

# Introduction of Auction System

## Response to submissions in relation to the ACCC's Consultation Paper

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### 1 Introduction

#### 1.1 Purpose of submission

This document sets out Vitterra's comments and observations in relation to certain issues raised in submissions made in response to the ACCC's Consultation Paper dated 28 February 2012.

#### 1.2 Vitterra's proposed auction system

Vitterra is pleased that a number of the submissions are supportive of many aspects of the proposed auction system set out in its Auction Variation Notice dated 17 February 2012. This reflects the significant efforts that Vitterra has made in consulting with industry participants and in designing a market leading auction solution which satisfies the requirements set out in the Access Undertaking.

Vitterra also welcomes the recognition by certain exporters – notably, Australian Grain Exporters Association (“AGEA”) and the South Australian Farmers Federation (“SAFF”) that the clear imperative is to introduce the auction system as soon as practicable in order to provide certainty to the industry and that, if required, certain changes can be made to “fine tune” the auction system once it is in place. SAFF has also recognised that certain changes are most appropriately considered in light of the experience after *“a couple of harvests with the auction system in place”*.

It is for this reason that Vitterra has expressly committed in the new Port Loading Protocols to undertake a review and to consult with industry participants after the 2012/2013 harvest period, with a view to determining what (if any) changes may further improve the auction system. Vitterra will undertake this review with the same good faith that it has demonstrated in the current process.

Vitterra also considers that an experience of the first ever port terminal services auctions in South Australia will assist exporters, Vitterra and the ACCC to approach this review from a more informed position.

Vitterra also notes the view expressed in some of the submissions that there are certain flaws in relation to the current CBH system. However, those criticisms relate to the CBH system, not the capacity allocation and management system proposed by Vitterra. There are a number of significant differences between the capacity allocation system proposed by Vitterra and that implemented by CBH. In particular:

- Vitterra has provided very substantial transparency and clarity in relation to its proposed processes. Clients have more information than ever before in relation to the booking processes and operational requirements. These clear rules are included in the Port Loading Protocols and Auction Rules;
- Vitterra provides a significantly greater level of transparency and earlier information on its shipping stem. This information provides substantial assistance to clients seeking to understand future capacity availability or to trade or move slots;

- based on industry feedback, Viterra has designed the timing of its proposed auctions to balance clients' requirements for certainty, forward planning and visibility of crop quality and volumes. This is recognised in a number of the submissions;
- the first-in-first-served system (which only applies on and from a clearly published time after the relevant auction or auctions have taken place) is an online and clearly auditable booking system with each client limited to five log-ins and each booking restricted to one port terminal and one slot. This places increased structural disciplines on bookings for capacity not acquired at auction. In particular, it prevents an exporter from securing significant volumes of the remaining available capacity by submitting a single booking application, and ensures that other exporters have a very realistic prospect of successful bookings. Importantly, this means that exporters who withdraw bids from the auction can have no certainty that they will be able to obtain export capacity as part of the first-in-first-served system; and
- Viterra provides very significant flexibility to clients once they have made a booking. There are no limits to the number of times clients can trade or move bookings. Clients can also surrender (and obtain a partial refund for) bookings and split their bookings. These differences in Viterra's system further support the efficient allocation of capacity.

These are all important factors which support the efficiency of Viterra's proposed auction system and are likely to address the issues experienced by some exporters in previous auctions in Western Australia.

### 1.3 The ACCC's consideration of the auction system

Viterra also considers that it is not appropriate for the ACCC to use the processes under Viterra's Access Undertaking, which were designed to facilitate the introduction of an auction system in South Australia, to revisit issues that may have arisen in a different State, in respect of one previous season and under different auction and port loading rules. While Viterra understands that certain industry participants consider that some of their fellow exporters may have engaged in "gaming" conduct last season in Western Australia, there is a very real risk that some of the proposals provided to the ACCC are so focussed on preventing past conduct in Western Australia, that they have lost sight of the primary intention of the auction system and the actual requirements of Viterra's Access Undertaking.

It is imperative that the ACCC is alert to its role and the requirements under the Access Undertaking.

It is also imperative that the ACCC recognises both the market-based nature of the auction system proposed by Viterra, and the very real risks of distorting these market-based outcomes by too much intervention or by placing additional restrictions on exporters. Viterra understands the natural desire of certain exporters to seek protection from the rigours of a market-based system (and to suggest that auction strategies by other exporters involve "gaming"<sup>1</sup>). However, while any changes to the proposed system may drive a different outcome, it is far from clear that any changes to the auction system proposed by Viterra would produce superior, more efficient or more market-based outcomes.

