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Shipping and Port Services Enquiry

Issues Paper

4 October 2006

Terms of Reference for Shipping and Port Services Enquiry

On 20 July 2006, the Chief Executive of the Economic Development Department formally requested, on behalf of the Minister for Economic Development, that the JCRA enquire into, report and make recommendations on:

- the current structure of, and level of competition in, markets for the provision of shipping and port services in Jersey (together, 'the relevant sectors');
- the current structure and level of fees and charges in these sectors;
- measures that could be taken under the Competition (Jersey) Law 2005 to increase the level of competition and efficiencies in these sectors; and
- alternative measures that could be taken to improve efficiencies in sectors that are naturally monopolistic and not amenable to action under the Competition (Jersey) Law, including measures to regulate and monitor prices.

The 'relevant sectors' were defined as;

- freight forwarding and haulage;
- shipping services (including passenger, car ferry and freight services);
- port infrastructure (land, berths, cranes, warehouses, etc);
- stevedoring services (the loading and unloading of ships, and the loading and unloading of freight of land transport operators servicing the port); and
- pilotage, towage and mooring.

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INTRODUCTION

Perspective: efficiency

The perspective of the enquiry is one of economic efficiency. That is, the JCRA has been asked to essentially advise on whether the current structure of the shipping and port services sectors is sufficient to ensure that these services are provided in the most efficient or least costly manner.

In short, economic efficiency means that there is no waste: both within the firm and within the wider Jersey economy, the least amount of resources are used to provide the greatest level of goods and services. Otherwise, resources that could be productively employed in other firms or allocated to other sectors of the Jersey economy are being wasted.

Economic efficiency plays a vital role in promoting economic growth and development because it squeezes the most out of the productive base of the economy. For business overall, it means higher returns. For labour overall, it means higher real wages and increased employment. And in respect of consumer welfare, it leads to lower prices, higher quality goods and better levels of service.

Efficiencies within the firm and within the economy are called productive and allocative efficiencies respectively. They are also known as static efficiencies because they assume things are constant, that today's resource availability and technologies do not change.

However, far more significant from the point of view of sustained economic growth and development are dynamic efficiencies. Dynamic efficiencies flow from innovations in production and distribution technologies which expand the economy's productive base and make possible greater levels of productivity and economic growth than would occur in a static, albeit efficient, economy.

Focus: competition

The focus of this report is on how competition in shipping and port services can improve the efficiency of their supply and thus contribute to the economic growth and development of the Jersey economy.

Implicit in this focus is that policies to promote competition are not about the pursuit of competition for its own sake. It is about the pursuit of efficiency through competition. Free and open competition drives efficiency in three main ways:

- in relation to **productive efficiency**, competition drives prices down to the level of costs and forces firms to produce efficiently to remain competitive and profitable;

- in relation to **allocative efficiency**, consumer choice between competitive products efficiently allocates resources in the economy as resources respond to consumer demand and flow to the production of goods and services most valued by consumers; and

- in relation to **dynamic efficiency**, competition encourages firms to develop innovative products and invest in new technological processes in order to keep ahead of the pack.

The benefits of competition, to consumers as well as to the economy as a whole, can be substantial. The benefits have seen a growing presence of competition law and policy worldwide and its recognition as a key element of national economic policy.

It was for this reason that the Competition (Jersey) Law was passed by the States of Jersey (the 'States') in June 2004. It was also the principal reason behind the Minister for Economic Development, Senator Philip Ozouf, requesting the JCRA to enquire into the shipping and port services sector with a focus on competition issues and remedies (refer the Terms of Reference at the head of this Issues Paper).

However, in seeking to promote effective competition in the interests of economic efficiency, the JCRA recognizes that it may not always be possible to promote effective competition in small Island economies like that of Jersey. The classic case is a so-called 'natural monopoly' where, because of economies of scale deriving from large up-front investments, a single firm can supply an entire market more efficiently than two or more firms in competition with each other.

Where competition is absent and monopolies exist, firms have incentives to charge prices above efficient and competitive levels. Such 'monopoly pricing' can be as detrimental to consumers and to the economy as collusion by competitors to fix prices and other anti-competitive practices. In such circumstances, the appropriate competition policy response may be to implement a carefully-targeted price regulation and monitoring process which acts as a proxy for the competitive process. Of course, being a proxy, price regulation is only a second-best solution to competition.

The promotion of competition will often be consistent with a range of other policy goals. However, there may be situations where competition policy may be in tension with other arms of States' policy, particularly social policy. Resolution of such tensions is ultimately a political decision for the States.

Importance: critical

Over 98 per cent of goods come to Jersey via sea.[1] As such, shipping and port services have been described as the lifeblood of the economy. Given the critical role they play in the economic well-being of Jersey, any inefficiencies in shipping and port services will inevitably flow into the Jersey economy, typically in the form of higher prices and less choice.

This Paper identifies a number of matters in shipping and port services which the JCRA considers raise questions of efficiency. The issues are listed in two parts: those relating to shipping and those relating to ports.

Under each issue, a brief outline of the issue is followed by a discussion of the potential inefficiencies.

Invitation for comments

The JCRA invites comments and submissions on each issue discussed in this Paper. Submissions are also sought on issues not covered in the Paper which may be considered relevant from an efficiency perspective. Submissions are sought from the public generally as well as interested and affected parties.

