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## Working Party No. 2 on Competition and Regulation

### COMPETITION ISSUES IN LINER SHIPPING

-- Japan --

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*More documents related to this discussion can be found at: <http://www.oecd.org/daf/competition/competition-issues-in-liner-shipping.htm>*

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-- Japan --

## **Introduction**

1. Export and import trade with other countries is essential for the economic development of Japan, an island nation, and the logistics aspect of this trade is supported by international transportation activities. In Japan, the majority of trade cargo transportation (99.7%) is borne by maritime transportation on ships.

2. All three of the major shipping companies in Japan (Nippon Yusen Kabushiki Kaisha, Mitsui O.S.K Lines, Ltd., and Kawasaki Kisen Kaisha, Ltd.) provide both liner shipping service and tramper shipping service and support the logistics aspect of Japan's trade.

3. This paper will focus in particular on the international ocean liner shipping sector and provide an outline of the sector, its competitive environment, the system of exemption from the Antimonopoly Act, such as the shipping conference, and a case of the Antimonopoly Act application.

### **1. Outline of the international ocean liner shipping sector**

#### ***1.1 History***

4. The history of the modern shipping industry in Japan began more than 130 years ago, and after being devastated in World War II, the shipping industry made an astonishing recovery in the post-war period. With the integration of major shipping companies into the six core companies in 1964<sup>1</sup>, the international ocean shipping companies in Japan continued to face severe business environment, such as the appreciation of the yen following the Plaza Accord in 1985.

5. In 1989, two of the six core companies, Yamashita-Shinnihon Steamship Co., Ltd. and Japan Line, Ltd., merged to form Navix Line, Ltd. In 1998, Nippon Yusen, another one of the six core companies, merged with Showa Line, Ltd. That same year Mitsui O.S.K. Lines, Ltd. was also formed through the merger of the former Mitsui O.S.K. Lines and Navix Line. This series of mergers gave rise to the present market structure dominated by three major companies<sup>2</sup>, which includes Nippon Yusen (hereinafter referred to as "NYK") and Kawasaki Kisen (hereinafter referred to as "K-Line") in addition to Mitsui O.S.K. Lines (hereinafter referred to as "MOL").

#### ***1.2 Liner shipping***

6. Liner shipping is the transportation provided by ships that operate in accordance with definite ocean route plans (with the fixed number of operating ships and navigations) on ocean routes in which the anchorage sites and dates (days) are decided in advance, regardless of the volume of shipments. Liners are categorized into container ships, which exclusively transport cargo in containers, and regular liners, which mainly transport cargo in the same shape as is packed. Currently most liners are operated by container ships. While the three major international ocean shipping companies in Japan offer liner shipping services, almost no other shipping companies in Japan offer these kind of services.

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<sup>1</sup> In 1963, in order to reinforce operating infrastructure of the shipping companies suffering from a slump in business, the Government passed two bills, on so-called "the two laws relevant to shipping industry reconstruction and adjustment" through the Diet, and in 1964, completed the integration of shipping companies.

<sup>2</sup> The JFTC reviewed those merger cases and concluded that those cases raised no competitive concern.

7. Shipping companies that offer liner shipping services maintain large-scale cargo booking systems through the establishment of branches, satellite offices, and agents in areas around anchorage sites. To maintain a steady level of services for consignors, that is, the users of their services, liner shipping companies own and operate a certain sized fleet of ships. They also own and manage container terminals and a large number of containers. For these reasons, liner shipping services require a huge amount of capital, and as a result oligopolistic market structure had been formed by a limited number of companies.

8. The three major companies in Japan possess one of the largest business scales in the world in terms of sales and the number of ships owned, but the sales from container ships account for a relatively low percentage of their total sales, with 21% for NYK, 40% for MOL and 41% for K-Line<sup>3</sup>. Moreover, as of July 2014, in the share of container ships in the world<sup>4</sup>, the Japanese shipping companies MOL, NYK, and K-Line held 3.4% (the tenth largest), 3.0% (the twelfth), and 2.1% (the sixteenth) respectively.

9. In general, shipping companies that offer liner shipping services mainly compete with each other in terms of (i) freight rates<sup>5</sup>, (ii) the provision of fixed day services, (iii) the shortening of transit time, (iv) the increase in the frequency of services, and (v) the improvement in information services.

