Supplementary Submission to the Inquiry into the National Fuelwatch Bills 2008

Federal Parliament
(Senate Economics Committee)

15 July 2008

BACKGROUND

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 member companies play various roles in each segment of the fuel supply chain. They operate all of the petroleum refineries in Australia and handle a large proportion of the wholesale fuel market. However, AIP member companies directly operate and control only a relatively limited part of the retail market.

AIP is pleased to present this submission on behalf of the AIP's four core member companies:

BP Australia Pty Ltd
Caltex Australia Ltd
Mobil Oil Australia Pty Ltd
The Shell Company of Australia Ltd

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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EXECUTIVE SUMMARY

- Australia currently has a free and open petroleum products market, featuring a highly competitive and dynamic retail fuel market.
    - This is clearly acknowledged in the ACCC's 2007 Petrol Prices Inquiry Report.
- This "fundamentally competitive market", according to the ACCC, has delivered to Australian consumers low petrol and diesel prices by international standards.
- The retail discounting cycle has delivered heavily discounted fuel, on a regular basis, to consumers.
- Three separate and detailed ACCC inquiries into retail price cycles (and related matters) have provided clear evidence that the weekly retail discounting cycle provides benefits to consumers.
    - Each separate inquiry has concluded that more than 60 per cent of weekly fuel sales were made when the average daily price was below the average weekly price.
- The ACCC Report also indicates that consumers clearly value the pattern and predicability of the regular retail price cycle, in terms of guiding their fuel purchasing decisions to days of the week when fuel has been heavily discounted.
- Based on this clear purchasing behaviour and evidence, it is difficult not to conclude that consumers already have valuable information about when and where to buy fuel.
- AIP considers there is considerable information that is freely and readily available to consumers, including on a current or real time basis, about comparative fuel prices at a local area level.
    - For example, service station price boards, newspapers, TV, internet sites of fuel retailers, motoring organisations websites, government or consumer agencies and private sector businesses providing extensive retail petrol price information on a free or commercial basis (eg. Informed Sources, FuelTrac and Motormouth).
- AIP supports effective measures that seek to further improve the quality and timeliness of information to consumers in a competitive market setting.
    - AIP considers that market based solutions to increased retail transparency might be available - at no cost to taxpayers.
    - For example, AIP member companies would take no exception to a mechanism that enabled consumers to access detailed retail pricing data (like that provided by Informed Sources) on a local area basis, provided retailer 'free-rider' issues can be resolved.
- AIP believes that any government policy measure to intervene in a competitive market is a decision for government.
- However, the rationale, objectives and potential benefits and costs of such intervention need to be clearly understood by those parties likely to be affected by the intervention.
- For example, consumers will naturally be concerned if heavily discounted fuel is not available at the pump to the same extent when the National Fuelwatch Scheme is operational.
    - In addition, consumers are also likely to be dissatisfied if restricting intra-day price movements creates more unpredictable retail petrol prices throughout the week (ie. less consumer certainty), as cautioned in the Government's Regulatory Impact Statement.
- There has been a notable absence of consultation with the oil industry and service station operators on the design and implementation of the National Fuelwatch Scheme.
    - Such consultation will be important given the Government estimates that 4700 retail businesses will have $4,000 in new compliance costs to meet every year.
- AIP considers that the Government/ACCC needs to conduct and/or release further detailed analysis in order to demonstrate a clear public benefit from the introduction of a 24 hour rule under the proposed National Fuelwatch Scheme.
    - This comprehensive analysis would have to consider the fundamentally competitive nature of the Australian fuel market and the costs (versus the status quo) of intervening in this free market – including regulatory, compliance and enforcement costs and broader economic costs in terms of potentially higher prices (shown in some independent analysis) and reduced competition in the market.
- Overall, AIP considers that retail price regulation under the 24 hour rule will not deliver improved market and supply outcomes, nor deliver lower prices to consumers than they currently enjoy.
- The ACCC Report identified a range of serious issues (on page 252) that required detailed consideration before the adoption of a National Fuelwatch Scheme.
    - The detailed consideration and analysis of these issues, and the conclusions reached, has not been made publicly available.

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(1) INTRODUCTION

This submission has been developed to inform and assist the Senate Economics Committee in its consideration of the range of issues identified under its Inquiry into the *National Fuelwatch (Empowering Consumers) Bills 2008*.

This detailed 'Supplementary' AIP Submission, complements the initial submission lodged by AIP on 2 July 2008, outlining our overall view in relation to the National Fuelwatch Scheme.

This submission provides information and data related to the operation and structure of Australia's retail fuel market (Chapter 2) and an overview of retail fuel pricing in Australia (Chapter 3). It also addresses the specific terms of reference for the Inquiry (Chapters 4 & 5).

In summary, this submission covers the following subject areas.

- The structure and operation of the Australian retail fuel market *{various TOR}*
- The facts about Australian retail prices and retail price cycles *{various TOR}*
- Objectives, design and implementation of the National Fuelwatch Scheme *{various TOR}*
- The impacts of the National Fuelwatch Scheme on:
  - Prices *{TOR a & i}*
  - Competition *{TOR d}*
  - Price Cycles & Discounting *{TOR b, e & f}*
  - Consumer Behaviour *{TOR b & c}*
  - Business Compliance Costs *{TOR c}*
  - Economic Impacts *{TOR a & h}*
- Other issues including the legal basis for the legislation *{TOR j & g}*.

In the preparation of this submission, AIP has drawn on previous AIP Submissions to Government and ACCC pricing inquiries and a wide range of other Government reports, papers and analysis. Details of the key references are set out in Attachment A.

The source of all data and charts in this submission is AIP data unless otherwise stated.

AIP member companies have also made submissions to this Inquiry, and those submissions address specific items on the terms-of-reference and deal with commercial and other issues related to the specific operations of those companies.

(2) THE AUSTRALIAN RETAIL FUEL MARKET

This chapter provides a brief overview of the key structural characteristics and operational features of the retail petroleum market in Australia. A key focus is who sets pump prices in the retail market and the potential influence of different market participants in the future. Progressive changes in service station numbers and ownership since 2000 are also outlined. This discussion provides important context to the subsequent chapter on retail fuel prices and the retail pricing framework and also for the purposes of understanding how the National Fuelwatch Scheme might impact across the whole of the Australian market and on specific market participants – particularly independent retailers.

(A) STRUCTURE OF THE MARKET

The structure of the retail fuel market has changed markedly over the last 30 years. Over this period, the dominant business model has shifted from a petrol station with a mechanical repair workshop to a multi-product service site. Under this model, service stations offer a range of products other than liquid fuels and rely on high volume fuel sales and significant convenience store sales for competitive advantage.

The competitive advantage of any individual site is determined by the package of goods and services being offered to consumers. The most obvious example is shopper dockets that have enabled independently operating supermarket chains to sell approximately 45% of the retail petrol and diesel in metropolitan Australia. Other important elements for consumers are the site location and access, the general condition of the site, and the extent of ancillary services, such as a convenience store.

These developments mean the retail fuel sector is competitive and dynamic. With the removal in 2006 of constraints posed by the Sites and Franchise Acts there are no barriers to location or ownership models. Consumers are also benefiting from reduced prices and better service.

In the case of AIP branded independents and independents not associated with AIP member companies, service station numbers have reduced. The main drivers for site closure continue to be general small business viability factors such as:

- Low fuel turnover and hence low profits from fuel sales (1 tanker per 2-3 weeks versus 1 tanker per day and sometimes more tankers per day at large metropolitan sites).
- Lower convenience store turnover/sales over which to meet service station operating costs (ie limited diversity of income base).
- Viability/expansion constrained by aging capital - older businesses without capital backing for site upgrades (eg for new storage tanks, extra pumps, new forecourt, modern and expanded convenience store).
- Viability/expansion constrained by State/Territory government regulations and environmental expenditure requirements (eg to prevent leaks from underground storage tanks – most ‘at risk’ sites are in non-metropolitan areas where quality of groundwater may be a priority).
- Families not wishing to continue to operate their small business.
- Competition from more efficiently run businesses, and businesses offering a wider range of convenience store services.
- Too many service stations in the town.

Analysis by AIP suggests that the average customer base for a service station in metropolitan areas (based on numbers of residents in the vicinity of the service station) is around 4500. In non-metropolitan areas the average customer base per service station is around 2000 (based on numbers of residents in the vicinity of the service station), and in many towns the customer base is between a half and one third of this figure.

BOX 1 - MAIN TYPES OF SERVICE STATION OPERATIONS

Outlined below is an explanation of the main types of service station operations:

- **Oil Company operated (sites may be owned or leased)**
  - Oil company supplies fuel to its own sites
  - Retail prices set by oil company
  - Convenience store options

- **Supermarket chain operated sites**
  - Term contract fuel supplies
  - Retail prices set by supermarket
  - Convenience store operations controlled by supermarket

- **Franchisee and Commission Agents**
  - Franchisee operated (declining in numbers)
  - Commission Agents (tenure extended in Oilcode)
  - Full marketing programme support by supplying oil company
  - Fuel supplies from franchisor
  - Retail prices set by franchisee (unless acting as a commission agent for fuel)
  - Convenience store options controlled by franchisee or CA

- **AIP Company Branded Independents**
  - Branded independents (major oil company brands) – still account for almost half the total number of service stations
  - May be operated by distributors or independent retailers (in some cases may be franchised by distributors or multi-site owners)
  - Subject to branding agreement with fuel supplier
  - Agreement may or may not include marketing programme support
  - Term fuel supplies
  - Retail prices set by independent operator
  - Convenience store options controlled by owner/operator

- **Non AIP company branded and other independents**
  - May be operated by distributors or independent retailers (in some cases may be franchised by distributors or multi-site owners)
  - Fuel may be obtained from more than one supplier
  - Retail prices set by independent operator
  - Convenience store options controlled by owner/operator

NOTE: Within this structure, sites may be owned by oil majors, supermarkets, franchisees/commission agents acting as investors, distributors, branded or non branded independent retailers, or unrelated investors. Sites may be operated by the owners or leased to other operators.

(B) RETAIL PRICING & THE ROLE OF DIFFERENT ENTITIES

Retail Price Setting

Retail prices are set in around 90-95% of cases by people other than the oil majors.

While the oil majors and some importers are responsible for setting the wholesale fuel prices, retail prices and hence retail margins are set at the vast majority of sites by the site operator.

Fuel Quality Management

Each of the oil majors operating in Australia guarantees the quality of the fuel purchased from service stations carrying that company's brand. For this reason, there are strict controls on sourcing fuel supplies only from an authorised distributor of that brand's fuel. The quality of the fuel will have been closely monitored and checked from the time it was produced at a refinery and fed into the distribution system.

All fuel produced and sold by the oil majors goes through rigorous checks for quality assurance.

For brand management and fuel quality assurance reasons and to avoid misleading consumers it is not acceptable for individual AIP branded service station operators to offer consumers fuel obtained from third party sources. This situation is no different from the arrangements that are rigorously applied in many other branded product wholesale and retail operations (eg. fast food and beverages).

The maintenance of clear fuel supply accountability is even more important under the Australian Government's Cleaner Fuels Program that imposes legal compliance implications on fuel suppliers. As Australian fuel suppliers guarantee their fuel quality, the supply of off-spec fuel to a retailer by a third party can have significant negative financial and reputation implications for the fuel supplier.

(C) SERVICE STATION NUMBERS

The following table summarises the changes in service station numbers since 2000.

TABLE 1 - Changes in Service Station Numbers since 2000

	2000	2004	2005	2006	2007	2008
AIP Member Company Branded Sites	7558	4886	4754	4543	4192	3832
Supermarket Chain Sites	153	872	1065	1083	1104	1127
Sub Total	7711	5758	5819	5626	5296	4959
Independents (non-AIP member service stations)	659	608	652	696	740	784
TOTAL	**8370**	**6366**	**6471**	**6322**	**6036**	**5743**

NOTE: 2005 to 2007 site data for independents are estimates (interpolation from 2004 to 2008 actual data).

The majority of Australian service stations continue to be AIP member company branded independents. These sites are operated by small businesses with a fuel supply and branding contract with an AIP member company.

Other highlights from Table 1 include the following.

- Overall, there was an estimated net reduction in service station numbers of 10% between 2004 and 2008, compared with a net reduction of 24% between 2000 and 2004.

- There was a reduction of around 1000 AIP member company branded sites between 2004 and 2008, but this was offset by increases in the numbers of supermarket chain sites and independent sites through transfer of ownership/branding.

- The rate of closure of service station sites has declined significantly over the last few years.
  - 2000 to 2004 - 501 sites closed per year
  - 2004 to 2008 - 156 sites closed per year

- Sites associated with independently operating Supermarket chains increased by 29% between 2004 and 2008.

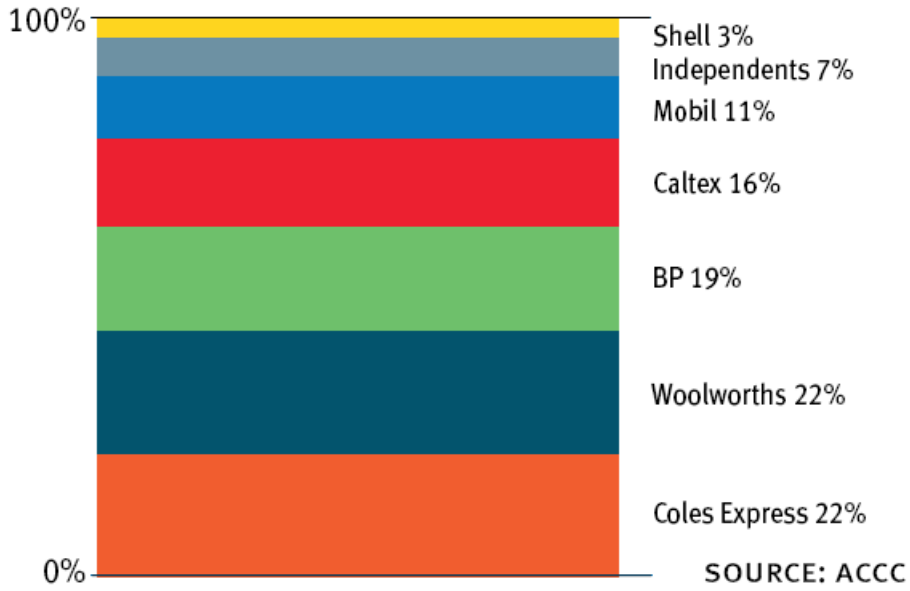
- Other independent service stations have also increased by 29% between 2004 and 2008.

While not reported in the table above, the number of franchisees was 525 in 2008, down from 958 in 2004.

(D) RETAIL PETROL MARKET SHARE

The recent ACCC Petrol Prices Inquiry Report (December 2007) compiled retail market shares for all grades of petrol (p76). This was based on data provided by refiner-marketers, supermarkets and a number of independent retailers as part of the ACCC's formal price monitoring powers under the Trade Practices Act (section 95ZK of the TPA). The market shares calculated by the ACCC are reproduced in Figure 1. This clearly shows that the independently operating supermarkets chains and other independents control more than half of the retail petrol market by volume.

FIGURE 1 – Australian Retail Petrol Market Share : 2006-07
(Volume by site branding)



The ACCC Inquiry Report (p77) also highlights how these market shares have changed since 2002-03. Changes to market share over time is evidence that effective and vigorous competition is occurring in the Australian petroleum market.

(E) RETAIL PRICE DISCOUNTING & SHOPPERDOCKETS

Strong competition at the retail level in Australia has ensured that fuel prices have remained amongst the lowest across the OECD countries. With the advent of the supermarket alliances, customer loyalty programs in the form of supermarket shopper dockets redeemable as discounts on fuel have become a significant feature of fuel retailing in Australia. Advice from the independent supermarket chains indicates that up to 4 million shopper dockets are now being utilised each week. Consumer surveys indicate that up to 75% of consumers are using shopper dockets.

The ACCC has considered over 800 shopper docket schemes and has confirmed that they increase retail price competition in the sector and provide a significant benefit to consumers.

(F) ROLE OF INDEPENDENT SERVICE STATION OPERATORS (EXCLUDING SUPERMARKET CHAINS) IN DRIVING COMPETITION IN THE RETAIL MARKET

Independent operators have a strong presence in the fuel retail market and AIP member companies do not expect this situation to change. However, in recent times we have seen independents playing a far less significant role in driving price competition in Australia.

From the mid 1990s to mid 2003 there were significant volumes of fuel available from refiners in Australia and in Asia at discounted prices, reflecting the excess production at refineries, and the availability of lower quality fuel from some Asian refineries. These factors were the basis on which much of the fuel discounting reputation of some independents was built.

However, there are no longer easy options for price discounting through access to cheap surplus fuel supplies. Rapidly growing demand in Asia has absorbed much of this excess production, and growing domestic demand and the mothballing of the Port Stanvac refinery in Adelaide has significantly increased Australia's net imports of fuel. This option of using cheap, lower quality fuel was further constrained with the introduction of more stringent fuel quality standards in Australia to enable the introduction of new vehicle technology needed to reduce motor vehicle emissions and to improve urban air quality.

In addition to these general fuel supply factors, the Northern Territory fuel pricing inquiry in 2006 concluded that while the opening of a service station by one of the larger independent chains was likely to create local price competition, the presence of the smaller chains or single site independent operators was not likely to generate price competition due to the basic economics of fuel retailing in Australia, particularly outside metropolitan areas.

(G) LONGER TERM ROLE OF OIL MAJORS AND SUPERMARKET CHAINS IN FUEL RETAILING

Some commentators have suggested that in the future there will be a fuel retail duopoly in Australia, based on the supermarket chain operations. AIP member companies believe the market share of supermarkets will only grow substantially if competition is stifled.

Following fuel market reform in 2006, all four oil majors are now able to compete on an equitable basis, without artificial constraints on choice of retail business model. This has enabled networks to be established that are commercially viable in size and hence able to optimise the economies of scale that exist in fuel retailing and convenience store operations.

Progressive improvement in the quality of service stations in rural and regional areas is also occurring with the quality and range of services targeted to meet current community needs.

Predictions of mass site closures, particularly in rural sectors and the commercial demise of the independent sector have not been realised. As AIP argued at the time, we expect the general trend of closures in the service station sector to continue because of the changes to business models and the impact of small business drivers (see page 6).

