



**BP AUSTRALIA PTY LTD**

**SUBMISSION TO**

**Inquiry into the National Fuelwatch  
(Empowering Consumers) Bill 2008 and  
National Fuelwatch (Empowering Consumers  
Consequential Amendments) Bill 2008**

**5 August 2008**

## **1. INTRODUCTION**

BP Australia Pty Ltd (BP) is pleased to make a submission to the Senate Economic Committee's Inquiry into the National Fuelwatch (Empowering Consumers) Bill 2008; National Fuelwatch (Empowering Consumers) (Consequential Amendments) Bill 2008.

BP's submission focuses on three core issues associated with Fuelwatch: the proposal to improve pricing information for consumers; the proposal to fix prices for 24 hours; and operability of the draft legislation. There is benefit in this submission being read alongside the submissions lodged by the Australian Institute of Petroleum, of which BP is a member, as these submissions also provide broader context of operations of the petroleum industry in Australia.

## **2. BACKGROUND ON BP'S OPERATIONS**

BP's operations in Australia consist of:

- two refineries, one in Queensland and the other in Western Australia, which are critical to the production and supply of fuel products in Australia, including to the resources and aviation sectors, as well as for general transport and motoring;
- partnership in the Woodside North West Shelf LNG operation which accounts for over 40% of Australia's oil and gas production;
- a solar module manufacturing plant at Sydney Olympic Park which is the largest solar module manufacturer and the only commercial manufacturer of solar photovoltaic technology in Australia;
- around 260 company owned and operated retail service stations and over 1,000 service stations independently operated under the BP brand;
- approximately 5,000 employees; and
- payment in excess of \$A500M in taxes each year.

In Australia BP is a fully integrated refiner-marketer of petroleum products. This means that BP imports both crude oil and refined product, operates and stores product in terminals, sells products at the wholesale and retail levels and manages a distribution network. BP's operations cover the full range of products, including bitumen for our roads, jet fuel to supply our military and civil aviation industry, and diesel, which is used primarily in the resource sector.

While BP's submission only deals directly with those elements of BP's operations that are affected by the proposed Fuelwatch scheme, given the integrated nature of the business, the scheme has the potential to impact the entire business and thus any long run impact should be considered in the context the impact on the economy generally and Australia's overall energy security goals.

### **3. BACKGROUND ON HOW BP PRICES FUEL**

Given that a key part of the Fuelwatch proposal concerns pricing it is helpful to understand how BP prices fuel in Australia.

Broadly speaking, for fuel that is expected to be sold in the retail market, BP pricing occurs at three levels:

- Sales ex-refinery. The price is based on the landed price of Australian fuel grade standard product, the Import Parity Price (IPP). If a refinery tried to sell product above the IPP other companies would simply import product. Thus refinery sales and margins in Australia are governed by international refining margins as reflected in the IPP. Ex-refinery sales are also known as Buy-Sell because refiners buy and sell from each other, as well as import their own refined product. (Ex-refinery sales can also be made to other customers who have their own terminal facility.) Given the long distances but small size of the Australian market buying locally from another refiner is more efficient than each refiner transporting their own refined product to markets where they don't have their own refinery. The term Buy-Sell does not indicate any reciprocity in contracts with each being negotiated on commercial terms.
- Wholesale sales, ex-terminal. This pricing is based on a Terminal Gate Price (TGP). BP sets a TGP at each of its terminals. This is a build up of IPP plus all costs to and including terminaling plus a wholesale margin plus excise and GST.
- Retail sales. BP sets the price at the retail level for around 260 sites that BP owns and operates. Approximately a further one thousand sites carry the BP brand where prices are set by the operators, not BP - it would contravene the Trade Practices Act if BP were to intervene in this process.

In addition, BP negotiates large volume contracts with commercial businesses, such as those in the mining, manufacturing and transport sectors.

BP believes that the petroleum industry in Australia is highly competitive, contestable at all levels, and price build-ups are amongst the most transparent of any industry in the country. There is nothing to be gained, and much to be lost by price regulation in BP's view and any proposal to regulate fuel prices is not supported on the basis that this is more likely to reduce rather than increase competition in the industry.

#### **4. FUELWATCH**

BP will operate within whatever regulatory framework is set by government. This has been demonstrated in Perth over the past seven years where BP has been able to continue to operate successfully under the Western Australian Government's Fuelwatch regulation. However, BP cannot see any justification for the proposed legislation given that the ACCC, in its December 2007 report *Petrol Prices and Australian Consumers*, noted that "Using all this gathered evidence we are able to conclude that the unleaded petrol industry in Australia is fundamentally competitive" (page v).

##### **Improving Pricing Information for Consumers**

While BP does not understand fully why further consumer information measures are required in a fundamentally competitive market, BP does not oppose those elements of Fuelwatch which seek to improve the availability and timeliness of pricing information for consumers. BP is of the view that well functioning markets foster competition in the interests of consumers and a more efficient industry. Providing consumers with more price information is consistent with that belief.

With technology available today it would be possible to provide consumers with real-time, location specific pricing information direct to their mobile phone or other hand held device. Such an approach would provide better information for consumers while retaining the ability of fuel retailers to discount their prices during the day.