## 2. Shipping Conferences, Consortiums, and Alliances

### 2.1 *Shipping Conferences*<sup>6</sup>

10. The shipping conferences of which Japanese shipping companies are currently members include<sup>7</sup> “the Australia New Zealand / Eastern Shipping Conference (ANZESC)”, a conference on the route that link ports in Japan and South Korea with those in Australia, New Zealand, and Papua New Guinea (participating members include NYK, MOL, and K-Line); “the Far East / South Asia - Middle East Conference (FESAMEC)”, a conference on the route that link ports in Japan with those mainly on the western coast of India, Pakistan, and the Persian Gulf (participating members include NYK, MOL, and K-Line); and “the Japan / Gulf of Aden & Red Sea Ports Conference (JGARSPC)”, a conference on the route that link ports in Japan with those on the Gulf of Aden and the coast of the Red Sea (NYK is a participating member, MOL is a non-member in the liner section, and K-Line left the conference in February 2013). There are also some other conferences of which Japanese shipping companies are currently members<sup>8</sup>. The amount and rates of basic freight rates and surcharges, such as the Bunker

<sup>3</sup> 2014 Nikkei Gyokai Chizu (Nikkei Publishing Inc.)

<sup>4</sup> Page 9 of Fact Book 2014, published by the Kawasaki Kisen Kaisha, Ltd.

<sup>5</sup> The freight rates of container ships in most cases are generally comprised of basic freight rates, surcharges, and special freight rates. Basic freight rates are set as bulk freight rates per container or are calculated, in principle, by multiplying the larger of either volume or weight in tones by freight rates. Surcharges are charged when the transportation costs become higher due to the conditions of ports, economic situations, and other factors. They typically include the CAF (Currency Adjustment Factor), BAF (Bunker Adjustment Factor), THC (Terminal Handling Charge), and PSS (Peak Season Surcharge). Special freight rates generally refer to freight rates that are set out in service contracts (agreements for discounted freight rates in exchange for consignors’ guarantee shipments for a certain period to shipping company).

<sup>6</sup> A shipping conference is an international shipping cartel in which multiple shipping companies that operate liners on the same ocean routes agree on freight rates and other operational matters to restrict competition between each other and to mutually generate profit.

<sup>7</sup> The world’s oldest and most traditional shipping conference is the Far Eastern Freight Conference (FEFC), and the three major Japanese shipping companies were also its members. However, as a result of abolishing the system for exemption from the EU competition law, the FEFC was closed and dissolved in 2008.

<sup>8</sup> Web page of the Shipping Conference and General Administration (SCAGA) <http://www.scaga.net/index.html>

Adjustment Factor (BAF) and the Currency Adjustment Factor (CAF), are determined by the above mentioned shipping conferences.

## **2.2 *Consortiums and Alliances***<sup>9</sup>

11. Among Japanese shipping companies, NYK is a member of the Grand Alliance (Hapag-Lloyd (Germany) and OOCL (Hong Kong) in addition to NYK are members). MOL is a member of the New World Alliance (APL (Singapore) and HMM (South Korea) in addition to MOL are members), while K-Line is a member of the CKYHE Group (COSCO (China), Yang Ming (Taiwan), Hanjin (South Korea), and Evergreen (Taiwan) in addition to K-Line are members).

12. The scale of the alliances among the above mentioned shipping companies appears to expand even further. In 2012, the Grand Alliance and the New World Alliance formed an alliance to establish the “G6 Alliance”.

## **3. Exemption from the Antimonopoly Act for the liner service sector**

### **3.1 *Outline of the exemption from the Antimonopoly Act***

13. The Maritime Transportation Act was enacted in 1949 to protect the interests of maritime transportation users, to promote the sound development of the maritime transportation business, and thereby enhance public welfare through adequate and reasonable operations by maritime transportation enterprises. In the Maritime Transportation Act, it is stipulated that agreements on freight rates by shipping conferences, etc. shall be exempted from the Antimonopoly Act on condition that prior notification is submitted to the Minister of Transport (now, the Minister of Land, Infrastructure, Transport and Tourism)(hereinafter referred to as the “Minister”) on the ground that establishing freight rates agreements was a common practice in the international ocean shipping sector, and such practice was exempted from the competition laws also in other jurisdictions. Under the Maritime Transportation Act, the exemption from the Antimonopoly Act is applicable to both liner services and tramp services. In fact, shipping conferences such as ANZESC, FESAMEC and JGARSPC referred to in 2.1 have been notified beforehand to the Minister based on the Maritime Transportation Act and thereby have been exempted from the Antimonopoly Act.

