



Senate Rural and Regional Affairs and Transport  
References Committee  
Inquiry into grain export networks

July 2014

## EXECUTIVE SUMMARY

Co-operative Bulk Handling Limited ("CBH") notes the Rural and Regional Affairs and Transport References Committee inquiry into grain export networks, including the on- and off-farm storage, transport, handling and export components of the various Australian grain supply chains.

In many respects, the CBH business is unique in Australia given both its co-operative structure and its attendant and singular business focus to create value for its Western Australian grower members. To this end, and in the context of the terms of reference set out for the Rural and Regional Affairs and Transport References Committee's review, CBH would suggest that its Western Australian based operations provide a model for grain export supply chain management and operational best practice worthy of attention.

This submission provides an overview of the CBH managed supply chain including detail of the co-operative's ongoing commitment to infrastructure investment and its efforts to ensure growers and their marketing customers can utilise that chain as efficiently as possible and in the manner which delivers the greatest return to the growers of Western Australia.

Growers have become accustomed to grain marketing arrangements since deregulation in 2008. Similarly, the CBH supply chain has adapted to this new and competitive environment, providing a platform from which multiple acquirers may purchase grain from growers.

CBH notes that section of the review which looks to understand the extent to which transport, storage and handling arrangements are transparent and accountable. Here CBH would seek to ensure that the Committee is cognisant of a range of issues, most notably:

- Since deregulation, CBH has out turned over 36 million tonnes of wheat in almost 1,000 separate bulk shipments to over 300 global and local grain traders. Access to the CBH network is among the fairest, most transparent systems in the world, with access to those buying grain from Western Australian growers ensured;
- There have been several industry stakeholders who have suggested that CBH providing supply chain services to both its internal marketing division as well as other exporters somehow creates a conflict;
- CBH has no incentive to exploit growers or exporters in their export supply arrangements. Rather, CBH and its Western Australian grower members have a significant interest in ensuring that their crops can be supplied into global market at an efficient price and CBH will always seek to encourage the most competitive environment possible;
- While regulators will often be obliged to form a national approach to drafting items such as Port Access regimes, CBH would urge Government to avoid developing a blanket approach to ensuring access to export facilities on the basis of its observations of supply chains operating throughout other Australian geographies;
- Such an approach would only serve to remedy a non-existent problem of supply chain access in Western Australia and encumber grain growers with unnecessary and costly regulation.

Given this position, CBH believes that the wheat export industry, certainly in Western Australia, has matured to a level that allows for further removal of regulations. The company has a view that it is incumbent on Government to generally aim to minimise supply chain regulation as it leads to increased costs, inertia, inefficiencies and market distortion; the adverse effect of which is ultimately borne by the grower.

While CBH would argue very firmly that it has gone to considerable length to ensure fair and open access to its storage and handling infrastructure, the challenge of obtaining similar arrangements to other key elements of the Western Australian grain supply chain such as the Western Australian Grain Freight Rail Network remains problematic.

CBH urges the Government to take leadership in the area of inland transport infrastructure planning and take a long term view of industry growth and what is required to facilitate this. Australian grain growers are operating in an export focused, global environment and it is imperative that they can compete effectively with international competitor supply chains. A long term view and plan is required for commercial entities to continue to make investment decisions and drive growth in export supply chains.

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# 1. INTRODUCTION

Co-operative Bulk Handling Limited ("CBH") notes the Senate decision that Grain export networks, including the on- and off-farm storage, transport, handling and export of Australian grain be referred to the Rural and Regional Affairs and Transport References Committee for inquiry and report by 3 December 2014 with particular reference to:

- The principles and practices underpinning an efficient grain supply chain from farm-gate to port;
- Grain marketing and export arrangements and their impact on farm-gate returns;
- Competition constraints on grain transport, storage and handling services;
- The extent to which transport, storage and handling arrangements are transparent and accountable; and
- Any other related matter.

As an organisation that has constantly innovated and grown with operations today extending from grain storage, handling and transport to marketing, shipping and processing, the CBH managed supply chain is considered among the finest in the world and one which may serve as a model for management and operational best practice.

To this end, this submission, seeks to articulate the structure and function that underpins CBH's farm-gate to port supply chain including examples of not just what functions well, but what the Federal Government may need to consider and address if Australian grain growers are to remain competitive with other international origins of grain supply.

## 2. BACKGROUND - THE CBH GROUP

CBH is a unique organisation with a history almost as long as the grain industry it serves. The co-operative's commitment to maintaining a partnership with its Western Australian grain grower members has helped build an industry that has been the backbone of the State's rural economy since the beginning of the bulk handling system 80 years ago.

This partnership has also been the basis of CBH's strength and success.

Now Australia's biggest co-operative and a leader of the nation's grain industry, CBH is controlled by 4,200 grain growers.

The co-operative exists for their benefit and the advancement of the grain industry in Western Australia.

CBH currently employs around 1,000 permanent employees supported by up to 2,000 casual staff during the months of harvest. These employees are located across the co-operative's ten regional offices, 195 receival site locations, four ports, engineering workshops, representative offices in Melbourne, Hong Kong, Tokyo and Portland (USA) and its head office located in West Perth.

### 2.1 The co-operative approach

As a co-operative, rather than being motivated by profit and shareholder dividends, CBH seeks to invest in supply chain infrastructure and undertakes its business operations in order to ensure Western Australian grain growers are part of an efficient, well managed supply chain that contributes to their farm-gate returns. For example:

- In 2010/11 CBH took the decision to pursue enhanced above rail efficiencies by investing \$175 million in new rolling stock (locomotives and wagons) to be operated by a new above rail operator for the dedicated service of grain haulage in Western Australia;  
  
These arrangements provide a higher level of reliability, enhanced usage rates and greater productivity and have had a significant impact on the efficiency of the rail task. During the 2012/13 harvest, CBH reduced rail freight rates to growers by an average of seven per cent;
- CBH's Grower Rebate Program allows growers to enjoy a reduction in storage and handling fees on the basis of their patronage with CBH Group. In 2013/14, growers enjoyed a rebate on the storage and handling fees of as much as \$2.60 per tonne, which promotes their competitiveness in the industry;
- Despite a very challenging cost environment, (labour costs alone have risen between five and six per cent) CBH has been able to maintain storage and handling fees at a consistent level in all but one of the past four years; and

- On the back of ongoing investment in the storage and handling system, the CBH network is the most efficient, and the lowest cost, grain storage and handling system in Australia. During 2013 alone, \$155.2 million was spent on capital expenditure and maintenance activities throughout the network.

## **2.2 The grain industry into the future**

CBH and the growers of Western Australia are aware of the many future challenges to grow and market grain profitably. Despite CBH's efforts to provide enhanced service at the lowest price, long term trends in inputs, yield, pricing and new competitor origins are having an increasing impact on farm profitability (and sustainability) throughout Western Australia.

There have been many reports on the 'Asian Century' bringing new prosperity to the region and creating unparalleled demand for Australia's raw materials and food. While this is an exciting and reassuring sentiment, it is by no means certain that Western Australian grain growers will benefit from this. Indeed, such an increase in demand and prices has to some degree just stimulated production from other locations which are often assisted by lower input costs, higher yields and new investment in supply chains to the market.

The more far-sighted reports suggest that the grain industry needs to look to ways that the Australian grain production and export industry can become more integrated and efficient, so it may benefit over the long term from growth in Asia.

It is CBH's view that growers must play a key role in that search for productivity and efficiency along every step of the supply chain; from the delivery of wheat seed on-farm through to the sale of flour into Asia.

## **3. PRINCIPLES AND PRACTICES UNDERPINNING AN EFFICIENT GRAIN SUPPLY CHAIN FROM FARM-GATE TO PORT**

An efficient farm gate to port grain supply chain is one that strikes a balance between the commercial imperatives of its users (growers and their customers) on the basis that:

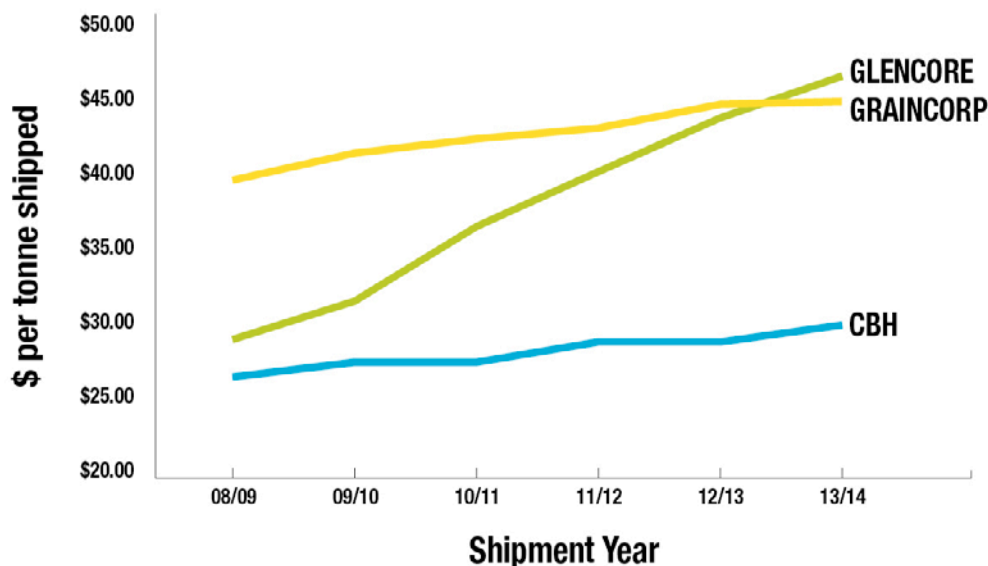
- Growers can deliver their grain into the network during the busy harvest period as efficiently as possible;
- The storage network (incorporating storage and in land freight) provides an operational platform from which grain buyers can acquire grain from growers and for that grain to then be out turned in line with market demand; and
- It functions within a regulatory environment that allows management of those supply chains at an appropriate commercial return to operators, to the extent that necessary levels of reinvestment can be made back into those chains.

### **3.1 Structure and function of the CBH supply chain**

CBH's Western Australian based storage and handling network is considered among the finest in the world. The co-operative offers a range of services to the growers of Western Australia and their end-user customers to ensure the State's annual grain harvest is handled, stored and shipped efficiently, cost-effectively and safely.

With 197 receival points located throughout the Wheatbelt, growers can deliver their grain into storage quickly and efficiently with subsequent options to choose a least cost transport pathway to port. Each harvest the CBH Group receives an average of 350,000 separate deliveries that are sampled, weighed, unloaded and segregated into over 50 different grades.

All CBH's services are provided to growers at charges lower than any comparable grain bulk handler in Australia with the company's ongoing strategies targeted at driving service levels up and charges down even further (see figure 1).



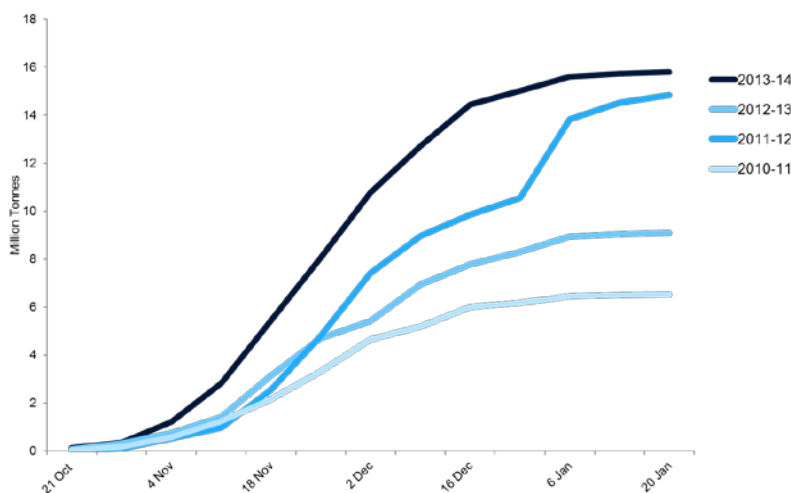
**Figure 1 - Comparison of storage and handling charges throughout Australian grain supply chains**

CBH's recurrent investment in the supply chain is without parallel; in the last ten years alone, CBH has invested in excess of \$1 billion in improving storage and handling infrastructure. CBH's co-operative structure and function enables this type of expenditure by allowing the company to take a "longer term view" on what are the usual payback provisions that organisations motivated purely by shareholder returns and profit might take.

The CBH business measures value as 'direct value to growers'; allowing the company to invest in areas such as storage and handling capacity that will increase returns of a grower's farming operations but not necessarily provide the greatest financial return on CBH's capital.

The principles underpinning the CBH operated supply chain are simple yet fundamental to ensuring growers are able to deliver their grain to export markets in the most efficient way possible. This incorporates:

- Providing growers with the best possible storage and handling service at the lowest possible price;
- Investing in receival infrastructure that allows growers to deliver their grain during the busy harvest period as quickly as possible. During the record 2013/14 season, the CBH network took 90% of the 16 million tonne harvest in just 21 working days (see Figure 2);
- Allowing growers to access the most efficient and effective in-land freight. Since CBH purchased its own rolling stock and assumed above rail operations in 2011/12, the company has been able to reduce rail freight costs by 7% through above rail efficiencies; and
- An integrated business model where growers are provided with a rebate on their storage and handling charges from surpluses generated through supply chain efficiencies and marketing and sales performance.



**Figure 2 - Rate of harvest receivals**



### 3.2 Integrated supply chains create optimal value

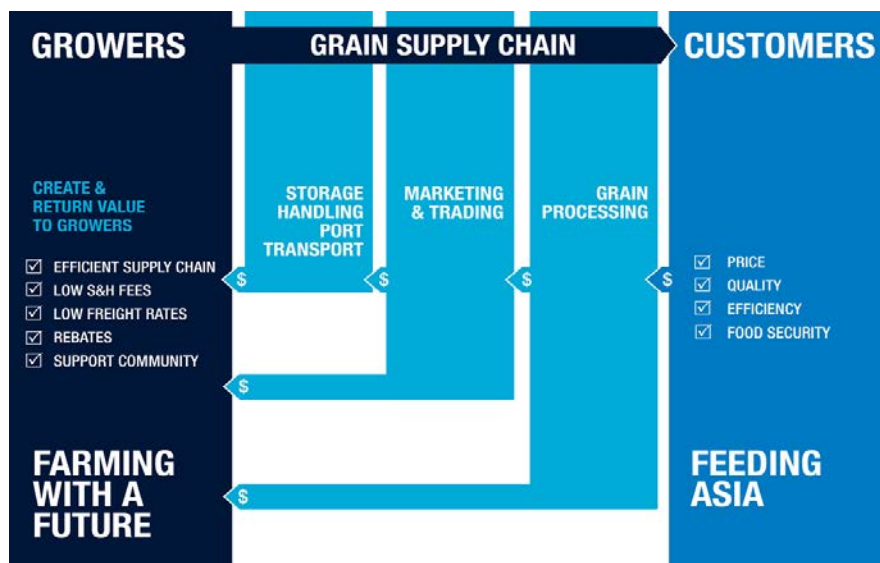
The ideal value chain is often described as one where growers and their customers are inextricably linked to the extent that growers' planting and cropping decisions are informed directly by the demands of the market (locally and internationally).

The reality is often however a little different; not least of which because grain growers will in the majority make planting decisions on the basis of agronomic factors and resulting gross margins (what grain type can deliver the highest yield for their particular geography). While factors such as attendant logistics (is there a storage service available for a particular grain) and the requirements of customers remain important, a grain (or a specific variety of a grain) and its capacity to be agronomically productive will often be the primary consideration.

As outlined in Figure 3, the CBH's integrated business model (storage, handling, transportation, marketing and port operations) operates to create value for the growers of Western Australia by ensuring they have influence and control throughout each element of the chain as well as providing the vital interface between growers and their customers.

This Australian based business has been augmented by the company's investment in 6 flour mills in South East Asia. CBH holding a fifty per cent stake in these processing facilities located in Indonesia, Vietnam and Malaysia means that growers can receive direct and transparent information around consumptive trends and quality requirements from these markets (such as increased demand for high protein milling wheat) and as a consequence make more informed planting/cropping decisions.

The fundamental value of CBH's integrated supply chain is that decisions are made on the basis of what is optimal for the entire chain rather than the alternative, more fragmented approach adopted in other geographies that will often see participants in a discrete section of the chain make decisions based purely on what is best for that specific component. The CBH's integrated approach takes the more holistic view; what creates the most value for Western Australian grain growers across the chain (see Figure 3).



**Figure 3 - CBH's integrated business model - a whole of chain approach**

There have been several industry stakeholders who have suggested that CBH providing supply chain services to both its internal marketing division as well as other exporters somehow creates a conflict of interest. CBH would contend very strongly that its sole obligation is simply to create value for its grower members irrespective of which commercial entity markets their crop. Indeed CBH's Marketing and Trading division holds just 50% of export share from Western Australia suggesting that other marketers are acquiring and exporting significant volume via the CBH supply chain (There are around 18 marketing and trading organisations, collectively exporting around 5 million tonnes grain from Western Australia each year).

