



Mr Gennady Kleiner
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Dear Gennady

We refer to your email correspondence dated 1 September 2020 seeking additional information from AIP to assist the ACCC in making a final determination in relation to the application for Authorisation (AA1000488). This further information request follows our meeting with you on the same date, where we discussed and elaborated on AIP's detailed response on 24 August 2020 to the ACCC's previous information request of 18 August.

In particular, you have sought additional information on supply disruptions related to a confluence of different factors and impacts, and the necessity for urgent industry response to manage such situations.

Our correspondence of 24 August emphasised that persistent operational and financial pressures impacting on the industry and supply operations, alongside the ongoing uncertainty surrounding the further impacts and recovery path of the pandemic, was creating a high potential for supply issues to emerge at short notice (which the Authorisation and the SRC are directly designed to address if beyond the ability of individual market operators to resolve on their own commercial basis).

As discussed at our meeting, the current operational environment for the industry is unprecedented. This is not just the persistent demand destruction and volatility across markets related to changes in border and movement restrictions. It also includes impacts on normal supply and freight logistics and timetables, including from border regulations for trucking operations, biosecurity/quarantine requirements and enforced delays for shipping cargoes, and also hygiene and distancing requirements by authorities across all industry operations and facilities. Also, the ability to promptly redirect and discharge shipping cargoes to where they are needed most (due to unforeseen circumstances, such as a supply disruption) continues to be constrained by the ongoing requirement for applications to the Government to vary Temporary Licences (TL) under Commonwealth coastal shipping legislation. AIP's authorisation application in April was made against this expected background.

At the early stages of the pandemic, strategies and actions were taken by individual market operators to manage these impacts and to match supply scheduling and planning with local demand at greatly reduced rates. For local refineries, these actions included slowing refinery production rates, changing refinery cut-points and crude diets, bringing forward scheduled refinery maintenance, slowing import schedules and retail resupply, and seeking a fuel quality waiver from the Government to assist with the management of excess jet fuel inventories. These strategies by individual market operators took some weeks to organise and implement but, notwithstanding the major financial and business impacts of these strategies, the timing pressure was not acute to ensure ongoing reliable supply to the market, because of the collapse in demand and excess inventory available to service consumers and the market. These strategies continue to be part of market operations right now, to deal with the current (lower) levels of demand.

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However, these strategies and supply planning will need to be unwound or reversed to meet rapidly escalating fuel demand and spikes at short notice with restrictions being eased, creating a new (potentially higher) level of risk for supply reliability to the market compared to the onset of the pandemic which presented different supply management challenges and impacts.

It will take some weeks for the complex readjustment of supply chain operations to much higher and unstable levels of demand across local markets, which will all recover differently. Supply can only adjust according to established production, ordering and shipping timeframes (which involve weeks), whereas demand requirements are typically for prompt delivery. The profile of fuel demand recovery is a major industry uncertainty now and is directly linked to government decisions on lifting border restrictions. For example, it will take some weeks for the jet fuel supply chain to readjust, because of minimal travel demand for such a long period and the uncertainty of how consumers and businesses will respond to greater movement ability and flight scheduling capacity.

In this uncertain environment and transition, a major new supply disruption event or confluence of events (as they have occurred in the past) could be expected to present a greater challenge for individual market operators to manage themselves and a higher risk of supply disruption, notwithstanding the planning and operator experience in dealing with such disruptions in a more normal operating environment.

As discussed at our recent meeting, an unexpected and immediate disruption to local refinery supply is one of the more challenging events for industry to manage in a COVID-19 environment. This is because the disruption is very close to customers, which provides less time for industry to respond and organise supply from alternative locations and suppliers before the impact is felt in the market. In addition, refineries are typically the primary or major supplier to multiple wholesalers (and their customers in turn) in that region, meaning a refinery outage typically and quickly becomes a more broadly based problem for many suppliers and customers. This is not just the suppliers and customers located with the refinery, but other regions and jurisdictions the refinery supplies. Also, as you are aware, some Australian refineries are either coming out of, or entering, periods of major refinery maintenance placing a greater reliance currently on imported fuel supply from various sources.

We discussed an example of this risk at our recent meeting, being the events in late 2012 when the two Victorian refineries experienced outages over a three week period, including as a result of electricity supply disruptions. As acknowledged in government reports, the market impact of these outages was exacerbated because each refinery assumed that the other was operational and would be able to cover the shortage in production from their own facility. The situation was further compounded at the time by diesel demand spikes and resulting low inventories in South Australia (from record harvest activity) and diesel supply disruptions in Sydney. The confluence of these events resulted in parts of Victoria experiencing shortages and some retail sites running out of diesel. That is, individual market operators did not have an understanding of the breadth of the supply problem, including the impacts on alternative and proximity supply sources (in SA and NSW) to help manage the Victorian supply shortfall in a timely way.

As the management of reliable fuel supply is the industry's core commercial business, there is constant monitoring and review by fuel suppliers of supply chains, customer demand, commercial stockholdings and bulk fuel transfers/shipping in every location. As a result, a disruption event which impacts or is likely to impact the supply reliability will trigger an orthodox organisational management approach to managing risk. The typical process involves the standing-up of a situation management team, establishing the size and duration of the supply disruption and the market impacts, assessment of resupply options and timeframes, and then the operational and commercial execution of agreed measures.

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Depending on the nature of the supply disruption/s and the likelihood of customer impacts, any process to address these disruptions would typically need to be determined and executed urgently within 24 hours in order to allow for the additional time required to secure and deliver replacement bulk fuel supplies to meet the supply shortfalls. For example, the delivery timeframe is usually days for shipping cargo redirections to new locations or by delivery by increased trucking operations or new pipeline transfers, and weeks in the case of ordering new supply from alternative suppliers across the Asian region. Failure to do so creates risks such as potential shortages in supply for consumers, as occurred in Victoria in 2012 (described above).

As highlighted in our previous correspondence, given the major ongoing uncertainties, challenges and risks relating to COVID-19 impacts and the recovery profile, as well as future refinery operations in Australia, the participating entities remain of the view that there is a need for the Proposed Conduct to be authorised and as defined in the Draft Determination. If these challenges are beyond the capability of individual operators to manage, then the Authorisation can be relied upon to address any issues, as it was designed to do on short notice and in an expedient manner.

We confirm this correspondence is non-confidential and can be included on the ACCC's public register.

Yours faithfully

A large grey rectangular box redacting the signature of Paul Barrett.

Paul Barrett
CEO

2 September 2020