(3) FACTS ABOUT AUSTRALIAN RETAIL PRICES

This Chapter outlines the basic facts about retail prices, including the retail pricing framework in Australia which reflects the diverse and competitive nature of the retail market (as outlined in the previous chapter). In particular, the chapter outlines the composition and movement of retail prices and provides an overview of why petrol prices at the pump change over time, including at different stages of the price cycle, across different cities/regions, at different times of the day and in response to other international and domestic factors. The clear conclusion is that retail price cycles currently favour consumers and follow a typical and reasonably predicable pattern, allowing consumers to make informed and timely fuel purchasing decisions.

(A) PRICE TRANSPARENCY

Pricing of crude oil and petroleum products — both internationally and domestically — is highly transparent along the entire supply chain, more so than for almost all other products or commodities. Crude oil and petroleum products are sold internationally and domestically through a variety of term contract arrangements and in spot transactions. They are also traded on futures markets like NYMEX.

International price transparency is underpinned by price benchmarks or 'markers' for crude oil and petroleum products of a similar quality, which are convenient indicators of what is happening with prices in specific markets. The main marker crudes are: West Texas Intermediate (WTI–USA); Brent (Europe and Africa); Dubai and Oman (Middle East); and Tapis and Dubai (Asia–Pacific). For Australia, the crude oil marker is the Asia–Pacific benchmark called Tapis Crude Oil and the petrol marker is the Singapore price of Petrol (MOPS95 Petrol). Information on changes in the prices of crude oil and petroleum products is extensively reported on a daily basis.

Wholesale price transparency in the petroleum market is assisted by Terminal Gate Prices (TGPs) for petrol and diesel being independently published by each of the AIP members. TGP is the price set by an AIP member at which any person with the necessary safety clearances can purchase fuel by the tanker load from the AIP member's fuel supply terminals.

Retail price transparency is assisted by highly visible price boards at each service station so that customers can readily observe price changes. Considerable information is also available to retail customers about comparative fuel prices at a local area level (including newspapers, TV, internet sites of fuel retailers, motoring organisations and government agencies. The recent ACCC Pricing Inquiry report also identified private sector businesses providing extensive retail petrol price information to businesses and consumers on a free or commercial basis (eg. Informed Sources, FuelTrac and Motormouth).

Overall market and price transparency in Australia is assisted by data published by AIP and its member companies. This includes:

- a range of AIP factual material on petrol and diesel prices in Australia (see Attachment D);
- extensive retail and wholesale market data across major Australian cities and towns on AIP's website (see www.aip.com.au) and on AIP member company websites; and
- AIP's Weekly Petrol Prices Report (see Attachment C or for the latest version go to the AIP website at www.aip.com.au/pricing/weeklyreport.htm).

All of these mechanisms underpin a highly transparent market and play an important role in providing pricing information to markets and fuel customers about impacts and changes that are occurring in international, regional and local product markets and how this will impact on market prices, including at the pump.

(B) RETAIL FUEL PRICES: COMPOSITION & MOVEMENT

Composition of Retail Prices

At both the wholesale and retail level, fuel prices are set by the competitive market.

Within that fundamental competitive framework, the overall retail or pump price in Australia reflects all the costs of getting the fuel from the refinery or terminal to the consumer.

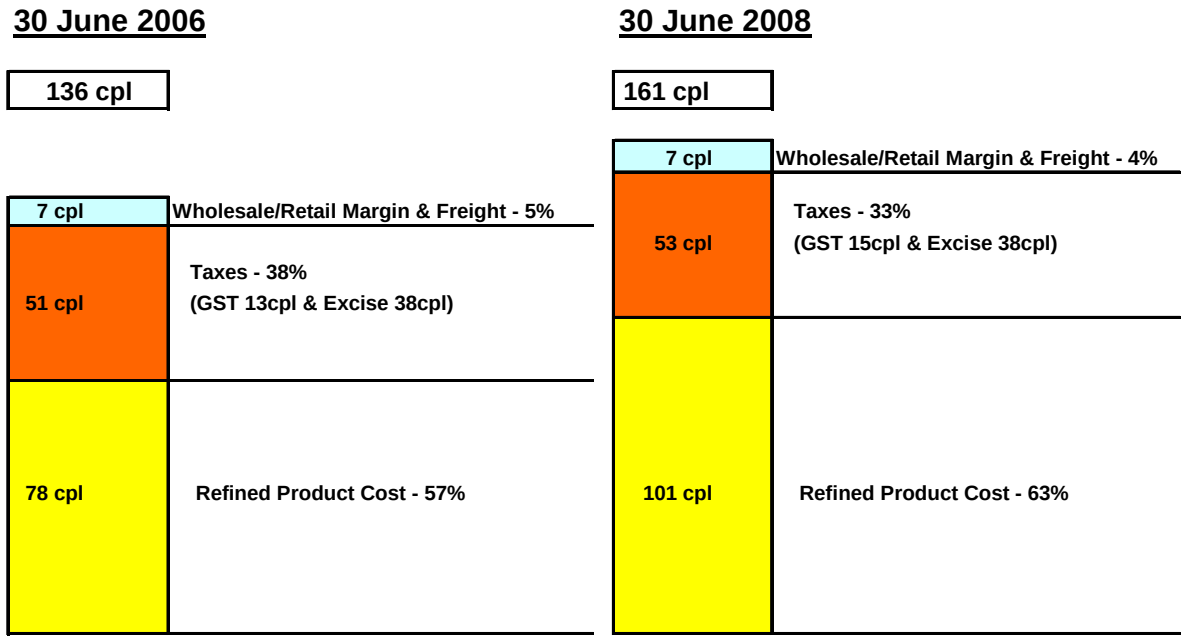
Figure 2 below shows the major components of the indicative retail price of petrol as at the end of June 2006 and at the end of June 2008.

Once the refined product cost and government taxes are taken into account, there is only a small proportion of the price which is received by fuel distributors and fuel retailers - around 4-5% on average.

Importantly, the wholesale/retail margin includes profit, and the amount the distributors and retailers have available to pay all of the costs from the refinery gate to the retail bowser. This includes freight/transport costs, administration and marketing costs, and the costs of running service stations like wages, rent and utilities.

Around 30-40% of the price of petrol is made up of government tax (excise and GST). Fuel excise provided over 6% of Australian Government taxation revenue in 2006.

FIGURE 2 - Components of National Average Retail Prices



The relationship between International & Retail Prices

In understanding movements in retail or pump prices, it is important to distinguish between the factors that contribute to the underlying price level and the factors that drive pump or retail price volatility around that underlying price level. Ultimately, the market sets the retail price which can be achieved.

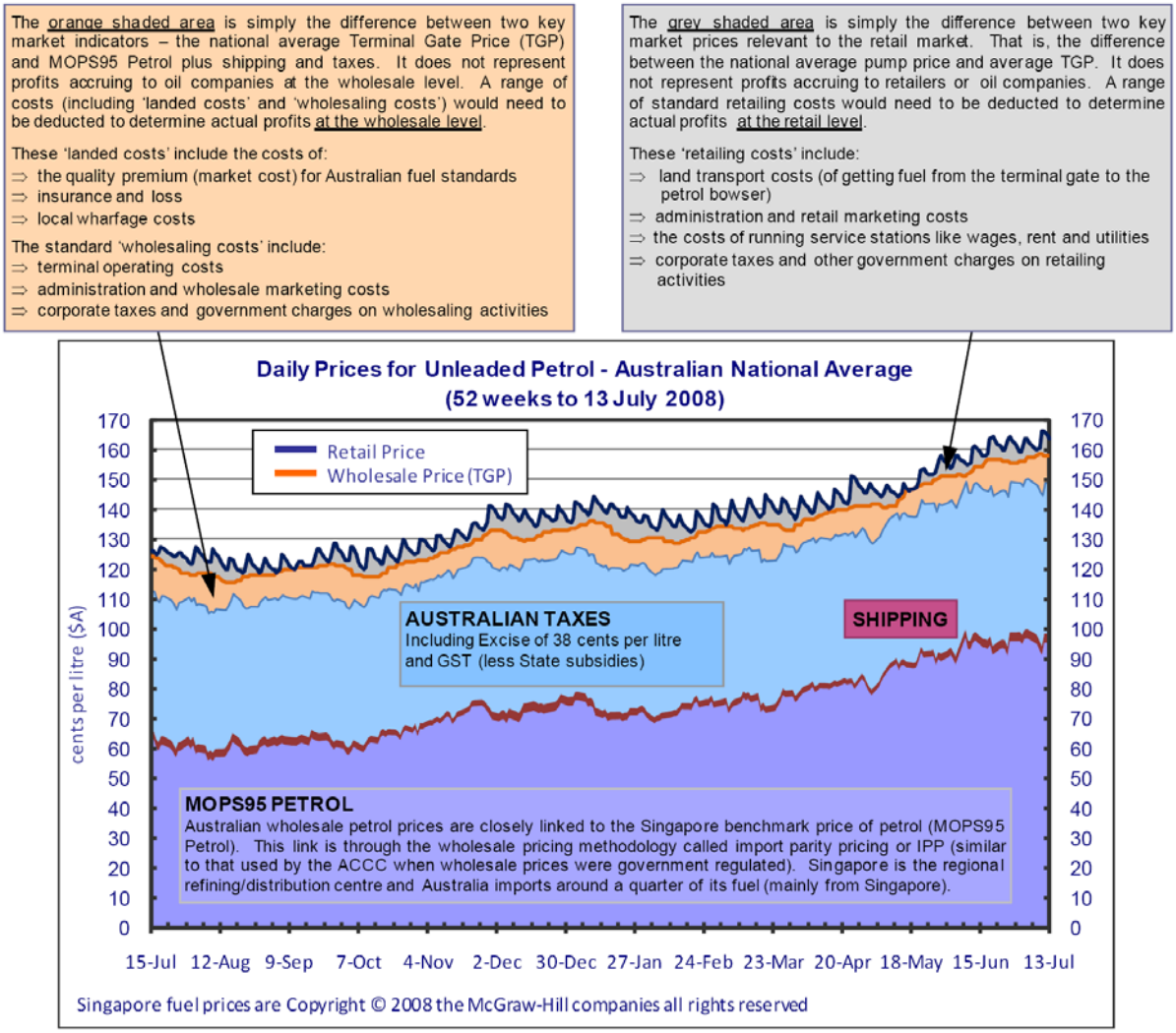
- The underlying price level is largely determined by international markets and influences and the domestic competitive market.
- In contrast, retail price volatility is caused by the structure of the retail market (Chapter 2) and by variations in local area competitive factors including price cycles (see below).

International and domestic factors can have different impacts.

- For example, there are often times when there are increasing or decreasing international petrol prices (eg. reflecting international supply and demand factors), but domestic petrol prices are moving in the opposite direction (eg. reflecting the domestic price cycle).
- As a general rule, it may take up to 1 to 2 weeks for changes in Singapore petrol and diesel prices to be reflected in Australian prices, and this time lag occurs whether prices are going up or down.

Figure 3 below illustrates this and also provides an overall 'snapshot' of movements in key international market indicators relevant to the price of petrol at the pump in Australia. It shows the contribution of the international price for petrol (MOPS95 Petrol) and landed costs (shipping & taxes) to the underlying price level (**orange line**), and the retail price cycle volatility (**blue line**) around that underlying price level.

FIGURE 3 - Australian Fuel Market Snapshot



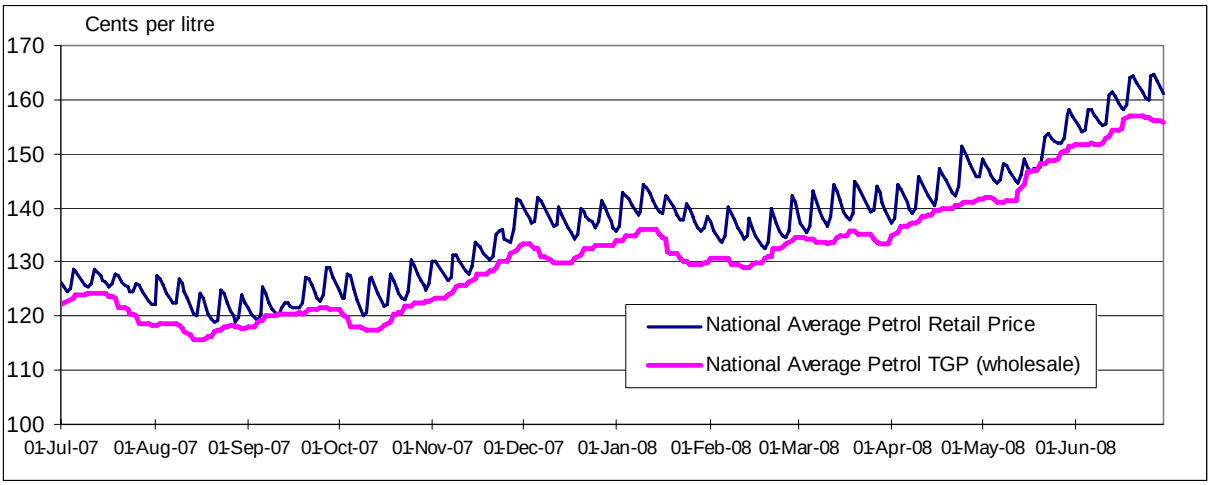
It should be noted that numerous Government and ACCC pricing inquiries, including in the 2007 ACCC Inquiry Report, have confirmed without doubt that there is a consistent and strong relationship between Australian prices and internationally traded prices of fuels in Singapore (as seen in Figure 3) and, according to the ACCC, there is "no systematic divergence" (p13).

For more detail on the key market (international and domestic) and other factors influencing petrol prices in Australia, see 'Facts About Prices & the Australian Fuel Market' (Attachment D). For the latest data on movements in international and domestic prices, see the 'AIP Weekly Petrol Prices Report' (Attachment C).

(C) RETAIL MARGINS

As shown in Figure 4, national average retail petrol prices closely follow the national average TGP (which in turn follows international petrol prices).

FIGURE 4 - National Average Petrol TGP versus Average Petrol Pump Price: 2007-08



The difference between the pump price and TGP is typically called the 'gross retail margin'.

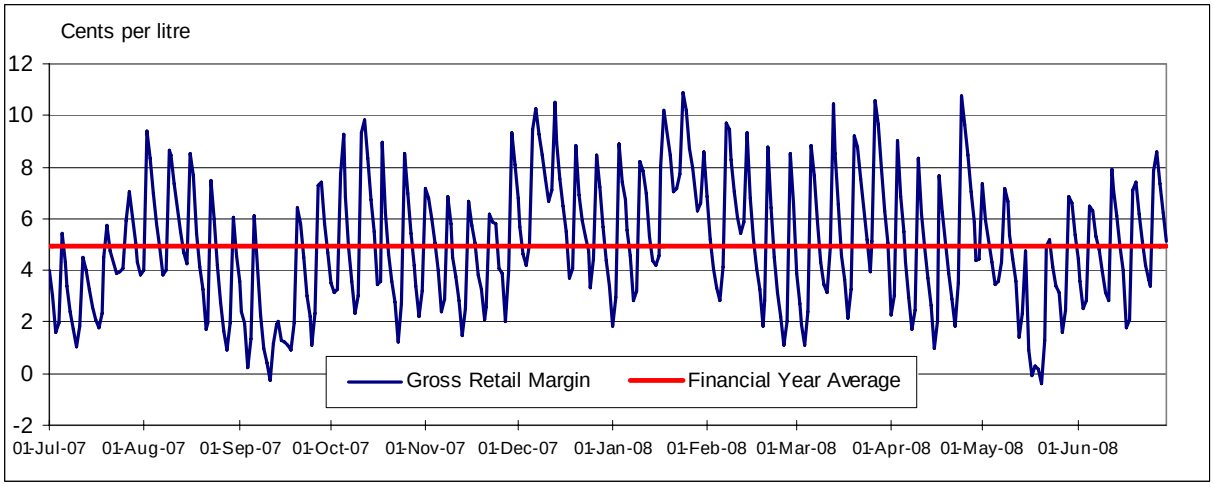
This gross margin includes profit and the amount the distributors and retailers have available to pay all of the costs from the refinery gate to the petrol bowser – including transport costs, administration and marketing costs, and the costs of running service stations like wages, rent and utilities.

Gross retail margins for 2007-08 are shown in Figure 5.

The gross margin averaged close to 5 cents per litre in 2007-08 and was similar in recent financial years.

This is consistent with the gross margins reported by the ACCC in the recent Petrol Prices Inquiry Report (p138 and p139).

FIGURE 5 - National Average Gross Retail Margin (Pump Price minus TGP): 2007-08



(D) RETAIL PRICES: DISCOUNT CYCLES

What is a Cycle?

The definition of a cycle assumed by the ACCC is that "a price cycle is considered to have occurred if there are total price movements between trough to peak of 1 cent per litre or more and from that peak to subsequent trough of 1 cent per litre or more."(p156)

Some common definitions of key points in a cycle (including retail petrol cycles) include:
- trough - refers to the lowest average daily price after a peak
- peak - refers to the highest average daily price after a trough
- cycle duration - the length of the price cycle is the number of days between two troughs
- variation/amplitude – of a price cycle is the difference in price between the peak and trough.

Drivers for Retail Discounting Cycles

The overall retail or pump price in Australia is set by the competitive market but also reflects all the costs of getting the fuel to the consumer. This includes the wholesale price (or TGP), transport costs, administration and marketing costs, and the costs of running service stations like wages, rent, utilities etc. The wholesale price is typically around 95% of retail prices (as also shown in Figures 3 & 4 above).

Historically, retail prices in metropolitan areas have followed a discounting cycle (ie. *a sawtooth pattern*) which typically has ranged up to 12 cents from peak to trough. Petrol prices fall steadily due to service station owners/operators aggressively discounting to capture market share. However, maximum discounts can only be sustained for short periods before prices recover. This is typified by a sharp lift in prices to a peak (at a later time in the week) before the discounting cycle starts again.

Customers in capital cities would be most familiar with these discounting cycles which often occur on a weekly basis. Highly visible petrol pricing boards allow both customers and competitors to readily observe these price changes.

While these cycles have tended to follow a general pattern they are not totally regular and therefore each cycle is likely to differ.