In general, written submissions should reach the JCRA by **17 November 2006**. However, because of tight decision-making timeframes in relation to Issues 5, 6 and 7, submissions on them should reach the JCRA by **31 October 2006**.

The JCRA will consider requests for extensions of time but notes that it is planning to report to the States in respect of Issues 5, 6 and 7 by mid-November and by the end of the year on the other issues.

The JCRA may publish submissions on its website. Confidentiality may be claimed for all or any part of a submission. Any claims for confidentiality should identify the parts claimed and be supported with reasons for its confidential status.

Submissions should be addressed to:

Ms Kerrie-Anne Bradley
Jersey Competition Regulatory Authority
6th Floor Union House Union Street
St Helier Jersey JE2 3RF
Channel Islands

Where possible, an electronic copy of the submission would be appreciated. These should be e-mailed to k.bradley@jcra.je Copies may also be faxed to the JCRA at +44 (0)1534 514991. For enquiries, please call Ms Bradley on +44 (0)1534 514995.

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[1] *Jersey Harbours Business Plan 2006-2008*, States of Jersey .

SHIPPING SERVICES

This section of the Paper outlines the structure of the shipping services sector in terms of market participants, barriers to entry and other factors which affect demand for, and supply, of shipping services. The section also overviews the States' shipping policy.

(i) Shipping operators

Shipping services in Jersey may be categorised into car and passenger ferry services and freight services.

Car and passenger ferry services

The principal operator of car and passenger ferries to and from Jersey is Condor Ferries Limited ('Condor Ferries'). It operates fast ferry services between Jersey, Guernsey and Portsmouth in the UK (the 'northern' route) and to St Malo in France (the 'southern' route). Condor Ferries is a Guernsey company which has been in operation since 1964.

A smaller ferry operator with two ferries in its fleet is Manche-iles-express. It operates passenger-only high-speed ferry services between the Port of St Helier and Granville in France and between Gorey Harbour and Carteret in France. It is a French company run in partnership with the Conseil Général de la Manche.

Freight services

Freight services may be separated into roll-on, roll-off ('ro-ro') and lift-on, lift-off ('lo-lo') services. Ro-ro is generally used for time sensitive goods (eg, food) while lo-lo is used for more bulky and less time-sensitive goods (eg, building products). Approximately 65 per cent of freight is shipped via ro-ro services while around 35 per cent is shipped via lo-lo.[2]

Condor Ferries is the sole provider of ro-ro freight services. It owns two ro-ro freight ferries and operates a daily and nightly freight service between the Channel Islands (Jersey and Guernsey) and Portsmouth in the UK. It also operates a year-round service to Weymouth and a daily summer service to Poole in the UK. It carries a small amount of unitized freight on its ro-ro car and passenger ferry service to St Malo in France. New cars for commercial sale in Jersey ('trade cars') are also carried.

Lo-lo freight shipping is often referred to as 'conventional freight'. Such services are currently provided by Huelin Renouf Shipping Limited ('Huelin') and Channel Seaways Limited ('Channel Seaways').

Heulin is a Jersey company which owns one ship capable of transporting approximately 125 containers. It operates a freight service three times a week between the Channel

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[2] JCRA, *Decision M 005/05 Ferryspeed (C.I.) Limited /Channel Express (C.I.) Limited,* July 2006: 6

Islands and Portsmouth. Channel Seaways is an Alderney company which operates a twice-weekly freight service around the Channel Islands on a 24-container capacity ship. It also operates services to Poole in the UK and to Rotterdam in the Netherlands.[3]

In addition, ad hoc bulk cargoes (such as oil, cement, fertilizer, scrap and timber) are shipped to and from Jersey on specialized bulk carriers (eg, the 'Ronez' for bulk cement, a carrier owned by Aggregate Industries Limited of the UK).

(ii) Factors affecting demand and supply

There are a number of key factors which can adversely affect the efficiency of both car and passenger services and conventional freight services to and from Jersey:

- the relatively small size of the Jersey population and economy, which may make it difficult to generate economies of scale;
- the large seasonal variations in demand for shipping services, which may make it uneconomical to operate year-round;
- an imbalance of import volumes over export volumes, which may make journeys from the Island uneconomical;
- large tidal variations, which limit ramp access times for ferries;[4]
- the configuration and depth of the Port of St Helier, which restrict the size of ships generally.

There are also a number of other factors particular to particular shipping routes and these are discussed under the various issues where relevant.

(iii) States shipping policy

In a nutshell, the shipping policy of the States is to secure year round, long term, reliable, robust and reasonably priced services of sufficient quality and frequency.[5]

Additionally, overarching economic policy of the States is to allow market forces to operate in relation to shipping and port services where there is no clear indication of market failure or threat to required service levels. However, economic policy does acknowledge the risks of allowing market forces to prevail in ferry services, not least in the danger of monopoly/price war cycles and the breakdown of the winter service.[6]

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[3] *Ferryspeed (C.I.) Limited /Channel Express (C.I.) Limited*, JCRA, Decision M 005/05, July 2006, p 7.
[4] The JCRA understands that there is a three-hour tidal window and two ramps.
[5] *Air and Sea Transport Policy Statement*, Minister for Economic Development, 23 March 2006.
[6] *Economic Growth Plan*, 2005.

