

Productivity Commission Submission- Wheat Export Marketing Arrangements

1. Accreditation of exporters

Why accredit bulk wheat exporters?

Have market participants benefited from accreditation of bulk wheat exporters?

There has been a perceived benefit of an orderly transition to the accreditation of bulk wheat exporters, however there are significant compliance costs associated with obtaining and maintaining export accreditation, without demonstrable benefits to industry participants. The assurances that industry participants need in the Australian industry context can be achieved through more efficient mechanisms.

The disparity between the compliance burden on bulk exporters, compared with the absence of such burdens from a large number of containerised wheat exporters, places bulk exporters at a disadvantage, given the reputation implications in both origin and destination markets for the bulk exporters in the event of non-compliance (temporary or permanent withdrawal of accreditation) under the current arrangements.

AWB Limited (AWB) contends that through the operation of the Wheat Exports Australia (WEA), the Commonwealth Government may be construed to warrant the ability of accredited exporters to successfully engage in bulk wheat export and obtain payment. This would be a misleading and potentially risky position for the Federal Government to adopt, given the many variables impacting whether a given bulk wheat sale is successfully executed, the costs associated with each transaction and the flow of funds through to growers.

Does the information provided by WEA through accreditation assist growers with their export marketing decisions? Does WEA provide information that cannot be obtained from other sources?

AWB contends that in addition to price agreement and related contractual terms there are only two significant requirements that a grower should need to be satisfied before making grain marketing decisions in either the export or domestic context.

They are:

1. Counterparty risk: the risk of the purchasing counterparty will fulfil their payment obligations to the grower.

AWB believes that the WEA has a very limited ability to mitigate this risk, given the lack of currency of information that is provided by applicants for accreditation. Growers are in as good a position as WEA to judge the financial standing of grain buyers based on a combination of past experience, buyer behaviour in the prevailing market environment at the time they market their grain, as well as price and contract terms at the time of negotiating and executing a contract for the sale of their grain.

2. Quality integrity: that the buyer of grain from the grower will protect the reputation of Australia's grain quality by accurately describing the physical quality characteristics and basic specifications (e.g. protein, moisture, test weight) of the grain they have purchased when on-selling this quality to a subsequent buyer.

AWB believes that there are other authorities better placed to manage this risk than WEA. AWB believes that the Australian Quarantine Inspection Service (AQIS) is the appropriate authority to take on this obligation in the case of export grain (although this may require a change to the regulations and legislation governing AQIS's charter) and Grain Trade Australia (GTA) in the event of domestic market transactions (through the GTA arbitration process).

What role, if any, does accreditation play in the efficient operation of the wheat export market?

Based on experience to date, AWB can see no improvement in efficiency in the operations of the wheat export market by the accreditation of exporters of bulk wheat.

Does it alter the incentive to export wheat in bags or containers rather than bulk, or vice versa?

It is possible that accreditation alters the incentive to export wheat in bags or containers however AWB has no evidence of this. It is more likely that market forces determine the channel of sale.

Is there an ongoing role for accreditation of some form or is it needed only for a transitional period?

AWB acknowledges the significance of accreditation in providing transitional guidance from a regulated environment to an open and contestable market. It is AWB's position that the transition to establishing an effective operating environment for bulk wheat exporters has now occurred successfully.

The significant issues impacting the efficiency of the grain export sector are best managed by other existing regulatory authorities including: Australian Competition and Consumer Commission (ACCC), AQIS, Grains Research & Development Corporation (GRDC) or industry representative bodies including: GTA, Wheat Classification Council (WCC), Grains Council of Australia (GCA) rather than maintaining WEA to oversee accreditation.

AWB supports the maintenance of this transitional period until October 2010, when the WEA's role should be removed by amendment of the Wheat Export Marketing Act 2008, and appropriate consideration given to utilising the entities listed above to ensure ongoing successful operation of the wheat export market.

If ongoing accreditation is required, are there alternative options for accreditation that would deliver better outcomes? What are the costs and benefits of alternative options for accreditation?

AWB does not believe ongoing accreditation of bulk wheat exporters is required.

Is it appropriate that bulk wheat exporters be subject to an accreditation process when those in industries such as the following are not?

- ***Non-bulk exports of wheat and other grains***
- ***Domestically traded wheat and other grains***
- ***Other bulk export grains?***

It is not appropriate in AWB's opinion. History demonstrates that many existing accredited bulk wheat exporters have been able to effectively operate in the export and domestic markets for other grains as well as export wheat in containers, and likewise, several participants in the Australian export sector only operate by selling grain in containers.

Unlike other licensing and accreditation systems in place in the Australian industry, the bulk wheat accreditation system requires considerable management effort to maintain compliance reporting and address spot audits as well as annual and in some cases half yearly, performance reporting. There is no evidence to date to suggest any benefit to the industry for this compliance burden.

If ongoing accreditation is not required, what is an appropriate time for it's to end?

An appropriate time to end accreditation would be on the 30th of September 2010, in advance of the 2010/2011 harvest and in alignment with the end of the financial year for many grain companies.

What would be the consequences of removing accreditation?

It is possible that an increased number of participants may enter the market. Those companies that could demonstrate wheat export capability, a track record in other grain markets and offer competitive bid and contract terms may be successful in securing support in the form of grain acquired from Australian farmers.

In the absence of accreditation, would regulation of other aspects of bulk wheat exporting still be required? If so, which aspects? Is there anything particular about the wheat industry that requires additional regulations that other grains and commodities are not subject to?

There are several areas of the grain industry that do require regulation:

1. Export terminal access: The ACCC should continue to oversee an effective open access undertaking from port terminal operators to ensure fair and equitable access arrangements for all bulk grain exporters.
2. Up-country storage access: The ACCC's supervision of open access undertakings should extend to commercial up country storage providers to ensure effective competition is provided to farmers for their harvest.

Export grain specification certification – AQIS should be mandated to assure industry participants that the quality of grain exported reflects the quality specified on sales contracts.

Criteria and conditions

Are the eligibility criteria for, and conditions imposed on, accreditation of bulk wheat exporters appropriate?

No. The eligibility criteria, although not unreasonable for a transitional period, do not appear to add any particular value.

If not, what changes need to be made?

In relation to conditions imposed, if conditions must be applied they should be applied consistently across the accredited exporters (with the exception of tonnage restrictions) and should not restrict the exporter from participating in the market on a level playing field with their competitors. Conditions can impact on the participation of the business, resulting in potentially anticompetitive arrangements, reducing the efficiency and competition of the export market.

What is the appropriate duration of accreditation?

It is of AWB's opinion that accreditation should cease in 30th September 2010.

If accreditation is ongoing, should there be more stringent tests for initial accreditation than for renewals?

Ongoing accreditation renewals should be less onerous than initial accreditation.

Is there an overlap between the accreditation criteria (and conditions) set out in the Act and requirements of other existing regulations, such as the Corporations Act 2001 (Cwlth) and the Customs Act 1901 (Cwlth)?

There is overlap between the accreditation criteria set out in the act and existing regulations including:

- The *Corporations Act 2001*: covers obligations regarding record creation and retention, conduct of directors and officers of the company and solvency and liquidity related requirements including financial statements and external auditing.
- *Trade Practices Act*: covers obligations relating to fair trading, competition and other types of market conduct regulated by ACCC
- *ASX Corporate Governance Principles*: as a listed company AWB is required to comply with ASX corporate governance principles which include risk management, disclosure, integrity of financial reporting, remuneration, rights of shareholders, structure of the board, ethical & responsible decision making & management oversight
- The *International Trade Integrity Act 2007*: imposing obligations relating to breaches in UN sanctions, providing false or misleading information related to import or export of UN sanctions

goods, dealing with 'designated persons or entities and bribery.

- *Customs Act 1901*: Outlines obligations in relation to export quality of certain commodities as monitored by AQIS.

Level of Assessment

Is the level of assessment and number of audits undertaken by WEA commensurate with the expectations of market participants?

In the marketing year Oct 08-Sept 09, AWB Limited's two accredited companies have filed or responded to in excess of 50 compliance requirements ranging from licence applications, renewals, additional information for application/renewal, requests for information, external audits (4), compliance reports, exports reports, new executive officers information, and advising of other notifiable matters. AWB feels this has been excessive.

What benefits are provided by the current level of assessment, including audits?

The current level of assessment has added little value when assuring the industry of the robustness of the exporter.

What compliance costs are associated with accreditation for bulk wheat exporters?

The compliance costs associated with accreditation include:

- The fees prescribed by the *Wheat Export Accreditation Scheme* including application fee of a licence \$13,299.00 + renewal \$7,084.00
- Wheat Export Charge (WEC) of \$0.22/tonne on all wheat exports
- Cost of resources to respond to WEA requests.
- The implementation of an internal compliance plan & procedures

Not including the costs to the industry of the Wheat Export Charge for the first year of accreditation, AWB estimates the compliance cost for the company being \$600,000 (based on employee time spent dealing with WEA compliance issues). The majority of this cost was resource time in responding, gathering and providing information.

