



Submission

to the

Inquiry into the Price of Petrol in Australia

conducted by the

Senate Economics Legislation Committee

July 2006

1. Introduction

The Royal Automobile Club of Victoria (RACV) is the Victorian automobile club, representing the interests of 1.3 million Victorian motorists. It has, on average, a member in 2 out of 3 Victorian households. RACV welcomes the opportunity to make a submission to the Inquiry into the Price of Petrol in Australia, being undertaken by the Senate Economics Legislation Committee.

One of RACV's key roles as a representative of motorists is to monitor consumer issues. Amongst consumer issues, few if any are more important to our members than the price of petrol. In response, RACV has a high profile role in the Victorian community on this subject, including:

- Media: we are frequently called upon to provide independent, informed comment on issues related to petrol and petrol pricing.
- Research: we maintain a close watch on developments within the industry.
- Information: we provide information to the Herald-Sun newspaper on a daily basis showing the maximum price which we recommend motorists should pay for petrol on that day.
- Awareness: each month in our members' magazine RoyalAuto, we provide a breakdown of the components of the costs of fuel.

We believe therefore that we are in a position to make informed comment on the Committee's terms of reference, with particular application to Victoria. Accordingly, this submission should be seen as complementary to the submission tendered by the Australian Automobile Association (AAA), the national secretariat for the Australia's automobile clubs, providing a Victorian perspective alongside AAA's national perspective.

In the following sections, we address each of the Committee's terms of reference.

2. The relationship between the landed price of crude oil, refining costs, the wholesale price and the retail price of petrol

The basis of petrol pricing in Australia is the Import Parity Price (IPP). Although this concept is frequently misinterpreted in the media, the IPP is essentially the landed cost for Singapore-refined 95 Octane petrol in Australia, plus a premium for quality, freight, wharfage, and insurance. The IPP is initially calculated in US dollars, and converted to Australian dollars to give a landed IPP value in Australian dollars. To this is added a local component for storage, marketing and distribution. To arrive at a retail price, Commonwealth excise, GST, and a retailer margin is added to this figure.

RACV believes that the IPP formula is appropriate, since Australia can not be isolated from world fuel prices.

RACV's view is that in the Melbourne market at least, competition acts in the consumer's interest keeping prices down (particularly in the context of the discount cycle – see Section 4), but we are not as confident that there is sufficient competition outside the metropolitan area to achieve this outcome. We therefore recommend

greater price surveillance from the Australia Competition and Consumer Commission (ACCC), as outlined in the AAA submission.

In summary, in relation to Term of Reference 1, RACV recommends:

- That the Import Parity Price policy remains in place.
- That ACCC regularly reports on the movements of fuel prices throughout Australia.

3. Regional differences in the retail price of petrol

RACV analysis of petrol prices in Victoria for June 2006 shows that the average metropolitan price over the month was 137 cents per litre (cpl), and the average non-metropolitan price was 139.9cpl.

The Industry Commission in 1994¹ found that freight and storage costs accounted for almost all the differential between metropolitan and rural prices at the time. There have been a number of changes since 1994, particularly the introduction of transparent terminal gate pricing and greater competition in some country towns, but RACV believes that this Industry Commission finding is still probably broadly true today.

In relation to terminal gate pricing, consumers can access via the internet the terminal gate price, up to date retail pricing in both metropolitan and selected country centres, and crude oil movements. RACV believes that this transparency has assisted motorists, and consumer organisations such as RACV, to access and analyse daily movements in petrol prices.

The Melbourne metropolitan area, and some regional centres on major highways, benefit from a discount cycle (see section 4). However, RACV experience is that country people often struggle to understand the large discrepancy in fuel prices between some country towns and the Melbourne metropolitan area which can occur at certain stages of the discount cycle. Melbourne is an extremely competitive market, and at the bottom of the price cycle this difference can be quite substantial.

Therefore, in relation to Term of Reference 2, RACV recommends:

- That the 1994 Industry Commission report into petroleum products be updated, so that country consumers can understand clearly why there are often substantial price differences between country and metropolitan fuel prices.

4. Variations in the retail price of petrol at particular times.

Retail petrol prices in Melbourne and some rural towns on major highways are quite volatile, with a discount cycle applying, typically on a weekly basis. The price cycles in these areas are fairly regular and predictable. They generally exhibit a saw tooth

1. Industry Commission July 1994, "Petroleum Products"

pattern, with prices increasing rapidly over a short period of time, and steadily decreasing over following days.

As noted above, RACV receives a great deal of consumer feedback about the price of fuel. However, we receive very few complaints in relation the price cycle as such. Victorian motorists have become used to the price cycle, and many of them, where possible, take advantage of it. The RACV service provided through the daily Herald Sun petrol price watch (see Section 1) means that the Victorian motoring public is informed about daily price movements and can take advantage of the price cycle.

The Australian Competition and Consumer Commissions (ACCC) in its 2001 report on reducing fuel price variability² showed how and why the price discount cycle operates, but reported that consumers were confused about the price cycle, especially when prices increased by 10 cents or more in a single day, and when they occurred before weekends or public holidays.

However, RACV's view is that overall the motoring public is better served by a discount cycle, since we believe that motorists can and do take advantage of it, and that overall average prices are less than they would be if there was a uniform price throughout the week.

It is our understanding that this Inquiry came about partly as a result of complaints in relation to petrol prices in the lead up to the June 2006 Queens Birthday weekend. However, RACV's view is that, in Melbourne at least, that week was typical. The following table shows the daily price cycle in Melbourne for that week, as well as the preceding and following weeks. It can be seen that a similar pattern occurred, and that the week containing the Queens Birthday holiday was little different – if anything, there was less volatility during that week.

