Chapter 3

Competition issues and market distortions

3.1 This chapter reviews a range of competition issues, including the impact of the market dominance of key players in the industry. The chapter also discusses the nature and extent of a range of market distortions. The chapter highlights the need for effective competition in the industry and for greater transparency.

Market dominance

3.2 The dominant market position of key players in the industry, especially Incitec Pivot Ltd (IPL) in eastern and southern states, and CSBP Ltd in Western Australia, and the possible implications this holds for competition, was commented upon extensively during the inquiry. For example, the National Farmers Federation (NFF) noted that 'it is prudent to examine the effect of increased rationalisation within the fertiliser supply market, particularly on the east coast of Australia, on the prices offered to Australian farmers'.[1]

3.3 Submissions expressed concerns about the market dominance of key players and the possible impact on fertiliser prices. The Australian Cane Farmers Association stated that:

> Our concern is that with recent mergers in the Australian fertiliser industry, additional profit resulting from domestic market power may also be embedded in the price increases. When accounting for currency, freight and handling, and margin, the price differential between global and Australian prices appears excessive.[2]

3.4 The Bookham Agricultural Bureau also raised similar concerns.

> We are concerned at the perception that a monopoly power is held by Incitec Pivot. That this monopoly power is beneficial to that company is apparent from is profitability and burgeoning share price. On two occasions the Australian Competition and Consumer Commission (ACCC) considered the competitive effects of mergers and acquisitions in the fertiliser industry and came to the conclusion that there would be no lessening of competition…One company now has fifty percent of the domestic fertiliser market. Irrespective of the global pressures on the price of fertiliser this cannot be a healthy situation for the consumer.[3]

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1 *Submission* 20, NFF, p. 8.

2 *Submission* 27, Australian Cane Farmers Association, p. 1.

3 *Submission* 9, Bookham Agricultural Bureau, pp 1-2.

3.5 Similarly, Mr Rodney Abbott of the Australian Fertiliser Services Association (AFSA) commented that:

> **Mr Abbott** – They [IPL] effectively control the market. They manufacture a very significant quantity of the fertiliser consumed in Australia. They sell a portion of that manufacture to the other wholesale suppliers so the market is very aligned, if you like, to one manufacturing source.
>
> **Senator O'BRIEN—**So there was an error made in permitting the merger of Incitec and Pivot?
>
> **Mr Abbott—**It certainly reduced competition.[4]

3.6 CANEGROWERS Isis Ltd stated that IPL, through acquisitions and mergers, 'has all but removed the competition in Queensland and can manipulate the market'.[5]

3.7 Similar concerns were raised in relation to the market dominance of CSBP in Western Australia. One witness characterised the situation in the following terms:

> Traditionally, CSBP were the only supplier here until some competition was introduced. They still have a strong presence and probably are the market leader—the trendsetter…despite not having a large manufacturing capacity these days, they have certainly maintained their market dominance.[6]

3.8 One submission stated that the fertiliser market in Western Australia is 'dominated by a small number of large suppliers'.[7] Another witness described the situation in Western Australia as 'maybe a duopoly or a cartel'.[8]

3.9 CANEGROWERS Isis provided a telling example of the use of market power by IPL. The company attempted to facilitate bulk purchase orders with fertiliser companies Incitec Pivot and Hi Fert, which ultimately proved unsuccessful. The company stated that Incitec Pivot was not prepared to discuss the matter, claiming it was a matter for their local distributor/retailer to offer. CANEGROWERS Isis argued that it was their understanding that Hi Fert wanted to build market share in the area but expressed concerns to CANEGROWERS at possible retaliation by IPL (by reducing the price, sales would then flow away from Hi Fert) and declined to negotiate an agreement.[9] CANEGROWERS Isis expressed the belief that the

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4 Mr Rodney Abbott, Australian Fertiliser Services Association, *Committee Hansard*, 16 May 2008, p. 28.

5 *Submission* 18, CANEGROWERS Isis, p. 2.

6 Mr Trevor De Landgrafft, WAFarmers, *Committee Hansard*, 16 May 2008, p. 64.

7 *Submission* 14, PGA Western Graingrowers, p. 1.

8 Mr Michael Fels, WAFarmers, *Committee Hansard*, 16 May 2008, p. 64.

9 *Submission* 18, CANEGROWERS Isis, pp 1-2; Mr Geoffrey McCarthy, CANEGROWERS Isis, *Committee Hansard*, 23 July 2008, pp 61-62.

companies 'were firm in their knowledge that that growers had limited options but to buy fertiliser at the prices charged'.[10]

3.10 Some submissions alluded to the existence of cartel-like behaviour amongst major companies.[11] One submission noted that in the eastern states there are strong business linkages between the major suppliers of fertiliser which facilitates 'cartel-like behaviours'.

> Specifically, the main producer/wholesaler is IPL (Incitec-Pivot Limited) a merger of the previous two main suppliers into South-east Australia. IPL through its ownership of Southern Cross Fertilisers in Queensland is currently a monopoly manufacturer of phosphorus products in Australia.
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> IPL's next biggest competitor is Hi-Fert, which was once owned by WMC and then BHP but is now wholly owned by Elders and Landmark. Yet two of IPL's largest wholesale/retail customers are Elders and Landmark.
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> Given the incestuous business relationships where various entities are both customer and competitor there is reduced price competition and increased opportunity for cartel-like behaviours.
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> IPL made a smart business decision, vertical integration, in purchasing Southern Cross Fertilisers – manufacturer and exporter of phosphorus products – and this seems to have contributed to their rapidly rising share price. However how much of the fabulous IPL share price has been generated by gratuitous profit made by wholesale and retail price gouging of the Australian farmer using the excuse of world parity pricing?[12]

3.11 The question was posed as to how the government can effectively ensure that farmers are protected from cartel-like pricing when the fertiliser companies are vertically integrated and 'enmeshed in business arrangements with competitors who are also their customers'.[13]

3.12 Another submission also noted that:

> Instead of opening the market to other competitors, the fertilizer industry has shrunk to eliminate local and international competition and any semblance of customer service, with local dealers being little more than debt collectors and delivery men for the cartels who control the market.[14]

3.13 AgForce Grains noted that while there seems to be little direct evidence of collusion or restrictions on competition, individual farmers are concerned that anti-competitive behaviour exists, particularly in the fertiliser market 'but do not have the

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10 *Submission* 18, CANEGROWERS Isis, p. 2.