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<sup>1</sup> Viterra notes that it is not clear why an exporter deciding not to participate in an auction, or to withdraw an auction bid, so that it can seek a first-in-first-served booking (if available) involves "gaming" or is inefficient. There is a very significant and important difference between fraud or manipulation of an auction that is enabled by market power (i.e. "gaming"), and an exporter taking a decision that it does not value the slot at the current auction price and that it therefore wishes to seek any remaining capacity at a later time. The second situation (i.e. exporters continuing to participate in an auction, or ceasing participation in an auction) involves independent decisions by the relevant exporters based on a range of factors (which may include predictions about how other exporters may respond). However, this is no more "gaming" than any other legitimate auction strategy. Exporters may, from time to time, take positions that turn out to be wrong (i.e. they pay more than others, or they may miss out on obtaining capacity). However, this is not something that can or should be the focus of the ACCC's review. If exporters have an equal opportunity to pay what they are willing to pay for a slot, the ACCC review should not seek to protect them from the consequences of that decision.

Grain traders are also very adept at exploiting new opportunities created by such changes. In this situation, Viterra considers that the ACCC should exercise caution in intervening.

Viterra considers that its proposed auction system satisfies the requirements set out in its Access Undertaking to the ACCC and that the ACCC should therefore not issue an Action Objection Notice.

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## **2 Response to issues raised in AGEA's submission**

### **2.1 Introduction**

This section sets out Viterra's comments and observations in relation to specific issues raised in AGEA's response to the ACCC's Consultation Paper.

### **2.2 Closing of slots prior to the end of the auction**

AGEA has suggested that rules or practices should be put in place to enable the bid to be booked if the slot is under-subscribed. The slot would remain open with capacity reduced by the amount which has been booked.

Viterra's observations in relation to this proposal are as follows:

- (a) This proposal would appear to provide significantly less flexibility for exporters as it would limit the extent to which they can change their bids and consider alternatives in response to auction developments.
- (b) This proposal would appear to distort consideration of the value that exporters attribute to particular slots. For example, a client may value a slot at Port Lincoln at \$8.50, but rather than move to the next round at \$9.00, prefer to move the booking to Wallaroo (or to a different slot at Port Lincoln). This ability to shuffle demand is central to the efficient valuing and allocation of the slots.
- (c) This proposal may result in capacity not being allocated to the exporters that value it the most, as required by the Access Undertaking. For example, if a booking was accepted for a slot after round 2 of the auction, this may result in the relevant exporter obtaining the booking at a lower price than others if there is subsequently increased demand for that slot.
- (d) Rather than resolving "flaws", this proposal would appear to exacerbate the concerns raised in relation to the CBH auction system. If an exporter cannot move a bid to the Wallaroo slot (because there is less capacity available for that slot), its only alternative may be to keep bidding up the price for other slots, or to withdraw its bid and to take a chance in relation to whether it can make a first-in-first-served booking (which requires a judgment that capacity will still be available and that the exporter will still obtain that capacity).
- (e) This proposal is likely to create significantly greater complexity in relation to any auction rebate calculation. Presumably, consistent with clause 9.5(d)(vi) of the Access Undertaking, the auction premium rebate would need to be shared with exporters who acquired the slot after round 2, even though they effectively reduced the alternatives available to other exporters.
- (f) [confidential].

### **2.3 Auction frequency**

AGEA has suggested that rules or practices should be put in place for more frequent auctions. Viterra's observations in relation to this proposal are as follows:

