Chapter 3

Regulation and competition issues

3.1 This chapter reviews a range of regulatory and competition issues in relation to the fertiliser industry. The chapter discusses industry concentration and market dominance of key players. The chapter also reviews the adequacy of the current regulatory arrangements and the adequacy of the *Trade Practices Act 1974* in addressing anti-competitive practices and misuse of market power. In addition, the chapter reviews the adequacy of pricing and supply arrangements operating in the industry and the efficacy of industry codes of practice. The chapter highlights the need for effective competition in the industry and for greater transparency in relation to pricing and supply arrangements.

Industry concentration

3.2 The fertiliser industry is dominated by two major companies. Incitec Pivot Ltd (IPL) has a dominant market position in eastern Australia – with a 70 per cent market share at the wholesale level and 58.5 per cent market share at the distribution level.[1]

3.3 In Western Australia, CSBP has an approximate market share of 65 per cent and annual sales of about one million tonnes, being a mix of imported and locally manufactured fertilisers. CSBP's market share has fallen from an estimated 90 per cent in 1995-96 as new fertiliser suppliers have entered the WA market. Summit Fertilisers has an estimated market share of 25 percent and United Farmers Co-operative an estimated market share of 10 per cent. A number of smaller operators, including Superfert, Whitford Fertilisers and ABB also operate in Western Australia.[2] The Australian Competition and Consumer Commission (ACCC) noted that a number of market participants are vertically integrated and have a presence across more than one level of the supply chain.[3]

3.4 The first Interim Report detailed concerns that the market dominance of key players in the industry had led to distortions in the market and advantageous pricing structures for companies which have greatly disadvantaged farmers. Specific allegations relating to the stockpiling of product, price gouging, difficulties in relation to the availability and pricing of fertiliser and the failure to honour contracts were discussed extensively in that Report.[4]

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1 Mr James Whiteside, IPL, *Committee Hansard*, 23 July 2008, p. 15; *Submission* 26, IPL, p. 10.

2 Information provided by CSBP Ltd.

3 ACCC, *ACCC Examination of Fertiliser Prices*, July 2008, p. 10.

4 Senate Select Committee on Agricultural and Related Industries, *Pricing and Supply Arrangements in the Australian and Global Fertiliser Market: Interim Report*, December 2008, pp 26-35. Hereafter referred to as the Interim Report.

3.5 Since the tabling of its first Interim Report, a number of other allegations have been raised with the committee.

3.6 Mr Ron Greentree provided a telling example of the use of market power by fertiliser companies. He made specific allegations of price fixing in relation to IPL and Orica. As a large fertiliser user – particularly of anhydrous ammonia or NH3 – he was frustrated in his attempts to obtain fertiliser other than through the existing retail market.

3.7 Mr Greentree had attempted to get a price quote for NH3 from Orica, which has a plant at Newcastle, and IPL, which has a plant at Brisbane, but neither company would quote or sell fertiliser to him outside the retail market.

> In relation to the prices difference between the retail price delivered here on-farm to northwest New South Wales, which is nearly equal to the distance between Brisbane and Newcastle, the prices are always exactly the same from either plant, even though they have different owners. We do not have the opportunity from Newcastle to buy from Orica; we can only buy it through IPL, but IPL take a lot of product to the urea plant, which also is in Newcastle.
>
> …They have this arrangement at Newcastle that they will not sell to farmers; it has to come through IPL.[5]

3.8 IPL, in response to these allegations denied that there is any arrangement in place with Orica that Orica will not supply ammonia to agricultural customers.

> IPL sources ammonia from Orica's Kooragang Island facility pursuant to a commercial agreement. IPL also supplies ammonia to Orica from IPL's Gibson Island facility. However, there is no restriction on Orica supplying ammonia to agricultural customers.[6]

3.9 Mr Greentree also alleged that there was an arrangement between IPL and Orica which did not allow operators like him into the market.[7]

3.10 Mr Greentree noted that his attempts to import his own urea were extremely difficult with IPL allegedly putting several obstacles in his path. Eventually he was able to import urea which was more than A$300 a tonne cheaper than if it had of been purchased through IPL.

> We landed it here at that time, which was in March, at A$525 a tonne. They put every obstacle in the way. The shipment was late. It was loaded out of Libya. We brought in 10,000 tonnes. IPL got word of it and really slowed it down because there was not a full boatload and it was made up with some IPL urea as well. They slowed it right down. In fact, that fertiliser did not arrive in Australia until about the middle of April whereas it was supposed

5 Mr Ron Greentree, *Committee Hansard*, 7 May 2009, p. 3.

6 IPL, Correspondence, dated 21 May 2009.

7 Mr Ron Greentree, *Committee Hansard*, 7 May 2009, p. 3.

> to be here at the end of February when we had to do a stock swap, but they put everything in the way to ensure that we could not get it. But we won in the end and that saved us from in excess of A$300 a tonne on the retail price.[8]

3.11 IPL denied allegations that it deliberately obstructed or delayed a shipment of urea referred to above.

> The shipment was allegedly co-shipped with a volume of IPL urea. IPL has not coshipped urea with any other party since at least 2006.
>
> It was further alleged that this shipment was sourced from Libya. According to public information regarding imports of urea into Australia, IPL does not believe that any urea has been imported into Australia from Libya since at least 2003.[9]

3.12 Mr Greentree also alleged price fixing by IPL and Orica in relation to NH3 and urea prices.

> It has just got to be complete price fixing. Why is the NH3 price always completely fixed to their urea price when it has less of a process to go through.[10]

3.13 IPL denied any allegation of collusion on the pricing of ammonia. IPL offered the following explanation:

> The reason that there is no difference between the price that IPL charges for ammonia sourced from its own facility at Gibson Island compared to product IPL sources from Orica out of Kooragang Island is because, as noted above, the price of ammonia is referable to the price of urea which is the primary substitute for ammonia. The price of urea effectively determines the price of ammonia, regardless of the source of the ammonia.[11]

3.14 Other examples, in one case relating to predatory pricing, were provided to the committee on a confidential basis. In this instance a major fertiliser company proposed a joint venture with a family fertiliser business to distribute fertiliser in the local area. The local business declined the offer to participate. The company nevertheless indicated their desire to obtain a substantial proportion of the local market and were prepared to 'operate at a loss' to achieve this outcome. The local business subsequently lost a number of clients to the major company.