11 A cartel is an organisation of independent firms which has as its aim some form of restrictive influence on the production or sale of a commodity.

12 *Submission* 22, Peter & Yvonne Abel, p. 2.

13 *Submission* 22, Peter & Yvonne Abel, p. 2.

14 *Submission* 34, Ms Margaret Menzel, p. 2.

resources or scope to investigate and prove it'.[15] PGA Western Graingrowers also noted that 'it is difficult, if not impossible for growers to assess whether cartel behaviour is having an effect on the price of fertiliser', just as it is for the Australian Competition and Consumer Commission (ACCC) to determine these matters.[16]

3.14 As alluded to above, much of the focus of the debate during the inquiry centred on the operation of Incitec Pivot due to various mergers and acquisitions that have occurred in recent years. As noted in chapter 2, Incitec Pivot is a relatively new company, created by the merger of Incitec Ltd and Pivot Ltd in June 2003.

3.15 The ACCC, in its assessment of that merger, determined that despite the merger leading to the merged party having very high market shares in some product categories, the importation of fertiliser products was likely to operate as an effective competitive constraint on the merged entity, thereby thwarting any attempt to raise the price of fertiliser to farmers.

> Although it is expensive to enter any of the markets through the establishment of a new manufacturing facility, the importation of fertiliser products is fairly routine and does not present an insurmountable barrier. Independent imports of fertiliser products represent in excess of 20 per cent of all fertiliser products used by Australian farmers.
>
> On this basis, the Commission believes that the proposed merger is unlikely to result in a substantial lessening of competition.[17]

3.16 Incitec Pivot's scale and production capacity was greatly increased in August 2006 with the purchase of Southern Cross Fertilisers Pty Ltd, Australia's only manufacturers of mono-ammonium phosphate (MAP) and di-ammonium phosphate (DAP). Again, the ACCC assessed that the proposed acquisition was unlikely to result in a substantial lessening of competition.

> The ACCC considered that the availability and substitutability of imports as an alternative to the domestic supply of phosphate fertilisers, together with the prevalence of import parity pricing for these products, would be capable of continuing to be a constraint on IPL (and SCF) post-acquisition.[18]

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15 *Submission* 24, AgForce Grains, p. 14.

16 *Submission* 14, PGA Western Graingrowers, p. 1.

17 ACCC, 'Acquirer: Incitec Ltd; Target: Pivot Limited', 16 October 2002, cited in ACCC, Correspondence, 24 April 2008. See also Mr Tim Grimwade, ACCC, *Committee Hansard*, 14 November 2008, p. 29.

18 ACCC, 'Incitec Pivot Limited – proposed acquisition of Southern Cross Fertilisers Pty Limited', 26 July 2006, cited in ACCC, Correspondence, 24 April 2008. See also Mr Tim Grimwade, ACCC, *Committee Hansard*, 14 November 2008, pp 29-30.

3.17 The committee questioned the ACCC in relation to the efficacy of the threat of imports as a restraint on the exercise of market power. Mr Tim Grimwade, General Manager, Mergers and Assets Sales Branch of the ACCC told the committee that:

> Often the threat is sufficient to constrain the exercise of market power by the merged entity. Indeed, if there is import parity pricing then that threat does exist. Market participants did point to—I am trying to recollect in Southern Cross—a number of potential or actual importers, including HiFert, and the threat of import by other participants in the industry.[19]

3.18 However, when pressed by the committee to provide an example of this actually occurring, Mr Grimwade stated that 'offhand, I cannot tell you'.[20]

3.19 More recently, Incitec Pivot announced the further acquisition of Dyno Nobel, an explosives manufacturer and supplier that is also involved in the North American fertiliser market. The ACCC concluded that the proposed acquisition was unlikely to result in a substantial lessening of competition in the manufacture and supply of ammonia, ammonium nitrate or fertiliser products.[21]

3.20 The fertiliser industry argued that, despite the market dominance of key players, a competitive market situation exists in Australia. IPL stated that:

> The supply of fertiliser in Eastern Australia is highly competitive, and cannot be described as monopolistic. The high degree of competition within the supply chain to supply product to distributors also disproves any suggestion of cartel conduct within the industry.[22]

3.21 IPL conceded that although the company is 'unquestionably a large player' in the supply of fertiliser in eastern Australia, other large manufacturers and suppliers such as Hi Fert and Impact place a 'constant and substantial competitive discipline' on IPL.

> Competitive tension is further heightened within Australia by the relatively low barriers to entry in the industry, given readily available port and distribution facilities, limited brand loyalty given the commodity nature of the products, and significant customer switching. IPL's market share in the distribution of fertilisers has dropped from 73% to 58.5% since 2003, providing clear evidence of the competitive nature of the industry.
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> In addition to direct competitors, IPL faces competition from numerous large, rural agribusinesses, some of which are also IPL's own customers.

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19 Mr Tim Grimwade, ACCC, *Committee Hansard*, 14 November 2008, p. 30.

