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Grain Express

CBH Grain Supply Chain Solution

Notification under *Trade Practices Act 1974* (Cth) section 93

11 June 2008

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1 Executive summary

- 1.1 This document provides information and analysis in support of a notification by Cooperative Bulk Handling Limited (**CBH**) of conduct it proposes in relation to the logistics of the grain Supply Chain in Western Australia (**Supply Chain**).

Notification

- 1.2 By the enclosing Form G, and pursuant to section 93(1) of the *Trade Practices Act 1974* (Cth) (**TPA**), CBH notifies its proposed conduct referred to in Form G and this document (**Notification**).

Characterisation of the conduct

- 1.3 CBH considers that the correct characterisation of the Grain Express conduct is that it is “full line forcing” that falls within section 47(2) of the TPA.
- 1.4 In substance, CBH will offer to supply storage and handling services on the condition that Growers or Marketers acquire:
- (i) Supply Chain coordination services from CBH¹; and
 - (ii) to the extent that grain remains in CBH's custody, that they acquire transport services from CBH (through its nominated carrier).

Inefficiency in the current grain Supply Chain

- 1.5 Appendix 1 to this document is the expert report of Synergies Economic Consulting. Having reviewed the functioning of the Supply Chain, Synergies points to two key factors driving inefficiencies in the Supply Chain, including:
- (i) information and coordination problems; and
 - (ii) misalignment of incentives between grain producers (**Growers**) and marketers, traders and other acquirers of grain (**Marketers**);
- 1.6 The current Supply Chain fails to align control of grain movements with information in a complex coordination task. CBH is the only Supply Chain participant in possession of accurate information concerning all grain in the Supply Chain, yet Marketers, which have access to information concerning only their own grain, exert substantial influence over the movement of grain from country to port.
- 1.7 This proposal does not intend in any way to blame Marketers for their conduct or to criticise the pending changes in the wheat marketing legislation. The situation dealt with by this proposal largely arises as a result of the nature of the product – the grain that is grown and delivered into the bulk handling system. CBH recognises that Marketers generally try to align their accumulations with the bulk system, but understands that they are often unable to do so. This is because Growers are not aware of the quality or quantity of

¹ Coordination services will be supplied at no charge.

their grain until very close to, or during, harvesting. As a result, Marketers are unaware which Growers are likely to deliver or contract with them. This is the primary reason that small parcels of grain are often distributed throughout the grain network. The impact of relatively small parcels of grain ownership thinly spread over all four port zones in the Western Australian wheat belt ensures that both rail and road based export distribution will be difficult to execute and increasingly expensive. A new coordinated logistics model such as Grain Express is essential to complement increasing competition in the marketing of grain in Western Australia. This is the basis of the proposal.

- 1.8 The tasks of storage, handling and transport require a high degree of cooperation between the handler (CBH) and transport providers. The current Supply Chain structure adds unnecessary complexity by inserting Marketers into the grain movement decision-making process.
- 1.9 The current structure does not use rail and road infrastructure efficiently. An efficient, coordinated Supply Chain requires a “whole of supply chain” approach. The current Supply Chain is characterised by inefficient outcomes, such as leakage of the rail grain task to road, which erodes the viability of the more efficient rail network and causes substantial negative economic, social and environmental effects.
- 1.10 As the contractual and financial structure of the Supply Chain stands, the interests of Growers and Marketers are often misaligned. AWB Services Pty Ltd (**AWBS**), for example, provides its logistics services to AWB (International) Limited (**AWBI**) in a non-contestable environment and is able to deduct transport and other Supply Chain costs from pool returns to Growers.

Consequence of inaction

- 1.11 With the likely increase in the number of export wheat Marketers in the next year, central and efficient coordination of the grain supply chain is urgently required.
- 1.12 The consequences of inaction will be serious, and possibly permanent. Immediate consequences of retaining the status quo for the coming harvest will include not only a continuation of the current inefficiencies but a substantial escalation in them as CBH and ARG struggle to deal with the competing and conflicting demands of multiple large scale Marketers and Growers.
- 1.13 The industry rail freight agreement will expire in October 2008, having already been extended by one year from its original expiry in 2007. As the March 2008 report of the Grain Infrastructure Group (**2008 GIG Report**) states, the rail network is barely viable and leakage of the grain task to road further deteriorates the relative competitiveness of the rail network. Once closed, rail lines are rarely recommissioned. The 2008 GIG Report concludes:

“With the deregulation of grain marketing resulting in fragmentation of the supply chain tasks and without significant urgent actions inevitable closure of the entire 2300 kilometre grain branch line network will result.”

CBH's proposed solution – Grain Express

- 1.14 CBH has examined a full spectrum of alternative means of addressing the issues identified above, with the ultimate aim of improving the efficiency of the Supply Chain.
- 1.15 CBH has determined that the only viable means of improving the current Supply Chain is for CBH to assume control of the coordination of the Supply Chain. Arguably, CBH already has this contractual and statutory right. However, Marketers may purport to control the movement of specific grain parcels as a party to contracts with transport carriers. CBH submits that the only practical means of resolving this uncertainty in the coordination function is to supply a bundled package of storage, handling, transport and logistics/coordination services.
- 1.16 Because CBH is a Grower cooperative, its primary incentive is to act in the interests of grain producers. This encourages CBH to reduce costs across the entire Supply Chain, whilst also ensuring the sustainability of the transportation network that supports the industry.
- 1.17 Supply Chain coordination is best achieved by a single entity, because each grain movement decision impacts other movements and no one Grower or Marketer has access to “whole of Supply Chain” information, nor do they have sufficient incentive to maximise efficiency for all participants. Central control is the only means of efficiently deploying resources to move a large volume of grain through a system with limited capacity. CBH is the only entity:
- (i) in possession of the complete array of information required to perform this task; and
 - (ii) with the ability to implement a solution without a detrimental effect on grain markets.
- 1.18 Effective planning for the entire supply chain is also difficult for any Marketer because Marketers have limited, if any, advance notice of which Growers will contract to deliver grain for that Marketer's entitlement. By contrast, CBH is the grower interface and, of necessity, plans for the entire grain task in order to provide an effective service to Growers. CBH has the most immediate and direct contact with Growers in an operational sense, and is the best positioned entity to flexibly respond to the needs of Growers. Grain Express provides both CBH and Growers with the operational flexibility to respond to dynamic circumstances during the harvest.
- 1.19 Until recently, AWB, as the operator of the wheat Single Desk, held an understandable view that it should exert direct influence on supply chain logistics. For this reason, AWB did not view CBH's attempted solutions favourably and opposed their introduction. With proposed changes to export wheat marketing, unless the current structure is changed, CBH faces the prospect of multiple large export Marketers seeking to influence the movement of grain between silo and port. The existing model, in which Marketers acquire freight services directly and assert influence on grain movements, is not sustainable in such an environment.

