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Dear Mr Eady

GRAINCORP – PROPOSED VARIATION TO THE PORT TERMINAL SERVICES UNDERTAKING IN RESPECT OF THE NEWCASTLE TERMINAL-RESPONSE TO INTERESTED PARTIES’ SUBMISSIONS

1. INTRODUCTION AND PURPOSE

The purpose of this submission is to respond to the submissions made by interested parties in relation to GrainCorp’s application dated 12 November 2013 to vary its Port Terminal Services Undertaking (**Undertaking**). The proposed variations to the Undertaking (**Variation**) relate to the provision of Port Terminal Services at GrainCorp’s Newcastle Port Terminal.

GrainCorp notes that several submissions supported or were neutral towards the Variation. A large proportion of interested parties’ submissions related to the level of competition and regulation in the wheat industry generally and was not specifically relevant to the ACCC’s assessment of the Variation. Having regard to the material presented by interested parties in so far as it was relevant to the Variation, this submission focuses on the following key issues:

- It is inappropriate to require GrainCorp to continue operating at a disadvantage to the neighbouring unregulated Newcastle Agri Terminal (**NAT**) and Louis Dreyfus (**LDA**) facilities until the proposed Mandatory Code of Conduct (**Code**) currently under development is settled. There is a lack of clarity as to when the proposed Code may be finalised or what level of regulation it will require. The only substantive guidance available to date is the findings of the 2010 Productivity Commission review, which concluded that it would be appropriate for the access test contained in section 9 of the Wheat Export Marketing Act 2012 (**WEMA**) to be abolished by 1 October 2014.

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- The unequal application of access regulation in the Newcastle port zone, under which GrainCorp is subject to an access undertaking and required to comply with continuous disclosure rules while the Newcastle Agri Terminal and the LDA facility are not regulated, creates an uneven playing field. This results in inefficiencies, the cost of which will ultimately be passed up the supply chain and borne by farmers in the prices they receive at the farmgate.
- Suggestions that the Variation is not a valid undertaking for the purposes of meeting the access test in the WEMA are without basis. The Variation is a valid undertaking capable of acceptance by the ACCC, so long as the ACCC is satisfied of the criteria contained in section 44ZZCA(1) of the *Competition & Consumer Act 2010 (CCA)*. It is also sufficiently related to the provision of access at Newcastle so as to meet the requirements of the access test contained in the WEMA.
- GrainCorp has no incentive to exclude third party access from its Newcastle Terminal, so as to create a closed supply chain, as suggested by Emerald. As submitted previously, shipments (for all exporters) only account on average for 23% of the capacity of the Newcastle Terminal.

For these reasons, the Variation represents an appropriate level of regulation of GrainCorp's Newcastle Port Terminal having regard to the criteria in section 44ZZA(3) of the CCA. Further reasons supporting this position are provided below.

2. THERE IS NO CLARITY AS TO WHEN THE PROPOSED MANDATORY CODE OF CONDUCT MAY BE FINALISED OR WHAT FORM IT WILL TAKE. ACCORDINGLY, THIS IS NOT A RELEVANT FACTOR FOR THE ACCC'S ASSESSMENT OF THE UNDERTAKING

As the ACCC is aware, Government and industry have formed a 'Code Development Advisory Committee' (**CDAC**) with the aim of developing a mandatory Code of Conduct to replace the wheat export undertakings by 1 October 2014. The working group was formed in response to amendments to the Wheat Export Marketing Act (**WEMA**) which provide the option of removing the Undertakings if a mandatory code is in place.

The Australian Grain Exporters Association (**AGEA**) notes in its submission that the CDAC has worked cooperatively to develop a set of principles that provide a solid basis for development of a more flexible and relevant regulatory framework, but that there is not full agreement in all areas.