20 Mr Tim Grimwade, ACCC, *Committee Hansard*, 14 November 2008, p. 30.

21 ACCC, 'ACCC not to oppose proposed acquisition of Dyno Nobel Limited by Incitec Pivot Limited', *News Release*, 15 May 2008.

22 *Submission* 26, IPL, p. 10.

These include ABB and Hi Fert, which also directly import fertiliser in competition with IPL.[23]

3.22 The committee questioned IPL in relation to the above assertions. IPL acknowledged that its market share at the wholesale level is 70 per cent of the east coast market – which is a considerable greater than its share of the retail market (which is 58.5 per cent).

CHAIR—In your executive summary of your presentation, you say:

The healthy state of competition in the industry means that it cannot be described as monopolistic, or involving any cartel conduct.

How much of the Australian market do you supply?

Mr Whiteside—At a retail level, our market share is—

CHAIR—No, at the wholesale level.

Mr Whiteside—It is around 70 per cent of east coast Australia.

CHAIR—You do not think that is monopolistic? You are pulling my leg, aren't you?

Mr Whiteside—I think, if you look at the structure of the market—

CHAIR—No. Isn't 70 per cent of anything a monopoly?

Mr Whiteside—No, I do not believe it is.

CHAIR –… Think about it: you do not think 70 per cent of the market puts you in a monopoly position?

Mr Whiteside—If you suggest that being in a monopoly position gives us control—

CHAIR—A majority.

Mr Whiteside—and means other organisations cannot operate freely in that market—

CHAIR—That is not what I am saying at all. You are the majority supplier with 70 per cent of the market. I would have thought you had a monopoly on the market.[24]

3.23 The committee notes that monopoly situations are generally characterised as situations where there is only one supplier and market barriers make it impossible for new competitors to enter the market. A monopoly firm has no competition and thus has market power. The committee notes, however, that complete monopoly situations are rare but there are often situations where one large firm dominates a market. In these situations, with only a few much smaller competitors, this larger firm is able to exercise monopoly control. In this sense, a monopoly-type situation in the fertiliser industry could be seen to exist with regard to IPL and CSBP.

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23 *Submission* 26, IPL, p. 10.

24 Mr James Whiteside, IPL, *Committee Hansard*, 23 July 2008, pp 15-16.

3.24 The committee further notes that barriers to entry in the industry are high, especially at the manufacturing level. An IBISWorld study of fertiliser manufacturing in Australia concluded that the barriers are high and 'these barriers are increasing'. The study noted that large initial capital outlays are required to enter the industry; strong customer loyalty derived from existing ownership structures can pose significant entry barriers; and given that the majority of raw materials are imported, manufactures must maintain a significant network of international suppliers to provide raw materials for fertiliser manufacture.[25]

3.25 Submissions and other evidence indicated a greater degree of competition at the retail level than at the wholesale level. A NFF member survey showed that on average, farmer survey participants had 3.3 distributors in their local region. However, the NFF stated that while there are multiple suppliers/distributors in each region there are only a limited number of fertiliser companies who supply these distributors. For example, there are seven stores in Bundaberg that sell fertiliser. Six of these sell Incitec Pivot and one sells Summit fertiliser. Summit also sources some of its fertiliser from Incitec Pivot.[26]

3.26 The NFF further noted that approximately 9 per cent of NFF survey participants also stated that they had only one fertiliser distributor in their local region. – 'it is these situations that particularly concern the NFF, as there is a greater potential for excessive profiteering and price gouging due to monopolistic pressures'.[27]

3.27 The Australian Fertiliser Services Association also argued that competition at the wholesale level has been reduced but competition at the retail level 'is still very strong'.[28]

Committee view

3.28 The committee considers that the market dominance of large players in the fertiliser industry seriously compromises effective competition in the industry. This in turn has implications for the pricing of fertiliser products in this country. The committee notes that recent mergers and acquisitions in the industry have resulted in an increase in market concentration and a lessening of competition.

3.29 The committee believes that an effective monopoly may exist in relation to the fertiliser industry in Australia – with the market dominance of Incitec Pivot in eastern and southern states and CSBP in Western Australia. The committee considers that the fertiliser industry operates in a distorted market not governed by the usual

25 IBISWorld, *Fertiliser Manufacturing in Australia*, November 2007, p. 16.

26 *Submission* 20, NFF, p. 10.

27 *Submission* 20, NFF, p. 10.

28 Mr Rodney Abbott, Australian Fertiliser Services Association, *Committee Hansard*, 16 May 2008, p. 37. See also *Submission* 5, Australian Fertiliser Services Association, p. 2.

supply and demand factors and is, to a large extent, a law unto itself in the setting of fertiliser prices.

3.30 The committee notes the widespread perception in the farming community that fertiliser was stockpiled to inflate prices paid by customers. The committee believes that fertiliser prices in these instances should not have increased when 'old' stock was still available. Similarly, companies should, as a matter of course, pass onto customers the benefits of the recent falls in global fertiliser prices in local prices.

Market distortions

3.31 Concerns were raised during the inquiry that the market dominance of key players in the industry have led to distortions in the market and advantageous pricing structures for companies which have disadvantaged farmers. Particular concerns were raised regarding the availability of supply of fertiliser products from late 2007 to early 2008, and these issues are discussed below.

Stockpiling of product

3.32 A number of submissions and other evidence alleged that there was hoarding of fertiliser product in sheds and on ships and that it was not released until prices increased.

