

February 28, 2003

The Secretariat,
Senate Rural and Regional Affairs and Transport Committee
Room SG.62, Parliament House,
CANBERRA ACT 3560

Re: Wheat Marketing Amendment Bill 2002 – NETCO Submission

NETCO is pleased to provide the following submission to the Committee. The issues raised and surrounding the operation and funding of the Wheat Export Authority are more far reaching than they may originally appear.

Australia's wheat industry is at the crossroads, and we have an historic opportunity to refocus the industry as it was originally intended and in a way that reflects the new commercial realities impacting the industry.

Many organizations claim to represent Australian grain growers. No one organization actually can claim the sole responsibility of projecting growers' views and interests. In this newly commercial era where publicly listed companies own or manage government sponsored monopoly arrangements it is easy to misrepresent commercial interests of shareholders as the interests of growers and industry. They are not and should not be considered as such.

In considering the structures and funding alternatives for WEA, NETCO asks the committee to consider not only the current growing community, many of whom are shareholders in a number of grain based companies, but younger growers who did not receive the gift of shares built up as WIF equity during the 1990's, and the growers of tomorrow who will have no direct interest in these commercial shareholder companies other than to be considered like any other off farm investment.

The Australian grain industry is changing rapidly and the current structures are failing to keep pace to the detriment of Australian farmers and the community as a whole. We have a real opportunity and responsibility to amend these failings and we compel the committee to do so.

Yours sincerely,

Mike Chaseling
Chief Executive Officer

**SUBMISSION TO THE SENATE RURAL AND REGIONAL AFFAIRS AND
TRANSPORT LEGISLATION COMMITTEE**

WHEAT MARKETING AMENDMENT BILL 2002

NETCO CO-OPERATIVE LTD

FEBRUARY 2003

PRE-AMBLE

The referring of the Wheat Marketing Amendment Bill 2002 to the Senate Rural and Regional Affairs And Transport Legislation Committee represents an historic opportunity to re-set the paradigms driving the Australian grain industry. It is an opportunity that should not be lost.

In 1999, after an exhaustive development process, the Australian wheat industry agreed in partnership with the government to privatise the old Australian Wheat Board. The Wheat Export Authority was established and the statutory export control of the old Australian Wheat Board passed to the Wheat Export Authority. The newly privatised AWB was to be appointed the “manager” of the single desk.

Original proposals debated by growers at this time revealed a structure where a subsidiary company, AWB(International) Ltd, would be established with an *independent* board and this company would be responsible for managing the single desk, in partnership with the Wheat Export Authority.

In a classic case of political and commercial brinkmanship, the final structure was rushed through in the final weeks of negotiations and revealed a single desk manager intrinsically entwined within the commercial structures of the to be ASX listed AWB Ltd. Growers were generally unaware of this significant change. Those that were appalled!

What has followed has lead the grain industry down a path of commercial conflict of interest between monopoly managers and their commercial operations, unbalanced commercial growth in favour of monopoly holders, identification of significant cost savings for industry and growers subsequently rejected by monopoly holders protecting their private commercial interest at the expense of industry and a culture of conflict between industry players which is destabilising and counter to the interests of growers and the community generally.

The Wheat Export Authority is the appropriate body to provide independent industry oversight and control. It must be free to do so without influence from vested interest, and must be resourced appropriately. It should not be resourced at all if it is incapable or unwilling to interpret its role as the industry oversight body working on behalf of all participants. It must have a mandate to investigate issues and drive the dissemination of accurate industry information and opportunity.

The Wheat Export Authorities role must be interpreted to support the development of a broad export culture throughout the wheat industry, whilst regulating the domestic impact of the legislated monopoly holder/manager. If this is not achieved our industry will become commercially mono-cultural, we will forgo significant opportunity in driving supply chain competitiveness and market development and the pressure that will result may well see the whole industry explode and destroy the very structures the current arrangements were established to protect.

In considering the Wheat Marketing Amendment Bill (2002) the committee is requested to examine the context of the issues and the long-term impact these decisions are likely to have. We have an historic opportunity to bring to a head the issues of conflict, abuse of market power and transparency currently ripping the industry apart.