This is an important point. CBH's Western Australian based chain is about providing growers and their customers with an efficient and assured platform of exporting grain to their international markets. While regulators will often be obliged to form a national approach to drafting items such as Port Access regimes,

CBH would urge Government to avoid developing a blanket approach to ensuring access to export facilities on the basis of its observations of supply chains operating throughout south and eastern Australia.

Such an approach would only serve to remedy a non-existent problem of supply chain access in Western Australia and encumber grain growers with unnecessary and costly regulation.

### **3.3 Access to the CBH network post deregulation**

Western Australia has the largest export focus of all of Australia's wheat producing states with around 90% of the annual crop exported in bulk.

Since deregulation, CBH has out turned over 36 million tonnes of wheat in almost 1,000 separate bulk shipments to over 300 global and local grain traders, marketers and end-users from a supply chain that ensures export cargoes are accumulated and loaded to customers' specifications; maximising value for both exporters and the grain growers of Western Australia.

Access to the CBH network is among the fairest, most transparent systems in the world, with access to those buying grain from Western Australian growers ensured.

CBH surveys its export customers on an annual basis as a means of better understanding views regarding its operational performance. Recent qualitative responses arising out of the 2013 survey suggest that exporters are both confident and satisfied in their use of the CBH system such as:

- *"Probably better than others. They listen a little more than others. The multinationals who own facilities elsewhere are more focused on trading than listening."*
- *"Strong operational relationship. Open and regular, trust."*
- *"System simple, open, even opportunity in the market, the same for everyone."*
- *"They seem to be able to move the crop well every year. Have acquired new trains. Good logistics."*
- *"Provided you adhere to processes, can expect product to be delivered efficiently."*
- *"World class export terminals."*

## **4. GRAIN MARKETING AND EXPORT ARRANGEMENTS AND THE IMPACT ON FARM-GATE RETURNS**

CBH's Marketing and Trading division is a specialist organisation with a reputation for supplying premium quality grain to the world's major markets.

CBH currently exports a variety of grain types to more than 30 export destinations and over 300 customers.

In 2013, CBH exported 5.7 million tonnes of grain (wheat, barley, canola, lupins and oats) in both bulk and containers, with over 75% of sales going direct to end-user customers.

Like all parts of the co-operative, CBH's Marketing and Trading Division is a trusted business partner of Western Australian grain growers, providing a range of pool, cash and payment options designed to maximise harvest value.

### **4.1 Value of a competitive marketing environment**

Since changes to Australian grain marketing arrangements (for wheat and coarse grain), grain growers, certainly in Western Australia, have adapted to the newly deregulated environment which while clearly different has proven to be advantageous.

Australia's system of multiple buyers now allows growers a more representative view of world values providing a closer relationship and understanding for ongoing fluctuations in price. Values quoted to Western Australia growers closely reflect Chicago Board of Trade ("CBOT") values providing a more transparent view of markets. A competitive environment of multiple buyers can facilitate increased purchase volumes during periods of high demand; meaning more growers can benefit from increased prices.

And importantly growers have absolute choice regarding which acquirer; local or international, with whom they may market their grain.

The CBH supply chain has adapted to this new and competitive environment, providing a platform from which multiple acquirers may purchase grain from growers. Indeed the discussion paper developed and released by the Wheat Industry Advisory Taskforce ("WIAT") *'A preliminary assessment of wheat export quality management practises'* is similarly supportive in particular:<sup>1</sup>

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<sup>1</sup> WIAT - Assessment of Wheat Export Quality Management Practices; February, 2014



- *Based on the volumes of wheat being sold and the lack of evidence to suggest that market share is being lost in premium markets, it is difficult to sustain the argument that there has been deterioration in quality since deregulation.*

## 4.2 Current marketing arrangements are effective

It is CBH's view that export and marketing arrangements, certainly in Western Australia, functions in a manner that supports an appropriate level of price discovery for grain growers.

There is little doubt that growers are accessing increasing levels of information to assist with their marketing decisions. In a recent survey of CBH grower members, 80 per cent of respondents listed online price discovery mechanisms as their first choice for grain pricing information. With this type of trend, CBH believes there is sufficient evidence that the market is moving to fulfil its information needs accordingly (augmented by the likes of farm consultants, marketing organisations and financial advisers).

Since the deregulation of Australian grain industry (wheat at a national level and coarse grains at the state level) there has been discussion about whether this flow of information is being appropriately coordinated. One example is the extent to which the level of publicly accessible stock information should be increased (volumes and quality details for growers' unsold grain held in store) and whether the release of this information would assist growers to make pricing and marketing decisions.

CBH notes the recent work undertaken by the Wheat Industry Task Force and is supportive of the conclusions outlined in the 2013 discussion paper that:<sup>2</sup>

- *... based on the reports considered by this paper, there does not seem to be obvious market failure resulting from the information that is currently available, even if this information must be paid for.*
- *... members believe that, as the Australian wheat export market progressively moves towards full deregulation, there is an increasing range of tools and information available for growers, and other industry participants, to manage risk, market their grain, and get the best price.*
- *The taskforce acknowledges that some industry participants are calling for stocks information held in BHC systems to be disclosed on a detailed level. However the taskforce believes such a requirement would potentially provide an incomplete picture of the actual stocks situation by not capturing those stocks held by other commercial operators and on-farm.*
- *The taskforce found that there was no evidence that growers would obtain a material benefit from an increased level of market information, including stocks. Through the CIE report, the taskforce found that a deficiency of stocks information was not placing Australian growers at a significant market disadvantage, with price instead being driven predominately by global market forces.*

## 4.3 Market development

It is contingent for organisations, such as CBH, operating in global grain markets to undertake and facilitate an effective link between growers and their customers. CBH does not consider that any form of statutory, regulatory or separate industry entity should undertake this function.

As an example, information such as seasonal wheat quality data, testing and functionality traits that CBH (along with other marketing and trading organisations) convey to their local and international customers forms a critical component of the competitive grain marketing landscape. An exporter's accurate communication of this information helps ensure not only their own standing and performance in the marketplace but the ongoing integrity and strength of the Australian wheat "brand".

Commercial entities seeking to market and export Australian grain (acting as a link between growers and their markets) will be absolutely cognisant that this brand must be managed and sustained into the future. That said CBH is aware of a number of organisations undertaking, or seeking to undertake a role in the general promotion of Australian wheat (Grain Growers Limited and the Australian Export Grains Innovation Centre).

While CBH does not seek to comment on any of the specific activities undertaken by these (and other) organisations, it does have concerns regarding the potential for mixed messaging arising out of this "multi-layered approach" and the potential for a disconnect between the promotional activity being undertaken by these third parties and that of commercial participants who have a financial stake in the ongoing and effective marketing and export of Australian wheat.

<sup>2</sup> Wheat Industry Advisory Taskforce 2013; A preliminary assessment of wheat export industry stocks information requirements - Page 17

CBH would support efforts to clarify and streamline the process for the promotion of Australian grain.

There has been considerable efforts and discussion regarding how the industry might de-commoditise grain or to brand it in such a fashion that its value can be enhanced. While the discussion is certainly welcome it is CBH's view that these activities are best driven from ongoing marketing opportunities identified by commercial participants working directly with customers (rather than any generic branding activity operating separate to this process).

A salient example is the introduction of the noodle wheat grade into Western Australia. This was driven by market demand and opportunity and subsequently promoted to producers (and responded to accordingly). The key here is having an environment capable of developing and responding to market opportunities not necessarily to create a forum for industry to drive the market direction or the approach of generic branding.

The inherently fungible nature of grain means it can be easily substituted (and has a highly elastic demand). Even if grain could somehow be successfully branded in such a fashion that it may be worth more to growers at the farm gate, it is possible that the additional costs associated with its segregated storage, transport, quality assessment and shipping would prove too costly.

The importance of growers' minimising costs of production in areas including inputs (seed, fertilisers, pesticides), labour and supply chains costs in order to ensure not just farm gate profitability, but in many instances, a farming enterprise's very survival is critical.

To this end, the fundamental premise of the CBH business is to ensure that Western Australian grain growers who are entirely reliant on international markets to acquire their grain, have access to efficient inland supply chains (storage, handling, above rail operations and port infrastructure) along with committed and professional grain marketers and traders.

## **5. COMPETITION CONSTRAINTS ON GRAIN TRANSPORT, STORAGE AND HANDLING SERVICES**

As a co-operative, CBH has no incentive to exploit growers or exporters in their export supply arrangements. Rather, CBH and its Western Australian grower members have a significant interest in ensuring that their crops can be supplied into global market at an efficient price and CBH will always seek to encourage efficient and competitive environments.

The CBH business operates on the basis of constantly seeking to satisfy the supply chain requirements of its grower members and has a range of measures in place to ensure that this continues. For example:

- The CBH Growers Advisory Council ("GAC") was established by the CBH Group in 2003 to help facilitate enhanced communication between the CBH Board and growers at the grass roots level. The fifteen member GAC meets in a formal sense, four times per year; providing a further and very valuable flow of information to the company, informing just how CBH can improve its service offering to Western Australian grain growers;
- The very essence of CBH's storage and handling service during the busy harvest period is based around growers submitting their annual Grower Estimate Forms. Completed on the finalisation of their individual seeding programs, Grower Estimates allow CBH to plan for the harvest period ensuring that storage services and segregations match growers cropping programs as closely as possible;
- Grower Estimates data is rounded out by CBH's comprehensive program of pre-harvest meetings. Here CBH staff undertake grower meetings throughout the state to discuss crops and their anticipated yield, the demand for specific grain segregations and any particular issue that may be relevant for the upcoming harvest period. CBH goes to considerable efforts to ensure that the harvest period runs efficiently for growers.

Very few, if any other grain organisation goes to these lengths to ensure growers have the right degree of capacity available to them to deliver their grain. To the extent that it has influence and control, CBH will always operate to ensure that any (and all) material competitive constraints on grain transport, storage and handling services are minimised and/or removed.

### **5.1 Port access - no market failure**

Since deregulation, CBH believes that the wheat export industry has matured to a level that allows for further removal of regulations. Indeed, port operators such as CBH had been providing consistent and equitable access to third parties for many years before wheat export deregulation, allowing them to export other grains through their facilities.

As outlined in section 3.2, network access regulation is only appropriate in the event that the market cannot effectively respond and a clear need is demonstrated. This is certainly not the case for Australia's grain industry and it is CBH's view that no market failure had been experienced.

In 2008, at the time the port terminal access regulation was proposed, there was concern by some sections of industry that there needed to be access regulation in order to prevent port operators from excluding competitors and blocking the export supply chain of growers. In particular, the claim was that port access regulation would prevent one national monopoly from being replaced with 3 regional monopolies.

However, this claim was without evidence and overlooked that each port operator had already been providing access to third parties, allowing them to export other grains through their facilities. No market failure had been experienced and the alleged problem of port access constraints was purely hypothetical.

Evidence of provision of access to export grains other than wheat was overlooked as it was inconvenient to the argument in support of regulation of wheat exports. Yet access for exports of non-wheat grains had been provided and has been provided for many years without access regulation being required. In the case of CBH, this has been operative in barley, canola and lupins for over 12 years, and longer in the case of other grains which have never been prescribed under a single desk marketing arrangement. In addition, CBH is subject to a legislative obligation under section 19 of the Bulk Handling Act 1967 (WA) to provide access.

The key assumption for implementing the solution was that port operators export facilities could not be replicated. However, all the evidence is to the contrary; new port operators have entered in a timely fashion, demonstrating that there is actually a competitive constraint on port operators.

Since deregulation of wheat exports, new ports have opened at Brisbane (QLD), Newcastle (NSW), Bunbury (WA) and expansion at Melbourne, competing with Geelong (VIC). Further plans have been announced for a new facility to be opened at Port Kembla and for the use of a woodchip loader at Albany (WA).

If new entrants are not constrained from entering to compete against incumbent port terminal operators, and the evidence of real and meaningful entry is irrefutable, then it follows that there is a significant actual and potential competitive constraint on port terminal operators. In this circumstance it is difficult to see the potential for abuse of market power that was so feared in 2008 becoming reality.

CBH has considered the above examples of a lack of market failure when considering the proposed Mandatory Code of Conduct.<sup>3</sup>

## 5.2 Port access into the future - ensuring appropriate and effective regulation

As a result of market deregulation and the subsequent introduction of the Wheat Export Marketing Act 2008 ("WEMA"), at present CBH is required to provide an access undertaking to the Australian Competition and Consumer Commission ("ACCC"), in relation to the export of wheat from its port terminals.

The expense of dealing with port access undertakings over the last six years have been substantial, estimated to have a direct cost on the CBH business and Western Australian growers between \$3 and \$4 million.<sup>4</sup>

Aside from this financial impost, the current port access arrangements also restrict the flexibility in which port operators and grain marketing organisations can respond to changing market conditions, be it price or production. This lack of flexibility increases the likelihood of international customers seeking grain from alternative origins of supply.

The industry has been working towards progressing port access regulation and in light of the recent released of the Mandatory Code of Conduct for Grain Export Terminals Exposure Draft, by DAFF on 3 June 2014, CBH's position regarding the draft Mandatory Port Access Code is that:

- Port access regulation is only appropriate in the event that the market cannot effectively respond and a clear need is demonstrated. This is certainly not the case for Australia's grain industry. No market failure had been experienced.
- As a grower controlled co-operative, CBH has no incentive to exploit growers or exporters in their export supply arrangements. Rather, CBH and its Western Australian grower members have a significant interest in ensuring that their crops can be supplied into their global market at an efficient price and CBH will always seek to encourage the most competitive environment possible.
- Since deregulation, CBH believes that the wheat export industry has matured to a level that allows for further removal of regulations. Indeed, port operators such as CBH have been providing

<sup>3</sup> CBH's submission to the Agricultural Competitiveness Issues Paper, April 2014 is attached as Appendix 1

<sup>4</sup> CBH submission to Productivity Commission Inquiry into the National Access Regime April 2013

consistent and equitable access to third parties, allowing them to export other grains through their facilities.

- Regulation is harming Australia's competitiveness in a global marketplace. Rather than enhancing efficient operation of export chains this regulatory impost is creating an environment of unnecessary and excessive cost, making Australian grain less competitive on world markets.
- Level regulation should apply to all Port Terminal Operators otherwise market distortions are fostered, creating disincentives for Australian companies to continue to invest in agricultural supply chains.

CBH welcomes the progression of the industry towards a reduced regulatory structure and seeks the development of the Mandatory Code of Conduct that recognises the current operating environment and future efficiencies for the Australian export market.

### 5.3 Multi-nationals gaining an unintended advantage

CBH considers that it is incumbent on Government to develop policy frameworks that strike a balance between creating an incentive for foreign investment, and where that investment involves key export infrastructure (railways lines and roads), that the users of that infrastructure have some assurance that they may continue to access facilities with reasonable service and reasonable pricing.

Global scale firms can develop if investment into the Australian marketplace by local incumbents is not regarded by regulators as prejudicial to competition. Typically Australian firms compete against organisations that are many times their size who are able to leverage significant economies of scale and scope into Australia.

A situation that sees Australian firms provide fair and open access to their local supply chains whilst not receiving similar opportunity in foreign jurisdictions will guarantee that Australian firms, particularly those without the necessary economic and operational scale, will be gradually subsumed into larger multinational corporations.

In line with the sentiment expressed in section 5.2, the playing field should not be tilted against those who have invested in Australia already and who are envisaged to continue to make substantial investments unless the wrong investment signals continue to be sent. For example, it is difficult to justify investment where new operators can compete without equivalent regulation thereby allowing them to offer different pricing and terms as well as being able to operate with more flexibility thereby undermining investment decisions.

As a further, more specific example, global competitors have sufficient access to capital to replicate the entire CBH network in a single year. In the past five years, Cargill has invested about \$15 billion in acquisitions and assets to expand its global reach and capabilities. At any one time, Cargill may have more than 500 vessels at sea, transporting 200 million metric tons of cargo a year (see Figure 4).

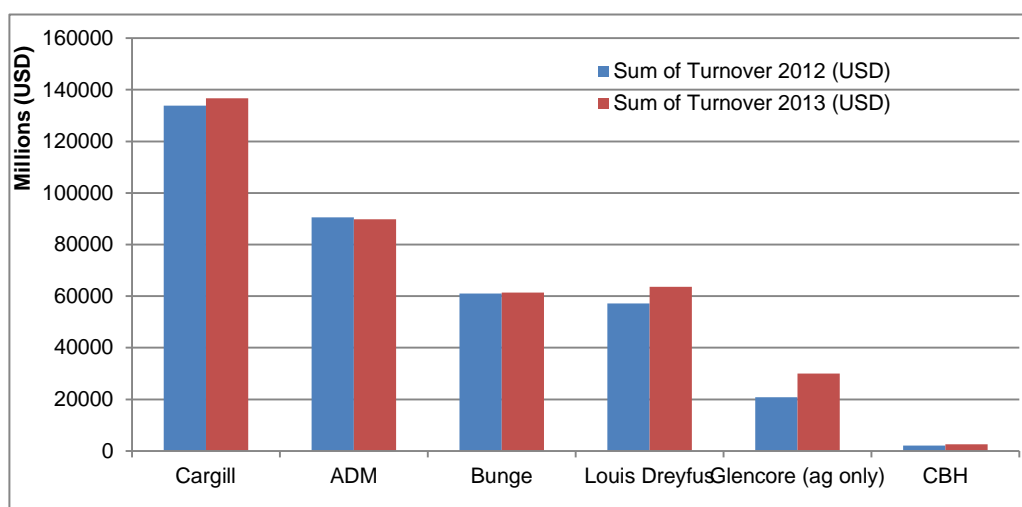


Figure 4 - Turnover in USD of major competitors

Indeed current regulation is actually creating considerable market power imbalances for Australian firms. As an example, and as outlined in section 5.2, CBH is required, pursuant to the provisions of the WEMA, to provide an access undertaking to the ACCC in relation to the export of wheat from its port terminals.