3.15 In the case of IPL, the committee notes that the possible closure of the company's Geelong plant will adversely impact on competition. The committee is

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8 Mr Ron Greentree, *Committee Hansard*, 7 May 2009, p. 4.

9 IPL, Correspondence, dated 21 May 2009.

10 Mr Ron Greentree, *Committee Hansard*, 7 May 2009, p. 7.

11 IPL, Correspondence, dated 21 May 2009.

concerned that this action, by reducing capacity in a market already largely dominated by one company, would lead to upward price pressures and consequently further adversely affect the ability of farmers to source fertiliser at reasonable prices.[12]

3.16 In the committee's Interim Report the dominant market position of key players in the industry and the possible implications this holds for competition, was commented upon extensively.[13] This was again highlighted since the tabling of the Interim Report, particularly with the entry of a new fertiliser company, Direct Farm Inputs (DFI) in December 2008.

3.17 When DFI released its price lists in December 2008 opposition fertiliser companies matched their prices, despite the fact that these same companies had indicated that fertiliser prices would continue to remain high into the foreseeable future.

3.18 Mr Leighton Huxtable, Chairman of DFI, recounted that:

> I started up the new company Direct Farm Inputs…That was born out of necessity. Being a farmer myself, I knew that the prices that were being spoken of at that stage of around $1,600 to $1,850 for MAP or DAP product was just not sustainable from a farmer's point of view. We started up Direct Farm Inputs to try and reduce prices. When we released our price on 12 December [2008] of $1,030 for MAP and DAP, with a further rebate to come, growers got right behind us and opposition companies immediately matched our price.[14]

3.19 Mr Huxtable stated that from January 2009 onwards other fertiliser companies further reduced their prices to match DFI prices.[15]

3.20 Mr Brian Cassidy, Chief Executive Officer of the ACCC, noted the importance of ensuring that impediments are reduced so that new players can enter the market.

> …with fertiliser being an internationally traded commodity and if domestic prices moved significantly out of line with world prices allowing for lags and so forth, you would get new entry and other competitors bringing in imports.
>
> Our point of view and our role or what is important to us is to make sure that that new entry can occur if the differential between international and domestic prices opens out beyond where it should be, which is the reason we are very interested in any suggestions and evidence about impediments

12 See, Mr Gary Brinkworth, *Committee Hansard*, 10 August 2009, pp 12-13.

13 Interim Report, pp 19-25.

14 Mr Leighton Huxtable, *Committee Hansard*, 4 February 2009, p. 1.

15 Mr Leighton Huxtable, *Committee Hansard*, 4 February 2009, pp 3-4.

being raised to new entrants to the market who want to do their own importing.[16]

Committee view

3.21 The committee concluded in its first Interim Report 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.[17] Evidence received since the tabling of the Interim Report has only reinforced the committee's view.

3.22 In the Interim Report, the committee noted 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.[18]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.

3.23 The committee re-iterates the view it formed in its first Interim Report 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 where prices are, to a large extent, determined by major players with little reference to usual supply and demand factors.

3.24 In the Interim Report a range of regulatory and competition issues were addressed.[19] These issues are now discussed in greater detail.

Regulation of the industry

3.25 As discussed in the Interim Report, regulatory arrangements in relation to the description, sale and use of fertilisers in Australia are the responsibility of state and territory governments. No state requires that fertilisers be registered, however, all have specifications for how fertiliser must be described and labelled, and the maximum permissible concentrations for certain impurities.[20]

16 Mr Brian Cassidy, *Committee Hansard*, 7 May 2009, pp 11-12.

17 Interim Report, pp 25-26.

18 Interim Report, p. 24.

19 Interim Report, pp 14-17, 26-39.

20 Interim Report, pp 14-15.

3.26 In relation to the testing of fertiliser products, the states generally, with the exception of Victoria, do not undertake regular testing of ingredients in these products, such as nitrogen (N), phosphorus (P) and potassium (K) levels. Victoria does sample testing each 2-3 years, with the last testing undertaken in 2004-5; further testing is scheduled for 2009. Some states, such as NSW, undertake testing when a problem has been identified to the department. Other states view the issue as a fair trading issue, more appropriately addressed under that specific legislation.[21]

3.27 The committee's attention was drawn to isolated instances where the constituent elements in fertiliser products did not appear to reflect the specified ingredient levels.[22] This information was of concern to the committee. As a result, the committee conducted its own investigations. The committee is concerned that in the interests of certainty regular sample testing by the states should be undertaken to provide consumer confidence in the product.