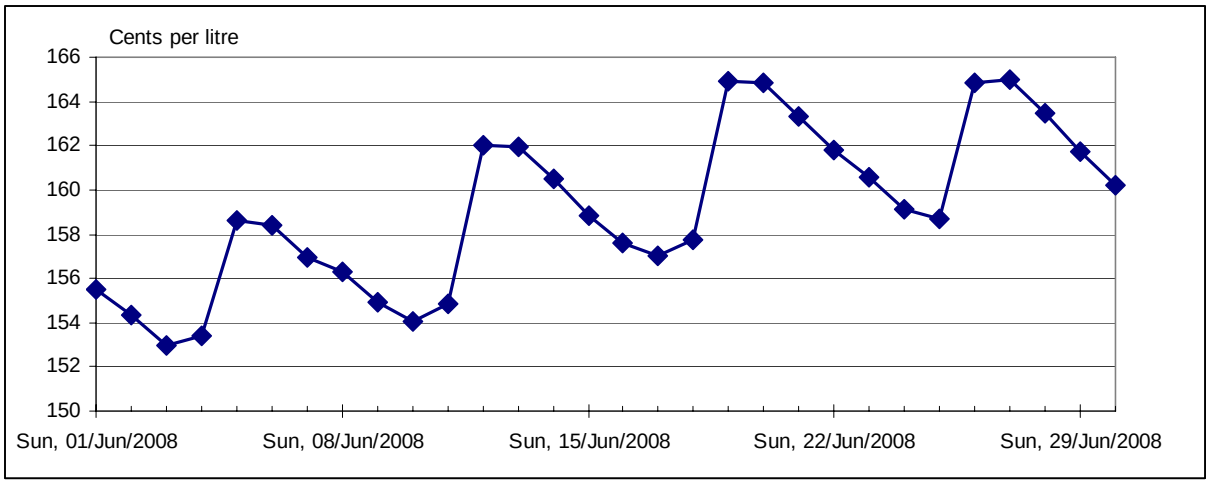
The ACCC has concluded in its past inquiries, that the discounting cycle is a clear demonstration of vigorous competition. Importantly, the recent ACCC Petrol Prices Inquiry Report concluded that there is no evidence to suggest that price cycles are 'caused' by the major oil companies (p16).

Metropolitan Retail Price Cycling

The typical saw-tooth pattern of the retail petrol cycle, including all the usual cyclical features, is illustrated in Figure 6. Figure 6 shows that, for the month of June 2008:
- the most common day for prices to peak was Thursday
- the most common days for prices to trough was Tuesday
- there were no days when prices both peaked and troughed
- the average amplitude of the cycle was around 7 cents per litre
- the weekly nature of the cycle.

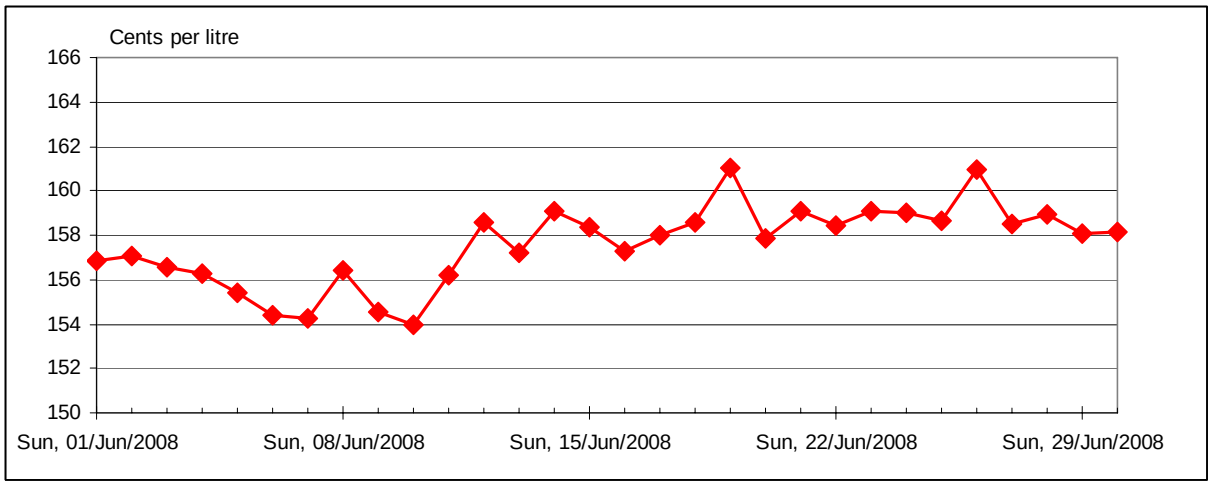
These trends are confirmed by the ACCC analysis of price cycles across capital cities in the recent ACCC Petrol Prices Inquiry Report. In summary, the ACCC concluded that *"the shape of price cycles is asymmetric – that is, prices increase rapidly over a short period and then steadily decrease. Generally, these cycles are weekly in nature (Perth is the exception) with peaks commonly on Thursdays and troughs commonly on Tuesday in recent years." (p155)*

FIGURE 6 - Retail Petrol Price Cycle – National Metro Average (June 2008)



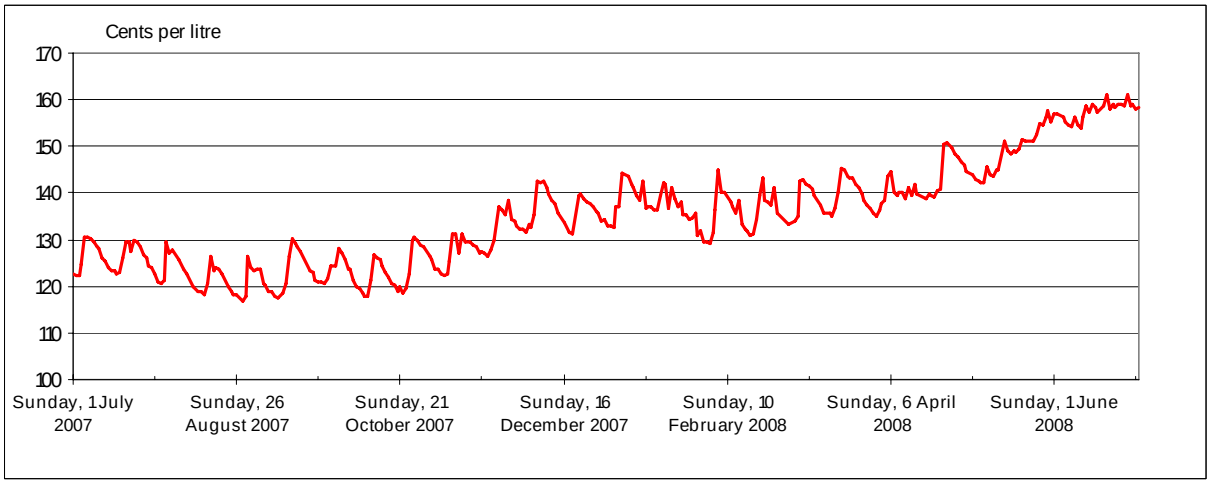
Over the same period, the price cycle for Perth (where the WA Fuelwatch Scheme applies) is shown in Figure 7. The pattern of the price cycle in Perth over June clearly is not as regular nor predicable for consumers as for the average metropolitan cycle shown above.

FIGURE 7 - Retail Petrol Price Cycle – Perth Metro Average (June 2008)



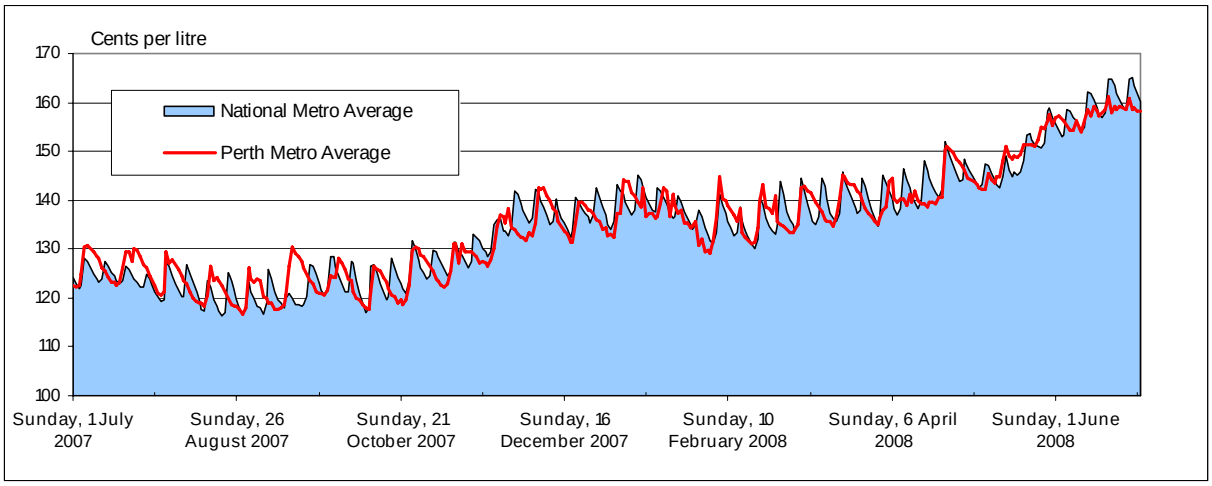
The pattern of the Perth average metropolitan retail price over a longer time period (2007-08) is shown in Figure 8. The fortnightly price cycle in Perth can be observed.

FIGURE 8 - Retail Petrol Price Cycle – Perth Metro Average (2007-08)



A comparison over 2007-08 between the Perth average metro retail price and the National average metro retail price is shown in Figure 9 below. The figure clearly contrasts the impact of the fortnightly price cycle in Perth against the weekly cycle in other metropolitan centres like Adelaide, Melbourne, Sydney and Brisbane (ie. represented by the additional shaded blue peaks in the middle of the Perth retail price cycle shown in red).

FIGURE 9 - Retail Petrol Price Cycles (2007-08):
Perth Average Metro Price versus National Average Metro Price



Retail Price Movements at Other Times (Public Holidays & Long Weekends)

Previous AIP analysis to public/government inquiries had clearly shown that retail petrol prices do not increase *because* of long weekends or public holidays.

The recent ACCC Petrol Prices Inquiry Report contained an analysis of a period covering several national and regional holidays and concluded that *"there is little evidence to support the media claim that cyclical petrol price increases before public holidays are always higher than the cyclical price increases that occur on non-holiday times".* (p16)

Why no Aggressive Retail Price Discounting for Diesel?

There is no aggressive retail price discounting for diesel as only 25% of diesel is sold through retail outlets (with much of that being sold to account customers).

In the Australian retail market, there is very little diesel sold to private customers. Most diesel is sold in bulk to commercial/industrial customers (eg. in mining, transport and farming) on long term contract. Such contracts are subject to rigorous competition under regular market tender.

Hence retail diesel prices, unlike petrol prices, are not subject to aggressive retail price discounting. At service stations, retailers concentrate on petrol and LPG discounting to drive overall fuel sales volumes and associated convenience store sales.

(E) RETAIL PRICES: CONSUMER BEHAVIOUR

The Relationship Between Point in Price Cycle and Consumer Volume Purchases

AIP members strongly believe that there is considerable evidence to suggest that consumers benefit significantly from buying heavily discounted petrol at the low point in the price cycle.

The ACCC found (in its '*Reducing fuel price variability*' Report, December 2001) that discount cycles favour the consumer, with over 60% of petrol sales occurring below the average price of the price cycle.

The ACCC reviewed this analysis in 2004, and confirmed this outcome remained valid.

In the recent ACCC Petrol Prices Inquiry Report (December 2007), the ACCC conducted a further detailed analysis of 'fuel sales by day of the week' (p176). This analysis includes volume data requested by the ACCC as part of the ACCC's formal price monitoring powers under the Trade Practices Act (section 95ZK of the TPA).

The key conclusion from this analysis was that:
"in Sydney, Melbourne, Brisbane & Adelaide, more than 60 per cent of weekly sales were made on the four days of the week (ie. Sunday, Monday, Tuesday & Wednesday) when the average daily price was below the average weekly price" (p177).

Thus, the ACCC has confirmed, through three separate and detailed analytical exercises, that the same benefit to consumers from retail price cycles has existed over the last 7 years.

In the context of these consistent and clear findings, AIP considers that there is no basis for the ACCC subsequently concluding in the Inquiry Report that *"it is not possible to say conclusively whether the cycles operate to the benefit of consumers and retailers"*. This ACCC conclusion is also at odds with several other ACCC Report findings and the ACCC's detailed consumer survey which shows that nearly 70% of consumers tend to buy petrol on low price days when the daily average price was below the weekly average price.

There was a deliberate decision by the ACCC to exclude Perth from comparisons with other major capital cities as part of the 'fuel sales' analysis on p177 of the Report. However, in Appendix P of the ACCC Petrol Prices Inquiry Report (p359), the ACCC analysis shows that there are only three days of the week in Perth when petrol is below the average weekly price and only 40% of petrol is sold on those days.

The price-volume interaction on any given day is a particularly vital relationship to observe when seeking to make a robust assessment about the impact of price cycles on consumers and on any measures which seek to alter average daily/weekly prices or the nature and predicability of current cycles operating in different Australian cities/regions.

AIP notes also that the econometric analysis in Appendix S of the ACCC's Inquiry Report has not incorporated sales volumes into the analysis.

Do Consumers Take Advantage of Price Cycles?

According to the ACCC, "many petrol consumers are price sensitive and are well aware of price cycles". To assist these consumers, the ACCC has provided advice for some time on the low price days of the week to buy petrol.

For the purposes of the recent Petrol Prices Inquiry, the ACCC commissioned ANOP to conduct an extensive survey of urban motorists in November 2007, focusing in detail on consumers' price cycle perceptions and preferences.

The key findings from the ANOP Survey for the 4 major capital cities (Sydney, Melbourne, Brisbane & Adelaide) include the following (p178):

- 83% of motorists believe there is a regular price cycle and 75% think there is a regular weekly cycle
- 90% of motorists perceive that petrol is cheaper on particular days, with 74% nominating Tuesday as the cheapest day
- 68% of motorists tend to buy petrol on particular days of the week, almost exclusively from Monday to Wednesday when the daily average price was below the weekly average price
- 20% of purchases occurred on a Tuesday (the typical weekly price cycle trough)
- Only 7% of motorists buy petrol on days that suit them.

In contrast to these results, there is a low awareness of, and response to, price cycles in Perth.

- Only 17% of Perth Motorists tend to buy petrol on particular days of the week (compared to 68% in other capital cities)
- Only 28-34% of Perth motorists buy petrol when it is cheapest.

This evidence clearly shows that motorist in capital cities apart from Perth clearly value the pattern and predicability of the regular price cycle, in terms of guiding their fuel purchasing decisions to days of the week when fuel is heavily discounted. According to the ANOP survey "there is a significantly lesser amount of shopping around in Perth where only 1 in 5 motorists always try to buy when fuel is cheapest".

Motorist Search Costs

AIP considers there is considerable information that is freely and readily available to consumers, including on a current or real time basis, about comparative fuel prices at a local area level including:

- service station price boards
- newspapers
- TV
- internet sites of fuel retailers
- motoring organisations websites/advice
- government or consumer affairs agencies
- private sector businesses providing extensive retail petrol price information on a free or commercial basis (eg. Informed Sources, FuelTrac and Motormouth).

The value to consumers of any additional information to that already freely provided must consider, among other things,

- the value and timeliness of the new information to consumers
- the ability/desire of the motorist to respond to the information
- the relative costs of the motorist responding (in terms of relative petrol used and the motorist's time and convenience).

For example, it is not unreasonable to expect consumers to only avail themselves of a 'known' cheaper fuel price in their local area if the price advantage on offer more than compensates them for any change in the timing and cost (additional distance travelled) of departing from their more convenient and regular travel routes and purchasing day/time.

In summary, the provision of 'more or more timely information' is not a desirable outcome unless it drives better outcomes for consumers and leads to improved economic efficiency or welfare overall.

For example, any benefits from potential lower consumer search costs from restricting intra-day price movements may be overwhelmed by less consumer certainty associated with more unpredictable petrol prices throughout the week (as occurs in Perth).

(F) RETAIL PRICES: REGIONAL VARIATIONS

The difference between metropolitan and regional retail prices is due to a number of factors including market structure, competition and small business commercial drivers.

Some of the key features of the retail market in regional Australia typically include the following:

- Prices are more stable in regional areas because of a general absence of price discounting.
- The general absence of discounting in regional/country areas also means that regional prices appear to be higher than fully discounted or average city prices.
- Retail margins are typically higher in the country compared with major capital cities, due to lower fuel volumes and shop sales over which to spread service station operating costs.
- The average customer base per service station is around 2,000 people in regional Australia (and well below in many towns) whereas metro service stations typically have a customer base of around 4,000 to 5,000 people.
- Regional service stations typically see 1 tanker per 2-3 weeks versus several tankers per day at some metropolitan sites.
- Freight is typically around 1.5 to 3 cents per litre greater for country than city delivery.
- Distribution costs may be significant for some country areas where fuel must be stored in depots and double-handled, rather than being delivered directly from coastal terminals.
- Competitive forces and costs also vary greatly between country towns, so that pump prices do not just reflect freight and handling differences.
- Generally the more successful service stations in regional Australia are in locally based chains of branded and unbranded independent retailers who are often involved in fuel distribution as well.

Retail prices in regional areas are largely set by independent owner/operators (including those who sell fuel supplied by one of the major brands under license).

