related products that require berthing access.

Recommendation

That the Working Group recommends to the Minister that SFC and private operators have equal access to overnight berthing facilities for vessels being used to compete in the scheduled cruise market.

5.3.5 Restrictive Advertising and Promotion

5.3.5.1 Wharf Signage

Sydney Ferries is able to advertise its services on all wharves it uses in Sydney Harbour with the use of permanent and attractive signs. This includes promotion of scheduled sightseeing and regular passenger services used by Sydney Ferries to compete in the scheduled cruise market.

Private operators are currently only permitted by government agencies owning wharves to advertise their services on these wharves with the use of standard temporary 'A' frame signs that are obviously less elegant and attractive than Sydney Ferries signage.

The operators consider that all competitors in the scheduled cruise market should be governed by the same signage and advertising requirements imposed by government.

Recommendation

That the Working Group recommends to the Minister that STA, SFC and any other government agency with control of wharf signage be required to grant to SFC and private operators equal access to signage and advertising.

5.3.5.2 Advertising On State Owned Public Transport Infrastructure and Assets

Sydney Ferries advertises its services on government owned transport and other assets, such as at rail stations and on Sydney Buses. This advertising supports Sydney Ferries promotion of its scheduled cruise and regular passenger services to national and international tourists in tourism publications discussed above. It also supports its use of the public transport system and related ticketing arrangements discussed above to attract tourists using the public transport system.

Sydney Ferries also advertises its services at bus stops owned and controlled by Sydney Buses in the specific tourist corridors at the Rocks and King Street wharf. These bus stops used by Sydney Buses services such as the Sydney Explorer. Private operators are not permitted to advertise at these stops.

While of itself, this kind of advertising is not of concern to us, we consider that it may breach competitive neutrality principles where Sydney Ferries gains access to advertising its services on government assets, particularly public transport assets, without a tender process and the payment of market rates for such advertising.

Recommendation

That the Working Group recommends to the Minister that STA, State Rail and any other government agency with control of assets used for advertising be required to grant to SFC and private operators equal opportunities to advertise on those assets through tender, EOI or other market processes.