When States intervention is to occur, however, the JCRA understands that there is a general policy resistance to state subsidies to assist in the commercial viability of private operations.

SHIPPING ISSUES

The issues relating to the efficiency of the shipping sector in Jersey are now discussed.

Issue 1: Scope for competition on the northern ferry route

Outline of issue

Obviously, the commercial viability of shipping services relies on there being sufficient demand. In turn, the efficiency of such services will largely depend on whether the various routes can sustain competitive operators or whether it is a natural monopoly. This first issue focuses on efficiency on the northern ferry route: is there sufficient demand on the northern ferry route to sustain competitive services or is it a natural monopoly?

Discussion

In 2004, the economic consultancy Oxera recommended that a franchised monopoly provider would be the best option for both the northern and southern ferry routes if year-round service was required.[7] Also, both P&O and Hoverspeed (who tendered for the northern route in 1998 against Condor Ferries) have argued in the past that the northern route was a natural monopoly.

Others have argued that investment in modern high-cost car and passenger ferries would only occur when there was some certainty of return and this would not happen where there was unstable competition and price-cutting wars. It has been further argued that there is less incentive to invest in ferries for the Jersey service because there is a limited market for the relatively small-capacity ferries suitable for Jersey.

On the other hand, there have been competitive services on the route in the past, albeit in times when tourism numbers were far greater than they are now.

A particular consideration in respect of the northern route is that its viability has traditionally been dependent on servicing both Jersey and Guernsey. This issue is discussed separately below.

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[7] *Viability of ferry services to and from the island of Jersey*, Report prepared for Jersey Harbours by Oxera, July 2004.

Submissions are requested on whether or not there is scope for competition on the northern route. To allow for a full and informed assessment, submissions should be supported by information on costs, demand projections, etc, and an outline of the key assumptions.

Issue 2: Scope for competition on the southern ferry route

Outline of issue

The second issue focuses on efficiency on the southern route: is there sufficient demand on the southern ferry route to sustain competitive services or is it a natural monopoly?

Discussion

There has been a greater history of competition on the southern route than the northern route. However, the competition that occurred was between a relatively slow car and passenger ferry and passenger-only fast hydrofoils. When the hydrofoils were replaced with fast car and passenger ferries, the balance was upset, Emeraude Jersey Ferries ('Emeraude') withdrew in December 2005, and Condor is currently the only operator on the route. Accordingly, the considerations are similar to those discussed above in relation to the northern route.

Submissions are requested on the scope for competition on the southern route. As for Issue 1, submissions should be supported by information on costs, demand projections, etc, and an outline of the key assumptions.

Issue 3: Ferry prices

Outline of issue

There have been complaints about relatively high ferry prices. If such complaints are justified, those prices may reflect inefficiencies in the provision of ferry services (such as poor management and resource use) or simply excessive monopoly pricing. In other words, they may be a symptom rather than a cause of inefficiencies. Accordingly, the issue is whether ferry prices are relatively high and, if so, why?

Discussion

In some respects, ferry prices to and from Jersey may be considered high. Prompted by significant price increases on the southern route following the exit of Emeraude from that route, a proposition was put to the States seeking to ensure that Jersey does not remain wholly dependent on a single ferry company. Prior to Emeraude's exit, it was stated in the proposition that there was aggressive price competition on the route. [8]

A short preliminary international price comparison by the JCRA yielded the following figures.[9]

from	to	price: car + 2 passengers	price: foot passenger	price: car only	maximum car length	travel time	price 7m lane space per hour
Liverpool	Isle of Man	£205	£20	£165	5.5	3	£36
Jersey	St Malo	£139	£29	£81	4.5	1	£34
Cherbourg	Portsmouth	£200	£57	£86	5.0	3	£20
Holyhead	Dun Laoghaire	£106	£22	£62	6.0	2	£16
Corfu	Patras	£141	£29	83	4.3	7	£12
Newcastle	Amsterdam	£200	£23	£154	4.5	15	£12
Larvik	Hirtshals	£127	£40	£47	5.0	3	£11
Jersey	Portsmouth	£166	£39	£88	4.5	10	£9
Aberdeen	Kirkwall	£119	£24	£71	6.0	6	£9
St Malo	Portsmouth	£189	£57	75	5.0	9	£8
Belfast	Stanrear	£75	£22	£31	6.0	2	£8
Calais	Dover	£55	£18	£19	6.0	1	£6
Ile Rousse	Toulon	£90	£28	£34	4.0	6	£6
Le Havre	Portsmouth	£63	£15	£33	5.0	5	£6
Genua	Barcellona	£187	£55	£77	3.9	18	£6
Gdynia	Kalskrona	£74	£32	£10	6.0	10	£1
Oslo	Copenhagen	£137	£65	£7	4.5	16	£0
Kiel	Gothenburg	£196	£101	-£6	6.0	13	£0

The price from Jersey to St Malo is the second highest price in the sample, the price from Jersey to Portsmouth is about average. It needs to be stressed that this was a very preliminary comparison and, for example, did not take into account any state subsidies or whether prices are regulated.

Submissions are sought on whether ferry fares are considered to be overly high. While it is not difficult to make assertions about high fares, submissions on this issue should be supported by hard evidence where possible (eg, by comparison to similar routes between other islands and countries, or by comparison to other periods when competition prevailed).

