



Submission to the

**Senate Rural and Regional Affairs and Transport
References Committee**

Inquiry into

Shipping Legislation Amendment Bill 2015

21 August 2015

ABOUT AIP

The Australian Institute of Petroleum (AIP) was established in 1976 as a non-profit making industry association. AIP's mission is to promote and assist in the development of a sustainable, internationally competitive petroleum products industry, operating efficiently, economically and safely, and in harmony with the environment and community standards. AIP provides a wide range of factual information and industry data to assist policy makers, analysts and the community in understanding the key market, industry and other factors influencing Australia's downstream petroleum sector.

AIP is pleased to present this submission to the Senate Rural and Regional Affairs and Transport References Committee on behalf of AIP's core member companies:

BP Australia Pty Ltd
Caltex Australia Limited
Mobil Oil (Australia) Pty Ltd
Viva Energy Australia Ltd

About AIP Member Companies

AIP member companies operate across the liquid fuels supply chain including crude and product imports, refinery operations, fuel storage, terminal and distribution networks, marketing and retail. Underpinning this supply chain is considerable industry investment in supply infrastructure, and a requirement for significant ongoing investment in maintaining existing capacity. Over the last decade, AIP member companies have invested over \$10 billion to maintain the reliability and efficiency of fuel supply meeting Australian quality standards.

AIP member companies play a very significant role in delivering the majority of bulk fuel supply to the Australian market.

- In relation to conventional petroleum fuels, AIP member companies operate all major petroleum refineries, operate the majority of the seaboard terminals in Australia, and supply around 90% of the transport fuel market.
- In relation to gaseous fuels, AIP member companies are the major suppliers of bulk LPG to the domestic market, representing around two thirds of the market.
- In relation to biofuels, AIP member companies are the largest suppliers of ethanol and biodiesel blended fuels to the Australian market.

Given this background and their significant role in the Australian fuels supply chain and broader economy, AIP member companies have a very strong interest in streamlining a broad range of regulations and the efficient discharge of compliance obligations under these regulations. Background information on the downstream petroleum industry is contained in the AIP publication Downstream Petroleum 2013 (<http://www.aip.com.au/topics/new.htm>) and the AIP submission to the Energy White Paper process (<http://www.aip.com.au/topics/submissions.htm>).

Contact Details

Should you have any questions in relation to this submission, or require additional information from AIP, the relevant contact details are outlined below.

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Summary

AIP member companies have a declining requirement for coastal shipping brought about by the fundamental restructuring of the Australian refining industry and associated changes to petroleum distribution. Nevertheless, efficient coastal shipping remains important to the industry and Australia because of the ongoing need for transport of crude oil and petroleum products around the coast.

AIP member companies strongly support the legislative amendments in this Bill to streamline the regulatory regime set out in the coastal trading legislation. The proposed amendments to the coastal shipping regulatory requirements will remove unjustified administrative burdens on the downstream petroleum industry.

The current cumbersome and inflexible regulations impede the efficient operation of domestic refineries and petroleum supply chains around Australia, do not facilitate liquid fuel supply security, and do not advance the objectives of the coastal trading legislation or the local shipping industry.

In its submission of 20 April 2012 to the then Senate Economics Legislation Committee on the Coastal Shipping (Revitalising Australian Shipping) Bill 2012, AIP foreshadowed structural changes in the downstream petroleum industry and argued that there was a strong case for initial exemption of the shipping of petroleum products on the basis that there is little likelihood of an Australian registered vessel being available for the shipping of crude oil or any additional Australian registered vessel for shipping of petroleum products.

Subsequent restructuring of the Australian refining industry and associated changes in the petroleum supply chain since that time mean that there is no chance of a viable Australian petroleum coastal shipping vessel with any long term business growth prospects.

AIP support for the Shipping Legislation Amendment Bill 2015

The Australian Institute of Petroleum and its member companies strongly support the legislative amendments in this Bill to streamline the regulatory regime set out in the coastal trading legislation. The petroleum industry believes these proposed changes will greatly improve the flexibility and ease of access by the petroleum industry to shipping that is essential to the cost effective operation of Australian petroleum refineries and the provision of secure fuel supplies across the country. Background information on the Australian downstream petroleum industry and recent structural changes in the industry is at Attachment 1.

The proposed changes will help optimise fuel supply options, particularly in the event of a disruption in the supply chain into and around Australia. In addition, the changes will

- reduce the cost impost of coastal shipping on Australian refineries which will increase their ability to compete against direct imports and improve the competitive position of Australian refineries
- help deliver cheaper freight costs for fuel supplies
- create greater choice and flexibility in options to supply fuel to the significant number of terminals around Australia
- reduce administration costs for industry and government
- significantly reduce the complexity of rules relating to shipping of petroleum products in Australia
- facilitate supply chain operations that best meet emerging fuel supply needs in regional markets across Australia.