3.28 As noted in the Interim Report, the state and territory acts regulating fertiliser products vary considerably in their scope and detail.[23]

Fertilizer Working Group

3.29 A Fertilizer Working Group (FWG), which is convened by the Department of Agriculture, Fisheries and Forestry (DAFF), and includes representatives of the states, CSIRO, Food Standards Australia New Zealand and the industry, has been established with the aim of ensuring that environment and food safety standards for fertilisers are consistent across jurisdictions.[24]

3.30 The Working Group has succeeded in harmonising heavy metal levels in fertilisers but there are still a large number of inconsistencies including product labelling and the requirements and wording of warning statements.[25]

3.31 With regard to labelling, the members of the Working Group have agreed in principle to the development of an Australian standard or industry code of practice that would specify the appropriate description and labelling for fertilisers to ensure harmonisation between states. The states are expected to continue to include public interest measures such as maximum permissible concentrations of certain impurities, and OH&S, environmental and food safety warnings in their regulations.[26] In August

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21 Advice from state agriculture departments.

22 Mr John Martin, Correspondence, dated 19 August 2009. The committee also received confidential material on this issue.

23 Interim Report, p. 15.

24 The Fertilizer Working Group reports to the Primary Industries Standing Committee. This committee reports to the Primary Industries Ministerial Council.

25 The Working Group is currently involved in a project with the CSIRO examining the issue of contaminants in fertilisers.

26 Advice from DAFF, 7 November 2008.

2008 the Working Group agreed that the states would review a draft code of practice for fertilizer description and labelling developed by the Fertilizer Industry Federation of Australia (FIFA) to determine any areas where it conflicts with current regulation.[27]

Committee view

3.32 As noted in the Interim Report, the committee was strongly of the view that the states and territories should have uniform standards relating to description, sale and use of fertiliser products. The committee notes that the Fertilizer Working Group has agreed in principle to the development of an Australian standard or industry code of practice that would specify the appropriate description and labelling for fertilisers. The committee believes that this work should be concluded as a matter of priority.

3.33 The committee also believes that state agriculture departments, as part of their regulatory oversight functions, should regularly test the specified ingredient levels, such as NPK levels, in fertiliser products to ensure that users have confidence in the integrity of these products.

Recommendation 1

3.34 The committee recommends that the states and territories should consider, as a matter of priority, adopting uniform description and labelling of fertiliser products to ensure consistency between jurisdictions.

Recommendation 2

3.35 The committee recommends that all state and territory agriculture departments should consider undertaking regular sample testing for specified ingredient levels, such as nitrogen/phosphorus/potassium (NPK) levels, in fertiliser products.

Role of the Trade Practices Act and the ACCC

3.36 As noted in the Interim Report, many of the allegations 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 1974* (TPA) and the ACCC.[28]

3.37 The TPA contains a number of provisions related to anti-competitive practices and misuse of market power. The relevant sections of the Act are discussed below.

27 FIFA, *Draft Code of Practice for Fertilizer Description and Labelling*, August 2008.

28 Interim Report, p. 37.

Part IV – restrictive trade practices

Section 45 – Anti-competitive practices

3.38 Sections 45 to 45E of the TPA deal with a variety of prescribed agreements and anti-competitive arrangements between businesses, including:

- agreements which involve market sharing or which restrict the supply of goods. These are prohibited if they have the purpose or effect of substantially lessening competition in a market.
- agreements that contain an exclusionary provision. These are agreements between persons in competition with each other which exclude or limit dealings with a particular supplier or customer or a particular class of suppliers or customers.
- agreements that fix prices. These are agreements which purport to 'recommend' prices but which in reality fix prices by agreement.

This section applies to cartel behaviour, although the TPA does not specifically use that term.

Section 46 – Misuse of market power

3.39 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.

3.40 Whether a corporation is regarded as having a substantial degree of market power depends on the circumstances in each case. The Court will take into account the extent to which the activities of the corporation in its market are constrained by the conduct of its competitors or potential competitors, or by the behaviour of those to whom it supplies or those who supply it. Section 46 will only be breached if the corporation in question has used its market power for one of the purposes listed above.

Section 47 – Exclusive dealing

3.41 Section 47 of the TPA prohibits anti-competitive exclusive dealing which has the purpose of substantially lessening competition in a relevant market. One form of exclusive dealing prohibited outright by the Act is third line forcing, which involves either:

- the supply of goods or services on condition that the purchaser also acquire goods or services from a nominated third party; or
- a refusal to supply because the purchaser will not agree to that condition.

3.42 Where a company considers there is some risk of breaching the provision, they can seek authorisation from the ACCC in accordance with the provisions of section 88 of the Act.

Section 48 – Resale price maintenance

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

3.44 Suppliers may try to impose a resale price to maintain brand positioning or to give resellers attractive profit margins. Any arrangement between a supplier and a reseller that means the reseller will not advertise, display or sell the goods the supplier supplies below a specified price is illegal.

3.45 It is also illegal for a supplier to cut off, or threaten to cut off supply to a reseller (wholesale or retail) because they have been discounting goods or advertising discounts below prices set by the supplier.

3.46 A supplier may recommend an appropriate price for particular goods but may not stop retailers charging or advertising below that price. In most cases, a supplier may specify a maximum price for resale.

Section 50 – Mergers and acquisitions

3.47 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

3.48 The concept of unconscionable conduct generally involves a stronger party exploiting an evident special disability or disadvantage suffered by another party. Three sections in Part IVA of the TPA address unconscionable conduct. They are:

- Section 51AA, which is a broad prohibition on unconscionable conduct as determined through the decisions of the courts over time.
- Section 51AB, which applies to transactions between businesses and consumers for goods ordinarily bought for household use.
- Section 51AC, which also sets out a range of matters that the court may take into account when determining if conduct is unconscionable – it applies to dealings between businesses in relation to the supply of goods or services where the value of the transaction does not exceed $10 million.