In contrast, global agribusiness Bunge recently completed construction of a grain export terminal at Bunbury with a capacity to export 500,000 to 1 million tonnes per annum. Based in the United States, Bunge generates revenue of over \$60 billion, with over 35,000 employees operating in over 40 countries.

CBH understands that as a result of the particular operating arrangements at the terminal, Bunge is not obliged to provide an access undertaking to the ACCC. This creates an uneven playing field and distorts the regulatory position on the basis that:

- Bunge will be able to discriminate in how it acquires and exports wheat through its Terminal in a way that is favourable to Bunge compared to all other Australian and international wheat exporters operating export terminals;
- CBH, an Australian co-operative, will not be able to match Bunge's ability to provide variable terms for particular wheat types or customers because CBH must offer the same export terms to all parties; and
- Bunge will not have to spend the time or cost in negotiating a new export undertaking with the ACCC, nor will be required to adhere to Tier 1 compliance and reporting requirements under the proposed Mandatory Code of Conduct.

Further, there can be disparities between Government incentives for new entrants and those for incumbent operators. CBH is increasingly asked to expend money beyond the boundary of its sites such as "run off" roads and intersection alterations in view of forecast additional traffic, yet the same State Government is building a truck marshalling yard in Bunbury; a primary beneficiary of which will be Bunge's Bunbury Port.

Addressing this type of disparity is critical to ensure a supply chain free of competitive distortions.

## 5.4 Importance of Government trade facilitation and support

CBH is supportive of Government's recent and ongoing efforts to enhance Australia's trade and investment relationships (as they relate to grain) with countries throughout the world. In particular, CBH welcomes Government's consultation with industry on these issues in advance of any deliberations as they relate to Australian Government support for bilateral and multilateral agreements. It is the CBH Group's view that the optimal benefit can be generated when Government/business collaborations take this type of broad approach.

CBH would endorse Government efforts to establish a policy and investment framework that ensures wherever possible that the agriculture sector (in this instance - grain growers) can be competitive with producers from other international origins of supply. For example, this might include a focus on negotiating more favourable terms of trade.

In line with CBH's position that it does not support increased regulation as it leads to increased costs, inefficiencies and market distortion that is ultimately borne by the grower, in an international context, the global "hold" on tariffs should be made permanent along with efforts for further trade liberalisation such as:<sup>5</sup>

- Addressing the way international jurisdictions apply local taxes which, when applied differently to specific products, becomes a form of tariff. As an example, Indonesia's VAT is applied to soybean imports differently from lupin imports for the local tempeh/tofu market (soybeans attract a zero VAT tax, whereas lupin splits from Australia attract a 10 per cent VAT tax). This added VAT on lupins makes it difficult for importers to offer product at a comparable price to soybeans (despite superior quality traits);
- Ensuring that quarantine regulations are not used to shape supply in certain food crops. The export of Australian canola into China from the regions around Albany in Western Australia and parts of South Australia have been banned due to concerns around a fungal pathogen (*blackleg*) which may create issues for domestic canola crop production; and
- The removal of restrictions for Australian companies selling grain into Iran. Currently Australian exporters are required to sell grain into the Iranian market via third parties due to tight controls on Australian trading companies, making it difficult to compete with grain from the US. US grain traders are able to sell into Iran via owned subsidiaries in European localities. Last year the value of the Iranian grain market was in excess of AUD300 million.

<sup>5</sup> Note that in the interests of expediency CBH has limited its opportunities for necessary trade liberalisation to the following three. As an organisation that exports grain across the globe, CBH has a range of further examples that can be tabled for further discussion as required.



## 6. THE EXTENT TO WHICH TRANSPORT, STORAGE AND HANDLING ARRANGEMENTS ARE TRANSPARENT AND ACCOUNTABLE

CBH urges the Government to take leadership in the area of inland transport infrastructure planning and take a long term view of industry growth and what is required to facilitate this. Australian grain growers are operating in an export focused, global environment and it is imperative that they can compete effectively with international competitor supply chains. A long term view and plan is required for commercial entities to continue to make investment decisions and drive growth in export supply chains.

While CBH would argue very firmly that it has gone to considerable length to ensure fair and open access to its storage and handling infrastructure, the challenge of obtaining similar arrangements to other key elements of the Western Australian grain supply chain remains problematic.

This needs to be addressed by both State and Federal Governments as a matter of urgency.

### 6.1 Grain growers are not currently able to access the Western Australian Grain Freight Rail Network fairly or equitably

While the Australian grain industry, like any sector, needs access to appropriate levels of capital and foreign investment to facilitate industry expansion and growth, with foreign investment comes the requirement to understand an investor's commercial goals and the extent to which these are complementary to local industry; in this case the Australian grain industry.

As a case in point, the 49 year lease (expires in 2049) for the Western Australian Grain Freight Rail Network ("WAGFRN") is currently held by various Brookfield entities and operated by Brookfield Rail; part of the Canadian based Brookfield Asset Management Group. While Brookfield's involvement has been publicly welcomed by the Western Australian State Government, it seems Brookfield's commercial objectives are increasingly at odds with the users of the WAGFRN; the growers of Western Australia and the States \$3-4 billion grain industry.

Brookfield Rail and the growers of Western Australia have fundamentally different positions regarding the operation of the WAGFRN. Brookfield is seeking to operate the rail network in order to maximise profit on behalf of its shareholders, notwithstanding that its profit maximisation inflicts a comparatively greater economic loss on the Western Australian economy. Meanwhile, the growers of Western Australia, as users of the track, are deprived of the most efficient and effective transport network possible in order to transport grain to their local and international markets.

It has become increasingly obvious that these two objectives are mutually exclusive; for example:

- Brookfield Rail is seeking to close those sections of the WAGFRN on which it is not making high levels of profit, without surrendering them to an alternate user, on the basis that it can continue to increase revenue and margins from a reduced section of the rail network without increasing its own productivity. This behaviour is indicative of a true monopoly asset, as it can be run without regard to the interests of its customers. This closure is sought despite those assets remaining an important component of the local supply chain the use of which would avoid increased costs being passed onto the community;
- Rail performance standards are decreasing while access fees are increasing:
  - Below rail track access constitutes around 40 per cent of a grower's freight costs; average access cost are \$7-8 per tonne across Western Australia;
  - CBH and the growers of Western Australia currently pay access rates to Brookfield that are 2.6 to 4 times greater than rates paid by Eastern Australia growers for tracks that have higher speeds/mass;
  - Freight rates in Canada and USA are 30-50 per cent lower than Western Australia;
  - In spite of plans to close over 800 kilometres of track, Brookfield Rail has proposed a significant increase in access fees; and
  - Despite Government committing \$164.5 million to fund required Tier 1 and Tier 2 track maintenance, there are currently over 750 separate speed and mass restrictions that



Brookfield Rail have placed on Tier 1 and Tier 2 line sections which remain unresolved and hinder effective supply chain operations.<sup>6</sup>

It is for these reasons CBH has sought access to the WAGFRN under the Railways (Access) Code (2000) ("Code"). CBH has previously expressed concern regarding Western Australian Rail Access Regime and the structure of the Code in a previous submission to the Productivity Commission's National Access Regime Issues Paper, not least of which are concerns regarding the Gross Replacement Value (GRV) costing methodology.<sup>7</sup>

Once again, CBH would suggest that it is incumbent on Government to develop policy frameworks that strike a balance between creating an incentive for investment (including foreign investment), and where that investment involves true monopoly infrastructure (railway lines and roads) ensuring that the users of that infrastructure have some assurance that they may continue to access those facilities with reasonable service and pricing. This doesn't mean a lack of returns, but it doesn't mean monopoly profits either.

When considering foreign investment, the Government requires a clear understanding of an interested company's commitment to the Australian grain industry and their plans to enhance the operations of Australian growers and their rural communities.

## 6.2 Access to the CBH network

In stark contrast to access arrangements for the WAGFRN and as outlined in section 3.3, access to the CBH owned and controlled supply chain infrastructure is absolutely assured for marketing organisations seeking to export from Western Australia. A fundamental principle for CBH is ensuring that its growers can maximise their harvest returns and sell to an acquirer of their choice.

CBH notes the discussion paper developed and released by the Wheat Industry Advisory Taskforce ("WIAT") 'A preliminary assessment of wheat export quality management practices' and is supportive of the observations outlined by the WIAT. In particular:

- *The taskforce does not believe there is a market failure in the storage and handling process, as there are processes in place to manage quality issues nor in the shipping phase given extensive testing procedures that are in place.*
- *Based on the volumes of wheat being sold and the lack of evidence to suggest that market share is being lost in premium markets, it is difficult to sustain the argument that there has been deterioration in quality since deregulation.*

## 6.3 Provision of stock information/data

There is little doubt that growers are accessing increasing levels of information to assist with their marketing decisions. In a recent survey of CBH grower members, 80 per cent of respondents listed online price discovery mechanisms as their first choice for grain pricing information. With this type of trend, CBH believes there is sufficient evidence that the market is moving to fulfil its information needs and that there is no overarching requirement to legislate for information provision.

Since the deregulation of Australian grain industry (wheat at a national level and coarse grains at the state level) there has been discussion about whether this flow of information is being appropriately coordinated. One example is the extent to which the level of publicly accessible stock information should be increased (volumes and quality details for growers' unsold grain held in store) and whether the release of this information would assist growers to make pricing and marketing decisions.

CBH notes the recent work undertaken by the Wheat Industry Task Force and is supportive of the conclusions outlined in the 2013 discussion paper that:<sup>8</sup>

- *... based on the reports considered by this paper, there does not seem to be obvious market failure resulting from the information that is currently available, even if this information must be paid for.*
- *... members believe that, as the Australian wheat export market progressively moves towards full deregulation, there is an increasing range of tools and information available for growers, and other industry participants, to manage risk, market their grain, and get the best price.*

<sup>6</sup> CBH's submission to the Western Australian Economics and Industry Standing Committee, April 2014 is attached as Appendix 2

<sup>7</sup> CBH's submission to the National Access Regime, Productivity Commission, February 2013 is attached as Appendix 3

<sup>8</sup> Wheat Industry Advisory Taskforce 2013; A preliminary assessment of wheat export industry stocks information requirements - Page 17

- *The taskforce acknowledges that some industry participants are calling for stocks information held in BHC systems to be disclosed on a detailed level. However the taskforce believes such a requirement would potentially provide an incomplete picture of the actual stocks situation by not capturing those stocks held by other commercial operators and on-farm.*
- *The taskforce found that there was no evidence that growers would obtain a material benefit from an increased level of market information, including stocks. Through the CIE report, the taskforce found that a deficiency of stocks information was not placing Australian growers at a significant market disadvantage, with price instead being driven predominately by global market forces.*
- *The taskforce noted that, since the conclusion of targeted government and industry funded stocks information publications, the industry has been through the 2012 harvest and most of the marketing period for that crop. The taskforce is unaware of any major disruptions to the effective operation of the wheat export market during this period.*

As a co-operative owned and controlled by the growers of Western Australia, CBH has raised reservations during industry consultations regarding proposals to force disclosure of additional stocks information beyond current provisions.

CBH does not believe that growers would truly benefit by allowing details of unsold stock information held in bulk handling systems to be disclosed to the market.

Grain growers have a naturally “long” position in the market; that is growers produce a crop and are then obliged to market that grain over the course of the year. In export dependent states such as Western Australia (and to a lesser degree South Australia), the notion that the release of information pertaining to grain held in store (specifically information relating to tonnage, grade and grain quality) would somehow give growers “market power” is not supported by any evidence and consequently makes very little sense.

Ultimately the price of grain destined for the export market is affected by the volume of grain in the global market that is available for trading, of which Australian grain is a small factor. It is information about grain production in foreign jurisdictions that drive the fundamentals of global grain pricing, and the Australian domestic price will respond to surges in global pricing that would make it more attractive to export than sell locally.

Rather, and in most cases, it is the buyers (marketers and traders) who seek this information because it will allow more informed decision making as to the global supply of grain. Traders can reduce acquisition prices in knowledge of abundant supply and simply compete at “market values” when volumes are at more normal levels.

In CBH's view, it is the buyers of that grain (or those commercial entities at the periphery of grain marketing such as traders, brokers, consultants and organisations publishing information) that will gain the most by having a more thorough understanding of the volume of grain held in store; not grain growers.

The storage and handling system operated by CBH was developed by and for the growers of Western Australia. While growers certainly welcome the opportunity for local and international grain buyers to access their grain via the CBH system, up until the point of sale, the grain and its attendant information remain the commercial property of growers.

## 6.4 The “pre-competitive” role for Government

A key role for Government is for it to assist in ensuring an appropriate policy framework exists in Australia that strikes a balance between creating an incentive for investment by allowing adequate returns versus ensuring market participants have access to essential infrastructure (specifically that which cannot be duplicated) at a reasonable rate of return. In the absence of a true monopoly asset, the market is the most efficient way to determine an efficient allocation of assets and to provide competition that values an Australian grain grower's agricultural products.

In determining whether and how to regulate access to supply chains, the relative incentives and constraints on participants needs to be carefully considered (with attention paid to the identity of benefiting stakeholders in determining whether regulation is needed to offset commercial imperatives that would otherwise harm grain growers). Governments should facilitate and encourage stakeholders who re-invest into the Australian supply chain and have an ongoing focus on driving productivity improvements to ensure the sustainability and profitability of Australian agriculture.

CBH considers it incumbent on Government to generally aim to minimise supply chain regulation as it leads to increased costs, inertia, inefficiencies and market distortion, the adverse effect of which is ultimately borne by the grower.

Likewise, poor or ineffective regulation in the absence of effective constraints can also result in unfavourable economic outcomes for Australia. This is particularly the case where the interests of the monopoly asset holder diverge from those of the users of services provided by the monopoly assets.

## **APPENDIX 1**

### **CBH's submission to the Agricultural Competitiveness Issues Paper, April 2014**



# Response to the Agricultural Competitiveness Issues Paper

Ensuring Western Australian grain growers remains  
internationally competitive

April 2014

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## INTRODUCTION

Co-operative Bulk Handling Limited ("CBH") welcomes the Federal Government's focus on the issue of agricultural competitiveness as a means of providing a platform for enhancing the contribution of agriculture to economic growth, employment creation and national prosperity, through increased innovation, productivity, investment and trade.

CBH is pleased to provide this preliminary input into the formulation of a Government White Paper that is seeking to address the issues that are in line with the co-operative's own purpose; to create and return value to grain growers of Western Australia.

While this submission responds to the matters raised in the Issues Paper (specifically those that are relevant for CBH), CBH's submission is shaped by a range of key themes that remain fundamental to the prosperity of not just the co-operative and its grower members; but the broader grain industry. More particularly:

- The need for a prevalent policy and investment framework that ensures wherever possible that the farming sector (in this instance - grain growers) can be competitive with producers from other international origins of supply;
- The importance of ongoing investment that increases the sustainability and profitability of primary producers. This includes an understanding of how crucial it is for growers to have access to supply chain infrastructure that transports grain efficiently and effectively to local and international markets;
- An understanding that agriculture and primary production must be supported by strong and vibrant regional communities; and
- The grain industry at a national level is diverse (geographically, agronomically, commercially and in export markets). It is critical that Government undertakes to consult as widely as possible across the grain industry before considering policy, regulation or decisions that may impact the industry.

## BACKGROUND - THE CBH GROUP

Co-operative Bulk Handling Limited ("CBH") is a unique organisation with a history almost as long as the grain industry it serves. The co-operative's commitment to maintaining a partnership with its Western Australian grain grower members has helped build an industry that has been the backbone of the State's rural economy since the beginning of the bulk handling system 80 years ago.

This partnership has also been the basis of CBH's strength and success.

CBH has constantly evolved, innovated and grown with operations extending along the value chain from grain storage, handling and transport to marketing, shipping and processing. Now Australia's biggest co-operative and a leader of the nation's grain industry, CBH is controlled by approximately 4,200 grain growers.

The co-operative exists for their benefit and the advancement of the grain industry in Western Australia.

CBH currently employs around 1,000 permanent employees supported by up to 2,000 casual staff during the months of harvest. These employees are located across the co-operative's ten regional offices, 195 receival site locations, four ports, engineering workshops, representative offices in Melbourne, Hong Kong, Tokyo and Portland (USA) and a head office located in West Perth.