There is currently a lack of clarity as to when the Code may be finalised. It is inappropriate to require GrainCorp to place its business on hold and continue operating at a competitive disadvantage in anticipation of the Code, which may still be significantly delayed given the wide range of stakeholders involved in its development. In the event that the Code is implemented on its scheduled date of 1 October 2014, there are still 7 months, or one harvest season, until it would take effect. GrainCorp notes that Viterra (Glencore) has already extended its undertaking beyond 1 October 2014, suggesting they see a possibility that the Code will not be in place by then.

The existence of the CDAC and the development of the Code is not a relevant factor to the ACCC's assessment of whether GrainCorp's Variation may be accepted. The ACCC is required to have regard to the factors set out in section 44ZZA(1) of the CCA. While this includes a 'catch all' provision under which the ACCC may have regard to 'any other factor it considers relevant', GrainCorp considers that the future (potential) introduction of the Code is not relevant to any of the considerations contained in section 44ZZCA(3) of the CCA. This is particularly so in circumstances when the substance of the Code is not known at this time.

3. THE VARIATION RECTIFIES THE APPLICATION OF UNEQUAL REGULATION AT THE PORT OF NEWCASTLE

3.1 Inequitable access regulation creates an uneven playing field and distorts the operation of efficient markets

Several submissions support the application of equal access regulation at the Port of Newcastle, for example as Glencore notes, unequal application *'can create potential risks, to, and place unwarranted limits on, effective competition.'*

GrainCorp strongly agrees with CBH's submission, a shareholder in NAT, that *'regulated entities face high costs and burdens associated with regulatory compliance, operational constraints and inflexibility in applying prices and managing how to acquire and export wheat'* and its observations that the *'unequal application of regulation creates an uneven playing field and distorts the operation of efficient markets with an adverse impact in both domestic and international wheat markets.'*

The Australian wheat exporters are participants in a global market, and are therefore constrained by global prices and market forces. Consequently, the costs of unnecessary regulation cannot be recovered in the form of higher wheat price, but must be passed back up the supply chain to farmers in the form of higher supply chain costs.

For example, in its submission to the 2010 Productivity Commission Review, GrainCorp noted that *'The access process imposes significant additional regulatory cost on GrainCorp. To date, approximately \$1 million additional compliance cost has been imposed upon the company.'*¹ We continue to bear this cost in terms of staff, systems and legals to comply with the regulatory requirements.

The National Competition Council also raised concern as to the cost of regulation in its submission to the Productivity Commission review: *'In particular, inappropriate access regulation could restrict investment and innovation, and impede desirable change.'*²

By way of example, regulation prevents us from negotiating tailored shipping solutions to meet the needs for individual exporters, prevents us from flexibly selling capacity to exporters and constrains the efficient operation of the terminal in terms of managing vessel order and inbound transport. This limits shipping capacity and competition and in turns adds cost to the grain supply chain.

¹ GrainCorp, submission to the Productivity Commission Review 2010 19 November 2009

² National Competition Council, submission to the Productivity Commission Review 2010, 11 November 2009

3.2 GrainCorp's Newcastle terminal is subject to a number of competitive pressures

As stated in previous submissions, GrainCorp's eastern Australian export terminals are competitively constrained by:

- Strong domestic demand;
- Substantial excess capacity along the whole grain supply chain; and
- Numerous viable alternative pathways for grain to be exported from eastern Australia, including the unregulated container trade.

This has been confirmed by the ACCC previously. For example, in its Final Decision accepting GrainCorp's Port Terminal Services Undertaking determination in 2011, the ACCC stated:

'The ACCC notes in particular that port terminal capacity is relatively unconstrained on the east coast and that the export of bulk wheat through GrainCorp's port terminals are subject to a number of competitive pressures, including from domestic users, up-country supply chains, from other ports and the threat of customers by-passing GrainCorp facilities..... incentive for self-preferential treatment is moderated by countervailing competitive pressures in the case of GrainCorp.'