Effectiveness of the Trade Practices Act

3.49 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.[29] Some witnesses argued for a review of the TPA.[30]

3.50 The limitations of the TPA in addressing anti-competitive behaviour were illustrated in evidence from the ACCC. Mr Cassidy of the ACCC 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.[31]

3.51 The ACCC in its report on fertiliser prices further 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'.[32]

Misuse of market power

3.52 The ACCC conceded that section 46 of the Act, which relates to misuse of market power, presents difficulties in securing prosecutions because of the requirement to distinguish between anti-competitive conduct and conduct that may have a genuine commercial purpose. Mr Cassidy noted that:

> Section 46 cases are very difficult because we have to find or gather evidence that there was either an anti-competitive purpose or an anti-competitive effect…that is difficult. We have done it. Indeed we have a couple of section 46 cases in the courts at the moment.[33]

3.53 Mr Cassidy stated that the ACCC has had a number of successful prosecutions under s.46 'although not all that many'.[34]

3.54 Predatory pricing, where a corporation prices a product below cost with the intention of driving a competitor out the market and the corporation raises the price again in an attempt to recoup previous losses, is difficult to establish. The difficulty

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

30 Mr Dean Brown, *Committee Hansard*, 16 May 2008, p. 9.

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

32 ACCC report, p. 26.

33 Mr Brian Cassidy, *Committee Hansard*, 7 May 2009, p. 17.

34 Mr Brian Cassidy, *Committee Hansard*, 7 May 2009, p. 21.

with predatory pricing is that in some instances, it appears like legitimate competitive behaviour, because an indicator of competition is price wars.

3.55 In cases where there is an exercise of market power for anti-competitive purposes there are currently no divestiture powers under s.46. The committee pursued this issue with the ACCC.

> Senator JOYCE—…. At this point in time, with Incitec Pivot, is there any power of divestiture?
>
> Mr Pearson—No.
>
> Senator JOYCE—Thank you. So there is really no recourse once they have got a monopoly position. You cannot do anything about it.
>
> Mr Pearson—If they are abusing it or misusing it, there is. We have two cases in court right now on section 46 misuse of market power, so to say that we cannot do anything about it—there are massive fines and injunctions and court orders—
>
> Senator JOYCE—But there are no divestiture powers, are there?
>
> Mr Pearson—No, there is no divestiture power.[35]

3.56 The committee questioned the ACCC as to whether the existence of divestiture powers would provide some constraint on a company's potential to exploit its market position. Mr Cassidy of the ACCC noted that:

> It may. On the other hand, in the US, where they have divestiture powers, they have been very rarely used. The famous break-up of Bell Telephone is one of the few instances where they have been used. So you then have to question: if you have a power which is very rarely used, how much does that concentrate the mind?[36]

Unconscionable conduct

3.57 The committee questioned the ACCC concerning the effectiveness of the unconscionable conduct provisions (s.51AC) of the Act. Mr Mark Pearson of the ACCC conceded that prosecutions under s.51AC are 'very tough, really hard fights'.[37]

3.58 The ACCC subsequently provided information to the committee that indicated that Commission has had 12 successful cases under s.51AC of the TPA. Of these, two were fully contested court cases. The remaining 10 cases were settled by consent with court orders. There are four cases that are the subject of current litigation.[38]

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35 Mr Mark Pearson, *Committee Hansard*, 14 November 2008, p. 32.

36 Mr Brian Cassidy, *Committee Hansard*, 14 November 2008, p. 51.

37 Mr Mark Pearson, *Committee Hansard*, 14 November 2008, p. 33.

38 ACCC, Answers to questions on notice, dated 19 February 2009.

3.59 The committee sought advice from the ACCC as to whether a strengthening of the unconscionable conduct provisions of the TPA would be the most effective way to regulate anti-competitive practices in the industry.

3.60 The ACCC argued that while section 51AC may, in some circumstances, be capable of coincidentally addressing some of the issues arising from anti-competitive conduct, it is not its focus or underlying rationale.

> Issues of possible anti-competitive conduct are best addressed by provisions specifically tailored to identify and remedy such behaviour. Part IV of the Act prohibits a broad range of anti-competitive conduct.[39]

3.61 The ACCC noted that the unconscionable conduct prohibition set out in section 51AC of the Act is designed to address harsh and oppressive conduct in business transactions. Generally defined, it is conduct which is so unreasonable that it goes against good conscience.

Failure to honour contracts

3.62 The ACCC noted that commercial disputes, such as a failure to honour contracts, are generally not within the ambit of the TPA.[40] The committee sought advice as to how these issues should best be addressed.

3.63 The ACCC stated that the provisions of the Act may in some circumstances assist parties in relation to matters involving contracts between businesses. In some circumstances, issues of false or misleading representations may arise or allegations of unconscionable conduct may be present. The ACCC will have regard to factors set out in its Compliance and Enforcement policy in determining whether it would become involved in such matters.[41]

3.64 The ACCC noted, however that generally speaking, commercial disputes as to the honouring of contractual terms and conditions between businesses are best dealt with between the parties, through mediation, or ultimately in the appropriate court – 'by their very nature, contracts set up agreed rights and obligations between the parties to the contract and it is generally up to those parties to enforce'.[42]

Price monitoring role

3.65 A formal price monitoring role is also available under the TPA. 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:

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39 ACCC, Answers to questions on notice, dated 26 May 2009.

40 ACCC report, p 27.

41 ACCC, Answers to questions on notice, dated 26 May 2009.

42 ACCC, Answers to questions on notice, dated 26 May 2009.

- 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.

3.66 The ACCC, in response to the committee's queries on this issue, questioned the effectiveness of a potential monitoring role for the Commission in relation to fertiliser prices.