Relevant markets

- 1.20 This document provides information in relation to a range of markets for the supply and acquisition of goods and services. As the Australian Competition and Consumer Commission (**ACCC**) has previously noted, in some cases it is not essential to define relevant markets with precision. CBH submits that this is such a case, because the effect of the relevant conduct on relevant markets and the claimed public benefits do not materially differ with the possible alternative market definitions. CBH's conduct will have effect throughout Western Australia and the most relevant services to be considered in this notification (storage and handling) are equally affected in each of the port zones and in all places in which services are supplied (Receival Points, Destination Sites and Port Facilities). The claimed public benefits are similarly derived and distributed across the entire grain Supply Chain in Western Australia.
- 1.21 To the extent that this submission addresses competition effects, it does so in terms of:
- (i) markets for the supply of country grain receival, storage and handling services in Western Australia, or alternatively, in each of the four port zones in Western Australia;
 - (ii) markets for the supply of bulk grain road haulage services in Western Australia, or alternatively, in each of the four port zones in Western Australia;
 - (iii) markets for the supply of bulk grain rail haulage services in Western Australia, or alternatively, in each of the four port zones in Western Australia; and
 - (iv) grain trading markets, which may include:
 - (A) a market in Western Australia for the acquisition and supply of wheat; and
 - (B) the market in Western Australia for the acquisition and supply of coarse grains.

As the ACCC noted in its determination in the Export Grain Logistics Authorisation², these markets may have international and domestic components.

Public benefits

- 1.22 The primary public benefits produced by the proposal concern the increased efficiency of the Supply Chain. These efficiencies are likely to have a direct and beneficial impact on Australia's exports³.

² C2004/1418.

³ *Trade Practices Act 1974* (Cth) section 90(9A) requires the ACCC to regard a significant increase in the real value of exports as a benefit to the public.

- 1.23 A range of other benefits flow from the proposed conduct, including:
- (i) more efficient grain delivery and handling at Receival Points, including:
 - (A) increased speed of receival, leading to deferred capital expenditure and more efficient investment;
 - (B) better information on marketing options and more time to decide on those options for growers;
 - (C) reduced errors in nomination of marketing options by growers; and
 - (D) increased automation of the receival process;
 - (ii) better coordination of storage and handling, including:
 - (A) reduced opening of bulkhead storages;
 - (B) better use of labour force (less mobilisations, reduced overtime and better rostering);
 - (C) reduced loss by division; and
 - (D) reduced risk of phosphine resistance;
 - (iii) improved efficiency of transport task, including:
 - (A) enhanced rail efficiency, with increased use of unit trains;
 - (B) below rail cost savings through better utilisation, such as possible deferred capital expenditure;
 - (C) certainty of volume on rail;
 - (D) insurance risk sharing;
 - (E) simplified operational interface between carrier and CBH;
 - (F) better negotiation capacity;
 - (G) greater transparency of costs to Growers; and
 - (H) a real likelihood of preserving the viability of the rail network;
 - (iv) enhanced port efficiency, including:
 - (A) better utilisation of infrastructure; and
 - (B) reduced demurrage;
 - (v) dynamic efficiency gains, which improve the prospect of efficient investment in infrastructure in future; and
 - (vi) better marketing decisions for Growers and Marketers.
- 1.24 Of these efficiencies, there are several that have self-evident credibility. For example, if Marketers continue to arrange their own rail haulage, they will not be in a position to optimise efficiency with unit trains because each Marketer will

have only a fraction of the total task⁴. By contrast, under Grain Express CBH will be able to aggregate volume into larger single grain/grade movements.

- 1.25 These benefits are referred to in Part 5 of the Synergies Report, and the sources and primary evidence also stated in that report. All of these benefits are achievable without sacrificing the substantial value captured by the effective use of information, such as quality information, to market grain. As is detailed later in this document, Grain Express includes a comprehensive improvement in the management of grain quality information.

Effects on competition

- 1.26 As a cooperative whose fees represent direct costs for its members, not only does CBH have no incentive to derive monopoly rents in storage and handling, it will undertake not to add any additional fee or margin in relation to its provision of transport and logistics services under Grain Express. CBH's interests are directly aligned with Growers. In addition, current Growers comprise 9 out of 12 directors on the CBH Board.
- 1.27 Grain Express conduct does not prevent Marketers from outturning their grain from CBH's custody, though it does require that Marketers only outturn grain from one of a certain number of larger sites, called Destination Points. In essence, Grain Express provides that, while grain is in CBH's custody, its movement will be arranged and coordinated by CBH.
- 1.28 Therefore, CBH does not consider that the Grain Express conduct will prevent or deter new entrants from building competitive storage or port loading facilities.
- 1.29 CBH submits that Grain Express will have a net positive effect on competition in freight markets, because central control of the freight task will maximise competitive tension between road and rail and may also facilitate competitive entry in rail.
- 1.30 In Marketing, the types of concerns that might arise from notified conduct may include:
- (i) the potential for CBH to discriminate against the marketing competitors of Grain Pool Pty Ltd (**GPPL**) (for example, by delivering unreasonably preferential terms and conditions for GPPL); and
 - (ii) the potential for CBH to disclose confidential information to GPPL.
- 1.31 These potential concerns may be effectively dealt with using appropriate information flow and arm's length dealing structures to address decision-making, implement non-discriminatory terms and conditions for all users of the system and ensure that information flows are appropriately controlled. These issues are the subject of the measures detailed in Appendix 2. To summarise those measures, CBH will have in place:

⁴ See 2.3.4 of the Synergies Report

- (i) an information flow policy, which restricts the flow of confidential information between CBH and its related marketing entities, GPPL and AgraCorp Pty Ltd;
- (ii) standard terms and conditions of supply for storage and handling services;
- (iii) a policy of access to CBH's services on non-discriminatory terms and conditions to all Marketers.

Conclusion

- 1.32 This submission describes the current Supply Chain, identifies its challenges and the inefficiencies inherent in its current structure. It is clear from the information set out in this document that urgent action is required.
- 1.33 Grain Express is the only workable proposal capable of being introduced before the next harvest. The case for its implementation is compelling.