What regulatory costs do WEA incur from running the accreditation scheme?

AWB is not in a position to answer this question.

Could accreditation present an unnecessary barrier to entry for potential exporters of bulk wheat?

It is possible that some potential exporters have decided against participating in the Australian bulk wheat export market, being content to buy FOB ex Australian ports than provide competition in the bulk wheat export market. However, given the relatively large number of accredited bulk wheat exporters participating in the industry since deregulation, any such reluctance to participate in the bulk wheat export market has had little, if any, negative impact on competition in the Australian wheat export market.

How might the compliance and regulatory costs of accreditation change as the Scheme matures?

AWB estimates that in excess of \$8.5M of revenue was generated by the WEA's fee structure and Government support in the year ending 30 September 2009.

AWB considers that all of the necessary functions of regulation could be borne by other existing regulators resulting in a significant reduction in revenue required to oversee the industry, including bulk wheat, wheat and other grain in containers and other grain bulk exports.

Is renewal of accreditation a less onerous process than initial accreditation? Should it be?

To the extent experienced by AWB Limited that holds accreditations for its pool management entity (AWB Harvest Finance) and two cash marketing entities (AWB Australia and Landmark Operations) there is a considerable administrative burden in preparing for either initial accreditation or renewal of accreditation.

Recognising some of AWB's accredited exporter entities were subject to more thorough assessment and more onerous criteria to secure accreditation than most other accredited exporters (including six monthly performance reporting in the first year of bulk wheat export accreditation and additional conditions not applied to other exporters), AWB's view is that the ease or cost associated with compliance does not diminish in subsequent reporting periods relative to the initial application.

It is fairer to assert that the workload is correlated to the level of export volume and number of shipments actually performed and the number of accreditation criteria to comply with, rather than the renewal process being simpler/easier due to experience or repetition.

Role and funding of WEA

Is there any ongoing role for WEA? If so, what should the nature of that role be and how should ongoing functions be funded?

In AWB's opinion there is no ongoing role for WEA (beyond 30 September 2010).

Are there any other organisations that could take on the role of accreditation? Is there scope for tendering out accreditation? If so, would this reduce the cost of the accreditation process?

As described earlier, there are particular aspects of the export grain sector that require close regulatory oversight: this work is best provided by the ACCC, AQIS, and GTA in AWB's opinion. However formal accreditation of exporters and associated cost, per se is not required.

Are the current funding arrangements for WEA appropriate and sustainable?

No. WEA have built, within one year of operation under the WEMA, a considerable operating surplus that represents a tax on all participants of the Australian grain industry.

AWB does not consider the current funding arrangements reasonable or necessary.

Are market participants getting value for money in the services provided by WEA?

Not in AWB's opinion, due to the presence of other regulators who are better qualified, empowered (ACCC) and/or positioned in the operation of the sector (AQIS) to carry out the necessary regulatory oversight of the grain sector.

Can Australia learn from the approach that other countries take?

Australia, due to the evolution of the local grain industry structure and relatively high export volume as a percentage of production, has established a unique operating model. However to remain globally competitive, the Australian grain industry should be aiming to maximise operational efficiencies, minimise administrative costs and create effective competition with the primary objective of creating transparent, accurate and timely market signals to growers, who can then make efficient resource allocation decisions in production, which flows through to efficient infrastructure investment decisions by the wider spectrum of participants in the industry.

2. Port terminal access and services

How significant are competition concerns relating to port access? Is there evidence of owners of port facilities gaining a trade advantage over rival exporters?

The perception that the port terminal facilities have natural monopoly characteristics is correct¹.

The bulk handling companies ("BHCs") are monopoly providers of port terminal services. Access to port terminal services is essential to export bulk wheat from Australia. Currently AWB has no option but to use BHCs services for the export of wheat from their terminals. As a result, access to those facilities and services **under reasonable terms and conditions** is essential to promoting competition amongst exporters.

There is a risk that BHCs are able to exercise their monopoly power by discriminating in favour of their trading arms, disadvantaging competitors by imposing unfair terms and conditions and restricting Australian Wheat Exporters ("AWEs") access to port terminal services.

Ausbulk/Viterra (ABB)

Recently, Credit Suisse reported that²:

"ABB's bulk export infrastructure is concentrated in South Australia where it is the dominant competitor."

GrainCorp

Credit Suisse went on to report that³:

"Strong position in grain export terminals

GNC has a dominant position in the bulk export of grain along the east coast of Australia, owning all except for one of the bulk export grain terminals along the east coast of Australia. GNC's terminals are located at Mackay, Gladstone, Fisherman Islands, Carrington Newcastle, Port Kembla, Geelong and Portland."

CBH

CBH's monopoly position is exacerbated by Grain Express, which enables CBH to supply grain storage and handling services on the condition that growers and marketers of grain acquire grain supply coordination services from CBH and transport services from CBH whilst their grain remains in CBH's custody.

The BHCs transfer the risk and cost on to AWB by imposing unfair terms, charging prices that are unrelated to the cost of providing the service and by refusing access to services unless AWB agrees their terms and conditions.

In the absence of access regulation, what is the likelihood of 'regional monopolies' being formed?

In the absence of access regulation, the formation "regional monopolies" is inevitable.

Is the 'access test' under the Wheat Export Marketing Act necessary?

The access test is necessary. However, it should include access to up-stream services.

BHCs are monopoly providers of port terminal services within geographical areas. There are either very limited or no alternative providers of port terminal services within a distance that make them commercially viable competitors. AWB refers to its submission above.

¹ Productivity Commission Issues Paper at p.9

² Credit Suisse Asia/Pacific/Australia Equity Research Agricultural Products & Agribusiness report dated 27 April 2009, p12.

³ Ibid at p.44

Additionally, the BHCs enjoy either a monopoly or near monopoly on facilities which are upstream from to the port terminal facilities. Upstream activities of port operators are closely related to and cannot be separated from port terminal services. As the BHCs standard grain storage and handling agreements have historically illustrated, the port operator usually (either by itself or by a related body corporate) provides the upstream services and the port terminal services under a single contract. It is only since the port terminal access test has come into force, that the BHCs have used different contracts for the upstream and port terminal services.

There is very limited ability to physically move wheat from one port to another owned by another terminal service provider. The cost of interstate movement of grain is prohibitive.

What is the prospect of rival port terminal facilities being built? Does this vary across jurisdictions?

Credit Suisse concluded in its recent report⁴:

“The port component of the supply chain requires capacity to be added in large increments. The structures of existing rail networks and the high cost of road transport limit the ports to which grain can be transported. These factors create significant barriers to entry for businesses seeking to compete in the provision of storage and handling or port services.”

Credit Suisse also concluded that there are high barriers to entry into the South Australian market for the operation of grain export port terminals⁵. As the incumbent in the South Australian market, Viterro has a strong competitive advantage.

The likelihood of a new entrant establishing a new & profitable port terminal competing with port operators is low given the cost and current geographical spread of port terminals servicing the grain belt and competitive advantage of the incumbents. The 40,000 tonne Melbourne Port Terminal cost \$42 million (and took 2 years to build); and the 60,000 tonne port terminal at Outer Harbor at Port Adelaide an estimated cost of \$150 million (and has so far taken 3 years and is not fully complete). Construction costs (in particular steel), have continued to increase significantly. Based on recent industry data, AWB estimates that it would cost upwards of \$100 million to construct a new port facility with sufficient capacity to operate efficiently and attract in excess of 1 million tonnes. Additionally, obtaining suitable land, development approval from the relevant authorities and capital in a tight market for the building of port facilities and other infrastructure such as rail and roads are likely to prove prohibitive in the short to medium term.

Could access to port terminals be adequately regulated using only Part IIIA of the Trade Practices Act (without any link to bulk export accreditation)?

Access to port terminal services should not be regulated using only Part IIIA of the TPA. That regime is too slow and very expensive. It will be impractical if not financially impossible for most accredited exporters to pursue fair access through Part IIIA of the TPA.

Would the port terminals be declared under the National Competition Council process if the requirement for accreditation were removed? If not, why is there a requirement for access undertakings under the Act? What would be the consequences of removing the ‘access test’ from the Act?

In theory an application could be made under the NCC process for declaration. However, as noted above, access to port terminal services should not be regulated using only Part IIIA of the TPA.

Removal of the access test will most likely exacerbate the adverse impact on competition of the existing BHC regional monopolies. At the very least, the BHCs will be the primary exporters of bulk wheat from Australia, with a small number of other companies playing a minor role.

⁴ Credit Suisse report dated 27 April 2009, p.3.

⁵ Credit Suisse report dated 27 April 2009, p.9.

As an indication of the BHCs behaviour, shortly after their Undertakings were accepted by the ACCC, the ACCC contacted GrainCorp and CBH in regards to conduct that the ACCC believed constituted a failure to allow port terminal access seekers an opportunity to negotiate non-standard port terminal access terms.