3.33 The NSW Farmers Association stated that their members questioned how there can be fertiliser stockpiled in sheds or on ships waiting to be unloaded yet retailers do not have any available for sale or they cannot inform the customer of when it will be available or at what price.[29]

3.34 The NSW Farmers Association noted that:

> …people who have been saying to me that there is no shortage of fertiliser; it is a matter of companies controlling the release of fertiliser, which is applying pressure to the market. I do not know whether that is right or not…I have heard similar stories where people do believe that there is product out there, but the release of that product is applying the pressure and is therefore applying pressure to the price variations.[30]

3.35 The Hon Dean Brown AO, Premier's Special Adviser on the Drought, South Australian Government, provided a number of statements from farmers on the Eyre Peninsula outlining serious concerns relating to trading practices, including the stockpiling of product. The farmers were identified as Farmers A to E. In the case of Farmer A the farmer had sought to obtain fertiliser from a company but the company

29 *Submission* 4, NSW Farmers Association, p. 5.

30 M Alexander Laurie, NSW Farmers Association, *Committee Hansard*, 16 May 2008, p. 16.

refused to supply it to the farmer, knowing that the price was likely to go up; the company told the farmer to get the fertiliser elsewhere.[31]

3.36 Another farmer noted that:

> It is also hard to work out the pricing of DAP this year and the availability of it. I have been told that there is plenty of fertiliser available but it is being held back as the price rises.[32]

3.37 The NSW Farmers Association noted that the Australian crop production is relatively constant, as is the area of crop planted. Similarly, one would expect the demand for fertiliser to be relatively constant, allowing fertiliser suppliers to fairly accurately predict patterns of demand – 'it is difficult to understand why with a relatively constant demand cycle how there can be a shortage of product'.[33]

3.38 IPL rejected the assertions of hoarding of fertiliser product.

> If people saw stock in our company's sheds during a time when we were not taking orders, then that stock had been either sold or allocated to customers and was awaiting dispatch. At no stage in 2007 or 2008 have we had fertiliser stocks in our sheds which we were unwilling to sell. Stock in up-country sheds in most cases is owned by our distributors, and IPL has no influence on its availability to farmers.[34]

3.39 The committee questioned IPL further on the allegations of hoarding. IPL initially denied that there were situations where there were fertiliser supplies in storage and that the company would not price or supply product.

> **CHAIR—**Are you denying that there were fertiliser supplies in storage that you would not price or supply?
>
> **Mr Rintel—**Yes.[35]

3.40 This statement was later qualified by IPL to indicate that there was a period when the company did not take orders due to insufficient stocks.

> **Senator NASH—**Are you saying that on absolutely no occasion did Incitec give any direction whatsoever to any agent or reseller to withhold a price?
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> **Mr Rintel—**To the best of my knowledge, absolutely not. There was a period of time in November and December last year when Incitec Pivot had stopped taking orders for ammonium phosphates as we did not have

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31 *Submission* 36, Mr Dean Brown, p. 1; Mr Dean Brown, *Committee Hansard*, 16 May 2008, pp 2, 7.

32 *Submission* 33, Mr Tony Hedges, p. 1.

33 *Submission* 4, NSW Farmers Association, p. 5. See also Mr Alexander Laurie, NSW Farmers Association, *Committee Hansard*, 16 May 2008, p. 14.

34 Mr James Whiteside, IPL, *Committee Hansard*, 23 July 2008, p. 14.

35 Mr Jamie Rintel, IPL, *Committee Hansard*, 23 July 2008, p. 20.

> sufficient stocks in our shed to meet the unprecedented demand, which had been brought forward significantly. On that basis, we were not in a position to provide pricing on ammonium phosphate because we did not have a known cost position on the product at that particular time.[36]

3.41 IPL provided to the committee, on a confidential basis, information on the quantity of MAP, DAP and single superphosphate (SSP) held in storage over the past two years and the overall storage capacity over that period. While the data indicate substantial volumes of stock on hand in late 2007 and early 2008, IPL noted that the stock on hand figures do not represent the volume of fertiliser 'sitting in sheds' and available to be sold. During the stock shortages in late 2007 and early 2008 IPL stated that up to 100 per cent of the volumes indicated in some months were already committed to IPL's dealers and agents.[37]

3.42 The committee further questioned IPL if any impediments were placed on agents by the company limiting their capacity to resell fertiliser products.

> **CHAIR—**Are you prepared to say here today that there were no agents in Australia whom you supplied in the spring of last year that had any restriction on their capacity to resell fertiliser as soon as it hit the shed?
>
> **Mr Rintel—**To the best of my knowledge, no.[38]

3.43 The committee also questioned IPL about their export of fertiliser products in late 2007, when farmers were experiencing difficulties in sourcing supply.

> **Senator NASH—**Given what you have said about the importance of the Australian market, why did you continue to export at the end of last year when there was obviously a supply issue here?
>
> **Mr Whiteside—**We did not. We exported at a time when we did not believe there was a supply issue…
>
> **Senator NASH—**We are talking about September last year onwards?
>
> **Mr Whiteside—**I will get our export program for you. Certainly by December we were not exporting any product. Our exports occurred in July, August and September, and maybe into October, when our forecast was that we would have sufficient product to meet domestic demand.[39]

3.44 As noted above, IPL stated that the company was not exporting product 'by December'. IPL subsequently provided information to the committee, on a confidential basis, on the total quantity of fertiliser exported by month between July and December 2007. The information indicated that the company did in fact export

36 Mr Jamie Rintel, IPL, *Committee Hansard*, 23 July 2008, p. 21.

37 IPL, Correpondence, 7 October 2008.

38 Mr Jamie Rintel, IPL, *Committee Hansard*, 23 July 2008, p. 41.

39 Mr James Whiteside, IPL, *Committee Hansard*, 23 July 2008, p. 34.

fertiliser product to several overseas countries in July through to October 2007 and in December 2007.[40]

3.45 The committee notes that IPL was exporting fertiliser products at the same time as Australian farmers were having difficulties in obtaining supplies locally.