2 Industry background

Overview

- 2.1 The Western Australian Supply Chain for export grain comprises the following functions:
- (i) **production** – Growers produce grain on medium and large scale farms in the Western Australian grain belt;
 - (ii) **transport from farm gate to silo** – Growers arrange for road transport between the farm gate and country storage and handling facilities (**Receival Points**);
 - (iii) **sale/acquisition of grain to Marketer** – Growers choose from a range of options in selling their grain. Marketers acquire grain at the Receival Point;
 - (iv) **trading and accumulation** – grain, like most other commodities, is traded and accumulated in a secondary market, as traders seek to derive value or manage risk by acquiring, accumulating and trading grain;
 - (v) **country storage and handling** – grain is unloaded at Receival Points, sampled, analysed, weighed, graded, stored and fumigated then loaded for transport;
 - (vi) **bulk freight**– Marketers and CBH contract with rail and road providers to transport grain from the Receival Point to the port, the container loading facilities (such as those at the Metro Grain Centre (**MGC**)) or the domestic market, as instructed by Marketers;
 - (vii) **port storage and handling** – bulk grain is stored for export at four major port terminals in Western Australia (Kwinana, Geraldton, Albany and Esperance);
 - (viii) **container loading & handling** – grain may be loaded into containers for export or shipment to domestic suppliers;
 - (ix) **export marketing** – Marketers contract with overseas grain buyers and arrange for shipping of bulk or container grain to the required foreign ports. For wheat, AWBI (as the current statutory monopoly bulk wheat Marketer) supplies bulk wheat to export markets and may arrange shipping to do so. For barley, canola and lupins, GPPL (as the current statutory main export licence holder) supplies to export markets and may arrange shipping to do so. Other bulk exporters compete with GPPL through the granting of special export licences from the Grains Licensing Authority (a Western Australian statutory body).
- 2.2 The Western Australian grain belt is roughly divided into four distinct zones, each served by a port.

- (i) The **Geraldton zone** comprises the area surrounding the Geraldton port and includes the regional centres of Mingenew, Mullewa and Morawa.
- (ii) The **Kwinana zone** comprises the largest area of the Western Australian grain belt, stretching from Kwinana in the west to Southern Cross in the east, and from Narrogin in the south to Wubin in the north. It is served by the Kwinana port to the south of Perth.
- (iii) The **Albany zone** covers the south-west corner of Western Australia from Hyden and Newdegate in the north-east, to Albany in the south and Bunbury in the west. This zone takes in the regional centres of Katanning, Lake Grace and Albany.
- (iv) The **Esperance zone** comprises the south-east grain belt, the area north of Esperance and surrounding Salmon Gums.

2.3 **Figure 2.1** below is a map of the Western Australian grain belt, showing the four port zones and the location of relevant infrastructure.

Figure 2.1 - Western Australian grain belt zones



- 2.4 The grain Supply Chain is largely geared toward grain exports, and the structure of storage and handling, transport and marketing arrangements reflects this.
- 2.5 Under the current arrangements, the flow of information, instructions and documents is complex, and varies according to the type of grain, and the identity and approach of Marketers.

CBH

- 2.6 CBH was incorporated on 4 April 1933 and is governed by the *Companies (Co-operative) Act 1943* (WA) (**Cooperative Act**).

[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]

- 2.7 CBH owns storage and handling infrastructure serving the four port zones of the grain belt in Western Australia. This infrastructure includes;
- (i) sampling equipment, analysing technologies, fumigation and aeration infrastructure;
 - (ii) weighbridge, road or rail loading/unloading and storage facilities in country locations;
 - (iii) the MGC, a large intermodal terminal, storage facility and container packing facility; and
 - (iv) road or rail unloading facilities, storage facilities and ship loading facilities in Esperance, Albany, Kwinana and Geraldton.
- 2.8 CBH receives grain from Growers at the country storage site. At this point, the Marketer acquires title in the grain from the Grower, and CBH takes physical possession of the grain.
- 2.9 CBH supplies a range of related services to Growers and Marketers, including:
- (i) receival services, which include:
 - (A) planning harvest receivals, including segregation and service availability based on Grower information and retained knowledge;
 - (B) sampling / testing grain proffered for delivery;
 - (C) unloading grain from Grower-arranged road transport;
 - (D) weighing grain received;
 - (E) testing grain quality and attributes; and
 - (F) collecting and providing information concerning the source, weight, quality, attributes, treatment and type/grade of grain;
 - (ii) storage services:
 - (A) determining segregation availability;
 - (B) fumigating grain and general grain husbandry;

- (C) tarping grain stacks (as required);
 - (D) maintaining and updating ownership records; and
 - (E) providing information to Marketers and financiers about grain receivals;
- (iii) handling services, which include:
 - (A) loading stored grain onto road or rail transport arranged by Marketers and/or CBH;
 - (B) unloading grain at next CBH destination (if any);
 - (C) blending grain parcels to provide required grain quality;
 - (D) loading grain into containers or bags;
 - (E) loading grain onto export vessels; and
 - (F) acting as shipping agent of various exporters.
- 2.10 CBH has approximately 5,150 shareholders that are Growers of grain in the Western Australian grain belt.
- 2.11 CBH has 12 directors. CBH's Articles of Association provide that CBH can have a maximum of 12 directors appointed as follows:
 - (i) 9 directors who are shareholders (or representatives of shareholders) (**Grower Directors**) (article 84); and
 - (ii) 3 directors who are appointed by the Grower Directors (article 85).
- 2.12 Under article 5 of CBH's Articles of Association, each shareholder of CBH can only hold a maximum of 5 CBH shares.
- 2.13 Article 110 of CBH's Articles of Association prevents CBH from distributing any income or profit of CBH to its shareholders. Article 111 of CBH's Articles of Association provides that "all income and property of the Company shall be applied towards the objects of the Company as set out in the Memorandum of Association and not otherwise".
- 2.14 Article 114 of CBH's Articles of Association provides that any surplus assets of CBH after the payment of its debts and liabilities and the costs of winding up are not to be distributed to shareholders.
- 2.15 CBH's objectives are contained in Article 2(a) – (ee) of its Memorandum. Its main objectives are contained in Articles 2(a), (b) and (f) which are:
 - "(a) *To establish maintain and conduct any schemes or systems for handling of wheat and/or other grain in bulk or otherwise.*
 - (b) *To receive handle transport grade classify and store wheat and/or other grain...*
 - (f) *To carry on either in conjunction with or separately from the business authorise to be carried on by the preceding paragraphs or any of them all or any businesses or business which in the opinion of the Directors*

may be conveniently carried on by the Company or promote assist be incidental or conducive to the attainment of its objects or any of them.”

2.16 In addition to its obligations under the Memorandum, the Articles of Association and the Cooperative Act, CBH has a number of obligations under the *Bulk Handling Act 1967 (WA)* (**Bulk Handling Act**) and Bulk Handling Act Regulations 1967 (WA) (**Bulk Handling Regulations**). These obligations are summarised below:

- (i) CBH must receive all grain tendered to it that meets the requisite standards: Bulk Handling Act, section 42, and Bulk Handling Regulations, regulation 13;
- (ii) CBH must determine the grade of the grain tendered to it and inform the person tendering the grain of CBH's determination: Bulk Handling Act, sections 6A and 43(2);
- (iii) On receipt of the grain tendered to it, CBH must cause the grain to be weighed and issue a weighbridge ticket for the grain to the person tendering the grain: Bulk Handling Act, section 36(1);
- (iv) CBH must issue a warrant for the grain tendered to it: Bulk Handling Act, section 37(1);
- (v) CBH must deliver the grain to the receipt point or port in the State as required by the person who is entitled to the grain under the warrant: Bulk Handling Regulations, regulation 20;
- (vi) The holder of the warrant issued under Bulk Handling Act section 37(1) must take delivery of the grain by 30 September next following the receipt of the grain by CBH: Bulk Handling Act, section 45(1);
- (vii) If the holder of the warrant issued under Bulk Handling Act section 37(1) does not take delivery of the grain by 30 September next, CBH can sell the grain, deduct its costs from the funds realised from the sale and pay the net proceeds from the sale to the warrant holder: Bulk Handling Act, section 45(2), and Bulk Handling Regulations, regulation 26;
- (viii) CBH must insure all grain in its custody or under its control: Bulk Handling Act, section 11.

