COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

SENATE

ECONOMICS LEGISLATION COMMITTEE

Reference: Petroleum Retail Legislation Repeal Bill 2006

MONDAY, 8 MAY 2006

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SENATE

ECONOMICS LEGISLATION COMMITTEE

Monday, 8 May 2006

Members: Senator Brandis *(Chair)*, Senator Stephens *(Deputy Chair)*, Senators Chapman, Murray, Watson and Webber

Participating members: Senators Abetz, Adams, Bartlett, Boswell, Bob Brown, George Campbell, Carr, Colbeck, Conroy, Coonan, Eggleston, Chris Evans, Faulkner, Ferguson, Ferris, Fielding, Fifield, Forshaw, Hogg, Joyce, Kirk, Lightfoot, Ludwig, Lundy, Ian Macdonald, Marshall, Mason, McGauran, Milne, Murray, O'Brien, Parry, Payne, Robert Ray, Sherry, Siewert, Stott Despoja and Wong

Senators in attendance: Senator Brandis *(Chair)*, Senators Allison, Watson and Webber

Terms of reference for the inquiry:

Petroleum Retail Legislation Repeal Bill 2006.

WITNESSES

Committee met at 4.01 pm

CHAIR (Senator Brandis)—This hearing is a resumed hearing of the Senate Economics Legislation Committee to receive evidence in relation to the provisions of the Petroleum Retail Legislation Repeal Bill 2006, which the Senate referred to the committee on 30 March. The bill will repeal the Petroleum Retail Sites Marketing Act 1980, which restricts the number of retail sites that major oil companies can directly own and operate in Australia. It also repeals the Petroleum Retail Marketing Franchise Act 1980, which sets the minimum terms and conditions for franchise agreements between major oil companies and their franchisees. The committee is due to report to the Senate on 9 May.

The committee's proceedings this afternoon will begin with representatives from the Department of Industry, Tourism and Resources. The Australian Competition and Consumer Commission will then comment on evidence received by the committee at the hearing in Sydney on 19 April 2006. I expect the proceedings to be completed by 6.30 pm. These are public proceedings, although the committee may agree to a request to have evidence heard in camera or may determine that certain evidence should be heard in camera.

I remind all witnesses that, in giving evidence to the committee, they are protected by parliamentary privilege. It is unlawful for anyone to threaten or disadvantage a witness on account of evidence given to the committee and such action may be a contempt of the Senate. It is also a contempt to give false or misleading evidence to a committee of the Senate. If a witness objects to answering a question, the witness should state the ground upon which the objection is taken and the committee will determine whether it will insist on an answer having regard to the ground that is claimed. If the committee determines to insist on an answer, a witness may request that the answer be given in camera. Such a request may also be made at any other time.

Any claim that it would be contrary to the public interest to answer a question must be made by a minister and should be accompanied by a statement setting out the basis of the claim. The Senate has resolved that an officer of a department of the Commonwealth or of a state shall not be asked to give opinions on matters of policy and shall be given a reasonable opportunity to refer questions asked of the officer to superior officers or to a minister. This resolution prohibits only questions asking for opinions on matters of policy and does not preclude questions asking for explanations of policies or factual questions about when and how policies were adopted.

[4.04 pm]

PAYNE, Mr Stephen, General Manager, Minerals and Fuels Branch, Department of Industry, Tourism and Resources

SQUIRE, Mr Martin, Manager, Petroleum Refining and Retail Section, Department of Industry, Tourism and Resources

CHAIR—Welcome. Gentlemen, you were present, I know, at the prior hearing in Sydney. Do you wish to address in an opening statement any of the matters there raised?

Mr Payne—I do have a short statement.

Senator WATSON—Mr Chairman, before you ask the witness from the department to respond, many senators had a lot of problems in trying to detect which way the industry was moving and who was going to encounter the greatest degree of difficulty. So I have found a response made by Mr Cassidy of the ACCC, which came as a result of those hearings, to be very helpful. I wonder whether that response could be incorporated in the Hansard. It will probably put some of our concerns in context and may answer some of the issues that the witnesses would like responded to, because undoubtedly they have seen that letter too. That would give those reading the *Hansard* a balance and an understanding of the difficult issues and how the ACCC, in particular, intends to address some of those issues. That is my wish. I know it can be treated as a document of the committee, but I think people's remarks have to be seen in the context of a response which has come through what I regard as the body that will oversight the regulation of these laws. That is why I have made this request.

CHAIR—Senator Watson, I am advised by Mr Hallahan of our secretariat that the ACCC's document has been received as a submission. I am also advised that it is not the custom of the committee to incorporate submissions, as such, as part of the *Hansard* record. However, can I suggest this course? Let us see what Mr Cassidy has to say in his opening statement. I expect that he will say in his opening statement pretty much what he has said in his submission. If that is not the case, we perhaps could revisit the matter then.

Senator WATSON—The only problem with that is that the letter was sent not as a submission but as the ACCC's response to a number of questions that were asked by me and a number of other committee members. I think it would be a pity if, in the questioning, some of that response did not find its way into the actual *Hansard* record but rather was seen only as an addendum in the form of a submission to the committee. I just want to elevate its status.

CHAIR—I do not think that does elevate its status. In the sense that a submission is part of the evidence of the committee, I do not think it stands on any higher basis than oral testimony given at a hearing.

Senator WATSON—It did not appear to me to be written as a submission.

CHAIR—I am told that it has been received by the secretariat as a submission.

Senator WATSON—That might be the case, but I do not think the letter was written as a submission. That is why I made this unusual request.

CHAIR—Senator Watson, why don't we see how Mr Cassidy wants to handle it? I am sure that the issues raised in the document can be raised with him during the course of the hearing and perhaps more fully so, because answers can be pursued by supplementary questions. But I would like to defer that essentially procedural issue until we have the ACCC before us.

Senator WATSON—With respect, that procedure will undoubtedly prolong the hearings of the committee, if we have to ask Mr Cassidy to repeat what he has said in his letter or what you regard as his submission.

CHAIR—It may or may not. Let us just see how we go. Mr Payne, do you have some introductory remarks to make?

Mr Payne—Yes, I do. Before responding to questions, I thought it would be useful to provide some background to the reform package.

The aim of the government's downstream petroleum reform package is to remove the current restrictions on competition imposed by the Petroleum Retail Marketing Sites Act 1980 and to introduce a mandatory code of conduct, the Oilcode.

The reform package is an integrated package consisting of two elements: repeal of the sites and franchise acts and the introduction of the Oilcode—a mandatory industry code under the Trade Practices Act. The government has made it clear it will not proceed with one element without the other.

The content of the Oilcode was finalised after extensive consultations with stakeholders, industry, industry associations, consumer groups, state and territory agencies and relevant Australian government agencies. The final text was conveyed to all stakeholder associations in August 2005 and the document was lodged on the department's website.

Unlike the current regime, the Oilcode will apply to all market participants and will provide wholesale suppliers with greater flexibility in determining the most efficient arrangements for the marketing of their products. In addition, the Oilcode will revise tenure provisions and apply to a range of agreements, including commission agencies not currently covered by the Franchising Industry Code or the Petroleum Retail Marketing Franchise Act 1980. Retailers operating under these types of agreements will obtain significant additional benefits and guarantees from the Oilcode, such as tenure and access to a dispute resolution service.

The Oilcode has three primary themes: transparency, accountability and national consistency. These are to be achieved through national terminal gate pricing. A set of TGP principles will be introduced to promote increased transparency and national consistency at the wholesale level of the petroleum sector. Under the Oilcode, minimum standards and conditions for petrol reselling agreements between retailers and their suppliers will apply. In addition, provisions dealing with issues on predisclosure, variation agreed early surrender and expiry have been strengthened to provide greater certainty and protection for parties.

The dispute resolution scheme provides an alternative, low-cost, independent mechanism for settling disputes between industry participants in the downstream petroleum sector and will be based on a commitment to accessibility, independence, fairness, accountability, efficiency and effectiveness. Parties covered by the Oilcode will retain their existing rights and obligations under the Trade Practices Act and will not be subject to any additional obligations.

The current legislative regime restricts the business options of the prescribed oil companies causing inefficient business structures to be utilised and provides minimum standards for the fuel reselling agreements of some industry participants, but not others. The government considers that the current regime's nature inhibits long-term competitiveness within the industry as higher overhead costs associated with inefficient business structures are passed along the value chain.

One of the options considered in the regulation impact statement, which was available in the parliament upon the introduction of the repeal bill last month, would be to repeal existing legislation and allow the industry to be regulated solely by general competition and corporations laws. This option would provide a more effective regulatory environment that will allow all industry participants the flexibility to choose the most appropriate business structure for individual retail sites and their networks.

However, given the imbalance between the market share held by the wholesale fuel suppliers and that held by many retailers in the industry, if there are no minimum standards for the wide range of contractual arrangements, small businesses operating under franchise type and commission agency type arrangements will be vulnerable to the market power of fuel suppliers during negotiations, particularly in relation to tenure; hence, the government's commitment to introducing an oil code.

CHAIR—Mr Payne, when the question of the Oilcode was raised during the Sydney hearings, as far as the committee could then determine, the document posted on the department's website was a draft document. Just to make it perfectly clear, are you telling us that the document that we accessed on the website on 9 May was in fact the final document?

Mr Payne—That is correct. That is the final document which the government has adopted after all the stakeholder consultations.

CHAIR—What is envisaged to be the legal status of that document? Will it be a regulation made under the Trade Practices Act?

Mr Payne—That is correct. There will be regulations under the Trade Practices Act and those regulations will constitute a mandatory industry code.

CHAIR—When you say a mandatory industry code, does that mean that, were there to be a breach by a party bound by its obligations under the Oilcode, a party affected by that breach would have a private right of action in the Federal Court to enforce compliance with the code?

Mr Payne—That is correct.

CHAIR—And the ACCC can also take action to enforce compliance with the code?

Mr Payne—That is correct.

Senator STEPHENS—Mr Payne, as you did get a chance to listen to the evidence in Sydney, I wonder if you want to make some comments quite particularly on the comments by

Senator Joyce about the impact of these two pieces of legislation on the regional supply and cost of petrol.

Mr Payne—The government has indicated that it believes the introduction of the reform package could lead to lower prices in regional Australia. The effect of increased competition in the industry could work towards that end.

CHAIR—Is it based on any economic modelling?

Mr Payne—No, not economic modelling but that would be what you would expect to be a normal outcome of increased competition in an industry.

CHAIR—If there is increased competition in the industry.

Mr Payne—Yes.

Senator STEPHENS—I wish to pursue the status of the Oilcode regulations. There is in *Bills Digest* a comment that the department conducted an industry briefing on section 46 of the Trade Practices Act. The *Bills Digest* says:

> Since these fora the Department has conducted an exercise with stakeholders to facilitate the changes outlined above and correct minor ambiguities identified in the previous draft Oilcode.

So those ambiguities are not in the document that we have as they have been addressed?

Mr Squire—That is correct.

Senator STEPHENS—Can you tell us how you see the Oilcode impacting on branded independents?

Mr Squire—Certainly. For example, the fuel-reselling agreement that is part of the Oilcode applies to those people that have a fairly tight integration with their wholesale supplier. To be covered by the fuel-reselling agreement part of the Oilcode, you need to have a supply agreement and you need to have a branding agreement. But you also need to have a degree of involvement by the wholesale supplier in the day-to-day operation of your business. For example, in the industry at the moment there are what we would typically regard as being franchise agreements or commission agency type agreements. Those sorts of agreements would be covered by the fuel-reselling agreement as part of the Oilcode. Branded independents—typically those with country sites which they own and operate—would certainly have a supply agreement and would typically have a branding agreement as well. They are not covered by the fuel-reselling agreement because the wholesale supplier does not have day-to-day operation of their business. As for the impact of the Oilcode on branded independents, there is no additional regulation, for example, on those participants.