14. Moreover, consortium and alliance agreements would not necessarily be deemed as cartels unless they are agreements on freight rates, market sharing, or limits on supply volumes. However, they will also be exempted from the Antimonopoly Act if prior notifications are submitted to the Minister based on the Maritime Transportation Act. In fact, alliances such as G6 Alliance and CKYHE referred to in 2.2 have been notified beforehand to the Minister and thereby have been exempted from the Antimonopoly Act.

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<sup>9</sup> Consortiums and alliances make agreements on the space charters for container ships, the joint use of quay terminals, the adjustments of operational schedules, and other matters without making agreements on freight rates or surcharges, unlike shipping conferences,

### **3.2 *Cases where the Antimonopoly Act is applicable (Article 28 of the Maritime Transportation Act)***

15. As described above, under the Maritime Transportation Act, the conclusion of international ocean shipping agreements shall be exempted from the Antimonopoly Act, on condition that prior notification is submitted. However, the Antimonopoly Act may be applied in cases where unfair trade practices are employed<sup>10</sup> and the interests of users are unduly impaired by substantially restraining the competition in a particular field of trade and in other cases.

### **3.3 *Alteration orders and prohibition***

16. The system has been established in which the international ocean shipping agreements in question may be altered or prohibited by the Minister's own or in response to the demand by the Japan Fair Trade Commission (hereinafter referred to as the "JFTC"), when notified international ocean shipping agreements unduly impair the interests of users or in other similar cases.

#### **3.3.1 *Alteration orders and the prohibition of international ocean shipping agreements by the Minister of Land, Infrastructure, Transport and Tourism (Article 29-2 of the Maritime Transportation Act)***

17. It is stipulated that, when the Minister receives notification of an international ocean shipping agreement, if the minister judges that the contents of the agreement does not conform to any of the following conditions, the Minister shall order the shipping company to alter the contents of the agreements in question or shall prohibit acts based on the agreement: (i) the agreement shall not unduly impair interests of users, (ii) the agreement shall not be unduly discriminative, (iii) the agreement shall not unduly restrict participation and withdrawal, and (iv) the agreement is the bare minimum in light of the objective thereof.

#### **3.3.2 *Demand by the JFTC to take measures (Article 29-4 and the proviso of Article 28 of the Maritime Transportation Act)***

18. According to these provisions, a notification of an international ocean shipping agreement that has been received by the Minister shall be conveyed to the JFTC without delay. If the JFTC deems that the details of the international ocean shipping agreement in question does not conform to any of the conditions (i) through (iv) of (3.3.1) above, it may demand the Minister to take measures to order the enterprises to alter the contents of the agreement or prohibit acts based on the agreement. In addition, when the JFTC issues such demands to take measures, it shall notice to that effect through official gazettes, and if the Minister does not issue alteration orders or prohibit acts within one month from the day when the above notice is placed by the JFTC through official gazettes, the agreement in question is excluded from exemption from the Antimonopoly Act, and the Antimonopoly Act is directly applied to the agreement.

### **3.4 *Developments related to the exemption system***

19. Relevant developments in the system for exemption from the Antimonopoly Act under the Maritime Transportation Act, including those related to revisions leading to the current system, are as follows. The provisions regarding the demand to take measures for order for alteration of the contents of the agreement or prohibition of the acts based on the agreement described in 3.3 has been introduced into the Maritime Transportation Act as a result of the review of the exemption in 1999.

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<sup>10</sup> The JFTC established Designation of Specific Unfair Trade Practices in the Maritime Business in 1959 for unfair trade practices in the shipping sector. This designation was abolished in 2006, and since then unfair trade practices in the shipping sector have been treated under the Designation of Unfair Trade Practices in the same manner as unfair trade practices in other areas.