2.17 Sections 35A(b), (c) and (d) of the Bulk Handling Act place restrictions on the manner in which CBH can use its income or property. In this regard, these sections provide:

- “(b) all income and property of the Company [that is, CBH] shall be applied, subject to this Act, towards the objects of the Company as set out in clause 2 of its memorandum of association and not otherwise.*
- (c) the directors of the Company may set aside out of the profits of the Company such sums as they think fit as reserves for application, in the discretion of those directors, in meeting contingencies or in achieving any other purpose that is, under the memorandum or*

articles of association of the Company but subject to this Act, a proper purpose for the application of profits of the Company;

- (d) *where any reserves set aside pursuant to paragraph (c) are not immediately required for application in accordance with that paragraph, they may, in the discretion of the directors of the Company, be applied in the business of the Company or in furthering, subject to this Act, the objects of the Company as set out in clause 2 of its memorandum of association, paying off or reducing some or all of its debentures for the time being outstanding, or liquidating any other indebtedness of the Company or they may be invested in such investments as those directors think fit”.*

Grain production

- 2.18 Western Australian grain Growers produce:
- (i) wheat;
 - (ii) barley;
 - (iii) coarse grains (sorghum, oats, maize and triticale);
 - (iv) oilseeds (canola and soy); and
 - (v) pulses (lupins, field peas and chick peas).
- 2.19 In Western Australia, the majority of grain is produced in the south western grain belt, which runs in a broad band just north of Geraldton to just east of Esperance.
- 2.20 Western Australia produces approximately 10.68 million tonnes of grain per year. The Western Australian grain belt produces a little over a third of Australia's grain crop. Western Australia's grain production is geared primarily for export, with approximately 90% of Western Australia's production destined for overseas markets.
- 2.21 Like many other agribusinesses, grain production is subject to a seasonal production cycle and substantial variation in yields resulting from variable climatic conditions. Grain production more than doubled from 2002 to 2003 and national average yields have ranged from 1.14 to 2.14 tonnes per hectare over the last decade⁵.
- 2.22 Approximately 70% of the total value of grain production is accounted for by wheat production, which averages about AUD\$4 billion per annum over five years. Australia accounts for between 8% and 15% of world trade in wheat and barley, making it one of the four largest exporters of grain in the world⁶.

⁵ AWB Ltd, *Grain Production* (2006) <www.awb.com.au/aboutawb/communityeducation/grainproduction> at 1 May 2008.

⁶ Ibid.

- 2.23 Western Australian grain production has been generally buoyant between 1960 and 2000. From 2000/01 to 2005/06, production has been characterised by significant seasonal variability, including two major droughts in 2000/01 and 2006/07⁷ and significant variability in 2007/08. Western Australian grain production is conducted in an area under crop of approximately 7 million hectares⁸. Wheat is the predominant grain, accounting for 10.1 million tonnes of the total grain crop of 15.3 million tonnes in 2003.
- 2.24 The Australian grain industry has grown in efficiency and productivity, with grain yields on average rising by about 1.65% per year over the past twenty years⁹.
- 2.25 Important information exchanges occur at the production stage, which influence the rest of the grain Supply Chain. Growers delivering to storage facilities are required by the Bulk Handling Regulations to provide crop estimate data before harvest. This information includes the Grower's hectares sown, estimated hectares for delivery for each type of grain and the preferred storage site to which delivery is to be made. Pursuant to section 11(3) of the Bulk Handling Regulations, CBH is not to receive grain from a person until the crop estimate data has been provided.
- 2.26 CBH uses this information to conduct pre-harvest planning for the movement of grain through its facilities, subject to the decision-making power of Marketers. As the description (below) of storage and handling services shows, CBH's management of capacity in its storage and handling system is crucial to Supply Chain management and the costs ultimately borne by Growers.

Grain storage and handling

- 2.27 CBH receives grain from Growers at the country storage site. It has a statutory obligation to do so, subject to quality requirements. Section 42 of the Bulk Handling Act provides:
- “(1) *Subject to subsection (2), [CBH] shall receive all grain that is tendered to it in bulk.*
- (2) *Notwithstanding the provisions of subsection (1), [CBH] –*
- (a) *shall not receive, as and when tendered, any grain that is unsound or that is inferior to the lowest grade then in force, but shall make arrangements to receive the grain at such time or place, or subject to such conditions, as it may require;*

⁷ Western Australia Strategic Grain Infrastructure Study(2005), 16, 17.

⁸ As the Western Australia Strategic Grain Infrastructure Study recognises, there is some inconsistency between Western Australia Agriculture statistics and ABARE statistics.

⁹ AWB Ltd, *Grain Production* (2006) <www.awb.com.au/aboutawb/communityeducation/grainproduction> at 1 May 2008.

- (b) *is not obliged to receive any grain except at a reasonably convenient time and place nominated by it.*"

- 2.28 At the receival point, if the Grower is supplying grain to a Marketer, the Marketer acquires an entitlement to receive grain of the same grade and type as that they have bought from the Grower. CBH takes physical possession of the grain in return for agreeing to provide grain of the same type and grade to the "warrant holder".
- 2.29 The legal status of this relationship is stated in section 18 of the Bulk Handling Act, which provides:
- "(1) *The receival of grain in bulk by the company does not confer on [CBH] any proprietary right or interest in the grain or render the grain liable to seizure or attachment, as against [CBH].*
- (2) *As regards grain, the position of [CBH] at law is that of a custodian for reward.*
- (3) *The proprietary interest in grain is vested in the person who, for the time being, is entitled to obtain it from bulk stocks held by [CBH] or under its control.*"
- 2.30 CBH supplies a range of related services to grain Marketers, including:
- (i) receival services, which include:
- (A) planning harvest receivals including segregation and service availability based on Grower information and retained knowledge;
- (B) sampling / testing grain proffered for delivery;
- (C) unloading grain from Grower-arranged road transport;
- (D) weighing grain received;
- (E) testing grain quality and attributes; and
- (F) collecting and providing information concerning the source, weight, quality, attributes, treatment and type/grade of grain;
- (ii) storage services:
- (A) determining segregation availability;
- (B) fumigating grain and general grain husbandry;
- (C) tarping grain stacks (as required);
- (D) maintaining and updating ownership records; and
- (E) providing information to Marketers and financiers about grain receivals;
- (iii) handling services, which include:
- (A) loading stored grain onto road or rail transport arranged by Marketers and/or CBH;