> …on the basis of the report that we did, domestic fertiliser prices are basically moving in line with international fertiliser prices. I am not quite sure what formal monitoring would actually achieve in that situation.[43]

3.67 The ACCC further advised the committee that while formal price monitoring can sometimes play a useful role in industries where lack of transparency around price levels may be serving as an impediment to competition, this appeared not to be the case in relation to fertilisers.

> The decision to adopt a monitoring regime in favour of other policy measures needs to involve a clear identification of the problem that the monitoring task seeks to address. Price monitoring does not enable the ACCC to directly intervene in an industry by setting prices.[44]

Committee view

3.68 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 by fertiliser companies. While the committee notes that provisions exist under the TPA to address anti-competitive practices, consideration needs to be given to the extent to which these provisions offer practical remedies to the concerns raised during the inquiry. Evidence presented during this inquiry raised similar concerns to other related-committee inquiries as to the effectiveness of the TPA in this regard.[45]

3.69 The committee believes that the powers of the ACCC need to be strengthened so that it can more effectively fulfil its role in promoting competition and fair trading and in providing for effective consumer protection.

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43 Mr Brian Cassidy, *Committee Hansard*, 14 November 2008, p. 36.

44 ACCC, Answers to questions on notice, dated 26 May 2009.

45 See, for example, Senate Rural and Regional Affairs and Transport, *Exposure drafts of the Wheat Export Marketing Bill 2008 and the Wheat Export Marketing (Repeal and Consequential Amendments) Bill 2008*, April 2008, pp 50-51.

3.70 The committee notes that the TPA, as it currently stands, has limitations in addressing anti-competitive behaviour. In relation to section 46 of the Act, which relates to misuse of market power, the ACCC noted difficulties in securing prosecutions because of the requirement to distinguish between anti-competitive conduct and conduct that may have a genuine commercial purpose. A limitation of this section of the Act is that there are no divestiture powers available. Such powers could potentially provide a constraint on a company's potential to exploit its market position.

3.71 The committee notes the advice provided by the ACCC suggesting that a strengthening of the unconscionable conduct provisions of the TPA would not be the most effective way to regulate anti-competitive practices in the industry. The committee notes the Commission's argument that Part IV of the Act, which prohibits a broad range of anti-competitive conduct, is the most appropriate vehicle to address anti-competitive conduct. The ACCC advised the committee that issues of possible anti-competitive conduct are best addressed by provisions specifically tailored to identify and remedy such behaviour.

3.72 The committee believes that there needs to be a strengthening of the provisions of the TPA relating to anti-competitive practices and abuse of market power. The committee considers that Part IV of the Act should be reviewed with a view to amending these provisions.

Recommendation 3

3.73 The committee recommends that the Commonwealth review Part IV of the *Trade Practices Act 1974* relating to restrictive trade practices with a view to amending these provisions of the Act so as to more effectively regulate anti-competitive practices and prevent abuse of market power.

Transparency in pricing and supply arrangements

3.74 Evidence to the inquiry indicated the need for greater transparency in pricing and supply arrangements across the whole fertiliser supply chain.

Pricing arrangements

3.75 Various arrangements exist with respect to pricing among wholesalers. Wholesale prices are generally set either in reference to international fertiliser prices (being formula-based) or after consideration is given to the prevailing cost of importing fertilisers. Some suppliers release recommended retail price lists. In addition, volume discounts or other benefits may be provided to customers.[46] The Australian Fertiliser Services Association (AFSA) stated that maximum retail prices

46 ACCC report, p. 12.

are virtually set by the manufacturers and importers leaving little scope in the other market sectors to have any real impact on pricing.[47]

3.76 The Australian Bureau of Agricultural and Resource Economics (ABARE) monitors and publishes annual statistics on Australian fertiliser prices, sales and trade in raw nutrient materials and manufactured fertilisers, as well world fertiliser prices. Fertiliser data collected by ABARE are published each December in *Australian Commodity Statistics*.[48]

3.77 Submissions noted that timely information on fertiliser prices is crucial to farmers' business decision-making.

> In recent years farm input and output markets have become increasingly volatile and farmers' exposure to 'raw' prices has increased (e.g. through deregulation). Access to timely information has become critical to farmers' commercial decision making.[49]

3.78 Mr Angus Taylor noted that most farmers currently rely on information gained from suppliers and distributors – few farmers have access to the underlying international prices and freight costs which influence domestic prices. Currently, fertiliser information is available through major market information providers, such as Bloomberg, although at a considerable cost which is beyond the means of most farmers. Access to the relevant Bloomberg information costs upwards of $20 000 per year.[50] Moreover, interpretation of this data requires a certain level of technical expertise.[51]

3.79 Mr Taylor argued that the issue of access to relevant information needs to be addressed through some leadership from government and/or farmers' organisations to ensure that this information is available to farmers in a readily accessible form.[52]

> There are two options to avoid a situation like this in the future. The first is that we expect the fertiliser suppliers to be forthcoming with that kind of information. Given the nature of the relationship between farmers and service providers and how that has evolved over recent years, I think that is unlikely as a practical outcome. I suspect that the more practical outcome to avoid a situation like this in the future is that farmers' organisations, government or others…should publish the international input price

47 *Submission* 5, AFSA, p. 2.

48 *Submission* 35, DAFF, p. 2.

49 Mr Angus Taylor, Tabled Document, 7 May 2009, p. 7.

50 Mr Angus Taylor, *Committee Hansard*, 7 May 2009, pp 31,33. Mr Taylor appeared in a private capacity. He is a director of Port Jackson Partners, a management consulting firm.