NETCO CO-OPERATIVE LTD

1. NETCO Co-operative Ltd is Australia's only "second tier" agricultural marketing co-operative. Our nine producer controlled co-operatives represent the interests of approximately 5,000 grower members. NETCO's growers are located in Queensland, New South Wales, Victoria and Western Australia. NETCO's growers produce an estimated 15% to 20% of total Australian grain production (around five to eight million tonnes) annually. NETCO's members also supply fertiliser and other cropping inputs to the grower membership. Consolidated group turnover is estimated for the 2002/2003 fiscal year at in excess of AUD\$250 million. Actual grain marketed and handled by the group in the 2001/2002 fiscal year was in the vicinity of 1,000,000 metric tonnes.
2. NETCO has an established interest in the issue of WEA operations and industry structure. As a co-commissioner of the report titled "*A Review of Structural Issues in the Australian Grain Market*" (2002), available on NETCO's web site (www.netcoop.com.au), NETCO has expended considerable time, effort and resources exploring these issues in order to be in a position to form informed opinions about what is driving the industry and what is actually in the interests of growers. As a co-operative NETCO has unambiguous motivation to seek industry structures that are in the interests of growers.

SUBMISSION FOCUS

3. This submission focuses on the issue of funding for the Wheat Export Authority (WEA). Central to the funding issue is the role of WEA and the ability of WEA to fulfil the role it was originally intended to fill. Have growers received fair value for their investment in WEA to date? How will WEA prove its relevance to growers and industry who fund it? How should WEA be funded?

4. This submission will highlight the many conflicts of interest and contradictions currently at play in the Australian grain industry (and particularly the wheat industry) and demonstrate how these issues have a material and negative effect on growers AND other industry participants. The lack of transparency, quality information, and quality analysis of the current industry structures represents a real challenge for WEA.
5. Appropriate structure and funding is essential in allowing WEA fulfil it's intended role as the custodian of the so called Single Desk Marketing System. It is imperative WEA has the independence and resource to provide the industry with appropriate regulatory oversight. Under the current system private companies that operate government sponsored monopoly arrangements are exerting undue commercial interest in deregulated domestic markets and along the domestic supply chain.

WHO OWNS THE SINGLE DESK?

6. It is NETCO's strong assertion that WEA is the sole custodian of Australia's Single Desk Marketing System on behalf of Australian wheat growers. WEA "contract" or "novate" this privilege to "Nominated Company B" so called under the Act – currently AWB (International) Ltd. AWB (International) Ltd (AWBI) is a wholly owned subsidiary of the ASX public listed company AWB Ltd. Some but not all of AWB Ltd's shareholders are Australian farmers. Many institutional investors now hold a stake in AWB Ltd.

AWB ROLE AND INFLUENCE OVER WEA

7. AWB Ltd and it's subsidiary AWB (International) Ltd have predominantly the same Board of Directors. AWB Ltd hold the Chairman's seat and a majority of board seats of AWB (International) Ltd. The three so-called "independent" directors of AWB (International) Ltd are actually selected and appointed by AWB!
8. AWB Ltd are currently the sole service provider to AWB(I). This is significant in relation to funding alternatives for WEA given AWB's excessive control over decisions of WEA. AWB(I) (in reality the same as AWB Ltd) has veto rights over any export bulk permit application to WEA. Not surprisingly no bulk permits have been issued by WEA/AWB Ltd to date. Additionally WEA seeks input and advice from AWB(I) in relation to other applications. Given AWB(I) actually does not employ one full time staff member (all staff are actually AWB Ltd employees) and given the majority AWB Ltd directors on the AWB(I) board, it is unsurprising consents for non-bulk permits are limited.
9. NETCO draws the committee's attention to the circumstances surrounding the growth in container exports, to the significant benefit of growers, during the 2000/2001 season. After significant market exploration and development, non-AWB exporters developed premium markets for Australian wheat in Vietnam. AWB moved to curtail the trade after the market was developed and subsequently opened an office in Vietnam – a market they previously had ignored or only sold to via specially appointed "agents" who effectively kept AWB shielded from the premiums available in that market. This example is important as Australian wheat was working to displace Indian wheat, which is a growing competitor to Australian wheat exports in South East Asia.
10. A further example of this influence was in the New Zealand market where Australian wheat for the first time in many years had displaced Canadian wheat. After AWB

pressured WEA to exclude or reduce permits for New Zealand, non-AWB exports became increasingly difficult to obtain for that market and Canadian wheat as a result again made it's way to New Zealand. In the WEA annual report we note of a total of approximately 50,000 mt of permits applied for AWB supported only approximately 500 mt for the New Zealand market. (*Source: WEA annual report 2001/2002*)