[8] *Sea transport: revised policy*, Proposition lodged in the States of Jersey by Deputy J.B. Fox of St Helier, 28 February 2006.

[9] For a random number of sea routes, the JCRA accessed relevant websites and from the fares for a single trip on 5 July 2006, it calculated consumer prices for 7 metres of lane space (6 metre car plus 1 metre walk-around space). JCRA divided the price by the travel time and then added another 2 hours to account for loading and unloading of the ferry.

Issue 4: Differential ferry prices

Outline of issue

The JCRA understands that different prices apply for Islanders and non-Islanders on certain ferry routes.[10] The issue is whether such differential pricing exists and, if so, whether it is symptomatic of inefficiencies in the provision of ferry services.

Discussion

Differential pricing (often called 'discriminatory pricing') is a common business practice which, in most circumstances, enhances consumer welfare and economic efficiency.

Differential pricing can be particularly beneficial when high up-front costs are involved (such as with ferries). In such circumstances, the high fixed costs can be recovered more efficiently by pricing 'as much as the market will bear' rather than by uniform pricing. In this way, profits from customers with a high willingness to pay may fund discounts to customers who otherwise would not have purchased tickets under a uniform pricing structure. The incremental revenue from these discount customers may well be the difference between recovering the costs of an up-front investment or not.[11]

While differential pricing may be considered as generally beneficial, there are circumstances where it may be detrimental when it is used to damage competition (eg, by pricing below-cost in markets where it competes and pricing high in monopoly markets to recoup those losses). From an economic perspective, this is generally the only time when it is considered detrimental. However, differential pricing may raise the social issues of equity and fairness.

Submissions are sought on the extent of differential pricing on either the northern or southern ferry routes. Such submissions should focus on the economic perspective and whether such pricing leads to inefficiencies.

Issue 5: Regulation of ferry services

Outline of issue

A corollary of any conclusion that there is a natural monopoly in ferry services on either the northern and southern routes is whether there is a need for specific economic

[10] *Pricing on the northbound and southbound ferry routes*, States minutes, 6 June 2006.
[11] A good lay understanding of the reasons for price discrimination may be found in *The Undercover Economist*, Tim Harford, Little, Brown, April 2006, Chapter 1.

regulation of that service and, if so, the form it should take.[12] A further corollary is whether prices for those services should be subject to some form of price regulation.

Discussion

As discussed in the introduction to this Paper, and in line with the States' economic policy, competition in markets is the preferred option for delivering efficiencies for the ultimate benefit of consumers and the economy as a whole. However, should there be insufficient traffic to support more than one operator, then regulation of the route may be required to ensure that efficiencies are delivered and resources are not wasted under a natural monopoly situation.

Ferry companies trading with Jersey are subject to the provisions of the Competition (Jersey) Law which generally prohibits anti-competitive conduct and abuses of dominance. This law has universal coverage across all industries.

In addition to competition law, industry-specific regulation has been used in many jurisdictions to control the conduct of dominant or monopoly providers of essential services such as telecommunications, post, gas, water and electricity. Currently, the States have adopted industry-specific law in relation to telecommunications and postal services which, amongst other things, contain detailed price control regulations. The JCRA is responsible for enforcing these laws.

There is currently no such industry-specific law in relation to shipping, although it may well be considered a 'lifeline' for Jersey consumers and the economy as a whole. Typically, regulation of ferry services in Jersey has been through service level agreements (SLAs) entered into between the shipping companies and the States. However, these have covered mostly non-economic matters such as service obligations (eg, capacity, frequency, safety and reliability) and back-up arrangements in the event of weather and/or technical disruptions.

Currently, there is only one SLA in place, that with Condor Ferries in relation to the northern route. It is non-exclusive and expires at the end of 2006. The Economic Development Department (the 'EDD') monitors compliance with the extant SLA. There is no current SLA in relation to the southern route to St Malo, France. Nor are there any in relation to conventional freight services.

The SLA does cover some economic matters, notably ferry prices. However, they only relate to maximum prices and do not cover fare structures or how fares may be charged (eg, Condor Ferries currently has in place a non-transparent 'fluid pricing model').

[12] 'Economic' regulation focuses on the commercial behaviour, particularly the pricing behaviour of companies. It is distinct from 'social' regulation which focuses on social aspects such as reliability, frequency and safety.

In their 2004 report concluding that ferry services should be provided by a monopoly provider on each route, Oxera also concluded that responsibility for the design and allocation of operating licences should be subject to regulation by the JCRA. [13]

Should it be considered that either the southern and northern ferry routes are natural monopolies, submissions are sought on whether there should be specific economic regulation of those routes in addition to the general requirements under the Competition (Jersey) Law. Further submissions are sought on the form these regulations should take (eg, whether regulation, including pricing regulation, should continue through the SLAs or under specific powers given to the JCRA).

*Please note that, as the current SLA is due to expire by the end of this year and decisions need to be made in respect of new SLA's before then, submissions on this issue should reach the JCRA by **31 October 2006**.*

Issue 6: Future arrangements for entry into the car and passenger ferry market

Outline of the issue

As noted, car and passenger ferry companies must enter into an SLA before they can ply their trade. The issue is whether these requirements impose an unreasonable restraint on trade and whether, if there are no natural monopolies, entry into the Jersey shipping market should be made less restrictive in the interests of economic efficiency.