- (a) Viterra is open to exploring changes to the frequency of auctions as part of the review following the 2012/2013 harvest. Actual experience in the first season with auctions in South Australia is likely to provide the best (and indeed only) factual basis for considering whether an increase in auction frequency would provide a system that is more efficient than the one currently proposed.
- (b) Viterra considers that an unspecified proposal to increase the frequency of auctions by an amount “*to be agreed*” (i.e. by an amount in respect of which there is currently no consensus) should not hold back the introduction of the system currently proposed. It is difficult to see how an unspecified increase in the frequency of auctions could be viewed as materially more efficient than Viterra’s current proposal. As stated by AGEA, an increase in the number of auctions also comes at an increased cost and requires increased resources and commitment from both Viterra and exporters.
- (c) Although the proposal to increase the frequency of auctions is presented as a means of addressing “flaws” in the current CBH system, Viterra notes that CBH’s response to the issues experienced in Western Australia last harvest was to reduce rather than increase the number of auctions. Accordingly, there remain divergent views in relation to auction frequency. If the past is a guide, exporters may also have different views depending on their trading position or commercial interests at any given time.
- (d) Viterra notes AGEA’s suggestion that “*the Port Terminal operator should have the flexibility to offer capacity 3-5 years out on an agreed deferred payment schedule*”. This is not a matter that has previously been raised in consultation. It would require detailed consideration by Viterra and significant changes to current systems which would each involve significant delays in the introduction of the auction system. This is clearly contrary to Viterra’s legitimate business interests. Given that the Access Undertaking expires in September 2014, this proposal also raises matters that are outside the scope of the Access Undertaking.

## 2.4 Reductions in bids

AGEA has suggested that rules or practices should be put in place to limit the volume a bidder can reduce their tonnage by, to the maximum volume that the slot is over-subscribed. Viterra’s observations in relation to this proposal are as follows:

- (a) It is not clear that this proposal would result in a more efficient allocation of capacity (which is the objective of the Access Undertaking). It would also appear to be premised on a presumption that all bookings potentially involve “gaming” or an “anti-competitive” purpose, such that it is necessary to take away the flexibility that exporters would otherwise rightfully have to change bids in response to auction changes. In contrast, Viterra’s starting point is that the auction system should deliver a flexible, liquid, market-based system for exporters.
- (b) This proposal would also appear to carry a significant risk of negative or unintended consequences. It is likely to result in clients being forced to pay more than they would otherwise be prepared to pay for a particular slot (i.e. if they are forced to continue bidding in successive rounds because they are prohibited from withdrawing their bids). It is difficult to reconcile this with the underlying objectives of an auction system.

## 2.5 Increasing capacity at auctions

AGEA has suggested that rules or practices should be put in place to give flexibility to the port terminal operator to increase capacity by an agreed tolerance to enable a slot to be closed out.

If this is something that is valued by exporters, Viterra would be open to exploring this change as part of the review following the 2012/2013 harvest. However, prior to introducing any change of this nature, it would be critical to consider the genuine efficiency gains expected to result from the change. Viterra's initial view is that:

- (a) the proposal would appear to create incentives to lessen the declared capacity for particular slots, rather than create any genuine efficiency benefit in relation to the allocation of capacity; and
- (b) the proposal (and the ability for the port terminal operator to change the amount of capacity for any slot mid-auction) would seem to be somewhat inconsistent with the requirement in the Access Undertaking that "*the auction should be conducted in a transparent... manner*". That said, if exporters wish to afford Viterra greater discretion in relation to how the auction operates and what capacity is available, Viterra is proposed to consider this as part of the review following the 2012/2013 harvest.

## 2.6 First-in-first-served as a secondary means to allocate capacity

AGEA has suggested that rules or practices should be put in place so that there is no default to a first-in-first-served system. Viterra's observations in relation to this proposal are as follows:

- (a) Any system which involves auctions as the **sole** method of allocating capacity is likely to be very inflexible, costly and involve unnecessary operational inefficiencies in relation to the actual purpose of the auction (i.e. to facilitate the export of a physical commodity). It is well accepted among economists that, while auction systems can involve a number of efficiencies, they are not without costs and limitations. The proposed first in first served system (as a secondary way of allocating capacity) is designed to complement the auction system (as the primary method of allocating capacity) by ameliorating some of these limitations. Ultimately, any increased costs and reduction in operational efficiencies are likely to be borne by growers without any offsetting benefit in relation to the underlying actual task of shipping grain.
- (b) Any system which involves auctions as the **sole** method of allocating capacity is likely to lead to less capacity used by exporters and a lower utilisation of Viterra's infrastructure. This is not efficient and is not in the interests of either Viterra or access seekers. For example, if an exporter approaches Viterra to book a slot to export grain on short notice, Viterra may be required to say "no", even if that slot is available because it has previously been passed in at auction. The requirement to wait for the next auction may also disadvantage exporters if the exporter requires immediate certainty in relation to available capacity so it can secure a sale (which certainty Viterra will not be able to provide), or if waiting for the next auction would not provide sufficient time to support the physical requirements for exporting grain (which will also result in lost sales or lost capacity). This is clearly inefficient and detrimental to both Viterra and exporters.
- (c) The main efficiencies created by auctions arise in circumstances where there is scarce capacity. It is far less clear what genuine efficiencies they deliver in circumstances where supply exceeds demand. The past two seasons in South Australia have seen significant crop sizes. However, historically smaller crop sizes and smaller export volumes are far more common (see **Attachment 1**). A requirement that capacity can **only** be allocated by auction is likely to result in a series of unnecessary and costly auctions in times when supply exceeds demand. It would also result in the Port Loading Protocols constraining the ability of exporters to deliver grain into global markets in times (e.g. droughts or small crop seasons) where those sales may be even more critical (see paragraph (b) above).
- (d) The Access Undertaking does not require that an auction system is the **only** way of allocating capacity. Clause 9.5(d)(i) of the Access Undertaking states that "*an auction should be the*