COMMENTS ON THE SCOPE OF THE BILL

11. In assessing the appropriateness of the Wheat Marketing Amendment Bill (the Bill) and particularly the funding structures for WEA, NETCO refers to the function of WEA, which is to:
 - a. Control the export of wheat from Australia
 - b. Assess non-AWB(I) applications for export permits for Australian wheat
 - c. Monitor the performance of AWB(I) in relation to the export of wheat and to examine and report on the benefits to growers that result from that performance
 - d. Review and report the performance of AWB(I) in the context of it's role as the appointed manager of single desk and it's use of it's export rights by 2004

FUNDING OPTIONS

12. The Bill looks specifically at two funding options for WEA, basically defined by industry (growers and exporters) pay directly via a levy or AWB pay as a "rent" if you like for having the management rights over single desk for wheat. In NETCO's view:
 - a. These are not the only options
 - i. Why can't the government contribute? After all it is a legislated monopoly?
 - ii. Why shouldn't AWB Ltd have to pay for the right to export wheat the same way as other exporters do?
 - b. On the basis of the two options put forward by the Bill, either way growers pay. Growers pay if they are levied directly, or indirectly as a tax on exports, which ultimately flow back as deductions to the price a grower receives.
 - c. The bill misleadingly refers to the cost of this tax in comparative terms to the FOB value. Growers receive in the vicinity of AUD\$40 to \$50 per metric tonne less than the FOB value, and as such the tax impost is not as insignificant as expressed.
 - d. NETCO believes if an export tax/levy is to be imposed, then the more direct and transparent that levy is the better. Therefore NETCO recommends the levy be directed on wheat exports, but be legislated to be shown as a direct deduction on all payments made from the national pool.
 - e. In NETCO's view the tax should not be applied to non-AWB(I) wheat exports on the following grounds:
 - i. AWB(I) exports account for 98% of all wheat exports from Australia
 - ii. The manager of the single desk has a dominant position in the market and has the systems in place to collect such a levy effectively
 - iii. Other exporters are already significantly dis-advantaged by the current system

- iv. The single desk system is designed to benefit growers who deliver wheat to the National Export Pool. These growers should pay for the authority which maintains and manages this system.

WEA REPORTING RESPONSIBILITIES & SCOPE OF OPERATIONS

13. Currently WEA has no direct reporting responsibility to growers or the industry generally, despite growers and industry again being responsible for funding WEA, as proposed by the Bill. NETCO believes adjustments to the current funding process should be considered within the context of a number of major issues. These include:
 - a. The independence of WEA to make decisions free from influence by vested interest, in-particular AWB Ltd for all wheat exports, bulk, bagged or containers
 - b. The ability, via regulatory authority of WEA to effectively fulfil it's charter. WEA requires appropriate power to investigate the number of issues of conflict of interest and domestic market and supply chain influence of AWB Ltd through AWB (I).
 - c. If growers and industry are to fund WEA, then WEA must have DIRECT LINE reporting to growers and industry, and WEA must be fully transparent to growers and industry in terms of the analytical methodology, market information and assessment process employed to determine approvals and rejections. Previously available information under the old Australian Wheat Board is now withheld from industry under the guise of "commercial confidentiality". It is our view the privilege of Single Desk management brings with it obligations, and supplying information to industry transparently is one of those obligations.
 - d. All services provided to the single desk manager, currently AWB(I), should be openly contestable. This should be a condition of privilege of management of the single desk. The current "closed shop" is nothing short of a farce, which diverts growers' funds away from export pool returns and into the pockets of AWB Ltd shareholders. WEA requires the authority and capacity to enforce this change
 - e. The entire relationship between AWB Ltd and it's subsidiary AWB (International) Ltd should be reviewed by WEA within the context of the spirit of the original legislation. AWB Ltd was established as a vehicle to manage the export of Australian wheat. The company now has investments and operations in seed breeding, storage and handling, export terminals, general logistics, quality testing, trading non-wheat grains, trading other origin wheat and other grains to traditional Australian wheat customers, chartering, food processing and non grain related investments such as it's 15% stake in Futuris Ltd (who owns Elders). Clearly the landscape is changing very quickly and it is imperative industry regulatory structures keep pace.
 - f. The growth in AWB's non-wheat export businesses is only achievable as a result of the closed shop arrangement between AWB Ltd, AWB(I) and WEA. It is NETCO's view management of the single desk for wheat is not a mandate for dominance in other openly contested markets, such as the market for storage and handling, the market for rail freight, the market for seed varieties etc.
14. NETCO believes the model adopted by the Western Australian government in the establishment of the Grain Licensing Authority represents a much more independent

structure for assessing the impact of grain export licenses and should be considered within the context of this Bill. In WA the manager of the state based single desk there has no power of veto, and has an onus of proof relating to the premiums they achieve in a particular market. Clearly this represents a system which is designed to succeed, rather than fail as is the case with the WEA/AWB structure.