- (B) unloading grain at next CBH destination (if any);
 - (C) blending grain parcels to provide required grain quality;
 - (D) loading grain into containers or bags;
 - (E) loading grain onto export vessels; and
 - (F) acting as shipping agent of various exporters.
- 2.31 These services are generally supplied under CBH's standard terms and conditions of supply to Marketers. A copy of the current 2007/08 season standard terms and conditions is at **annexure A** to this document.
- 2.32 Efficient storage and handling requires a high degree of integration with other Supply Chain tasks in order to (as far as is practicable):
- (i) promote efficient information flows;
 - (ii) align incentives of Supply Chain participants; and
 - (iii) optimise operational efficiency by finding the most cost-effective route to market, reducing double-handling, demurrage and other avoidable costs; and
 - (iv) to meet quality requirements of Australia's international grain market.
- 2.33 When grain is delivered to CBH, the Grower (or its representative, the trucking company) provides information to CBH concerning the delivered load. A form (called a "Carter's Delivery Form") captures this information. This form provides the following information:
- (i) which Grower, property and season the grain comes from;
 - (ii) grain type and variety;
 - (iii) the date of delivery;
 - (iv) the details of the truck delivering the grain;
 - (v) who the acquirer may be and the form of contract (eg cash, contract or pool). The Grower may choose to warehouse the grain and then outturn grain later by an outturn request or transfer title to another person (by a Load Transfer Form) or sell to the pool or contract; and
 - (vi) a Grower's action plan, if the load results are not as expected (downgraded or undergrade).
- A blank Carter's Delivery Form is at **annexure B** to this document.
- 2.34 CBH then tests the load weight to determine whether each bin of the road transport vehicle meets the legal requirement for delivery, and performs a sample test of the quality of the grain. This testing is performed at the weighbridge and the results are immediately provided to the Grower.
- 2.35 Growers are invoiced directly by CBH for receival services and, if they opt not to supply grain to a particular Marketer or pool, they may also be invoiced for storage or "warehousing fees".

- 2.36 As the recipient and custodian of detailed information in relation to a traded commodity, CBH takes care to ensure appropriate procedures are in place for the storage and dissemination of data collected. CBH stores data electronically in its stock management system, and transmits data to Marketers under Data Transmission Guidelines. These Guidelines designed to ensure security, accuracy, non-discriminatory access and efficient information flow.
- 2.37 Information gathered in relation to every grain delivery in CBH's system enables CBH to provide Marketers with prompt access to detailed information concerning their grain entitlements.
- 2.38 Under CBH's Data Transmission Guidelines, CBH can provide the following information to Marketers (as it is relevant to that Marketer):
- (i) Grower loads;
 - (ii) name and address of each Grower;
 - (iii) movements (including freight) from site to site within the CBH system;
 - (iv) outturns of domestic grain leaving the control of CBH; and
 - (v) stocks held by CBH at a site, type of grain and grade level.
- A copy of CBH's Data Transmission Guidelines is at **annexure C** to this document.
- 2.39 Marketers may then transmit receival marketing options to the system (eg cash, pool, estimated silo return) at each site, as well as the grain grade level for a specified date range. The Grower decides on a marketing option with the benefit of this information. Marketers may transmit grain service requirements to CBH so that CBH can provide service availability (ie what grain types they are willing to buy at each site).
- 2.40 The movement of a particular parcel of grain through CBH's system affects other movements. This is due to the physical constraints upon the system as a whole, which include:
- (i) the need to cater for seasonal variations in crop yield and quality in different regional areas;
 - (ii) the need to offer receival services for multiple grain types grown in the areas surrounding a site (which may vary by season);
 - (iii) the capacity of grain storage infrastructure;
 - (iv) in many cases, the need to aggregate grain from a number of sites to keep these sites operational, and to reduce the loss by division;
 - (v) common storage of grain owned by multiple parties, and loading or handling costs associated with accessing a parcel from common storage;
 - (vi) grain treatment/fumigation requirements;
 - (vii) capacity of loading facilities;

- (viii) limitations of road and rail infrastructure; and
 - (ix) variation and changes in market outturn requests.
- 2.41 Significant operational efficiency issues arise in the coordination of this task. CBH's infrastructure has been built over a long period and is not efficient to replicate. Storage and handling infrastructure has an inherent susceptibility to suffer from localised capacity constraints at particular points in the system. CBH considers that these constraints are capable of being addressed through more efficient capacity utilisation and sensible investment in capacity enhancement.
- 2.42 The biggest user of CBH's storage and handling services is AWBI.

[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]

Storage and handling infrastructure

- 2.43 CBH operates 193 country grain receival points in the Western Australian grain belt. The receival sites vary in size, capacity and capability, from:
- (i) remote, small capacity receival points served by road and narrow gauge rail (satellite and secondary sites); to
 - (ii) larger "primary sites", closer to ports and served by road, dual or standard gauge rail; to
 - (iii) MGC, a unique purpose-built receival point and container loading facility, served by road and rail.
- 2.44 For optimal utilisation of its storage and handling infrastructure, CBH requires the best possible information from:
- (i) Growers, regarding their expected crops – encompassing grain types, varieties and projected yields of each grain in an upcoming harvest;
 - (ii) transporters, regarding their available trucks, trains and rolling stock and accurate scheduling on the availability of this transport capacity; and
 - (iii) Marketers, regarding their projected current, short range and long-range marketing forecasts, coupled with their specific shipping plans and individual vessel nominations.
- 2.45 CBH offers grain receival services for particular grains at particular sites. Not all sites may be geared to receive all grains or grades of grain at all times during the harvest. CBH configures its sites ahead of harvest, using a combination of the crop estimate information provided by Growers, close consultation with Grower elected bin representatives and the information provided by export Marketers (including forward shipping plans). For example, a particular area may be projected to yield predominantly barley and canola at one stage of the harvest, and then yield wheat at a later stage. The site serving that area may therefore be set up to initially receive barley and canola, and then wheat – but that site may not offer a service to receive lupins. Growers in

that area who have harvested lupins will be told in advance the location of the nearest site offering to receive lupins.