### The co-operative approach

As a co-operative, rather than being motivated by profit and shareholder dividends, CBH seeks to invest in supply chain infrastructure and undertakes its business operations in order to ensure Western Australian grain growers are part of an efficient, well managed supply chain that contributes to their farm-gate returns. For example:

- In 2010/11 CBH took the decision to pursue enhanced above rail efficiencies by investing \$175 million in new rolling stock (locomotives and wagons) to be operated by a new above rail operator for the dedicated service of grain haulage in Western Australia. These arrangements provide a higher level of reliability, enhanced usage rates and greater productivity and have had a significant impact on the efficiency of the rail task. During the 2012/13 harvest, CBH reduced rail freight rates to growers by an average of seven per cent;
- CBH's Grower Rebate Program allows growers to enjoy a reduction in storage and handling fees on the basis of their patronage with CBH Group. In 2013/14, growers enjoyed a rebate on the storage and handling fees up to \$2.60 per tonne, which promotes their competitiveness in the industry;
- Despite a very challenging cost environment, (labour costs alone have risen between five and six per cent in 2012/13) CBH has been able to maintain storage and handling fees at a consistent level in all but one of the past four years; and
- On the back of ongoing investment in the storage and handling system, the CBH network is the most efficient, and the lowest cost, grain storage and handling system in Australia. During 2013 alone, \$155.2 million was spent on capital expenditure and maintenance activities throughout the network.

## **The grain industry into the future**

CBH and the growers of Western Australia are aware of the many future challenges to grow and market crops profitably. Despite CBH's efforts to provide enhanced service at the lowest price, long term trends in inputs, yield, supply chain costs, pricing and new competitor origins are having an increasing impact on farm profitability (and sustainability) throughout Western Australia.

There have been many reports on the 'Asian Century' bringing new prosperity to the region and creating unparalleled demand for Australia's raw materials and food. While this is an exciting and reassuring sentiment, it is by no means certain that Western Australian grain growers will benefit from this. Indeed, such an increase in demand and prices has to some degree just stimulated production from other locations which are often assisted by lower input costs, higher yields and new investment in supply chains to the market.

The more far-sighted reports suggest that the grain industry needs to look to ways that the Australian grain production and export industry can become more integrated and efficient, so it may benefit over the long term from growth in Asia.

It is CBH's view that growers must play a key role in that search for productivity and efficiency along every step of the supply chain; from the delivery of wheat seed on-farm through to the sale of flour into Asia.

## **RESPONDING TO THE ISSUES PAPER**

In each of the nine "Issues Snapshots" CBH has limited its response to those questions that are relevant to the CBH business (storage, logistics, marketing and processing).

This submission does not respond directly to those matters that might affect CBH's individual grower members in the context of their respective farming operations; as these will be responded to by individual grain growers and their representative groups.

## 1.0 ENSURING FOOD SECURITY IN AUSTRALIA AND GLOBALLY

### 1.1 Do farmers have access to timely, relevant and accurate information to fully inform production decisions to meet domestic and global food demands?

The grain industry often considers information in a broader context incorporating two key areas:

- Information that helps to inform production decisions, such as signals from the market including customer demand for specific grain type and quality; and
- Information that might assist growers to be suitably informed regarding price (and pricing) including information and data regarding grain held in store (unsold volumes, grain quality etc).

#### Information that assists in informing production decisions

The ideal value chain is often described as one where growers and their customers are inextricably linked and where growers' planting and cropping decisions are informed directly by the demands of their customers (locally and internationally).

The reality is often a little different; partly because most grain growers will make planting decisions on the basis of agronomic factors and resulting gross margins (what grain type can deliver the highest yield for their particular geography). While factors such as attendant logistics, such as storage services available and the requirements of customers remain important, a grain (or a specific variety of a grain) and its capacity to be agronomically productive will often be the primary consideration.

The ability of value chains to convey demand signals to grain growers will always be inhibited by the capacity of those chains to make a timely response. As an example, plant-breeding programs can often take decades to produce new varieties suitable for commercial propagation. Striking a balance between markets (grain processors) communicating a desire for growers to produce particular grain varieties, qualities and volumes and a growers' capacity to make an agronomic and financial return on those signals is the very essence of world grain markets.

CBH's investment into its Asian flour mills is a prime example of an organisation seeking to bring growers and their processing customers closer together. As a result of CBH holding a 50 per cent stake in six flour mills in Indonesia, Vietnam and Malaysia, growers can receive direct and transparent information around consumptive trends and quality requirements from these markets (such as increased demand for high protein milling wheat) and as a consequence make more informed planting/cropping decisions.

These specific examples aside, it is contingent for organisations, such as CBH, operating in global grain markets to undertake and facilitate an effective link between growers and their customers (rather than expecting a statutory or regulatory entity to undertake this function). Information such as seasonal wheat quality data, testing and functionality traits that CBH (along with other marketing and trading organisations) convey to their local and international customers forms a critical component of the competitive grain marketing landscape. By extension, an exporter's accurate communication of this information helps ensure not only their own standing and performance in the marketplace but the ongoing integrity and strength of the Australian wheat "brand".

Commercial entities seeking to market and export Australian grain (acting as a link between growers and their markets) will be absolutely cognisant that this brand must be managed and sustained into the future.

Despite this predisposition for the natural forces of world grain markets, CBH considers that there are opportunities for Government to play a role in ensuring integrity and function of the Australian grain industry such as supporting the role that Wheat Quality Australia ("WQA") plays in the area of wheat variety classification, in particular the function of promoting the class structure for Australian wheat.<sup>1</sup>

CBH considers that beyond this point, the responsibility of wheat variety classification and the broader function of creating a link between grain growers and their customers, must reside with the key marketers of Australian grain.

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<sup>1</sup> A key challenge for WQA is to finalise a longer-term funding strategy to which CBH understands GRDC and GTA are working to resolve.

## Access to accurate information to assist pricing decisions

There is little doubt that growers are accessing increasing levels of information to assist with their marketing decisions. In a recent survey of CBH grower members, 80 per cent of respondents listed online price discovery mechanisms as their first choice for grain pricing information. With this type of trend, CBH believes there is sufficient evidence that the market is moving to fulfil its information needs and that there is no overarching requirement to legislate for information provision.

Since the deregulation of Australian grain industry (wheat at a national level and coarse grains at the state level) there has been discussion about whether this flow of information is being appropriately coordinated. One example is the extent to which the level of publicly-accessible stocks information should be increased (volumes and quality details for growers' unsold grain held in store) and whether the release of this information would assist growers to make pricing and marketing decisions.

CBH notes the recent work undertaken by the Wheat Industry Task Force and is supportive of the conclusions outlined in the 2013 discussion paper that:<sup>2</sup>

- *... based on the reports considered by this paper, there does not seem to be obvious market failure resulting from the information that is currently available, even if this information must be paid for.*
- *... members believe that, as the Australian wheat export market progressively moves towards full deregulation, there is an increasing range of tools and information available for growers, and other industry participants, to manage risk, market their grain, and get the best price.*
- *The taskforce acknowledges that some industry participants are calling for stocks information held in BHC systems to be disclosed on a detailed level. However the taskforce believes such a requirement would potentially provide an incomplete picture of the actual stocks situation by not capturing those stocks held by other commercial operators and on-farm.*
- *The taskforce found that there was no evidence that growers would obtain a material benefit from an increased level of market information, including stocks. Through the CIE report, the taskforce found that a deficiency of stocks information was not placing Australian growers at a significant market disadvantage, with price instead being driven predominately by global market forces.*
- *Evidence from Viterro grower questionnaires suggest growers have little interest in providing their stocks information for public release. This suggests that growers surveyed do not see increased availability of disaggregated stocks information as critical to their business decisions. This is supported by the GHD Ltd observation around price being the most critical factor affecting marketing decisions. This price information is readily available on a daily basis.*
- *The taskforce noted that, since the conclusion of targeted government and industry funded stocks information publication, the industry has been through the 2012 harvest and most of the marketing period for that crop. The taskforce is unaware of any major disruptions to the effective operation of the wheat export market during this period.*

As a co-operative owned and controlled by the growers of Western Australia, CBH has raised reservations during industry consultations regarding proposals to force disclosure of additional stocks information beyond current provisions.

CBH does not believe that growers would truly benefit by allowing details of unsold stock information held in bulk handling systems to be disclosed to the market.

Grain growers have a naturally "long" position in the market; that is growers produce a crop and are then obliged to market that grain over the course of the year. In export dependent states such as Western Australia (and to a lesser degree South Australia), the notion that the release of information pertaining to grain held in store (specifically information relating to tonnage, grade and grain quality) would somehow give growers "market power" is not supported by any evidence and consequently makes very little sense.

<sup>2</sup> Wheat Industry Advisory Taskforce 2013; A preliminary assessment of wheat export industry stocks information requirements - Page 17

Ultimately the price of grain destined for the export market is affected by the volume of grain in the global market that is available for trading, of which Australian grain is a small factor. It is information about grain production in foreign jurisdictions that drive the fundamentals of global grain pricing, and the Australian domestic price will respond to surges in global pricing that would make it more attractive to export than sell locally.

Rather, and in most cases, it is the buyers (marketers and traders) who seek this information because it will allow more informed decision making as to the global supply of grain. Traders can reduce acquisition prices in knowledge of abundant supply and simply compete at "market values" when volumes are at more normal levels.

In CBH's view, it is the buyers of that grain (or those commercial entities at the periphery of grain marketing such as traders, brokers, consultants and organisations publishing information) that will gain the most by having a more thorough understanding of the volume of grain held in store; not grain growers.

The storage and handling system operated by CBH was developed by and for the growers of Western Australia. While growers certainly welcome the opportunity for local and international grain buyers to access their grain via the CBH system, up until the point of sale, the grain and its attendant information remain the commercial property of growers'.

## **2.0 FARMER DECISIONS FOR IMPROVING FARM GATE RETURNS**

### **2.1 What alternative actions or measures by governments, farmers or others would result in improved financial performance at the farm gate?**

There is little doubt that long- term trends in inputs, yield, supply chain costs, prices and new competitor origins are having an increasing impact on farm profitability. One of the key current challenges, certainly for the growers of Western Australia is that they have access to supply chains that enable them to transport their grain to international markets effectively and efficiently.

To this end, and as outlined in sections 3.1 and 8.1, Government can assist in this process by ensuring an appropriate policy framework exists in Australia that strikes a balance between creating an incentive for investment by allowing adequate returns versus ensuring market participants have access to essential infrastructure (specifically that which cannot be duplicated) at a reasonable rate of return. In the absence of a true monopoly asset, the market is the most efficient way to determine an efficient allocation of assets and to provide competition that values an Australian grain grower's agricultural products.

In determining whether and how to regulate access, the relative incentives and constraints on participants needs to be carefully considered. Attention must be paid to the identity of benefiting stakeholders in determining whether regulation is needed to offset commercial imperatives that would otherwise harm grain growers. Governments should facilitate and encourage stakeholders who re-invest into the Australian supply chain and have an ongoing focus on driving productivity improvements to ensure the sustainability and profitability of Australian agriculture.

As outlined in section 7.1, CBH considers it incumbent on Government to generally aim to minimise supply chain regulation as it leads to increased costs, inertia, inefficiencies and market distortion, the adverse effect of which is ultimately borne by the grower.

Likewise, poor or ineffective regulation in the absence of effective constraints can also result in poor economic outcomes for Australia. This is particularly the case where the interests of the monopoly asset holder diverge from those of the users of services provided by the monopoly assets.



## 3.0 ENHANCING ACCESS TO FINANCE

### 3.1 How can foreign investment best contribute to the financing and productivity growth of Australian agriculture?

CBH is not opposed to foreign investment. The Australian grain industry, like any sector, needs access to appropriate levels of capital to facilitate industry expansion and growth. However with foreign investment comes the requirement to understand an investor's commercial goals and the extent to which these are complementary to local industry.

As a case in point, the 49 year lease, which expires in 2049 for the Western Australian Grain Freight Rail Network ("WAGFRN") is currently held by various Brookfield entities and operated by Brookfield Rail; part of the Canadian based Brookfield Asset Management Group. While Brookfield's involvement has been welcomed by the Western Australian State Government, it seems Brookfield's commercial objectives are increasingly at odds with the users of the WAGFRN; the growers of Western Australia and the States \$3-4 billion grain industry.

Brookfield Rail and the growers of Western Australia have fundamentally different positions regarding the operation of the WAGFRN. Brookfield is seeking to operate the rail network in order to maximise profit on behalf of its shareholders notwithstanding that its profit maximisation inflicts a comparatively greater economic loss on the Western Australian economy. Meanwhile, the growers of Western Australia, as users of the track, are deprived of the most efficient and effective transport network possible in order to transport grain to their local and international markets.

It has become increasingly obvious that these two objectives are mutually exclusive; for example:

- Brookfield Rail is seeking to close those sections of the WAGFRN on which it is not making very high levels of profit, without surrendering them to an alternate user, on the basis that it can continue to increase revenue and margins from a reduced section of the rail network without increasing its own productivity. This behaviour is indicative of a true monopoly asset, as it can be run without regard to the interests of its customers. This closure is sought despite those assets remaining an important component of the local supply chain, the use of which would avoid increased costs being passed onto the community; and
- Rail performance standards are decreasing while access fees are increasing:
  - Below rail track access constitutes around 40 per cent of a grower's freight costs; average access cost are \$7-8 per tonne across Western Australia;
  - Western Australian grain growers are paying around four times what growers in eastern Australia pay for track access (on tracks that have higher speeds/mass );
  - Freight rates in Canada and USA are 30-50 per cent lower than Western Australia; and
  - Despite plans to close over 800 kilometres of track, Brookfield Rail has proposed a significant increase in access fees.

Into the future, it is incumbent on Government to develop policy frameworks that strike a balance between creating an incentive for investment (including foreign investment), and where that investment involves true monopoly infrastructure (railway lines and roads) ensuring that the users of that infrastructure have some assurance that they may continue to access those facilities with reasonable service and pricing. This doesn't mean a lack of returns, but it doesn't mean monopoly profits either.

When considering foreign investment the Government requires a clear understanding of an interested company's commitment to the Australian grain industry and their plans to enhance the operations of Australian growers and their rural communities.

## **4.0 INCREASING THE COMPETITIVENESS OF THE AGRICULTURAL SECTOR AND ITS VALUE CHAINS**

### **4.1 How might existing laws and regulations be changed to address any market power imbalances in the agricultural supply chain, without limiting prospects for global-scale firms developing in Australia?**

CBH does not, as a general rule, support increased supply chain regulation as it leads to increased costs, inefficiencies, inertia and market distortion; the adverse impact of which is ultimately borne by the grower.

CBH considers that it is incumbent on Government to develop policy frameworks that strike a balance between creating an incentive for foreign investment, and where that investment involves key export infrastructure (railways lines and roads), that the users of that infrastructure have some assurance that they may continue to access facilities with reasonable service and reasonable pricing (see Section 7.1)

Global scale firms can develop if investment into the Australian marketplace by local incumbents is not regarded by regulators as prejudicial to competition. Typically Australian firms compete against organisations that are many times their size who are able to leverage significant economies of scale and scope into Australia.

A situation that sees Australian firms provide fair and open access to their local supply chains whilst not receiving similar opportunity in foreign jurisdictions will guarantee that Australian firms, particularly those without the necessary economic and operational scale, will be gradually subsumed into larger multinational corporations.

## **5.0 ENHANCING AGRICULTURE'S CONTRIBUTION TO REGIONAL COMMUNITIES**

### **5.1 What impact does the growth of population in regional centres and the decline in more rural or remote townships have on farming businesses and the agriculture sector?**

The CBH Group has demonstrated a strong and sustained commitment to rural Western Australia and the broader grain industry by supporting a range of community projects and initiatives that contribute to regional capacity building.

Given the diminishing number of large organisations operating (and residing) in rural Western Australia and coupled with the company's unique co-operative structure, CBH's annual Community Investment expenditure of \$1.5 million is an important part of the co-operative's ongoing commitment to rural Western Australia.

However, diminishing rural populations remain a major factor to be addressed by the Western Australian grain industry, particularly to ensure it can source supplies of labour that is sufficiently skilled both now and into the future.

To address this, CBH would ask the Government to consider:

- Developing incentives for organisations to invest in rural areas and/or to locate infrastructure (including administrative resources) into regional communities;
- Supporting the development of key infrastructure in regional centres;
- Consulting with key organisations currently operating or located in regional Australia to ensure the opportunity for enhanced collaboration in capacity building efforts; and
- Assisting with building an enhanced understanding amongst regional communities of the global environment in which they are operating.

## 6.0 IMPROVING THE COMPETITIVENESS OF INPUTS TO THE SUPPLY CHAIN

### 6.1 What skills including specialised skills and training, will be required in the future and how can these be delivered and uptake encouraged and;

#### **How can we attract workers to agriculture – particularly in remote areas and promote career pathways for the agriculture sector, including models to enable younger farm workers to gain broader industry experience?**

A survey of the literature for the Australian agricultural sector (undertaken by the AGI)<sup>3</sup> suggests that the rural workforce is declining at a considerable rate. Allen Consulting (2012) suggest this could be as much as 30 per cent over the next ten years. It is considered that individuals working in the sector will increasingly require more intensive training and skills development and that fewer students based in rural areas are pursuing tertiary education, let alone studies in agricultural based disciplines.