We support the concept of a single Coastal Trading Permit (applying to Australian and foreign vessels) to replace the existing tiered permit system, and believe that the new system will reduce administrative actions and will leverage international maritime conventions rather than additional Australian regulations. In particular, AIP Member Companies believe that

- Vessels used by the petroleum sector must have the flexibility to deliver and/or move petroleum (crude oil and petroleum products) to and between any Australian port (i.e. both inter and intra-State cargo movements).
 - Current legislation makes it exceedingly difficult (because of relatively lengthy approval times and the complex approval process, as well as excessive paperwork) for Australian fuel suppliers to make short term decisions necessary to optimise the Australian fuel supply chains in ways that can best meet emerging fuel supply needs in Australia.

- Contestability is provided through the competitive shipping market – it is in the interest of business that cargo is moved at least cost.
 - Current legislation creates a significant administrative burden for the petroleum industry and Government with no practical purpose since there are no Australian registered petroleum tankers available to contest proposed coastal trading voyages.
- Foreign vessels used by the petroleum industry to pick up crude oil and condensate from FPSOs in Australian waters and deliver that cargo to an Australian port, and petroleum tankers used to store crude oil or petroleum products on a temporary basis in Australian waters (as a form of temporary fuel storage during refinery maintenance periods) must be exempted from the ‘importation’ provisions of the Customs legislation, in the same way as all other foreign vessels used by the downstream petroleum industry.
 - Current legislation does not properly address these operational issues and as a result imposes significant unintended consequences and costs on the petroleum industry, and constrains potential options to optimise the fuel supply chain operations in Australia and hence fuel supply security. In the case of FPSO production, the current provisions actively discourage the use of Australian crude oil and condensate in Australian refineries.
- The period of validity of a Coastal Trading Permit must be for 12 months and the Coastal Trading Permit must be able to be granted quickly, particularly so that short notice spot charter options can be utilised more effectively to enable the most efficient operation of fuel supplies to Australia as well as enable emergency supply needs to be met without any delay
 - Current legislation involves delays of up to 15 days for the initial annual application, and 7 to 9 days for approvals of new voyages or variations to voyages. In addition, public holidays impose more delays and further limit flexibility of the current approvals process. These delays are unacceptable in a complex supply chain such as that for delivery of fuel to the Australian market, particularly when there are no Australian registered vessels available to ‘contest’ these voyages.
- The new reporting requirements suitably reflect the revised purpose of the legislation and take account of vessel reporting requirements under other legislation (such as Customs and HSE legislation etc.).

AIP member companies support the proposed minimum Australian crewing requirements noting that the minimum crewing requirements are clearly stated in the legislation, along with appropriate compliance requirements.

Coastal Shipping of Petroleum Products

The current coastal shipping task

The supply of petroleum products to meet Australia's demand for liquid fuels involves the refining of crude oil at Australian oil refineries and supply of these products to terminals, the import of the finished petroleum products to seaboard terminals, and the distribution of petroleum products from terminals to major commercial customers and service stations.

The involvement of the petroleum industry in coastal trading includes the movement of:

- domestically produced crude oil to Australian refineries
- intermediate products between refineries
- finished products from major distribution terminals to other major seaboard terminals.

The crude oil to supply Australia is largely imported from Asia (55% of imports), the Middle East (21% of imports) and Africa (21% of imports) and in 2012-13 the proportion of domestically produced crude oil processed in Australian refineries was 14.9%. The reason for the prevalence of imported crude oil processed in Australian refineries is the higher cost of Australian crudes which command a premium in the crude oil market and the configuration of Australian refineries which require a heavier crude oil than that which can be supplied from Australian sources.

Crude oil from Bass Strait is supplied by pipeline to the Altona refinery in Melbourne and the Geelong refinery. However, the production of crude oil from Bass Strait is declining as the fields are depleted and the production from Bass Strait is progressively becoming a lighter condensate which is unsuitable for processing in Australian refineries in more than small volumes. However, there are still movements of crude oil by ship from Bass Strait to other Australian refineries. Other Australian sources of crude oil include the Cooper Basin and North West Shelf which are also moved by ship.

There are movements of intermediate products between Australian refineries by ship because of greater capacity to process certain types of inputs and the nature of consumer demand in the regional supply footprint of the receiving refinery. Past examples of these intermediate product movements include cracker feeds for processing in a fluidised catalytic cracker, high sulfur gasoil for processing in a hydrogen desulfurisation unit to produce diesel and occasionally the re-routing of off-specification product for further processing.