*3.4.1 Revision of the system for exemption from the Antimonopoly Act and the introduction of provisions related to the involvement of the JFTC (Article 29-3 and Article 29-4 of the Maritime Transportation Act) (1999)*

20. In the 1990s of Japan, it has been widely recognized that it was essential to actively develop competition policies, in addition to the promotion of deregulation, to achieve a free and fair economic society. At the backdrop of such situation, the system for exemption from the Antimonopoly Act was revised in 1999, resulting in the abolition of 34 systems.

21. In this revision, exemption system for international ocean shipping was also in the scope of review, but it was decided that the exemption system would remain in effect, mainly due to the fact that such exemption systems for international ocean shipping were also adopted in other jurisdictions. However, in this revision, although it was decided that the exemption system under the Maritime Transportation Act would be maintained, the following provisions were introduced into the Maritime Transportation Act: (i) an agreement notified by an international ocean shipping companies shall conform to the four conditions, including the condition that the agreement shall not unduly impair the interests of users, (ii) if the contents of a notification do not conform to any of the conditions, the Minister shall order the operator to alter the contents of the agreement in question or prohibit acts based on the agreement, and (iii) the notification on the contents of the international ocean shipping agreement that has been received by the Minister shall be conveyed to the JFTC without delay, and if the JFTC deems that the agreement does not conform to any of the four conditions above, it may issue a demand to the Minister to take measures.[Please refer to 3.3].

*3.4.2 A report by the Study Group on Regulations and Competition Policy: "Issues Concerning the International Shipping Market and Competition Policy" (published on December 6, 2006)*

22. In January 2005, the JFTC started to conduct research that focused largely on the state of competition in international ocean shipping, and it conducted interviews and surveys with consignors, shipping operators, relevant organizations, experts, and other parties. Based on this research, the JFTC examined the state of competition in international ocean shipping and competition policy issues, and, as part of this research, it also conducted the studies on the exemption system for international ocean shipping as necessary. The report offered the following views on the reasons for maintaining the exemption system in the revision of 1999 such as (i) the existence of opinion that shipping conferences provide for stable freight rates and are also favorable to consignors, and (ii) the need to sustain international accord with the situations in the United States and the European Union, etc.

(i) Unified freight rates (tariff) set by shipping conferences are no longer effective in practical terms. Although agreements on surcharges other than shipping rates among shipping companies and concerted rate increases, also known as rate restoration, remain effective, consignors claim that shipping operators may possibly charge more than the actual costs they incur, that the calculation grounds are not clear, and that notice is given in a unilateral way. For these reasons, the report indicates that there would be the possibility that the interests of consignors (users) may have been impaired.

(ii) The scope of exemption varies among Japan, the United States and EU, and the EU decided to abolish the exemption system in October 2008.

23. Thus, the report presented the JFTC's views that the two previously mentioned reasons do not hold any ground today. The report concluded that it expected the Ministry of Land, Infrastructure, Transport and Tourism (hereinafter referred to as the "MLIT") to review the need for the exemption from the Antimonopoly Act for international ocean shipping by taking into account the views of the JFTC and the contents of the report of the study group.

### 3.4.3 *Recent developments related to the exemption system*

24. In response to the cabinet decision in Japan about the policy on regulatory/systemic reforms on June 18, 2010, it was determined to consider the revision of the system for exemption from the Antimonopoly Act for international ocean shipping, and the MLIT that holds jurisdiction over the Maritime Transportation Act and the JFTC held deliberations. During these deliberations, the MLIT claimed that (i) Japan's major trading partners still maintained such exemption systems and (ii), considering fluctuations in freight rates in ocean routes in Europe, etc. that took place after the abolition of the system for exemption from the EU competition law, there were concerns about the negative effects that would be caused by the abolition of the exemption system in Japan. Consequently, it was decided that the exemption system would remain in effect. However, the MLIT concluded that, taking into account the future developments in other jurisdictions on the system, interests of consignors, effects on the Japanese economy, etc., it would re-examine the revision of the system within fiscal year 2015, holding deliberations with the JFTC.