In the case of Newcastle, the degree of competition is now even higher, as described below:

- The 3 export terminals operating at Newcastle have a combined **4.3 million tonnes** of annual elevation capacity to service an average bulk export grain demand of only **1.1 million tonnes** and peak demand of **1.8 million tonnes**.
- The average annual utilisation of capacity at Newcastle, based on past actual annual exports is 23%. The peak utilisation in recent years was 43% in 2005, followed by 38% in 2012.
- The combined capacity of the NAT and LDA terminals can comfortably handle the total annual average and peak bulk grain export task at Newcastle.
- Approximately 63% of grain production (around 2 million tonnes) from the Northern NSW catchment zone (ie which is serviced by the Port of Newcastle), is consigned into the domestic and container markets.
- Upcountry, GrainCorp faces competition from:
 - 10 major country silos owned by major grain exporters, Cargill, Glencore and Louis Dreyfus. These competing silos have an estimated capacity of 800,000 tonnes;

- 8 local container packers with an estimated capacity of 1 million tonnes;
- on-farm storage.

In that respect, GrainCorp notes recent recognition by Government that the level of competition at Newcastle is robustly developing. In Treasurer Joe Hockey's statement in relation to his decision not to grant foreign investment approval of Archer Daniel Midland's acquisition of GrainCorp³, he noted that *'the transition towards more robust competition continues and a more competitive network is still emerging'* and that *'a number of new players have entered the market and new infrastructure (such as the Newcastle Agri Terminal) is being built.'*

GrainCorp further notes Emerald's observation that *'it is evident that GrainCorp now faces competition at the port of Newcastle'*.

In light of:

- (a) the general acceptance that there is a significant degree of competition amongst the three grain export terminals at Newcastle (supported by clear evidence of strong competitive constraints), together with
- (b) recognition that inequitable regulation gives rise to inefficiencies and costs, which will ultimately be passed up the supply chain to farmers,

GrainCorp submits that the Variation provides an appropriate level of regulation of GrainCorp's Newcastle Terminal and therefore should be approved by the ACCC.

4. THE PROPOSED VARIATION CONTINUES TO COMPLY WITH THE ACCESS TEST AND THE REQUIREMENTS OF PART IIIA OF THE CCA

4.1 The Variation is 'in connection with the provision of access to a service at the Newcastle terminal' and therefore capable of satisfying the access test

Interested parties have questioned:

- (a) whether the Variation is a valid undertaking capable of acceptance by the ACCC under Division 6, Part IIIA of the CCA (in respect of Newcastle); and
- (b) whether the Variation is sufficient to meet the Access Test contained in the WEMA.

Section 44ZZA(1) provides that *'a person who expects to be the provider of a service may give a written undertaking to the Commission in connection with the provision of access to the service.'*

'Service' is relevantly defined as a *'service provided by means of a facility'*.

³ <http://www.joehockey.com/media/media-releases/details.aspx?r=371>

Section 9 of the WEMA provides that *'a person passes the access test in relation to a port terminal service at a particular time if:*

(a) at that time, there is in operation, under Division 6 of Part IIIA of the Competition and Consumer Act 2010, an access undertaking relating to the provision to wheat exporters of access to the port terminal service for purposes relating to the export of wheat.

...

Accordingly, the access test will be passed if the Variation is an undertaking *'in relation to the provision of access to port terminal services at the Port of Newcastle.'*

The Variation is *'in connection with'* or *'in relation to'* the provision of access to Port Terminal Services, at Newcastle. It contains the following provisions which impose obligations on GrainCorp in respect of the provision of access at Newcastle:

- the obligation to comply with the continuous disclosure rules, including:
 - an obligation to publish the Port Terminal Services Protocols which apply to the loading of vessels at the Newcastle terminal;
 - an obligation to publish a shipping stem, which includes ships which have nominated to load at the Newcastle terminal;
- an obligation that the Newcastle Port Terminal Services protocols are a comprehensive statement of GrainCorp's policies and procedures for managing demand for Port Terminal Services;
- an obligation to keep information previously provided in the context of an access dispute or negotiation confidential.

