



**Supplementary Submission to the
Senate Economics Legislation Committee
Inquiry into the Provisions of the
Petroleum Retail Legislation Repeal Bill 2006**

2 May 2006

The Australian Institute of Petroleum (AIP) is pleased to present this supplementary submission on behalf of the AIP's four core member companies:

BP Australia Pty Ltd
Caltex Australia Limited
Mobil Oil Australia Pty Ltd
The Shell Company of Australia Ltd

AIP was established in 1976 as a non-profit making industry association. AIP's mission is to promote and assist in the development of a sustainable, internationally competitive petroleum products industry, operating efficiently, economically and safely, and in harmony with the environment and community standards.

AIP member companies play various roles in each segment of the fuel supply chain. They operate all of the petroleum refineries in Australia and handle a large proportion of the wholesale fuel market. However, AIP member companies operate and control only a limited part of the retail fuel market.

Contact Details

Should you have any questions in relation to this submission, or require additional information from AIP, the relevant contact details are outlined below.

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The purpose of this supplementary submission is to answer the question taken on notice by AIP and to provide further clarification of points raised in the Senate Economics Legislation Committee hearing on 19 April 2006.

Question on Notice

AIP took a question on notice from the Committee about the compromises which had been made by AIP member companies in negotiating the Oilcode package.

The market reform package is the outcome of several phases of consultation and negotiation with interested parties over the past 10 years. Over that period, many compromises have been made in order to find a workable solution for all parties.

A major concession was the introduction of a mandatory Oilcode under the *Trade Practices Act 1974* (the TPA). AIP member companies do not see the need for regulation that relates specifically to the oil industry, as no viable case has been made for treating the retail petroleum sector any differently than any other sector of the economy.

In the most recent phase of consultation during 2005, a major concession from AIP member companies was the maintenance of tenure provisions for franchisees at 9 years when the original proposal was for 5 years tenure.

In addition, AIP members have seriously considered a number of proposals from independent service station representatives. For example, various formulations were considered to prohibit below cost selling in the Oilcode; none of the proposals were found to be workable and were withdrawn from the draft Oilcode.

As a result of these compromises, AIP believes that the issues that can be addressed in the market reform package have been addressed.

Other Issues raised in the Committee

In summary, for the issues raised at the Committee hearing, AIP believes the following concerns have been addressed.

Issue raised	Addressed	Comment
1. Vertical integration	No longer relevant	Explicitly priced supply contracts for all Australian refinery customers.
2. TGP not transparent	Incorrect	Highly transparent at each stage of the supply chain.
3. Discounting from TGP	s. 155 TPA	Normal commercial practice is for large customers to receive bulk discounts. ACCC has the power to acquire this information if acquisition is warranted.
4. Predatory pricing	ACCC investigations	No breach found or prosecuted by the ACCC.
5. Access to Supply	s. 11 Oilcode	Any person with appropriate safety clearances can purchase a 35,000 litre load at TGP.
6. Less competition in the market as a result of fewer retail sites	Incorrect	Competition has intensified in retail petroleum even though sites have reduced from 20,000 in 1970 to 6,650 in 2004.
7. Oilcode is unenforceable and has no penalties	Incorrect	Oilcode is a regulation under the TPA. Oil companies have a strong company ethic of compliance with all regulations.
8. \$20,000 minimum is a loophole for oil companies	Incorrect	AIP member companies recall that this proposal originated from a major independent chain. The \$20,000 limit seeks to assure that the business relationship is more substantial than a supply contract.
9. Oilcode does not guarantee current contract terms	s. 32 Oilcode	As well as the protection in the Oilcode, AIP member companies have given public assurances on this issue.
10. Dispute resolution adviser should make binding rulings	Incorrect	The intent of the Dispute Resolution Adviser is to provide a low cost alternative to legal action but legal remedies remain an option under the proposals.
11. Oil companies do not have staff able to discuss fuel purchasing	Incorrect	All AIP member companies have customer service personnel available. In addition, dealers and distributors are supported by field service representatives.
12. AIP member companies do not comply with Victorian temperature correction legislation	Incorrect	AIP member companies comply with the law.
13. LPG should be included in the Oilcode provisions	Incorrect	This proposal was rejected in the Victorian TGP legislation because the participants and market dynamics are different to liquid fuels.