	Week prior to QB	Week including QB	Week following QB
Monday	131.9	137.3	No data collected
Tuesday	131.4	135.3	133.5
Wednesday	131.0	133.9	132.3
Thursday	142.0	143.4	144.2
Friday	140.0	140.6	141.9
Saturday	139.6	139.1	139.7
Sunday	138.1	136.8	137.3

Therefore, in relation to Term of Reference 3, RACV recommends:

- That there should be no legislative intervention to control the weekly discount cycle in retail petrol prices in Melbourne.

² Australian Competition and Consumer Commission, December 2001, "Reducing fuel price variability".

5. The industry's integrated structure

The oil industry in Australia has been traditionally vertically integrated, with refining, distribution and wholesale, and retail elements each under the control of one or other of a small number of oil majors. RACV's view is that vertical integration of the industry can produce efficiencies and cost savings, and therefore we do not have any objection in principle to this structure, bearing in mind that the Australian market is quite small in international terms.

However, at the wholesale and retail levels, the field is open to players other than the oil majors, and Australia has long had an independent fuel wholesaling and retailing sector. We believe that this has added competition, particularly in the metropolitan areas and major regional centres.

More recently, the market has changed again with the movement of the supermarkets (particularly Coles and Woolworths / Safeway) into the market, with these two chains effectively acting as the retail arm for Shell and Caltex products respectively.

This development has placed the other oil majors (BP and Mobil) at a potential disadvantage, since they are required to abide by the *Petroleum Retail Marketing Franchise Act (1980)* and the *Petroleum Retail Marketing Sites Act (1980)* in relation to their retail outlets, whereas by contract, Coles and Woolworths are considered under the Act to be a multi-site franchise.

The situation with Mobil is of particular concern to RACV. Mobil operates a refinery in Melbourne, and if the rules that Mobil has to comply with (that their competitors do not) make it uneconomic for them to remain in the market, we are concerned that it may consider closing its Melbourne refinery. This has already happened in South Australia, so it is not an unreal fear. This would leave Victoria in a precarious position, constantly in a state of under-supply, and heavily reliant on imports from overseas. While we do not of course have any knowledge of the long term plans of Mobil, we do note its moves in relation to the South Australian refinery, and the recent sale of many of its service stations to independents.

In the interest of maintaining a competitive environment, we believe that there must be a level playing field between all parties, and therefore we believe that the outdated legislation must be repealed, and the Oil Code (first recommended by the Industry Commission in 1994) be introduced immediately.

Therefore, in relation to Term of Reference 4, RACV recommends:

- That the Committee recognise the importance of a viable oil industry in Australia, and recommend that all those operating within the industry compete on a level playing field in order to deliver the best outcome for the community.
- That outdated legislation controlling the oil industry be repealed, and that an Oil Code as recommended by the Industry Commission in 1994 be introduced immediately.

6. Other Matters

The Committee's fifth term of reference invited comment on other matters. RACV suggests that no inquiry into the price of petrol in Australia would be complete without consideration of the taxation element. Currently, there is a fixed federal excise component (38.1cpl), and a GST component, with the latter based on the retail price including the excise component.

RACV takes particular exception to the fact that there is a GST on excise, since we believe that the principle of a "tax on a tax" is fundamentally flawed.

The feedback that we receive from our members suggest to us that governments must be seen to be doing something to relieve the very real pain that motorists are currently feeling at the petrol pump, and we believe that governments cannot continue to ignore this genuine and understandable public concern.

We therefore again call on governments to remove the GST on the excise component of the fuel price. This would produce an immediate drop of around 3.4cpl for unleaded petrol.

In addition, we suggest that the community is expecting the Federal Government to do something to recognise the pain of higher fuel prices, and do something about it. In the short term, the Commonwealth can reduce the pump price directly by reducing the amount of petrol excise it collects. RACV suggests that the Commonwealth consider a reduction in excise of 10 cpl as a means of easing the burden of higher petrol prices.

In the long run, RACV believes that excise should be replaced with an explicit road user charge, to more accurately reflect the costs of different classes of road user on both road infrastructure and the environment. The elements of this proposal are contained in the AAA submission.

Finally, we also draw attention to the recommendations in the AAA submission concerning investment in roads, and the call by Australia's automobile clubs to increase Commonwealth road investment to an amount corresponding to 12cpl.

In summary therefore we recommend:

- That the GST on the excise component of petrol be removed immediately.
- That the Commonwealth reduce petrol excise by 10 cpl.
- That in the longer term, fuel excise be replaced with an explicit road user charge.
- That investment in road infrastructure be increased to a figure corresponding to 12cpl.

7. Summary of recommendations

- That the Import Parity Price policy remains in place.
- That ACCC regularly report on the movements of fuel prices throughout Australia.
- That the 1994 Industry Commission report into petroleum products be updated, so that country consumers can understand clearly why there are often substantial price differences between country and metropolitan fuel prices.
- That there should be no legislative intervention to control the weekly discount cycle in retail petrol prices in Melbourne.
- That the Committee recognise the importance of a viable oil industry in Australia, and recommend that all those operating within the industry compete on a level playing field in order to deliver the best outcome for the community
- That outdated legislation controlling the oil industry be repealed, and that an Oil Code as recommended by the Industry Commission in 1994 be introduced immediately.
- That the GST on the excise component of petrol be removed immediately.
- That the Commonwealth reduce petrol excise by 10 cpl.
- That in the longer term, fuel excise be replaced with an explicit road user charge.
- That investment in road infrastructure be increased to a figure corresponding to 12cpl.