- 2.46 Loads are segregated in storage, not only by the type of grain delivered, but by the grade of that grain. For example, grain with a high protein level will be separately stored from grain with a lower protein level. Or, if a Marketer has acquired a particular parcel of high quality “noodle wheat” for export to Japan, that wheat will be stored separately from a parcel of Australian Standard White wheat acquired by a different Marketer.
- 2.47 A truckload of grain, once delivered to storage, is inevitably commingled with other loads of similar grade grain already received into storage. In this way, grain has some similarity to gas or fluids. It is neither efficient, nor possible, for a warrant holder to insist that CBH deliver the same grain to the warrant holder at port as was delivered by the Grower at the country receival point.
- 2.48 The Bulk Handling Act and Bulk Handling Regulations recognise this in two ways:
- (i) a Marketer is not entitled to delivery of the same grain that was delivered to CBH by a Grower. Instead, as section 44 provides, the warrant holder is entitled to “receive an equivalent weight of grain of the type corresponding with, and of a grade at least equal to, that in respect of which the warrant was issued”.
 - (ii) Regulation 20 provides that before 1 March in any year, CBH shall deliver grain to the point nominated by the warrant holder. It also states that CBH “is not obliged to deliver grain from the particular point of receival as shown on the warrant”.
- 2.49 Any requirement for separation creates the inherent potential for lost capacity. This is due to the space required between parcels in horizontal or bulkhead storage, and the lost capacity of silo storage. This lost capacity in CBH’s storage facilities is referred to as “loss by division”. It represents a substantial potential inefficiency (or potentially an inability to cope with the entire harvest) for CBH if its infrastructure is under-utilised due to unnecessary division. As is discussed below in relation to transport, any ability of Marketers to require the movement of particular parcels of grain to occur in an ad-hoc or uncoordinated fashion increases the incidence of capacity waste, particularly in country sites. This cost is ultimately borne by Growers.
- 2.50 **Annexure D** shows the number of commodities and grade segregations that CBH has handled from 1960/61 to 2007/08. CBH presently handles more than 40 different grades of 8 different commodities. Each grade of each commodity requires distinct storage.
- 2.51 **[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]**
- 2.52 Another crucial issue for CBH is the appropriate management of fumigation. To address the risk of insect infestation and damage, CBH treats grain with phosphine. Parcels of grain being stored under fumigant must have the fumigant level maintained for a minimum period of 28 days. Failure to do so

may create a risk of infestation or phosphine resistance. If a parcel under fumigant is required to be opened, and a proportion of the grain outloaded for a particular requirement, a risk arises that a fumigant-resistant strain of insects will evolve. This has actually occurred in the Eastern States of Australia, which has resulted in the use of more toxic and less environmentally stable fumigants such as methyl bromide. Studies on resistant strain development have been conducted by independent bodies, and substantial evidence exists to support the connection between fumigant management and the development of resistant strains of insects¹⁰.

- 2.53 **[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]**
- 2.54 The efficient use of CBH infrastructure is also closely related to the transport links serving each site. In Western Australia, sites are served by any one or more of road, narrow gauge rail and standard gauge rail.
- 2.55 Of the 197 receival sites, 42 are serviced exclusively by road because no rail exists. There are 28 “road to rail” sites, where the Australian Railroad Group (**ARG**) contract road carriers to handle the first leg of the journey to port.
- 2.56 **[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]**
- 2.57 **[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]**
- 2.58 For the export wheat Supply Chain, AWB provides CBH with instructions in relation to the unloading, storage and loading of export grain. CBH implements those instructions with the combined logistical assistance of AWB and the required transport carriers.
- 2.59 A key issue in ensuring improvement in Supply Chain efficiency is the coordination of transport, storage and handling between country sites and port. If the task is run in a less coordinated fashion as a result of increasing fragmentation in the grain marketing market, costs will increase as a function of double-handling, excessive mobilisation (deployment of labour and equipment to sites which are not permanently manned), losses by division, capacity under-utilisation, bottlenecks, idle transport capacity, sub-optimal transport pricing, demurrage costs and foregone dispatch.

Transport silo to port/container loading facilities

- 2.60 As warrant holders of grain in CBH's possession, some Marketers have purported to exercise control of the movement of that grain between country silo and port or container loading facilities.
- 2.61 Grain is moved by road, rail or a combination of the two at the instruction of Marketers or at CBH's behest. Certain Marketers may acquire carriage services from road and rail carriers and then instruct CBH to load and unload grain to and from trucks and trains as required, while other Marketers rely on CBH to contract and perform these functions.

¹⁰ See, for example, Wallbank & Collins, *Recent studies in resistance to grain protectants in Eastern Australia* (2003) Stored Grain Research Laboratory <http://sgrl.csiro.au/aptc2003/12_wallbank&collins.pdf> at 1 May 2008.

- 2.62 Unlike other international grain industries, most growers do not rely on on-farm storage, so the Western Australian storage network offers Growers and Marketers a unique competitive advantage. The network capabilities within the Supply Chain provide the potential to accumulate export cargoes in world-class timeframes.
- 2.63 The movement of grain between country silo and port comprises a substantial proportion of the export grain logistics task. Due to capacity constraints, shipping timetables, rail gauge issues, loading logistics and the grading of grain by quality, the movement of grain between silo and port must be carefully coordinated to maximise efficiency and to ensure that storage capacity required during the harvest period at country receival points can be available for continued access by Growers.
- 2.64 If sites must be closed due to no available capacity, Growers are forced to travel further on road with their grain, paying higher rates for peak period road transport and creating significant costs in maintaining roads and addressing community and safety issues.

Contractual arrangements - Rail

- 2.66 Marketers contract with both road and rail carriers to acquire carriage services. Rail services are acquired under an industry contract between Australia Western Railroad Pty Ltd (**AWR**) (a subsidiary of ARG), AWB, AWBS, GPPL, AgraCorp Pty Ltd, the Pastoralists and Graziers Association of Western Australia Inc (**PGA**), Western Australian Farmers Federation Inc (**WAFF**) and CBH. The current industry contract was due to expire in October 2007 and has been extended by agreement for 12 months.
- 2.67 CBH is a party to this agreement, both as the party responsible for loading and unloading grain, and also because it moves grain in its own right as a grain trader and accumulator. **[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]**

Contractual arrangements – Road to rail

- 2.68 Road to rail movements occur when AWR arranges for grain to be moved by road from a country receival site (designated as a “road to rail” site under the industry freight agreement) to another site where it will be loaded onto rail.
- 2.69 These arrangements are made by ARG with a road carrier (currently Marley’s Transport Pty Ltd), with the road carrier effectively acting as AWR’s sub-contractor. The principal transport arrangement is between the Marketer and ARG under the current industry freight agreement.

Contractual arrangements – Road

- 2.70 For the movement of bulk export grain, there are various road transport services agreements between Marketers and carriers. These agreements are specific to each port zone.
- 2.71 The contracts and parties are as follows:
- (i) **Albany zone** – AWBS, GPPL, CBH and Halls Haulage Pty Ltd (expires 31 October 2008);
 - (ii) **Geraldton zone** – contracted on a spot basis due to persistent drought;
 - (iii) **Kwinana zone** - AWBS, GPPL, CBH and Marley’s Transport Pty Ltd (expires 31 October 2008);
 - (iv) **Esperance zone** – two contracts (both expire 31 October 2010):
 - (A) AWBS, GPPL, CBH and OD Transport (WA) Pty Ltd;
 - (B) AWBS, GPPL, CBH and Daytona Investments Pty Ltd Trustee for the Crane’s Haulage Trust Trading as Cranes Haulage.
- 2.72 **[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]**

CBH Dedicated Fleet

- 2.73 In addition to the agreements between Marketers, CBH and road carriers, CBH has contracted in its own right with Cataby Cascades and Crop Line Haulage.