51 Mr Angus Taylor, Tabled Document, 7 May 2009, p. 7; Mr Angus Taylor, *Committee Hansard*, 7 May 2009, pp 28-31.

52 Mr Angus Taylor, Tabled Document, 7 May 2009, p. 7.

> information, delivered and properly calculated which in itself would take some work.
>
> That information should be distributed to farmers on a real-time basis and in a way that is accessible to them.[53]

3.80 Mr Taylor explained that the international price input information would be a FOB (free on board) price from relevant ports added to shipping costs to create a CFR (delivered at port) benchmark price. This then becomes an international price benchmark for the input – 'any retail margin will be additional, but it allows farmers to compare the international benchmark with their retail prices. Retail gross margins then become transparent'.[54] The committee understands that the price information would be a new type of data set that ABARE or other relevant body would need to collect from a variety of, and, in some cases, specialised sources. The raw data would then require fairly complex analysis to derive the relevant price information.

3.81 IPL indicated that it would support farmers' access to global fertiliser price information. Mr Gary Brinkworth, General Manager, Australian Fertilisers, IPL stated that:

> …would farmers benefit from being able to access global information or good information about what is happening in the global fertiliser market? I think we would agree the answer to that is yes. So, in terms of your first question, any approach or initiative that helps and informs farmers is something we would support.[55]

Committee view

3.82 The committee believes that there needs to be greater transparency with respect to pricing arrangements in the fertiliser industry. The committee considers that the Commonwealth through ABARE should collect and publish international input price information on fertiliser products on a regular basis and that this information should be widely disseminated to farmers. The committee believes that ABARE would be well placed to undertake this collection and analysis given that it already monitors and publishes a range of data related to fertilisers.

3.83 The committee considers that ensuring farmers have access to accurate, timely and accessible international prices and delivery costs for major inputs will ensure that they are well positioned to make judgements about the timing and quantity of their purchases.

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53 Mr Angus Taylor, *Committee Hansard*, 7 May 2009, p. 29.

54 CFR refers to Cost and Freight – basically, the price delivered at port. See Mr Angus Taylor, Correspondence, dated 10 June 2009.

55 Mr Gary Brinkworth, *Committee Hansard*, 10 August 2009, p. 4.

Recommendation 4

3.84 The committee recommends that ABARE:

- **collect and publish international input price information on fertiliser products on a regular basis on its website; and**
- **disseminate this information widely to farmers through the ABARE website, farmers' organisations, the rural press and other appropriate avenues.**

Supply arrangements

3.85 A variety of arrangements exist for the supply of fertilisers, with variations across functional levels and individual suppliers. Fertilisers can be supplied on the basis of formal contractual arrangements or less formal oral or written agreements.

3.86 Supply arrangements at the wholesale level (that is, arrangements between manufacturers, distributors and retailers) are typically made under long-term contractual arrangements. Due to the seasonal nature of demand and timeframes required for importation, suppliers often estimate their requirements on the basis of historical and seasonal forecasts and customers' preliminary indications of tonnage and product type before committed orders are taken. To accommodate ongoing variations in demand, contractual arrangements may be generally framed without specific obligations for supply or purchase.

3.87 Supply at the retail level (that is, supply to the end user) may be by written or oral arrangements. Farmers typically indicate their requirements immediately before or during a season. Supply to end users is often flexible and informal to accommodate unexpected seasonal variations affecting demand.[56] The ACCC noted that 'arrangements between the parties can be quite loose, with end users generally providing only an indication of future fertiliser requirements without intending to take on any legal obligations'.[57]

3.88 Concerns were however raised during the inquiry indicating that when farmers attempted to order fertiliser, especially from late 2007 and in 2008, they were unable to receive any certainty regarding price and/or supply. The NSW Farmers Association also reported that when farmers had managed to purchase fertiliser, the price had suddenly increased when the product arrived. [58]

3.89 The Association stated that:

> This year [2008] 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

56 ACCC report, p. 12.

57 ACCC report, p. 27.

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

> 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.

3.90 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.[59]

3.91 The ACCC also indicated that it received complaints from farmers' organisations about the lack of willingness of suppliers to commit to prices for the supply of fertilisers at the time of accepting orders.[60]

3.92 IPL indicated that it is improving its communications and business arrangements with customers. Mr Brinkworth of IPL stated that the company has introduced new ways of doing business to address concerns about fertiliser price uncertainty. This includes providing pricing options to give greater price certainty in a rising market, as well as deferred payment options. Mr Brinkworth further stated that:

> …we have continued to listen to what our customers are telling us. We have increased and improved our communications through an ongoing program, which includes face-to-face presentations to farmers and seasonal agronomic publications. I have personally met with many of our customers and farmers and I have presented at a number of industry conferences and events.[61]

3.93 The committee questioned IPL as to whether the company would be prepared to offer fertiliser at a premium in an effort to stabilise prices. IPL indicated that:

> Ultimately…we do price on an import parity basis, so whether the product is imported or comes from Phosphate Hill should make no difference to the farmer in terms of the price he pays.
>
> If farmers were willing to pay and there was a commercial proposition for farmers and for ourselves, then absolutely we would be keen to explore that. As I have been going around, I have not heard any of our customers indicate that they would be willing to pay a premium or to pay for that expense.[62]

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59 Mr Jock Laurie, NSW Farmers Association, *Committee Hansard*, 16 May 2008, p. 14.