*primary means of allocating port-loading capacity at each Port Terminal*". This clearly envisages that it is permissible under the Access Undertaking for there to be other secondary or tertiary ways of allocating capacity. It would be inconsistent with, and contrary to, the Access Undertaking to suggest that there cannot be secondary or tertiary ways of allocating capacity which complement the primary auction method.

- (e) Only 6 to 8 months ago, the ACCC accepted the existence of a first-in-first-served system as the sole method for allocating capacity in New South Wales, Queensland and Victoria and as a secondary way of allocating capacity in Western Australia. It would involve a highly inconsistent and unreasonable approach by the ACCC if it were to form the view that the first-in-first-served system should be removed totally, but only in South Australia.

[confidential].

Having regard to these matters, Viterra considers that this proposal represents a clear example of certain submissions being so focused on preventing conduct that occurred in a previous season in a different State and under a different system, that they have lost sight of the primary objective of facilitating the export of a physical commodity, and the actual requirements of the Access Undertaking.

## **2.7 Visibility of bidding strategies**

AGEA has suggested that rules or practices should be put in place to enable visibility of bidders and tonnes (which would be by code, not specific names). Viterra's observations in relation to this proposal are as follows:

- (a) It is not clear to Viterra what efficiency or other benefits are likely to arise from this proposal. If the intention is to reduce the ability of exporters to change their bids during an auction, this would not seem to be a desirable outcome. If the intention is to provide much greater transparency in relation to the bidding strategies of individual exporters:
  - (i) it is not clear that this is desirable – the purpose of the auction is to enable exporters to compete for slots using a market-based system, employing their own strategies; and
  - (ii) it is not clear that this would provide any greater ability to detect or prevent "gaming". There are many legitimate reasons why exporters may change their bids from round-to-round, and it is already clear that exporters bid for – and adjust bids for – large amounts of capacity on a round-to-round basis. If there is a concern about "gaming" or anti-competitive practices, the ACCC is able to seek this information. However, Viterra has significant doubts that the provision of this information would provide any efficiency benefits in relation to the operation of the auction system, or enhance the ability of other exporters to participate in the auction.
- (b) [confidential].

## **2.8 Determination of capacity made available at auction**

AGEA has suggested that the capacity offered at auction should reflect the capacity that is made available to exporters to enable the export of bulk grain, and that there is evidence of over-selling in the past season. AGEA has suggested that the implementation of appropriate accountability agreements would assist to avoid this scenario by providing improved market signals for industry participants to ensure "*supply chain optimisation, accountability and performance*". Viterra's observations in relation to this proposal are as follows:

- (a) As required by the Access Undertaking, Viterra is seeking to introduce an auction system in relation to the “*allocation of port-loading capacity*”. AGEA’s suggestion about accountability agreements to facilitate “*supply chain optimisation, accountability and performance*” would seem to go well beyond the requirement to auction port-loading capacity. It is not appropriate that these matters are considered in any assessment of Viterra’s Auction Variation Notice.
- (b) Viterra agrees that a number of booked slots have not been executed by exporters in the past season. However, this is not due to “over-selling” of capacity. A key factor is the very large number of vessels (across all exporters) that have failed mandatory vessel surveys. Details of these large vessel failure rates are set out in **Attachment 2**. As set out in Attachment 2, there are certain months in respect of which all vessels presented have failed survey. This is clearly a significant factor in delays. While outside the scope of the current auction process, Viterra considers it essential that this material failure by exporters to present vessels which satisfy mandatory survey requirements is addressed going forward as it imposes significant costs on the entire industry.