3.46 The ACCC in its report on fertiliser prices stated that suppliers withholding stock from the market in order to sell later at higher prices will not generally breach the *Trade Practices Act 1974* (TPA) unless it involves some misleading or deceptive conduct on the part of suppliers. For example, a supplier might misrepresent the reason for its inability to supply or not truthfully explain why it chose not to supply.[41] The committee notes that the TPA needs to be strengthened to address this concern.

Price gouging

3.47 General allegations of price gouging by companies were made during the inquiry. 'Price gouging' refers to situations where suppliers are said to be taking advantage of rising international prices by increasing their own prices beyond levels that could be justified in the circumstances.

3.48 One witness stated that:

> It is hard to believe that there would have been no price gouging. I believe there would have been product within Australia that was sourced at much lower cost and the opportunity has been taken. It will be difficult to achieve that evidence, of course, but it is very hard to believe that it would not have occurred. It would also be useful to simply look at a company like Incitec Pivot, which has been manufacturing here and making considerable profits over time when the competition from overseas was very strong. Now that the competition from overseas is different and there is a shortage of supply, they are simply choosing to make more profit. It is nought to do with their cost of production.[42]

3.49 Witnesses raised the issue of price gouging by companies in relation to fertiliser that was in store yet companies were reluctant to provide information on pricing or availability of the product.[43]

3.50 The committee also raised the issue of whether the expectation of high grain prices and a shortage of fertiliser encouraged price gouging by companies. The NSW Farmers Association argued that such situations may reflect profiteering by companies.

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40 IPL, Correspondence, 7 October 2008.

41 *ACCC Examination of Fertiliser Prices*, July 2008, pp 26-27.

42 Mr Trevor De Landgrafft, WAFarmers, *Committee Hansard*, 16 May 2008, p. 64. See also Mr John Hall, Hall Farms Pty Ltd, *Committee Hansard*, 23 July 2008, p. 9.

43 See, for example, Mr John Hall, Hall Farms Pty Ltd, *Committee Hansard*, 23 July 2008, p. 12.

> The phrase ‘price gouging’ is very strong and there is a certain amount of allegation there which I do not want to make. All I can tell you is that there have been lots of discussions about people having concern in that area. I suppose if you are sitting on the other side and you are a commercial operator then obviously commercial operators are about making profits for their companies so I cannot tell you what their basis of thinking is, but I can tell you that ours is extreme frustration at the prices.[44]

3.51 The committee notes that in evidence to the inquiry, IPL rejected 'outright' any accusation of price gouging or unfair conduct.[45]

3.52 The ACCC, in its report on fertiliser prices, found little evidence of price gouging. The report noted that practices such as raising of prices by suppliers until a sufficient number of purchasers drop out of the market, unless carried out in conjunction with anti-competitive arrangements 'is neither illegal under the Trade Practices Act nor economically inefficient or undesirable'. The ACCC noted that charging higher prices in a time of shortage is not uncommon and 'is not of itself a breach of the Trade Practices Act'.[46] Again, the committee notes that the TPA needs to be strengthened to address this issue.

Availability of fertiliser

3.53 Evidence to the committee indicated that the availability of fertiliser was a problem for farmers, especially in the period from late 2007 to early 2008. The NSW Farmers Association stated that members reported that when they approached their retailer they were unable to get information on when fertiliser would be available. Furthermore, when farmers attempted to order fertiliser they were unable to receive any certainty regarding price. The Association also reported that when farmers had managed to purchase fertiliser, the price had suddenly increased when the product arrived.[47]

3.54 The Association stated that:

> This year would appear to me to be a very different situation. If you go back and have a look over the last 10 to 15 years, many fertiliser companies were actually offering fertiliser with payment two, three and four months down the track. Now you are getting into a situation where you cannot even get a price for the product in some cases because they are not sure what it is going to be, or we are led to believe they are not sure what it is going to be.[48]

44 Mr Alexander Laurie, NSW Farmers Association, *Committee Hansard*, 16 May 2008, p. 22.

45 Mr James Whiteside, IPL, *Committee Hansard*, 23 July 2008, p. 14.

46 ACCC report, p. 26.

47 *Submission* 4, NSW Farmers Association, pp 5-6.

48 Mr Alexander Laurie, NSW Farmers Association, *Committee Hansard*, 16 May 2008, p. 15.

3.55 The Association noted that this creates a great degree of uncertainty for buyers in the market.

> …many members of ours and many members of the industry are out there and are extremely frustrated. They struggle to have control over any pricing and inputs they really must be using. They do have a lack of control over any pricing, a lack of ability to budget…We do not know where it will be in six months time and, when we have to do some key budgeting for all of these things, it is impossible to work that in.[49]

3.56 The Australian Fertiliser Services Association (AFSA), which represents small and medium size businesses in the retail sector, complained about the lack of transparency with regard to information from manufacturers and importers concerning fertiliser supply and pricing. The Association argued that their members are the 'meat in the sandwich' between manufacturers and their customers – the farming community. Mr Abbott, National President of AFSA, noting difficulties in sourcing supplies of fertiliser, stated that:

> These supply limits are affecting most regions but are particularly severe in Victoria. The reasons and mechanisms for these supply limits to date have been poorly communicated by the manufacturing and importing sectors, creating an element of distrust in the market.[50]

3.57 Mr Abbott noted that 'in the case of our own business, we were unable to source fertiliser from our normal supplier for two months, without explanation'.[51] AFSA also noted that small retailers:

> …[have] little or no control over the content, accuracy and timing of communication from manufacturers and importers about current and future supplies. A lack of communication raises concerns about transparency and therefore what is likely to happen in the industry in the future.[52]

3.58 IPL acknowledged difficulties in meeting demand in 2007-08. IPL noted that while fertiliser suppliers can generally anticipate likely farmer demand based on historical consumption and forecast conditions, in 2007-08 there was a significant change in farmer purchasing patterns which resulted in many farmers bringing forward fertiliser purchases. In addition, there was an improved rainfall outlook across many regions in eastern states after years of drought.