With regard to each of these issues raised in the Committee, AIP makes the following more detailed observations.

1. Issue raised

“There is still a public policy imperative to regulate the oil industry because of the degree of market power created by vertical integration in the industry.”

Oilcode is industry-specific regulation, so the claimed public policy imperative is satisfied. However, the degree of vertical integration in the industry is over stated particularly in relation to the refinery exchange system.

The system of refinery exchange contracts which operated between refineries for supply was abandoned in 2002 and replaced by explicitly priced supply contracts. In Australian States where an oil company operates a refinery, it remains vertically integrated in relation to its own refinery production. Everywhere else, that oil company is in the same position as any other customer and is not vertically integrated with refining. For wholesale supplies, Australian oil companies purchase oil and product from all over the world from a variety of producers and pay international prices, whether or not these sources are associated with AIP member companies.

2. Issue raised

“The Terminal Gate Price (TGP) does not provide transparency because discounting is allowed and very few sales are conducted at TGP.”

The various terminal gate prices quoted in Australia are based on the widely used Singapore price for fuel. As such, it is a highly transparent commodity with pricing information available at every stage of the supply chain (that is, crude oil, wholesale products and retail products). As was heard in evidence at the Committee hearings, BP conducts 70% of its sales to the retail market at TGP while Caltex conducts very few sales at TGP. This indicates (contrary to the evidence given by the Service Station Association) that oil companies do not operate in a similar manner and in fact have markedly different pricing strategies.

3. Issue raised

“There should be no discounts allowed from TGP but if discounts are allowed then the contract price should be scrutinised by a third party such as the ACCC.”

Prohibiting discounting would reduce competition at the wholesale level, resulting in higher wholesale and retail prices. It is normal practice in a market economy that large customers will achieve lower prices from suppliers than small customers because of their bargaining power. The retail petroleum industry is no different in this respect.

In addition, the MTAA argument against discounting of terminal gate prices does not recognise the cost savings and other benefits that accrue to the suppliers from bulk contracts. It is not true that it costs the same to supply a small customer as it does a large customer “because the same truck is used to deliver the fuel”. This assertion ignores the cost reductions in the supply chain associated with large and regular uplifts of product. Large supply contracts allow for a constant base load in the supply chain which improves the efficiency of these refining and distribution infrastructure assets.

As a matter of principle, AIP does not consider that contractual arrangements between private parties should be scrutinised by the ACCC as a matter of course. If the ACCC has a reasonable belief that an offence may have been committed, we note that it has the power under s.155 of the TPA to collect such information. We further note that price discrimination is no longer an offence under the TPA and we are not aware of any assertion that discounting at the terminal gate contravenes any provision of the TPA.

4. Issue raised

“Regional service stations can only purchase fuel above the board prices of supermarkets and other regional competitors.”

The ACCC has full power under the TPA to investigate and prosecute any allegations or instances of abuse of market power.

Regional service stations generally purchase fuel from distributors who purchase the fuel from refiners or importers. The distributors aim to charge a margin to cover the transport and storage of fuel as well as a profit but prices will reflect local competition. An independent service station operator has the option to purchase from another distributor or seaboard terminal but in practice will often contract for particular branding and supply arrangements which provide significant benefits but restrict flexibility during the contract term.

Any assertions about pricing would need to be considered on a case-by-case basis as to whether any illegal conduct could be involved. In any case, complaints of this behaviour have been made to the ACCC but no grounds were found to take legal action and no legal action has been initiated.

5. Issue raised

“The proposed Oilcode does not guarantee access to supply.”

Any person with the appropriate safety clearance can purchase a 35,000 litre load at any terminal. Section 11 of the Oilcode also guarantees supply at TGP.