Senator STEPHENS—You also heard evidence from the representatives of the Motor Traders Association. They were very concerned about the impact that the repeal of these two bills will have on the future viability of sites and they talked about the whole issue of independent service station operators considering their service station as their superannuation and they were concerned about getting out of the business. They talked about a structural adjustment fund that they had proposed. If some service stations are to close, has the department a position on how we are going to deal with the issue of contaminated sites?

Mr Squire—The issue of contaminated sites is an issue for state governments. It has not been considered as part of the reform package.

Senator STEPHENS—And the idea of a structural adjustment package that was proposed by the Victorian association—has that got any status?

Mr Payne—The government has not considered that necessary and there is not an assumption by the government that the introduction of the reform package will lead to a major exodus from the industry of independent operators.

Senator STEPHENS—Thank you for that evidence. Senator Watson has several questions to pursue.

Senator WATSON—Firstly, are all the participants in what we are discussing subject to the Oilcode?

Mr Squire—The Oilcode will apply to all market participants. Some aspects of the Oilcode go to their form of participation in the market. For example, that applies to wholesale suppliers. Typically, currently the oil majors and in some cases independent chains are covered by the fuel-reselling agreement as part of the Oilcode. The terminal gate pricing arrangements in the Oilcode certainly apply to those wholesale suppliers. There are some people, some participants within the industry, for whom the Oilcode will not cause any real change to their current method of operation. That applies to the branded independents, for example.

Senator WATSON—What about the Coles-Woolworths types of operation which have about 40 per cent of the market? Aren't they outside of it?

Mr Squire—To the extent of our understanding of the arrangements say, for example, between Shell and Coles Myer, Coles Myer is a franchisee of Shell under the current franchise act and the sites act. To the extent that the Oilcode would apply to a participant like Coles Myer, they would be a retailer for the purposes of the fuel-reselling agreement as part of the Oilcode. In that case, the Oilcode does apply to them as a retailer. If, at a future date, different arrangements were to apply—for example, if Coles Myer were to supply fuel, supply a brand and have a deep involvement in the day-to-day operation of sites—they would be covered as a wholesale supplier.

Senator WATSON—But Coles Myer are not interested in brand; they are interested in price. Issues of brand really could be argued in court as being outside their real domain because all they want is for petrol to be sold at the cheapest possible price.

Mr Squire—The arrangement between Coles Myer and Shell, from what we observe, is that brand has a particular part to play in those operations. That is equally the case with the Caltex-Woolworths arrangement where the Caltex brand is particularly prominent in the signage displayed at those particular retail sites.

Senator WATSON—It is not on all of them, is it?

Mr Squire—In the Caltex-Woolworths arrangement typically the shop is branded Woolworths and there is some signage on both the pumps and on the price board which is generally Caltex. I cannot speak for all those sites, but that is generally the arrangement we have observed.

Senator WATSON—I notice that the government has tabled amendments to the Petroleum Retail Marketing Sites Act 1981. It is my understanding that those amendments, which commenced on 4 April, amended regulation 3, which specified which oil companies were prescribed oil companies. I have an interest in this because I the chair the Senate Standing Committee on Regulation and Ordinances and this matter is yet to come before us. That specified regulation 3. What of the oil companies that were prescribed companies for the purposes of the sites act and therefore limited in the number of sites they could operate directly? As a result of those amendments there are currently no companies specified in the regulations in the sites act and therefore they apply to no-one. Is that conclusion correct? If it applies to no-one what impact will those amendments have on the structure of the market in the event, for example, that the Senate does not repeal the sites act and the franchise act?

Mr Payne—I have an explanation of the government's introduction of that deprescription of the four oil majors. Consistent with the intent of the reform package and to prevent market uncertainty and potential breaches of the sites act while the repeal bill is under consideration by the parliament, the regulations to which you are referring suspend the oil majors reporting and compliance obligations under the sites act. The regulations will not affect commercial relations under the franchise act. Market uncertainty would be created because a number of oil major franchise agreements are coming to the end of their nine-year tenure cycle under the franchise act and the oil majors must make a decision about the future of each individual retail site. Under the current legislative framework, the oil majors may temporarily operate a retail site for a period of up to eight months while they determine the best business structure for that site. However, while the repeal bill is under consideration by the parliament, the oil majors may not be able to meet the sites act requirement of temporarily operating a site in good faith.

To explain that, under the sites act, to temporarily operate a site, the franchisor must have a good faith intention to either dispose of or franchise a site at the end of the temporary operation period. The introduction of the reform package into parliament would diminish the ability of the oil majors to meet this intent while the passage of the package was uncertain, as they may choose to alter the business structure of individual fuel retail sites should the repeal bill be passed by the parliament. This uncertainty may force the oil majors to re-enter nine-year franchise agreements, close retail sites or enter into arrangements with third parties, despite a different business structure being more appropriate. So the government considered that the oil majors would not be able to meet the good faith requirements of the current sites act while the whole reform package was being debated by parliament.

Senator WATSON—But in this intermediate situation it is possible that the oil majors could use that repeal ahead of schedule. I have a concern about it being an unusual measure to introduce a regulation of this nature when the Australian parliament is currently considering the future of the two acts. Are there any other precedents that you can mention?

Mr Payne—I am not sure about precedents.

Senator WATSON—I just find it a little bit unusual to find that situation—that you are using regulations to nullify the effect of the act. If I am correct in assuming that the omission of regulation 3 means that there are no companies specified in the regulations, it does not apply to anybody.

Mr Squire—That is correct, Senator. Since 4 April, the sites act does not apply to any prescribed companies; so there are no current quotas applicable.

Senator WATSON—But that is jumping the gun a little bit in anticipation of the legislation being passed. Changing the regulation, which has the effect of changing the act ahead of its consideration by the parliament, does seem to me, as a legislator, a little bit premature. I just ask for the precedents.

Mr Payne—I think it was more that the government believes that the deprescription to which you refer is fully in accord with its objectives for the whole reform package. There were particular reasons—with franchise agreements coming to an end before the parliament would be able to fully consider the reform package—which required the action that the government took. So some franchise agreements would have been coming to an end, and oil companies would have been in the situation of entering into that temporary operation of site arrangement. There was a feeling that they would not be able to meet the legal requirement of the sites act, to operate such sites in good faith, not knowing what the outcome of the parliament's consideration of the package was going to be.

I should point out that the deprescription of the oil majors has no impact on current or future franchise agreements. Current franchisees' agreements will continue to be covered by the franchise act, including any renewal periods, and any new franchise agreement entered into before the commencement of the Oilcode will have its tenure preserved. That is a provision of the Oilcode.

Senator WATSON—So we have to read the omission of regulation 3 in relation to the Oilcode, which has not yet passed the parliament?

Mr Payne—Yes.

Senator WATSON—I am just trying to get a nexus, but I cannot see that nexus because the parliament has not passed, as yet, the bills and, associated with that, the Oilcode itself.

Mr Payne—The minister did refer to that and explained the government's thinking in the second reading speech for the reform package.

Senator WATSON—Which was?

Mr Payne—It was, basically, as I outlined it to you, in my previous answer, but the minister clearly referred to this in that second reading speech.

CHAIR—When does the act come into effect? Is it conditional upon the Oilcode coming into effect?

Mr Payne—They will have the same date of effect.

CHAIR—Will they have the same commencement date?

Mr Payne—Yes.

CHAIR—Is that in the bill?

Mr Squire—The trigger for the commencement of the Oilcode is the repeal of the sites act.

CHAIR—Which, it is proposed, does not occur until the repeal bill commences?

Mr Squire—Correct.

Senator WATSON—The purpose of my question is to ask the department to ensure that the amendments will not disturb the tenure of existing franchise agreements—and I think you said that.

Mr Payne—That is correct.

Senator WATSON—So you can confirm that? We currently find ourselves in a market situation in Australia where we really have some of the cheapest pretax petrol prices in the world. From what I read, you say the reforms are necessary to enhance competition. Is that right?

Mr Payne—Yes. That is the government's reasoning, Senator.

Senator WATSON—And you say that the rationalisation will occur whether we have the continuation of the sites act or we have this new legislation?

Mr Squire—That is correct.

Senator WATSON—There has been a massive rationalisation, hasn't there, because not all the players have been within the scope of the existing act. Was that not the problem with the existing act—that Coles and Woolworths were outside it, joint ventures were outside it, and so on? Is that right?

Mr Squire—No, Senator—

Senator WATSON—And now you tell me this afternoon that under this new legislation they have been brought within the scope of the act and within the scope of the code—

Mr Squire—Yes, that is correct, but I think it is—

Senator WATSON—because you brand them as retail.

Mr Squire—As retailers within the code, but I think it is important to note that the difference between those two regimes is that under the current regime some market participants—namely, the oil majors—are restricted as to the number of sites that they can operate, whereas the supermarket retailers are not subject to any restriction.

Senator WATSON—That is right.

Mr Squire—The difference under an Oilcode environment is that no market participant would be restricted on the numbers of sites that they could own and operate.

Senator WATSON—Suppliers who are outside the Coles-Woolworths' arrangements, like the BPs and the Mobils, really have a difficulty if, for example, as in the case of BP, they cannot market into blended fuels. That is why they want extra capacity to buy sites under their own name so that they can sell their product. Is that right?

Mr Squire—That is correct. The evidence that was presented in Sydney by BP—and there has been some comment in the media on this issue—indicated that allowing BP to operate more sites would better enable BP, for example, to support its branded network. You also heard evidence from Mobil about the sale of their network in Tasmania to United. I guess one could suggest that is an example of the difficulty that the oil majors may have had with the current arrangements.

Senator WATSON—How will independents therefore compete against a supermarket chain like Coles or Woolworths? Previously they had an opportunity to buy from a wider range of suppliers than they have at the moment. In my own state even a Liberty price can be above a Shell price. I feel that possibly the opportunity for independents to be involved in providing discounts is now lost on the community.

Mr Squire—There was some commentary provided to a Victorian radio station during the past few weeks by Jim Lamb, who is president of the Independent Petroleum Marketers Association of Australia. In his view, he believes that independents—and I am paraphrasing his words—operated at much lower cost than some of the oil majors. For that reason, to the extent that Oilcode represents a deregulated environment, independent operators should continue to have a presence in the market with a lower cost structure.

Senator WATSON—When talking about the market, I think he was essentially referring to the narrower market rather than the whole of the market. Obviously, unless these sorts of independents can get volume in terms of the big centres, they are going to have real problems, I would say, in terms of competing against the majors in a capital city environment.

Mr Squire—Volume is certainly a critical factor in the ability of a retailer to participate in this market successfully.

CHAIR—So is the price.

Mr Squire—Certainly.

CHAIR—Is it the real driver in relation to the independents that in the recent past they have had a capacity to buy surplus output from refineries at spot prices, but that that capacity has diminished because there is simply less surplus fuel in Australia now?

Mr Squire—That is correct. One of the arrangements within Oilcode relates to purchasing at the terminal gate price. The Oilcode prevents wholesale suppliers from unreasonably refusing to supply resellers who, for example, turn up at their refinery gate with a fuel tanker and meet the appropriate health and safety standards and have capacity to pay. But in a market where there is a shortage of product, obtaining supply is a difficult and problematic issue.

CHAIR—There is an absolute right now on prospective purchasers, subject to volume and equipment issues, to purchase at the terminal gate price.

Mr Payne—Under the Oilcode there is.