## 2.9 Auction premium rebate

Viterra notes and welcomes AGEA’s support for the auction premium rebate design as set out in the Auction Variation Notice.

In relation to AGEA’s suggestion that the rebate should be paid more frequently, Viterra notes that the rebate cannot be calculated and paid until after the end of the relevant auction period (i.e. when it is known whether or not the client has executed against that slot, and other exporters have executed against their slots). This is fundamental to the requirement in the Access Undertaking that the auction system should create disincentives which apply equally to all clients on booking in excess of reasonably anticipated requirements.

In relation to AGEA’s comment that it would like to see “*greater transparency of auction costs*”, Viterra has always been clear that it intends to provide transparency for all exporters.

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## 3 Response to issues raised in Louis Dreyfus’ submission

In response to Louis Dreyfus’ submission<sup>2</sup>, Viterra wishes to re-iterate that:

- (a) the proposed auction system differs from that implemented by CBH in a number of key respects (see section 1.2 above). Each of these differences supports the efficiency of Viterra’s proposed auction system and is likely to ameliorate and address the issues experienced by some exporters in previous auctions in Western Australia. Accordingly, Viterra does not agree with the assertion that “*the proposed model ... does not address the shortcomings of the model on which it was based*”; and
- (b) under Viterra’s proposal, the auction system will unequivocally be the primary means of allocating port-loading capacity. The availability of a first-in-first-served system to provide capacity *after* exporters have decided not to acquire capacity at the auction does not mean that the first-in-first-served system is a primary means of allocating that capacity.

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## 4 Response to issues raised in Grain Producers SA’s submission

Viterra’s response to the issues raised in the submission by Grain Producers SA Ltd (“GPSA”) is set out below.

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<sup>2</sup> [confidential].

- (a) GPSA has suggested that “*any slots that have been bid on twice at the same price should be knocked down to the bidder rather than these slots having to be bid on in subsequent rounds*”. Viterra’s response to this issue is set out in section 2.2 above.
- (b) GPSA has suggested that “*there should be a system in place to prevent bidders withdrawing bids and then reverting to a first come first served basis*”. GPSA appears to suggest that exporters should be required to provide a letter of credit or be precluded from participating in the next auction if they withdraw bids. Viterra’s response to this issue is set out in section 2.3 above. In addition, Viterra has difficulty understanding any suggestion that exporters should provide a letter of credit (presumably to pay for the maximum amount of tonnes they bid, even if they do not acquire those tonnes), or be precluded from participating in the next auction if they withdraw bids. As the ACCC will appreciate, there are many legitimate reasons why an exporter may withdraw bids. Indeed, the auction system relies on, and is specifically designed to facilitate exporters withdrawing bids so that excess demand is reduced to meet available capacity.
- (c) GPSA has suggested that “*the publication of the nomination date and acceptance date of first come first served bookings needs to be included in the protocols. This allows for transparency and auditability of the allocation system*”. Viterra notes that it has always published the “date nominated” and “date accepted” on its shipping stem. This does not require any amendment to the Port Loading Protocols.
- (d) GPSA has suggested that “*the making available of additional capacity of more than 50,000 tonnes rather than 200,000 tonnes through the auction system [would be] more appropriate*”. Viterra notes that 50,000 tonnes is less than one panamax vessel. Accordingly, this suggestion would appear to be very restrictive both for Viterra and exporters.
- (e) Viterra notes GPSA’s suggestion that auction premiums could initially be covered by letters of credit. This is an issue that Viterra is open to exploring as part of the review following the 2012/2013 harvest. However, it should not hold up the introduction of the auction system.

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## 5 Response to issues raised in PentAG’s submission

Viterra’s response to the issues raised in PentAG’s submission<sup>3</sup> is set out below:

- (a) **Early acceptance of certain bookings** - PentAG has suggested that rules should be implemented so that a booking can be accepted if a slot is under-subscribed (with only the un-booked capacity staying open during the remainder of the auction). Viterra’s response to this issue is set out in section 2.2 above.