ADDITIONAL INFORMATION RELEVANT TO CONSIDERING THE BILL

15. If WEA is to be effective it requires significant resources to build the capability to make informed decisions about markets and the impact of requests for export permits. It also requires the ability to contest claims made by the single desk manager whilst ever that company is involved in other activities.
16. NETCO believes the Wheat Marketing Amendment Bill fails to address a number of the key issues facing the industry and specifically:
 - a. Powers of WEA**
 - i. The Bill does nothing to strengthen the powers of the WEA to look after growers' interests nor does the Bill alter the reporting obligations of the Authority so as it's primary reporting lines are back to growers and industry who are paying the costs of running WEA.
 - ii. There needs to be a reinterpretation of the current charter to strengthen the WEA so it can be an effective industry regulator. The current interpretation of WEA's role is deliberately minimalist and is being manipulated away from the original intent. WEA openly admit they have no interest or authority to oversee any action by AWB Ltd, even though that company clearly has full operational control of the single desk
 - b. Transparency**
 - i. The current system provides no transparency to growers or industry in terms of the relationship between WEA and AWB, or the relationship between AWB Ltd and AWB(I). AWB(I) do not provide independent financial reports or cost breakdowns and growers are unaware of the contract relationship between these two entities.
 - ii. Links between the WEA, AWB and Grains Council of Australia do not constitute reporting to growers. Grains Council of Australia (GCA) is hopelessly compromised in terms of it's relationship with AWB Ltd. AWB Ltd have been responsible for large funding streams for GCA and the list of GCA presidents who miraculously end up with seats on AWB's board is in our view inappropriate. It appears a cushy arrangement and one not promoting transparency or rigorous policy development on behalf of growers.
 - iii. The list of conflict of interests being promoted by the current system is seemingly endless. We have the monopoly operator in Australia with commercial interests along the length and breadth of the domestic supply chain. AWB Ltd own seed companies, yet they are the company responsible of approving wheat varieties and appear unwilling to share information with GRDC under the guise of commercial interest. AWB Ltd own port facilities yet they control which ports grain will flow to for export, AWB Ltd negotiate freight rates utilising the export monopoly volumes as leverage, yet they set the freight deductions for all silo's

across the country, and they allow their domestic trading operation to have access to the monopoly sponsored freight rates, ensuring dominance across all grains in the freely competitive domestic market and supply chain. These activities are steaming ahead unchecked and with seemingly no consideration to the impact on a competitive market place in Australia, and without consideration for the overall impact on Australian grain farmers.

- iv. Rules should be established which:
 1. Identify what is industry based information and ensure the single desk operator has an obligation to share this information with growers and industry
 2. Openly disclose to industry and growers the basis for any contract for supplying services between AWB Ltd and AWB(I)
 3. Clearly obligate the manager of the single desk to make available to all in the industry information and historical data which is related to the operation of the single desk. No private company owns the single desk. The single desk is a community resource or structure and it's information is not proprietary to AWB Ltd. The single desk is a monopoly on accumulation and selling wheat, not on information.

c. AWB Ltd and AWB (I) Relationship and Service Contestability

- i. The boards of AWB Ltd and AWB (I) MUST be completely separate. AWB(I) must have an independent board in order to fulfil it's charter as the steward of the single desk.
- ii. The current closed shop service relationship between AWB(I), the single desk manager and it's parent company the ASX listed public company AWB Ltd is not serving the interests of growers and is operating outside the intent of the structure. AWB Ltd are using their privileged relationship with the single desk manager to build a domestic service supply monopoly. This is not in growers interests, is not what they want and is clearly anticompetitive behaviour in a freely contested market place