60 ACCC report, p. 27.

61 Mr Gary Brinkworth, *Committee Hansard*, 10 August 2009, p. 2.

62 Mr James Whiteside/Mr Gary Brinkworth, *Committee Hansard*, 10 August 2009, p. 7.

3.94 The committee also questioned IPL as to whether permitting farmers to access fertiliser directly from the Phosphate Hill facility was a viable option. IPL stated however that:

> There is no simple solution. It was never built as a distribution centre. Significant capital investment would be required—
>
> …We would not allow a product to leave unless it met our quality standards, which would require screening and other, as I said, capital investment. There are some commercial challenges because it is a long way from many of the markets it would be supporting. Given the scale and the basis of the existing infrastructure, we do obviously have a rail contract where product is moved to Townsville. It is not simply a matter of loading up a truck and arriving at our Phosphate Hill facility, but we are open. We are looking at whether it is doable but I would have to say that there are a lot of challenges in making this happen.[63]

3.95 The NSW Farmers Association argued that information should be provided on the level of supply available. The Association noted that the amount of fertiliser available for purchase is unknown to consumers at present. While the Association recognised that companies have legitimate commercial-in-confidence considerations, the Association argued that general details of supply availability, including fertiliser shipments, would be useful to customers in being able to place forward orders and arrange finance in a timely fashion. This would allow farmers to structure their purchasing habits. Similarly, the Association suggested that if farmers were assured supply at agreed prices it would be beneficial for the industry to implement a more structured purchasing system where orders can be placed earlier in the season to prevent spikes in demand. The Association noted that, to a certain extent this is available, but the system could be improved to prevent uncertainty in the case of product orders not being fully met. The Association noted that farmers sometimes place orders but find that only a proportion of the order is eventually filled.[64]

3.96 Incitec Pivot noted that historically, the majority of Australian farmers have ordered fertiliser from distributors on a just-in-time basis, and have not placed firm orders until immediately prior to or during a season.[65]

3.97 The inquiry also received numerous allegations of suppliers failing to honour contracts and agreements. The farmers in question were then compelled to renegotiate contracts but at a higher price. The Hon Dean Brown, the SA Premier's Special Adviser on the Drought, in particular, provided a number of statements of concern in relation to trading practices from farmers on the Eyre Peninsula in South Australia. These, and other examples, are discussed in detail in the Interim Report.[66]

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63 Mr Gary Brinkworth, *Committee Hansard*, 10 August 2009, p. 8.

64 *Submission* 4, NSW Farmers Association, p. 6; personal communication, 23 June 2009.

65 *Submission* 26, IPL, p. 11.

66 Interim Report, pp 32-35.

Committee view

3.98 The committee believes that the industry should improve the level of information available to consumers on fertiliser prices and supply to provide for greater consumer certainty. Farmers, especially in 2007 and 2008, faced many difficulties and challenges due to rising fertiliser prices and issues of access and supply. Farmers have also become more aware of global prices, nutrient options and import alternatives and therefore need to be assured that suppliers deal with them fairly and that the industry operates in a transparent manner. The committee welcomes the initiatives by IPL to improve communications and business practices with customers as useful first steps towards improving transparency.

3.99 In the previous section, the committee recommended that international price input information should be published to address the issue of price transparency. The committee believes that, based on the evidence it received during the inquiry, it is unrealistic to expect that fertiliser suppliers would be forthcoming in this regard.

3.100 The committee also considers that there should be greater transparency in supply arrangements. The committee is of the view that fertiliser companies should publish general information detailing the amount of product in stock. This information would be useful for customers placing forward orders and in arranging appropriate finance. In addition, the committee believes that companies should provide greater certainty in the filling of product orders so that customers can be assured that their requirements are met.

3.101 The committee further considers that supply agreements between suppliers and customers should be on a more structured basis to address concerns in relation to suppliers failing to honour prior agreements with farmers for the supply of fertilisers. In situations where demand and prices are relatively stable, relatively loose arrangements between suppliers and end users may work satisfactorily, but where this is not the case, as was evident in late 2007 and 2008, the committee believes that more structured arrangements are needed.

Recommendation 5

3.102 The committee recommends that in the interests of transparency the industry improve its business practices to ensure that fertiliser companies:

- **publish general information, including arrival of shipments, detailing the amount of fertiliser available in stock; and**
- **provide greater certainty in the filling of orders, especially orders for fertiliser products placed earlier in the season.**

Recommendation 6

3.103 The committee recommends that, wherever possible, supply agreements between suppliers and customers be more structured and equitable, and, where appropriate, include standard contractual terms and conditions.

Industry codes of conduct

3.104 As noted in the Interim Report, industry codes of practice provide a mechanism for greater transparency in relation to pricing and supply issues for certain industries.[67] The TPA provides for the establishment of industry codes of practice.

3.105 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.

3.106 A non-prescribed voluntary industry code of conduct is administered by the industry itself and sets standards that are voluntarily administered by the industry. 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. 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.[68]

3.107 The operation of two such mandatory codes of conduct are described below for illustrative purposes.

Oilcode

3.108 The Oilcode came into effect in March 2007 as a prescribed industry code of conduct under the TPA. The purpose of the Oilcode is to regulate the conduct of suppliers, distributors and retailers in the petroleum marketing industry. The Oilcode aims to:

- improve transparency in wholesale pricing and provide better access to petroleum products at a published terminal gate price (TGP); [69]
- assist industry participants to make informed decisions when entering, renewing or transferring a fuel re-selling agreement by requiring disclosure of specific information; and
- improve the operating environment for all industry participants by providing access to a cost-effective and timely dispute resolution scheme.

3.109 The Oilcode establishes minimum standards for fuel re-selling agreements between retailers and their suppliers and introduces a nationally consistent approach to terminal gate pricing arrangements. The Code requires suppliers to post a TGP for

67 Interim Report, pp 38-39.

68 www.accc.gov.au

69 The TGP is the price for a wholesale sale of a petroleum product that is calculated on a temperature-corrected basis and expressed in cents per litre.

petroleum products and allows access for all customers, including small businesses, to petroleum products at TGP.