Viterra disagrees that the current system (under which all slots remain open until the end of the auction) creates a “*massive incentive to ‘game’ with very little sanction*”. However, the proposal to accept certain bookings before the end of the auction:

- (i) will provide significantly less flexibility for exporters and will remove export alternatives for them;
- (ii) is likely to distort the value that exporters attribute to particular slots. The ability to re-allocate bids in response to auction developments is central to the efficient valuing and allocation of the slots;
- (iii) is very likely to result in capacity not being allocated to the exporters that value it the most, and is therefore contrary to the Access Undertaking;

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<sup>3</sup> [confidential].



- (iv) is likely to exacerbate the concerns raised in relation to the CBH auction system. If an exporter cannot move a bid to an alternate slot (because there is less capacity for that slot), its only alternative may be to keep bidding up the price in other slots or to withdraw its bid and seek to make a first-in-first-served booking; and
- (v) will create significantly greater complexity in relation to any auction rebate calculation. It is not consistent with the intention of the Access Undertaking that exporters who may not have paid the true value of the slot (as can only be determined by the auction), and the allocation of capacity to whom reduces choices for other auction participants, should obtain a share of the auction premium rebate.

Viterra also disagrees with the unsupported assertion that “*if Viterra ran an auction system tomorrow under their proposed system, there can be little expectation that a different outcome to the last three CBH auctions would occur*”. First, there are a number of key differences between the CBH and Viterra auction systems. Second, this statement seems to draw universal conclusions from the experience in one season (in a different State and under a different system). Viterra’s very long standing experience is that each season brings different outcomes, different participants and different approaches. Third, Viterra considers that exporters will (and should) respond to differing market situations and any differences in the technical rules that apply to them. It is far from clear to Viterra that the change proposed by PentAG would be a complete panacea to the issues it has raised as concerns or create a more efficient solution.

- (b) **Visibility of bidding strategies** - PentAG has suggested that individuals should be identified by a designated code to “*allow other participants to recognise and keep firm evidence of gaming behaviour*”. Viterra’s response to this issue is set out in section 2.7 above. Given that the auction system (as proposed by Viterra and as required by the Access Undertaking) is fundamentally based on exporters reducing the amount of capacity they bid until supply and demand are in balance, it is unclear how this actually occurring (even if the bidder can be identified by a code) will provide other exporters with evidence of “gaming”. Auctions are already subject to oversight by the ACCC. It is appropriate that the ACCC can, if necessary, consider whether an exporter’s actions involve the legitimate withdrawal of bookings, or anti-competitive gaming. However, the change proposed by PentAG is unnecessary and undesirable.
- (c) **Access to capacity** - PentAG has suggested that there should be no first-in-first-served system after the relevant auctions have taken place. Viterra’s response to this issue is set out in section 2.6 above. Viterra also disagrees with PentAG’s assertion that the existence of a secondary first-in-first-served system “*does not hold with tenets of transparency and competitive access and is impossible to police when administered by the BHC*”. Viterra has provided very substantial transparency and clarity in its Port Loading Protocols and through the information contained on the shipping stem. Clients have more information than ever before (and substantially more information than the CBH system) in relation to the booking processes and operational requirements. Both the auction system (as the primary method) and the first-in-first-served system (as a secondary method) provide competitive access and can be readily policed by the ACCC, WEA and exporter clients.
- (d) **Increasing capacity** - PentAG has raised certain issues in relation to Viterra’s incentives to increase capacity. It is unclear how these issues may relate to the introduction of an auction system. However, even more fundamentally, those issues are misconceived and appear to be based solely on unsupported allegations and not on any evidence or experience over the past few years.

The past two years have seen two of the largest shipping seasons in South Australia’s history. Viterra has previously provided the ACCC with a number of statistics that show

record crops, record exports and significant increases in export throughput and capacity. It is extremely difficult to reconcile this hard data with PentAG's assertions.

In addition, Vitterra's clear incentive is to maximise throughput in order to achieve a return on its infrastructure assets. Even before the requirement to have an Access Undertaking, Vitterra operated its port terminals on an open access basis. Vitterra therefore strongly disagrees with this issue raised by PentAG. It does not in any way reflect the business environment in which Vitterra operates.

- (e) **Auction premium rebate** - PentAG has suggested certain adjustments to the timing of payment of the auction premium rebate. As set out above, Vitterra is open to exploring the introduction of an instalment process or letters of credit as part of the review following the 2013/2013 harvest. However, these potential changes should not hold up the introduction of the auction system.