How significant are the compliance costs (to exporters and others) and regulatory costs (to the ACCC) associated with the requirement to have access undertakings?

The costs incurred by AWB have been significant. However, the cost of not participating in the ACCC process far outweighs the alternative.

Have export opportunities for bulk handlers been disrupted due to the uncertainty stemming from the access process?

There have been disruptions. Some has been as a result of the access undertakings being a new process.

As noted by the ACCC, some BHCs have drawn out this proposed Undertaking process. They have not been open and frank. Each revised submission has in reality, been an attempt to have the ACCC accept their proposed Undertakings with as little as possible monopolistic advantages surrendered.

The timing of majority of the BHCs submissions to the ACCC has excluded the possibility of those submissions being subjected to proper public scrutiny and consultation before the ACCC provided its draft decisions.

Has the uncertainty around the access undertakings affected other exporters?

The BHCs did restrict access to their services until they obtained accreditation.

Is the requirement for port terminal access undertakings affecting investment in port facilities? If so, how?

Undoubtedly. In AWB's opinion any existing or potential future bulk wheat exporter seeking to develop new port infrastructure investments or acquire existing port infrastructure will assess the ease and viability of investing through an 'access undertaking' remote structure. The example created by the exemption of the MPT port facility demonstrates the real possibility of this approach. It should be noted that MPT is located in the one port zone in Australia where effective competition exists for port terminal services. However the fact remains that MPT is not subject to the same regulatory oversight as all other grain export terminals in Australia.

Should terminal access arrangements be consistent across all grains? If so, what should be the nature of those arrangements? If not, what are the consequences, if any, of bulk wheat being treated differently?

Yes. The same risks apply irrespective of the grain involved. To create a tilted playing field by only regulating access arrangements for one grain encourages BHCs to maximise their natural advantage in these other grains with limited to no effective recourse for other existing or potential exporters of those other grains. This is to the detriment of Australian grain producers and many buyers of Australian grains, including domestic buyers.

Is the publish-negotiate-arbitrate approach to access regulation the best approach? If not, what would be better?

As the publish-negotiate-arbitrate approach is new, it is not possible to provide a thorough comment at this time. It will be possible to provide a more substantive comment, when it becomes clearer whether the BHCs are actually willing to negotiate on their standard terms.

The ACCC has taken the view that the standard terms provided under the BHCs' indicative access agreements are intended to be the minimum terms and conditions of access to port terminal services and that access seekers will have the ability to negotiate (or arbitrate) non-standard terms that vary from any of those standard terms that they consider to be unacceptable, based on their own particular commercial considerations and circumstances. Only time will tell whether the BHCs do actually enter into meaningful negotiations.

The ACCC has also noted that should the publish-negotiate-arbitrate framework established by the Undertakings prove to be ineffective, the ACCC may adopt a more prescriptive method in any future access undertaking assessments. AWB agrees that a more prescriptive approach, which includes prescribing fair and transparent terms and conditions, including prices, may become necessary.

Are the charging mechanisms used by bulk handlers transparent? Do they advantage wheat exporting by the bulk handlers?

The charging mechanisms are not transparent and do advantage the BHCs.

BHCs transfer their risk and costs on to their customers (who are often also their competitors) by imposing unfair terms, charging prices that are not transparent and are not proportionate to the cost of providing the service. BHCs also achieve this anti-competitive effect by refusing access to essential wheat export services unless the customer agrees their one-sided, commercially unreasonable terms and conditions. It also often not clear whether more than one fee is being charged for provision of the same service.

Example: Viterra charges a vessel booking fee of \$5.00/t and up to a further \$1.50/t, where the vessel's ETA is less than 10 days. Viterra also charges a road under-performance fee of \$2.00/t, which is not applied against Export Select. CBH charges an upfront marketer fee of \$3.00/t, plus export fee of \$14.10/t. GrainCorp charges a cargo application booking fee of \$5.00/t and loading fee of \$2.45/t.

The BHCs' actual operating costs associated with vessel notifications do not increase in line with the tonnage that is to be loaded on board the vessel. All charges are in addition to other fees and are charged without any additional service being provided nor cost necessarily being incurred by the BHCs. In the event that the nominated vessel arrives outside the ETA, the same or similar fee is additionally charged to the AWE. Payment of the fee does not guarantee that the ship will be loaded on a scheduled date.

The charging mechanism advantages wheat exporting by the BHCs.

Is the ACCC well placed to deal with access disputes? Should another body be available to facilitate negotiation and arbitration of day-to-day issues where prompt resolution is important to exporting opportunities?

There are certain disputes such as substitution of vessels in shipping stems or any dispute affecting the timing of a vessel's loading that require a resolution within 24 hours. For these types of disputes, there must be a clear dispute resolution mechanism whereby disputes may be referred to an independent umpire for a binding decision within 24 hours. The GTA may be the appropriate body to facilitate this mechanism through the GTA Arbitration process.

Otherwise, the ACCC is well placed to deal with access disputes.

Should the bulk handlers have their wheat exporting businesses 'ring fenced'? If so, what form should ring fencing arrangements take?

The ring-fencing rules are critical to a fair and transparent access regime.

The substantial number of failings identified by the ACCC in the BHCs proposed Undertakings that require wholesale rectification is telling.

The BHCs have shown that they will not provide fair and transparent access to port terminal facilities to AWEs, unless required to do so under the risk that their trading arm loses export accreditation.

The imbalance in information is exacerbated by the fact that the BHCs provide upstream and downstream services. The result is that the BHCs possess a great deal of information about the trading activities of the customers who are often their competitors and are consequently in a position to advantage the BHCs related entities, or to disadvantage the customers.

The flow of information that creates an unfair trading advantage between the BHCs handling and trading divisions should be prohibited and there must be transparency and accounting separation between the two.

There should be a requirement for an annual audit regarding the transfer of information between the division and those findings should be publicly released.

There ought to be an obligation upon the BHCs to notify the relevant customer of any event that has or could likely result in a breach of the ring-fencing policy.

There must be a provision for employees to be adequately sanctioned for breaches that they might commit.

To what extent would ring fencing result in a loss of economies of scope from a more vertically integrated business?

If the Australian Government does not wish to have three regional monopolies, it should ensure fair and transparent access to BHCs services.

If there is to be a level playing field, robust ring-fencing arrangements must be in place.

Would it affect investment and innovation decisions?

Investment and innovation will arise where & when companies believe that they can compete in a fair and open market. There should be an increase in confidence to invest and innovate if effective ring fencing were in place.

What is the relationship between the 'access test' under the Wheat Export Marketing Act and state legislation relating to bulk handling companies? Do interactions between the Acts create unnecessary regulatory costs?

There is no direct relationship between WEMA and any state based legislation with the exception of the Essential Services Acts applying in Victoria and NSW.

It would be preferable for harmonisation of these State and Commonwealth Acts or a repeal of State Acts and strengthening of WEMA in relation to access test requirements.

Is there evidence of land-banking by bulk handlers? If so, is it of concern?

AWB has not been privy to that information. However, State and Federal Government agencies should be aware of the risk to the incumbent BHCs of competition being introduced at ports and actively encourage new entrants to assess opportunities to invest to create greater efficiencies in the supply chain to for Australian grain.

Are there any issues raised by the exemption of the Melbourne Port Terminal from the access undertaking requirements? Is the exemption appropriate? What are the likely consequences?

In AWB's opinion there are issues raised by the exemption of MPT from access undertakings. The exemption is not appropriate. However competition in the MPT drawing arc occurs due to the existence of the GrainCorp operated port of Geelong, the Viterra Australia port of Outer Harbor and GrainCorp's control of Port Kembla which all compete across the natural export grain drawing arc of MPT. Hence this is the only competitive market for port terminal services in Australia, creating a need for efficiency and competitive terms to attract volume into the MPT facility.

Are the shipping problems experienced in the first year of deregulation likely to persist?

It is likely that significant problems will persist however there is a better appreciation of the constraints in the supply chain held by the BHCs and exporters. Some remedial action has been taken with new shipping protocols and some investment in infrastructure however there is still a significant risk of delays occurring.

For example AWB expects the following issues to persist in the forthcoming season that will impact shipping programs:

1. Excessive heat will create issues for building stocks at ports as rail lines in particular branch lines, are not able to be utilized
2. Securing sufficient rail slots into ports remains an issue at ports on the East Coast
3. AQIS Shipping Inspectors are still required to wait until a vessel is alongside a berth before inspection: vessels failing survey are then pushed off the berth creating unnecessary delays at port and blocking terminals with grain
4. New shipping nomination rules are still sufficiently opaque with regard to interpretation (e.g. vessel nominations have been accepted in predefined months or monthly buckets with insufficient clarity on rules regarding priority to berth) that AWB expects issues when multiple vessels arrive simultaneously, raising the prospect of demurrage.