Finished petroleum products are moved by ship from Australian refineries to other seaboard terminals around Australia. The major regular supply areas from Australian refineries are Northern Queensland, South Australia, North West Western Australian and Tasmania. There have also been ad hoc movements of finished petroleum products between major metropolitan terminals particularly in the event of supply disruptions.

However, the volume of petroleum products shipped locally is in long term decline. Data from the Bureau of Infrastructure, Transport and Regional Economics on Australian Sea Freight 2011-12 (August 2013) showed a reduction of coastal trading volume for petroleum products from 15.9 million tonnes in 2002-03 to 10.5 million tonnes in 2011-12 (Table 2.8, p 13). This 34% decline in coastal shipping of petroleum products over the period is in the context of a 22% growth in total Australian demand for petroleum products.

Structural change in the Australian downstream petroleum sector

This reduction in the need for coastal shipping of petroleum products is largely a result of the ongoing rationalisation of the Australian oil refining industry and associated changes to the petroleum distribution system brought about by increasing competition from larger and more efficient refineries in the Asian region.

In 2003, Australia had eight operating refineries with the capacity to supply over 95 per cent of Australia's liquid fuels demand. The Australian Government's Cleaner Fuels Program that commenced in 2001 required a progressive tightening of fuel standards to deliver urban air quality benefits and facilitation of more advanced motor vehicle technologies. The Australian refiners were required to spend over \$3 billion by 2010 in order to stay in business and resulted in the refineries operating with significantly less flexibility.

As a result of the capital requirements to meet these fuel specifications, ExxonMobil announced the mothballing of the Port Stanvac refinery in Adelaide in 2003 and subsequently it was announced in 2009 that the facility would be decommissioned. The Cleaner Fuels program also caused the de-rating of the ExxonMobil Altona refinery in Melbourne reducing from 135,000 barrels per day to 82,000 bpd. These ExxonMobil decisions reduced the capacity of the Australian refining sector by 15%.

During the mid-2000s a supply surplus began to emerge in the Asian region as a result of large scale refinery construction programs in India and China. This surplus was exacerbated by the Global Financial Crisis which saw the emergence of a global overcapacity in the supply of refined petroleum products. The Australian refining industry faced an unprecedented level of competition from larger and more efficient Asian export refineries leading to significant financial losses in 2008, 2011 and 2012.

In response, Shell's Clyde refinery in Sydney was converted to an import terminal in 2012. Agreement was also reached in 2014 on the sale of the remainder of the Shell downstream petroleum assets in Australia to Vitol, the world's largest petroleum trader. The Vitol sale also included the Geelong refinery, and the Australian operating company Viva Energy Australia Ltd has indicated that it will continue to operate the refinery.

Further rationalisations include the closure of Caltex's Kurnell refinery in Sydney, which has been converted into Australia's largest fuels import terminal in the fourth-quarter 2014; and the recent closure of BP's Bulwer Island refinery in Brisbane, which may be converted to an import terminal in the future.

The remaining Australian refineries, BP Kwinana in Western Australia, Caltex Lytton in Brisbane, ExxonMobil Altona in Melbourne and Viva Energy Geelong will still be subject to ongoing intense competitive pressures. The unprecedented level of oversupply, both globally and in the Asian region, is not expected to ease until 2020. Assuming the level of Australian refining capacity stabilises at these levels, the closures, de-rating and conversions will have accounted for a 50% reduction in Australian refining capacity, and as a consequence the Australian refining sector will be capable of producing about half of Australia's 2014-15 liquid fuel requirements.

This fundamental restructuring of the Australian refining industry has significant implications for fuel distribution and consequently the volume and type of coastal shipping needed to move liquid fuels around the country.

The coastal shipping task going forward

The total crude oil requirements of Australian refineries will reduce substantially as capacity is reduced and the proportion of Australian crude oil used in Australian refineries is expected to also decline. As a result, the requirement of coastal shipping to supply Australian refineries will also substantially decline. For this reason, AIP considers there is no likelihood of an Australian registered crude oil tanker entering coastal shipping in Australia.

The reduction in refining capacity will also mean the reduction in refinery transfers of intermediate products between Australian refineries. There will be no opportunities for intra-company transfers as each company will only have one refinery. Moreover, there do not appear to be any economic refining models that would support the transfers of intermediate products between the remaining Australian refineries on a regular basis. AIP therefore considers that the transfer of intermediate products between Australian refineries will decline substantially and will in most likelihood cease.

The coastal shipping of finished petroleum products is also expected to decline. With the various refinery closures a greater proportion of Australian petroleum products demand will be supplied by imports and it is likely a significant proportion will displace domestic production shipments to the northern areas of Australia.