Senator WATSON—If you and I were in competition, and I am an independent and I turn up with my chequebook or a bank cheque, are you saying that they could refuse to supply me with fuel?

Mr Payne—No. The Oilcode provides that they cannot unreasonably refuse to supply you with fuel. If you have a concern about that, you can take up that issue with the dispute resolution adviser.

Senator ALLISON—What is a reasonable excuse?

Mr Squire—For example, you cannot sell product that you do not have available. If you do not have product for sale, you obviously cannot sell it.

Senator WATSON—Fair enough.

Mr Squire—Likewise, if you have contracted volumes, for example. One of the issues here is that the close integration between the retailer and the wholesale supplier is very important in terms of access to product at a competitive price.

CHAIR—It seems to me, Mr Squire, that, plainly, a prospective purchaser at the terminal gate is in a stronger position now because of that provision in the Oilcode than they would have been if they had to rely on section 46 of the Trade Practices Act, because that provision does not depend upon them establishing the various thresholds that it would currently be necessary to establish under section 46 before refusal to supply constitutes a contravention of that provision.

Mr Squire—Yes, Senator.

Senator WATSON—That leads to another point. One of the submissions suggested that perhaps the legislation should be accompanied by changes to the Trade Practices Act. How do you view that notion?

Mr Payne—The government made a decision that this downstream petroleum reform package would not be the vehicle to pursue reform to the Trade Practices Act. The government has announced what it is going to do about the Trade Practices Act and is fully aware of this proceeding parallel with its response to the review.

Senator WATSON—What are the changes that are proposed to the Trade Practices Act? Will that resolve the problems of the witness who suggested that it is necessary to bring about changes to the Trade Practices Act in association with this bill or as close to the passage of this bill as possible?

Mr Payne—I would prefer if you addressed questions about the Trade Practices Act to the ACCC witnesses who will be appearing soon.

Senator WATSON—How do you see the structure of the market evolving if the Senate passes the repeal bill? Are we going to see the Coles and Woolworths percentage of the market rise above 40 per cent to 50 per cent or 60 per cent? The other question is: if we are not careful, couldn't we see the possible closure of one of the refineries in Australia? From a security point of view, I perceive that to be quite disastrous. Can you give us an assurance that there will not be a closure? Perhaps you should answer the first part. How do you see the future—say, 12 months or two years down the track—and the respective shares after the passage of this act? Is there a possibility that the passage of this bill could result in the closure of one of our refineries in Australia?

Mr Payne—It is difficult to predict how such a complex market as the petroleum market will go in the future.

Senator WATSON—I know. Try to rationalise our position in deciding whether or not to pass the bill!

Mr Payne—Are you referring to expansion of the supermarket share of the market?

Senator WATSON—Yes.

Mr Payne—The government would argue that the passage of the reform package would free up other players to more effectively compete against the supermarkets. You heard the evidence from BP and ExxonMobil at the previous hearing.

Senator WATSON—Their prices are going to be consistently higher. Admittedly, they offer more service at the moment—and that is how they are staying in business—but how are they going to compete in the long term without losing some market share?

Mr Squire—In relation to BP, for example, removing the restrictions on the number of sites that they can directly own and operate will improve their ability to compete in the marketplace.

Senator WATSON—And supply biofuels, which I am in favour of.

Mr Squire—Yes. In the case of Mobil, for example, they have already mothballed their Port Stanvac refinery, but the significant investment they have made in Altona signals a very strong commitment to remain in Australia. That being said, the sale of their retail networks in WA and in Tasmania signals that they are looking to find a market structure in which they can run a competitive network.

CHAIR—At the Sydney hearings, I think it was the Mobil witness who was most tentative about giving firm assurances about continued presence in the Australian market.

Senator WEBBER—Although it was BP who made the implied threat to close a refinery.

Mr Payne—I am not sure that we are in a position to speculate or wish to speculate.

Senator WATSON—As legislators, from a national security point of view, we do not want to be held entirely hostage to a few companies and to the Middle East. Do you believe that all these changes will lead to a situation where we will retain the current number of refineries in this country?

Mr Payne—As I said, we cannot really speculate. But if you look at Port Stanvac, which was mothballed, I would argue that the passage of the reform package would lead all oil majors to be able to compete in a way that they choose, which they cannot do at the moment. They are forced to adopt certain business structures in the retail sector.

CHAIR—I suppose, Mr Payne, you would also draw our attention to the obvious fact that all of the oil majors are eager to see this legislation passed as an indication that it would, if anything, enhance rather than detract from their willingness to remain in the market.

Mr Payne—Yes, they do all support the package.

Senator WATSON—You cannot give us an assurance. What about the respective competitive positions? You have not answered that question. Do you see the share of Coles and Woolworths lifting above 40 per cent, or do you see increased competition stabilising or even reducing?

Mr Squire—The model that we observe in the marketplace of the supermarkets would suggest that they have probably reached about the limit of their network. Coles announced, as part of their releases to the ASX, that they have close to around 600 open sites; likewise, there may be potential for some more growth in the Woolworths' arrangements with Caltex.

In terms of relative market share, if you accepted the argument that Mobil and BP lost market share as a result of the supermarket arrangements, then removing the restrictions on the number of sites that they could operate would certainly be a step in the right direction to enable BP and Mobil to better compete with those supermarket retailers.

Senator WATSON—If that happens, won't there be an additional squeeze on the independents?

Mr Squire—That is not a conclusion that I would necessarily agree with. The increased competition within the market by the removal of the sites act would have an impact on all market participants, including the Coles and Woolworths arrangements, for example.

Senator WATSON—You are suggesting that, if I am an independent and a supplier from one of the major companies and I suddenly find that my business is going to be acquired by a major, that is going to remove an independent from each decision that a major makes. It must happen. But you are suggesting that that loss will be made up by new people—maybe a United Petroleum or somebody else. Is that what you are suggesting?

Mr Payne—The oil majors who gave evidence at the previous hearing spoke of the extent to which they valued independents as part of their network. I think they made it clear that they were not out to remove such players.

Senator WATSON—That is right.

CHAIR—But surely the more competitive the majors are against each other, the more competitive they will be against the independents also—ergo, the greater threat they will be to the independents.

Mr Squire—Correct.

CHAIR—So the only set of circumstances in which the independents will be truly competitive is when they have a capacity to act as price leaders, which, as I pointed out to you before, is a consequence of their capacity opportunistically—I do not say that in a pejorative sense—to mop up fuel on the spot market at lower than routine supply prices.

Mr Squire—Or, for example, where they have a lower cost of operation. From what we observe, independent chains, particularly the larger ones—the Uniteds et cetera—do not have the same operating costs as some of the other market participants have. They do not necessarily have boards to report to or, in the case of Caltex, a Stock Exchange listing, government affairs advisers et cetera, so they can run a lean and low-cost operation. If an independent has a good site with a good retail offer and is able to access supply, there is no reason why, in a post-sites act environment, they will not be competitive. United would not be investing—and I think they are up to about 130 sites now—if they did not see a future in this market as an independent retail chain.

Senator WATSON—But only if they have huge volumes. I think that is the caveat you have to add.

Mr Squire—The higher the volume you have, the greater the capacity you have to provide discounts and lower cost fuel to consumers.

CHAIR—And also certainty of supply—

Mr Squire—Certainty of supply.

CHAIR—which the Oilcode gives them by prohibiting unreasonable refusal to supply.

Mr Squire—Correct.

Senator WATSON—With respect, I come now to what I perceive as a weakness in your argument. If joint venturers continue to secure a greater proportion of the retail market, is it likely that the ability of companies outside the Coles and Woolworths supermarket arrangement—such as your BPs and Mobiles that can operate more sites now, just as Caltex will and many other companies want to—will be significantly impacted in competing with them because of that unique advantage?

Mr Squire—It is our belief that BP and Mobil are of the view that they can compete effectively with the joint venture arrangements. For example, BP view their product quality and representation as an ability in the marketplace to differentiate themselves from the supermarket retailers.

Senator WATSON—Coming back to access of supply, if I turn up with my tanker, I can be told, for example, 'Sorry, we can't supply, because all our product is committed.'

Mr Squire—Under an Oilcode environment?

Senator WATSON—Yes.

Mr Squire—That is correct.

CHAIR—And under the status quo.

Mr Squire—Under the status quo, yes. It is impossible for a wholesale supplier to sell a tanker load of fuel twice. If they have already got contracted commitments to supply—

Senator WATSON—But aren't we entering into an environment where that is much more likely because of the limited number of supply outlets? Since we last looked at this, we have gone from nine to four.

Mr Squire—In a market where there is a shortage of product, there is a greater incentive from the point of view of a retailer to have a contractual supply arrangement with a wholesale supplier.

Senator WATSON—In a sense, if the oil companies wanted to be smart, they could just say: 'Sorry. At the moment we haven't got supply.' But what they might not tell them is, 'Come back at nine o'clock in the morning and we may have supply.' That is the problem that the independents are going to face. There is no protection.

Mr Payne—They would face that now, and under the Oilcode you would be able to go to the dispute resolution adviser and say, 'I was refused supply because' and he can investigate whether the refusal to supply was reasonable or not.

CHAIR—Under the Oilcode, can you also go directly to the court or do you have to go through the dispute resolution process first?

Mr Payne—No, you have the option. You do not have to use the dispute resolution adviser. Current rights to a court action are preserved.

CHAIR—Could an independent which considered that it was being unreasonably refused supply apply in the Federal Court for a mandatory injunction?

Mr Payne—Yes.

Mr Squire—As a supplementary answer, what the evidence is showing there is that in a market shortage you are in a potentially better position to have a secure supply contract with a wholesale supplier or an independent importer. Relying on the spot market in a market where there is a shortage of product would be a difficult method of operation.

Senator WATSON—Are there many independent importers? I thought the storage facilities were fairly limited now for independent importers.

Mr Payne—There has been a reduction in the volumes which are imported but that has largely been as a result of Australia’s tightening fuel standards, which make it more difficult to obtain that quality of fuel in the Asia-Pacific region.

Senator WATSON—The dispute resolution process under the Oilcode appears to be narrower than under the Franchising Code of Conduct. It is my understanding that the matters that can be mediated under the Oilcode dispute resolution are limited to those matters which are set out in the Oilcode and they are narrower than those matters which form part of the wider business relationship between the parties to a fuel reselling agreement. Is that correct?

Mr Squire—The dispute resolution aspects of the Oilcode apply to disputes about the refusal to supply which we have already mentioned and to disputes about fuel reselling agreements.

Senator WATSON—Can you give the committee an assurance that the Oilcode will ensure security of tenure of existing agreements?

Mr Squire—Yes.

Senator ALLISON—Can I go back to a couple of answers that you provided earlier. Was serious consideration given to limiting the number of sites in which supermarkets might be able to operate in conjunction with the oil majors?

Mr Payne—No, the government has considered that, but it has decided not to do anything about it.

Senator ALLISON—Why was that?

Mr Squire—The evidence would be that the supermarket retailers had a very significant role in providing discounted fuel to consumers. You may wish to refer this issue also to the ACCC. If I recall correctly there is some evidence in the ACCC annual report which suggested that, as a result of the supermarket retailers entering into the market, retail margins had declined and that petrol prices were, I think, about 1c per litre cheaper than what they otherwise would have been. The government did not pursue restricting the number of sites because that would have reduced competition in the market.

Senator ALLISON—And you did not take into account the study—whatever study was done at the time in thinking about this—to look at the longer term consequences of the supermarkets driving the price down to this extent?

Mr Squire—In what sense?

Senator ALLISON—In a competitive sense.