To what extent were there teething problems in the first year of deregulation? Or are they symptomatic of broader problems, or typical of a peak load situation?

There were significant teething problems and there have been endeavours to address some of these issues. However the broader problems, especially in relation to rail performance, AQIS Shipping Inspectors vessel inspection protocols and the participant uncertainty regarding interpretation of shipping stem management by the BHCs remain.

What role did the Grain Express arrangements play in alleviating (or exacerbating) these logistical problems?

CBH's monopoly position is exacerbated by Grain Express which allows CBH to supply grain storage and handling services on condition that growers and marketers of grain acquire grain supply coordination services from CBH and transport services from CBH whilst their grain remains in CBH's custody.

Grain Express has not alleviated the logistical problems. It has merely provided CBH with greater control over the bulk wheat export market in Western Australia.

Under the operation of Grain Express the transparency of the operation of the supply chain in WA became very opaque. CBH has publicly blamed the contracted rail operator (ARG) for creating the logjam, however it is clear that through poor planning and a lack of experience, CBH committed to far more shipments than the end to end system had capacity to support.

Logistical efficiency will be gained in WA by a rationalisation of some narrow gauge sites to road only sites and increased investment in rolling stock to expand the effective operational capacity of the ports. Additionally a more effective shipping stem management system will provide greater certainty to all participants regarding capacity and allow a more efficient allocation of resources.

The Grain Express system effectively removes the ability of the exporter to select specific parcels of grain from up country locations to meet their export customer requirements.

Did these logistical problems impede Australia's export performance?

The logistical problems greatly impeded Australia's export performance. Australia's reputation as a reliable supplier of bulk wheat was tainted. Further, sales were either lost to other countries or Australian exporters lost revenue when late shipment clauses in sales contracts were breached, meaning that that buyer was entitled to a lower purchase price.

Will the new CBH (auction based) shipping allocation system in WA work adequately to allocate port capacity at times of peak load?

An auction process will not address upcountry inefficiencies, encourage efficient utilisation of resources or provide incentives to upgrade facilities.

Auctioning shipping slot windows will not improve access to port terminal services for the following reasons:

- (a) An auction of shipping slots is not equivalent to access to ports. By its nature, not everybody can be successful at an auction. Those that miss out must turn to the secondary market, thus creating a demand for a secondary market and driving up prices in the primary and secondary market.
- (b) CBH admits that ship loading capacity is in excess of historical exports and, therefore, it is clear that what is being auctioned is the supply chain, not shipping capacity. CBH has consistently failed to stipulate what is the limiting factor to capacity in each port and continues to confuse the issue by vaguely claiming it depends on a wide range of factors and circumstances.
- (c) CBH treats shipping capacity at a specific port zone in a specific window as a commodity of which a fixed quantum is available. However, CBH is the sole arbiter of the quantum and no independent verification is available. CBH is proposing to offer 70% of whatever volume it decides to offer, in its absolute discretion. CBH has too much control over the decision-making at this point and its decision is not subject to scrutiny.
- (d) Auctioning of shipping slots does not create accountability for service standards that would address the damage to export performance.

CBH claims that the reason for auctioning shipping slots is that they anticipate that demand exceeds supply after the harvest period and therefore additional capacity, in the form of “surge” capacity, will be made available at a premium over the base core price. However, the capacity either exists or it does not. Describing it as “surge” capacity is a misnomer – it is the capacity at which CBH charges a premium for the service.

The auction process is ever-changing. There is no certainty as to what service is actually being provided. Discretions built in at every stage of the accumulation and vessel movement process remove certainty and accountability.

Exporters sell to their overseas customers under forward contracts. These may range from prompt shipment to up to twelve months’ forward, depending on customer requirements and market view. In order for exporters to fill their requirements to execute sales contracts, at present, they potentially will need to go through three different phases in order to achieve this:

- (e) The First Phase Auction - 70 pct of core capacity for whole year;
- (f) Second Phase Auction - balance 30 pct core plus surge 2 months prior shipping window with surge price only known before that auction;
- (g) Secondary market at unknown cost.

The risk for AWB and other exporters is that they do not know the actual cost of shipping until they have completed the acquisition of shipping slots. Further, they assume the risk that, in the end, they may still be short.

The consequence may be the loss of export market share to other origins.

The auction model is labour intensive, time consuming and complicated. Loading ships with grain is a relatively straightforward activity. The proposed detail in CBH's auction system will make the auction model unnecessarily rigid and complex. The auction process needs to match the fluidity of the grain and shipping markets, otherwise it will likely lead to confusion and chaos.

The first auction undertaken since the access test has not been successful. In many cases, AWB and other wheat exporters have only been allocated partial shipments. It is neither efficient nor cost effective to deliver bulk wheat to a discharge port in several ships, instead of one. Failure to load an entire ship will generally result in the charterer incurring dead freight (IE payment for failing to load the ship to full capacity). This can make the allocation worthless unless it can be combined in the secondary market.

CBH should be providing slots that are sufficient to load whole vessels.

Could the scheme be improved?

The scheme could be improved by bringing transparency in the allocation of vessel slots (see below) and ensuring that customers are allocated slots that enable the exporter to fully load a vessel.

It should be noted that the CBH 'rebate' unnecessarily complicates the understanding of costs. It is a season average which favours large volume exporters, like CBH over small players. The rebate only applies to the actual shipper, this means the secondary market is unlikely to trade except under duress. The cost for non use of is very high and the rigidity of CBH rules make non-performance likely or force rolling shipping positions at great expense.

Are similar problems likely to emerge in other states when those states have larger harvests?

Yes, in particular in NSW and Victoria there is a lack of rail capacity to manage large export programs and a lack of trucks to maximise port capacity thereby reducing competition for grain at times when prices should encourage grower selling.

Furthermore the GrainCorp port of Newcastle is capacity constrained due to its location, configuration and lack of investment (only two ship loaders were able to be maintained at an operational standard at GNC Newcastle this year, road delivery turnaround times at the port are very slow, and 40 wagon rail rakes are broken into 10 wagon shunts to discharge in the final few kilometres in the City of Newcastle).

Additionally at the GrainCorp port of Fisherman Islands in Brisbane significant delays in road discharge at the port created significant increases in freight charges in the last 12 months (mainly for bulk sorghum export movements). If a large wheat crop were to precede or follow a large sorghum crop, this port would not be able to operate near capacity, due to a lack of modest investment in upgraded sampling huts, weighbridge facilities and road discharge pits.

3. Transport and storage

Do upcountry facilities exhibit natural monopoly characteristics? Are alternative transport and storage arrangements being inhibited by the current arrangements?

Port terminal services are only one part of the services necessary for access to bulk wheat export markets. Competition in bulk wheat export markets requires that BHCs provide access to *all* of the services provided by facilities that are upstream from and separate to port terminal facilities. It is artificial to try to compartmentalise port terminal services from the upstream services when such services were until recently all provided by the same company and under the same contract.

Without some degree of oversight by ACCC on supply chain competition "beyond the ship loader" investment will be restrained. Potential investors in more efficient equipment (eg rolling stock) have no certainty over their ability to utilise this infrastructure and therefore have little confidence in an acceptable commercial rate of return.

The intake of grain at port by the BHC is subject to the judgement of best operational outcome for the port operator. The allocation of shipping slots is based on a risk assessment that includes an assessment of the available transport to the applying exporter in the case of GNC. In fact it is the commercial freight division of GNC who makes that decision. This decision flows through to:

- granting shipping slots on the basis that they purchase rail from the GNC freight book; or
- showing preferential treatment to those who have already booked freight with the GNC freight book over those who are utilising alternate freight modes or providers; and
- Knowledge as to who has booked freight with non-GNC freight providers.

AWB has been "locked out" of delivering to port by rail in 2009 due to GNC using their rail to accumulate grain to port (and filling available storage space) for non nominated vessels.

If so, at what cost?

The fixed (capital & overhead) cost of operating a typical east coast train set is in the order of \$10,000 per day. Therefore, the uncertainty that wheat exporters have over the port operators discharging the train can multiply into material amounts where significant delays are encountered in the event that the port operator does not provide unloading services for the train or utilises available storage by transporting other grain in to utilise their own assets.

Do the terms and conditions of access to upcountry facilities represent a barrier to entry for potential exporters?

Yes, examples include the higher fees at port imposed on receivals from third party storage and the lack of transparency and access at upcountry storage effectively "locking out" other entities from accessing rail capacity due to preferential allocation of that capacity to the controlling entity.

AWB is currently experiencing difficulties in accessing GNC up country storages to accumulate grain to port for a 3rd party customer due to GNC using its rail capacity to move grain to port for "potential" but not nominated shipping. This has the effect of ensuring the efficient operation and utilisation of GNC's port & contracted rail assets but limits the opportunity of competitors to develop their own supply chain capacity to ensure that they can accumulate required stocks for their shipments.

What is the prospect of competing facilities emerging? Does it vary across jurisdictions?