> The combination of these factors led farmers to bring forward their fertiliser purchases and resulted in an unforeseen level of early season demand for fertiliser in Australia, well beyond forecasts. In the period October 2007 to

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49 Mr Alexander Laurie, NSW Farmers Association, *Committee Hansard*, 16 May 2008, p. 14.

50 *Submission* 5, Australian Fertiliser Services Association, p. 2.

51 Mr Rodney Abbott, Australian Fertiliser Services Association, *Committee Hansard*, 16 May 2008, p. 26.

52 *Submission* 5, Australian Fertiliser Services Association, p. 2.

> February 2008, IPL experienced a significant increase in fertiliser demand compared to the same period 12 months earlier.
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> Domestic suppliers moved rapidly to meet this unanticipated demand. However, their ability to source substantial volumes on very short notice was affected by global supply chains. Lead times for delivery of imported product meant that during December 2007, and January and February 2008, IPL stocked out of fertiliser at a number of its distribution facilities.[53]

3.59 The committee questioned IPL as to why the company failed to anticipate the increased demand from farmers, given that all in the industry – both farmers and suppliers – were aware of likely price increases.

> **Mr Rintel**—It was not reflected in the forecast which we rely on our business partners to provide us of, firstly, quantity of produce and, secondly, timing of requirement…
>
> **Mr Whiteside**—…we did everything we could to bring forward supply. We brought forward a number of imported vessels to try and meet early demand but we were not able to meet all additional demand because of the short notice.[54]

3.60 IPL noted that there was 'unforecast demand' in the spring for the subsequent winter cereal crop 'which we had never experienced before' which meant agents and dealers were unable to supply product.[55]

3.61 IPL provided to the committee, on a confidential basis, information on historical demand and known demand forecasts for fertiliser products for 2007 and 2008. The data indicates a significant bringing forward of demand in December 2007 to March 2008, with actual sales well above the previous year levels and significantly above forecasts. The data shows that while IPL was able to supply more fertiliser than it had anticipated in response to demand, there were inadequacies in meeting overall demand.

Failure to honour contracts

3.62 The inquiry received numerous allegations of companies failing to honour contracts. The farmers in question were then compelled to renegotiate contracts but at a higher price.

3.63 Mr Dean Brown provided a number of statements of concern in relation to trading practices from farmers on the Eyre Peninsula. The farmers were identified as Farmers A to E.[56] In one case, Farmer B, had ordered fertiliser from a rural supply

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53 *Submission* 26, IPL, pp 10-11.

54 Mr Jamie Rintell/Mr James Whiteside, IPL, *Committee Hansard*, 23 July 2008, pp 30-31.

55 Mr James Whiteside, IPL, *Committee Hansard*, 23 July 2008, p. 41.

56 *Submission* 36, Mr Dean Brown, pp 1-4.

outlet at an agreed price. The company withdrew from the contract, having reached an earlier agreement to supply it. As a result, the farmer's only option was to re-order at a higher price. Farmer C placed an order with a supplier. The supplier informed the customer that their supplier had refused to honour the order, yet there was ample product in store.[57] Mr Brown observed that:

> Each of these cases reflects a rising fertiliser price. The company, having agreed to a price—this is for the breach of contract—then pulled back from supplying it and eventually the farmer had to buy it at a higher price.[58]

3.64 Further statements were provided by Mr Brown involving alleged breach of contract. Farmer D alleged that a company broke a contract to supply fertiliser that had been ordered via a local agent. This resulted in a dramatic loss of income for the farmer as the crops were unable to be sown in time. Farmer E also placed an order for the supply of fertiliser which the company did not honor – 'the result of all of that was that Megafert did not end up supplying the fertiliser. It was sold to someone else, apparently at a higher price'.[59]

3.65 Mr Brown also cited the case of a farmer near Ceduna:

> …where they had actually had a firm, written contract for a certain tonnage but where they only got about half that tonnage at the contract price and then had to pay about $300 more per tonne for the other half is, I think, a clear example of an extreme breach of a contract and there was absolutely no doubt in that case exactly what had occurred.[60]

3.66 Mr Brown indicated that the cases cited above reflected the 'norm' in terms of problems encountered by farmers on the Eyre Peninsula.

> In the examples I have had of personal conversations with farmers, I think there are much more extreme cases than these. In some cases, though, the farmers were not willing to provide evidence…So I stress the fact that I think there are much more extreme cases than are outlined in the letters from farmers A to D.[61]

3.67 The committee notes that IPL stated that 'the broken contracts that the committee has heard about in South Australia are not contracts involving Incitec Pivot; they are contracts between farmers and fertiliser distributors'.[62]

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57 *Submission* 36, Mr Dean Brown, pp 2-3; Mr Dean Brown, *Committee Hansard*, 16 May 2008, p. 2.

