

1 April 2015

Mr Tim Watling
Committee Secretary
Senate Standing Committees on Rural and Regional Affairs and Transport
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By email: rrat.sen@aph.gov.au

Dear Mr Watling

During the Committee's hearing held in Townsville on Friday, 13 March 2015 the time to respond to the Committee's questions was short. This letter responds to a competition policy issue raised by Senator Canavan and addresses two issues raised during the hearings.

Section 46 – Australian Competition and Consumer Act (CCA) 2010

In Townsville, Senator Canavan sought my views on the comments the Chairman of the Australian Competition and Consumer Commission (ACCC) made in the 25 February 2015 Public Hearings of the Senate Economics Legislation Committee (Estimates) in relation to Section 46 of the *Australian Competition and Consumer Act (CCA) 2010*.

In those Senate Estimates hearings Senator Dastyari expressed a concern of many small businesses that the current system does not enable them to easily address anticompetitive behaviour of larger businesses.

In his response Mr Sims identified deficiencies in the CCA saying in relation to Section 46 in part:

"... the provision is a competition provision. It only kicks in if you are misusing your market power to damage one of your competitors. If you are just doing something nasty to someone downstream or upstream, it is not a misuse of market power" (Hansard, p139).

In their final report, Competition Policy Review (31 March 2015), the Harper Committee also found Section 46 of the CCA is "deficient in its current form". The Committee reports:

"It does not usefully distinguish pro-competitive from anti-competitive conduct. Its sole focus on 'purpose' is misdirected as a matter of policy and out of step with international approaches.

Section 46 should instead prohibit conduct by firms with substantial market power that has the purpose, effect or likely effect of substantially lessening competition, consistent with other prohibitions in the competition law. It should direct the court

to weigh the pro-competitive and anti-competitive impact of the conduct” (Harper Review, p9).

On 15 May 2014, CANEGROWERS and ACFA wrote to the ACCC raising our concerns about mills misusing their regional mill monopoly processing power by coupling their sugar production and marketing activities in contravention of Section 46. By denying growers’ rights and preventing them from exploring competitive offers and engaging the sales and marketing services of others, sugar mills are engaging in anticompetitive behaviour. In the short term, this exercise of their monopoly market powers will substantially damage or eliminate QSL as a competitor. In the longer term it will prevent the entry of new suppliers, and with it, will prevent the development of a market of these services. We also expressed concern that Wilmar’s proposed marketing structure is an arrangement that would be in contravention of Section 47 of the CCA which prohibits exclusive dealing.

The ACCC Chairman and the conclusions drawn by the Harper Review make it clear that as presently cast the provisions of Section 46 do not adequately deal with cases where there are significant imbalances in market power between different segments of a supply chain as occurs between sugarcane growers and the mill they supply and where the use of that market power has the likely effect of substantially lessening competition.

In response to Senator Canavan’s question in relation to Section 46 of the CCA: It is clear that Section 46 of the CCA does not effectively deal with monopsonistic situations such as those confronting sugarcane growers where mills’ actions have “the purpose, effect or likely effect of substantially lessening competition in that or any other market” (Harper Review, p23). A *bona fide* role for government is to restore balance in the market for sugarcane and to establish a regulatory structure that prevents the misuse of market power, addresses market failure, and ensures cane growers are not disadvantaged by the mills they supply.

In the case of the Senate’s present review of sugar marketing, time is of the essence. Growers need a framework in which they can have confidence to enable their ongoing investment in the industry. In the normal course of business, pricing and investment decisions are made well before the commencement of a season. For the 2017 season, a critical time is the commencement of the 2015 season, when the first investment decisions will be made following the Wilmar, MSF Sugar and Tully Sugar announcements of their withdrawal from QSL and subsequent notice of termination of cane supply agreements.

The establishment of a sugar industry specific mandatory code of conduct under the relevant provisions of the CCA will provide a timely resolution to the competition policy issue so clearly enunciated by Mr Simms and by the Harper Review Committee.

Grower’s pricing ability

In his opening remarks in Townsville Mr Rutherford (Wilmar) said,

“Today, Queensland cane (*sic*: cane) growers can also forward price their cane and manage up to 99 per cent of their sugar price explosion (*sic*: exposure)” (Hansard, p37).

In making these remarks Mr Rutherford was referring to growers' ability to have some say over the pricing of the futures component of the sugar transaction. He did not say that this pricing ability is limited to 20% of each grower's expected production three years forward. This increases to 40% two years forward and peaks at 60% one year forward. In any given season a grower can price a maximum of 60% of their futures exposure. The balance of their price risk management is in the hands of the marketer, presently QSL. In the absence of grower choice in the marketing of grower economic interest sugar, this pricing will be undertaken by the mill the grower supplies.

While the industry's present marketing arrangements and associated pricing structures provide growers with a number of pricing options, in any given season, a grower can price no more than 60% of their production. The balance of each grower's production is pooled and allocated to the QSL Harvest Pool. This pool, used to manage production risk, is priced by QSL independently of the mill the grower supplies.

Following their withdrawal from QSL, Wilmar, MSF Sugar and Tully Sugar will assume the responsibility for pricing this element (40%) of their growers' futures market price exposure.

Such a change would represent a fundamental shift in each grower's price risk profile. A business change over which growers had no say or no choice and a direct consequence of mills misusing their regional mill monopoly power.

Sharing Arbitrage Gains

In his response to a question from Senator Bullock about how Wilmar proposed to share the trading profits or arbitrage gains associated with their trading activities, Mr Rutherford confirmed the concerns that CANEGROWERS and ACFA hold about the potential dilution of returns to growers when he said,

"These are potential value-adding opportunities that exist over and above the current marketing arrangements that QSL can deliver, so this is an added component of value. That added component of value is generated because of the synergy between the Australian-origin sugar that is traded in Wilmar's book and the other-origin sugar. As you would appreciate, Wilmar has a large book of other-origin sugar. Where there are opportunities to generate synergies between those books by virtue of the fact that there is other sugar that is owned by Wilmar Sugar Trading, those benefits will be split fifty-fifty. But I really want to emphasise the point that this is value that is over and above the value that QSL can deliver" (Hansard, p47).

To be clear, QSL presently engages in the trading activity Mr Rutherford suggests that Wilmar will be looking to exploit. All of the gains QSL makes from such trading activities are shared between mills and growers on the basis described in the industry's longstanding payment structures, approximately two-thirds to growers and one-third to mills. Confirming the profit sharing approach outlined in section 6.1 of CANEGROWERS-ACFA joint submission to the Committee (13 October 2014), Mr Rutherford makes it very clear that it is Wilmar's intention to share with growers just 50% of the gains Wilmar makes from such trading activities.

In doing so, Mr Rutherford confirms Wilmar's intention to reverse the industry's longstanding payment structures for profits from such sales, with approximately one-third of the revenues flowing to growers and two-thirds flowing to Wilmar.

CANEGROWERS is not calling for the re-establishment of the heavy hand of a single desk but a call for a light form of regulation that restores balance by taking account of and addressing the competition policy issues our industry faces.

Yours faithfully

Warren Males
Head-Economics