There is limited prospect of large commercial facilities being built, however there is an increase in on farm storage (OFS) nationwide in response to excessive interior supply chain costs. OFS generates quality control issues, however growers in response to escalating supply chain costs, are increasingly investing in assets they can control.

Is there any evidence of owners of upcountry facilities gaining an advantage over rival exporters?

BHCs are currently discriminating against receivals from competitor sites. In the case of GNC the charge is \$1.50/t greater for a competitor and in the case of Viterra and CBH the cost of trying to use third party stores outside of their bundled interior to port packages is prohibitive.

Should upcountry facilities be subject to access regimes? Can access issues be addressed through Part IIIA of the TPA? What about for grains other than wheat?

For the reasons set out above, upcountry facilities should be part of the access regimes.

As noted above, it will be impractical if not financially impossible for most accredited exporters to pursue fair access through Part IIIA of the TPA.

This should apply to all grains.

If upcountry facilities were subject to access regimes, what would be the impact on the efficiency of the transport and storage system as a whole?

The access regime would not have an adverse affect on efficiency of the transport and storage system as a whole as it will encourage greater certainty for customer and encourage greater investment to fix infrastructure bottlenecks.

Would it distort the transport system in favour of road and container transport?

No it should not distort the transport system in favour of road and container transport. Conversely it should encourage efficiency which supports rail and efficient bulk export pathways.

Do the Grain Express arrangements raise competition concerns? If so, to what extent do these offset benefits of economies of scale and scope provided by Grain Express?

Grain Express has the effect or likely effect of substantially lessening competition.

The existing market power of CBH is already strong enough that the restraints arising from the proposed exclusive dealing will reduce the ability of other suppliers and dealers to choose alternative sources of supply, particularly given the existing barriers to entry, and the long-term nature of the restraint once implemented.

There will in future be limited choice of road carriage providers in Western Australia if the selection is limited to successful tender (s) to Grain Express. Some road carriage providers who are currently operating in bulk grain collection and distribution are likely to be shut out unless they are a successful tender to Grain Express.

On the east coast over the past 10 years various exporters have made strategic “up country to ship” supply chain investments in the areas of up country receival facilities (AWB, ABA, Cargill etc) rail transport (AWB, Viterra (ABB) GrainCorp, Cargill), or road transport (Glencore) and ports (MPT). Under the Grain Express system, the exporter is bound to use all facets of the supply chain in a bundled manner, thereby effectively excluding the opportunity to make strategic investments.

This all but eliminates competition in the supply chain unless an exporter/s is prepared to invest in all three components simultaneously. Again, this has the impact of ensuring the efficient operation and utilisation of CBH's port and contracted rail assets but limits the opportunity of competitors to develop their own supply chain capacity to ensure that they can accumulate requires stocks for their shipments.

The public benefit is not served by protecting inefficiencies, cross-subsidisation, market distortion and eliminating competition as is the inevitable effect of Grain Express.

Is the rail system a problem for the export wheat industry? Has deregulation changed this in any way?

The rail system is a challenge for the export wheat industry. Simultaneously with deregulation, we have seen increased commitment to rail by industry participants. However, the uncertainty over the effective

utilisation of rail assets through the behaviours of port operators and the fragmented and substandard nature of the grain rail network has curbed the level of commitment and investment that industry participants have been prepared to make in storage and ports. Production volatility over time also constrains increases to the volume of rolling stock.

Are limitations of the rail, road and receival and storage systems impeding Australia's wheat export performance?

Yes. Capacity is being constrained in rail and port operation in particular and by incumbent BHC behaviour that limits investment in necessary infrastructure upgrades (Newcastle, Fisherman Islands) and results in suboptimal outcomes in logistics management (stock management and blending, rail acceptance protocols, shipping stem management in particular) to the advantage of the BHCs trading arms and to the detriment of growers, other traders and customers of Australian grain.

Additionally the lack of effective competition in the rail sector, created by a lack of investment in below ground infrastructure by private and government owners over many years has led to declines in rail capacity and led to higher rates being charged than are necessary. This inefficiency has also allowed monopoly port operators to under-invest in port efficiency as the lack of demand on port infrastructure has not maintained pressure on port owners to upgrade and remain cost competitive.

The lack of competition in most port zones for port terminal services has led to monopoly rents being extracted from export elevation charges that are well in excess of any comparative sector in competing origins. The historical structure of the industry has led to this outcome, and only effective competition or effective regulation will ensure that Australia's export grain sector does not suffer long term economic damage as a result of these arrangements being maintained.

Given the absence of commercial returns on many rail lines, can large scale investments be justified? To what extent is the system in need of rationalisation? Could the rural road system cope if some rail lines were closed?

The standard of grain network rail lines in Australia is a problem for the grain industry. Multiple gauge lines, speed restricted lines, equipment class restricted lines and axle load restricted lines are prevalent and all have the impact of reducing the efficiency under which rail can operate across the network. The flow on impact of this is two fold. Firstly it discourages investment because participants cannot either transfer equipment across zones/states to manage seasonal task variability or within zones to manage the task efficiently with the same equipment. Secondly, it increased the net cost of rail, thereby making road more competitive across many areas of the network

The industry would be substantially better off operating rail on a consistent, reasonable speed, reasonable access load network. If there is a need to rationalise some lines to accommodate this, up country inter-modal grain hubs need to be developed to accommodate the transfer of grain from farm to road, to rail and through to port. Unfortunately, the incumbent BHCs have significant legacy investments in inefficient, rail based infrastructure on sub standard lines and, by operating Grain Express (CBH) Export Select (Viterra) or the government granted branch-line service (GNC) they will continue to support the operation of all possible rail lines to service these sites at the expense of upgrading the core network that can generate material levels of efficiency.

Careful assessment and the creation of more inter-modal grain hubs (road to rail) will minimize road utilization but upgrades to some roads will be required.

Are rail logistics a more significant problem on the East coast?

Rail logistics are not necessarily a more significant problem on the east coast. However, there are specific issues on the east coast in the areas of multiple gauges, restricted lines within the same gauge (requiring different rail equipment) and limited pathway access to port, particularly in Newcastle and Melbourne.

If so, to what extent does the road system alleviate this?

Road movements to port have overcome some of the shortfall, more effectively where production zones exist within 200km of port (e.g. southern Queensland and areas of SA, VIC and Southern QLD).

Opportunity exists to use road to move grain from production points to the nearest efficient rail point to achieve most effective grain movement and transport mode utilisation.

Is truck access to port facilities a problem?

Ports are generally not well established to receive large volumes of trucks and are often located in metropolitan areas that lead to additional road congestion when high volumes of road are used to supplement rail shortfalls. As such, high volume and efficient movements to port are eminently more achievable with rail.

AWB is aware that CBH for example is upgrading road receivals in Kwinana to facilitate this need and reduce reliance on rail movements.

Do bulk handlers use the prospect of additional charges to discourage use of rival upcountry supply chains? To what extent are additional charges justified?

The BHCs do charge additional fees to discourage use of non-BHC supply chains. Some examples are set out below. AWB has requested how these charges have been quantified. No response has been received.

Example: GrainCorp charges a quality management fee of \$1.54/t for wheat received ex-approved storage and \$6.17/t for ex non- approved storage.

Example: CBH charges a fee of \$1.10/t additional non-grower receival fee and a fee of \$8.50/t where a customer wishes to have its wheat cleaned and dried by an external company.

Example: Viterra charges AWE's a fee of \$2.15/t more where AWB does not use Viterra's upcountry services, before the wheat is delivered to port. Additionally, Viterra charges a road under-performance fee where the customer does not use export Select of \$2.00/t.

Quality management fees are not justified given AWB has an incentive as an exporter to maintain quality irrespective of up country origins of the grains.

To what extent do bulk handlers continue to have relatively flat charging structures? Does this have efficiency implications?

The BHCs do continue to apply flat charges for services that may not be required or even provided.

Example: CBH is charging a fee whether or not services are used (cl.17.1(a)).

Example: CBH charges a vessel cancellation fee of \$3.00/t. In addition, CBH charges a shipping relocation fee of \$2.30/t in Kwinana or \$4.00/t in Esperance, Albany and Geraldton. CBH's explanation is that the shipping relocation fee may be charged if cargo for a nominated vessel is held at the terminal and needs to be relocated due to cancellation or delay – but this charge should be covered by the vessel cancellation fee.