d. Competitive Supply Chain

- i. Two major industry studies, the "Kronos Report" and the "Accenture Review" have highlighted benefits running into *hundreds of millions* of dollars from freeing up the domestic grain supply chain from the clutches of a monopoly operator. These recommendations have no impact on the operation of the single desk marketing system yet they have been rejected out of hand by AWB Ltd and AWB (I). WEA must be in a position to ensure these savings are made available to growers and not stolen away by the sponsoring of one dominant player in what is an open domestic market.
- ii. In Western Australia Co-operative Bulk Handling who are the major port and upcountry terminal operator in that state have offered AWB(I) to provide all services up to point of FOB for AWB(I) for **FREE**. A **saving to WA grain growers in excess of AUD\$40 million per year**. AWB(I) and AWB Ltd have rejected the proposal out of hand. AWB Ltd's response was to offer to buy half of WACBH. Additionally AWB

Ltd has threatened to build huge storages in WA in competition to CBH despite having proposals in front of them to reduce costs for WA growers.

- iii. It should be noted that AWB Ltd have built in excess of 2.5 million tonnes of new storage over the last few years. An approximate 3.3 million tonnes of new storage capacity has been built in total over this period (*Source: Kronos Report, 2002*) Clearly AWB's position as manager of single desk is sponsoring such growth at the expense of operators who try to compete in an open market. This imbalance must be addressed.

CONCLUSION

17. Any amendment to the arrangements surrounding WEA must be addressed within the context of the issues at play within the industry. To not address these issues at the same time as imposing funding obligations on Australian grain growers and the export industry would be immoral.
18. WEA requires the resources to actually control the process of export of Australian wheat. At present they are simply handing a free reign to a publicly listed company which is aggressively utilising and abusing it's market power to drive it's own growth at the expense of growers' interests and at the expense of a competitive domestic industry.
19. The wheat single desk selling monopoly should not, as is currently the case, translate into a monopoly on the provision of services to growers.
20. Services to the manager of the single desk must be openly contestable
21. NETCO draws the committees attention specifically to recommendations in the "Kronos Report" (A Review of Structural Issues in the Australian Grain Market 2002) which of which NETCO was a co-sponsor and which include:
 - a. *"A greater degree of accountability and transparency is appropriate as an inherent responsibility associated with an export monopoly. In particular a fully disaggregated breakdown of all logistics and finance costs deducted from pool returns should be made publicly available. Appropriate corporate governance would also include a declaration of where these services are provided by associated entities, and what margins are being extracted."*
 - b. *"In a market structure that contains an export monopoly there is a need for public information to be provided by the monopoly holder to ensure that the market is functioning properly. Too much of this information is currently not available under the guise of commercial in confidence."*
 - c. *"In its current form WEA is not effective. Both the WEA and Grains Council of Australia (GCA) need to be adequately funded and resourced to provide an important oversight role. At the present time neither has sufficient funding or current expertise to be able to adequately assess the performance of AWBL and the impact that its activity has on grower returns."*
 - d. *"For the WEA to play an effective role it needs to be more independent of AWB in its activities. It is our recommendation that the structure of the export arrangements, and the WEA itself, be reviewed and enhanced."*
 - e. *"Full details of rail arrangements negotiated by the holders of export monopolies be disclosed to appropriate bodies such as WEA, UGH or GCA so*

that growers can confirm whether the cash activities of these organisations are using pool volume for advantage in their non pool activities.”

22. WEA funding should be increased and should be collected via a transparent levy on all National Pool wheat exports, but ONLY if this is considered within the context of reporting direct to growers and industry who fund the levy, and operations of WEA and ensuring WEA has the appropriate power and independence to effectively regulate the industry.
23. The Wheat Marketing Amendment Bill should only be considered if it includes provision for services provided to the export monopoly to be openly contestable. To not demand good process in this way is immoral and potentially sponsoring poor corporate governance practices.
24. AWB 's veto rights on export permit applications should be extinguished allowing WEA alone the power to regulate the export of Australian wheat.
25. Access to container and bagged export permits should be more widely available and not restricted to so called “niche markets” given the clear and obvious advantage a bulk supplier (AWB) has in terms of freight and logistical capacity. We note AWB Ltd is not excluded from the container trade however they do not require a permit to export in this manner.
26. Any changes to the current legislation should demand that the proposed scope of the 2004 WEA review of AWB(I) performance be expanded to clearly encompass the issues of domestic supply chain impact, transparency, service contestability, and the relationship between AWB ltd and AWB(I). The review should be a public one, calling for public submissions and be reported directly to industry and government. The review should be conducted by independent observers supported by WEA and industry.



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