Under these agreements, Cataby Cascades and Crop Line Haulage supplied a dedicated fleet to CBH for the purpose of moving grain between its smaller country sites and larger primary sites.

- 2.74 The need for these movements arose from a number of factors including supply chain inefficiency, the limited capacity of storage facilities, the variations in crop yields in particular regions from year to year and the need to efficiently move grain through CBH's network in an orderly and efficient manner.
- 2.75 Once grain has been sampled, received, weighed, tested and the relevant information processed, an immediate tension arises in the interests of CBH, as storer and handler, and any bulk grain exporter. CBH's country storage infrastructure has limited capacity at certain points, and due to variations in harvest yields and carry-over, may experience bottlenecks in some areas of its network at peak demand times during harvest. For this reason, CBH may determine that it is efficient for grain to be transported away from these sites to storage facilities closer to port in order to free up capacity. CBH, as a Grower cooperative, does not wish to fill and close country sites, which would cause Growers to incur:
- (i) additional delays in getting their crop off the farm and into CBH storage where it is insured against weather damage; and
 - (ii) additional expense in transporting their grain further at high cost.
- 2.76 Cost of running dedicated fleet has been partially absorbed by CBH, and partially absorbed by Marketers. Because CBH acquires its dedicated fleet service on a year-round basis, and acquires at greater scale than Growers, it achieves lower freight rates from carriers.
- 2.77 An exporter's interests favour leaving grain stored in country sites and thereby delaying the payment of transport fees to CBH and carriers until absolutely necessary. As a result, exporters may oppose movements of grain toward primary sites unless those movements are for the purpose of loading a specific vessel.

Instructions and information flows

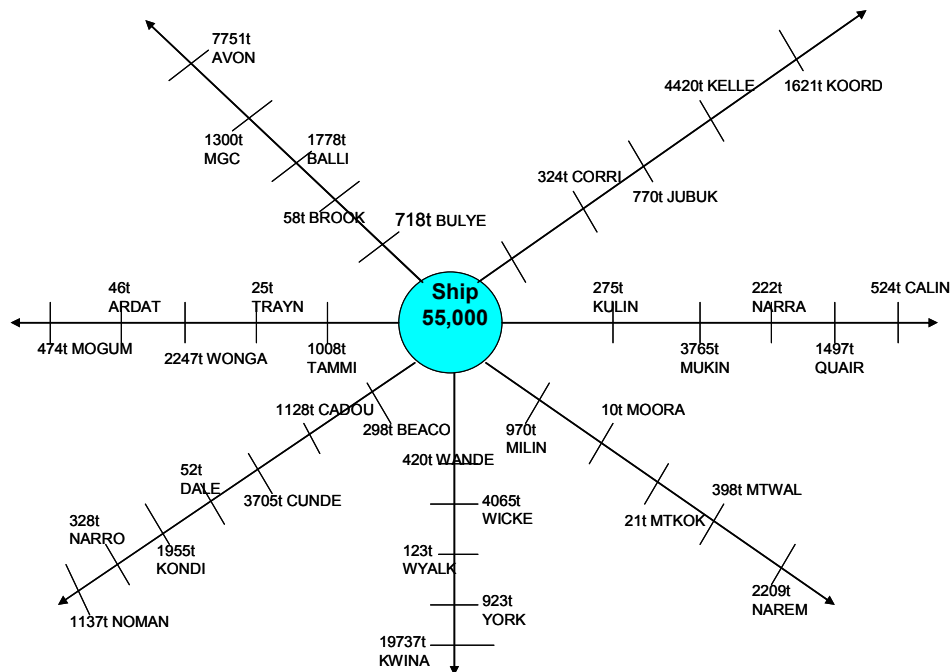
- 2.78 Marketers initiate the movement of grain to port by instructing CBH as to the storage and loading of grain onto road or rail transport for carriage to port.
- 2.79 In the case of bulk export grain, these instructions begin with the Marketer providing a 12-month forward shipping program, which estimates the likely requirements of that Marketer for the coming year. This document assists CBH to plan for the movement of grain through its system, but it is not accurate enough to be relied upon in detail.
- 2.80 The first specific step in the process of moving grain to port for a specific vessel is when the Marketer provides a vessel nomination document to CBH. The nomination advice informs CBH of:
- (i) the vessel identity and type;
 - (ii) estimated date of arrival in port;

- (iii) loading port;
 - (iv) stevedore; and
 - (v) load contents (eg grade and quantity of grain required).
- 2.81 **[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]** CBH requests that Marketers provide the vessel nomination 14 days prior to the vessel's estimated time of arrival, to allow time for grain to be removed from storage and transported to port if necessary.
- 2.82 The Marketer then issues a Cargo Assembly Plan for the vessel nominated. The Cargo Assembly Plan outlines which grain the Marketer requires, the sites from which the grain should come and how the grain should be loaded.
[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]
- 2.83 Inefficiencies arise at this point of the Supply Chain for bulk export wheat. This is because the AWB Cargo Assembly Plan frequently nominates country site sources for a particular grade of wheat, when there is sufficient wheat of equivalent grade (that meets the specification stipulated) at port already. This creates an inherent potential for inefficiencies, because the rapid movement of grain on an ad-hoc load-by-load basis:
- (i) results in under-utilisation of port storage facilities while country facilities may be at or near capacity with grain that will ultimately be transported to port in any event;
 - (ii) exacerbates seasonal peak demand issues at country sites;
 - (iii) creates flow-on problems for other users of the storage, handling and transport infrastructure;
 - (iv) fails to take advantage of opportunities to coordinate large scale movements of grain in planned, orderly and cost effective movements;
 - (v) risks incurring substantial demurrage costs if loads are not ready in time for the nominated vessel; and
 - (vi) jeopardises fumigation protocols by seeking grain that may still be under fumigation
- 2.84 The Cargo Assembly Plan at annexure J illustrates such an inefficiency. The Plan provides for the movement of a parcel of 60,000 tonnes of Australian Standard White (**ASW**) wheat and specifies for stock to be accumulated from high protein ASW-reserved sites. CBH, as the custodian of AWBI's grain, is in possession of detailed information concerning the location of AWBI's ASW wheat stock. CBH knows that 200,000 tonnes of ASW wheat (which would meet the cargo quality specifications) is already in port. Moving stock from country reserved sites at short notice would be likely to incur greater costs, such as crew and equipment mobilization, stack preparation for out-loading, re-fumigation and possible compromise of fumigation protocols (which are ultimately passed on to Growers), as well as creating a critical path of grain movements with little or no margin for error and risk demurrage charges. This

would all occur even while there was more than three times the quantity of suitable ASW wheat already stored at the port.