In the recent ACCC Petrol Prices Inquiry (December 2007), the ACCC concluded that in regional and country petrol markets *"the number of competitors is less, costs were higher (transport, distribution and site operation), and regular price cycles are absent. As a general rule, retail margins are consequently higher"*. (p145)

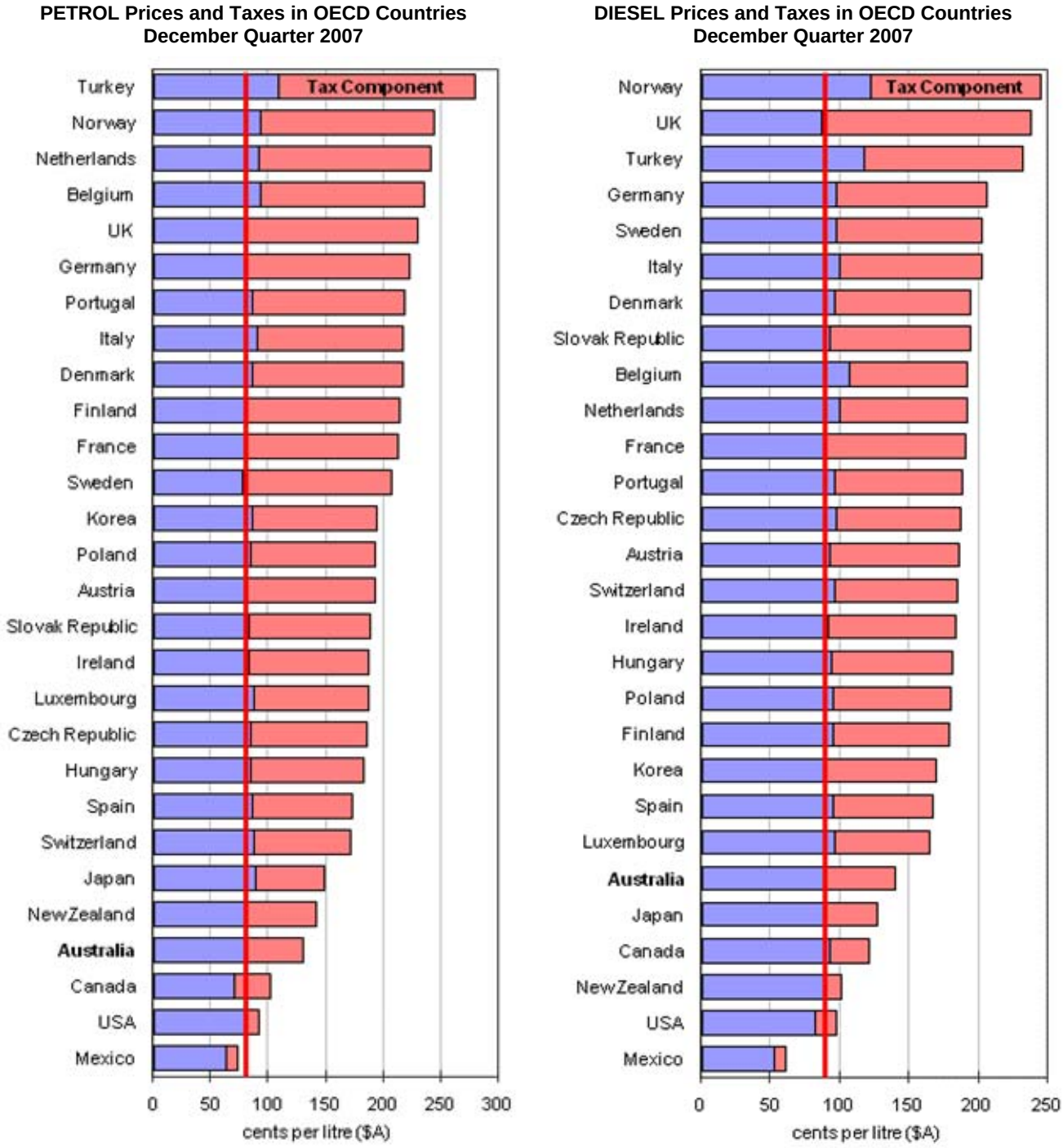
(G) RETAIL PRICE: INTERNATIONAL COMPARISONS

While international price pressures in recent years have affected retail price movements here, Australia continues to have among the lowest petrol and diesel prices of all OECD countries - both on a pre and post tax basis - according to official statistics from the Federal Department of Resources, Energy and Tourism (and the International Energy Agency).

- Australia's comparative OECD ranking is shown in Figure 10 below.

While exact rankings can change slightly from quarter to quarter (largely reflecting exchange rate movements from period to period), Australia has enjoyed among the lowest rankings for some time, largely reflecting the fundamentally competitive nature of Australia's downstream sector and the comparatively low fuel taxation here. This is a view shared by many government and ACCC reviews of the petroleum market and by many informed commentators and analysts, including the International Energy Agency.

FIGURE 10 - Petrol & Diesel Prices & Taxes in OECD Countries



Source: *Australian Petroleum Statistics*, Department of Resources, Energy & Tourism

When comparing Australian petrol and diesel prices to other countries, allowance must be made for different government taxes and tax rates applying to fuel in each country and also for any subsidies and road user charges that apply in those countries but not in Australia.

- For example, New Zealand has a very low tax on diesel at the pump, which is the GST Only (12.5%). However, the New Zealand Government applies a road user charge to diesel powered vehicles. A passenger diesel vehicle (less than 3.5 tonnes) traveling 25,000 km per year will pay road user charges of around NZ$820 per annum in New Zealand.

- In addition, many countries in the Asian region heavily subsidise retail fuel sales.

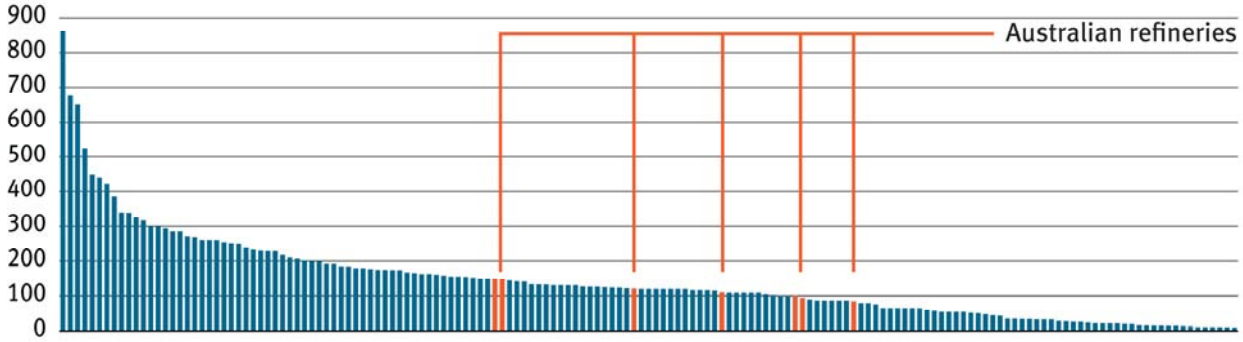
(H) RETAIL PRICES: FUTURE PRICE PRESSURES

A key ongoing industry concern is government policies and regulation that raise uncertainty about the future viability of Australian refineries and the downstream petroleum sector more broadly, including the retail market.

In this context, the development of effective climate change policies that do not stifle economic growth potential is the most significant challenge to the ongoing viability of Australia's trade exposed refining and downstream industry.

Since a significant proportion of liquid fuel (around 25%) is imported into Australia, largely from countries that are unlikely to impose a carbon cost on their refineries, it will be essential that Australian refineries are recognised as trade exposed, energy-intensive businesses under an Australian emissions trading scheme. Future Australian industry viability will be dependent on ensuring that Australian refineries are not placed at a further disadvantage relative to regional competitors in the Asia-Pacific (see Figure 11 below) as a result of additional carbon costs. Depending on the point of acquittal for emissions from liquid fuels, it will also be important that there are no barriers to the pass through of any carbon price to final fuel consumers in Australia.

FIGURE 11 - Asia-Pacific refinery capacity (thousands of barrels per day)



The potential impact of Government climate change policies on fuel prices and the ongoing viability of Australian refineries are significant industry and community issues.

For example, from a consumer perspective, emissions permits (under an Emissions Trading Scheme) valued at $30 per tonne of CO_2 are equivalent to an additional direct cost of 8-9 cents per litre on the retail price of petrol and diesel.

AIP member companies are working closely with the Australian Government to assist with the development of a comprehensive and sustainable suite of policies to address climate change concerns.

(4) THE NATIONAL FUELWATCH SCHEME LEGISLATION: OBJECTIVES, RATIONALE, OPERABILITY & IMPLEMENTATION

This Chapter outlines AIP's overall view of the National Fuelwatch Scheme and provides specific comments on the legislative package and the publicly available analysis and communications supporting the National Scheme. The main focus of AIP's comments is on the objectives and rationale for the National Scheme and on appropriate implementation principles from AIP's perspective. AIP considers that some assumptions and statements made in the legislative package are unsupported by clear and publicly available evidence or detailed analysis.

(A) THE NATIONAL FUELWATCH SCHEME

The National FuelWatch Scheme, in it's current form and as reflected in the current legislative package, mirrors the WA model and includes the following features.

- Sites in metro and major regional centres will notify the ACCC of their next day's prices by 2pm the day before and maintain this advised price for a 24 hour period (the '24 Hour rule').
- Apart from major centres, rural authorities will be able to "opt in" (subject to negotiation).
- The scheme will apply to ULP, PULP (95 & 98), LPG, diesel and biodiesel blends.
- The price information collected will be made available to consumers through email, SMS alert, toll free number and through a dedicated website (ie. with station by station, day by day and suburb by suburb petrol price information).
- The Scheme is estimated to cost taxpayers $20.9 million over four years.
- The Scheme will commence on 15 December 2008.
- The Scheme will be reviewed 12 months after the start date.

It is important to underline that any current analysis or assessments about the potential impact of a National FuelWatch Scheme might be overtaken by any changes to the Scheme that may occur through the legislative, consultation and implementation phases.

In addition, an implicit assumption has been made by the Scheme's proponents that the impacts of the national adoption of Fuelwatch will have the same impact as that which has occurred in Western Australia. AIP considers that this can only be assumed with confidence if there has been a robust analysis of the potential impacts of the Scheme on all markets and local areas where the Scheme will operate, recognising the established and unique features of each retail fuel market.

(B) OVERARCHING AIP VIEW

In AIP's initial submission (2 July 2008) to this Senate Inquiry, AIP made the following overarching comments about the adoption of a National Fuelwatch Scheme.

> *"The Government announced a National Fuelwatch Scheme on 15 April 2008.*
>
> *In a statement on 16 April 2008 (Attachment B), AIP indicated that AIP member companies will co-operate with the Government's proposed implementation of a National Fuelwatch Scheme.*
>
> *AIP member companies did not express opposition to the National Fuelwatch Scheme as is regularly suggested by some commentators. Rather, AIP member companies expressed concern about some of the Scheme's proposed features and possible impacts."*

"AIP believes that any government policy measure to intervene in a competitive market is a decision for government.

- *This would include government intervention in the Australian petrol market, which the ACCC has recently found to be "fundamentally competitive".*

AIP considers that market determined outcomes have proven to be better for consumers than regulated outcomes.

- *This is evidenced by Australia's open and competitive market delivering low petrol and diesel prices by international standards.*

Given the Government's decision to introduce a National Fuelwatch Scheme, AIP is strongly of the view that this government intervention into the free market in Australia to regulate the retail price of petrol must be:

- *equitable – applies to all market participants;*
- *transparent – leads to improved information for all parties;*
- *effective – the scheme's design and implementation achieves the government's objectives of increasing consumer information and not increasing prices; and*
- *administratively efficient – low compliance and administration costs.*

In addition to these key implementation principles, AIP strongly believes that the objectives of the National Fuelwatch Scheme must be clearly stated by the Government and publicly communicated to all fuel consumers.

AIP supports effective measures that seek to improve the quality and timeliness of information to consumers in a competitive market setting.

We do not support, however, government regulation (the 24 hour rule) *which prevents the delivery of competitive market outcomes to consumers such as making intraday price movements, including price discounting, illegal.*

AIP has also indicated that it will be important for the Government to ensure that there are no other anti-competitive effects or unintended consequences from the implementation of a National Fuelwatch Scheme.

For example, industry concerns include:

- *the potential reduction in consumers' ability to access discounted fuel;*
- *excessive administrative and compliance costs; and*
- *lack of predictability for consumers in the fuel price cycle.*

AIP expects that further analysis of the costs and benefits of the Scheme, including the issues and concerns noted above, will be conducted prior to the implementation of the National Fuelwatch Scheme. Such analysis should include the expected impacts of the Scheme on fuel prices and the discounting cycle in all markets and local areas where the Scheme will operate, drawing on information and experience in the WA fuels market, as well as established features of the fuel markets in other States/Territories.

Similar rigorous analysis must also be undertaken as part of the Government's announced review of the National Scheme after 12 months of operation."

The industry concerns noted above are outlined in detail in this chapter and in Chapter 5.

There are a number of statements and assumptions underpinning the objectives and rationale for the National Scheme that AIP considers are not supported by evidence or publicly available analysis, including in the Explanatory Memorandum (EM), the Regulatory Impact Statement (RIS), the ACCC Inquiry Report and in public communications. These are considered below.

(C) OBJECTIVES & RATIONALE FOR THE NATIONAL FUELWATCH SCHEME

AIP considers that there has been no clear, consistent and easily understood explanation available to Australian consumers of the primary objective of the National Fuelwatch Scheme.

In particular, we consider there have been conflicting public statements by the Scheme's proponents and an ongoing public redefining of the Scheme's key objective. There is also conflicting guidance from the ACCC, since there is a disconnect between the findings and the recommendations in the ACCC Inquiry report, and inconsistencies with previous ACCC inquiry recommendations in relation to the WA Fuelwatch Scheme.

There can be no dispute that the National Fuelwatch Scheme was initially communicated to the general public as a measure intended to provide 'savings' to Australian consumers at the pump in the face of rising international and domestic fuel prices. The expected savings were estimated at 1.9 cents per litre according to econometric analysis by the ACCC and were promoted on that basis. The Petrol Commissioner has been reported as indicating available savings of up to 5 cents per litre. Government communications then shifted to emphasise that the objective of the scheme was to provide intra-day price stability to consumers and reduce search costs for consumers. Following this, the objective of Fuelwatch was emphasised as a 'fuel price transparency measure', to address an information imbalance between fuel retailers and consumers as a result of the pricing information provided to retailers by '*Informed Sources'*.

The 'price savings' are no longer strongly emphasised in current communications. In fact, the ACCC Chairman has indicated that the ACCC's relevant benchmark for recommending the national adoption of the Scheme was that "Perth motorists did not suffer harm" as a result of the introduction of FuelWatch[1]. In an ACCC media release on 29 May 2008, the ACCC has defined harm as *"consumers paying higher prices for petrol"*. This benchmark will be discussed further in the context of the ACCC's econometric analysis of the potential impacts of the National Scheme on prices (see Chapter 5).

AIP encourages the government and the ACCC to ensure that the primary objective of the National Fuelwatch Scheme, and all of the likely/possible consequences, are clearly understood by fuel consumers – particularly those consumers who are currently benefiting from significant savings on low price days of the week.

AIP also urges consumers to carefully assess whether the benefits claimed from the introduction of this Scheme, and the Scheme's objectives, will in fact be delivered.

Following much public commentary on the National Scheme and its claimed benefits since announcement on 15 April, the legislation package was entered into Parliament on 29 May.

The Regulatory Impact Statement (RIS) contained in the legislative package indicates that the Government has two objectives in relation to Fulewatch (p6) including to:

- address petrol price volatility and hence allay consumer anxiety; and
- reduce consumer search costs and enhance retial petrol price transparency.

The Explanatory Memorandum to the National Fuelwatch Bills (p1) indicates that there are in fact 6 objectives of the National Scheme, including:

(a) empower consumers to make informed decisions and purchase fuel at the lowest possible price;
(b) increase reliability and certainty of fuel price information available to consumers;
(c) reduce consumer search costs;
(d) address consumer anxiety by eliminating intraday price volatility;
(e) address the existing information imbalance between petrol retailers and consumers; and
(f) promote competition in the retail fuel market.

[1] ACCC testimony to the Senate Standing Committee on Economics (Estimates) on 5 June 2008 (p15,16,17,48, 68, 69, 70 & 71).

These objectives also represent the underlying rationale or case supporting the adoption of a National Fuelwatch Scheme. AIP's comments on these objectives, and on some additional statements of benefit provided in the legislative package, are outlined below.

Objective (a) - Empowering consumers to make informed decisions and purchase fuel at the lowest possible price

AIP notes that:

- consumers are already making informed and timely purchasing decisions on the basis of:
  - considerable information that is freely and readily available about comparative fuel prices at a local area level - including on a current or real time basis (see p19);
  - their clear understanding of the operation and benefits of the weekly cycle (p19);
- according to the ACCC Inquiry Report, consumers are already purchasing fuel at the lowest weekly price (see p18 & 19).

The ACCC Petrol Prices Inquiry Report itself (p252) recommends that before considering the adoption of a National Fuelwatch Scheme, there needs to be a detailed assessment of, among other things, the effect of a National Scheme on price cycles and consumers' ability to predict the days of the week when prices are likely to be relatively low.

AIP is not opposed to, and would assist in the development of, any measures which seek to provide timely information to fuel consumers to make informed purchasing decisions.

Depending on the nature or design of the price information system and the extent to which the problem of retailer free-riders is addressed, AIP member companies would consider continuing to provide data in the same way as they currently do for Informed Sources. Similarly, AIP member companies are unlikely to take exception to a mechanism that enabled consumers to access Informed Sources data on a local area basis, provided 'free-rider' retailer issues can be resolved.

Objective (b) - Increase reliability and certainty of fuel price information available to consumers

Compared to the currently available (known/certain) pricing information, AIP considers that it is difficult to assess any potential increase in reliability and certainty of pricing information to consumers as a result of the National Fuelwatch Scheme (as currently proposed). Clearly, an accurate assessment of reliability improvements can only be made once the final design of the National Fuelwatch Scheme is known and there has been some significant experience in relation to the Scheme's operation.

The ACCC Petrol Prices Inquiry Report itself (p252) recommends that before considering the adoption of a National Fuelwatch Scheme, there needs to be a detailed assessment of, among other things, the dependence on the media to realise the benefits of a National Scheme and the potential for a reduction in the predicability of price to consumers.

Objective (c) - Reduce consumer search costs

AIP considers that consumer search costs for petrol are already reasonably low, once adequate consideration is given to: (i) the considerable information that is freely and readily available about comparative fuel prices at a local area level - including on a current or real time basis; and (ii) the likelihood/capacity of consumers to respond in a different way to any additional pricing information (to that available now) provided by Fuelwatch.

Importantly, the RIS indicates (p9) that any benefits created by reducing consumer search costs from restricting intra-day price movements may be lost due to less certainty associated with more unpredictable petrol prices throughout the week (as occurs in Perth).

Objective (d) - Address consumer anxiety by eliminating intraday price volatility

As noted above, consumer anxiety might be expected to increase if restricting intra-day price movements leads to consumer uncertainty associated with less predictable petrol prices throughout the week (as concluded in the Regulatory Impact Statement (RIS) on page 9).