The Variation therefore imposes these publication obligations on GrainCorp in respect of the supply of Port Terminal Services, and more specifically in respect of the loading of vessels at the Newcastle terminal. The fact that the Undertaking contains reduced obligations in respect of Newcastle, does not mean that it is not *'in connection with'* or *'related to'* access to services at Newcastle.

4.2 The Variation gives appropriate weight to 'the interests of persons who might want access to the service' and 'the public interest, including the public interest in having competition in markets (whether or not in Australia)'

The Undertaking exists in a unique situation, where there is (a) a legislative obligation on GrainCorp under the WEMA to submit a voluntary undertaking to the ACCC in respect of a service provided by infrastructure which is not in fact *'monopoly'* infrastructure and (b) there is inconsistent application of regulation of like infrastructure due to a peculiarity of the WEMA. This arises because the requirement to meet the access test is determined by the shareholding structure of the infrastructure owners, rather than by the nature of the service provided by the infrastructure.

In this circumstance, the Variation gives appropriate weight to (a) the interests of persons who might want access to the service and (b) the public interest, including the public interest in having competition in markets (whether or not in Australia). In assessing these criteria it is necessary to have regard to the fact that the service in question is being provided in a competitive market where GrainCorp is constrained by competing terminals.

5. PRIOR ACCC DECISION MAKING

GrainCorp disagrees with Emerald's remarks that the Variation would require the ACCC to make a decision that was inconsistent with the approach it took when initially approving the Undertaking in 2009. At that time, the ACCC observed that *'in having regard to the WEMA, the ACCC has not conducted a comprehensive market analysis in relation to each of the ports that will be subject to the Proposed Undertaking to assess whether they should be subject to access regulation...the ACCC considers that parliament has expressed a clear intention to require port terminal operators to provide access undertakings to mitigate the potential for anti-competitive harm and it is in this context that the ACCC must consider the appropriateness of those undertakings as provided.'*⁴

Those observations were made when the industry was newly deregulated and were entirely appropriate given that context. At that time the ACCC had no basis on which to assess the likely levels of competition that would ensue following the removal of the single wheat desk. In the five years since the commencement of the WEMA, the industry has matured and there is now a clear picture of how the industry has functioned and the competitive dynamics that exist, not to mention the construction of new infrastructure. It is entirely appropriate for the ACCC to now have regard to the operation of the industry and to take a different approach to the one it took in 2009.

We also note that to the best of GrainCorp's knowledge, in that period, no access disputes have been raised for its port terminals.

6. EXCESS CAPACITY

There is no basis for Emerald's suggestions that it be assumed that *'GrainCorp's capacity will be withdrawn, in part or in whole, from the industry.'* As GrainCorp has stated in numerous submissions, the high fixed cost nature of its infrastructure means that it is economically incentivized to maximize throughput in order to recover those costs.

GrainCorp has always, without legislative compulsion, actively promoted and provided country and port storage and handling services to all growers (through warehousing) and all grain traders. It has done so because it has a commercial incentive to maximise grain receipts at country receival sites and the export of grain through port terminals.

GrainCorp's revenue from bulk handling services depends on throughput, therefore it has a clear incentive to maximise throughput at its terminals.

⁴ ACCC draft decision in respect of GrainCorp's 2009 Undertaking 6 August 2009

7. NSW FARMERS' ASSOCIATION SUBMISSION

The NSW Farmers submission largely sets out concerns as to the nature of competition in the wheat industry rather than specific concerns with respect to the Variation. These issues have been raised by interested parties previously and assessed by the ACCC in the context of GrainCorp's 2009 and 2011 Undertakings. GrainCorp's responses to these issues are set out below.