Example: CBH charges a transfer of ownership fee of up to \$0.30 p/t, Viterra charge up to \$1.00 p/t for the same service. Viterra also charges a vessel substitution fee of \$2,000 and possibly a combination of a further positioning fee up to \$2.00/t, storage fee of \$2.00/t, bunker positioning fee of \$6.00/t and Outer Harbor positioning fee of \$8.10/t. GrainCorp has an inter-zone transfer fee up to \$2.82/t and buyer to buyer transfer fee of up to \$0.33/t. CBH charges its customers a \$0.05/t administration fee in the event that they wish to transfer capacity. CBH and GrainCorp apply a shrinkage factor of 0.5% for all wheat received. CBH and GrainCorp then apply a wheat dust deduction of 0.25% to wheat entitlement upon outturn. Viterra applies a shrinkage factor of up to 0.6% of all wheat received and a grain dust deduction of 0.1% to AWEs wheat entitlement upon outturn. Dust and shrinkage are the same thing. The BHCs therefore apply two deductions to their outturn obligations for the one cause. Further, there is no evidence of dust volume provided. Viterra charges a minimum cargo lift fee of \$1.50/t in the event that a vessel loads less than 15,000 tonnes at any one port. GrainCorp charges \$3.59/t where less than 5,000 tonnes is loaded and \$1.50/t where between 5,000 and 10,000 tonnes is loaded. These fees are not based upon additional costs incurred by the BHCs.

Example: Despite GrainCorp charging AWB \$1.10/t for Pesticide Residue Free Grain, GrainCorp will not provide details as to where that stock is held. Further, GrainCorp excludes liability in the event that the

grain is not free of such residues, unless negligence can be shown and in that case, GrainCorp limits its liability.

Example: Viterra charges all customers an administration fee of \$1,000. It is unclear for what service this 'administration' fees is charged or whether this fee is based on the cost incurred by the BHC of providing those services plus reasonable commercial margin.

Example: BHCs storage and handling agreements allow BHCs to move AWEs' grain between sites without permission while requiring that AWEs bear the costs and delay associated with the unauthorised movement. An example where this has occurred is referred to in one of AGEA's confidential submissions.

Example: AWEs are forced to bear the risk on wheat specifications and phytosanitary certificates.

Is there a need for rationalisation of supply chains and are current pricing practices impeding this?

It is widely recognised that there is a need for greater consolidation of up-country storage to increase the efficiency of rail movement by relying on fewer rail lines but more efficient utilisation of fewer lines to port (shuttle movements). Competing supply chains are desirable in a de-regulated market, given there is a market driven pricing signal to encourage efficient solutions to arise. In AWB's view this leads to longer distance grain movements on rail and shorter distance (less than 200 to 250 kmt) movements on road, as a rough rule of thumb.

Operating systems that exclude new up-country storage competition from accessing existing ports and cross-subsidise the operation of inefficient sites at a cost to more efficient sites (e.g. Grain Express) or the provision of subsidised rail assets (NSW) to maintain inefficient branch-lines are examples of pricing practices that are impeding the rationalisation of supply chains.

Governments should be encouraging rationalisation through appropriate policy settings (transport and land development policies in particular) to ensure an allocation of resources to efficiently operate and expand (or contract) supply chains to meet the requirements of farmers who can sustainably produce grain.

Does the ownership structure (or previous ownership structure) of some bulk handling companies lead to supply chain inefficiencies? Does it make rationalisation of uneconomic receival and storage facilities more difficult?

A cooperative ownership structure and the resulting approach to 'network pricing' across the port and up-country storage assets that is misaligned or not in concert with rail infrastructure asset decisions has led to inefficiency in the supply chain.

In particular under this approach the lack of investment in rail (which is not owned by the cooperative) to match the investment in up-country storage or ports by the cooperative, has led to a significant issue in WA. Due to the mismatch in mandates and investment expenditure over time, significant over-investment in up-country storage has occurred and an under-investment in rail infrastructure has occurred.

Growers (who are also members of the cooperative) have had expectations of service levels at local up-country storage facilities raised by the cooperative over-investing and are subsequently at risk of making incorrect resource allocation decisions on-farm (impacting whether or not to build on-farm storage, buy trucks, and impacting grain planting decisions) in response to this over-investment by the cooperative.

In corporate ownership structures there is a clear duty of the manager of the BHC to serve the interests of the share-holders but because most BHCs control a natural monopoly, there is also a tendency to protect inefficient sites to preserve market share and extract excessive returns from the operation of ports to offset the losses of operating inefficient up-country sites. In the East Coast the introduction of competition in up-country storage and the fact that the major competitors are all publicly listed corporations, increases the likelihood that over time rationalisation of uneconomic receival and storage facilities will occur. If competition at port were to increase this would speed the rationalisation up-country.

Does it make it difficult to price efficiently?

Network pricing of services by the cooperative masks the inefficiencies of particular sites making rationalisation more difficult. In general grower sentiment is heavily against rationalisation irrespective of ownership structure however this is exacerbated by the expectations of farmers who are also cooperative members.

Generally BHCs have failed to provide transparency in the pricings of services (greater bundling is occurring in WA, but also in SA) and this leads to the risk of inefficient storage facilities being maintained. Again, the extraction of excessive profits from the operation of the ports does offset the losses incurred by inefficient up-country facilities and this has prolonged the inevitable rationalisation of services.

The subsequent impact of this price distortion affects rail infrastructure: subsidised storage attracts greater grain deliveries than should otherwise occur and this historically has required rail providers to service these inefficient sites but on equipment (lines) that have not been maintained, reducing the returns to rail providers and ultimately leading to more expensive rail costs across the whole network.

Are issues of legal liability (transport related) constraining trade in wheat? How might this problem be solved?

BHCs deal with large volumes of stock and require advance notice and payment for shipping services, yet they do not guarantee the quality of the grain (or provide information to ensure transparency on quality) and take no responsibility, exclude any significant or commercially reasonable liability for loss caused by their conduct and do not provide any transparency on performance.

BHCs transfer the risk and cost on to AWEs by imposing unfair terms, charging prices that are not proportionate to the cost of providing the service and by refusing access to services unless the customers agree their terms and conditions.

Given the volume of stock BHCs handle, BHCs should not be allowed to cap their liability, exclude consequential loss claims or exclude liability unless caused by negligence (gross or otherwise) or wilful default. Examples of liability caps include:

- GrainCorp limit damages to \$500,000 for wheat outloaded on any shipping vessel and \$10,000 for wheat outloaded onto rail or road trucks.
- CBH limit Liability to \$100,000 for any single event and limit maximum aggregate of \$250,000 for the term of the contract
- Viterro limit liability to \$250,000 per event or per series of related events
- ABA limits liability to \$100,000 in total in respect of all events occurring within the term of this agreement and will be limited to \$30,000 per event.

The potential magnitude of a loss for an exporter can very significant. For example a 40,000 mt bulk vessel with contaminated grain at today's average price of USD 250.00/t would result in a multi million dollar loss to AWB.

The trend over the past 12-24 months has seen BHCs redefining quality standards for outturned grain to shift all risks onto the shipper. For example, the definition for nil tolerance by one BHC in regards to defects and contaminants is 0.05% by weight and this is way above the industry receival standards of 0.00%. This places the exporter at significant risk with the subsequent buyer.

This trend to redefine standards that only suit the BHCs and liability caps may motivate some exporters to ship out of specification grain which will negatively impact on Australia's international reputation. Liability terms and limits must reflect commercial reality and contain realistic limits on liability. Requiring BHCs to be responsible for loss or damage caused more equitably would improve efficiency. Currently BHCs have no incentive to do so. As a result, they fail to do so.

4 Information provision and market transparency

Is the information currently provided by the ABS and ABARE useful and timely?

The information provided by both these Commonwealth agencies is useful and beneficial in providing a base level of market intelligence and transparency into the operation of the Australian grain industry.

To create effective and accurate understanding of market dynamics, which facilitates a more efficient operation of the market and accurate pricing signals over time, it is imperative that information relating to crop production, export sales, domestic usage and stock on hand (both at port and at least in commercial up-country storage) assist all market participants to make more informed decisions regarding the operation of their respective businesses (grain production, storage management, transport management, domestic and export sales, port operations, industry policy).

The critical issues in this regard are accuracy and timeliness. Needs regarding timeliness will vary depending on the purpose behind the assessment of the data, however the need for accuracy in order to create an efficiently performing market is self evident. However currently, there is a significant ability for the current BHCs to access information in a more timely, more detailed and accurate manner than other market participants, creating an asymmetry of information that can generate substantial commercial advantage if this information is transferred to the trading arms of the BHCs.

The required information from ABS and ABARE should be provided more regularly (monthly) and greater interagency collaboration may be required to generate accuracy of information provided to all industry participants.

If timeliness is a problem, are there any mechanisms to facilitate more timely provision of information?

Information should be able to be collected electronically (online) and there should be means of compelling the provision of the information to avoid asymmetry of knowledge being created (e.g. a two tiered GRDC levy to apply to industry participants – substantially higher levies for non-compliant participants).

What amount and type of market information should be made available and who should pay for it?

At a port zone level the information that should be made available on a user pays basis for all commercially produced grains, oilseeds and pulses on a monthly basis includes; Crop production estimated, export sales both containerised and bulk, domestic usage and stock on hand figures.

With what frequency should information be provided?

Monthly with export sales (as performed, in bulk and containers) being reported weekly

Is there a role for WEA to provide information on the performance of accredited exporters? Would this assist growers in making marketing decisions?