Objective (e) - Address the existing information imbalance between petrol retailers and consumers

AIP does not accept that a case has been made that the use of Informed Sources services by fuel retailers is acting to the detriment of consumers.

AIP member companies believe that retail price competition is maximised when businesses are fully aware of the going market prices in the local areas. The Informed Sources services empower such competition, particularly when compared to previous approaches relying on physical sighting of price-boards of local competitors.

As noted above, AIP member companies would take no exception to a mechanism that enabled consumers to access Informed Sources data on a local area basis, provided the retailer 'free-rider' issue can be resolved.

Objective (f) - promote competition in the retail fuel market.

AIP considers there is little or no public explanation or rigorous analysis in the legislative package or in the ACCC Petrol Prices Inquiry report on the potential impact of the National Scheme on competition and the structure of the retail market in the future.

The ACCC Petrol Prices Inquiry Report itself (p252) recommends that before considering the adoption of a National Fuelwatch Scheme, there needs to be a detailed assessment of, among other things, the competition effects of the price commitment (24 hour rule), particularly on independent retailers, and whether regional/country markets are sufficiently competitive to benefit from the price information to be provided under the National Fuelwatch Scheme.

Perhaps this ACCC view responds to a concern the ACCC has previously tabled that the WA Fuelwatch arrangements, particularly the 24 hour rule, has severely limited the role of independent retailers in the WA fuel market and their ability to be a competitive force.

The RIS supporting the legislative package also concludes that *"independent fuel retailers provide some evidence that Fuelwatch has not enhanced competition in Western Australia and has, in fact, harmed the competitive position of independents".*

AIP believes that further detailed assessment and consultation is required to clearly establish that there are no unintended or anti-competitive impacts from the national introduction of a scheme similar to the WA Fuelwatch.

Public testimony by the ACCC to the Senate Standing Committee on Economics (Estimates) on the 5 June 2008 indicated that such an assessment may have already been undertaken by the ACCC in consultation with Treasury (see Hansard p22 & 26), but has not yet been made publicly available.

This assessment also appears to have considered the other serious issues of particular concern to the ACCC on p252 of their Inquiry Report (ie. that should be considered before adoption of the scheme and 24 hour rule nationally).

Specifically, the Chairman of ACCC indicated (p26 Hansard) that these issues including:
"the extra potential harmful effects for rural and regional Australia where there is less competition, the potential to affect the presence and influence of independents and the potential for the reduction in the predictability of price to consumers—were the subject of further analysis and further work that we did in conjunction with Treasury and the department of finance. The administrative costs were dealt with the department of finance and were dealt with in terms of the material that was put to the ERC and, ultimately, as I understand it, in the decision that was made by government."

Other Claims and Rationale

An additional rationale for the adoption of the Scheme is the claim that Fuelwatch encourages retailers to sell at their best price or risk being effectively excluded from the market for 24 hours.

- AIP considers that the clear impact of the 24 Hour rule will be that it will not encourage maximum (unfettered) competition.
- It is very difficult to make an accurate assessment of the likely responses of retail chains and smaller independent retailers.
- This claim also appears to ignore the impact on the majority of consumers who show allegiance to their local (preferred) service station and/or fuel brand.

Claims in the legislative package that the oil majors have a strong retail presence is wrong and reflects a limited understanding of the distinction between market share and control over price setting (as outlined in detail in Chapter 2).

(D) THE OPERABILITY OF THE LEGISLATION

The operability of the legislation will be improved through open consultation on the most efficient design and implementation of the scheme. AIP notes that there has been little consultation with industry to date on the details and operation of the National Scheme.

AIP member companies will provide detailed comments on the workability of the scheme as defined in the legislative package, including on the basis of their practical experiences with the WA model.

AIP notes that there is almost no publicly available details on the ACCC's compliance and enforcement regime which will apply under Fuelwatch, but the costs of such a regime have been estimated with some precision (p8 of EM).

AIP also notes that civil penalties will apply where retailers notify a price for the 24 hour period, but do not sell fuel at the notified retail price. There is no explanation in the legislative package of what this means in the context of 'stockouts' of fuel at service station sites running out of fuel and what evidence will be required to satisfy inspectors that there is no hoarding occurring.

(E) THE LEGAL BASIS FOR THE LEGISLATION

The Government intends to use its corporations power to achieve nation-wide implementation of the National Fuelwatch Scheme from 15 December 2008. AIP notes that concerns have been raised by legal experts in relation to whether the Bill may be unconstitutional as it applies to 'unincorporated entities'. AIP notes that unincorporated entities include independent petrol retailers, who represent a significant and increasing presence in the Australian retail market (as outlined in Charter 2).

AIP expects that this issue would be rigorously assessed by the Government, as the exclusion of a significant class of retailers from the scheme would seriously impact on the Scheme's workability and impact.

(5) IMPACTS OF THE NATIONAL FUELWATCH SCHEME

This Chapter considers the potential impacts of the National Fuelwatch Scheme on prices, price cycles, competition, consumers and business - largely based on the experience and evidence related to the operation and impacts of the WA Scheme.

(A) INTRODUCTION

Australia's open and free market has delivered to consumers low fuel prices by global standards. Against this performance, AIP considers that it must be clearly demonstrated how government intervention in the domestic retail market (particularly the regulation of retail fuel prices via the 24 hour rule) would, in fact, deliver improved outcomes to Australian consumers and the broader economy including:

- consistently lower prices to consumers than currently occurs;
- a higher level of supply reliability than currently enjoyed by consumers;
- improved price signals to consumers about energy efficiency; and
- more broadly, improved price signals and incentives to invest in the downstream petroleum industry.

It is AIP's view that retail price regulation under the 24 hour rule will not deliver improved market and supply outcomes, nor will it deliver lower prices to consumers than they currently enjoy.

In addition, given the costs of regulation to government, business and the economy, AIP considers that it is not satisfactory for the case for a National Fuelwatch Scheme to be made on the basis that "it will not harm motorists".

Since the case for a National Fuelwatch Scheme has been based on the perceived success and positive economic and consumer impacts of the WA Fuelwatch Scheme since its commencement in 2002, the impact of the WA Scheme on prices, price cycles, competition, market structure and consumer behaviour needs to be rigorously assessed.

AIP notes that there has been little consultation with industry to date on the details and operation of the National Scheme.

(B) IMPACTS OF THE SCHEME ON 'PRICES'

A critical element of the case for the national adoption of the Fuelwatch Scheme was the claimed price savings provided by the WA Scheme, as demonstrated by a comparison of price levels between Perth and eastern capital cities. After all, it is not unreasonable to assume that consumers would not be satisfied with more pricing information if higher petrol prices and less competition were the associated costs.

The potential price savings highlighted by the ACCC, and subsequently by the Government, was 1.9 cents per litre (cpl). This was based on econometric analysis contained in Appendix S to the December 2007 ACCC Petrol Prices Inquiry Report. This analysis was later supplemented with analysis results outlined in an ACCC media statement on 29 May 2008.

The econometric analysis in Appendix S seeks to test whether the introduction of Fuelwatch was associated with a 'structural break' in petrol prices in WA, by comparing the relative price levels in Perth with the average of the eastern capitals before and after the introduction of Fuelwatch. The analysis breaks the price data series (provided by Informed Sources) into two periods - 1998-2000 and 2001-2007. The WA FuelWatch scheme commenced on 2 January 2001 (but we understand it was not fully operational until September of that year).

The results show that in the second time period (2001-07), the weekly minimum average prices are 0.90 cpl lower and weekly average prices are 1.92 cpl lower. Monthly average prices were estimated as 1.86 cpl lower.

The ACCC's results are the subject of significant caveats - as outlined in detail in Appendix S (p377) and the main body of the ACCC's Report (p252). The ACCC acknowledges that the main problem with the analysis is that you cannot be sure that the price declines (assuming they are robustly calculated) are due to FuelWatch.

There is no attempt by the ACCC to analyse 'causation' of the structural break, just to identify 'correlation'. They suggest that results observed could in fact be due:

- to some unspecified change in the retail market in WA.
    - AIP considers that the most obvious change is the entry of the supermarkets (Coles and Woolworths) into WA, and this may go some way to explain any structural break.
- "something else" like higher relative economic growth in Perth.

A more robust and complete econometric analysis would seek to test for (at a range of levels), and explain in statistical terms, why the structural change occurred - rather than simply suggesting that price changes might be related to Fuelwatch.

Apart from the econometric analysis, the ACCC also indicates that the data series constructed for the purposes of the analysis might also have some serious limitations. For example, the ACCC analysis does not include any allowance for changes in the relative cost of transport/freight between Perth and other capitals over the period of the analysis. AIP considers that the omission of any changes in freight cost relativities may have a significant impact on the ACCC's results and should be further investigated. In addition, the analysis does not consider fuel sales over the week, or over the period of analysis – that is, fuel sales volumes are not incorporated into the econometric analysis.

There has been substantial rebuttal and criticism of the ACCC's econometric modelling, the economic results, the data series used by the ACCC, and on the ACCC's reporting of their analysis. In the face of the significant and ongoing public criticism of the econometric analysis, the ACCC Chairman has clarified that the purpose of the econometric modelling was simply: *"to enable us (ACCC) to be satisfied that no harm had come to Australian motorists through the adoption of the FuelWatch scheme in Perth."*[2]

The ACCC Inquiry Report acknowledges analysis from 'Informed Sources' which shows an increase in WA prices averaging 1 to 1.5 cents following the introduction of FuelWatch (p246). There is no attempt to reconcile this analysis with the ACCC's own assessment, other than to suggest the issue needs to be addressed if FuelWatch is to deliver a net public benefit. The findings from Informed Sources are also consistent with analysis conducted by motoring associations showing lower petrol prices in eastern capitals compared to Perth.

The Institute of Public Affairs (Professor Sinclair Davidson) provided a critique of the econometric analysis conducted by the ACCC. His research casts doubts on the ACCC's claim that the FuelWatch scheme has lowered petrol prices in WA. Professor Davidson found that the ACCC analysis was highly sensitive to the starting and end points of the time period under consideration. Minor changes to these start and end points reduce the statistical significance of FuelWatch on petrol prices.

Professor Don Harding of Latrobe University, who has econometric expertise, has also completed an assessment of the ACCC's econometric analysis, and completed an econometric analysis himself based on a replication of the ACCC's data.

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[2] ACCC testimony to the Senate Standing Committee on Economics (Estimates) on the 5 June 2008 (page 16)

The key conclusions from Professor Harding's econometric analysis were:

- *"the ACCC findings are not robust"; When I apply the correct version of the procedures used by the ACCC to the correct variable I find that the data does not support the original ACCC finding. Specifically, it is not possible to conclude as the ACCC did that FuelWatch did not raise petrol prices in Western Australia."*
- *the econometrics in Appendix S of the ACCC Report is "deeply flawed" and "substandard in application of techniques and in reporting of what was done"*

Both Professors Davidson and Harding are also very critical of the ACCC's reporting of its analysis.

- Professor Davidson suggests that *"ACCC data has not been released to the public, nor have they been very clear as to what analysis has been done. The ACCC has been vague in reporting their econometric techniques and have simply published tables, expecting the public to accept their analysis on face value"*.
- Professor Harding supports this view and also recommends that *"the quality of econometric work is always improved by public scrutiny"*.

What is clear is that the ACCC's analysis has only been peer reviewed within Government – it has not been independently and rigorously assessed. This is in part because the full details and data associated with the ACCC's econometric analysis are not publicly available.

AIP considers such an independent assessment needs to occur as a priority, so Australian consumers can have confidence the National FuelWatch Scheme will not lead to higher prices overall, with consequent economic impacts.

(C) IMPACTS OF THE SCHEME ON 'COMPETITION'

As noted above, AIP considers there is little or no public explanation or rigorous analysis in the legislative package or in the ACCC Petrol Prices Inquiry report on the potential impact of the National Scheme on competition and the structure of the retail market in the future.

The ACCC Petrol Prices Inquiry Report itself (p252) recommends that before considering the adoption of a National Fuelwatch Scheme, there needs to be a detailed assessment of, among other things, the competition effects of the price commitment (24 hour rule), particularly on independent retailers, and whether regional/country markets are sufficiently competitive to benefit from the price information to be provided under the National Fuelwatch Scheme.

One of the few assessments made in the legislative package in relation to competition impacts is contained in the RIS, which concludes that *"independent fuel retailers provide some evidence that Fuelwatch has not enhanced competition in Western Australia and has, in fact, harmed the competitive position of independents".*

AIP believes that further detailed assessment and consultation is required to clearly establish that there are no unintended or anti-competitive impacts from the National Fuelwatch Scheme.

This analysis must consider the current and future structure of the retail market (as outlined in Chapter 2) and the scope for retailers and retailing chains to respond efficiently to the price regulation introduced by the 24 hour rule.

Public testimony by the ACCC to the Senate Standing Committee on Economics (Estimates) on the 5 June 2008 indicated that an assessment of the impact on competition of the National Fuelwatch Scheme has already been completed. This assessment was undertaken by the ACCC in consultation with Treasury (see Hansard p22 & 26), but has not yet been made publicly available (see page 27).

(D) IMPACTS OF THE SCHEME ON 'PRICE CYCLES & DISCOUNTING'

The clear evidence in the ACCC report is that since the WA Fuelwatch Scheme was introduced, the retail cycle in Perth has become flatter (smaller amplitude) and of longer duration (2 weeks) compared to the retail cycles currently operating in eastern capital cities. This impact is also clearly illustrated by AIP analysis in Chapter 3 of this submission.

In simple terms, a flattening and lengthening of the cycle in Perth means that retail price discounting does not occur in Perth to the same extent as in other capital cities.

Consumers will naturally be concerned if heavily discounted fuel is not available to the same extent once the National Scheme is operational.

More broadly, the extent to which the impacts in WA will happen on the East Coast when a National Scheme is introduced is uncertain and no attempt has been made by the ACCC to analyse the likelihood of this occurring in the context on these markets. To a large extent, it will depend on the business strategies adopted by retailers and reatiling chains in response to the Scheme.

(E) IMPACTS OF THE SCHEME ON 'CONSUMER BEHAVIOUR'

The ACCC Petrol Prices Inquiry Report provides a detailed survey of consumers' price cycle perceptions and preferences (by ANOP) – see page 19 of this Submission for the Survey's key findings. The Survey clearly shows that consumers in capital cities apart from Perth clearly value the pattern and predicability of the regular price cycle, in terms of guiding their fuel purchasing decisions to days of the week when fuel is heavily discounted. In contrast, "there is a significantly lesser amount of shopping around in Perth where only 1 in 5 motorists always try to buy when fuel is cheapest" (p280).

The Survey supports AIP's overall view that consumers are already making informed and timely fuel purchasing decisions on the basis of a clear understanding of the operation and benefits of the weekly pricing cycle and on the basis of the considerable pricing information that is freely and readily available about comparative fuel prices at a local area level. This conclusion is also supported by the ACCC Inquiry Report's key finding that most consumers continue to purchase fuel at the lowest weekly price. This is clearly providing cost savings to consumers.

Given this consumer behaviour in the eastern capitals, any value to these consumers of additional (taxpayer funded) pricing information must consider, among other things:

- the value and timeliness of the new information to consumers
- the ability/desire of the motorist to respond to the information
- the relative costs of the motorist responding (in terms of relative petrol used and the motorist's time and convenience).

For example, it is not unreasonable to expect consumers to only avail themselves of a 'known' cheaper fuel price in their local area if the price advantage on offer more than compensates them for any change in the timing and cost (additional distance travelled) of departing from their more convenient and regular travel routes and purchasing day/time.

In summary, the provision of 'more or more timely information' is not a desirable outcome unless it drives better outcomes for consumers and leads to improved economic efficiency or welfare overall. For example, as outlined in the legislation's Regulatory Impact Statement, any benefits from potential lower consumer search costs and from restricting intra-day price movements may be overwhelmed by less consumer certainty associated with more unpredictable petrol prices throughout the week (as occurs in Perth).

(F) IMPACTS OF THE SCHEME ON 'BUSINESS COMPLIANCE COSTS'

The Regulatory Impact Statement (RIS) estimates (on p10) the compliance costs on retail fuel businesses. The key conclusions from the RIS are:

- the estimates startup cost is $2 million or $424 per business;
- the estimated annual ongoing cost is $18.7 miilion or $3974 per business; and
- the estimated business compliance cost is $20.7 million (including start up costs and one year of ongoing business compliance costs).

The total compliance costs for business noted above are thereby understated since the total cost only includes one year of ongoing costs.

AIP notes that these costs are based on specific costing assumptions and include a number of compliance activities and responsibilities that will need to be performed by retailers.

AIP also notes that the conclusions about compliance costs in the RIS are different to the conclusion reached in the legislation's EM (on page 8), which says *"the estimated net compliance cost to retailers associated with the establishment and ongoing operation of National Fuelwatch is negligible".* There is no cost information (or costing assumptions) provided to clearly demonstrate that the significant costs identified in the RIS would be offset either partially or wholly.

To small independent retailers, an annual ongoing cost of $4,000 would not be "negligible", and in fact might risk their ongoing viability unless the cost could be passed on to consumers.

AIP member companies may provide further information on the extent to which these compliance costs may be accurate or otherwise and on any practical difficulties in complying with the legislation (and the possible costs of these).

The RIS also indicates that the scheme would apply to 4700 retail businesses across Australia, but there is no explanation of how this estimate was derived.

(G) 'ECONOMIC IMPACTS' OF THE SCHEME

A comprehensive assessment of the economic impacts should have regard to, among other things, the impact of the National Fuelwatch Scheme on prices, competition, market conduct, market structure, demand and supply, and consumer welfare.

A number of these impacts are discussed separately above and in Chapter 4. As noted previously, AIP considers that there is almost no assessment in any of the legislative or ACCC documents of the potential impact of the Scheme on the structure and conduct of the retail fuel market.

It is clear from the discussion in Chapters 4 & 5, that specific economic impacts of the Scheme have not been rigorously assessed (at least on the basis of what information and analysis is publicly available).

It is therefore reasonable to conclude that an overall economic assessment of the Scheme has not been conducted to determine the net economic benefit or cost of this Scheme. Such an assessment would have to consider the fundamentally competitive nature of the Australian fuel market and the costs (versus the status quo) of intervening in this free market – including regulatory costs, compliance costs, enforcement costs and broader economic costs in terms of potentially higher prices and reduced competition and consumer welfare.