After extensive investigations of this issue, AIP is only aware of one instance of refusal of supply which was on safety grounds. Caltex refused to load a partly loaded tanker of ethanol because of safety concerns about splash blending at the terminal, particularly the lack of firefighting equipment for colourless ethanol fires.

6. Issue raised

“The loss of service station sites would make the retail market less competitive.”

The overwhelming trend in the service station market has been to higher volume sites with ancillary services such as convenience stores. The increased presence of such sites has resulted in increased local competition. Spreading the site overheads across a greater volume and more services reduces costs to the site operator. Competition is across the complete offer to the customer, which is readily evident in the success of shopper docket and convenience store operations. Over the longer term, it is clear that the retail service station sector has become more competitive even though the number of sites has reduced from 20,000 in 1970 to about 6,650 in 2004.

7. Issue raised

“The proposed Oilcode regulations are unenforceable and do not contain any penalty provisions”.

The Oilcode is a regulation under the TPA and contravention can lead to action by the ACCC for breaching the TPA. Regardless of this fact, AIP member companies have a strong corporate ethic of compliance with all relevant legislation including with the provisions of the Oilcode.

If a company engages in any conduct that contravenes the Oilcode (which would be a breach of section 51AD of the TPA):

- the court may grant an injunction restraining it from engaging in that conduct (section 80);
- a person who suffers loss or damage as a result of its contravention may recover the amount of the loss or damage from the company. The aggrieved party may commence proceedings against the company at any time within 6 years after the contravention (section 82); and
- the court may make such orders as it thinks appropriate to compensate the person who has suffered loss or damage as a result of the company's contravention or to reduce that loss or damage.

8. Issue raised

"The \$20,000 minimum for franchise contracts creates a loophole for oil companies to structure contracts to exclude many franchisees from the Oilcode."

The recollection of AIP member companies is that the \$20,000 minimum was proposed by a major independent chain. AIP member companies consider that the intent of the minimum is to ensure that the business relationship is more substantial than a supply contract.

9. Issue raised

"The Oilcode does not guarantee that contracts "on foot" will retain tenure."

The accusation that Caltex has a contract clause which could be used to terminate franchise agreements in the event of repeal of the Sites and Franchise Acts has been repeatedly denied by the company. The Managing Director of Caltex, Mr Dave Reeves, has given public assurances to this effect and has conveyed these messages in writing to their franchisees. In addition, the Oilcode (s.32) expressly guarantees that tenure is retained on commencement of the Oilcode.

10. Issue raised

"The dispute resolution adviser should be empowered to make legally binding rulings."

The role of the dispute resolution adviser (DRA) is to provide a low cost alternative to legal proceedings. As the Committee heard in evidence from Associate Professor Zumbo, 70% of dispute resolution cases under the Franchising Code of Conduct were resolved through mediation with further cases resolved separately to the mediation process. Legal remedies are still open to aggrieved parties as an option at any time or in the event that mediation is unsuccessful. It would also be open for the DRA to report the outcomes of mediations to the ACCC and the Minister for Industry, Tourism and Resources.

We believe the introduction of legally binding rulings would substantially increase the costs (including the costs of representation) to all parties with no additional benefits.

11. Issue raised

"Oil companies do not have any staff able to talk about fuel purchasing."

AIP member companies all have customer service personnel who are available to discuss any aspect of fuel purchase. In addition, dealers and distributors are supported by field service representatives who are a key point of contact for any inquiries.

12. Issue raised
“Oil companies do not comply with Victorian temperature correction legislation.”

AIP member companies comply with all legislation.

13. Issue raised
“LPG sales should be included in the Oilcode.”

The inclusion of LPG in the TGP provisions was examined in public consultation of the Victorian TGP legislation. The proposal was subsequently rejected because the market participants and the dynamics of market competition are quite different from other liquid fuels. The same considerations apply to the inclusion of LPG in the Oilcode.