Mr Payne—The government has considered the role of the supermarkets, has given regard to what the future structure of the market will be and, taking that into account, has decided to pursue this package.

Senator ALLISON—What did you discover about the future structure of the market?

Mr Payne—I have answered that earlier, after a question from another senator.

Senator ALLISON—I must have been out of the room. So if we can just pursue that again, if you would not mind.

Mr Payne—I think Senator Watson asked me if we could predict the share of the market that the supermarkets would have, and we said no. Mr Squire gave an answer that our belief is that the supermarket share of the market has just about plateaued.

Senator ALLISON—On what basis do you regard that plateauing as being the case?

Mr Squire—I guess it is the capacity within the market to grow. There has been some speculation, for example, in the media that we will end up with a supermarket duopoly, with Coles and Woolworths operating all the sites.

Senator ALLISON—That is speculation. I am interested in what process you went through which led you to suggest that that speculation is not likely to be the outcome.

Mr Payne—The reform package frees up the oil majors to compete more effectively. They say this. They said that in their evidence at the previous hearing. You heard from Caltex, ExxonMobil and BP that this would free them up to more effectively compete against the supermarkets.

Senator ALLISON—And so it is on that basis that you have formed this view?

Mr Squire—Also on the basis that we do not believe there is a credible or sustainable argument for the conclusion that we would have a supermarket duopoly.

Senator ALLISON—At the time Oilcode was first developed, what did you anticipate would be the market share of the supermarkets? How many years ago was this?

Mr Payne—In 1996 the Oilcode was first developed.

Senator ALLISON—What was anticipated at that point?

Mr Payne—I do not know.

Mr Squire—Woolworths had just entered petrol retailing in 1996. I think it had about 16 sites around that time. The reform package is not designed around a particular market structure or a particular industry structure. It is not designed—

Senator ALLISON—So at the time this Oilcode was first envisaged you did not consider what the likelihood was of supermarket share of the market. You did not make a study of this or anticipate it.

Mr Squire—In 1996, when the Oilcode was first proposed, I do not believe anyone would have predicted that the supermarkets would have got the market share that they currently enjoy.

Senator ALLISON—So you did not anticipate that in 1996?

Mr Squire—That is correct.

Senator ALLISON—So what makes you so sure about the plateauing—apart from what the other two major oil companies have said about their ability to compete, effectively because of selling groceries? If you did not anticipate the current arrangements in 1996, why should the committee believe that, without a study of any sort that you can point us to, the scenario in a few years time will not be just what is being suggested by many of the submissions, that these supermarkets will be the only two players in the game?

Mr Squire—For the supermarket retailers to be the only participants in the market, BP would need to exit from the market, from retailing—

Senator ALLISON—That I understand.

Mr Squire—Mobil would need to exit from the market—

Senator ALLISON—Correct.

Mr Squire—all the independent chains would need to exit the market, the branded—

Senator ALLISON—I understand this. You are telling me something I already know.

CHAIR—Senator Allison, let him finish. He is entitled to answer the question in his own way. Go on, Mr Squire.

Mr Squire—The approximately 3,000 branded independents who are not supermarket retailers would need to exit the market. Essentially, to get to the supermarket duopoly you are suggesting, if there were not increased numbers of sites, 4,000 to 5,000 service stations would close down. It is not a sustainable argument.

Senator ALLISON—Why is that?

Mr Squire—I do not see any evidence that those branded independents or BP or Mobil intend to exit the market. The evidence they provided in Sydney suggests that they are very keen to compete and to remain competitive in the market. The government is of the view that the best method of ensuring that the market remains competitive is that those oil majors who are not in alliances with the supermarket retailers are free to determine the most effective and efficient method of marketing their own product.

CHAIR—Mr Squire, are BP and Mobil trading profitably in Australia at the moment?

Mr Squire—That is not a question I can answer. Unlike with Caltex, we do not have any access to that information.

Mr Payne—I think we would rather not answer beyond what you can find in public statements from those companies.

CHAIR—We have heard their evidence, and perhaps it was not an appropriate question to you. Are you aware of whether BP and Mobil are expanding their Australian operations at the moment?

Mr Squire—In the case of Mobil it is very clear that they are attempting to bring their refining and retail network back to a market structure in which they believe they can make it competitive and, presumably, profitable.

CHAIR—What about BP?

Mr Squire—From the media reports we have read, if the reform package progresses BP intend to increase the number of sites they directly own and operate from around 87 sites up to possibly 250. It appears that they believe they could operate that network profitably.

CHAIR—Do you think that, if BP were to expand from 87 sites to 250, that is an indication they are likely to withdraw from the market or an indication that they are likely to remain in it?

Mr Squire—It would be a significant investment on their part and an indication that they are committed to remaining in the market.

Senator ALLISON—The MTAA points to the UK and France as countries that have done something similar, where supermarkets have entered the market, and it points to some problems associated with that. Did you study those two countries in any depth in terms of the likely outcome in Australia?

Mr Squire—Both the United Kingdom and France have very competitive petrol pricing, and the supermarkets have been present in those markets for some time.

Senator ALLISON—What problems did you discover when you looked at those countries?

Mr Squire—I am not sure whether it would be characterised as a problem but one of the changes observed in the published material on those markets is that there was rationalisation of retail sites, by both independents and what we would consider oil major branded sites.

Senator ALLISON—By rationalisation do you mean that service stations closed down?

Mr Squire—That is correct.

Senator ALLISON—And they closed down in country areas, didn’t they?

Mr Squire—I cannot recall whether it was specifically country or city areas.

Senator ALLISON—That is what the MTAA says to us, and I do not have any further information than that. Is this an issue that you could see occurring in Australia as well?

Mr Payne—The experience in France and the UK has been that independent operators have survived, as Mr Squire was saying earlier. If they have an attractive retail offer they survive.

Senator ALLISON—Do you have any information about those two countries that you could provide to the committee?

Mr Squire—There is a report which we will make available to you.

Senator ALLISON—A report?

Mr Squire—About supermarkets and retailing in the United Kingdom and France.

Senator ALLISON—That is prepared by the department.

Mr Squire—No, it is a published report which we will find a copy of.

CHAIR—Who by?

Mr Squire—I cannot recall the authors at this stage.

CHAIR—In providing that to the committee you do so as a matter of courtesy but you do not necessarily adopt what it says or its conclusions.

Mr Payne—That is right.

CHAIR—You do not necessarily adopt its conclusions.

Mr Payne—No.

Senator ALLISON—Have you had a chance to look at the submissions and the *Hansard* from our last hearing to do with the terminal gate price, the discounting which takes place and the complaints of even the most recent submission about the apparent anomalies even over short distances in the discounts that are available to independent retailers? Do you have a comment to make about that?

Mr Payne—I think the fundamental issue was the question of whether there should be large volume discounts or whether there should be a pristine terminal gate price.

Senator ALLISON—Correct.

Mr Payne—The government has given specific consideration to this issue in extensive consultations with stakeholders and has decided that it would be anticompetitive to fix the terminal gate price and to go away from what is a very normal arrangement in retailing—

Senator ALLISON—I do not think fixing the terminal gate price was what anybody had in mind.

Mr Payne—Sorry, not fixing it; having the same terminal gate price for all—

Senator ALLISON—Nor that.

CHAIR—I think, Senator Allison, you will have to frame your question in a way that you convey to the witness what you are saying.

Senator ALLISON—I think the points which were made—I did ask for a general response, which is why I couched it in those terms—and the general tenor of the submissions was that there should be greater transparency, that it should be understood how a discounting arrangement would have been derived and be clear to all of those who are purchasing from the same supplier what that might be.

Mr Squire—At the hearings in Sydney you heard evidence from a retailer who believed that they should be able to purchase product at the same terminal gate price as a retailer purchasing a billion litres a year. Is that what you mean by transparency?

Senator ALLISON—No. That was one of the points that was made—and I am not suggesting we necessarily agree or disagree with that but that there should be greater transparency. It should be possible to know, for instance.

Mr Payne—The Oilcode provides that if you buy petrol the wholesaler has to make very clear to you how the price was arrived at which you are paying so that would identify the terminal gate price and then add the other factors which have led to the total amount that you are paying as the retailer buying that petrol. That is a specific requirement of the code. Is that the kind of transparency you are—

Senator ALLISON—But that information is not available to anyone else.

Mr Payne—No, but terminal gate prices are posted and under the Oilcode they will be—

Senator ALLISON—But levels of discount are not nor are their reasons for discounting.

Mr Payne—Not made public, no.

CHAIR—Mr Payne, are you aware of any sector of Australian commerce in which it is a requirement of law that the price at which a private company sells to another private company under a contract should be a matter of public record?

Mr Payne—No, I do not think there is any such requirement in any other industry.

CHAIR—Perhaps there might have been in the former Soviet Union but of course they did not have private companies.

Senator WEBBER—Pursuing that issue for a moment, when we got some evidence in Sydney even the majors seemed to interpret terminal gate price as different things. You are saying under the Oilcode that there will be a consistent approach to terminal gate pricing and that therefore, subject to other contracts, independents will be guaranteed supply at that. Yet if we are still going to allow—and I am not saying we should not—discounting for large volumes, we are not guaranteeing them supply, are we?

Mr Payne—We are guaranteeing that they can buy the product at the terminal gate price, so they may not get—

Senator WEBBER—But if most of the product is sold below the terminal gate price, then guaranteeing that you can buy it at a price that it is not sold for does not really help.

Mr Payne—It does guarantee that if you turn up with your truck at the terminal gate, you can get that truck filled and not be unreasonably refused supply, and you can get it at a published price, which you know about before you drive the truck up.

Senator WEBBER—BP Australia gave us a different definition of how they operate a terminal gate price that was rather ornate, and which, as a novice to this industry, made me more confused rather than less.

Mr Squire—The TGP arrangements in the Oilcode do not specify a particular model or method of determining terminal—

Senator WEBBER—So how do we have a nationally consistent approach, then?

Mr Squire—To the extent that the wholesale suppliers are required to post a terminal gate price.

Senator WEBBER—So it is just nationally consistent that you have to tell people what it is.

Mr Squire—And importantly, as Mr Payne has reminded me, it is a temperature corrected terminal gate price.

Mr Payne—Which is something stakeholders were keen to have.

Senator WEBBER—Yes, I understand that. Before I embark on my next question, I will preface it by saying that since we had our hearings in Sydney, we have been provided with a brief from the minister's office. This has made things a lot clearer to me. Sydney would have been a bit easier if I had read this beforehand. With the compulsory Oilcode and the fact that independents are guaranteed to be able to buy at a certain price if supply is available, and you have said they have access to a dispute resolution process if they think supply is being withheld for some other reason, are they the two issues in the Oilcode that are advantageous to independents, or is there something else there that I have not picked up?

Mr Squire—No, that is correct.

Senator WEBBER—So we do not guarantee supply, we guarantee it at a price if it is available.

Mr Squire—That is correct.

Senator WEBBER—And if they can prove it is being withheld for other reasons, they can spend money on going to the Federal Court or embark on a dispute resolution procedure.

Mr Squire—Yes.

Senator WEBBER—In this briefing note that we received it says that as part of the Oilcode:

The new regime will be reviewed after 12 months to ensure it is operating satisfactorily.

What is the process for that? Do those new regulations or does that report come back to the parliament, or is that something that is going to happen purely internally, so none of us will know anything about it? So once we pass this bill, we do not get involved in this process again.

Mr Squire—The Oilcode is regulations under the Trade Practices Act. If there were amendments made as a result of that review, then they would be subject to potential disallowances regulations—

Senator WEBBER—So they would be disallowable instruments if you felt the need to change them accordingly. I want to ask you about one last issue, because others have picked up on most of the points I want to make. We have already talked about the retraction in the number of retail sites from 20,000 in 1970 to 6,500 now. This briefing note also talks about how:

… rationalisation will eventually plateau as retailers compete on an even playing field facilitated by the Oilcode and the number of retail sites reaches an optimal level.