From BP's perspective the only requirement of this or any other approach to improving consumer information is that all participants must face equal costs. This is currently not the case with the service provided by Informed Sources where only a limited number of fuel retailers, albeit covering a large segment of the market, elect to pay for this service.

##### **Regulating prices (the 24-hour rule)**

BP cannot predict accurately what impact Fuelwatch would have if introduced nationally as each market is different. However, it is worth noting that BP has continued to operate in Perth with the Fuelwatch scheme in place in that market. There is no evidence that BP's business has suffered in Perth relative to other markets where Fuelwatch was not in place. Indeed BP does not believe that Fuelwatch has had any impact on retail prices in Perth.

Any argument by third parties that BP's opposition to Fuelwatch is because it will reduce profits is wrong. Rather BP is opposed in principle to those elements of Fuelwatch which regulate how and when individual businesses can change the price for the goods that they sell.

To date there has been no compelling analysis put into the public domain which makes the case for regulating prices. Certainly, no market failure has been identified. And prices are among the lowest in the OECD. In fact, as noted above, the ACCC concluded that the unleaded petrol industry in Australia is fundamentally competitive.

While it is true that the ACCC suggested that Government consider benefits of introducing a national Fuelwatch scheme and expanded pricing information for consumers, the ACCC noted that "...in time available it was not possible to fully review all the options...". The ACCC also noted that "a detailed assessment addressing these issues would have to be made before government could confidently embark on any one of the suggested options". Notwithstanding the additional analysis released by the ACCC, BP does not believe that the preconditions specified by the ACCC for introducing Fuelwatch have been met.

However, as the Prime Minister has noted on several occasions, the ACCC is the "only Government agency which has done the economic modeling" (interview on Sunrise Program, Seven Network, 30 May 2008). It is this very fact that concerns BP given that in its report the ACCC noted with regard to its econometric analysis, "These results have important caveats..." (page 247).

BP is of the view that these caveats are important to understanding whether or not Fuelwatch caused prices to fall in Perth relative to capital cities on the east coast. In particular, BP believes that the failure of the ACCC to include the differentials in the cost of freight by State is fundamentally important when assessing the robustness of their analysis. This is because freight is a key element of the Import Parity Price which, as noted in section 3 above, is central to the wholesale price at which petroleum products are sold in Australia.

BP has observed that since 1998 the cost of freight to transport product from Singapore to Perth has not risen as fast as the cost of shipping the same product to the east coast of Australia. In addition, the higher cost increases for the east coast apply to a higher base price than the relatively smaller increase in the cost of shipping to Perth.

As the ACCC noted in its report (page 252) "Any impact from transport or port charges is likely to be small as it would need to entail a significant change in the relativity between Perth and the other capitals, not simply a change in the level for Perth." And BP believes that that caveat is exactly what has occurred. BP has observed that shipping costs have increased significantly and contends that they are therefore quite material to any analysis of the impact of Fuelwatch on the Perth market. This could easily have manifested itself in the appearance of prices in Perth becoming relatively cheaper than prices on the east coast, as concluded by the ACCC, without necessarily being correct if changing differentials in shipping charges by State are excluded from any such analysis.

Given the exclusion of changing differentials in shipping charges by State from the ACCC analysis, which is a key component of the Import Parity Price (and hence wholesale prices), BP believes that further detailed analysis of the impact of Fuelwatch should be undertaken by the Government before proceeding to implement any proposal to regulate prices.

If such analysis has already been undertaken then it should be made public. As the ACCC noted in its report, "there are potential benefits and potential costs of adopting a national price commitment arrangement that need to be carefully considered". Further analysis should be undertaken and/or made public on both the benefits and costs of the proposal to fix prices for 24 hours.

### Intra-day Pricing

BP has noticed a shift over time in the Government's public explanations – or at least emphasis - of its rationale for introducing Fuelwatch, including but not limited to the shift from lowering petrol prices to removing intra-day price movements.

This rationale seems at odds with the December 2002 report *Terminal Gate Pricing Arrangements in Australia and other Fuel Pricing Arrangements in Western Australia* in which the ACCC concluded (page 3) that "Contrary to widely held perception, petrol prices are relatively stable on average within a day. In Perth during the period 16 October 2000 to 12 November 2000 (i.e. prior to the introduction of the 24-hour rule) the average number of changes was only 1.18."

BP cannot understand how reducing a fuel retailer's ability to lower prices during the day can benefit consumers. With the weekly discount cycle in place in most east coast markets the vast majority of intra day price movements are downwards. Indeed BP there is generally only one price increase per week. In an average week BP has observed that prices may be reduced in more than 90% of cases, with less than ten per cent of price change in a typical week being a price increase.

Consumers who are most price sensitive are already aware of this and thus have the most to lose from a policy which may change the well-established weekly price cycle. Coles, Woolworths and Nuemann all gave evidence to the ACCC inquiry showing that they sell more fuel at the bottom of the price cycle (ACCC report p175).