PentAG has also suggested that a proportion of the rebate should be provided "*as soon as possible post performance and well before the end of the entire season*". As set out in section 2.9 above, the amount of the rebate payable to any exporter cannot be calculated and paid until after the end of the relevant auction period (i.e. when it is known whether or not the client executes against that slot, and other exporters execute against their slots). This is fundamental to the requirement in the Access Undertaking that the auction system should create disincentives which apply equally to all clients on booking in excess of reasonably anticipated requirements.

Vitterra considers that interim measures and part payments are likely to add significant complexity and increase Vitterra's (and exporters') exposures to payment by other exporters.

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## 6 Response to issues raised in Anonymous Submission A

Vitterra's observations and comments in relation to the issues raised in Anonymous Submission A are as follows:

- (a) **The first-in-first-served system** - Vitterra's response in relation to the proposal that there is no secondary first-in-first-served mechanism and that certain bookings should be accepted before the auction closes are set out in sections 2.6 and 2.2 above.

Vitterra welcomes the acknowledgement by Anonymous A that the first-in-first-served system should be available in respect of additional or forfeited capacity. However, it is unclear what efficiency benefits there would be in imposing a rule that required Vitterra to make that capacity available at a higher price than it otherwise would, particularly when that higher price relates to the supply of different capacity at a previous auction. The purpose of the auction is to set a market price for the capacity that is available at the auction. It is not to set a minimum price for potential future capacity.

- (b) **Auction frequency** - Vitterra's response to the proposal for more frequent auctions is set out in section 2.3 above. However, it is important to dispel the assertion in Anonymous A's submission that more frequent auctions would enable Vitterra (as the infrastructure operator) to make a "*much more transparent and realistic determination of available capacity*". Vitterra's supply chain and port capacity planning horizon extends significantly beyond the quarterly auction proposal by Anonymous A. Accordingly, any proposal to increase the frequency of auctions should not be based on an erroneous view that this will assist the infrastructure operator.
- (c) **Timing of auctions** - Anonymous A has suggested that there should be quarterly auction periods as this "*aligns to the demand profile where buyers generally only buy 60-90 days in*

*advance rather than the entire capacity being auctioned and/or acquired well in advance*". However, Viterra has some concerns that this is not representative of the feedback that it has received from all exporters. In addition, a number of exporters demonstrated in March 2011 that they were willing to make "long range" bookings on Viterra's shipping stem. AGEA's submission has also clearly stated that Viterra should *"offer capacity 3-5 years out on an agreed deferred payment schedule"*. These are all inconsistent with Anonymous A's suggestion.

Viterra also notes that GrainCorp has recently announced that it proposes to open its shipping stem to reflect two booking periods. Those booking periods are similar to those proposed by Viterra.

Finally, Viterra, as an infrastructure operator, has substantial concerns with any suggestion that capacity should only be booked around 60 days in advance. This appears to ignore entirely the reality that the port operations involve a physical task of receiving, handling and loading grain for a number of different clients. While it may be possible to conduct quarterly auctions (and Viterra's comments on this issue are set out in section 2.3 above), those auctions could not be held only 60-90 days in advance of the proposed slot dates. This would bring port operations to a halt.

- (d) **Role of the Auction Review Committee** - Anonymous A has suggested that there should be a greater role for the Auction Review Committee ("ARC"). As set out in Attachment 1 of Viterra's communication with clients dated 17 February 2012, there are likely to be number of real issues in providing the ARC with an ability to allow or disallow bids based on an assessment of bidder's requirements. The difficulties in making subjective judgments about a client's ability to execute capacity were highlighted in discussions with the ACCC concerning the current access undertaking, and resulted in the removal of the anti-hoarding provisions from the Port Loading Protocols. For these very practical reasons, Viterra is extremely reluctant to take on (or delegate to the ARC) a responsibility to "second-guess" the functioning of the auction which is designed to allocate capacity to clients who value it the most (a requirement of the Access Undertaking).
- (e) **Secondary trading platform** - Anonymous A has suggested that consideration should be given to the creation of a platform that will facilitate transfer in the secondary market. As set out in Attachment 1 of Viterra's communication with clients dated 17 February 2012, Viterra would be prepared to discuss the issue of a transfer platform further with the industry as the system evolves. However, this proposal falls outside the scope of the current proposal to introduce an auction system.