When do we think that is going to happen, and what is it going to be? Because if we can say it is going to plateau, we must know something.

Mr Payne—The government has not attempted to predict an answer to those kinds of questions you are raising.

Senator WEBBER—Right, so we do not know—

Mr Payne—You are asking whether the government has said what the ultimate number of service stations in Australia will be, and the answer is no, it has not attempted to do that.

Senator WEBBER—I just thought going from 20,000 in 1970 to 6,500 now, we must have some idea about the relationship between the—

Mr Squire—I cannot speculate on what that optimum number would be. But, for example, assume that the fixed costs in the industry are the same—the rent of a site, the cost of operating your pumps, your wages and so on. If you have two service stations each selling 400,000 litres a month and if you have one service station selling 800,000 litres a month, it follows that the costs in that second scenario would be lower than the costs spread across the two service stations—the most efficient market outcome.

Senator WEBBER—So we do not really know what is going to happen then?

Mr Payne—You are asking for specifics which the government has not attempted—

Senator WEBBER—I guess what I am trying to say is that you cannot really say it is going to plateau. We cannot really say anything. I am not necessarily saying these are reasons for not doing it, although I have noticed since our hearings in Sydney that the four majors are very keen on this. BP is threatening to withhold the supply of Opal if this does not go through, which I find an interesting approach to having happy relations with the Senate—but there you go. But we do not really know what is going to happen.

Mr Payne—Not if you want to quantify outcomes.

[5.22 pm]

CASSIDY, Mr Brian David, Chief Executive Officer, Australian Competition and Consumer Commission

CHMIELEWSKI, Mr Konrad, National Manager, Industry Codes, Australian Competition and Consumer Commission

DOBINSON, Mr Gary Martin, Director, Petrol Monitoring Section, Australian Competition and Consumer Commission

RIDGEWAY, Mr Nigel Cameron, General Manager, Compliance Strategies Branch, Australian Competition and Consumer Commission

CHAIR—Welcome. The committee has your written submission for which we thank you. I invite you like to make an opening statement.

Mr Cassidy—Given that we have given you a written submission with some comments on issues which I think were raised in your last hearing, I was not proposing to make an opening statement. I thought I would leave it to the committee to ask any questions.

CHAIR—For the record, I will ask you in the broadest possible terms: what is the commission's attitude to this legislation—and by that I mean the legislation and the Oilcode as a package deal?

Mr Cassidy—In relation to legislation, the commission indicated as far back as a report we did in 1996 that we did not see much benefit in the legislation. It did not seem to be achieving its stated objectives.

CHAIR—Those are the two existing legislation acts and not the bill before us.

Mr Cassidy—That is right, the franchising act and the sites act. They did not seem to be achieving their stated objectives and were probably imposing some efficiency costs, at least, on the industry. As I said, that is the position the commission has held for some time. In terms of the Oilcode itself, we can see some attractions in that in terms of greater transparency. Also we think that the dispute resolution process within the Oilcode could serve some useful purpose. It has a fairly similar dispute resolution mechanism as in the franchising code. We would not want to go overboard about it. There is obviously some fairly significant structural change occurring within the petrol retail industry—and has been for some time. We would not hold out that this package is somehow going to bring that to an end or necessarily make life that much easier, particularly for small retail petrol outlets. They probably have some more fundamental issues confronting them than the issues that this package seeks to address. But, that said, in broad terms we think it is a worthwhile reform within the petroleum retail industry.

CHAIR—You do not consider the package to be anticompetitive?

Mr Cassidy—No, we certainly would not consider it anticompetitive.

CHAIR—If anything, it will promote competition?

Mr Cassidy—Yes. As I say, you would not want to overstate that—

CHAIR—No.

Mr Cassidy—but nonetheless I think the greater transparency and the mechanism for people to have disputes resolved would add to the competitive structure of the industry.

CHAIR—And I suppose the rights that will be available for independents under the Oilcode in obtaining supply from the refiners would be more easily exercisable through the dispute resolution process or, if it came to that, through litigation, than through their having to rely, as they do at the moment, on the highly generic and more complex rights under section 46.

Mr Cassidy—Yes, I think that is right, certainly as a general proposition. I must say that we have not seen access to refinery supply as being a significant issue. Certainly it is not one that we have had a large number of complaints about in recent years. But, nonetheless, there probably are some pluses in having, if you like, that right of access more clearly spelt out, in terms of both its existence and also its terms and conditions.

Senator STEPHENS—Mr Cassidy, thanks for this submission. It has helped to clarify some of the issues that we examined in the first public hearing. I want to pursue this issue of the Oilcode. First of all, you outline here the role of the dispute resolutions adviser under the Oilcode. Just looking at this now, I understand that the DRA can refer a price related matter to the ACCC to investigate, but obviously the ACCC is not required to investigate it—is that the case? Would it be more likely for the ACCC to investigate it if it came through the DRA?

Mr Cassidy—As a general proposition, I think yes. The DRA, as we understand it—as with what is called the OMA under the Franchising Code of Conduct—will have disputes to look at, some of which will perhaps potentially involve a breach of the code and some of which will not. The DRA is not limited to disputes that look as if they are purely an actual breach of the code. Where, in the DRA's view, they do involve a breach of the code or potential breach of the code and they are referred to us, they are certainly something we would have a look at—and, I think, feel obliged to have a look at, given where they have come from. So they might receive a higher and more immediate level of attention from us than perhaps disputes or issues that were just coming to us separately, some of which would probably not require much consideration before we got to a point of view that they did not involve a breach of code—even if there was a genuine dispute at issue. So, yes, I think that as a general proposition that would be the case, although clearly, as with anything that is referred to us, having started to investigate it, if we decided that there most likely was not a breach of the code involved then we would not continue to investigate it simply because it had come from the DRA. We would call it on its merits, as we do with other issues.

Senator STEPHENS—So how has the ACCC been involved in the drafting of the Oilcode?

Mr Cassidy—We were involved in the ongoing consultation process in relation to the code. Indeed, we had some involvement with the department in the drafting of the code before it got to the consultation process. It is obviously not appropriate for me to go into the detail of what was said, or what was agreed or what was not agreed, but we certainly would not have any complaint that we were not adequately consulted during the course of its preparation.

Senator STEPHENS—So you have been involved in the drafting. You obviously have had a good chance to look at the submissions. What do you think about the small business operators' concerns—which they have expressed to the committee both in their oral evidence and in their submissions—about the repeal of the franchise and sites acts?

Mr Cassidy—My colleagues have spent more time looking at the submissions than I have. I go back to my earlier comment. Perhaps there are some—and I can well understand this—who are looking to this sort of package to alleviate the sort of structural change which is occurring within the industry, and which we think has become fairly competitive in recent times. The source of competition has changed a bit. Nonetheless, it is fairly competitive. The economics of petrol retailing have moved against the small retail operator. Some of the comments I have seen are of the nature of looking for a package which will reverse or halt some of that sort of structural change process—certainly not this package. I don't know whether there is any package that could really hold out against the underlying economics of all that. My colleagues may have more specific comment they want to offer.

CHAIR—Before you go to more specific comments, just staying with you, Mr Cassidy, at a general level, when you talk about the change in the structure of the dynamics of petrol retailing, is it by and large true that, whereas perhaps 10 years ago—at least in some Australian markets—the independents were the price leaders, that has ceased to be the case?

Mr Cassidy—I think that is right. It depends on what you call an independent. Let me, for the purposes of answering, put aside Coles and Woolworths—

CHAIR—The junior players.

Mr Cassidy—The true independents, for a variety of reasons, cease to be the, if you like, source of competitive pressure within the industry.

CHAIR—I remember the Trade Practices Commission wrote a report some years ago which made the point very strongly that the independents were the price leaders. That is no longer the position.

Mr Cassidy—Certainly not to the extent they were. In more recent times, a couple of years ago, you probably recall that there was some coming and going and a discussion about the new environmental standards for petrol in Australia. That was a fairly complex decision which involved weighing up a number of competing considerations. But one of those considerations was that the standard proposed and subsequently adopted really isn't the standard that exists exactly as is in Australia or just about anywhere else. So it means that the ability of the independents to pick up particularly cheap spot supplies of crude oil refined product and bring them in and then use that as a source of competitive pressure in the Australian market has been somewhat reduced. In line with that, their role has declined in recent years and tended to be supplanted to some extent by Coles and Woolworths and the larger independent chains, relying fairly heavily on bulk discounts that they obtain from the refiners in Australia. That has been the source of competitive pressure in the domestic market.

CHAIR—Thank you, Mr Cassidy. You were going to invite your officers to address more specific—

Mr Cassidy—Yes. I invite my colleagues to say anything further about the submission.

Mr Dobinson—Picking up on what Mr Cassidy said, when we examined the shopper dockets issue in 2004 we made a broad distinction in terms of the role of independents in the market. We looked at the impact of the independent chains, such as Gull, Liberty and Matilda. They are able to obtain fuel at a discount, they have economies of scale, and their size enables them to push costs across each operation. We compared them with the smaller independents, which have less capacity to access fuel at a discount and they often have smaller sites which are not as well located as some of the other chains. We identified those smaller players as being particularly vulnerable to the whole rationalisation process which, as Mr Cassidy has pointed out, was related to issues such as the capacity to source excess fuel from refineries or even independent imports, because of the fuel standards.

CHAIR—Would it be right to say, as a generalisation, that the smaller independents are more reliant on their capacity to purchase spot supplies at the terminal gate rather than taking supply through long-term bulk contracts?

Mr Dobinson—I am not sure that you could quite generalise it that way. There are certainly some smaller independents who will buy at spot sales. But clearly, if you have a tighter fuel supply situation, having a contract is beneficial, because you want to make sure you maintain your supply. But certainly in the past it was the case that some of those smaller independents were able to do that.

CHAIR—Whereas what we call the independent chains tended to have supply contracts.

Mr Dobinson—They would tend to have significant volume contracts—or, in fact, their own importing facilities.

Mr Ridgway—I have nothing to add, unless there are some specific concerns.

Senator STEPHENS—Moving back to the whole dispute resolution process, under the Oilcode, do franchisees have access to a binding dispute resolution process or just processes such as mediation?

Mr Ridgway—Perhaps I could attempt a response. In our understanding, there are basically two forms of dispute resolution under the proposed Oilcode, one dealing with those circumstances of perceived failure of supply and another that deals more broadly with disputes between franchisees and franchisors but also with terminal gate pricing. In the first, there is a process which enables a non-binding determination to be made. In the latter, there is a mediation regime which may or may not include a non-binding determination at the end of that process. So broadly, there is a mediation regime but also opportunities for non-binding determinations.

Senator STEPHENS—I am sure Senator Watson is going to have some questions about that.

CHAIR—Have you finished with your questions, Senator Stephens?

Senator STEPHENS—I have some other questions, but if we want to talk about the Oilcode itself, that would be helpful.

CHAIR—Okay, we will come back to you then.

Senator WATSON—I have a range of questions, not necessarily on the Oilcode.

CHAIR—Perhaps we should keep going with Senator Stephens for the moment, Senator Watson, so that she can finish all of her questions, and then you can adjust yours accordingly.

Senator STEPHENS—Thank you, Chair. In your submission you also suggest to us that there is an issue around the terminal gate price and there is provision for a terminal gate pricing regime. Can you tell us who is going to be monitoring that regime and ensuring that there is fair access to supply for independents.