Allen Consulting (2012) reported a national drop in the number of farmers and farm managers operating in Australia from 250,000 in 1997 to around 168,000 in 2011.<sup>4</sup> The issue is exacerbated in that while the number of people employed in farm related labour is declining, the level of skills required by those working on farm is actually increasing. In other words, a declining workforce needs an increased level of skills and training. In fact the demand for employees on farm is increasing at a rate of around 0.9 per cent annually and the nature of the skills required is diversifying into a range of emerging disciplines such as soil science, supply chain management, environmental management and expertise in carbon capture.<sup>5</sup>

So not only does the grain industry need to consider how it can find new employees, it also needs to ensure that those workers currently employed in the sector are suitably trained. This is further complicated by the generally increasing trend in work place complexity and that it is estimated that for every agriculture graduate, there are ten job opportunities from which they can choose.<sup>6</sup>

Of the labour currently working on farm, 50 per cent do not possess tertiary qualifications.<sup>7</sup> While this is not always necessarily negative, more important is the reality that this is around three times less than the broader Australian workforce; providing a considerably lower educational base from which the agricultural sector is required to build.

While not necessarily a lead indicator for future workforce capacity, 2008 was the culmination of five consecutive years of decline in tertiary enrolments in agriculture suggesting that things are getting worse not better. Also, the pipeline for students choosing to study agriculture is similarly diverted with statistics for the group that the grain industry might expect to be most predisposed to enter agriculture (or an agricultural based program) showing that just 36 per cent of qualifying Year 12's living in rural areas accept a place at tertiary institutions compared with 78 per cent in the metropolitan area.<sup>8</sup>

CBH supports the recent work being undertaken by The Australian Grain Institute Council ('AGI Council') (within the Grain Industry Association of WA) as part of its ongoing mandate to enhance and support capacity building throughout the Western Australian grain industry.

The AGI Council has quite correctly focused attention on Western Australia's ability to source suitable skilled labour to service current and future requirements across the value chain. And while there have been a range of studies examining the issue (the vast majority with a national and agricultural sector focus)

<sup>3</sup> The Australian Grain Institute Council ("AGI Council") is one of the seven (7) Councils of the Grain Industry Association of Western Australia ('GIWA'). The AGI Council's vision is to nurture and support sustainable capacity building within the grain industry.

<sup>4</sup> In this instance, agriculture refers to horticulture, grain, sheep and beef cattle farming; intensive livestock farming (dairy and poultry); other livestock farming (e.g. deer); broad acre farming; and services to the agriculture sector

<sup>5</sup> Allen Consulting Group: Rebuilding the Agricultural Workforce, Jan, 2012.

<sup>6</sup> Review of Post-Secondary Agricultural Education in Western Australia: Cowan, 2010

<sup>7</sup> Review of Post-Secondary Agricultural Education in Western Australia: Cowan, 2010

<sup>8</sup> Review of Post-Secondary Agricultural Education in Western Australia: Cowan, 2010

considering related areas such as how best to attract tertiary students into agriculture based disciplines, very little has been done in the way of tangible interventions for the local grain industry.

The efforts therefore of the AGI Council become a very important rallying point for the Western Australian grain industry to take action and address what will become an even more critical issue affecting all industry participants if left unattended.

The literature suggests unequivocally that:

- Rural workforce numbers are declining at a considerable rate;
- Those that are working in the industry will increasingly require more intensive training and skills development; and
- Traditional sources of labour and employment pathways for the industry are changing with fewer students based in rural areas pursuing tertiary education, let alone studies in agricultural based disciplines.

To this point, interventions proposed to enhance labour capacity issues cited throughout the literature have generally proven unproductive. Recommendations are often too expansive and become problematic to implement. There are constant references to the formation of national peak bodies, the establishment of advisory committees or the need for governing councils but tangible and effective action is rarely taken. Published plans often adopt language such as *promoting, supporting or encouraging* which while inclusive, rarely achieve immediate and measurable outcomes and the Western Australian grain industry desperately needs something more direct in its approach if it is to address diminishing workforce capacity in an effective manner.

The AGI Council is currently seeking support for the development of a new approach that:

- Makes the Western Australian grain industry the primary focus: There have been a number of studies into issues of workforce capacity across the Australian agricultural sector and while this research is certainly relevant and applicable, only the Western Australian grain industry will be truly focused and committed to solving the issue at hand;
- Create a resource or body that is solely responsible for addressing the issues: The Western Australian grain industry needs a single entity or resource that can truly represent the interests of its commercial stakeholders to coordinate a unified response to declining workforce capacity. A business plan outlining the structure and function of this organisation (membership based) should be developed as a priority, with support gained from key stakeholders both during and subsequent to the development of this strategy;
- Liaise with stakeholders at a national agricultural industry level but let the local industry drive the issue in order to ensure the local industry has the necessary clarity of purpose and intent that it needs to develop and deliver suitably direct and immediate solutions on the issue of decreasing workforce capacity.

It is proposed that should the approach be suitable for the Western Australian grain industry, the model may be extended to other agricultural sectors throughout Australia; and

- Ensure all key Western Australian grain industry commercial participants are part of the solution; garner support from all key commercial stakeholders operating in the Western Australian grain industry to establish a suitable resource to address pre-competitive issues such as workforce capacity. Once a business plan is endorsed and a resource is in place, the industry can then start addressing some of the specific issues (building on some of the work already undertaken) as a matter of urgency.

**6.4 What irrigation, transport, storage and distribution infrastructure are required to support the food and fibre production systems of the future and how should this be funded?**

See Section 8.1



## 7.0 REDUCING INEFFECTIVE REGULATIONS

### 7.1 How well do regulations affecting the industry meet their policy objectives?

CBH does not, as a general rule, support increased supply chain regulation as it leads invariably to increased costs, inefficiencies and market distortion that is ultimately borne by the grower. Increased regulation would only be appropriate where the market cannot effectively respond (as a result of a true monopoly) and a clear need is demonstrated.

An example of this is the current port access regulation regime where CBH, pursuant to the provisions of the Wheat Export Marketing Act 2008 ("WEMA"), is required to provide an access undertaking to the Australian Competition and Consumer Commission ("ACCC"), in relation to the export of wheat from its port terminals.

The expense of dealing with port access undertakings over the last five years have been substantial, and estimated to have cost the CBH and Western Australian growers between \$2.6 and \$3.5 million.<sup>9</sup>

Not only do the current port access arrangements cost CBH and the grain industry millions of dollars every year, they also restrict the flexibility with which port operators and grain marketing organisations can respond to changing market conditions, be it price or production. This lack of flexibility increases the likelihood of international customers seeking grain from alternative origins of supply.

An example of this is the length of time it takes to make changes to the capacity allocation method. Amendments can take over six months to implement and must commence as harvest finishes in order to be ready for the next harvest.

Since deregulation, CBH believes that the wheat export industry has matured to a level that allows for further removal of regulations. Major grain industry participants have been working towards a Wheat Port Access Code of Conduct for over two years in an effort to ensure the ongoing competitiveness of the industry.

Unfortunately the Code is yet to be implemented and has resulted in CBH having to seek an access undertaking in order for the agreements to be in place for September 2014, incurring further costs.

If the Wheat Port Access Code is approved, then there is the potential for duplicative and inconsistent regulation between any undertakings given and the Wheat Port Access Code, with all additional cost having an impact on growers at the farm gate.

CBH is keen to see the implementation of the code at a voluntary level and applied across industry to all port operators. Adding further regulation to the industry would be contrary to the current deregulation process and approach to the grain industry. It would also be contrary to the recommendations of the Productivity Commission.<sup>10</sup>

#### The need for level playing fields

Current regulation is creating considerable market power imbalances for Australian firms. As an example, CBH is required, pursuant to the provisions of the WEMA, to provide an access undertaking to the ACCC in relation to the export of wheat from its port terminals.

In contrast, global agribusiness Bunge recently completed construction of a grain export terminal at Bunbury (around 200km south of Perth) with a capacity to export 500,000 to 1 million tonnes per annum. Based in the United States, Bunge generates revenue of over \$60 billion, with over 35,000 employees operating in over 40 countries.

CBH understands that as a result of the particular operating arrangements at the terminal, Bunge is not obliged to provide an access undertaking to the ACCC. This creates an uneven playing field and distorts the regulatory position on the basis that:

- Bunge will be able to discriminate in how it acquires and exports wheat through its Terminal in a way that is favourable to Bunge compared to all other Australian and international wheat exporters operating export terminals;

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<sup>9</sup> CBH submission to Productivity Commission Inquiry into the National Access Regime April 2013

<sup>10</sup> Productivity Commission Inquiry No. 51, 1 July 2010 into Wheat Export Marketing Arrangements

- CBH, an Australian co-operative, will not be able to match Bunge's ability to provide variable terms for particular wheat types or customers because CBH must offer the same export terms to all parties; and
- Bunge will not have to spend the time or cost in negotiating a new export undertaking with the ACCC, something that CBH now faces due to the uncertainty associated with the Wheat Port Access Code of Conduct.

Further, there can be disparities between Government incentives for new entrants and those for incumbent operators. CBH is increasingly asked to expend money beyond the boundary of its sites such as "run off" roads and intersection alterations in view of forecast additional traffic, yet the same State Government is building a truck marshalling yard in Bunbury; a primary beneficiary of which will be Bunge's Bunbury Port.

## **7.2 What opportunities are there to reduce ineffective or inefficient regulation?**

As outlined in section 7.1, CBH considers it incumbent on Government to look to minimise supply chain regulation wherever appropriate as it otherwise leads to increased costs, inertia, inefficiencies and market distortion; the adverse effects of which are ultimately borne by the grower.

Given the significant investment in wheat export terminals in Australia (something mirrored in Canada as well) it is clear that wheat export terminals are not a true monopoly as they can and have been subject to bypass.

It is also recognised that integrated supply chains offer the opportunity to capture efficiencies (seen in the world's leading iron ore supply chains operating in the north west of Western Australia). With this in mind, Government should examine whether there are unnecessary regulatory impediments to the operation of the most efficient and effective grain export supply chains operating in Australia.

## **7.4 How do we coordinate across governments to reduce regulations whose costs exceed their benefits?**

In line with CBH's stance against increased regulation, and consistent with the recommendations of the Productivity Commission, CBH seeks a broader comment from Government on its longer term vision for regulation together with detail on its agenda for the continued deregulation of the grain industry, so that the industry has a greater degree of certainty for the future and may plan accordingly.

Likewise, when planning a supply chain operation, activities must be coordinated across three levels of government to avoid the potential for inconsistent application of regulations resulting from misaligned incentives (lack of consistent policies and determinants for heavy vehicle pathways are one example of potentially inconsistent application detrimentally affecting the supply chain).

## 8.0 ENHANCING AGRICULTURAL EXPORTS

### 8.1 How can industries and government respond to the key challenges and opportunities to increase or enhance exports?

Australian grain growers face the inherent challenge that while global demand for grain may be increasing, the nature of commodity markets means that this enhanced demand may not necessarily translate into higher prices. Take for example USDA data that suggests Asia will consume considerably larger quantities of wheat (Figure 1), but this increased consumption is unlikely to have any attendant short term impact on prices (Figure 2).

#### Asia will buy more wheat (20% annually)

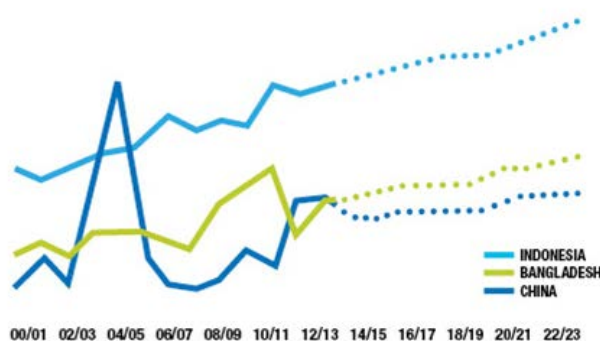


Figure 1 - Projected demand for wheat- 2023

#### No impact on prices in the short term

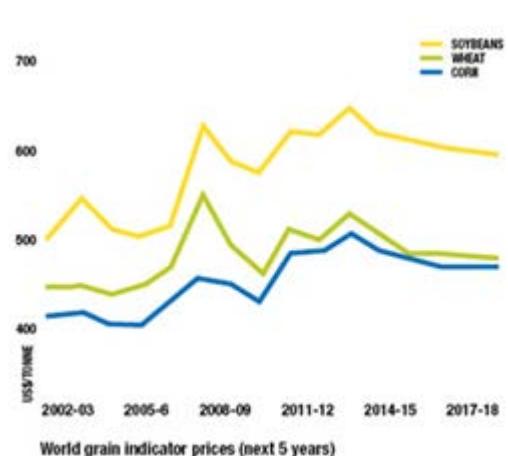


Figure 2 - Indicator of grain prices - five years to 2018

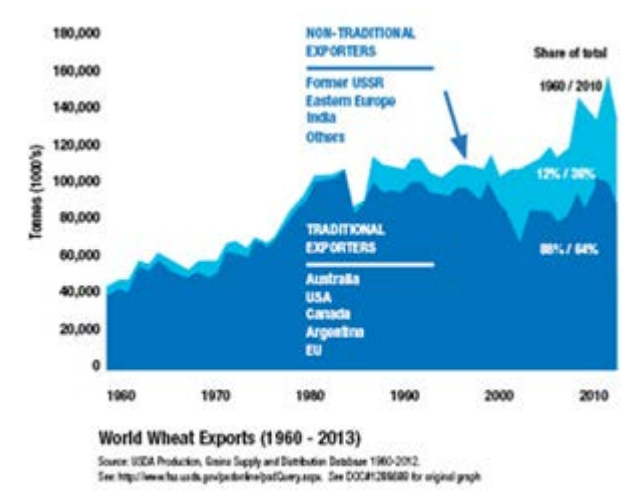
The inherently fungible nature of grain brings into starker contrast the importance of growers' minimising costs of production in a range of areas, including inputs (seed, fertilisers, pesticides), labour and supply chains costs, in order to ensure not just farm gate profitability, but in many instances, a farming enterprise's survival.

To this end, the fundamental premise of the CBH business is to ensure that Western Australian grain growers, who are entirely reliant on international markets to acquire their grain, have access to efficient inland supply chains (storage, handling, above rail operations and port infrastructure).

However, despite CBH investing more than \$600 million in up country infrastructure over the last ten years, and more recently an unprecedented \$175 million investment into rolling stock to enhance above rail operations to create a more efficient in-land supply chain that meets the shipping demand of international customers, Western Australian grain growers still face considerable challenges from other origins of supply.

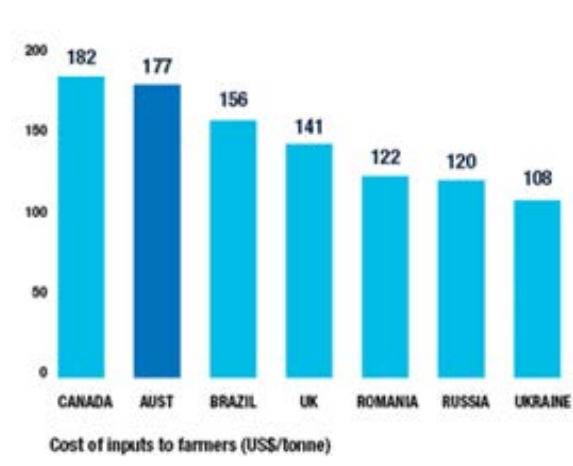
Take for example the increase in production from what are considered non-traditional producers such as Russia and the Ukraine who are gathering an increasing share of global markets; just 12 per cent in 1960 to close to 36 per cent 50 years later (see figure 3).

<sup>11</sup> Source - USDA Production Grains Supply and Distribution Database 1960-2012



**Figure 3 - Increase in non-traditional exporters**

Exacerbating the importance of this issue is that these origins of supply are operating from supply chains that are often half the cost of those utilised by Australian grain growers. In the context of Western Australia, while growers have access to one of the world's most efficient storage and handling networks, they are still at a considerable input cost disadvantage (see figure 4).



**Figure 4 - Comparative farm input costs**

## What is needed?

While CBH will always seek to invest in supply chain infrastructure and undertake its business operations to provide Western Australian grain growers with access to an efficient and well managed value chain, the co-operative would welcome increased collaboration with Government to ensure that:

- An environment is created that incentivises ongoing investment into agricultural supply chains that increases the sustainability and profitability of primary producers;

- There is a wider understanding and appreciation that agriculture is vastly different to other industry sectors (such as mining) given issues of weather, geography and global markets and must be treated differently if it is to provide an ongoing contribution to the national economy;
- Policy is developed that strikes a balance between creating an incentive for foreign investment, but where that investment involves monopoly infrastructure (railway lines and roads) that the users of that infrastructure have some assurance that they may continue to access facilities with reasonable service and reasonable pricing: and
- Supply chain regulation is minimised as it leads to increased costs, inefficiencies and market distortion that is all ultimately borne by the grower.

## 8.2 How can the government take best advantage of multilateral and bilateral trade negotiations (including through the World Trade Organization and through free trade agreements (FTAs)) to advance the interests of the sector?