58 Mr Dean Brown, *Committee Hansard*, 16 May 2008, p. 2.

59 Farmer E, cited by Mr Dean Brown, *Committee Hansard*, 16 May 2008, p. 3.

60 Mr Dean Brown, *Committee Hansard*, 16 May 2008, p. 10.

61 Mr Dean Brown, *Committee Hansard*, 16 May 2008, p. 10.

62 Mr James Whiteside, IPL, *Committee Hansard*, 23 July 2008, p. 14.

3.68 In other evidence to the committee, a farmer stated that he had placed an order with a company which he understood to be a binding agreement at a particular price, but that the supplier refused to honour the order. The farmer participated in verbal negotiations, but this was later confirmed in written advice from the company, including their buy-in price.[63]

> We were given a delivery date…On the day the fertiliser was to be dispatched from Incitec we got a message from our local rep, who said that they had turned the trucks around and they were not going to deliver the fertiliser. This caused some ructions with our supplier. We rang them and they said they had found some product and they were going to continue with the supply...We kept ringing and eventually it got to the point where, in early February, the agreement was withdrawn and we had to meet another agreement to secure supplies. It cost the group I am involved with about $60,000 extra, over the cost of the fertiliser.[64]

3.69 The witness indicated that although he may have a civil claim against the company, he was reluctant to pursue the claim through the courts because of the imbalance in potential resources available to a small group of producers vis-a-vis the supplier involved.[65]

3.70 The NSW Farmers Association stated that indicative prices are often quoted but this is often not the final price paid by farmers:

> We have certainly had people who have gone in to get indicative prices of fertiliser and been told a price, only to be told another price later on. It is not my experience that firm contracts have been written, but it is most definitely my experience that indicative prices have been given. I think some of the companies have been very cautious in how they are giving those indicative prices because of the volatility in the market. There is some of that going around; there is no doubt about that. It also adds very much to the frustration when people think they have locked it in at a price and have then gone and done their budgets on that, only to turn around and find that the input costs due to fertiliser increases have moved once again. It is something that has happened. You have heard it from growers and we have most definitely heard it from growers. All I can say is that that sort of thing has been worrying people.[66]

3.71 The ACCC, in its report on fertiliser prices, stated that it was not provided with specific allegations of suppliers failing to honour contracts on a systematic, or even individual basis, with the allegations being general in nature. The ACCC noted

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63 Mr Terence Fishpool, *Committee Hansard*, 16 May 2008, pp 50-51, 54-55.

64 Mr Terence Fishpool, *Committee Hansard*, 16 May 2008, p. 50.

65 Mr Terence Fishpool, *Committee Hansard*, 16 May 2008, pp 50-51.

66 Mr Alexander Laurie, NSW Farmers Association, *Committee Hansard*, 16 May 2008, p. 16.

that commercial disputes such as these are of a contractual nature and generally do not fall within the ambit of the TPA.[67]

3.72 The ACCC indicated to the committee, however, that if allegations of bullying or intimidation were involved it could come under the unconscionable conduct provisions of the TPA. The ACCC, could not, however, cite a successful prosecution under these provisions in recent years, although three cases are before the courts at present.[68] The committee considers this situation again highlights the need for a strengthening of the TPA.

Misuse of market power

3.73 Other examples of the misuse of market power were highlighted during the inquiry.

Port access

3.74 Some witnesses argued that there is difficulty in accessing portside warehousing space for imported fertiliser products, in circumstances where companies wish to deal directly with overseas suppliers. Mr Andrew Helps of Climate Friendly Fertiliser Pty Ltd stated that:

> It is always a problem when quasi-monopolies are operating in a marketplace, when there is no genuine competition. You look at what is happening and you say, 'Gee, I could make a dollar; I could bring some cargoes in there,' but you cannot get them in because there is no port capacity.[69]

3.75 The committee also received *in camera* evidence supporting these arguments.

3.76 Other witnesses argued that port access is not a major problem. Mr Paul Duckett of the Australian Energy Company stated that:

> One of the features of the industry is that, as long as you have the storage capacity at the ports, anyone can order a shipload of urea or phosphate fertiliser and bring it in tomorrow. In fact, we have seen a number of start-up organisations in recent years which have done just that.[70]

Restricted distribution arrangements

3.77 Confidential information was received from a fertiliser manufacturer indicating that for over 30 years the company has been unable to purchase raw

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67 ACCC report, p 27.

68 Mr Brian Cassidy/Mr Mark Pearson, ACCC, *Committee Hansard*, 14 November 2008, pp 32-34.

69 Mr Andrew Helps, *Committee Hansard*, 16 May 2008, p. 48.

70 Mr Paul Duckett, *Committee Hansard*, 23 July 2008, p. 5.

chemicals directly from an overseas manufacturer or their Australian agents but instead has to go through several middlemen to make a purchase which forces up the price of the product.

Other issues

3.78 Other questionable business practices were highlighted during the inquiry.

3.79 The committee received evidence of alleged intimidation of resellers where a single supplier operates. One witness noted that:

> **Mr Katter**—I am reluctant to say anything that would indicate any of my retailers, because—
>
> **CHAIR**—They are intimidated.
>
> **Mr Katter**—They are definitely intimidated. I would not like to go beyond saying that there is an implied intimidation out there. None of them would divulge that because they have to rely for a range of products—
>
> **CHAIR**—On a sole provider.
>
> **Mr Katter**—Yes. There is no-one else in Australia who can provide that range of products, so if you want to be a single-stop shop then you better stay in with Incitec.[71]

3.80 In other evidence, the committee received confidential information of sugarcane farmers on 30-day accounts having the costs to the reseller passed onto the users of the 30-day account from the original supplier at 18 per cent per cent. Mr Brian Cassidy, Chief Executive Officer of the ACCC, indicated that such practices may be a breach of the unconscionable conduct provisions of the TPA.

> If in the contract you have a unilateral variation clause which allows you to subsequently change the contract having signed it, you can change the contract and say that the percentage is going to be 18 per cent a month. That is something that is able to be examined under the unconscionable conduct provisions. I cannot give you a straightforward answer on that. It would really depend on the circumstances surrounding how they get charged the 18 per cent.[72]

3.81 Other practices also came to light. In confidential evidence, a reseller stated that notification of fertiliser price increases are often advised close to close of business with little time given to pick up the fertiliser product. Previously, price lists were notified allowing a period of grace to collect the product.