3.110 The Code also provides for a dispute resolution scheme, where disputes cannot be resolved in-house. The key objective of this scheme is to provide the industry with an effective and relatively inexpensive way of resolving disputes.

3.111 The role of the ACCC is to ensure compliance with the Oilcode and the TPA, including informing industry participants of their rights and obligations under law. Failure to comply with the Oilcode is a breach of s.51AD of the TPA. The ACCC can institute legal proceedings against parties in breach of the Oilcode and/or the Act.[70]

Horticulture Code of Conduct

3.112 The Horticulture Code of Conduct was introduced in May 2007. Prior to the introduction of the Code concerns were raised surrounding the relationship between growers and buyers of their produce, including the lack of transparency and clarity in relation to price and contract terms and the lack of an effective dispute resolution mechanism.

3.113 The Code aims to provide a set of basic minimum trading provisions that are enforceable through the TPA. Specifically, the Code aims to provide transparency and clarity with respect to price, contract terms, status of the buyer as well as access to an expedient dispute resolution mechanism.

3.114 The key requirements of the code are that traders (merchants) publish their preferred 'terms of trade' – that is, basic information on how they intend to do business with growers. The 'terms of trade' document outlines the minimum legal contract requirements under the Code. Under the Code, growers and traders use written agreements; traders are required to provide written transaction information to growers; and independent assessment is available on transactions.[71]

Effectiveness of mandatory codes of conduct

3.115 The committee sought advice from the ACCC as to the operation and effectiveness of mandatory codes of conduct.

3.116 The ACCC stated that these codes each promote a greater transparency in business dealings between contracting parties within the relevant industries. They also provide a low cost dispute resolution mechanism.[72]

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70 www.accc.gov.au. See also Issues Paper, *Trade Practices (Industry Codes – Oilcode) Regulations 2006 Review*, pp 1-7.

71 NFF/Horticulture Australia Council, *Horticulture Code of Conduct*, pp 1-8; NSW Farmers Association, *Horticulture Code of Conduct*, February 2006.

72 ACCC, Answers to questions on notice, dated 26 May 2009.

3.117 The ACCC also advised that the identification of benefits and disadvantages that might flow from the imposition of mandatory industry code obligations on a particular industry 'requires careful consideration of the harm sought to be addressed and the idiosyncrasies of the industry in question'. The Commission stated that:

> In the ACCC's experience, some care should be taken in this process to minimise the prospect of unintended consequences that might flow from such regulatory intervention.[73]

3.118 The ACCC noted that the extent to which any code would improve the level of transparency would depend on the current level of transparency; the mechanism proposed to deliver transparency; and the practical application of such requirements in the context of the specific industry in question.

3.119 In relation to contractual arrangements, the ACCC stated that an industry code can provide for some standardisation of contract terms though current industry codes do not specify the use of particular terms.

> Consideration of the advantages and disadvantages associated with some standardisation in contracts should involve careful consideration of the harm sought to be addressed and the specific characteristics of the industry in question. Any assessment would be influenced by the mechanism proposed to be used to deliver standardisation and the impact that mechanism would have on current industry practice.[74]

3.120 In respect to transparency in relation to pricing, the ACCC noted that price transparency can be described in terms of the costs in time and money for market participants to determine market prices, for transactions that will occur or have occurred.

> Where these costs are lower, the market has greater price transparency. In general increased price transparency has benefits for consumers unless it significantly increases the risks of anti-competitive practices among sellers. Where there is a concern that a market has a tendency to anti-competitive coordination, the nature of any proposed increase in price transparency needs to be carefully considered.[75]

3.121 In relation to the Oilcode, which requires wholesalers to publish daily a terminal gate price, the Commission noted that it concluded in its 2007 petrol inquiry that by requiring the posting of a TGP led to an increase in transparency, compared with a situation where prices were not published. However, the report also noted that the posted TGPs may reflect, only at the margin, the actual price paid by anyone in the market and therefore should be regarded as benchmark or reference prices, rather than 'actual' market prices.

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73 ACCC, Answers to questions on notice, dated 26 May 2009.

74 ACCC, Answers to questions on notice, dated 26 May 2009.

75 ACCC, Answers to questions on notice, dated 26 May 2009.

Committee view

3.122 The committee considers that some features of the mandatory codes of conduct described above could be applied to the fertiliser industry and may provide the basis for increased transparency in business dealings between contracting parties.

3.123 In terms of contractual arrangements, the committee notes that the Oilcode provides for standard contractual terms and conditions to be in place. The Horticulture Code also provides for a basic set of minimum trading conditions that are enforceable through the TPA. These features could potentially address several of the concerns expressed by farmers in relation to the need for improved transparency in respect of contractual arrangements.

3.124 In terms of pricing, a code of conduct may be less effective. The committee notes that the Oilcode provides that wholesale prices must be posted daily. Posting of fertiliser prices may be more problematic given the different suppliers, multiple sources of supply, and different types of fertiliser products involved.

3.125 The codes also provide for the establishment of an independent dispute resolution scheme. Such a scheme may not be as effective in relation to the fertiliser industry given the need for a very speedy resolution of disputes between farmers and suppliers. In the case of the fertiliser industry, the appointment of an arbiter may be a more effective option, given the need for an expeditious resolution of disputes in many cases.

3.126 The committee believes that, while the introduction of a mandatory code of conduct for the fertiliser industry would have some advantages, given the nature and structure of the industry, it may not be the best option to achieve transparency in pricing and supply of fertiliser products. The committee, therefore, does not recommend that a mandatory code of conduct for the fertiliser industry should be introduced.