In line with CBH's position that it does not support increased regulation as it leads to increased costs, inefficiencies and market distortion that is ultimately borne by the grower, the global "hold" on tariffs should be made permanent along with efforts for further trade liberalisation such as:<sup>12</sup>

- Addressing the way international jurisdictions apply local taxes which, when applied differently to specific products, become a form of tariff. As an example, Indonesia's VAT is applied to soybean imports differently from lupin imports for the local tempeh/tofu market (soybeans attract a zero VAT tax, whereas lupin splits from Australia attract a 10 per cent VAT tax). This added VAT on lupins makes it difficult for importers to offer product at a comparable price to soybeans (despite superior quality traits);
- Ensuring that quarantine regulations are not used to shape supply in certain food crops. The export of Australian canola into China from the regions around Albany in Western Australia and parts of South Australia have been banned due to concerns around a fungal pathogen (*blackleg*) which may create issues for domestic canola crop production; and
- The removal of restrictions for Australian companies selling grain into Iran. Currently Australian exporters are required to sell grain into the Iranian market via third parties due to tight controls on Australian trading companies, making it difficult to compete with grain from the US. US grain traders are able to sell into Iran via owned subsidiaries in European localities. Last year the value of the Iranian grain market was in excess of A\$300 million.

## 8.3 How can engagement between industry and government on market access priorities for Australian agricultural products be improved, including informing negotiations on FTAs?

CBH is supportive of FTAs and considers the optimal benefit can be generated when FTA's are undertaken as a joint Government/business collaboration that takes a broad approach and avoids the potential for unintended consequences. The live export ban to Indonesia, while not a trade agreement, is an example of where a policy decision undertaken in the context of one sector (live cattle exports worth \$200 million annually) can have significant implications for other key industries (annual wheat exports to Indonesia worth in excess of \$1 billion each year).

It is critical that the grain industry, often under-represented in previous FTA consultations is given suitable input and an opportunity for representation in future related delegations with international trading partners.

<sup>12</sup> Note that in the interests of expediency CBH has limited its opportunities for necessary trade liberalisation to the following three. As an organisation that exports grain across the globe, CBH has a range of further examples that can be tabled for further discussion as required.

## **9.0 ASSESSING THE EFFECTIVENESS OF INCENTIVES FOR INVESTMENT AND JOB CREATION**

CBH and the Western Australian grain industry has been assisted by the Federal Government's working visa policy that allows tourists (such as "backpackers") to extend their visas based on obtaining work in rural areas. However, further flexibility in the 457 Long Stay Business Visa process is required to attract and secure labour that can remain working with CBH and in rural Australia beyond this initial period.

The 457 Visa is a skilled migration program and only recognises a specific list of skilled labour roles; unfortunately, CBH's Receival Point Operator position was not recognised on the skilled labour list. As such CBH was required to establish a labour agreement to facilitate hiring employees under the 457 visa for remote locations where there is little or no available Australian labour. While the labour agreement has a further two years to run, the task of preparing for a further labour agreement is considerable and CBH seeks to have its Receival Point Operator and Plant Operator roles returned to the list of skilled positions eligible under the 457 visa program. Further we seek to have the qualification requirements reduced when the position being filled is in a rural or remote location.

As an example, the current skill and qualification requires a person to hold either a Certificate III in Transport and Logistics or a minimum of 5 years' relevant experience within the farming or transport and logistics industry. This strict requirement makes it difficult for CBH to maintain employment of staff that have worked on a casual basis for CBH (on a holiday visa) and have the proven skills and ability but don't meet the previous experience criteria.

Considering Certificate III qualification in other industries or giving weight to the willingness to work in rural and remote areas with a limited labour supply would increase flexibility and assist in maintaining our ongoing operations.



## **APPENDIX 2**

### **CBH's submission to the Western Australian Economics and Industry Standing Committee, April 2014**



# Submission to the Economics and Industry Standing Committee

Inquiry into whether the current lease arrangements and  
management of the Western Australian freight rail network  
facilitates or hampers state development.

April 2014

## EXECUTIVE SUMMARY

Rail freight is one of the key enablers for the efficient operation of the Western Australian grain supply chain. Any restrictions or limitation in track performance creates significant issues for Western Australian grain growers to supply their international markets.

The Western Australian Grain Freight Rail Network ("WAGFRN") is plagued with a range of issues such as axle weight limits and speed restrictions to the extent that the CBH Group ("CBH") now has significant concerns that the current approach to management by Brookfield Rail is neither sustainable nor is it best serving the interests of Western Australia's \$3-4 billion grain industry.

These concerns are based on a range of factors:

- The division of the freight carriage and network infrastructure parts of the WAGFRN diverged from the originally intended vertically integrated model. Whereas profits from below rail operations (arising from access fees paid by above rail users) were once reinvested into ongoing development of the below rail asset, today are being returned to shareholders as dividends;
- Aside from plans to close the Tier 3 lines, Brookfield Rail has in recent months announced a range of operational restrictions to the Tier 2 Miling line. These have caused considerable concern throughout regional Western Australia and a number of key stakeholders have joined CBH in questioning what other parts of the WAGFRN are to be closed;
- Despite Government committing \$164.5 million to fund required track maintenance, there are currently over 750 separate speed and mass restrictions placed on Tier 1 and Tier 2 line sections which hinder effective supply chain operations;
- Brookfield Rail has recently proposed a significant increase in access fees despite plans to close around 800 kilometres of track (which CBH estimates would provide considerable annual maintenance savings to Brookfield Rail);
- WAGFRN performance standards are decreasing while access fees are increasing. Western Australian grain growers are currently paying around 4 times what growers in eastern Australia pay for track access (that have higher speeds/mass);
- Freight rates in Canada and USA are 30-50 per cent lower than Western Australia. Despite this, Brookfield Rail are advocating to further increase access fees; and
- Brookfield's management of the WAGFRN coupled with confidential Lease arrangements and less than effective oversight has created precisely the monopoly environment that the original regulatory structure was seeking to avoid.

It is unacceptable to the Western Australian grain industry that the operator of the WAGFRN is able to let the below rail asset deteriorate to a point where it doesn't serve the economic interests of the State or the commercial requirements of the users.

Given these concerns, this submission makes a range of comments and recommendations for change to the way in which the WAGFRN is managed, how this management would be more appropriately overseen and how key users of the rail asset must have a greater say and influence into ongoing maintenance and performance including:

- To clarify the meaning and intended operation of clauses regarding 'fit for purpose' and that rail performance standards should meet the ongoing requirements of above rail users;
- Addressing flawed pricing methodology that sets floor and ceiling price on "gross replacement value" (that could see growers charged \$110 million per annum) and that provides a greater provision for a direct correlation between access fees and below rail performance;
- That Government consider ways it may reintroduce the surrender provisions contained in the original Lease that obliged Brookfield Rail to "surrender to Government" those line sections that it no longer chooses to operate (such as Tier 3 Line sections and the Tier 2 Miling Line);
- For third parties to be given the opportunity of operating those line sections that the lease holder (Brookfield Rail) chooses not to operate;

- Developing a collaborative approach to overseeing management of the WAGFRN which incorporates input from key above rail users in planning and prioritising maintenance and line upgrades into the future; and
- Increased transparency such as the terms and conditions of the Lease between Brookfield and the Western Australian State Government to be made public.

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## 1.0 INTRODUCTION

On 12 March 2014, the Economics and Industry Standing Committee resolved to inquire into and report on whether the current lease arrangements and management of the Western Australian Grain Freight Rail Network ("WAGFRN") comprising Tier 1, Tier 2 and Tier 3 lines facilitate or hamper state development.

In particular the Committee confirmed it would investigate:

- The recent strategic directions and policy decisions relating to the current network lease, particularly in relation to the low-traffic lines;
- The regulatory arrangements in place for the network; and,
- The management of the network by the Public Transport Authority.

### 1.1 CBH's view

For some time now, the CBH Group ("CBH") has been growing increasingly concerned that the current approach to management of the WAGFRN by Brookfield Rail is not sustainable. CBH is therefore strongly supportive of the inquiry initiated by the Economics and Industry Standing Committee.

In recent years, CBH has been persistent in its view that:

- There is a need for increased and effective statutory or regulatory oversight into the performance of Brookfield Rail from the Department of Transport ("DoT") and the Public Transport Authority ("PTA");
- Despite CBH now pursuing an access agreement with Brookfield Rail under the Railways Access Code (2000), considerable change is required to the Code to ensure that it provides a more appropriate regulatory framework governing oversight of the WAGFRN. This would include addressing the current flawed pricing methodology, providing a greater provision for a direct correlation between access fees and below rail performance and ensuring a more suitable definition of the term "fit for purpose";
- Aside from plans to close the Tier 3 lines, Brookfield Rail has in recent months announced a range of operational restrictions including the speed and weight limits on other sections of the WAGFRN such as the Tier 2 Miling line. This has caused considerable concern throughout regional Western Australia and a number of key stakeholders have joined CBH in questioning the manner in which the entire WAGFRN is being operated;
- Despite Government committing \$164.5 million to fund required track maintenance, there are currently over 750 separate speed and mass restrictions placed on Tier 1 and Tier 2 line sections which hinder effective supply chain operations;
- There is a need for increased transparency including the terms and conditions of the Lease between Brookfield and the Western Australian State Government being made public;
- As highlighted in the January 2013 report by the State Auditor General, the division of the freight carriage and network infrastructure parts of the WAGFRN diverged from the 'vertically integrated' model chosen by the original Sale and Lease Taskforce. This change meant that the lessee of the rail network no longer received profit from related entities carrying freight over those lines (with those funds no longer available for reinvestment into the below rail asset);<sup>1</sup> and
- There is a pressing need to address the various issues raised in the State Auditor General's 2013 Report regarding deficiencies in the management and lease of the WAGFRN.

### 1.2 The importance of the WAGFRN

The efficient operation of the WAGFRN including Tier 3 line sections forms a critical component of the grain supply chain helping to ensure Western Australia grain growers remain internationally competitive.

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<sup>1</sup> Western Australian Auditor General: Management of the Rail Freight Network Lease: Twelve Years Down the Track January, 2013.



Grain growers are facing increasing competition in the international market place. Regions such as the Black Sea, that operate from a very low cost base (often almost half that of the input costs incurred by Western Australian growers) means that our farmers more than ever need access to the most efficient supply chain possible.

This is not just about growers being a little more profitable, but in many cases ensuring their ongoing viability and survival.

Knowing this, the CBH Group recently made an unprecedented \$175 million investment into rolling stock to enhance above rail operations, part of the co-operative's ongoing commitment to create a more efficient in-land supply chain that can meet the shipping demand of Western Australia's international grain customers.

However the current management and operation of the WAGFRN is making the realisation of any efficiency generated in above rail operations problematic.

With access payments to Brookfield constituting in excess of 40 per cent of rail supply chain costs (currently around \$40 million annually) and with track performance in perpetual decline, the prospect of Brookfield Rail continuing to exert such ongoing and considerable control is simply not sustainable for the growers of Western Australia or the State's \$3-4 billion grain industry.

## **2.0 BACKGROUND – CBH GROUP**

CBH is a unique organisation with a history almost as long as the grain industry it serves. The co-operative's commitment to maintaining a partnership with its Western Australian grain grower members has helped build an industry that has been the backbone of the State's rural economy since the beginning of the bulk handling system in 1933.

This partnership has also been the basis of CBH's strength and success.

CBH has constantly evolved, innovated and grown with operations today extending along the value chain from grain storage, handling and transport to marketing, shipping and processing. Now Australia's biggest co-operative and a leader of the nation's grain industry, CBH is controlled by 4,200 Western Australian grain growers.

The co-operative exists for their benefit and the advancement of the grain industry in Western Australia.

### **2.1 Current access arrangements to the WAGFRN**

CBH has been in extensive, "in good faith" consultations with Brookfield Rail to reach an acceptable commercial arrangement to replace the current rail access agreement which expires in June 2014. Negotiations have focused around CBH achieving satisfactory access to train pathways, to ensure that general performance standards of the track are maintained and that access fees charged by Brookfield Rail are reasonable to the extent that the grain supply chain in Western Australia can remain competitive with other international origins of supply.

Despite four months of consultations, CBH and Brookfield Rail were not able to reach common ground in any of these key areas and it is considered highly unlikely that agreement can be reached by direct commercial negotiation. As an example, Brookfield Rail has proposed a significant increase in access fees despite exhibiting little commitment to addressing the large number of track restrictions it has imposed on the Tier 1 and Tier 2 line sections along with plans to close around 800 kilometres of track (which CBH estimates would provide considerable annual maintenance savings to Brookfield Rail).

CBH therefore took the decision to achieve an access agreement within the Rail Access Code (2000) overseen by the Economic Regulation Authority ("ERA").

In a broader context, it would appear that Brookfield Rail is seeking to operate the WAGFRN only if it can make monopoly profits on behalf of its shareholders while CBH (and the growers of Western Australia) as users of the track are seeking the most efficient and effective network possible (with a reasonable rate of return to the track operator).

It has become increasingly obvious that these two objectives are mutually exclusive.

### **3.0 THE RECENT STRATEGIC DIRECTIONS AND POLICY DECISIONS RELATING TO THE CURRENT NETWORK LEASE, PARTICULARLY IN RELATION TO THE LOW-TRAFFIC LINES**

#### **3.1 The separation of above and below rail**

CBH understood that the sale of Westrail in December 2000 to the consortium of Wesfarmers and Genesee and Wyoming (G&W) was to be a “whole of business” transaction with the above rail operation to be sold “freehold” (including all yards, depots and workshops) and the below rail business “leasehold” (on a 49 year lease).

Despite State Government intentions to maintain the business as a single above/below rail entity, in 2006 Wesfarmers Genesee & Wyoming took the decision to sell the Westrail business, splitting the rail assets into two. The above rail operations and rolling stock were sold to Queensland Rail National operating as “ARG” (now known as Aurizon) and the below rail (track lease) business sold to Babcock and Brown, (as WestNet Rail Infrastructure).

It is understood that following the 2008 Global Financial Crisis, Babcock and Brown went into receivership and was acquired by Prime Infrastructure. Prime Infrastructure (operating the below rail asset as WestNet Rail) was in turn acquired by Brookfield Infrastructure; part of the Canadian based Brookfield Asset Management Group. In 2011, WestNet Rail formally became known as Brookfield Rail.

While specific details remain private and confidential, given the considerable deterioration in track performance, it appears WestNet invested very little in maintenance to such an extent that in 2011, and after protracted debate, the State and Federal Governments agreed to fund necessary cyclical resleeper works (it being WestNet’s view that it was not liable to meet the cost of capital maintenance).

At the time of the 2000 sale, 30 million tonnes of freight were being transported across the network annually. In 2006, this figure was estimated to be closer to 56 million tonnes with growth over the next 2 years projected to take annual freight to over 80 million tonnes of freight across the network by 2016.<sup>2</sup>

As highlighted in the January 2013 report by the state Auditor General: Management of the Rail Freight Network Lease: Twelve Years Down the Track, the division of the freight carriage and network infrastructure parts of the rail freight business diverged from the ‘vertically integrated’ model chosen by the original Sale and Lease Taskforce. This change meant that the lessee of the rail network no longer received profit from related entities carrying freight over those lines (with those funds no longer available for reinvestment into the below rail asset).

Similarly, terms of sale and separation of above and below rail operations has created further challenges in removing the potential for flexibility in usage of rail yards and terminals. These key assets which would normally provide critical capacity for rolling stock to be “stabled”, provisioned or reconfigured into larger/smaller consists are in the hands of either Brookfield Rail or Aurizon (who have no interest in assisting each other or competing above rail providers) leaving little to no “common user” rail infrastructure to locate those rail assets not currently in use.<sup>3</sup>

#### **3.2 CBH’s fundamental concerns regarding the sustainability of the WAGFRN**

It is CBH’s very strong view that this divergence is one of the major factors in Brookfield’s claims that the Tier 3s are no longer viable and why CBH holds grave concerns for the long-term viability of the entire WAGFRN.<sup>4</sup>

Brookfield Rail has intentions to close the Tier 3 line sections on 30 June, 2014 and has in recent months announced a range of operational restrictions including the speed and weight limits on other sections of the WAGFRN including the Tier 2 Miling line (along with the existing unresolved operational restrictions that Brookfield Rail has in place throughout Tier 1 and Tier 2 line sections). This has caused considerable

<sup>2</sup> Western Australian Auditor General: Management of the Rail Freight Network Lease: Twelve Years Down the Track January, 2013.

<sup>3</sup> Brookfield Rail is endeavouring to place “parking / stabling” charges on CBH if a train has to park up in a load loop/siding.

<sup>4</sup> It is important to make the distinction given Brookfield’s suggestion that the lines are not viable. CBH would contend that operating the Tier 3s is certainly “viable”, just not profitable to the extent of Brookfield’s targeted return on capital.

concern throughout regional Western Australia and brings into question the manner in which the WAGFRN is being operated.

This planned closure of the Tier 3s and the various operational restrictions throughout the rest of the network provides a graphic illustration that the current approach to managing the WAGFRN (the Tier 1s and Tier 2s) is not sustainable; performance standards are decreasing while access fees are increasing. For example:

- Below rail track access constitutes 40 per cent of a growers' freight costs with average access \$7-8 per tonne across Western Australia;
- Western Australian grain growers are paying around 4 times what growers in eastern Australia pay for track access (that have higher speeds/mass );
- As an example, the Beacon to Burakin line section, despite being re-sleepered as part of the recent Government funding package still only allows for 30km/h operations for full trains;
- Freight rates in Canada and USA are 30-50 per cent lower than Western Australia; and
- Despite plans to close around 800 kilometres of track, Brookfield Rail has proposed a significant increase in access fees.