Discussion

A tender process was adopted in 1998 for an SLA in respect of car and passenger ferry services between Jersey and the UK. The same process has also been adopted in relation to the southern route to St Malo in France.

However, these were not fully open tender processes as tenders were evaluated against 'beauty parade' criteria such as frequency, capacity, quality, reliability and back-up. Should it be decided, in line with the Oxera conclusion, that the northern and southern routes should be served by a monopoly provider, the process for determining the sole provider may involve either a similar beauty parade contest or an open tender focusing on economic aspects such as the level of prices.

The alternative argument is that, despite exits from the routes in the past, market forces are best placed to decide whether the northern and southern routes can only be economical with a monopoly service provider or whether they may be viable with competitive providers.

Submissions are sought on whether there should be specific restrictions on entry into the northern and southern routes, perhaps on beauty parade criteria or perhaps involving an

[13] *Viability of ferry services to and from the island of Jersey*, op. cit.

open tender process, or whether there should be a free and open market with limited restrictions on market entry.

Please note that, as the current SLA is due to expire by the end of this year and decisions need to be made in respect of new SLA's before then, submissions on this issue should reach the JCRA by ***31 October 2006****.*

Issue 7: Pan-Island economics and regulation

Outline of the issue

In addition to the SLA with the States, Condor Ferries also has a SLA with Guernsey for its northern route. Unlike the Jersey SLA, however, the Guernsey one is exclusive and does not expire until the end of 2008. Current policy is to develop with Guernsey a joint approach to ferry services in the Channel Islands.[14] Should agreement be reached, the issue is how pan-Island SLAs should be structured so as to reap the most efficiencies from such harmonised regulation.

Discussion

There would appear to be clear economies of scale for a ferry operator in servicing both Jersey and Guernsey. However, to fully reap those scale economies and make shipping routes more commercially viable, co-operation and harmonisation of regulatory treatment between the Channel Islands may be desirable.

As the Jersey SLA expires before the exclusive Guernsey SLA, interim measures will be required in Jersey pending any harmonised regulatory treatment from 1 January 2009. Should agreement in-principle be reached between the States and Guernsey on harmonised regulatory treatment, the issues relating to the form such pan-Island regulation should take would be similar to those discussed above in relation to Jersey, for example:

- should there be industry-specific regulation as well as the general application of competition law (note that Guernsey does not have a general competition law);
- if there is industry-specific regulation, should it be through the instrument of an SLA or under new joint powers given to the JCRA and the Office of Utility Regulation in Guernsey;
- should there be an open tender process or beauty parade-type restrictions on entry?

[14] *Air and Sea Transport Policy*, Statement by Minister for Economic Development, 23 March 2006.

Submissions are requested on the scope for competition on the need for pan-Island routes for commercial viability. Further submissions are requested on the form any pan-Island regulation should take.

Please note that, as the current Jersey SLA is due to expire by the end of this year and decisions need to be made in respect of new SLA's before then, submissions on this issue should reach the JCRA by ***31 October 2006****.*

Issue 8: Vertical integration between freight forwarders and shipping companies

Outline of the issue

There is a degree of vertical integration between some freight shipping companies and freight forwarders in Jersey. Such vertical integration may create incentives for companies in a corporate group to favour their own to the competitive disadvantage of outsiders. The issue is whether vertical integration between freight forwarders and freight shipping companies should be regulated in the interests of promoting competition and efficiencies in the provision of freight forwarding services.

Discussion

As mentioned, Condor Ferries is the sole provider of ro-ro freight services in and out of Jersey. Condor Ferries is in the same corporate group as Condor Logistics, a competitor in the provision of freight forwarding services into and out of Jersey. In addition, Heulin, which is the major lo-lo freight shipping company in Jersey, operates a freight forwarding service under its corporate banner. Channel Seaways is also vertically integrated into freight forwarding.

There can be distinct benefits in vertically integrating two levels of economic activity (in this case, shipping and freight forwarding). These benefits are generally in the form of improved efficiencies as a result of reduced transaction costs, greater information flows and co-ordination, and more synchronised investment in facilities and technologies.

However, where there is vertical integration between a non-competitive activity (such as ro-ro freight shipping) with competitive activities (such as freight forwarding), there are clear incentives for the sole provider to discriminate in favour of its related downstream companies to the competitive disadvantage of independent third parties. There a number of independent competitors in the freight forwarding sector in Jersey, including Paul Davis Freight Services Limited, Ferryspeed C.I. Limited, Bowman (Haulage) Limited and DFDS.[15]

Such conduct is sometimes called 'leveraging of market power' and may be prohibited under general competition law, including the Competition (Jersey) Law, as an abuse of

[15] Det Forenede Dampskibs-Selskab (The United Steamship Company), a Danish shipping line and freight forwarding company.

dominance if it substantially restricts competition. However, a position of dominance must be established and this may not necessarily be the case in Jersey (particularly in respect of Huelin and Channel Seaways). Further, competition law does not deal with the incentives to engage in such conduct. Also, it may be difficult and resource-intensive to prosecute such conduct under the law.