AIP expects that further analysis of the costs and benefits of the Scheme, including the economic impacts, will be conducted prior to the implementation of the National Fuelwatch Scheme.

(H) IMPACTS ON 'BUSINESS STRATEGIES'

It is difficult to speculate on the strategies that petrol retailers and retailing chains may employ to remain competitive following the implementation of the National Fuelwatch Scheme. .

There has been some speculation, including in the media, that one possible outcome might be that retailers might utilise alternative (price and no-price) offerings or discounts to reduce the net spend of consumers purchasing fuel from them, compared to their competitors.

ATTACHMENT A

REFERENCES & INFORMATION SOURCES

AIP has drawn on a wide range of reports, papers and analysis in the preparation of this submission. Details of the key reference documents and resources are set out below.

Pricing Information

This submission draws from pricing and other material presented on the following websites:
www.aip.com.au
www.bp.com.au
www.caltex.com.au
www.exxonmobil.com.au
www.shell.com.au
www.industry.gov.au
www.accc.gov.au
www.fuelwatch.wa.gov.au

Data – Pricing & Service Stations

In addition to the pricing information/data contained on the websites above, other primary sources are:
Australian Petroleum Statistics, Department of Energy, Resources & Tourism, Australian Government
Platts (McGraw-Hill Inc), crude oil, petroleum product and freight rates which AIP publishes on its website (under Copyright © 2005 the McGraw-Hill companies)
Petrol pricing data prepared by ORIMA Research Pty Ltd (on behalf of AIP)
TGP data prepared by ORIMA Research Pty Ltd (on behalf of AIP)

Previous Inquiries, Submissions & Pricing Reports

NT Government, 'Inquiry into Fuel Prices in the Northern Territory', May 2005
ACCC, 'Reducing fuel price variability' Report, December 2001
ACCC, Inquiry into the Price of Unleaded Petrol, *'Petrol Prices & Australian Consumers'* December 2007
AIP, 'Submission to the Australian Government Biofuels Taskforce', 24 June 2005
AIP, 'Submission to the Inquiry into Petrol Pricing in Queensland', December 2005
AIP, Submission to the Inquiry into the Provisions of Petroleum Retail Legislation Repeal Bill, April 2006
AIP, 'Submission to Senate Inquiry into the Price of Petrol in Australia, August 2006
AIP, *'Downstream Petroleum 2003'*
AIP, *'Downstream Petroleum 2005'*
AIP, *'Downstream Petroleum 2007'*
Legislative Assembly of Queensland, Report of the Inquiry into Petrol Prices in Queensland, April 2006
Australian Parliament, Senate Economic Committee, 'Inquiry into Petrol Prices in Australia', Dec 2006

Public Testimony & Critiques of the Fuelwatch Scheme

ACCC, Inquiry into the Price of Unleaded Petrol, *'Petrol Prices & Australian Consumers'* December 2007
ACCC, 'Reducing fuel price variability' Report, December 2001
Legislative Assembly of Queensland, Report of the Inquiry into Petrol Prices in Queensland, April 2006
Parliament of Australia, Senate Standing Committee on Economics (Estimates) on 4 June 2008, Hansard
Parliament of Australia, Senate Standing Committee on Economics (Estimates) on 5 June 2008, Hansard
Prof Don Harding, Department of Economics & Finance, LaTrobe University, *'Foolwatch: A Case Study of Econometric Analysis & 'evidenced-based-policy making' in the Australian Government',* July 2008
Institute of Public Affairs, Prof Sinclair Davidson, *'A critique of the ACCC analysis of the FuelWatch Scheme'*, May 2008

ATTACHMENT B

Australian Institute of Petroleum

MEDIA RELEASE

16 April 2008

Petroleum Industry Response to Announcement of National FuelWatch Scheme

The Australian Institute of Petroleum (AIP) advises that AIP member companies will cooperate with the Government's proposed implementation of a National FuelWatch Scheme.

AIP Executive Director, Dr John Tilley, said today, "the key industry objective will be to help ensure that a truly competitive fuel market is maintained, while ensuring that the compliance burden for the industry is not onerous".

In designing and implementing the National FuelWatch Scheme, it will be important for the Government to ensure there are no anti-competitive effects nor unintended consequences such as:

- a reduction in consumers' ability to access discounted fuel;
- excessive administrative and compliance costs - especially for small site operators; and
- a lack of predictability for consumers in the fuel price cycle.

The Government has announced a review of the Scheme after 12 months of operation.

Dr Tilley said, "as part of this review, we would expect there will be a rigorous analysis of the costs and benefits of the National FuelWatch Scheme. Such analysis would include the impact of the Scheme on fuel prices and the discounting cycle in all markets and local areas where FuelWatch will operate".

AIP encourages governments and the ACCC to ensure that the objectives of the National FuelWatch Scheme, and the likely consequences, are clearly understood by fuel consumers – particularly those consumers who are currently benefiting from significant savings on low price days of the week. AIP urges consumers to carefully assess whether the benefits claimed from the introduction of this Scheme do, in fact, materialise.

Media Contact: Dr John Tilley
Executive Director
(02) 6247 3044

ATTACHMENT C

Australian Institute of Petroleum

WEEKLY PETROL PRICES REPORT

Week Ending 13 July 2008

Please find attached a copy of the latest AIP Weekly Petrol Prices Report.

All data, charts and tables in this Report are based on the latest available market data to Sunday, 13 July 2008.

For more detailed information on:

Pricing Facts	– see **www.aip.com.au/pricing/facts.htm**
Terminal Gate Prices (wholesale)	– see **www.aip.com.au/pricing/tgp.htm**
Pump Prices (retail)	– see **www.aip.com.au/pricing/retail.htm**
International Fuel Prices	– see **www.aip.com.au/pricing/international.htm**

Should you have any questions about the material in this report, please contact AIP at **petrolprices@aip.com.au.**

THE AUSTRALIAN FUEL MARKET - AN OVERALL SNAPSHOT

Understanding Movements in Key Petrol Price Indicators

The Chart below provides an overall 'snapshot' of movements in key market indicators relevant to the price of petrol at the pump in Australia.

The Australian refining sector is a price taker. Domestic prices are closely linked to relevant international prices. The Singapore benchmark price of petrol (MOPS95 Petrol) is the key price benchmark for petrol in Australia. As the chart below shows, MOPS95 Petrol plus shipping costs and Australian taxes represents almost the entire wholesale price of petrol (around 95%).

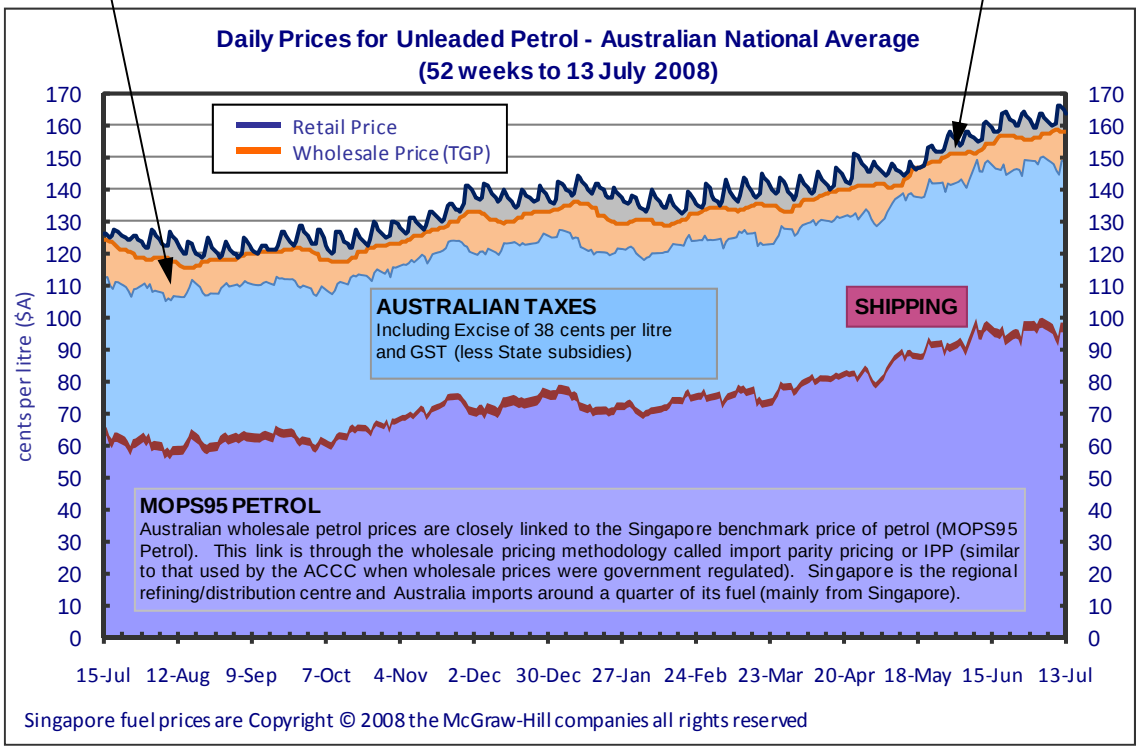
The orange shaded area is simply the difference between two key market indicators – the national average Terminal Gate Price (TGP) and MOPS95 Petrol plus shipping and taxes. It does not represent profits accruing to oil companies at the wholesale level. A range of costs (including 'landed costs' and 'wholesaling costs') would need to be deducted to determine actual profits at the wholesale level.

These 'landed costs' include the costs of:
- ⇒ the quality premium (market cost) for Australian fuel standards
- ⇒ insurance and loss
- ⇒ local wharfage costs

The standard 'wholesaling costs' include:
- ⇒ terminal operating costs
- ⇒ administration and wholesale marketing costs
- ⇒ corporate taxes and government charges on wholesaling activities

The grey shaded area is simply the difference between two key market prices relevant to the retail market. That is, the difference between the national average pump price and average TGP. It does not represent profits accruing to retailers or oil companies. A range of standard retailing costs would need to be deducted to determine actual profits at the retail level.

These 'retailing costs' include:
- ⇒ land transport costs (of getting fuel from the terminal gate to the petrol bowser)
- ⇒ administration and retail marketing costs
- ⇒ the costs of running service stations like wages, rent and utilities
- ⇒ corporate taxes and other government charges on retailing activities



PROFITS OF OIL COMPANIES
Once all wholesaling and retailing costs are considered, together with competitive market pressures, the total profit made across wholesale and retail activities is a very small proportion of the final pump price. Average oil company profit over the last 10 years is around 1 cent per litre of fuel sold.

NOTES

(1) MOPS95 Petrol: the international petrol prices are provided by Platts (Copyright © 2008 The McGraw-Hill Companies, all rights reserved), and represent the end of day assessment for the mean of Singapore prices for 95 Octane Petrol (MOPS95 Petrol). No portion of the publication may be photocopied, reproduced, retransmitted, put into a computer system or otherwise redistributed, without prior written Authorisation from Platts. Platts is a trademark of the McGraw-Hill Inc. Information has been obtained from sources believed reliable. However, because of the possibility of human or mechanical errors by sources, McGraw-Hill or others, McGraw-Hill does not guarantee the accuracy, adequacy or completeness of any such information and is not responsible for any errors or omissions or for results obtained from use of such information.

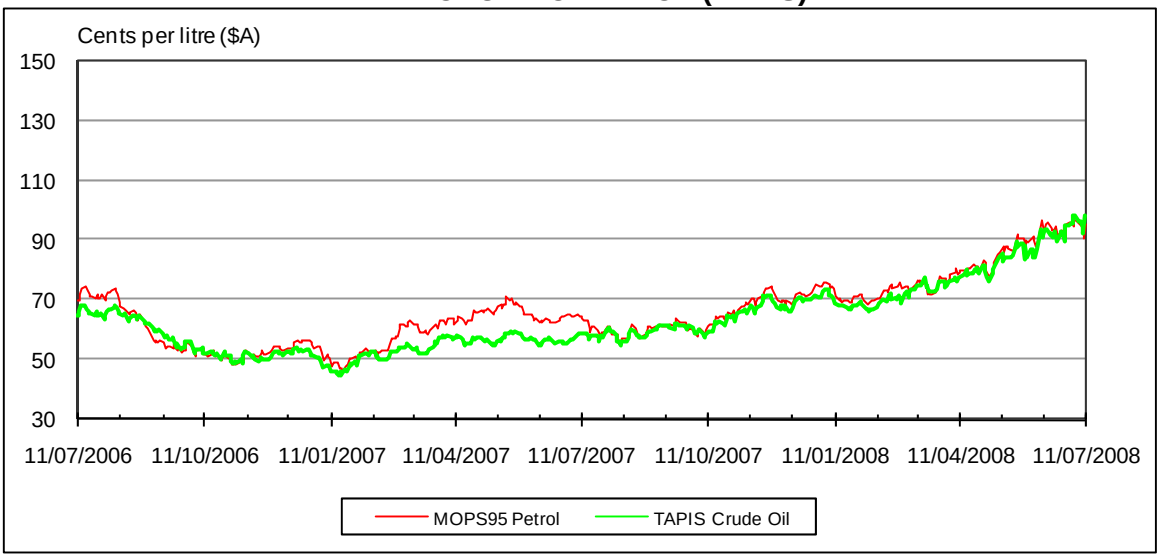
(2) SHIPPING: is the weighted average of daily market shipping rates (Australian cents per litre) for journeys from Singapore to major Australian ports (weighted by the volume of fuel sales in the relevant State). Source data include Platts, Worldscale, Australian Petroleum Statistics and the Reserve Bank of Australia.

(3) TAXES: is excise and GST less any relevant state rebates weighted by the volume of petrol consumed in each State.

(4) NATIONAL AVERAGE PRICES: are derived from capital city prices weighted by fuel volume consumed in each State.

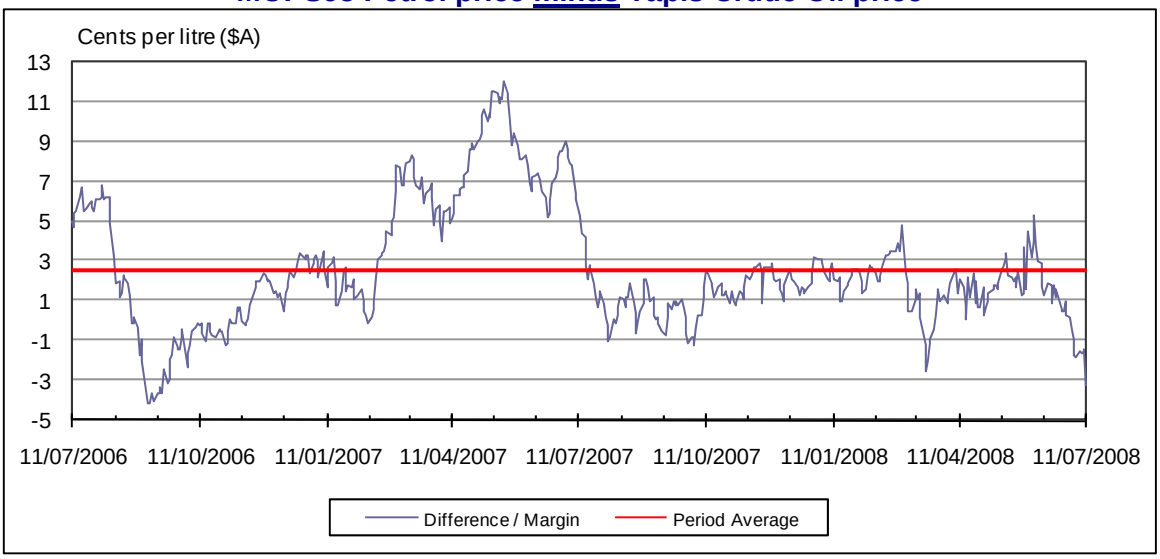
INTERNATIONAL MARKET TRENDS

FIGURE 1: COMPARISON OF SINGAPORE PETROL PRICE (MOPS95 PETROL) WITH CRUDE OIL PRICE (TAPIS)



***NOTE**: Australia is part of the Asia Pacific fuel market (Singapore is the regional refining/distribution centre) and the relevant market benchmark is Tapis for crude oil and Singapore petrol prices for unleaded petrol (MOPS95 Petrol). Tapis crude oil and MOPS95 Petrol prices are provided by Platts (McGraw-Hill Inc), see Notes on page 2.*

FIGURE 2: DIFFERENCE BETWEEN MARKET PRICES
MOPS95 Petrol price minus Tapis Crude Oil price



***NOTE:** The refiner margin above is the difference between market prices for MOPS95 Petrol and Tapis. It is not a figure determined by refiners.*

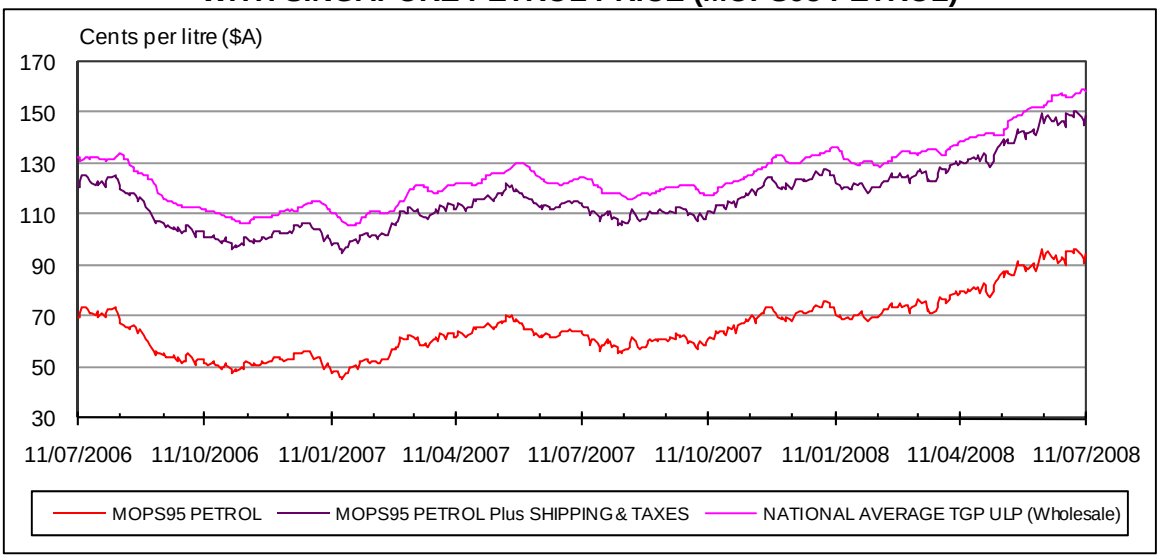
TAPIS CRUDE OIL	Cents per litre (A$)
Average: Last Week (to Friday 11/07/08)	95.6
Average: Previous Week (to Friday 04/07/08)	96.8
Average: Last 4 Weeks	94.1
Average: Last 12 Weeks	88.1
Average: Last 12 Months	71.4