Brookfield Rail has indicated that they are willing to continue operating the Tier 3s but only with a substantial injection of capital from the Western Australian State Government of in excess of \$90 million. Even with this injection (and further increases in access fees) given recent trends, CBH fears that the result will be deteriorating track conditions and rail performance without any long-term sustainability.

### 3.3 SGNR and the decision to close Tier 3 line sections

The CBH Group was a willing and active participant in the Strategic Grain Network Committee's (on behalf of the Freight and Logistics Council of Western Australia) December 2009 report into the Strategic Grain Network Review ("SGNR"). At the time, the co-operative articulated "in principle" support for the report's main recommendation that future investment into the network should be undertaken in line with the longer term competitiveness of each particular line section (along with the classification of the plan for three tiers of line section categories).

This was over and above the report's primary recommendation to fund and undertake re-sleepering maintenance on the Tier 1 and 2 line sections (of \$164.5 million) and upgrading road infrastructure adjacent to Tier 3 line sections, which would be scheduled for closure (saving an estimated \$93.5 million in required rail investment).

When the value of all lines in the grain freight rail network was considered by the SGNR committee, it was noted that "*under no plausible circumstances could Tier 3 line investment be justified.*" However these evaluations and statements were all based on the less than optimal input, data and operating models used by ARG (now Aurizon) and WestNet Rail (now Brookfield Rail).

In 2010/11, following CBH's decision to appoint United States based Watco Companies Group to undertake above rail operations on its behalf and to invest \$175 million in new rolling stock (locomotives and wagons), it was considered many of the SGNR costings should be reviewed on the basis that CBH's new operating model for above rail operations will have fundamentally changed the original assumptions.

Despite the CBH Group's initial in principle support for the SGNR report, the changes and developments that have taken place in the Western Australian grain industry (arising out of CBH's above rail investment) are of such significance that they contradict some of the SGNR's key findings. Some of these developments since December 2009 include:

#### *Locomotives*

- CBH invested in new locomotives which deliver higher horsepower, with more efficient tractive effort than the old ARG grain locomotive fleet (which has an average operational age of over 35 years);
- These new locomotives provide considerable improvements in reliability, fuel savings, higher grain hauling capabilities and modern technologies that can greatly reduce train operating costs (e.g. auto stop/start - reduces idling costs over the old ARG grain fleet especially in the Merredin Feeder Line operations where the oldest and least reliable locomotives have historically been used);

- CBH have purchased three classes of locomotives to operate on the network in Western Australia standard gauge, plus two types of narrow gauge locomotive. The locomotives that will run on all 16 tonne per axle rated line sections, including the Tier 3 lines, will have a maximum axle loading rating of 17.33 tonnes per axle (note that this is the same maximum mass as a current concession that Brookfield has granted ARG to operate the “P” class locomotive across the network today, and has been in place for the last 20 years); and
- Locomotives are built to US Tier 2 emission standards and will reduce the future impact of carbon pricing on CBH growers compared to both ARG’s higher polluting fleet and competing road transport alternatives.<sup>5</sup>

### *Wagons*

- CBH have purchased state of the art wagon technologies including auto-hatch and discharge doors creating a safer and faster discharge unit over the current wagon fleet. The previous ARG Merredin Feeder lines’ wagon fleet utilised old converted coal wagons (XNW class), which only have a wheat payload of 38 tonnes per wagon;
- CBH’s narrow gauge wagons are new aluminium wagons with a wheat payload of 47 tonnes – a 21 per cent payload increase from the old ARG XNW wagons;
- The CBH wagons have a cubic capacity that would allow loading up to 19 tonnes per axle if capacity permitted;
- The CBH wagons are shorter in length allowing for a greater number to be loaded at many of the length restricted sidings; allowing more wagons, each with their greater capacities, resulting in significantly more tonnes per trip and at a reduced cost; and
- Testing of the wagons has shown significantly reduced track wear through improved design, therefore enhancing the rail network and reducing the need and costs for maintenance.

Two years on and with the introduction of such a considerable innovation in above rail operations, it is considered that the conclusions of the SGNR are no longer valid as they are based on out of date assumptions.

## **3.4 Current opportunity regarding the Tier 3s**

CBH has said on a number of occasions that:

- It is simply unacceptable that the below rail operator can “lock away” the Tier 3 rail track on the basis of Government funding not being available and that Brookfield can’t generate a monopoly profit;
- The co-operative’s overwhelming preference is to keep grain on rail and will utilise the Tier 3s if they are presented for use in an appropriate state, and that the access fees charged by Brookfield Rail make the asset competitive to use;
- Closure of the Tier 3s would strand millions of dollars of CBH’s key supply chain infrastructure such as rapid rail loading facilities at Kulin and Quairading; and
- With Tier 3 line sections scheduled for closure on 30 June, 2014, the growers of Western Australia desperately need a lasting and sustainable solution that can ensure their continued operation, not merely a stop-gap proposal by Brookfield Rail’s for extra Government funding every few years.

CBH considers that to operate the Tier 3s into the future, it is critical that they are managed differently and as a function of the proposed freight task. On this basis, CBH has developed an alternative approach that can sustain operation of the Tier 3 assets in a condition that achieves an acceptable and sustainable level of service and safety, while minimising maintenance costs throughout the asset’s useful life.

This approach provides a long-term solution for the continued operations of the Tier 3s as a vertically integrated network with open access to all above rail users.

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<sup>5</sup> CBH notes the Federal Government’s intentions to abolish the Carbon Tax.

By contrast, Brookfield's continued management of the Tier 3s will require a frequent "re-injection" of funds from Government as profits generated from track access are returned to shareholders rather than reinvested into track performance.

### 3.5 Surrender provisions

The opportunity for a lasting and sustainable solution for the continued operation of the Tier 3s has been hampered by an apparent decision to remove the provision contained in the original Lease that obliged Brookfield Rail to "surrender to Government" those line sections that it no longer chooses to operate (such as Tier 3 Line sections and the Tier 2 Miling Line at the end of 2015).<sup>6</sup>

Unfortunately and as outlined by the Auditor General (Page 9):

*"...Limited information is available to Parliament and the public regarding the lease of the network or its condition. The lease and its variations have not been tabled in Parliament, and no regulatory agency reports publicly on the condition of the network or its use."*

CBH would contend that this represents a serious issue in terms of oversight and would urge the Western Australian State Government consider ways to reintroduce the provision that would enable it to "take back" those line sections Brookfield are choosing not to operate.

The Auditor General goes on to stipulate (Page 35):

*"Placing the lines into care and maintenance while leaving them with the current lessee potentially obstructs prospective new operators from entering the market. This also benefits the lessee by reducing the likelihood of competition while allowing the lessee to retain the right to future economic benefit from disused rail line corridors. The uncertainty over whether the market can provide an alternative viable operator can only be fully resolved by testing the market, which PTA has not formally done. However, it has received unsolicited approaches."*

Given Brookfield's desire to close the Tier 3s, and the benefit operating those line sections could mean for the growers of Western Australia, CBH has sought (on several occasions) to reach an agreement with Brookfield for CBH to take on the operation of the Tier 3s by way of:

- Leasing the Tier 3 line sections direct from Brookfield (with the understanding that a sub-lease arrangement would require the imprimatur from the State Government);
- Leasing the Tier 3s from Government (on the basis of Brookfield surrendering those line sections to the Western Australian State Government); and
- An arrangement whereby CBH would operate the Tier 3 line sections on behalf of Brookfield.

Brookfield Rail has rejected all of these proposals.

## 4.0 THE REGULATORY ARRANGEMENTS IN PLACE FOR THE NETWORK

CBH would contend that the current lease arrangements hamper state development for a range of reasons as outlined below.

### 4.1 The terms and conditions of the Lease remain confidential

CBH, like the vast majority of key stakeholders are not, and have never been, privy to the Lease between Brookfield Rail and the Western Australian Government. As such, CBH is obliged to rely upon comments made by the Western Australian Auditor General in its January 2013 report which articulates a range of issues with the Lease and its management by the Public Transport Authority ("PTA").

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<sup>6</sup> Note that given that the terms and conditions of the Lease between Brookfield Rail and the Western Australian State Government remain confidential, CBH has no means of confirming that this provision has been removed.



Indeed the Auditor General was pointed in its concern regarding the inherent silence on details of the lease where it stated (page 24):

*“Parliament has had limited information regarding the condition of the network, partly because PTA is bound by a broad confidentiality clause in the lease, and partly because little information is required to be or has been made public by the other agencies with regulatory responsibilities in this area. Although Parliament has been partially informed about lease terms and conditions through various Ministerial statements, a full copy of the lease and subsequent agreements modifying the lease has never been tabled in Parliament, and only the first five-yearly track condition report in 2005 has been tabled.”*

CBH would argue that it is simply unacceptable that the community is not able to access a document that outlines the way in which a key public asset is to be used, maintained and offered to users. It is CBH's view that transparency is required when dealing with public assets, particularly when those public assets are managed by commercial entities. As is the case with other Government contracts (such as Serco's contract to manage the new Fiona Stanley Hospital) these contracts must be fully disclosed to stakeholders.<sup>7</sup>

#### 4.1.1 The Lease is not protecting the ongoing condition of the WAGFRN

Despite intentions that at the conclusion of the lease period, the WAGFRN is handed back to the Western Australian State Government in an appropriate “fit for purpose condition”, the State Auditor General suggests (Page 6):

*“The lease of the rail freight network was set up to do a number of things... It was also intended to ensure that the State's asset is maintained and handed back in a fit for purpose condition, and to allow the State to pursue its policy objectives and protect its interests, particularly where those may diverge from the operator's commercial interests.”*

Further comments by the State Auditor General (page 7):

*“The condition of the narrow gauge lines used primarily for carrying grain has degraded. The ‘grain lines’ have required substantial government funding to remain in service. Two of the uneconomic ‘Tier 3’ grain lines have been placed in care and maintenance, and without further government funding, the remaining eight are likely to be taken out of service after 2013.”*

CBH would suggest that on present operations, the WAGFRN is certainly not of the same standard as when the lease period commenced in 2000 and that there is a requirement:

- To give further consideration whether the current model for management of the WAGFRN is sustainable and whether change may be required; and
- For Government (and the PTA) to adopt a collaborative approach by consulting with above rail users in order to define a more appropriate, less ambiguous “fit for purpose” standard for each line section.

#### 4.1.2 Managing the lease with the envisioned “light touch” has not worked

As outlined by the Auditor General (page 9):

*“The lease anticipated a relatively ‘light touch’ role for government in managing the lease, which is appropriate given the State's original objectives. The State retains a range of risks related to market conditions, the lessee's commercial interests, and the policy of the government of the day. These risks require proactive monitoring and management.”*

*Available documentary evidence indicates that an additional \$400 million investment commitment was made by the successful bidder during the tender process, but this was not incorporated in the lease. There is no clear record of why.*

*PTA has not had a contract management plan in place for the lease and has not yet completed a structured risk assessment, or formalised its ongoing objectives for the lease. This increases the risk that reactive decisions in response to individual issues may adversely affect the State's interests over the remaining 37 years of the lease.”*

<sup>7</sup> - [http://www.serco-ap.com.au/media/46101/facilities\\_management\\_services\\_contract.pdf](http://www.serco-ap.com.au/media/46101/facilities_management_services_contract.pdf)



Given these statements, CBH would suggest that there is a requirement:

- For Government to investigate why this \$400 million investment commitment was not included in the amended Lease and provide stakeholders with an appropriate explanation regarding why this occurred;
- To understand why a physical track inspection and audit of the track was undertaken in 2005 but not 2010. Why was this oversight allowed to occur and when will this inspection be undertaken and the report tabled;<sup>8</sup> and
- To consider what changes are required to ongoing oversight of the Lease that would assist the PTA to ensure the WAGFRN does not continue to degrade.

#### 4.1.3 Unclear definition of “fit for purpose”

Similar to those issues raised in section 4.1.1, CBH has concerns that the Lease definition of “fit for purpose” is not satisfactory and that the attendant ambiguity created is jeopardising the state and performance of the WAGFRN.

The State Auditor General raised similar concerns (Page 9):

*“The lease contains ‘fit for purpose’ performance standards that are intended to ensure the network remains in the condition required by the State and by users of the network. There are a number of possible interpretations of ‘fit for purpose’ as used in the lease. Based on internal legal advice, PTA has interpreted the lease so that the only usable standards are the Initial Performance Standards, set at year 2000 levels. This is a substantial reduction of the ‘fit for purpose’ obligation, as it does not include the requirement to meet the needs of rail users or reflect changes in rail technology. This increases the risk of a gap emerging between the required standards and the needs of rail users, and the risk that at the end of the lease in 2049 the network will be required to be in essentially the same condition it was in 2000.”*

Further comments from the State Auditor General (page 10):

*“The lease anticipates a review of performance standards every five years across the network, seeking to ensure that the standards remain in step with market needs and changing technology. The use of this mechanism is constrained by PTA’s interpretation of ‘fit for purpose’, risking a situation where the five yearly track condition reviews assess the condition of the network against out-dated requirements.”*

CBH would suggest that there is a requirement:

- For Government to consider whether it is comfortable that the licensee appears able to let the WAGFRN asset deteriorate to a point where it doesn’t serve the State’s interests or the commercial requirements of the users;
- To clarify the appropriate accounting method for applying costs to ‘uneconomic’ lines;
- To clarify the meaning and intended operation of clauses regarding ‘fit for purpose’ and the related adjustment of rail performance standards that would ensure standards stay up to date. This process should be undertaken with both the operator and above rail users of the WAGFRN; and
- For the PTA as part of the contract management plan, consider and formulate a strategy in relation to end of lease issues.

#### 4.1.4 A lack of transparency in the management of the WAGFRN

CBH has a range of questions and concerns regarding the manner in which Brookfield Rail undertakes management and maintenance on the WAGFRN.

The Auditor General stated that (page 11)

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<sup>8</sup> Though not confirmed, CBH understands that a “desk top” audit of the track may have been undertaken in 2010.

*“In the past 10 years, the lessee (Brookfield Rail and its predecessor WestNet Rail) has spent over \$2.4 billion on the leased railway infrastructure...”*

Given such a considerable quantum of expenditure, CBH would seek:

- An audit as to where, when and how this \$2.4 billion has been spent;
- Given this expenditure, why are users of the WAGFRN seeing a decline in track performance? As an example in August 2013, Brookfield Rail advised CBH (and its above rail operator Watco) that they are putting in place a range of restrictions for the WAGFRN including:
  - Special Train Notice #256; which took effect immediately, advising that due to deteriorating track condition, double consist trains in both empty and loaded consists on nominated line sections are no longer permitted to operate. The STN refers to not just logistically important Tier 3 line sections but also the Tier 2 Miling to Bolgart line section;
  - Whereas CBH would traditionally operate a 52-54 wagon “dual locomotive” consists on this Tier 2 line section, the STN forced CBH to only run 1 locomotive and a train consist of 26-28 wagons. Watco (and CBH) are now exposed to considerable additional cost and logistical issues to move the same tonnage to port;
  - It is understood resleepering of this line section was undertaken in 2004 with the then track operator utilising a 1 in 2 sleeper replacement methodology similar to that adopted by Brookfield Rail today. That this line section is now subject to such considerable deterioration in track condition that Brookfield Rail have announced the line will be placed into care and maintenance at the end of 2015, reinforces CBH’s concerns that the current approach to management of the entire WAGFRN is not sustainable; and
  - This is despite Brookfield Rail’s obligations under clause 6.1 of the Operational Track Access Agreement requiring Brookfield Rail to maintain a section of the Network (i.e. the Miling to Bolgart section) at all times to the general standard of that section at the Commencement Date. The issuance of the STN is a clear departure from this standard.

This lack of transparency and oversight regarding the Lease has further issues for Western Australian grain growers.

Brookfield Rail have proven adept at dealing with negative developments regarding the network and the manner in which it is managed to ensure that any blame for increases in cost or diminished levels of performance can be sheeted across to other stakeholders; not Brookfield Rail.

For example, it is suggested that Brookfield Rail, when initially seeking closure of the Tier 3s (in 2009/1010 and around finalisation of the SGNR process) placed increasingly onerous and questionable operational restrictions on above rail operations (such as speed and weight restrictions). Track users were forced to question the ongoing functional viability and use of the Tier 3s, rather than Brookfield having to formally close those line sections.

Consequently a number of key stakeholders suggested incorrectly that it was CBH that chose not to run trains on the Tier 3s, rather than Brookfield Rail seeking to close those line sections. It is suggested Brookfield Rail is seeking to initiate a similar process with the STN for the Tier 2 Miling line.

CBH would:

- Ask how the Western Australian grain industry can operate with any degree of competitiveness when the State’s below rail operator can simply and arbitrarily announce a restriction on key line sections causing considerable operational and financial imposition for the Western Australian grain industry;
- Question how is it that Brookfield Rail offers nothing in the way of compensation or operational alternatives when these unilateral track restrictions are imposed;
- Suggest that with this Miling Line STN, Brookfield Rail is seeking once again to place increasingly onerous and questionable operational restrictions on above rail operations forcing track users to question their ongoing functional viability, and so Brookfield can avoid any accusation that they are closing those line sections; and
- Propose that it seems remarkable that similar line sections in South Australia’s Eyre Peninsular can operate “triple locomotive” consists on line sections of a standard considerably less than that of the Western Australian Tier 3s (NG light axle lines). For this reason CBH, grain growers and

the Western Australian grain industry find it difficult to understand that operational restrictions are required due to issues with safety and asset preservation (as advised by Brookfield Rail).