Mr Ridgway—My understanding is that there will be a process as we move forward towards fleshing out some of the detail of the operation of the code, should it proceed. In that case, insofar as the ACCC has a role in enforcing the requirements of the code, we will have processes in place to ensure that those requirements are observed and complied with. We do this with various parts of our act, working with those upon whom the obligations are imposed to ensure those mechanisms are in place.

Senator STEPHENS—If I can be so bold, what level officer is the DRA going to be?

Mr Cassidy—Well—

CHAIR—Obviously, a very experienced one.

Senator STEPHENS—Are you trying to say something about the industry!

Mr Cassidy—We are not involved in appointing the DRA. I think that is really something for the minister and his department. It is an appointment by the minister, as I understand it.

CHAIR—Do you have to be a lawyer?

Mr Cassidy—I am not aware that there is anything in the Oilcode that says it has to be a lawyer, be that good or bad.

Senator STEPHENS—Do they have to be familiar with the Trade Practices Act?

Mr Ridgway—My apologies. I understand there is a tender process which is being pursued by the department of industry that includes seeking a dispute resolution adviser. I am not sure that there is a particular level envisaged.

Senator WEBBER—Or profession!

Senator STEPHENS—In your submission you also advise that the ACCC can take action under section 46 of the Trade Practices Act if required or if it believed that there was a case. But in our previous discussions on a range of issues we talked about the threshold for bringing successful cases under section 46. Have you lodged any new section 46 proceedings since our last discussion, whatever that was about? It was probably estimates.

Mr Cassidy—No, we have not. That question has been framed to me in different contexts—I think, before this committee in different incarnations. I have basically said that we have not instituted any new section 46 court proceedings since the Boral High Court decision. I have also said that we do have a number of matters under detailed investigation, because section 46 is an important part of the act and therefore in a sense we cannot afford to ignore it. I would say that, to the extent that there are shortcomings in the current section 46—and that is obviously well-travelled ground—we think the answer to that is to amend the section. We are fairly wary of proposals which would result in what I call a Balkanisation of the competition provisions of the Trade Practices Act, where you perhaps end up with a section 46 type provision for the oil industry and another section 46 type provision for some other sector. If you go back to the Hilmer report and the competition policy reforms that started in the mid-nineties, one of the key recommendations there was that we ought to have uniform competition law of uniform application. We have basically achieved that in the intervening period and I think that, for a whole host of reasons, it would be a great pity if we started to move away from that now—if, for example, we had tailored section 46 provisions developing for different sectors or, for that matter, targeted price-fixing provisions or whatever the particular provision might be.

Senator STEPHENS—Are you confident that the ACCC can rely on section 46 to ensure an adequate supply of fuel products to independents under this new regime?

CHAIR—You won't need to, will you? You will have the Oilcode provisions.

Mr Cassidy—Let me try and explain something else, which is perhaps not properly understood. Section 46 is in a sense about so-called horizontal conduct—a firm with market power seeking to damage and eliminate one or more of its competitors. The Oilcode, the franchising code and indeed part IVA and part IVB of the act, which are about unconscionable conduct in the industry code divisions, are really about what we would call vertical conduct—that is to say, how a supplier treats those they are supplying to or how someone purchasing treats their supplier. Inevitably in those arrangements the supplier or the buyer is, if you like, the more dominant party and then you have got the individual firm in the middle who perhaps has the lesser economic power. Really what this is about is, as I say, that sort of vertical relationship rather than what we would see as being the more horizontal competitor type relationship that section 46 seeks to address.

CHAIR—Do you think that the provision in the Oilcode which prohibits unreasonable refusal to supply is sufficient to deal with constructive refusal to supply? In other words, is it to be read as prohibiting refusal to supply other than on reasonable terms?

Mr Cassidy—As you have probably gathered from my pausing, it is something I have not thought closely about. I think that is probably right, in which case, in a sense, you could say there is an overlap between that part of the Oilcode and section 46. Again I come back to my point that I think the Oilcode is basically about the relationship between the oil majors and those they are supplying, which is not really what section 46 is about. If a petrol retailer came to us—as they have done, I might say—and alleged section 46 behaviour because their contracted supplier was not supplying them for some reason, then that simply is not a 46 issue, because they are not competitors in any sense.

Senator STEPHENS—We had some evidence in Sydney about the alleged practice of below-cost pricing of fuel products and how that operates in the industry. That was described by various of the players in different ways. Is that something the ACCC are aware of?

Mr Cassidy—Yes. It is something we have put a fair few resources into, although I would have to say there are various parts of the retail petroleum industry who probably feel fairly disappointed with us over the outcome. But we have had a number of complaints about predatory pricing and below-cost selling. I suppose there are a couple of issues there. One is that the cost is often identified as either the posted terminal gate price of the relevant refinery or the cost at which the complainant is able to purchase fuel. Neither of those is necessarily the cost for the entity that is actually selling the fuel at a low price. I think that is the first point to make when you are thinking about alleged predatory pricing.

CHAIR—So your point is that the relevant baseline to determine whether a price is a predatory price is the cost to the break-even point to the supplier of selling, not the posted terminal gate price?

Mr Cassidy—You can characterise it in a couple of different ways. That would be one. Another would be whether the price that the petrol is being sold at is abnormally low compared to the industry norm. What seems to be an automatic assumption—that the posted terminal gate price is the relevant benchmark—is quite often simply not right, not the case.

CHAIR—That would seldom be the relevant benchmark because, presumably, the terminal gate price is the price at which the supplier announces it is prepared to sell to get a profit.

Mr Cassidy—I would not necessarily argue with you on that; I am just saying that that is an assumption which is often made. A second issue is that, in order to establish predatory behaviour, the second leg required is that there is predation—that there is intent to do harm. In a number of cases we have investigated, we have found that one service station will be selling petrol at a price which is below even the price at which another service station nearby can purchase that petrol, but the first petrol station is selling it at price because they are responding to someone else in the regional market who, for some reason or other—they have received a larger discount on a recent load of fuel or perhaps have been able to pick up a load of imported fuel—is able to sell it at price. But there is no element of predation in that. There may be the very unfortunate consequence, of course, that one or two of the retail petroleum outlets find it very hard to compete in that sort of situation, but that does not constitute predation or intent to do harm to those who are finding it hard to compete.

Incidentally, I should explain that, when we investigate, if it looks as if we have got what might be a genuine issue of predation, we do put a fair few resources into it. We identify the relevant region and then we monitor petrol price movements in that region, obviously on a confidential basis, over a period of time so we can track just who is responding to who and whether there does seem to be predatory behaviour going on. That is fairly resource intensive; nonetheless, that is the way we do it. Having done a number of those—despite some industry claims that we do not do anything—we have not yet found an issue of predation.

CHAIR—I thought the industry claimed you did too much, Mr Cassidy.

Mr Cassidy—It depends who in the industry you talk to. But we have found a number of instances where, sure, this service station is selling at a relatively low price compared to this one, but the reason they are selling it at a low price is that another service station up the road—perhaps the same brand, perhaps another brand—has dropped their price for whatever reason, and they are responding to that drop in price.

Senator WATSON—They will go out of business pretty quickly if they do that.

Mr Cassidy—It depends: they might be using, as I say, a bulk discount they are able to draw on; sometimes—and I am afraid this goes to the economics of modern petrol retailing—the large integrated sites sell not only petrol but also fast food and groceries, on which they make quite nice margins, and they will apply those margins, when needed, to remain competitive on the petrol side of things.

Senator ALLISON—We have heard and read evidence that, in fact, discounting can take into account other local discounts. In other words, petroleum companies do factor in the neighbouring retailer who has got a lower price, and so on. Is that not the case?

Mr Cassidy—True. But if you get the situation where one service station drops its price and then the other responds, it is very hard to get out of that a provable case that the second one is seeking to predate in terms of the first one as opposed to responding to a competitive pressure in the market. That is the point I am making.

Senator WATSON—Would you see the Coles and Woolworths share of the market increasing significantly? My understanding is that they currently have approximately 40 and this number has been growing quite rapidly.

Mr Cassidy—That takes us to the area of prediction, which makes it a little hard. Both Coles and Woolworths have indicated target levels of service stations they wish to acquire which between them come to about 1,100, from memory.

Senator WATSON—But they might be putting in three times as many pumps.

Mr Cassidy—They might. The point I was going to make is that we have gone through a period where they have been building to that 1,100, which they now more or less have. Unless they decide to exceed that number, further growth would require them to, as you say, be putting in more pumps. Typically, I think the process they have been going through is that they acquire what might be small sites, but then they do actually increase the number of pumps on that site. I think we have been through what has obviously been a fairly rapid period of growth for both Coles and Woolworths sites. Unless they change their plans in terms of the number of sites they wish to have, I would expect that that would probably level out to some extent. Whether it is going to level out completely or whether there is going to continue to be growth but at a slower rate I think is a fairly difficult issue to answer.

Senator WATSON—In terms of the small independents limited access to a range of supply as compared with previously, can you see the small independents going broke if they are trying to compete with the Coles-Woolworths price, unless they can offer something additional like extra services or something? If they just compete on price, I can see them going broke.

Mr Cassidy—Unfortunately, I think there is an element of truth in what you say. I would not characterise it just as being Coles-Woolworths because there is now quite a number of these arrangements around: Metcash, Foodland and Dimmeys. There are quite a number of arrangements where, if you like, people can basically acquire discounted petrol as a result of the other purchases they have made in one form or another. I think those sorts of arrangements obviously do make it difficult for small independents and also for, in a similar vein, what I refer to as the integrated service station operations, which not only have petrol but have fast food, groceries and whatever else. Similarly, they also make it a difficult and competitive environment for the small petrol retailer who is predominantly just relying on the margin he gets on the sale of petrol. On the other hand, the economics of the retail part of the petroleum industry operate on very fine margins. It is a very competitive industry.

Senator WATSON—You say it is very competitive in the short term and I would agree with you. But are we really looking to the longer term implications for Australia? If the Coles-Woolworths share continues to grow, will that lead them to a position where they would be able to edge the price up, maybe not significantly, to take advantage of their near-monopoly position? We see that in groceries now. You have price leaders and some items are sold at a very fine margin.

Mr Cassidy—In relation to petrol that is something we have given some thought to and addressed in the report on the shopper docket arrangements that Mr Dobinson referred to. It is something that we continue to monitor. I suppose we were influenced a bit by the overseas experience where these sorts of arrangements have existed. In the UK I think it has existed for 10 years now.

Senator WATSON—They have shorter distances.

Mr Cassidy—You are quite right. But, equally, the shopper docket arrangements in the UK have not completely squeezed out by any means the petrol retailers not involved in the provision of shopper dockets. Whether over time what you might call the stand-alone petrol retail outlets will be squeezed out by the integrated outlets is a much broader issue. Again, this goes to the economics of petrol retailing and perhaps a structural change that has been going on in that sector for at least the last 20 years.

Senator WATSON—In trying to get the cheapest possible price for Australian motorists we have the short-term solution. But in the longer term wouldn't it be a tragedy if, for example, we lost further refining capacity in Australia? That would virtually play into the hands of Coles and Woolworths vis-a-vis the rest of the industry, because the sources of supply would become more and more limited. For example, if Mobil is moving back a bit in its refining capacity and if BP does the same thing or we lose a major refinery, that would be of concern. Obviously price is one thing but national security is another. I would think it rather horrific if we were to lose refining capacity in this country simply because we are fighting a short-term situation to give Australian motorists the lowest possible price, which is essentially flowing through a Coles or Woolworths type of operation.