GrainCorp rejects the assertion that it holds a natural monopoly position (particularly in the East Coast of Australia) in relation to wheat storage and handling. As GrainCorp has previously stated, there are a large number of competing country storage providers (eg. Cargill), container packers and on-farm storage. Detailed metrics of the competing country storage facilities were provided in our submission dated 12 November 2013. Indeed, the ACCC has acknowledged that on-farm storage imposes significant competition for the provision of wheat storage and handling services on the East Coast.⁵ In the ACCC's decision to accept GrainCorp's 2011 Undertaking, it noted that:

'There is significant competition for the provision of such services from:

- *on-farm storage (which makes up a relatively greater proportion of total storage capacity than in other regions);*
- *a significant number of independent bulk handlers. There is a wider choice of independent storage and transport providers compared to other regions; and*
- *limited overlap of GrainCorp's and Viterra's up-country storage networks⁶*

The ACCC has also previously recognised that the domestic market provides a competitive constraint on GrainCorp for the reason that it has first call on grain.

In a footnote to the above passage the ACCC observed that *'The PC report observed that the larger stock of on-farm storage in the East Coast may be attributable to the relative importance of the domestic market and longer history of choice in domestic marketing: Productivity Commission Inquiry Report No. 51: Wheat Export Marketing Arrangements, 1 July 2010, p. 68.'*⁷

GrainCorp disagrees with NSW Farmers' suggestion that eastern Australian containerised sector is unlikely to have a significant impact on the bulk export sector. As demonstrated in our Submission, container packers in northern NSW have 1.1 million tonnes of capacity – the ability to handle around 33% of average production.

The ACCC has previously considered the nature of competition from the containerised sector and concluded that *'containerised export grain volumes on the east coast are significant and have expanded in recent years'*.⁸

⁵ ACCC, Decision to Accept GrainCorp Operations Limited Port Terminal Services Access Undertaking, 22 June 2011.

⁶ ACCC, Decision to Accept GrainCorp Operations Limited Port Terminal Services Access Undertaking, 22 June 2011.

⁷ ACCC, Decision to Accept GrainCorp Operations Limited Port Terminal Services Access Undertaking, 22 June 2011.

⁸ ACCC, Decision to Accept GrainCorp Operations Limited Port Terminal Services Access Undertaking, 22 June 2011.

GrainCorp disagrees with NSW Farmers' suggestion that parties are unwilling to voice their concerns and that investigation into the grain market is necessary. Again, the majority of affected parties are large multinationals operating in a global market with a large number of options available to them in how they run their global businesses. Furthermore a number of these companies (Glencore and Pentag (Niderra) and Emerald (Sumitomo)) did make public submissions.

GrainCorp disagrees with NSW Farmers' suggestion that GrainCorp could exclude other exporters from obtaining capacity during the immediate post harvest period. As stated in our Submission, as Newcastle only operates at 23% capacity utilisation GrainCorp has the incentive to maximise shipments. Furthermore even if our GrainCorp Marketing division could use all the shipping capacity at Newcastle during this period, we would still face significant competition from NAT and LDA (which can comfortably accommodate the total annual average and peak bulk grain export task) and have a combined export capacity of 150,000 per month.

For completeness, GrainCorp notes that a number of issues raised by NSW Farmers have been considered previously by the ACCC and are not raised by the Variation. In particular, the terms of GrainCorp's Port Terminal Services Agreement which the NSW Farmers criticise was approved by the ACCC in 2008. Similarly, the ACCC has had the opportunity to consider and object to GrainCorp's Port Terminal Services Protocols on a number of occasions since 2008.

8. CONCLUSION

For the reasons set out above, GrainCorp considers that it is appropriate for the ACCC to accept the Variation having regard to the considerations set out in section 44ZZCA(1) of the CCA.

We would be pleased to meet with the ACCC or should you require any additional information please contact myself or Angus Trigg, Director, Government & Media Relations (or 02 9325 9132 atrigg@graincorp.com.au).

Yours sincerely



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