#### 4.1.5 A lack of protection against monopoly powers

As outlined by the Auditor General (page 16):

*“The intended privatisation of the freight rail network by lease was supported by a regulatory structure to prevent the abuse of monopoly positions in the market, to guarantee that all freight carriers could use the network at fair prices, and to ensure the safe operation of the network.”*

CBH would contend that:

- Brookfield's management of the WAGFRN coupled with confidential Lease arrangements and less than effective oversight has created precisely the sort of monopoly environment that the original regulatory structure was seeking to avoid. For example, there would appear to be very little provision for a direct correlation between access fees charged by Brookfield Rail and level of performance in the below rail asset;<sup>9</sup>
- Given this original intention has now been compromised, CBH would urge Government to develop more appropriate safe guards to ensure that the standard of the track is brought back to a reasonable standard; and,
- This would include a need for consideration of amendments to the Rail Access Code to ensure an appropriately balanced future for the grain industry (see section 4.2).

#### 4.1.6 A lack of ongoing monitoring of maintenance and performance

The Auditor General outlines (Page 17):

*“The lease enables PTA to monitor the lessee's compliance with the lease, to ensure the State's asset is maintained in a fit for purpose condition. The lease requires the lessee to provide PTA with five-yearly independent network condition reports, followed by maintenance plans that address issues raised in the condition reports. PTA may also seek evidence from the lessee that planned maintenance has been satisfactorily completed.”*

CBH considers that there are a range of issues that must be addressed to ensure that the WAGFRN can be a key component of the Western Australian grain supply chain into the future, in particular:

- Consideration to what additional powers the PTA needs to ensure it can provide more effective oversight;
- For the PTA to adjust its monitoring over time and where appropriate to reflect emerging risks on specific lines, such as those at risk of becoming uneconomic, receiving government funding, or needing major upgrades; and
- For the PTA to collate and update all lease-related documents, variations, maps, plans, and performance standard agreements in a comprehensive lease management volume, to provide a transparent view of the lease and the network.

#### 4.1.7 The need for the immediate surrendering of uneconomic line sections

The Auditor General stated (Page 18):

*“To avoid the unplanned deterioration of these marginal parts of the network, the lease sought to ensure that the operator of the standard gauge track would have ‘a financial or legal interest in the continued maintenance and operation of the narrow gauge track’, to the extent that this remained government policy. The lease achieves this through two main means: the inclusion, and ongoing adjustment of performance standards, and the application of a State-controlled process for the surrender or support of marginal lines.*

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<sup>9</sup> CBH is reminded regularly by Brookfield Rail when discussing Brookfield Rail's approach to pricing that *“It's not what it costs but what the market will bear that is the key driver.”*

*The ‘surrender’ option allows the State to use free market competition to find a more efficient operator for marginal lines. “*

This raises a number of very key issues:

- Brookfield Rail’s plans to close the Tier 3s and Tier 2 Miling Line section suggest that this original intention to “*avoid unplanned deterioration*” has now been compromised. Consideration is urgently required to consider what safe guards are appropriate to ensure that the standard of the track is brought back to a reasonable condition;
- The correct method for applying costs to assess whether a line is uneconomic and qualifies for State support is unclear. The absence of an agreed method increases the risk that more lines will be regarded as making a loss, increasing the potential requirement for further State Government funding (or line closures);
- What are the Government’s intentions regarding the ongoing management of the WAGFRN given the likelihood of further line sections falling into a similar state; and
- Why were the surrender provisions contained in the Lease that obliged Brookfield Rail to “surrender to Government” those line sections that it no longer chooses to operate (such as Tier 3 Line sections and the Tier 2 Miling Line) apparently removed? CBH would contend should this be the case that this represents a serious issue in terms of oversight and would urge the Western Australian State Government to take immediate steps to reintroduce this provision into the Lease.

The issue that the below rail operator having the capacity to choose to not operate a key State asset on the basis of a claim that it is uneconomic to do so represents a considerable strategic matter for the state of Western Australia in that an overseas company now has the capacity to influence the international competitiveness of a substantial Western Australian export industry.

#### **4.1.8 Longer term issues regarding management of the lease**

CBH notes comments made by the Auditor General (Page 36) regarding the need to consider the broader issues regarding management and oversight of the lease, in particular:

*“As the end of the lease approaches, the interests of the lessee and the State are likely to diverge. This is because, without an agreement to renew the lease, the lessee faces a commercial risk that the future benefits from its investments may flow to the State or to a new lessee, and this will affect investment and maintenance decisions by the lessee. This represents a risk to the condition of the network.*

*To manage this risk PTA needs to ensure that the performance standards are regularly updated to reflect the contemporary needs of rail users;*

*there is a potential incentive for the lessee to minimise the actual amount it has to place in escrow and to do this it may reduce spending in the years prior to year 45 to establish a lower baseline of maintenance spending. To manage this risk, PTA should ensure it is effectively monitoring maintenance and repair activity to detect any changes in patterns of activity.”*

Given these matters, CBH believes that it is critical that further consideration is given to:

- Whether the lease (and the separation of above and below rail operations within the WAGFRN) has contributed to a failure in meeting the ongoing needs of the market and to facilitate necessary investment;
- The implications for Parliament that it has received such little feedback regarding the fulfilment of the obligations under the lease. It must have further information if it is able to better address the question of fit for purpose and the Lessee’s obligations to manage and “hand back the track in an appropriate state;
- Given the previous question regarding “fit for purpose” (section 4.1.3) – whether the track meets the requirements of rail users or their attendant changes in technologies;
- The need for a collaborative approach (incorporating the input from above rail operators) to plan for maintenance and line upgrades over the next decade; and

- The PTA's planned "risk based approach" to ongoing management and oversight of the Lease is welcome. However inherent in a risk based approach is engaging with CBH as the primary consumer of the contracted services. CBH is yet to be contacted by the PTA in this regard.

## **4.2 Issues with the Railways Access Code (2000)**

In essence, CBH considers there is a requirement to make a range of changes to the Railways Access Code (2000) that would have as its core:

- Addressing flawed pricing methodology that sets floor and ceiling price on "gross replacement value" (that could see growers charged \$110 million per annum);
- Provides a greater provision for a direct correlation between access fees and below rail performance;
- Ensure a more appropriate definition of the term "fit for purpose";
- Ensure that the PTA has greater powers of oversight regarding the management of the WAGFRN. This would include ensuring the more frequent undertaking of track audits (as prescribed within the RAC);
- Allow track users (such as CBH) to have direct input into track maintenance priorities;
- For the terms and conditions of the lease between Brookfield and the Western Australian State Government to be made public;
- For third parties to be given the opportunity of operating those line sections where the lease holder (Brookfield Rail) chooses not to operate those line sections; and
- For the management and associated terms and conditions of the management of the WAGFRN to be undertaken in line with national guidelines such as that used by the Australian Rail Track Corporation ("ARTC").

## **5.0 THE MANAGEMENT OF THE NETWORK BY THE PUBLIC TRANSPORT AUTHORITY**

It is CBH's view that there is a requirement for the PTA to have increased oversight of the Lessee's management of the WAGFRN.

In line with several of the key themes raised in the 2013 State Auditor General Report (relating to PTA's management of the WAGFRN) CBH considers that management of the WAGFRN by the PTA could be enhanced:

- Clarifying the meaning and intended operation of clauses regarding 'fit for purpose' and the related adjustment of rail performance standards, to ensure standards stay up to date. This process should be undertaken with both the operator and above rail users of the WAGFRN;
- Developing a collaborative approach to overseeing management of the WAGFRN which incorporates input from key above rail operators in planning and prioritising maintenance and line upgrades over the next decade;
- Adjusting its monitoring over time and where appropriate to reflect emerging risks on specific lines, such as those at risk of becoming uneconomic, receiving government funding, or needing major upgrades;
- As part of the contract management plan, consider and formulate a strategy in relation to end of lease issues;
- To collate and update all lease-related documents, variations, maps, plans, and performance standard agreements in a comprehensive lease management volume, to provide a transparent view of the lease and the network;
- Undertaking the planned 2010 physical audit of the track (2005 was undertaken but not 2010) and outlining to stakeholders why this oversight was allowed to occur; and

- Overseeing trials to examine the potential to load heavier axle consists on certain line sections to better meet the needs of rail users. As an example, CBH estimates that increasing current 16 tonnes per axle ("TAL") line sections to 17 TAL would allow an 8.5 per cent increase in cargo carried, creating a significant improvement in rail productivity.

## **APPENDIX 3**

### **CBH's submission to the Productivity Commission's National Access Regime Issues Paper, February 2013**





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8 February 2013

National Access Regime  
Productivity Commission  
LB2 Collins Street East  
Melbourne VIC 8003

Dear Sir/Madam

#### **Submissions – National Access Regime**

Co-operative Bulk Handling Limited ("CBH") refers to the Productivity Commission's National Access Regime Issues Paper release on 30 November 2012 (**Issues Paper**) and the Productivity Commission's request for submissions from interested parties.

CBH welcomes the opportunity to participate in the Productivity Commission's public submissions process and wishes to raise some of the issues it has encountered in relation to the Western Australian rail access regime (to which this letter solely relates).

#### **Background**

CBH is a co-operative with 4,700 grower members. CBH was established to promote the West Australian agricultural industry through the development and conduct of bulk grain storage and handling operations for the Western Australian grains industry. As a co-operative, CBH is unique in that it is committed to activities which are predominantly for the benefit of the industry as a whole. For a more detailed summary of the history of CBH, please refer to our website: [www.cbh.com.au](http://www.cbh.com.au).

The Western Australian rail network used for transporting grain to port is a vital piece of infrastructure and provides the most efficient and safe method of transporting grain (as compared to road). The significance of the Western Australian grain industry to Australia's national economy is evidenced by the fact that up to 50% of grain exported from Australia originates from Western Australia. Western Australian grain growers are export dependent with up to 90% of grain exported annually to over 20 international customers. Having access to an efficient and cost effective rail network is essential to ensuring that WA grain growers are able to compete against other international suppliers.

### ***The Western Australian Rail Access Regime, Certification and the role of Ministers***

The Western Australian Rail Access Regime established by the *Railways (Access) Act 1998 (WA)* and the *Railways (Access) Code 2000 (WA) (Code)* was considered by the National Competition Council (NCC) in December 2010 in accordance with section 44M of the *Trade Practices Act 1974* (as it was then).<sup>1</sup> The NCC considered whether the rail access regime ought to be certified as an effective access regime and recommended that the Commonwealth Minister **not certify** the access regime as effective.

Despite the findings and recommendation of the NCC, the Commonwealth Minister decided that the WA rail access regime is an effective regime under section 44N of the *Competition and Consumer Act 2010* on 11 February 2011.

Page 24 of the Issues Paper provides:

*“However, the Hilmer Committee also noted that Ministers may face pressure to advance private interests, and as a result, proposed that declaration be based on explicit criteria and advice from an independent expert body — the NCC. Furthermore, the Committee recommended that the Minister could only make such a declaration if recommended by the NCC and only on the terms and conditions recommended by that body unless the infrastructure service provider agreed to alternative arrangements (these elements were not adopted).”*

The Hilmer committee's findings are clearly inconsistent with the process followed by the Minister's certification of the WA Rail Access Regime - rather than base the declaration/certification on a NCC recommendation, the Minister certified the access regime as being effective notwithstanding a recommendation from the NCC that the Minister not certify the access regime.

CBH agrees with the Hilmer committee and is of the view that decisions should follow the advice and findings of an independent body (i.e. the NCC). This removes any political or commercial pressures that may be faced by Ministers to make declarations or certifications which favour private interest rights.

Another acceptable process would be for the Minister to make the declaration or certification only once the findings and recommendations of the NCC have been put into place. If this were adopted, current issues with the WA Rail Access Regime could have been addressed while there was political will and motivation to do so.

By way of example, in the NCC Final Recommendation paper dated 13 December 2010 for the Western Australian Rail Access Regime, the NCC acknowledges the difficulties associated with adopting a Gross Replacement Value (GRV) cost methodology, noting that the WA Rail Access Regime is the only regime to adopt the GRV and consistency in national regulation would be promoted with a review, and potentially replacement of the GRV methodology (at page 62).<sup>2</sup>

The NCC, at page 64, continues by saying that the content of the current review of the Code by the Economic Regulation Authority of WA (ERA) and the submissions made to the NCC by the WA Government suggest changes may be made to the GRV methodology which are expected to address some of the concerns.

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<sup>1</sup> The NCC Final recommendation is available at: <http://www.ncc.gov.au/images/uploads/CERaWAFR-001.pdf>

<sup>2</sup> CBH notes that the Productivity Commission has commented on this issue in its submission to the NCC's

Review of the WA Rail Access Regime:

[http://www.pc.gov.au/\\_data/assets/pdf\\_file/0013/8005/warailaccess.pdf](http://www.pc.gov.au/_data/assets/pdf_file/0013/8005/warailaccess.pdf)

Since the NCC's Final Recommendation paper, the GRV concerns flagged by the NCC, the ERA, the State government and other industry participants are still unresolved. The ERA's 2009 review of the Code (the ERA is required to review the Code every 5 years) initially recommended the removal and replacement of the GRV to a cost methodology similar to those used by Eastern States railways and other infrastructure assets but later withdrew this recommendation after receiving push back from the leaseholder of the WA rail network.

The opportune time to make changes to the WA Rail Access Regime addressing NCC concerns (not just the GRV issue) would have been at the time the Minister was faced with deciding whether to declare/certify the access regime and not hope that the matters would be dealt with later. As of today, issues flagged by the NCC in 2011 have not been addressed and the ERA's Final Report (commenced in 2009) has been with the State government since December 2011 with recommended changes to the Code still to be implemented. The period of inaction has extended for so long that it risks overlapping with the next 5 year review of the Code by the ERA which is to commence in 2014.

### ***Efficient Investment in Infrastructure***

On page 21 of the Issues Paper, the following questions are raised:

*"What is the evidence that the access regime has had an effect on investment? In particular, possible 'chilling' effects, or apparent strategic responses relating to investment decisions, including infrastructure capacity, to limit competitor access? What evidence is there that efficient investment has proceeded as a consequence of access regulation?"*

These questions are particularly timely in light of the recently released Western Australian Auditor General's Report: *Management of the Rail Freight Network Lease: Twelve Years Down the Track*<sup>3</sup> (AG Report).

The objective of the audit was to assess the management of the 49 year rail freight network lease by WA State Government, by determining whether the outcomes to date are in line with original objectives, and whether the WA State Government agencies are managing the rail freight lease to protect the State's interests into the future.

In respect of investment in the WA rail freight network used for grain, the Auditor General concludes:

*"The condition of the narrow gauge lines used primarily for carrying grain has degraded. The 'grain lines' have required substantial government funding to remain in service. Two of the uneconomic 'Tier 3' grain lines have been placed in care and maintenance, and without further government funding, the remaining eight are likely to be taken out of service after 2013."*

In other words, parts of the grain rail network are receiving little or no investment such that they are being put out of service and mothballed. CBH, as the primary user of these lines with dedicated loading facilities built along these lines, are effectively being denied access to these lines as they continue to remain under the control of the current lessor of the rail network.

On page 35 of the AG Report, the Auditor General provides:

*"Placing the lines into care and maintenance while leaving them with the current lessee potentially obstructs prospective new operators from entering the market. This also benefits the lessee by reducing the likelihood of competition while allowing the*

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<sup>3</sup> The Auditor General's report is available at: [http://www.audit.wa.gov.au/reports/pdfreports/report2013\\_01.pdf](http://www.audit.wa.gov.au/reports/pdfreports/report2013_01.pdf)

*lessee to retain the right to future economic benefit from disused rail line corridors. The uncertainty over whether the market can provide an alternative viable operator can only be fully resolved by testing the market, which PTA has not formally done. However, it has received unsolicited approaches."*

It is difficult to reconcile the findings in the AG Report with the objectives of the National Access Regime of "promoting the economically efficient operation of, use of and investment in the infrastructure by which services are provided, thereby promoting effective competition in upstream and downstream markets".

### ***The Broader Policy Framework***

In relation to rail, CBH notes that the Issues Paper summarises the requirements of the Competition and Infrastructure Reform Agreement (**CIRA**) to implement a consistent system of rail access regulation – using the Australian Rail Track Corporation (**ARTC**) access undertaking as a model.

CBH agrees with the CIRA requirements noting that WA rail access regulation diverts significantly from the ARTC model. For example, the ARTC model adopts a more appropriate asset valuation model (the Depreciated Optimised Replacement Cost methodology rather than the GRV model discussed above). The ARTC model also provides more transparency to access seekers including publically available information on track performance, investment strategies, pricing, capacity availability, access terms and conditions (amongst others) which are not available in Western Australia.

CBH requests that the Productivity Commission considers what measures (if any) are being undertaken to implement a consistent system of rail access regulation inline with the CIRA requirements.

Yours sincerely

***For: Co-operative Bulk Handling Limited***

**Karlie Mucjanko**  
**General Manager – Corporate Affairs**