Given the lack of timeliness, administrative compliance cost to the exporter, lack of coverage of all exporters (not containers) and the additional cost of running the WEA, (given other agencies are better placed to oversee the performance of exporters), there is no role for WEA in providing information on the performance of accredited exporters.

What are the requirements of disclosure of information on the amount and type of stocks held at grain receival facilities? Should they be changed? If so, how?

Presently, there is no guarantee of accurate information on the amount and type of stocks held at grain receival facilities. The BHCs reserve the right to move stocks without permission and no responsibility is taken for the accuracy of information provided. BHCs should disclose month end stocks on hand, without disclosing ownership. This information should be provided on each BHCs website.

Do industry participants have sufficient knowledge of how to use market information?

Yes, industry participants do have sufficient knowledge of how to use market information.

Who is best placed to provide market information and why? Can the industry deal with the provision of market information itself (for example, with a code of conduct)? Or is government involvement required? If so, what form should that involvement take? Regulation? Funding? Provision?

- Crop production estimated (ABARE),
- Export sales both containerised and bulk (from ABS but sourced from AQIS),
- Domestic usage (ABS)
- Stock on hand (at port, in domestic processors storage and at least in commercial up-country storage) (ABS)

Government involvement will be required. Government agencies should be given power through WEMA amendment to compel provision of information.

5. Wheat classification and market segmentation

Is the WCC adequate for ensuring wheat quality and the usefulness of wheat classifications?

Yes. WCC's role should be supported by peak industry groups (GCA, GTA, AGEA, FMCA). However WCC requires a mechanism to enforce compliance to decisions of the WCC to ensure the integrity of the WCC role (e.g. GRDC levy tiers).

Ideally WCC members would be elected by industry with minimum allocated representation for growers, domestic processors, exporters and plant breeders and an independent elected chairperson to ensure a democratic process is in place to create a truly representative body.

Could the market deal with these issues without such a body?

It is likely that short term commercial needs would override long-term commercial interests of the entire industry, at potentially significant cost to the reputation and economic value of the sector, if there was not a self-regulated body of expertise, elected by all aspects of the industry to oversee this decision making forum.

Does the market differentiate adequately between qualities of grain? Is the current level of commingling activity appropriate?

AWB is firmly of the view that there is not enough control being exercised by regulatory authorities over the description of basic grain quality (e.g. for export grain physical grain at load-port matches sales terms for protein, screenings, moisture requirements). This lack of independent oversight is undermining the reputation of Australia's grain quality. It is particularly evident that some container exporters are misdescribing grain quality without considering the long term damage these actions are having on the local industry.

Commingling at storage site is an accepted feature of grain storage practices across Australia. Operational costs would be substantially higher for all participants if commingling did not occur. As long as the rules for commingling are known in advance of the physical receipt of grain into a storage facility and the storage operator/agent warrants that the outturn quality will meet the minimum required receival standard quality, industry participants recognise that there will be some risk of loss (or gain) on quality terms as grain is turned through storage facilities.

For specific parcels (pesticide residue free, organic, genetically modified, or varietal specific segregation) buyers have the option of paying a premium to maintain the integrity of the specific quality they require, and this systems appears to be serving the needs of the market satisfactorily.

AWB considers the current level of commingling to be acceptable.

Is there adequate scope for marketing of particular types of wheat to service niches markets that are more narrowly specified than GTA standards? Does exporting through containers and bags provide a satisfactory way to exploit non-standard marketing opportunities?

Yes. There is sufficient segregated storage available for niche markets. Bulk, bags and containers can cater to these 'non-standard' marketing opportunities.

Are growers able to extract an adequate value for the quality of their wheat?

Yes. There is sufficient competition on quality terms and growers can exercise bargaining power with respect to grain quality by using on farm storage, warehousing and marketing grain over the course of a season.

Can quality control be left to market-driven forces, with commercial incentives placing a check on the quality delivered to overseas buyers?

There are sufficient mechanisms to drive accurate signals to growers on the production of needed quality but there are insufficient controls in ensuring exporters comply with contracted sales terms.

While the exporters who consistently deliver less than contracted specification are likely to lose repeat custom, there has already been significant damage to Australia's reputation as a quality supplier. AQIS as the most appropriate regulatory authority should be required to test grain cargoes at load point to assess whether contract terms for basic grain standards are being met.

Has deregulation affected the reputation of Australian export wheat?

There has been some damage created due to:

1. Excessive blending of lower quality grades (e.g. AH9) into higher quality grades (e.g. APW and AH2), without recognising the performance of the flour (rather than the visual assessment of the blended stock) will not meet the customers needs, despite the contract specification being achieved on basic (non-technical) standards.
2. Rogue container exporters who are wilfully misstating the quality of the grain being exported relative to sales contract terms, and
3. Inefficiency of the logistical capabilities of certain ports (e.g. Kwinana, Albany, Newcastle) creating risk to the buyers of late delivery and demurrage, which jeopardised their processing operations and has forced them to seek alternative origins to ensure adequate supplies remain accessible as required.

Has deregulation and the comingling of stocks increased biosecurity risks?

No.

Is quality control more of an issue for container wheat exports than it is for bulk wheat exports?

Yes, given the lack of regulatory response risk on container exporters. However this issue can be addressed without the need for WEA to be given control of container export accreditation. AQIS could more easily and effectively regulate quality in the bulk and container pathways to market.

Is quality control an issue in the domestic market?

It is not as significant given the domestic buyer has the ability to sample on receipt and reject deliveries, on relatively small volumes (truck or wagon loads) and force the seller to take immediate responsibility and risk to resolve the issue and still meet contracted terms and volumes by replacing the 'out of spec' volumes.

6. 'Industry good' functions

Does the list above represent legitimate 'industry good' functions? How should 'industry good' function be defined?

The list mentioned in the Productivity Commission issues paper reaches beyond a reasonable definition of 'industry good' functions in AWB's opinion.

Specifically research and development (GRDC), wheat variety classification (WCC), wheat receival standards (GTA), information provision (ABS, ABARE) and forms of trade advocacy (DFAT) are legitimate industry good functions.

AWB believes that 'industry good' functions are those services that should be undertaken by either government authorities or industry representative bodies to ensure information or services are provided in an independent manner for the benefit of all industry participants. These services should create long term benefit by neutralising the impact of issues that would destroy value for the industry in the long term if they were permitted to be undertaken through commercial channels.

The other categories identified by the Productivity Commission represent services that are best conducted by commercial entities where the action of the parties in undertaking these initiatives are predominantly or completely for the benefit of the party involved or where significant conflict arises within the 'industry' when addressing the issues arising in these categories.

Are there currently gaps in the provision of 'industry good' functions? If so, can these be left to the market to provide? Or is government involvement required? If so, how should these be funded?

The only significant gap in AWB's opinion is the adoption of uniform receival GTA standards for all grains. The lack of adoption of this uniformity creates a hidden cost and reduces the efficiency of the market in establishing price signals and creates barriers to the creation of trade flow liquidity, which increases the risk to growers, buyers, exporters and traders in the market-place.

This issue would not exist if BHCs effectively ring-fenced their operations activity from trading activity. If this occurred the BHC operator would be solely driven to maximise returns through grain handling assets by creating a common standard for all customers who would assist in maximising the attractiveness of their offering to grain buyers and sellers.

This change could be mandated as part of an effective open access regime requirement under the oversight of the ACCC.

Is there scope to use other grains or other agricultural industries as case studies for how 'industry good' functions could be delivered for wheat? Is there potential for synergies in shared provisions of 'industry good' functions across industries?

As a legacy of the heavily regulated statutory grain market monopolies and previously state government owned or operated or mandated storage and handling facilities, Australia has developed a unique grain marketing structure. It is doubtful that good proxies exist that closely reflect the needs of the Australian wheat industry and AWB observes that it is usually the case that excessive regulation of industry good functions creates a wasteful use of time, resources and taxpayer or industry participant funding and leads to excessive politicisation of the industry for limited benefit.

In AWB's opinion there are limited synergies available in sharing the provision of 'industry good' functions outside the Australian grains industry.

Is there anything to learn from the way that other countries deal with the provision of industry good functions in the wheat industry? Or other industries?

The US system reflects a relatively 'light-touch' approach to industry-good functions, but even there the existence of the US Wheat Associates, as a wheat promotion, trade and regulatory advocacy body duplicates many roles that are better undertaken by commercial participants.

The Canadian system is still regulated and heavily funded by the government and therefore is not a good example for Australia to follow.

AWB has limited knowledge of the approach in other industries to industry good functions, except that worthwhile 'industry good' initiatives (e.g. National Livestock Identification Scheme), require a construct of incentives and/or penalties to achieve outcomes that are viewed to be in the long term interests of the industry.

7. Performance of the wheat export marketing arrangements

Does the market provide sufficient signals to growers to enable them to make informed decisions about growing and selling wheat?