## 4. **A case of the application of the Antimonopoly Act**

25. Case concerning to international ocean shipping companies that provide automobile shipping services<sup>11</sup> (March 18, 2014; Cease and desist orders and surcharge payment orders)<sup>12</sup>

26. This case is an example of the application of the Antimonopoly Act to the shipping operations of pure car carriers and pure car and truck carriers, which are trampers. Although it is not a case in the liner transportation sector, we would like to introduce the case as an example in a similar sector because shipping conferences also exist among car carriers, and exemption from the Antimonopoly Act stipulated in the Maritime Transportation Act is applicable to them as previously described.

### 4.1 *Outline of the Violations*

27. The international ocean shipping companies (NYK, K-Line, etc.), from at least as early as around mid-January 2008, for the purpose of maintaining existing transactions and preventing freight rates from falling, agreed to mutually refrain from contending for customers by not offering lower freight rates and to raise or maintain freight rates for respective consignors, in the fields of particular international ocean shipping services for automobiles<sup>13</sup> in four ocean routes<sup>14</sup>.

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<sup>11</sup> The international ocean shipping companies mean companies that are engaged in the business that carries persons or goods by ship at sea, other than the harbor transportation enterprise, as stipulated in paragraph 2 of Article 2 of the Maritime Transportation Act.

<sup>12</sup> <http://www.jftc.go.jp/en/pressreleases/yearly-2014/March/140318.html>.

<sup>13</sup> "Particular international ocean shipping services for automobiles" means the services for transporting new cars and trucks from Japan to other countries, upon demand of consignors, namely automobile manufactures and trading companies, located in Japan (excluding the shipping services related to the sole and preferential trade between the particular consignor and the particular shipping company which this consignor have invested).

<sup>14</sup> North American route, European route, Middle and Near Eastern route, Oceanian route

28. In accordance with the agreements, the companies, among other things:

(i) fixed freight rates, the rate of increase, etc. and/or colluded freight rate quotations to submit to consignors among the companies who have trade with the same consignors at negotiating with respective consignors; and

(ii) refrained from bidding against one another for the purpose of securing incumbent trades by submitting higher freight rate quotations than the incumbent shipping companies that have trade with the consignor.

29. By the agreement, the international ocean shipping companies substantially restrained the competition in the field of particular international ocean shipping services for automobiles in each ocean route, contrary to the public interest. The JFTC found that the companies violated Article 3 (prohibition of unreasonable restraint of trade) of the Antimonopoly Act, and issued cease and desist orders and surcharge payment orders against the companies, under Article 7(2) and Article 7-2(1) of the Antimonopoly Act.

#### **4.2 *Relationship between the violations and the exemption from the Antimonopoly Act under the Maritime Transportation Act***

30. In some parts of the four ocean routes, the international ocean shipping companies (including the violators) had notified the Minister of cartels exempted from the Antimonopoly Act (hereinafter “exempted cartels”). However, the said violations as described in above 4.1 were different from the exempted cartels notified by the companies<sup>15</sup>. From the fact that such conducts were not exempted from the Antimonopoly Act, the JFTC applied the Antimonopoly Act to this case.

#### **4.3 *The Request to the MLIT***

31. As a result of its investigation, the JFTC found that the freight rates were decided through bilateral negotiations between respective consignors and the shipping companies, depending on consignors’ demand. Hence the tariffs (freight rate tables consisting of the basic freight rate and/or any other surcharges, which are uniformly applied to all consignors) stipulated in the exempted cartels were rarely or never applied to actual transactions.

32. Reflecting the facts mentioned above, it would be possible that the notified exempted cartels do not comply with the requirements for exemption from the Antimonopoly Act, stipulated in each item of paragraph 2 of Article 29 of the Maritime Transportation Act. Accordingly, the JFTC requested the MLIT to review the applicability of the requirements and take necessary measures swiftly on exempted cartels related to the international ocean shipping services for new automobiles, including their abolition. In response to the requests by the JFTC, the MLIT is currently considering further responses.

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<sup>15</sup> In the part of four ocean routes, the companies had notified the Minister of exempted cartels on the freight rate tables (tariffs) consisting of the basic freight rates and/or any other surcharge, which are uniformly applied to all consignors. However the violators committed the violations as described in above 4.1 which were different conduct from cartels on tariffs.