This submission to the Petrol Price Inquiry [‘the Inquiry’] is made as a direct and indirect consumer of unleaded petrol, for both business and private purposes.

My submission is limited to one main point only: namely the apparent use by refiners of the Singapore Mogas 95 Unleaded ex-refinery price [‘the Singapore Price’] in setting the ex-refinery price for unleaded petrol produced in Australia [‘Australian Refinery Prices’].

The largest of the refiners, Caltex, has suggested in its published materials on Australian petroleum prices that the Singapore Price is used as a benchmark to set its Australian Refinery Prices. Other refiners similarly suggest that the Singapore Price is used to set their Australian Refinery Prices. For example, the Caltex publication ‘**Petrol pricing - the plain facts**‘ states that: ***‘Prices for petrol in Australia are based on a calculation of what it would cost an importer to bring a shipload of petrol from Singapore to Australia’*** **.** Mobil states that: ***‘Mobil sets its wholesale (terminal gate) price for petrol competitively, with reference to international (Singapore market) prices’.*** The Shell web site also suggests that it uses the Singapore Price to set its ex-refinery prices, for example, its statement: ***‘Why do we use import parity price?’***

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I have not been able to find any regulatory basis for setting Australian Refinery Prices (or terminal gate prices) in this way. It is, therefore, unclear to me whether there is, as between refiners, some agreement, practice or understanding relating to the use of the Singapore Price in setting Australian Refinery Prices. In my submission, the Inquiry should clearly identify the basis (whether regulatory, collusive or otherwise) of any such practice; and also just how the Singapore Price is so used.

However, even if, in a regulatory sense, it is legitimate for the refiners to use the Singapore Price in setting Australian Refinery Prices, in my submission this is not justifiable:

- The Inquiry will presumably establish approximately the proportion of Australian unleaded petrol derived from indigenous crude oil. My understanding is that, conservatively, about 80% to 85% of unleaded petrol sold in Australia is refined in Australia from indigenous crude [the Caltex publication ‘**Petrol pricing - the plain facts**‘ says that, overall, about 16 percent of our petrol was imported in the previous year].
- If this is anywhere near right, then it is not at all obvious why [at least any longer] the Singapore Price is relevant or should be used to set Australian Refinery Prices. Australian Refinery Prices should rationally be determined by ordinary market forces including: the cost of feedstock; production costs; a suitable return on capital employed; and market based supply and demand forces. Substitutability of imported product, and the price at which domestic product can be sold into the export market, would be no more, nor less, relevant than for any other domestically produced goods. For example, it would be remarkable [and, I suggest, wholly unacceptable] if the ex-mill price of flour in Australia were set by the Australian flour milling industry by direct reference

to the ex-mill prices in the United States. The practice, if it be, of using the Singapore Price in the manner suggested by the refineries in their published materials is, in my submission, suggestive of collusive or oligopolistic behaviour or behaviour exploitive of vertical integration.

Caltex seeks to justify the use of the Singapore Price as follows:

> *'It would not be reasonable for an Australian refiner to receive less for its products than an importer would receive for those same products from Singapore. Different prices for local and imported petrol would also raise the question of who would be willing (or forced) to purchase the higher-priced petrol and who would receive the cheaper petrol.'*

This apparent justification raises several serious issues for competition policy and enforcement:

- Why has what is 'reasonable' for a producer to receive got anything to do with a price determined by market forces [for example, a few years ago Australian orange growers would have loved to have received what they thought was 'reasonable' for their oranges but had to suffer the effect of lower prices for imported product]?;
- As for the proposition about possible differentials between prices for imported product and domestically produced product, this is quite normal across a whole range of goods and services where, rightly, the market determines the result through consumer behaviour and preferences – I can see no good reason that with unleaded petrol we should allow the refiners to arrogate this decision to themselves;
- This reasoning by Caltex gives rise, in my submission, to an inference that the refiners are colluding among themselves to procure the stated outcomes – if the market were operating freely, the suppliers could not confidently assert [as Caltex does] that these outcomes follow from their individually determined pricing practices.

It is, I submit, useful in determining whether the Australian Refinery Prices are appropriate to look at the pricing of Australian indigenous crude, more particularly if it be true that some 80% to 85% of unleaded petrol sold in Australia is produced from indigenous crude:

- There are obviously various costs of production, including the need for a return on capital invested etc, to bring the crude to the well-head;
- At that point, a royalty is imposed by the relevant governmental authorities [the term used is often 'the Designated Authority']. Generally, this is 10% of the value at the well-head as agreed between the Designated Authority and the producer. My understanding is that the value at the well-head for this purpose is usually agreed between the Designated Authority and the producer by reference to a relevant international benchmark price. There can, I believe, be little objection to this *as a basis for fixing the royalty* [the alternative would probably be a 'production cost plus margin' mechanism that would be un-responsive to market forces and could, therefore, lead to un-economic values].
- However, as far as I can ascertain, there is no further regulatory intervention in the setting of crude prices to the Australian refineries. I am unaware of the prices at which indigenous crude is transferred from the producers to the

refineries. In my submission, the Inquiry should seek to identify, clearly and transparently, the pricing mechanism in use between the producers and the refineries. [I can see that an import parity price could legitimately be used as one component of the transfer price at this point – a refiner at arms length would not be prepared to pay more than that for which it could import its feedstock; nor would a producer at arms length be prepared to sell its production for less than it could sell its production on the international market. The most obvious international benchmark price would, it seems to me, be the Malaysian Tapis price].

Although it is true that the cost to the refineries of their feedstock is only one component of their prices, the Australian Institute of Petroleum agrees that 'the cost of crude oil is the major input cost for refiners'. Thus, a clear understanding of the basis of the cost of such an important input is needed to form a view on the appropriateness of the pricing of their output. This is very much the more so in an industry as vertically integrated as the Australian petroleum industry, in which owners participate at various levels, from [in at least one case] basic production of crude; to refining; to wholesale supply; and, in various ways, to retail distribution. A small number of participants clearly have direct impacts on prices at various levels.

As a supplementary, though related, submission, I suggest that the Inquiry set out its findings on the way in which Australian unleaded petrol prices are determined, from beginning to end, as clearly, transparently and simply as possible:

- There is much frustration, confusion and cynicism among many Australian consumers about the pricing of unleaded petrol in Australia.
- My attempts to research the pricing mechanisms have confirmed how little transparency and rationality seems to exist. For example, even seemingly informed commentators seem quite confused about the relevance of the Singapore Price;
- Even the impact of governmental imposts is not completely transparent [although the impact of the excise duty and the GST is clear enough, the impact of the well-head royalty is not];
- It is not sufficient to be told that Australian retail prices for unleaded petrol are relatively cheap compared with those prevailing in selected foreign countries [even if that be true, some people, though not including me, might argue that the price should be driven higher, to constrain use for environmental reasons, by higher taxes but not by monopoly or oligopolistic profits to the oil industry];
- It is, I believe, also important for the Inquiry to make findings specifically in relation to the pricing of *unleaded petrol* as a separate category of refined petroleum product [the analysis for other petroleum products may well be quite different, not the least because it may be that indigenous crude is not suitable for the production of other types]. The statements by the oil companies seem deliberately to lump all their main products together when explaining unleaded petrol prices.