As stated by Coles, retailers rely on averaging their retail margins between the high and low points of the cycle. Any dampening of the amplitude of the price cycle will be noticed immediately by consumers who currently align their purchases to take advantage of the deepest discounts (ACCC report, p171).

Similarly, if there is a move nationally away from a weekly price cycle, as has occurred in Perth, this could disadvantage consumers who need fuel on a weekly basis and currently purchase in line with the weekly discounting cycle.

## Impact on small business

While most people's experience of BP is as a fuel retailer, a much bigger part of BP's business is as a fuel wholesaler. In addition to around 260 service station sites owned and operated by BP there are around a further one thousand sites that carry the BP logo. It is in this context, as a major fuel wholesaler, that BP is concerned about the impact that Fuelwatch will have on our dealers and distributors who own and operate or supply BP branded sites.

BP has a long established relationship with many of these small businesses and from this perspective is concerned at the disproportionate impact that Fuelwatch is expected to have on smaller operators. For example, a requirement to lock in prices for 24 hours provides the greatest risk to operators of the fewest sites. A single site operator who guesses wrongly and sets their price too high has their entire income stream locked out of the market for 24 hours. If the price is set too low they risk making insufficient margin to cover long run costs and, worse, running out of product, which damages their reputation as a fuel retailer. In contrast, the greater the number of sites operated the greater the ability to spread risk by pricing across the expected market range.

## **Operational issues**

While BP does not believe that sufficient public justification has been made to introduce Fuelwatch nationally, if the Parliament passes the legislation BP would nonetheless like to see some changes made to the Bills as drafted. As noted above, BP has continued to operate in Perth with the existence of a Fuelwatch scheme in that market which is essentially the same as that proposed to be introduced nationally. The views below are therefore based on the understanding gained from operating under Fuelwatch. The changes suggested aim to increase compliance while keeping to a minimum any additional costs, which are eventually passed onto motorists in the form of higher prices.

Firstly, BP has been able to operate in Perth with the requirement that prices on the console and main display board at retail sites must be changed at 6am, no earlier and no later. This has largely been possible due to the small size of the Perth market and time difference with the east coast. To replicate this nationally will require more staff, including extra staff at retail sites and in the main BP office in Melbourne prior to 6am seven days a week.

Extra staff will be required at sites because it is physically impossible to change the main price display board and the console within the 60 second window provided under the legislation. (BP has been challenged in the past for not changing prices by 6.02am.) Also, if a staff member is changing over the main display board they necessarily have to leave the console which means that they must stop serving customers and potentially poses an extra security risk. As a company committed to the health and safety of our number one asset, our people, BP now employs two staff at each of our sites in Perth for this changeover period. We would expect this to be replicated across the 260 sites we own and operate nationwide if legislation is passed in its current form.

Additionally, extra IT and support staff will be required to be rostered on and/or on-call much earlier than usual to deal with the inevitable computer glitches which, if not fixed immediately, require the site to be shutdown.

If the Government is committed to fixing prices – an approach BP believes is bad for consumers – moving the time required to change prices from 6am to 10am would minimise compliance costs as 10am is a slower time during the day for a site, but generally more than one person at site, so there are no additional labour costs or safety concerns. Also, at 10am there is generally a site manager or assistant site manager on duty with access to the office if there are IT issues which require manual entry of the price.

Additionally, a window within which to change prices e.g. 10 to 10.30am would assist compliance and reduce costs. As indicated above, it is physically impossible to changeover the console and main price display board simultaneously. At present head office staff and the operations team in Perth spend time chasing up details to respond to breach notices that may relate to the board being changed at 6.05am, when it can legitimately take that long for a service attendant to accept the price change and head outside with the board numbers. This all adds costs to the process, which inevitably is passed onto consumers in the form of higher prices.

Finally, as drafted, section 10(2) is too prescriptive in that it imposes a positive obligation to sell fuel (even where we may have none for sale due, say, to a stock out). This is quite distinct from an obligation, if an offer to sell is made, to sell at the notified price. The WA legislation makes it clear that it is only if a retailer offers fuel for sale that they must sell it at the notified price.

## **5. CONCLUSIONS**

BP does not believe that there has been sufficient evidence made public that fixing prices for 24 hours will result in lower petrol prices for Australian consumers, who already receive some of the lowest prices in the OECD. On the contrary, BP believes that the regulation of prices is generally bad for competition and thus may even result in higher prices over the longer term.

The Prime Minister has stated that the ACCC “did the economic modeling ... that was the advice upon which the Government acted” (interview with Lyndal Curtis, ABC AM program 30 May 2008). BP is concerned that the analysis undertaken by the ACCC included several caveats which do not appear to have been addressed in any subsequent analysis. In particular, BP believes that changes in the relative freight cost between Singapore and Perth and between Singapore and the east coast is significant.

While BP will endeavor to operate within whatever regulatory framework is set by government, given the conclusion from the ACCC that the petroleum industry is fundamentally competitive, the exclusion of shipping costs from the ACCC analysis, and the lack of public analysis available justifying the regulation of prices, BP would like to see further analysis on the potential costs as well as benefits that fixing retail prices for 24 hours will have on competition and prices.