MOPS95 PETROL	Cents per litre (A$)
Average: Last Week (to Friday 11/07/08)	93.7
Average: Previous Week (to Friday 04/07/08)	95.8
Average: Last 4 Weeks	93.9
Average: Last 12 Weeks	89.5
Average: Last 12 Months	72.9

PLEASE NOTE

*Differences/margins between market prices or benchmarks are used as indicators of general trends in the petroleum market, **they do not represent profits** accruing to oil companies at the refining, wholesale or retail segments of the market. For each market segment, a range of costs would need to be deducted to determine actual profits.*

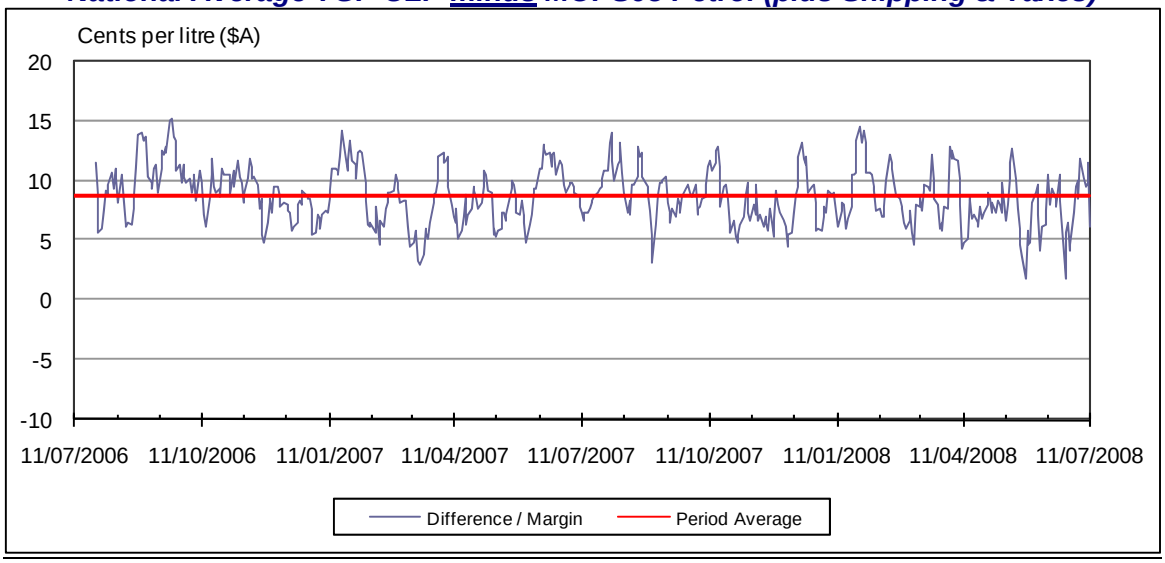
FIGURE 3: COMPARISON OF AUSTRALIAN TGP ULP (OR 'WHOLESALE PRICE') WITH SINGAPORE PETROL PRICE (MOPS95 PETROL)



NOTE: *The MOPS95 Petrol prices and Shipping rates are provided by Platts (McGraw-Hill Inc), see Notes on page 2.*

FIGURE 4: DIFFERENCE BETWEEN MARKET PRICES

National Average TGP ULP minus MOPS95 Petrol (plus Shipping & Taxes)



MOPS95 PETROL	Cents per litre (A$)
Average: Last Week (to Friday 11/07/08)	93.7
Average: Previous Week (to Friday 04/07/08)	95.8
Average: Last 4 Weeks	93.9
Average: Last 12 Weeks	89.5
Average: Last 12 Months	72.9

TGP ULP (National Average)	Cents per litre (A$)
Average: Last Week (to Friday 11/07/08)	158.6
Average: Previous Week (to Friday 04/07/08)	156.5
Average: Last 4 Weeks	157.0
Average: Last 12 Weeks	149.8
Average: Last 12 Months	132.4

PLEASE NOTE

Differences/margins between market prices or benchmarks are used as indicators of general trends in the petroleum market, ***they do not represent profits*** *accruing to oil companies at the refining, wholesale or retail segments of the market. For each market segment, a range of costs would need to be deducted to determine actual profits. For example,* ***at the wholesale level,*** *a range of costs (including 'landed costs' and 'wholesaling costs') would need to be deducted to determine actual profits at the wholesale level. These 'landed costs' include the costs of the quality premium (market cost) for Australian fuel standards, insurance and loss, and local wharfage costs. The standard 'wholesaling costs' include terminal operating costs, administration and wholesale marketing costs and corporate taxes and government charges on wholesaling activities.*

AVERAGE TERMINAL GATE PRICES (TGPs) ACROSS AUSTRALIAN STATES/TERRITORIES

Week ended 11 July 2008

UNLEADED PETROL (cents per litre $A)

	Monday 7 July 2008	Tuesday 8 July 2008	Wednesday 9 July 2008	Thursday 10 July 2008	Friday 11 July 2008
Sydney	157.7	158.7	159.0	158.9	158.5
Melbourne	157.1	158.0	158.4	158.3	157.9
Brisbane	157.7	158.7	159.0	158.8	158.4
Adelaide	158.0	158.8	159.3	159.2	158.8
Perth	158.0	159.0	159.3	159.3	159.0
Darwin	161.4	162.3	162.8	162.7	162.3
Hobart	160.3	161.2	161.7	161.7	161.2

DIESEL (cents per litre $A)

	Monday 7 July 2008	Tuesday 8 July 2008	Wednesday 9 July 2008	Thursday 10 July 2008	Friday 11 July 2008
Sydney	179.0	180.7	181.4	181.5	182.3
Melbourne	178.4	180.2	180.7	180.8	181.5
Brisbane	178.8	180.6	181.1	181.2	182.0
Adelaide	178.7	180.5	181.2	181.3	182.1
Perth	178.4	180.2	180.8	180.8	182.0
Darwin	182.5	184.1	184.9	185.0	185.8
Hobart	182.2	183.8	184.7	184.7	185.5

NOTES: Daily TGP data are published by all wholesale fuel suppliers. AIP's website presents average TGP data for each weekday – see www.aip.com.au/pricing/tgp.htm. This data has been prepared by ORIMA Research Pty Ltd on behalf of AIP, using information from BP Australia, Caltex, Shell Australia, and ExxonMobil Australia. Prices shown are the average TGP for unleaded petrol and diesel across each of these companies for the day. Brisbane prices are exclusive of the Queensland Government fuel subsidy.

EXPLAINING THE TIME LAG BETWEEN CHANGES IN SINGAPORE PRICES AND CHANGES IN AUSTRALIAN WHOLESALE PETROL & DIESEL PRICES

Generally, there is a short time lag of 1-2 weeks between changes in Singapore prices and changes in Australian prices.

⇒The lag can be seen in FIGURE 3 on the previous page. That is, see the slight delay in the peaks and troughs in the pink line (National Average TGP) compared to the **purple line** (MOPS95 Petrol plus Shipping & Taxes).

⇒Importantly, this time lag occurs whether: prices are going up (when the lag slows price rises to consumers) or prices are going down (when the lag delays price falls).

⇒The lag is a result of using a rolling average of Singapore prices as part of the wholesale pricing methodology (very similar to that used by the ACCC when wholesale prices were regulated by government). The pricing methodology is called import parity pricing (IPP).

⇒The use of rolling averages smooths day-to-day price volatility.

⇒Not accounting for this lag, introduced by the rolling average, leads to incorrect conclusions about how Singapore prices flow through to prices in Australia.

The very close relationship between changes in MOPS95 Petrol and changes in Australian TGPs can be seen by applying a rolling average to the MOPS95 Petrol data (a 7 day rolling average is used in the Chart to the right to illustrate this).

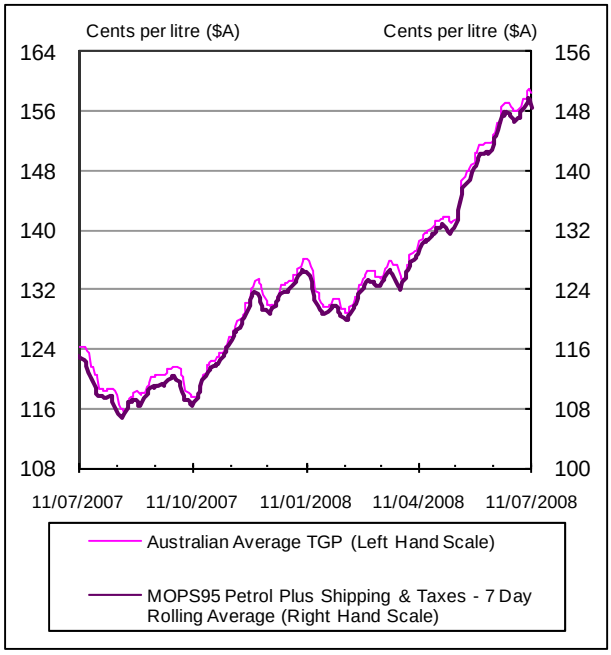


FIGURE 5: COMPARISON OF AUSTRALIAN PUMP PRICE WITH AUSTRALIAN TGP
Average Retail Price versus Average Wholesale Price

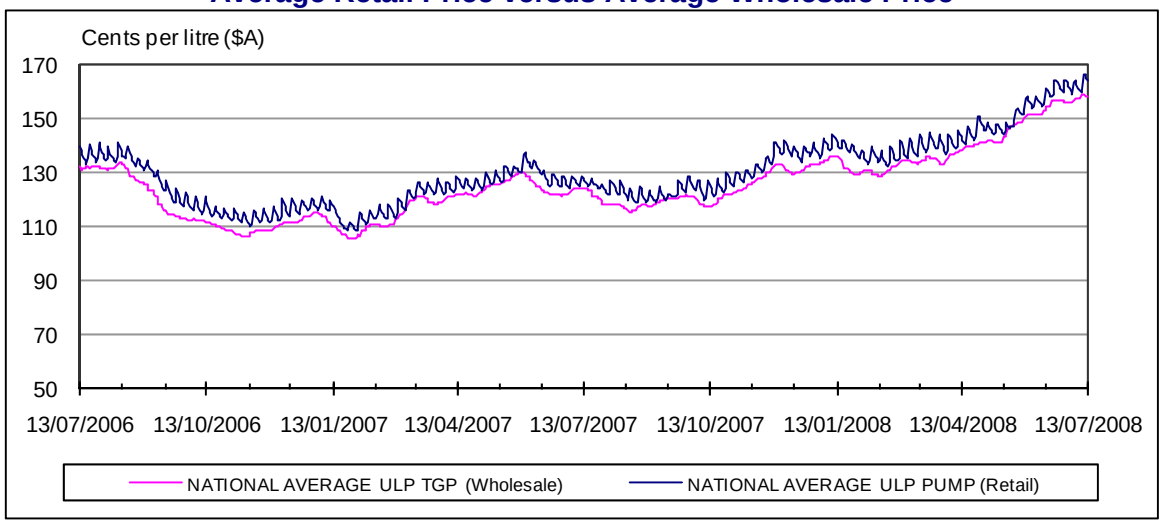
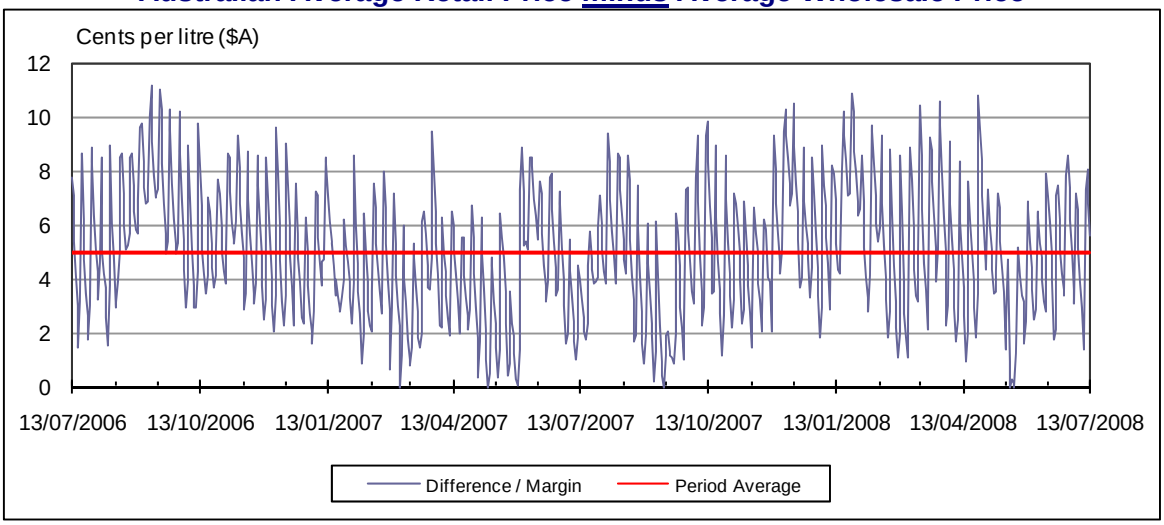


FIGURE 6: DIFFERENCE BETWEEN MARKET PRICES
Australian Average Retail Price minus Average Wholesale Price



Wholesale: TGP ULP (National Average)	Cents per litre (A$)
Average: Last Week (to Friday 11/07/08)	158.6
Average: Last Week (to Friday 04/07/08)	156.5
Average: Last 4 Weeks	157.0
Average: Last 12 Weeks	149.8
Average: Last 12 Months	132.4

Retail: Pump Price ULP (National Average)	Cents per litre (A$)
Average: Last Week (to Sunday 13/07/08)	163.4
Average: Last Week (to Sunday 06/07/08)	161.8
Average: Last 4 Weeks	162.2
Average: Last 12 Weeks	154.7
Average: Last 12 Months	137.6

PLEASE NOTE

Differences/margins between market prices or benchmarks are used as indicators of general trends in the petroleum market, ***they do not represent profits*** *accruing to oil companies at the refining, wholesale or retail segments of the market. For each market segment, a range of costs would need to be deducted to determine actual profits.*
For example ***at the retail level,*** *a range of standard retailing costs would need to be deducted to determine actual profits. These costs include:*

⇒ *land transport costs (of getting fuel from the terminal gate to the petrol bowser)*
⇒ *administration and retail marketing costs*
⇒ *the costs of running service stations like wages, rent and utilities*
⇒ *corporate taxes and other government charges on retailing activities*

SUMMARY: RETAIL PETROL PRICE TRENDS ACROSS STATES/TERRITORIES

Week ended 13 July 2008

'NATIONAL AND STATE' AVERAGE PRICES (cents per litre $A)

	Weekly Average	Weekly Change	Low	High
National Average	163.4	1.5	160.1	166.5
NSW / ACT	165.0	1.9	161.1	169.4
Victoria	164.5	0.0	160.6	167.8
Queensland	157.4	2.5	154.4	160.5
South Australia	165.6	1.9	161.5	170.8
Western Australia	162.7	2.3	160.1	165.7
Northern Territory	176.0	1.7	174.4	177.9
Tasmania	168.7	0.8	168.1	169.7

'METROPOLITAN' AVERAGE PRICES (cents per litre $A)

	Weekly Average	Weekly Change	Low	High
National Metro Average	162.8	1.6	158.3	167.2
Sydney	163.9	2.0	158.5	169.5
Canberra	167.9	3.5	165.1	171.3
Melbourne	164.2	0.0	159.3	168.8
Brisbane	157.0	2.9	150.7	162.9
Adelaide	165.2	2.4	159.6	172.3
Perth	159.8	2.5	156.7	163.5
Darwin	175.0	1.8	172.5	176.9
Hobart	166.8	1.1	165.7	169.3

'REGIONAL' AVERAGE PRICES (cents per litre $A)

	Weekly Average	Weekly Change	Low	High
National Regional Average	164.4	1.3	163.5	165.7
NSW / ACT	166.9	1.5	165.3	168.9
Victoria	165.5	0.3	164.1	167.3
Queensland	157.8	2.1	157.1	158.2
South Australia	166.6	0.7	166.1	167.1
Western Australia	172.8	1.6	171.9	173.5
Northern Territory	178.5	1.5	175.6	180.4
Tasmania	170.1	0.5	169.6	171.1

For average weekly retail (pump) prices for petrol and diesel across Australian cities and towns, please see www.aip.com.au/pricing/retail.htm

NOTES

(1) The National Average is calculated as the weighted average of each State/Territory's metropolitan and non-metropolitan retail petrol prices, with the weights based on the number of vehicles using unleaded petrol registered in each of these areas.

(2) The Regional Average price is calculated as the weighted average of the retail petrol prices for the non-metropolitan regions in each State/Territory, where the weights are based on the number of vehicles using unleaded petrol.

(3) The vehicle data source is *ABS Motor Vehicle Census, 2005, Cat No 9309.0*.

(4) 'Weekly Low' and 'Weekly High' are based on the lowest and the highest average daily prices in the relevant area. The average daily price for each region (eg. Geelong) is calculated as a straight numerical average of all 'price points' provided for that day. Aggregate daily prices are based on a weighted average of all regions (eg. Geelong, Ballarat, Wodonga etc) in the relevant area (eg. Victoria) where weights are based on the number of vehicles using unleaded petrol in each region.

(5) Weekly Average prices are a straight average of the seven days.

(6) Weekly Change is the change compared with the Weekly Average last week.