Mr Cassidy—In the long term I think the pressure on Australian refineries is not going to come from the retail end of the market and whatever Coles and Woolworths are doing. I think the basic problem Australian refineries have is their lack of scale. There are refineries in Asia which have a capacity that exceeds the total refinery capacity of all the Australian refineries put together. That is the economics of petroleum refining. I am afraid that we have a structure in our petroleum refining industry which I think goes all the way back to the days of state purchasing preference, when there was an encouragement by all the states to all sorts of industries to set up in particular states and receive various tax concessions. That has led us to have a petroleum refinery in virtually every state—or, it used to be. It is by no means clear, and in fact there are arguments quite the other way, that that is an economical way for the industry to operate in Australia. So I think the real pressure on our refiners is not and will not come from what is happening at the retail end. The real pressure will be if the rest of the world, particularly Asia, moves to a position of being able to more readily supply petrol which reaches our environmental standards. The real pressure on our refining industry will come from the fact that their economies of scale are not anything like the economies of scale of refineries located nearby in Asia.

Senator WATSON—That is not altogether very comforting.

Mr Cassidy—I am sorry. I was not meaning to be comforting. I was trying to be realistic.

Senator WATSON—And give the stark reality.

Mr Cassidy—I was trying to be realistic and honest.

CHAIR—It is called the ‘dismal science’, Senator Watson.

Mr Cassidy—I think there is a real structural problem in our petroleum refining industry.

Senator WATSON—Coming back to the concept of structure: how do you see the structure of the market evolving on the passage of this bill in the longer term?

Mr Cassidy—To be honest, in the longer term I do not think this bill will have an enormous impact on the structure of the retail petroleum industry because I think it is being basically driven by other considerations. As I said at the outset, while we think that the package is a worthwhile one, I would not want to say to you that it will have a dramatic impact on the level of competition in the retail petroleum market. We think it will have some impact, but other forces apply in retail petroleum which are greater than this package, I would think.

Senator WATSON—The nature of the competition will change. Some independents will go out as the oil companies get additional sites, but you are saying that at the same time there will be newer players, called independents, who will come in and either take that up or increase that share of the market. It is that right? Is that your reasoning?

Mr Cassidy—No. I think the question starts from a proposition that the sites act has had an impact in restricting the acquisition of sites by the oil majors. I do not know that we would necessarily support that proposition. We think that the use of multifranchising arrangements has probably largely stepped around the sites act anyway. What I was getting to is that I think there is a fundamental driving force in petroleum retailing which means that the future is going to be with larger, integrated sites rather than with the smaller, stand-alone traditional petrol retailer. There will be areas where the traditional petrol retailer will continue to survive, perhaps where the competitive pressures are not as great. They would be, I expect, particularly in country and rural areas, but once you get to areas where there is high-volume demand then, as I say, I think the future of petrol retailing is with large integrated sites which are really more about retailing, of which petrol is just one commodity, rather than a dedicated retail petrol site as we have known it.

Senator WATSON—So the implication of that is that people will travel 20 kilometres to the nearest volume supplier of fuel—from one country town to another. Is that right?

Mr Cassidy—Not necessarily. I think country towns are the area where you may well have what I call the traditional petrol retailer perhaps being able to survive, although that very much depends on how close one of these large-volume sites is to a nearby highway. I probably do not need to tell anyone that consumers are enormously price sensitive when it comes to petrol, and the notion that someone would drive a sufficient distance and consume any amount they save to buy their petrol at a lower price is not one that would be necessarily all that unusual when you are talking about petrol.

Senator WATSON—I understand the Oilcode does not apply in a number of situations. One of those situations is where the investment is under $20,000. How many stations fall under that exemption?

Mr Ridgway—We might have to take that on notice.

Mr Cassidy—My gut feeling would be 'not many', simply because, when you talk in terms of thresholds relating to aggregate turnover, sales volume and so forth, petroleum retailing tends to be one of those sectors where you tend to talk about having larger figures rather than lower.

Senator WATSON—That was my initial reaction, but I have been informed by sections of the industry that there are many more than I would certainly have anticipated.

Mr Cassidy—I am a bit like you, Senator. It would surprise me if that were the case, but none of us can really give you a hard answer on that.

Senator WATSON—How was that $20,000 threshold established?

Mr Cassidy—I am looking to my colleagues, but I do not know whether we can answer that. It may be something for the department to answer. Our main role in this was in relation to the Oilcode—

Senator WATSON—But you would be interested in ensuring that the maximum number would be under the Oilcode to ensure uniformity, wouldn't you?

Mr Cassidy—I would think so, but—

Senator WATSON—If there is going to be a significant number outside the Oilcode, I think we need to know as part of the —

Mr Cassidy—I take your point. I am just explaining that our main role in relation to the Oilcode was the interface with us and the Trade Practices Act, so some of what I might call the stand-alone type issues were issues that were more the domain of the department and the minister rather than being based on advice from us.

Senator WATSON—Right. I am a little bit worried. BP are essentially working on biofuels and, according to their submission, they want more sites to be able to market those blended products. I see that as a real positive in terms of bringing down the price and making us less dependent on an imported product. If the joint venturers continue to secure a greater proportion of the retail market, is the ability of BP and Mobil, for example, to directly operate more sites likely to have a significant impact on the ability of those companies to compete with the joint venturers?

Mr Cassidy—My immediate reaction would be that, to me, that all smacks of more competitive pressure, and probably more benefit in terms of the margins and the prices within the retail petroleum industry. At the moment, as I said, Coles and Woolworths have between them about 1,100 sites—that is out of about 6,500 or 7,000 sites currently operating, so if—

Senator WATSON—It is a huge volume.

Mr Cassidy—That is true. But just looking in terms of sites, if what I call the two non Coles-Woolworths refiners—basically BP and Mobil—were seeking to expand the number of sites they have, it seems to me that there is reasonable scope for them to do so. If they are expanding to sell a more competitively priced product then that should—

Senator WATSON—This package will help them, won't it?

Mr Cassidy—help them to secure the associated volume.

Senator WATSON—I am a little worried that the matters that can be mediated under the Oilcode are narrower than under the Franchising Code of Conduct. Why have you agreed that the dispute resolution arrangements are narrower than under the franchising code?

Mr Cassidy—I will ask Mr Ridgway to answer, but let me just make one clarification. We have not agreed; we just had an input into the overall process. We offered advice, and the department and the minister took that advice to the extent that they wished to. Do not get me wrong and say that here is an Oilcode that we do not necessarily agree with. However, do not take it either that we necessarily agree with everything in it. Having made that clarification, it probably does not do anything to actually answer your question.

Senator WATSON—I cannot really ask any more questions, can I!

Mr Cassidy—I will hand over to Mr Ridgway to answer the substance of your question.

Mr Ridgway—Broadly, my understanding is that the Oilcode provides for dispute resolution with respect to those matters that apply to, for example, agreements between franchisees and franchisors and the various matters that are associated with those agreements. That is broadly the breadth of the dispute resolution that is currently provided by the Franchising Code of Conduct, which broadly provides that disputes may be notified by franchisees with respect to issues associated with the agreement and also issues with respect to the franchising code. So I suspect that, to the extent that there is a distinction, the Oilcode focuses on the agreement, whereas the franchising code provides a slightly broader opportunity with respect to issues such as the termination provisions et cetera. That said, the matters under agreement also turn on issues of termination and so forth so, to some extent, it is not particularly narrower. The Oilcode also provides some dispute resolution, as noted before, with respect to concerns associated with terminal gate pricing. To that degree, that is the breadth of a problem or dispute that is broader than that currently anticipated by the franchising code. Those matters go to the issue of a perceived refusal to supply under reasonable terms.

Senator WATSON—I gather from that that you are not particularly perturbed as a regulator about that perceived narrowing because you think there are other benefits that will be introduced to offset that in terms of the ability to mediate?

Mr Cassidy—I will try to summarise. I think there are two answers to that question. Whether there is a narrowing is something which you need to look at. While there are some things which are covered under the franchising code dispute mechanism which are not covered under the Oilcode mechanism, there are other things which are covered under the Oilcode mechanism which are not covered under the franchising code. So whether, in total, that leaves you with a narrowing is probably a matter of judgment. From our point of view, we do not see any issue that should be subject to the Oilcode dispute resolution mechanism that is not covered. We cannot see any obvious standout or exclusion, if I can put it that way.

Senator WATSON—I would like to turn to section 32(11)(c), which applies to both new and renewed agreements. Considering that many agreements are renewed without payment of any up-front fees, is this clause likely to impact on the tenure of renewed agreements, as far as you are concerned?

Mr Cassidy—I am afraid that is one where I will have to look to my colleagues.

Senator WATSON—I am quite happy for you to take it on notice, because it is a specific issue.

Mr Cassidy—That is probably the best idea, because we will need to have a look at that before we can give you a proper answer, I suspect.

Senator ALLISON—There are several submissions that suggest that, from the earliest days of the discussion about this change, it was anticipated that there would be a strengthening of the Trade Practices Act sitting alongside the Oilcode. Could you advise the committee as to whether that is likely to happen?

Mr Cassidy—The government has certainly announced an intention to make amendments to section 46, which I think is the particular section in question. Where exactly those amendments are at, I am afraid I cannot readily tell you. It is something which Treasury, as the policy department, and of course the Treasurer, are closer to than we are. Our understanding is that there is a bill drafted to give effect to what the government announced: what the timing of the introduction of that bill might be. As I say, I am afraid it is something we are not aware of.

Senator ALLISON—You were consulted about the scale and particulars of the amendments to the act?

Mr Cassidy—This committee, in the same incarnation, had a review of the Trade Practices Act and small business. We presented fairly extensively to the committee. The government announced changes in response to that committee's recommendations. In that sense it was a very public process and we did have a chance to make our input.

CHAIR—I think I can say that the draftsmen at the government centres report that the ACCC submissions had a great deal of influence on what the committee decided.

Mr Cassidy—Modesty would probably prevent me from making that sort of comment, Senator, but you can.

Senator ALLISON—So in your view is it reasonable to consider one without the other, as it were?

Mr Cassidy—As I was saying earlier, I see the two as being about different types of conduct, with 46 being about what I call horizontal conduct, which is about one competitor trying to damage another, whereas the Oilcode and the existing franchising code are about the way, say, a supplier deals with those he supplies—in other words, a vertical relationship. So personally I do not see enormous interaction between codes, generally, and what you might call the more horizontal provisions, the competition provisions, of the Trade Practices Act.

CHAIR—And as well, Mr Cassidy, section 46 is generic, and this is sectorally specific.

Mr Cassidy—That is right.

Senator ALLISON—To be clear, if the supermarkets sell petrol from their outlets at a price which is clearly less than that for which they are provided the petrol—in other words, supermarket goods are subsidising the petrol—that is not an abuse of market power?

Mr Cassidy—No. To be an abuse of market power, there would need to be predatory pricing, which would mean that not only are they selling below cost, but they are also doing so to deliberately damage one of their competitors.

Senator ALLISON—What other reason would they have for selling below cost?

Mr Cassidy—Say to increase their market share. There is a difference between me saying 'I am going to target you and drive you out of business by setting my prices so that I am consistently below you and take away your customers' and me saying, 'All you on that side of the table, you each have a certain share of the market; I would like to increase my own share, so therefore I am going to try to be competitive with all of you and see if I can get some customers off you, and some customers off you.' Can you see the difference? One is targeted at a particular competitor, saying 'I am going to behave in a way that tries to drive you out of the market or does serious damage to you' , whereas the other is more general competition behaviour where I am looking to improve my position at the expense of all my competitors, whoever they might be.

CHAIR—In other words, below cost pricing with absent predatory intent is not a section 46—

Mr Cassidy—That is right.