Signals occur in the following forms:

- Classification of wheat varieties
- Seed, fertiliser, chemical, land, machinery, fuel and equipment price
- Forward price signals (physical forward or grain futures forward curves)
- Grain storage costs (commercial up-country storage providers, port receipt charges or on-farm storage costs)
- Grain storage segregation planning at harvest in commercial upcountry storage providers
- Road and rail freight prices and containerisation costs
- Interest charges (pool finance rates, inventory warehouse finance costs)
- Additionally a significant amount of market information is available from independent market analysts and grain marketing companies that have both local and global reach.

How easy is it for growers to enter into a contract with an accredited exporter? Are transactions costs an issue?

It is extremely easy for a grower to enter a contract with an accredited exporter. Contract terms are available for review before contracts are signed and GTA and major grain companies have sponsored a national effort to increase grower awareness to the importance of appreciating terms and conditions of contracts before contracts are signed as well as providing guidance on the best approach to assessing and negotiating contract terms when marketing their produce.

In AWB's view transaction costs are not an issue for growers seeking to market their production.

Has deregulation opened opportunities not previously available to Australian wheat growers? Has deregulation enabled growers to extract a premium for their wheat that was previously unavailable? If not, is there potential for this to occur in the futures?

As expected a degree of innovation on grain contracting, price establishment, financing, grain storage and offshore marketing (new buyers being introduced to Australian wheat) has occurred since deregulation.

Export wheat marketing under the previous legislated statutory monopoly applied an approach to maximising returns that aimed to achieve an equitable outcome for all National Pool participants. The National Pool adopted an approach creating a reasonably predictable, single form of grain acquisition to acquire wheat and also involved a market clearing mandate as the buyer of last resort. Additionally when selling, the National Pool approach was to achieve price maximisation through quality differentiation (achieving a premium for Australian white wheat characteristics) and price discrimination into certain markets that excluded some offshore grain buyers from procuring Australian wheat. This approach is no longer relevant or optimal in a deregulated context.

AWB would argue that in most instances the ability for Australian farmers to achieve price premiums based on quality differentiation and by price discrimination in the preferencing of one buyer against another is no longer achievable given multiple Australian sellers now compete against each other to achieve a market position.

It is most likely that the premiums that growers are seeking will be achieved through the creation of more efficient supply chains (reduced costs) than in creating a sustainable price premium (beyond sea freight advantage and a premium for the low moisture, low screenings white wheat that is recognised as inherently superior value for flour millers in many offshore markets) for their wheat.

Has deregulation presented new challenges for growers? Have any developments been unexpected?

Growers have had to deal with higher freight costs to port and a larger percentage of farmers are now appreciating the challenge of understanding and executing marketing strategies across the year to achieve an acceptable level of return.

It was expected that on-farm storage investments would occur to assist the farmer to maintain greater control of their marketing programs and reduce freight and grain handling costs.

However many growers have been caught short by the lack of sufficient rail infrastructure and resulting lack of available road transport to substitute. This situation would have been substantially exacerbated had a large crop been produced in 2008 or 2009 on the east coast where the end to end export infrastructure is in a relatively poorer condition than in SA or WA.

Has deregulation affected large and small growers in the same way? Are smaller growers able to receive the same prices that larger growers receive?

The most significant affects of deregulation have been felt by those farmers who were less prepared to take active control of their marketing decisions and had less on farm storage. This distinction cannot be neatly ascribed to larger or smaller farmers.

Have the distributional impacts varied across jurisdictions or regions?

East coast farmers (particularly in NNSW) have been impacted more heavily by the loss of rail freight services given their distance to port and the resultant increase in freight rates to port, although this is not necessarily directly linked to deregulation, rather an indirect link based on the lack of investment in infrastructure that occurred during the period of regulation by both commercial interests and state governments.

Does the effectiveness of the current bulk wheat export arrangements vary across jurisdictions or regions?

No

Has the global financial crisis had an impact on the operation of the new wheat export marketing arrangements?

It could be argued that the Australian grain industry benefited significantly from the impact the global financial crisis, given the GFC precipitated a significant decrease in ocean freight rates and thus demurrage rates.

If the logistical inefficiencies of the WA and NSW rail and port systems had been experienced in early 2008 and the new wheat export marketing arrangement had been in place at that time rather than early 2009, demurrage bills on vessels caught by the inefficiencies of these supply chains could have had financially disastrous impacts on grain exporters, farmers, export grain buyers and resulted in substantial claims and possible class actions against bulk handlers and rail companies.

What have the costs of transition to the new arrangements been? Quantify these to the extent possible – note earlier estimates?

In addition to the direct fees of the new arrangements, transitional costs have largely been created by additional administrative compliance (estimated for AWB to be >\$600,000), additional representation to regulatory authorities to highlight the problems and iniquities of proposed or current regulatory arrangements.

Marketing expenses have been modestly higher as commercial participants have sought to distinguish their presence in the market to farmers and buyers.

How do these compare with the benefits of the new arrangements?

The significant benefits are yet to be demonstrated, albeit many growers and buyers appreciate the freedom to select new marketing and purchasing channels respectively.

New investment in infrastructure to reduce supply chain costs, increase export capacity and create new supply channels for both farmers and buyers, which in turn will drive the need for further innovation and stimulate further productivity within the sector are yet to be fully expressed.

AWB believes that beyond the first two years of transition, the costs of maintaining the current accreditation arrangements represent an un-necessary burden on the industry, whereas the need to create a more competitive supply chain infrastructure to ensure Australian grain farmers can extract sufficient returns to continue producing for export markets is a far more significant issue that needs and justifies continuing regulatory oversight through the ACCC's requirements for open access undertakings by BHCs.

Has deregulation altered trends in the share of wheat exported in bulk and in bags and containers? If so, will the trend continue to change if current arrangements remain in place?

The trend has not changed due to deregulation. The trend to an increased volume of containers was initiated by relative value of bulk ocean freight prices (inflated by substantial demand for bulk minerals from China and India) relative to container ocean freight values and the fact that Australian is a net importer of packed containers and was a net exporter of empty containers.

Deregulation of the export wheat sector in Australia has coincided with this development and facilitated a rapid increase in grain containerisation capacity.

It is likely that with the continuing increase in demand from South East Asian markets, (from both existing and new entrants), the current capacity is maintainable but in future periods the economics of bulk delivery of grain will substantially out compete the economics of container supply and this is most likely to be driven by the availability of supply of dry bulk vessels globally and supply of packed containers entering Australia.

Given the relatively recent introduction of such major changes, how do you see developments in the wheat export sector in the medium to long term under the existing arrangements? Do you consider that there is still some way to go in allowing the arrangements to 'bed down' and for industry participants to adapt to, and further exploit, the opportunities that a more open marketing arrangement allows?

AWB expects further consolidation in the number of market participants in the bulk export sector (fewer but larger trading houses), growth in demand from the domestic sector (local processors) and an increased level of investment in the supply chain at both the port, rail and on-farm storage links.

Rationalisation of outdated rail line network configurations will occur leading to a greater reliance on road movements to rail consolidation points in the interior and an increase in road to port movements to supplement shuttle rail movements.

GM technology will be adopted more widely in Australia to meet the increasing demand for protein in neighbouring countries and to increase on-farm productivity in an increasingly erratic climatic setting.

Australia's share of the world trade in wheat should decline as alternative origins increase productivity substantially faster than Australia can, given the limited available arable area for crop production (e.g. Black Sea and Brazil). However, absolute volumes will increase with continued productivity improvements, albeit with common drought events, as experienced in the last five years in Australia, resulting in greater revenue variability for sector participants.

Australia's grain industry will need to continue to be flexible and innovative to meet these challenges. To facilitate this and increase the profitability of Australia's grain farmers the industry should seek to extract efficiencies as quickly as possible.

In AWB's opinion, maintaining transitional arrangements that add little value, or to allow natural monopolies to flourish at the expense of the wider industry, is not the optimal environment to facilitate

the necessary changes to drive greater efficiencies throughout the Australian grain industry over the long term.

A further period of 'bedding down' of the current arrangements represents a lost opportunity to address the key issues of supply chain efficiencies. Farmers have adjusted to the transition to export deregulation as the domestic buyers did post domestic deregulation of the wheat industry in 1989. However addressing the issues associated with the unsustainable export supply chain remains the primary challenge for the industry for the foreseeable future.

If some form of regulation is required only for a transition period, how long should this transition period last?

AWB believes the transitional period should end by October 2010, when an amended WEMA should be legislated to introduce further reforms that address how greater efficiencies in the export supply chain will be achieved in the Australian grain industry.

What indicators could be used to assess:

- ***The effectiveness of the current wheat export marketing arrangements***
- ***Whether ongoing regulation is required?***

Indicators for assessment could include:

1. Profitability of participants over time
2. Productivity gains on farm, and in transport at port over time
3. Measure investment in infrastructure over time
4. Surveying growers and customers for satisfaction