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71 The Hon Bob Katter MP, *Committee Hansard*, 11 November 2008, p. 26.

72 Mr Brian Cassidy, ACCC, *Committee Hansard,* 14 November 2008, p. 41.

Addressing anti-competitive behaviour

Review of the Trade Practices Act

3.82 Many of the allegations cited above relating to stockpiling of fertiliser products, price gouging, and problems related to the availability of fertiliser raise important issues concerning the role of the Trade Practices Act and the ACCC.

3.83 The Trade Practices Act contains a number of provisions related to anti-competitive practices and misuse of market power. The relevant sections of the Act are outlined below.

Part IV – restrictive trade practices

Section 45 – Anti-competitive practices

3.84 Sections 45 to 45E of the TPA deal with a variety of prescribed agreements and anti-competitive arrangements between businesses. This section applies to cartel behaviour, although the TPA does not specifically use that term.

Section 46 – Misuse of market power

3.85 Section 46 provides that a corporation that has a 'substantial degree of power' in a market shall not 'take advantage' of that power for the purpose of eliminating, or substantially damaging, a competitor in that, or any other market; preventing the entry of a person into that or any other market; or deterring or preventing a person from engaging in competitive conduct in that or any other market.

Section 47 – Exclusive dealing

3.86 Section 47 of the TPA prohibits anti-competitive exclusive dealing which has the purpose of substantially lessening competition in a relevant market.

Section 48 – Resale price maintenance

3.87 Section 48 of the TPA states that a corporation or other person shall not engage in the practice of resale price maintenance.

Section 50 – Mergers and acquisitions

3.88 Section 50 prohibits acquisitions which would have the effect, or be likely to have the effect, of substantially lessening competition in a substantial market in Australia, in a state or territory.

Part IVA – Unconscionable conduct

3.89 The concept of unconscionable conduct generally involves a stronger party exploiting an evident special disability or disadvantage suffered by another party.

3.90 During the inquiry concerns were raised as to the effectiveness of existing powers under the TPA to address anti-competitive practices and misuse of market power. One submission commented on the 'complacency' of the ACCC which has allowed monopoly or near monopoly situations to develop.[73]

3.91 The limitations of the TPA in addressing anti-competitive behaviour was illustrated in evidence from the ACCC. Mr Cassidy stated that:

> The Trade Practices Act, as it currently stands, does not make unlawful so-called price gouging, price exploitation or any other name that you might want to use for prices rising more rapidly than perhaps they should. Whether they should or not is a matter for the government. As the law stands at the moment, there is nothing that we can do to stop prices from increasing.[74]

3.92 The committee believes that there is a need for a strengthening of the competition provisions of the TPA to better protect consumers from anti-competitive behaviour.

Industry codes of conduct

3.93 Industry codes of conduct provide a mechanism for enhanced transparency especially in relation to pricing and supply issues for certain industries. The TPA provides for the establishment of industry codes of conduct. There are a number of different types of industry codes – non-prescribed voluntary industry codes of conduct, prescribed voluntary codes of conduct and mandatory codes of conduct.

3.94 A non-prescribed voluntary industry code of conduct is administered by the industry itself and sets standards that are voluntarily administered by the industry. The Commonwealth Government does not have a role in enforcing non-prescribed voluntary industry codes of conduct.

3.95 A prescribed voluntary code of conduct is a code that is binding on signatories and is enforced by the ACCC under the TPA. A breach of a prescribed voluntary code of conduct is also a breach of the TPA. There are currently no voluntary codes of conduct prescribed under the Act.

3.96 Mandatory codes are administered and enforced by the ACCC and are binding on the industry they cover. There are currently three mandatory codes in operation – the Franchising Code, the Oilcode and the Horticulture Code of Conduct.[75]

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73 *Submission* 9, Bookham Agricultural Bureau, p. 2. See also *Submission* 12, Mr Sam Nucifora, p. 1; *Submission* 43, Mr Peter Schwarz, p. 1.

74 Mr Brian Cassidy, ACCC, *Committee Hansard*, 14 November 2008, p. 17.

75 www.accc.gov.au (accessed 12 November 2008).

3.97 The committee will examine the efficacy of industry codes of conduct and their applicability to the fertiliser industry in its final report.

Monitoring role

3.98 Part VIIA of the TPA enables the ACCC to examine the prices of selected goods and services. The ACCC's functions under this Part are:

- to hold price inquiries in relation to the supply of goods and services, and to report the findings to the responsible Commonwealth minister;
- to examine proposed price rises when, for example, the minister has declared the relevant goods or services to be 'notified' goods or services;
- to monitor the price, costs and profits of an industry or business under the direction of the minister and to report the results to the minister.

3.99 The committee believes that an increased monitoring role for the ACCC in relation to the fertiliser industry has some merit and is another option that it will examine further in its final report.

Committee view

3.100 Evidence to the inquiry raised serious concerns regarding the degree of protection available to farmers and others from anti-competitive practices and abuses of market power under the Trade Practices Act. Instances of the stockpiling of fertiliser product; price gouging; difficulties in securing supply of fertiliser; uncertainty regarding price; and a failure to honour contracts were provided during the inquiry.

3.101 The committee believes that the powers of the ACCC need to be strengthened so that the Commission can more effectively fulfil its role in promoting competition and fair trading and in providing for effective consumer protection. The committee will examine in greater detail the most effective means of achieving this outcome in its final report.

3.102 The committee will also examine, in its final report, the potential for increased transparency of the fertiliser industry through the introduction of an industry code of conduct. It will also examine the efficacy of implementation of an increased monitoring role of the industry by the ACCC.

Senator the Hon Bill Heffernan
Chair