Senator ALLISON—Would the changes proposed to section 46 alter that at all?

Mr Cassidy—No. In our view they shouldn't because below cost pricing is common in the economy. It occurs for various reasons in various ways. You have heard, no doubt, of loss leader type arrangements, which is basically selling a particular product, a product line, below cost in order to get a foothold in a market or increase your share in a market. So if in the general competition provision you were to say that below cost pricing is prohibited, then that would put a dampener on that sort of competitive pricing behaviour right across the economy and would have a significant impact in terms of the overall competitive process—particularly for a new entrant.

A classic strategy of a new entrant to a market is to price below cost, at least for a period of time, in order to get established and to get their products selling. Having done that, they increase their price so that they are making a profit on what they sell. Below-cost selling is a classic strategy for a new entrant. If you had a general provision in the Trade Practices Act which said, 'That's prohibited,' then, apart from other effects, that immediately makes it more difficult for any firm to enter a new market.

Senator ALLISON—With four oil majors, we now have fewer players in the system. Does the ACCC have an ideal number of petroleum companies that Australia should aspire to, and would you be concerned if it fell back to two?

Mr Cassidy—We are often asked a similar question in relation to banks. No, we do not. Part of the reason I say that is that what our ideal number might be at any point in time would depend on a number of considerations, including, for example, how easy it was for imported fuel to come in.

Senator ALLISON—It has become less easy in recent times.

Mr Cassidy—That is right. Therefore, without putting a number on it, if at the moment there was a proposition put to us that four might become three, we would probably want to be looking at that more closely than we would in a situation where there was a ready ability to import.

Senator ALLISON—But you cannot stop one from disappearing out of the market.

Mr Cassidy—Not if they just decide to pack up and go—you are quite right. I was thinking more in terms of some sort of takeover proposal. If it is one just closing up then we may well be concerned about that in a particular market circumstance, but it would not be something we could do anything about.

Senator WEBBER—I want to return to the issues Senator Watson was exploring. When the committee had our hearings in Sydney we received evidence, I think from BP and Mobil, that it was their view that between 50 and 65 per cent of site profits came from the supermarket end for those other ones. Given that, is the ACCC concerned about the effect of the supermarket outlets, particularly in regional centres? Have you or will you monitor what happens to fuel prices when the presence of that supermarket outlet can be seen to force out the neighbouring branded independents? Do fuel prices then rise after the branded independents are gone?

Mr Cassidy—There are a couple of questions intertwined there, so let me see how I go. We certainly are watching it. We certainly agree with that proposition about the margin on petrol being relatively low and that people rely on the sale of other goods and services. Really, that was part of what I was referring to as the underlying economics of petrol retailing. But the point I would make is that it is then wrong to just think about this as a Coles-Woolworths proposition. Let me pick one of the independent chains, 7-Eleven, which is very much an integrated petrol-cum-grocery operation.

Senator WEBBER—I guess I was talking more about regional. In Australia it is Coles and Woolworths in regional centres.

Mr Cassidy—That is true, although I could pick various others. We have had, since the initial shopper docket arrangements by Coles and Woolworths, 450 other notifications of similar sorts of arrangements.

CHAIR—How many?

Mr Cassidy—Four hundred and fifty, a lot of which have come out of regional Australia and a lot of which consist of a local hardware merchant or local grocery merchant striking up a shopper docket arrangement with the two, three or four service stations in that particular town. The 450 notifications I think cover about 1,000 or 1,100 service stations, a lot of them in regional Australia. So this arrangement of cross-trading between petrol and groceries or petrol and other retail goods and services is much more widespread than just the Coles-Woolworths large capital city phenomenon, if I can put it that way.

In terms of the effect, we have been watching fairly closely as Coles and Woolworths have rolled out their arrangements to see what the impact is, and of course these things are always a bit difficult to unpick, particularly when petrol prices seem to be moving all over the place. But we have been gauging petrol prices against what you might call an independent indicator, for which we have been using the import price indicator. It seems to us that where Coles and Woolworths have rolled out their operations there have been sustained reductions in petrol prices relative to the independent indicator of between half a cent and 3c a litre, depending on the particular area and various other factors. We are not seeing, at least at this stage, any real examples of that being—

Senator WEBBER—So, if we end up with their being the only game in town, the discounted price still does apply? It does not then return?

Mr Cassidy—Yes. If I might draw a comparison, without wanting to open up a whole new can of worms. In relation to retail grocery, it is often said that when Woolworths or Coles enter a country town, sure, prices drop for a while, but then when the local grocer, butcher or whatever has gone prices go up again.

Senator WEBBER—That is certainly what the people of Port Hedland think.

Mr Cassidy—Again, in the context of some of the mergers that we have agreed to, we have done ex-ante and ex-post monitoring of the effects of the establishment of a large retailer in a country town. Sure, we see some of what you might call rebound once the retailer has established itself, but we see prices that on average are lower than they were in that town or region before the retailer entered. That is in a sense what we are seeing in the retail petrol side of things.

Senator WEBBER—The only other issue that I want to return to is this dispute resolution process. In the government's explanatory memorandum they say that one of the benefits of the Oilcode is that it will allow for access to a low-cost alternative dispute resolution procedure. From an ACCC point of view, are you satisfied that it is low cost and it is open, transparent and easily accessible so it will actually give us a fast, timely remedy?

Mr Cassidy—If I could draw a comparison with the Office of the Mediation Adviser and the franchising code, which is basically very similar. It has been effective. I think it has mediated over 700 disputes during the time it has existed, and in 70-something per cent of those it has reached a satisfactory outcome so far as the parties are concerned. In other words, they have walked away having resolved their dispute. So we certainly think the existence of this sort of dispute resolution mechanism has the potential to sort out a lot of issues and disputes that arise. We do not see why the retail petroleum side of things should be in that sense any different to franchising more generally. In terms of it being low cost—this is when I need to look at my colleagues—I think under the franchising code the OMA process is $800.

Mr Ridgway—On average $811 something.

Mr Cassidy—$811 for each party—say $1,600 and something in total. Some might immediately say, 'Gee, $800; that's not an insignificant amount of money for a small business,' and there is certainly an element of truth in that. On the other hand, if you compare that to the cost to small business of having to march off to court or some sort of independent process, assuming they could get the other side to come to the party, it is low in relative terms. I am not aware that that sort of detail has yet been decided in relation to the Oilcode, but our expectation is that the sort of cost involved will be similar to what it is under the franchising code. As I say, while it is not insignificant where a small business is concerned—

Senator WEBBER—It is a lot more cost effective than going to the Federal Court.

Mr Cassidy—on the other hand, it is a heck of a lot cheaper than having to get yourself a lawyer and march off to one court or another.

Senator WEBBER—Thank you.

Senator WATSON—Thank you so much for your letter dated 3 May. The committee has treated it as a submission. I refer to your item 2, the role of the ACCC in relation to codes mandated under the act. You say:

In carrying out this role the ACCC uses a combination of enforcement and compliance strategies including educating and working with stakeholders.

As well as elaborating on educating stakeholders, could you tell us what harsh enforcement and compliance strategies you are going to employ?

Mr Ridgway—Perhaps I could respond to this question. As with many of the strategies employed by the ACCC in various sectors, what we do is look at a mixture of options. Option A, as you have indicated, Senator, is a process of educating the various beneficiaries, as you might call them, about their rights under the code and bringing to their attention mechanisms to assist them. Option B is working with those upon whom the obligations are imposed and very firmly saying: 'Here is our view of what's required of you under the code. Here are some practical things that we see as necessary, and we advise you to do them.' If they do not and we find breaches of the code or related breaches of the Trade Practices Act then at that point we will potentially revert to the sharper end of the compliance spectrum to take some enforcement action, to clarify and to reinforce to all the industry that these obligations are seriously enforced by the ACCC. So, by way of response, it is a mixture. We seek to educate, to inform, to persuade. In any event, a number of the traders generally follow that education and persuasion. But those who do not, those who wish to stand and perhaps breach the law, we will deal with at the sharper end.

Mr Cassidy—Could I just say, Senator, that of course Oilcode is intended to be a mandated code, which means that it becomes part of the law we administer.

CHAIR—That is right.

Mr Cassidy—I think we have taken 25 cases to court in relation to the franchising code. In addition, we have attained settlements—I do not have the number off the top of my head—in a number of additional matters under threat of court action. If the Oilcode is mandated and becomes part of the law which we administer then we will take it just as seriously as we take other parts of the law.

Senator WATSON—So it will be more than a rap over the knuckles with a feather duster?

Mr Cassidy—My word. This is one of the reasons why—and I think this is on the record—we are always a bit wary of rushing to make codes mandatory: once they are a mandatory code, under part IVB of the act they are law, and our role is to enforce the law when we see it being breached.

Senator WATSON—Are you happy that the law is being adequately prosecuted? In the Corporate Law area, the regulator is of the view that perhaps the views are not imposing stiff enough penalties on the corporate sector. Are you happy with the penalty regime?

Mr Cassidy—In the context of the Dawson review process, we are on record as saying that we believe we should have higher penalties, particularly in relation to the competition provisions of the act. The government, in responding to the Dawson committee, has indicated an intention to increase the penalties substantially, including criminal sanctions for so-called cartel behaviour. We would certainly support that.

CHAIR—Most of your penalties are negotiated penalties anyway, are they not?

Mr Cassidy—I suppose I could fairly say that, in more recent times, we have started to test a bit more the court in terms of what sorts of penalties will be imposed. We have had a couple of consent order judgments where judges, while agreeing with the penalty, have commented that perhaps the penalty is a bit in the lower end of the range. Those sorts of comments have not gone unnoticed. In recent times, if we cannot reach agreement on a penalty which we think is at the higher end of the range, we are prepared to have that decided by the court.

Senator WATSON—Finally, after listening to all the evidence, do you think in Australia we need something more in the short term than just the raw price mechanisms for Australians to turn more to natural gas, where Australia has an abundance?

Mr Cassidy—That is a fairly broad question. Let me give a hint by saying that I suspect that, if we are going to have significant usage of natural gas as a petroleum fuel, perhaps something needs to be done about the conversion costs involved in that or the price differential—and people will not like me saying this, given the current petrol prices—may need to widen further so in a sense the market might end up doing it. I will not say any more than that, given that it raises all sorts of issues.

Senator WATSON—But, in the meantime, Australians will be paying a lot more than they might otherwise be paying.

Mr Cassidy—That may well be so, but I am afraid that that question raises a whole lot of issues that are outside our purview.

CHAIR—Thank you, Mr Cassidy, and gentlemen. I think you took two questions on notice: one about section 32(11)(c) of the Oilcode and I think the other was about the number of sites that fell below the jurisdictional threshold of the Oilcode. The reporting date to the Senate is Thursday. So this report will need to be written by basically Wednesday afternoon. Could I trouble you to get the responses back to the secretariat by the close of business tomorrow, if that is possible?

Mr Cassidy—Sure. I am just not entirely sure whether we are going to be able to—

CHAIR—Express a view?

Mr Cassidy—Yes, particularly in relation to saying that there were so many service stations that have a turnover below that figure.

CHAIR—I understand that.

Mr Cassidy—We will see if we have something that we can give you.

CHAIR—If you could address the questions as best you can, if it is not possible for you to address them completely, that would be fine.

Senator WATSON—If your hunch and my hunch were well out of sync, that is my worry.

Mr Cassidy—Quite so. As I say, I think our hunches are the same, but I just do not know whether we can quantify that for you.

CHAIR—Thank you very much indeed, gentlemen. That concludes these hearings into the Petroleum Retail Legislation Repeal Bill 2006.

Committee adjourned at 6.44 pm