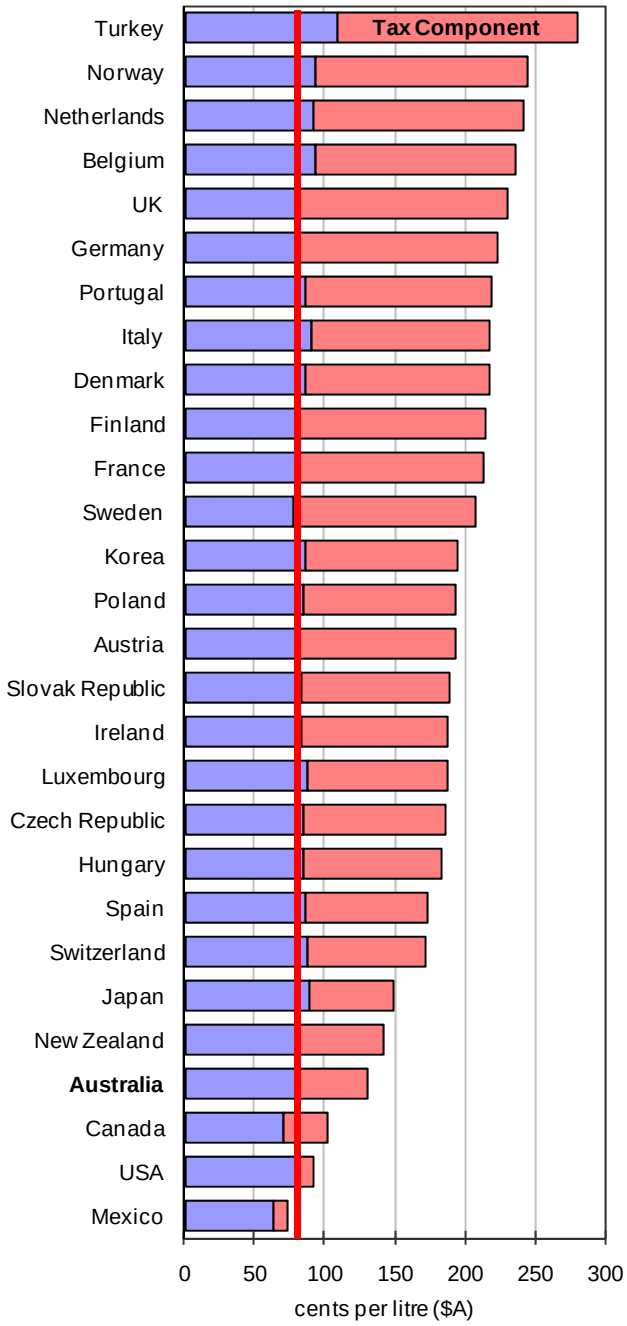
For more information on data methodology, please see the AIP Website (www.aip.com.au/pricing/retail.htm).

PETROL AND DIESEL – PRICES & TAXES IN OECD COUNTRIES

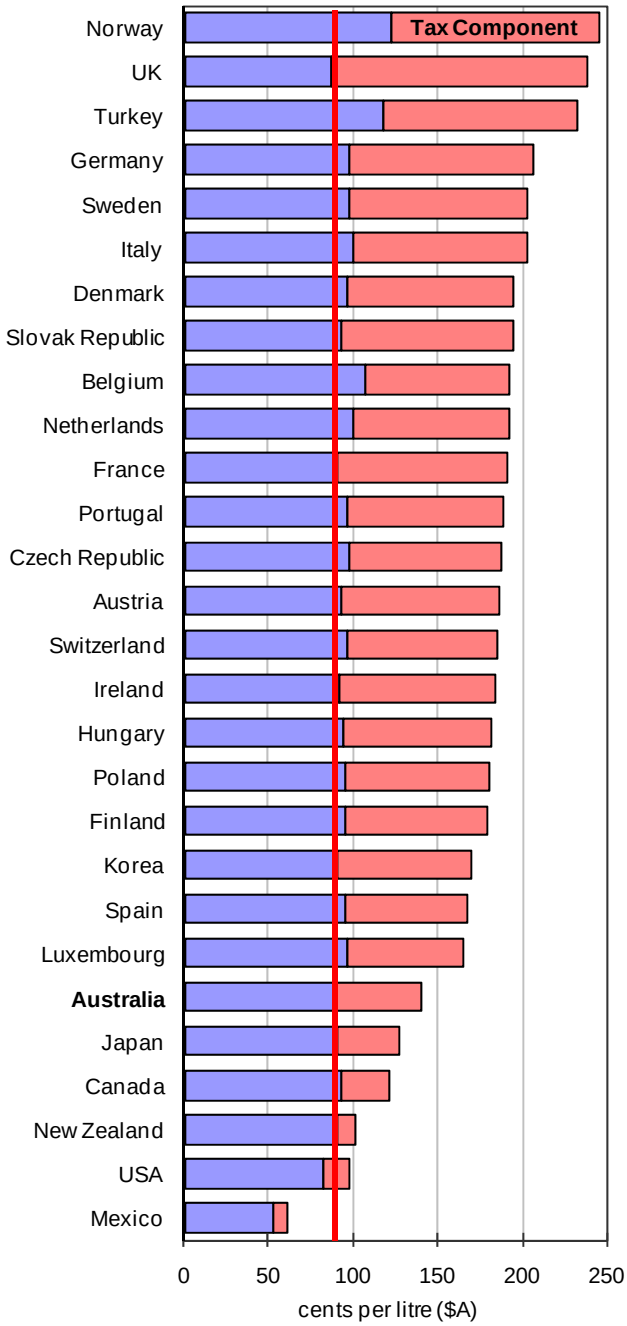
December Quarter 2007

The Charts show Australia has among the lowest petrol and diesel prices of all OECD countries.

Petrol Prices and Taxes in OECD Countries



Diesel Prices and Taxes in OECD Countries



Source: Australian Petroleum Statistics, Department of Industry, Tourism and Resources

ATTACHMENT D

Australian Institute of Petroleum

FACTS ABOUT PRICES & THE AUSTRALIAN FUEL MARKET

INTERNATIONAL PRICES

Crude oil, petrol and diesel are bought and sold in their own markets.

Each market is typically regionally-based and there are linkages and transactions between regional markets.

Prices in regional markets reflect the supply and demand balance in each market and the physical characteristics and quality of each commodity.

Prices in regional markets can be volatile and can move in different directions from each other.

⇒ This can be due to the impact of factors and events unique to one market – such as supply and demand pressures in a region, hurricanes, wars and civil unrest.

This is why focusing on relevant markets and longer term price trends is more important than daily or week-to-week price movements.

Australia's regional market is the Asia-Pacific market.

Tapis crude oil is the key crude oil benchmark for the Asia Pacific region and Australia – not West Texas Intermediate crude (the US market benchmark) widely reported in the media.

The Singapore benchmark price of petrol (MOPS95 Petrol) & diesel (Gasoil) are the key petrol and diesel price benchmarks for Australia.

⇒ To meet Australian fuel demand, around a quarter of fuel is imported (mainly from Singapore). Singapore is the regional refining and distribution centre and among the world's largest.

If Australia's petrol and diesel prices were below Singapore prices, Australian fuel suppliers would have no commercial incentive to import to Australia (because sales of that fuel would be at a loss here). In addition, Australian refiners would have an incentive to export production.

'Refiner margins' are the differences between product prices and crude prices, both of which are set by the market, not by oil companies (eg. a Singapore petrol 'refiner margin' is the difference between the market prices for MOPS95 Petrol and Tapis).

AUSTRALIAN WHOLESALE PRICES

Australian wholesale prices for petrol and diesel (called Terminal Gate Prices or TGPs) are closely linked to the Singapore prices of petrol and diesel – not Tapis crude oil prices.

⇒ This relationship has been in place for many years. According to public statements, Australian fuel wholesalers use a pricing methodology very similar to that used by the ACCC when wholesale prices were regulated by government. This pricing methodology is called import parity pricing or IPP and it is based on what it would cost to import fuel into Australia.

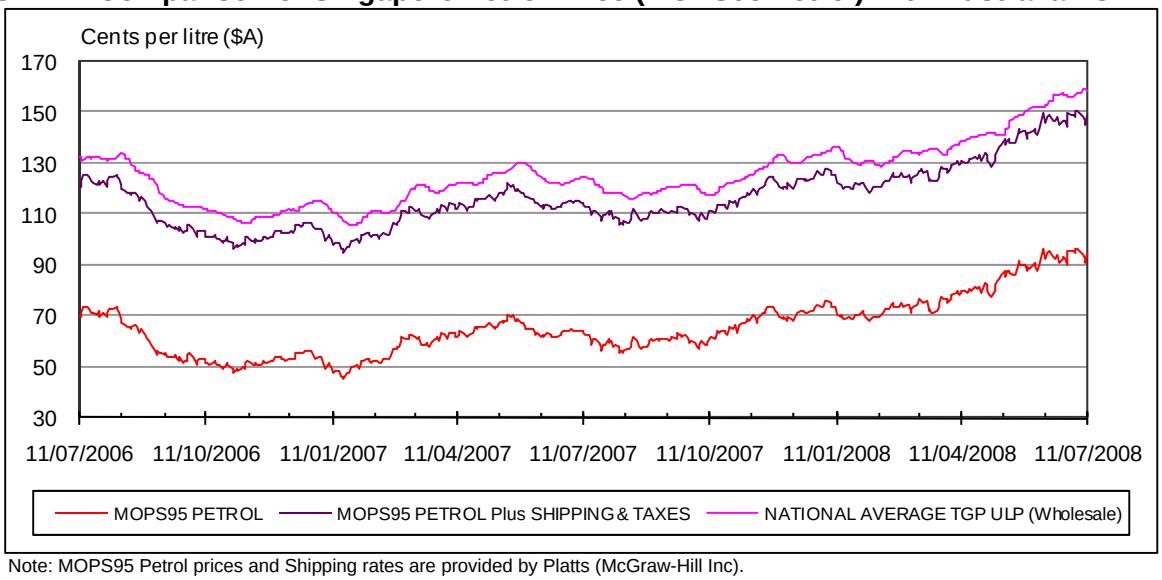
Recent movements in Singapore petrol prices and Australian TGPs are shown in Figure 1.

The Singapore price of petrol plus shipping costs and Australian taxes represents almost the entire wholesale price of petrol - around 95% (as shown in the chart below).

⇒ Australian taxes include excise (38 cents per litre) and GST (10%) less any state subsidy.

The remaining 5% of TGPs is accounted for by insurance, a quality premium for Australian fuel standards, local wharfage and terminal costs, and a wholesale marketing margin (where competitively possible).

FIGURE 1: Comparison of Singapore Petrol Price (MOPS95 Petrol) with Australian ULP TGP



Note: MOPS95 Petrol prices and Shipping rates are provided by Platts (McGraw-Hill Inc).

Generally, there is a short time lag of 1-2 weeks between changes in Singapore prices and changes in Australian wholesale prices.

⇒ The lag can be seen in Figure 1 above (ie. see the slight delay in the peaks and troughs in the **pink line** (National ULP TGP) compared to the **purple line** (MOPS95 Petrol plus Shipping & Taxes).

⇒ The lag is a result of using a rolling average of Singapore prices; the rolling average smooths price volatility from day-to-day.

⇒ Importantly, this time lag occurs whether prices are going up (when the lag slows price increases to consumers) or going down (when the lag delays price falls).

⇒ Not accounting for this lag leads to incorrect conclusions about how Singapore prices flow through to prices in Australia.

Daily TGP data are published by all wholesale suppliers. AIP's website presents average TGP data – see www.aip.com.au/pricing/tgp.htm and the website extract in Figure 2.

⇒ Australian Government Oilcode regulations require the publication of TGPs by all wholesale suppliers on a daily basis.

FIGURE 2: Average Terminal Gate Prices: Unleaded Petrol (cents per litre)

(Wholesale price for bulk purchase at the terminal)

	Monday 7 July 2008	Tuesday 8 July 2008	Wednesday 9 July 2008	Thursday 10 July 2008	Friday 11 July 2008
Sydney	157.7	158.7	159.0	158.9	158.5
Melbourne	157.1	158.0	158.4	158.3	157.9
Brisbane	157.7	158.7	159.0	158.8	158.4
Adelaide	158.0	158.8	159.3	159.2	158.8
Perth	158.0	159.0	159.3	159.3	159.0
Darwin	161.4	162.3	162.8	162.7	162.3
Hobart	160.3	161.2	161.7	161.7	161.2

All values are in cents per litre and are inclusive of GST.

RETAIL OR PUMP PRICES

Once fuel leaves the terminal gate (where TGPs apply), retail prices vary across metropolitan and regional areas, reflecting local area factors and competition.

⇒ Figure 3 shows the relationship between recent movements in national average ULP TGPs and national average ULP pump prices.

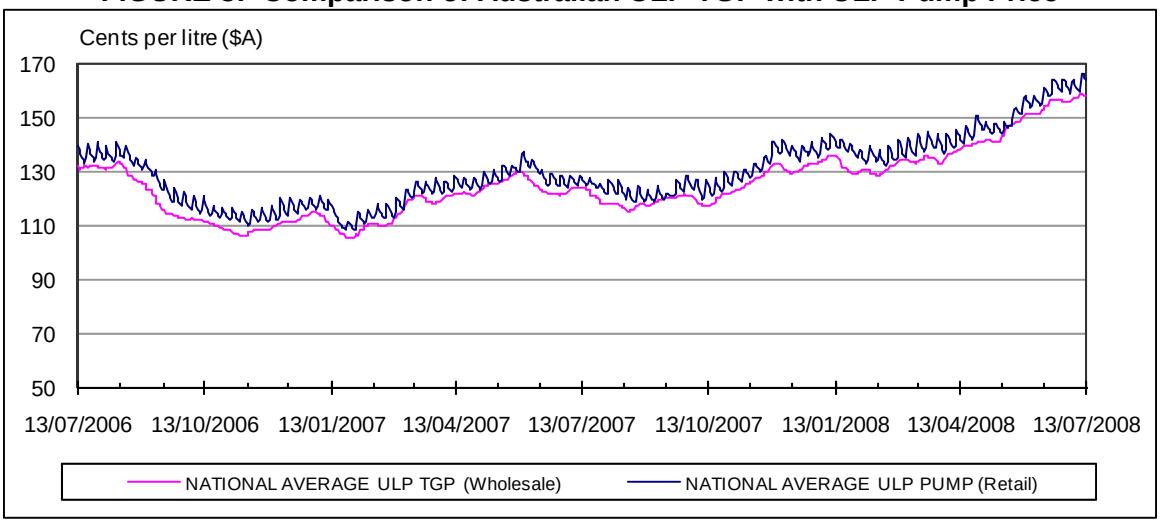
The TGP is typically around 95% of retail prices (as also shown in Figure 3 below).

Apart from TGP, the retail or pump price in Australia also reflects all the costs of getting the fuel from the refinery/terminal to the bowser.

⇒ This includes transport costs, admin and marketing costs, and service station running costs like wages, rent and utilities. The ability to cover costs depends on local area competition.

⇒ There is only a small proportion of the pump price (around 5% on average) which is received by fuel distributors and fuel retailers to cover these costs.

FIGURE 3: Comparison of Australian ULP TGP with ULP Pump Price



Retail prices in metropolitan areas also follow a discounting cycle (the saw tooth pattern shown in the chart above) which historically has ranged up to 12 cents from peak to trough.

⇒ Customers in capital cities will be familiar with these discounting cycles on a weekly basis. The current weekly cycle's low point is typically early in the week. Highly visible price boards allow customers to take advantage of low prices and competitors to observe price discounting.

⇒ Petrol prices fall steadily due to service station owners/operators aggressively discounting to capture market share. However, maximum discounts can only be sustained for short periods before prices recover. This is typified by a sharp lift in prices to a peak (at a later time in the week) before the discounting cycle starts again.

⇒ Analysis (including by the ACCC) clearly shows that petrol prices do not increase *because* of long weekends or public holidays.

Consumers clearly benefit by buying heavily discounted petrol at the low point in the cycle.

⇒ The ACCC provides advice on low price days of the week and they estimate that 60% of petrol sales are below the average price of the cycle. **According to the ACCC, the discounting cycle is a clear demonstration of vigorous competition.**

The major oil companies only set retail prices at a limited number of service stations across Australia (around 5-10%) and these are largely in metropolitan areas.

CITY VERSUS COUNTRY PRICES

Prices are more stable in regional areas because of a general absence of price discounting.

⇒ The general absence of discounting in regional/country areas also means that regional prices appear to be higher than fully discounted or average city prices.

⇒ Retail margins are typically higher in the country compared with major capital cities, due to lower fuel volumes and shop sales over which to spread service station operating costs.

- The average customer base per service station is around 2,000 people in regional Australia (and well below in many towns) whereas metro service stations typically have a customer base of around 4,000 to 5,000 people.
- Regional service stations typically see 1 tanker per 2-3 weeks versus several tankers per day at metropolitan sites.

⇒ Freight is typically around 1.5 to 3 cents per litre greater for country than city delivery.

⇒ Distribution costs may be significant for some country areas where fuel must be stored in depots and double-handled, rather than being delivered directly from coastal terminals.

⇒ Competitive forces and costs also vary greatly between country towns, so that pump prices do not just reflect freight and handling differences.

Retail prices in regional areas are largely set by independent owner/operators (including those who sell fuel supplied by one of the major brands under license).

PRICES & COMPETITION

By international standards, Australia has among the lowest petrol and diesel prices – with petrol prices today around the same level as back in the early 1980s (in today's dollars).

This is because the Australian petroleum market is highly competitive.

This is a view shared by many government reviews of the petroleum market and by many informed commentators and analysts, including the ACCC and International Energy Agency.

All the way along the crude oil and products supply chains there are several large (integrated) and numerous smaller (selective) market participants constantly driving market competition.

PROFITS OF MAJOR OIL COMPANIES

The profits made by oil companies are volatile (due to the nature of the market) and are typically a very small proportion of the final or retail price.

⇒ For example, while profits have improved in recent years, the average profit over the last 10 years made by oil companies (across refining, wholesaling and retailing operations) is around 1 cent per litre.

Recent improvements in the financial performance of the sector have provided the cash-flow to help fund investments of over $2 billion by the industry in the cleaner fuels program and refinery upgrades to help enhance fuel supply reliability.

⇒ These investments are generating significant environmental benefits, particularly improvements in air quality in metropolitan areas.

Since 1997, the major oil companies have invested around $5 billion in the Australian downstream industry. Total industry assets are almost $15 billion.