Such concerns were behind the recent decision of the Minister for Economic Development to ask the JCRA to review the structure of Jersey Telecom. As the Minister commented, one possibility is for the Jersey Telecom network to be separated from service provision in order to promote as much competition as possible among service providers using the network.[16]

Submissions are sought on whether vertical integration between freight forwarders and freight shipping companies is of concern and whether it should be regulated in the interests of promoting competition and efficiencies in the provision of freight forwarding services. Further submissions are requested on whether the abuse of dominance provisions in the Competition (Jersey) Law are adequate to deal with the issue, or industry-specific regulation is required.

Issue 9: Demand stimulation and dynamic efficiency of shipping services

Outline of the issue

As discussed in the introduction to this Paper, there are a number of key factors which may adversely affect the efficiency of shipping services. These are factors which affect either demand for, or supply of, shipping services. The issue is whether these limiting factors can be changed to make shipping services more viable and efficient.

Discussion

Much discussion on shipping issues is conducted on the premise that the factors limiting the efficiency of shipping services are 'immutable'. From this premise, conclusions have been reached that shipping services are a natural monopoly. Oxera reached its conclusion in its 2004 report that a monopoly provider would be the best option for both the northern and southern ferry routes on the basis of an unchanging overall level and pattern of demand.[17]

While some factors cannot be changed, not all factors are necessarily immutable. A key limiting factor is the level of demand generated by the small Jersey population and economy. However, is this necessarily immutable?

As mentioned previously, the key to sustained economic growth is the dynamic efficiencies which flow from investment in innovative new products and technologies.

[16] *JT could be sold off in pieces*, Jersey Evening Post, 2 October 2006, p 2.
[17] *Viability of ferry services to and from the island of Jersey*, op. cit.

They expand the economy's productive base and make possible higher levels of economic growth than would otherwise occur in a static, albeit efficient, economy.

Competition is the typical way by which dynamic efficiencies are stimulated. However, where competition is not possible, policies to stimulate demand can realise those efficiencies. Such policies, if fully developed and effectively implemented, can be a proxy for competition in much the same way that government intervention to control monopoly abuses are a proxy for competition.

An example of state aid applying on Channel Islands routes is the assistance given to the French ferry company, Manche-ils-express. Since April 2005, in an effort to improve tourism and cultural links between the Channel Islands and Normandy, the local Normandy regional government, Conseil Général de la Manche, subsidises the high-speed ferry services provided by Manche-ils-express between Granville, Carteret and Dielette in France and Jersey, Guernsey, Alderney, Sark and Herm in the Channel Islands.

More further afield, the Province of British Columbia in Canada has contracted with British Columbia Ferry Services Inc. ('BC Ferries') to provide specified numbers of ferry services on specified routes in return for an annual subsidy called a 'service fee'. A provincial authority, the British Columbia Ferry Commission regulates the ferry fees and imposes a maximum permitted level of average ferry fees for all BC Ferries' routes.

As a final example, the Australian Government introduced in 1996 a rebate scheme for vehicles using the Bass Strait ferry between the mainland and Tasmania. By reducing ferry costs, the aim was to stimulate demand and, ultimately, tourism and the Tasmanian economy. The scheme has contributed significantly to growth in passenger vehicles shipped (from 63,000 vehicles in 1995-96 to 228,499 vehicles in 2003-04). A further benefit has been the increased commercial viability of the ferry company, TT-Line, such that in 2002 it put on two new ferries with improved facilities, more frequent services, and greater passenger and vehicle capacity.[18]

A general characteristic of subsidies such as those involved in the above ferry services is that they may keep prices below cost. Accordingly, they can distort markets and lead to the misallocation of resources which could otherwise be put to more valuable uses elsewhere. In economic parlance, subsidies can create allocative inefficiencies. Largely for this reason, there is the previously-mentioned resistance to subsidies by the States.

On the other hand, if critical mass in demand can be achieved, the economy may reach a tipping point where competitive shipping services become sustainable on a fully commercial basis without the need for subsidies.[19] In the longer term, consumer welfare is increased and the economy as a whole benefits.

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[18] *Bass Strait Passenger Vehicle Equalisation Scheme*, Monitoring Report No. 7, Bureau of Transport and Regional Economics, Australian Government, April 2004.

[19] Similar effects, called 'network effects', occur in telecommunications: increasing numbers of subscribers to a network will make it increasingly valuable to other subscribers and the resulting 'positive feedback

Ultimately, questions of subsidy are decided by the States. However, in so far as subsidies may lead to greater long-run economic efficiency, the JCRA considers it appropriate to call for submissions on the potential for demand stimulation to make shipping services more competitive and, hence, more efficient. Submissions are also called on the type of demand stimulation measures that may be considered appropriate.

A particular form of demand-stimulation discussed below is concerned with developing French trade. Two other measures not discussed in this Paper but which may be relevant, and which are open for submission, are the development of tourism and the joining of the southern and northern routes into a UK-France route serving the Channel Islands en route. There well may be other potential measures.

Issue 10: Development of car, passenger and freight routes to France

Outline of issue

As discussed above, demand stimulation measures may lead to critical tipping points into sustained commercial viability of shipping services. This issue is concerned with the French connection as a potential area for such demand stimulation.