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## 7 Response to issues raised in Anonymous Submission B

Viterra's observations and comments in relation to the issues raised in Anonymous Submission B are as follows:

- (a) **Determination of capacity – Export Select and Export Standard** - In accordance with the Access Undertaking, the auction system will relate only to port terminal capacity. It will not relate to upcountry logistics capacity, and accordingly, exporters will not "bid" for that logistics capacity during auctions. As set out in Attachment 1 of Viterra's communication with clients dated 17 February 2012, Viterra is aware of this issue, and proposes to engage with industry regarding the available Export Select capacity prior to auction. This will enable exporters to factor that information into their respective bidding strategies.
- (b) **First in first served** – Viterra welcomes the acknowledgement by Anonymous B that the first in first served system is appropriate as a secondary method of allocating capacity, and the importance of the features of Viterra's system which structurally limit bookings of

significant volumes. Viterra would be pleased to provide further details about the log-in process to exporters. However, essentially, once an exporter using one log-in has made a booking, that log-in terminal is free to make another booking application.

- (c) **Capacity allocation** – Viterra’s response on this issue is set out in section 2.5 above.
- (d) **Auction premium pool** – Anonymous B has made certain suggestions in relation to management of the auction premium pool. Viterra considers that this proposal, if implemented, would be likely to raise a number of complex issues given the significant flexibility that Viterra offers for clients to move bookings between different port terminals. If an exporter were to acquire a slot at one port terminal at auction and then subsequently move that slot to another port terminal, this could have a significant (and unintended) impact on the calculation of the auction premium.

The transparency of pricing and available capacity at all ports during the auction, and the ability to transfer booked capacity between ports, are also important components of the auction system design. The impact of pricing at each port and the estimated rebate are factors that may be taken into account by exporters when bidding. Given that all exporters have an equal ability to bid during each auction, it is unclear how this could be viewed as favouring certain exporters.

Viterra is also unaware of this previously being raised as an issue with respect to CBH’s auction system, where capacity is auctioned at four different ports and the rebate is applied equally.

- (e) **Additional Capacity** – Viterra’s comments and observations in relation to the proposal that auctions be the sole method for allocating capacity are set out in section 2.6 above. This would have a material detrimental impact on the primary task of exporting grain. In addition, Viterra considers that Anonymous B’s proposal that “Additional Capacity” be capped at 5,000 is unrealistic. This represents less than the *tolerance* that Viterra currently grants in respect of panamax vessels.
- (f) **ARC** – Anonymous B has suggested that Viterra should have only one representative on the ARC as the existence of a further non-voting Viterra representative may “*open up the potential for further influence to occur*”. Viterra considers that this proposal misunderstands the intended nature and role of the ARC. The ARC’s powers are quite limited, and Viterra is strongly opposed to giving powers to the ARC which would enable it to exercise a discretion to assess the bidding strategies or volumes of bids made by participants or to alter the course of auctions (other than in circumstances where there has been an error). In contrast, Viterra having representatives involved in the ARC for its own auction system would seem to enable it to be more responsive to issues as they arise.
- (g) **Amendments to Port Loading Protocols** – Viterra’s response to each of the issues raised by Anonymous B are set out in Attachment 1 of its communication with clients dated 17 February 2012.

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## 8 Response to issues raised in Emerald’s submission

Viterra’s response to the issues raised in Emerald’s submission<sup>4</sup> is set out in Attachment 1 of its submission dated 17 February 2012.

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<sup>4</sup> [confidential].

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## **9 Response to issues raised in Gavilon's submission**

Viterra's response to the issues raised in Gavilon's submission<sup>5</sup> is set out in Attachment 1 of its submission dated 17 February 2012.

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## **10 Next steps**

If the ACCC has any further questions, Viterra would be pleased to assist.

**19 March 2012**

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<sup>5</sup> [confidential].

## Attachment 1 – Size of wheat crop in South Australia

Year	Size of crop (tonnes)	Tonnes exported
2001/2002	4,778,000	4,635,760
2002/2003	2,072,000	1,363,903
2003/2004	3,490,000	3,204,550
2004/2005	2,621,000	1,897,502
2005/2006	3,853,000	3,177,630
2006/2007	1,446,000	548,981
2007/2008	2,346,000	1,105,537
2008/2009	2,295,000	1,878,950
2009/2010	4,052,000	3,535,627
2010/2011	5,818,500	5,481,492
2011/2012	4,444,800	2,509,018 (current as at 29 February 2012)

## Attachment 2 – Vessel survey failure rates by port