Discussion

Oxera has recently concluded that increasing trade with France is unlikely to deliver significant overall benefits to Jersey.[20] However, their conclusion is based on 'static world' assumptions, including a focus on the current link to St Malo rather than any future links to France (eg, Cherbourg).

However, all is not static and there is potential for demand stimulation. For example, work is currently being undertaken in Normandy on developing a Cherbourg freight hub. The potential for French supermarkets such as the Carrefour group or the Super U chain to establish stores in Jersey is another issue. Student exchanges with French schools and universities and the export of waste to France are other possibilities for demand stimulation.

Submissions are requested on the potential for increasing trade with France and the methods by which it could be achieved.

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loops' that are created ultimately tip the network into sustained commercial viability. Until that tipping point is reached, companies have to cross-subsidise network roll-out costs from other revenue sources.

[20] *Increased trade with France: what are the potential benefits and barriers?*, Report prepared for The States of Jersey by Oxera, June 2006.

PORT SERVICES

The Port of St Helier (the 'Port') has a virtual monopoly in the movement of passengers, vehicles and freight by sea – only a small amount of trade occurs outside of the Port (eg, from Gorey Harbour). Many of the issues raised in this section of the Paper are competition issues which flow directly from this monopoly.

The States owns the land, premises and certain facilities in the Port estate. Jersey Harbours, a State-owned instrumentality, is responsible for the operation of the Port and its infrastructure. Of particular relevance to this enquiry, Jersey Harbours has responsibilities to provide:

- facilities for transferring passengers, vehicles and freight between ship and quay side (such as cranes, roll-on roll-off linkspans and mechanical gangways); and

- navigation services (including pilotage and tug services).

Jersey Harbours also manages the Island's other coastal harbours and operates three marinas for local and visiting craft. It provides a coastguard service, and is responsible for other professional maritime services, such as Jersey Radio and the ships registry.

There is currently only one stevedore operating in the Port: George Troy & Sons Limited ('Troy'). It operates under a non-exclusive stevedoring licence which also grants Troy and its workforce (around 20 dockers) access to the Port facilities.[21] In consideration, Troy pays Jersey Harbour a nominal annual licence fee. There are no terms and conditions in the licence relating to how much Troy may charge for stevedoring services.

The main shipping companies which use the Port are Condor Ferries, Huelin, Channel Seaways, Manche-iles-express as well as the bulk cargo carriers. The background to these companies has previously been outlined in the shipping section of this Paper.

There is a high degree of cross-ownership between Troy and the two major shipping companies which service Jersey, Condor Ferries and Huelin. In addition, the largest builders' merchant in Jersey, Normans, owns a significant proportion of Troy. Normans was a former part-owner of Condor Ferries.

The majority of Troy's business is provided to its own shareholders. The same shareholders of Troy also own the only independent ship's agent in Jersey (St Helier Port Services). A number of the issues discussed below flow from these cross-shareholdings between the sole stevedores, the two main shipping companies and the only independent shipping agent.

[21] Troy owns some equipment such as forklifts and tugmasters.

Issue 11: Future provision of stevedoring services

Outline of the issue

While the general stevedoring licence granted to Troy is non-exclusive, in practical effect it has been the sole provider of stevedoring services in the Port for around the past 30 years.

In September 2005, the States and Troy agreed to extend the licence until 1 October 2007. Jersey Harbours will need to arrange for the provision of stevedoring services when the current licence extension expires no later than 1 October 2007. The issue is how to arrange for the future provision of such services in the most efficient manner.

Discussion

In a small port like that of St Helier, there may be a natural monopoly in the supply of stevedoring services. Characteristically of natural monopolies, it is more efficient for one firm to supply the services than two or more in competition with each other. However, also characteristically of natural monopolies, there is the potential to abuse the monopoly through inefficient monopoly pricing which harms consumers and businesses using the Port facilities and the Jersey economy as a whole.

Where competition 'in the market' is not workable, competition 'for the market' through a tender process may be an effective option for protecting consumer welfare and economic efficiency. On the other hand, in a small port like that of St Helier, a small number of bidders would increase the risk of bid-rigging. Indeed, there may not be competing bids at all.

Another option is for Jersey Harbours to perform the stevedoring services itself. It owns the main facilities and in operating its own equipment, such an option would avoid the 'moral hazard' of operating someone else's equipment.[22] Efficiencies from vertical integration may also be realised. However, a major difficulty with such an option is that there are no competitive constraints on the pricing of the stevedoring services.

A third option is to allow each shipping company, if it chose to for commercial reasons, to do its own stevedoring in relation to each of its ships ('self-handling'). Self-handling may be particularly an option in respect of ro-ro ships but currently, the JCRA understands that only Troy stevedores can be used to drive trucks and trade cars on and off a ro-ro- ship. The JCRA is not aware of any particular reason why a ship's own crew could not safely perform this activity, nor truck owners and operators or any other suitably credentialed person with a driving licence.

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[22] The presence of incentives for individuals to act in ways that incur costs that they do not have to bear. For example, the user of equipment that he doesn't own will not have the same incentive to care and maintain the equipment that an owner would.

A fourth option is to extend the status quo beyond October 2007. Some argue that the current stevedores provide good service but, on the other hand, the JCRA is aware of a number of complaints about current service levels (such as the limited working hours). To assess this option, the JCRA needs feedback on experiences with the level of services provided by Troy.

The JCRA seeks submissions on this issue. In particular, submissions are sought on each of the options mentioned above (ie, by tender, perform in-house, self-handling or extending the status quo). In relation to the status quo option, the JCRA would appreciate comments on the efficiency and level of stevedoring services currently provided. Submissions on any other options are also welcomed.

Issue 12: Cross-shareholdings between Troy and Condor Ferries and Huelin

Outline of the issue

Troy is currently the sole, though not exclusive, provider of stevedoring services in the Port. As previously mentioned, there are cross-shareholdings between Troy and the two major shipping companies, Condor Ferries and Huelin. Such cross-shareholdings create incentives for Troy to favour Condor Ferries and Huelin at the expense of independent third party shipping companies in providing stevedoring services. The issue is whether cross-shareholdings between stevedores and shipping companies should be regulated in the interests of promoting competition and efficiencies in the provision of shipping services.

Discussion

Cross-shareholdings are a form of vertical integration between two levels of economic activity (in this case, between stevedoring and shipping). As previously discussed in relation to Issue 7, there are economies to be gained from vertical integration such as reduced transaction costs, greater information flows and co-ordination, and more synchronised investment in facilities and technologies.

However, where there is vertical integration between a non-competitive activity (such as stevedoring) with potentially competitive activities (such as shipping), there are clear incentives for the sole provider to discriminate in favour of its related downstream companies to the competitive disadvantage of independent third parties. As mentioned in the discussion on Issue 7, such conduct is called 'leveraging of market power' and may be prohibited under competition law.

Submissions are sought on whether cross-shareholdings between stevedores and shipping companies is of concern and whether it should be regulated in the interests of promoting competition and efficiencies in the provision of shipping services. Further submissions are requested on whether the abuse of dominance provisions in the Competition (Jersey) Law are adequate to deal with the issue, or industry-specific regulation is required.

Issue 13: Commercialisation of Jersey Harbours

Outline of the issue

Current States' policy in relation to the Port is for the greater commercialisation of Jersey Harbours activities and to give the JCRA the role of monitoring the pricing of the services of what would become 'Harbours Limited'.[23] The issue is, as for the regulation of shipping services, what form this regulation should take (eg, efficiency audits, accounting separation, price monitoring, etc).

Discussion

The cost of Port services to transport operators and freight forwarders has been the subject of a number of reports over the years, particularly in respect of harbour dues (the cost of stevedoring services is an integral aspect of Issue 10 discussed above).

Jersey Harbours has a number of profit centres and each, other than the provision of coastguard services, is expected to trade profitably and provide a return to its owner, the States. Commercialisation of the business activities of government owned instrumentalities is a key principle of competition policy: without commercial incentives, it is difficult to create the incentives to improve efficiency and reduce costs to users.

In a commercial environment, competition drives prices down to the level of costs. In the absence of competitive in relation to the provision of Port services in Jersey, the 'second-best' option would appear to be regulation by the competition authority as a proxy for the absent competition. Particular areas for future regulation may be the commercial leasing of Port facilities to stevedores, the level of harbour dues, and any cross-subsidisation between commercial and non-commercial services (such as coastguard activities).

Submissions are requested on the form regulation should take in relation to the commercial services of Jersey Harbours. Should it be similar in form to that for Jersey Telecom and Jersey Post? Or should other forms of regulation be adopted?

Issue 14: Ramp permits

Outline of the issue

Current shipping policy is that no car and passenger ferry should obtain ramp access unless its operating company has secured a SLA. Freight services require a ramp permit but no SLA. The States propose that future applications for ramp access be considered on their merits taking into account criteria set by the Minister for Economic Development in addition to Harbour operational and safety requirements. The issue is how ramp permits should be most efficiently allocated.

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[23] *Future Air and Sea Transport Policy*, Consultation Document, Economic Development Committee, May 2005, para 5.18.

Discussion

The outcome of previous SLA negotiations has been the granting of permits for the use of the ramps in St Helier Harbour on condition that the provisions of the SLAs were met.

The JCRA seeks submissions on whether ramp permits should be issued by Jersey Harbours on a fully commercial basis or be subject to criteria in future SLAs. If the latter, submissions are sought on the content of those criteria. Submissions on this issue should also take into account the regulatory issues discussed under Issues 5 to 7.

Issue 15: Other issues

There are a number of 'micro' issues in relation to the Ports. Though grouped together in this miscellany, they may nonetheless cause significant inefficiencies in the Port. Two of the issues are discussed below.

Stevedoring for 'Ronez'

The JCRA understands that a full stevedoring gang is required for the berthing and unloading of the cement carrier Ronez when in practice the only stevedoring service that is required is the connection of the ship to a cement discharge pipeline which goes to the storage silo.

Number of tugmasters

Claims have been made that there is an excessive number of tugmasters.[24] Currently, the JCRA understands that there are about 20 in Troy's fleet and it has been suggested that an efficient tug service could be provided by half that number.

The JCRA seeks submissions on the efficiencies of the Ronez stevedoring and tugmaster services provided by Troy. Submissions are also requested on any other issues in the Ports which may be considered relevant from an efficiency perspective.

Jersey Competition Regulatory Authority

3 October 2006

[24] Tugmasters are the 'lorry cab bit' which are used to haul trailers off ro-ro freight ferries.