- 2.85 In order to carry out the Cargo Assembly Plan, CBH meets with road and/or rail transporters to coordinate the necessary tasks required to comply with the Cargo Assembly Plan. At that meeting, CBH provides information such as the type of grain, the quantity and the location from which the grain should come.
- 2.86 The outcome of this meeting is a transport plan, which nominates the loading, scheduling and truck fleet or rolling stock requirements to move grain as required. **[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]** These types of issues emphasise the importance of coordinated, orderly grain movements controlled by persons whose interests are entirely aligned with Supply Chain efficiency, whilst meeting the quality needs of CBH's customers.
- 2.87 To facilitate the loading and unloading of bins at storage, CBH organises employees to open storage bins to unload grain for transportation.
- 2.88 CBH may then issue a Road Movement Authority to road transporters. **[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]** CBH does not issue a similar authority for rail transport because the rail loading schedule serves as an authority.
- 2.89 Once a parcel of grain is moved from storage, CBH issues a summary of the freight movement to the transporter and a copy of this report goes the Marketer on request. **[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]**
- 2.90 Figure 2.7 below is an example of a failure of supply chain coordination under the current system, in relation to deregulated barley. Figure 2.7 is a "spider diagram" which represents the assembly of a cargo from different sites in the CBH system. The total cargo requirement is shown at the centre and each quantity of grain sourced from specific sites is shown on the "legs" of the diagram.
- 2.91 The 55,000 tonnes of barley used to load the ship in this figure was assembled from specific parcels at individual sites. As a result, various sized quantities of barley were sourced from 36 different locations in order to assemble cargo for this ship. Assembling this cargo from a smaller number of locations or a single location would obviously be much more efficient for reasons made clear in the Synergies report. Figure 2.7 illustrates a means of managing the grain task that is inefficient and unsustainable. Grain Express would dramatically improve the efficiency of the system by eliminating cargo assemblies of this kind.

Figure 2.7 – Supply chain coordination: deregulated barley



Financial arrangements

- 2.92 Pursuant to the contractual arrangements in place between transport carriers and Marketers, a transport carrier issues an invoice to the Marketer at the completion of a movement.
- 2.93 The carrier derives the necessary data for generating the invoice for its carriage services based upon the movement data it has been provided by CBH.
- 2.94 The transport carriers' invoices are paid by the Marketer. In the case of bulk export wheat, AWBS pays these invoices and then invoices AWBI for the services it renders in coordinating transport, storage and handling. AWBS invoices are ultimately deducted from Growers' pool payments, with Growers receiving their pool entitlement less Supply Chain costs (substantially comprised of AWBS charges).
- 2.95 Transparency of Supply Chain costs is a real issue in the Western Australian Supply Chain because, in the case of AWBS, service fees (including transport) are deducted in an aggregated fashion and the fees for particular movements are not distinctly disclosed.

Transport infrastructure

- 2.96 Each of the four port zones has a different arrangement of transport infrastructure as follows:
- (i) The Kwinana port is served almost exclusively by rail. A dual gauge rail line operates from Northam to Kwinana.
 - (ii) A single narrow gauge line running from Hyden serves the Albany port, which is also served by road access. However, the Albany

terminal is placed on a narrow site that creates some restrictions on concurrent access by road and rail.

- (iii) The Geraldton port is served by two main narrow gauge rail lines as well as main roads from Mullewa, Morawa and Mingenew. A high proportion of deliveries to the Geraldton port (approximately 20%) are direct Grower deliveries¹¹.
- (iv) Esperance is predominantly served by road with Growers delivering 40% of total production direct to the port of harvest¹². Only 14% of grain harvested in this zone is delivered to port by rail. Rail links are on standard gauge track mainly used for non-grain haulage purposes. There are two sites served by rail in this zone.

2.97 While rail has traditionally been the primary means of transport used for grain, road has become increasingly competitive. The Western Australia Strategic Grain Infrastructure Study of 26 April 2005 includes detailed analysis of export and domestic grain and port receivals. It also includes an analysis of the volumes of grain moved in each of the port zones and the rail freight task in comparison with road, both in tonnage terms and in tonne per kilometre terms. As the report identifies, the average haul distance for Western Australian grain on rail is 290 kilometres, almost double the average haul from road sites. Of the total farm to port (and domestic consumer) task, rail currently accounts for approximately 70% of all net tonne kilometres¹³. The report also projects the transport task to grow by 28% by 2025.

2.98 The structure of Western Australian transport infrastructure creates a number of efficiency and sustainability issues including:

- (i) the efficiency and sustainability of the narrow gauge network; and
- (ii) the efficiency, sustainability and desirability of further use of roads to carry a substantial proportion of the export grain tasks.

Rail network

2.99 Until February 2006, the relevant rail infrastructure in Western Australia was owned by ARG. ARG was a 50/50 joint venture by Wesfarmers Limited and Genesee & Wyoming Inc, formed in 2000. ARG acquired the WestRail freight business from the Western Australian government in December 2000. In February 2006, the ARG railway assets in Australia were acquired by Babcock & Brown and Queensland Rail (**QR**).

2.100 These assets include Westnet Rail, the company that holds a 49-year lease on approximately 5,300 kilometres of freight rail track in Western Australia. Access to this rail track is governed by access agreements negotiated between access seekers and the asset owner, through a regulated access regime.

¹¹ Western Australia Strategic Grain Infrastructure Study (2005), 37.

¹² Ibid.

¹³ Ibid 33.

- 2.101 Under the arrangement between QR and Babcock & Brown, the above-rail and below-rail assets have been split, so that Babcock & Brown owns the lease of the rail track and QR owns the above-rail assets. Therefore, rail freight agreements will be negotiated with QR and Babcock & Brown.
- 2.102 The Western Australian rail system comprises a combination of standard and narrow gauge lines built at different times. As a result, the length and weight of trains used on the network accord with the characteristics of the relevant track. A number of other issues impact upon train size and configuration, including terrain characteristics, siding lengths and outload speeds at particular receival sites. As a result, it is not productive to operate trains of a standard length across the network, which has cost implications for users of the network¹⁴.
- 2.103 The Western Australian grain storage and handling system and the location of grain receival sites is substantially built around the rail network. The Western Australia Strategic Grain Infrastructure Study used a series of models to examine the sustainability of the rail-based network for the grain task in Western Australia. That study concluded that:
- (i) growth in the grain export task will improve rail service revenue and productivity;
 - (ii) increased range (between poor and peak harvest) will add to capital and operational costs for both ARG and CBH;
 - (iii) a cohesive rail network will be increasingly essential to handle peak harvests, particular peaks in sequential seasons;
 - (iv) rail will also be vital for Growers to obtain early season price premiums in an increasingly competitive global market place.
- 2.104 The study also notes that under the current commercial structure, there are incentives for ARG/Westnet to close branch lines that face a disproportionate maintenance burden. The study suggests that network rationalisation based upon closing lines as they fall due for maintenance investment would not be practical or optimal. The report also states “provision of a stable long term rail network, maintained to an agreed standard is a pre-condition for the continued viability of rail services to the export grain industry.”

Road network

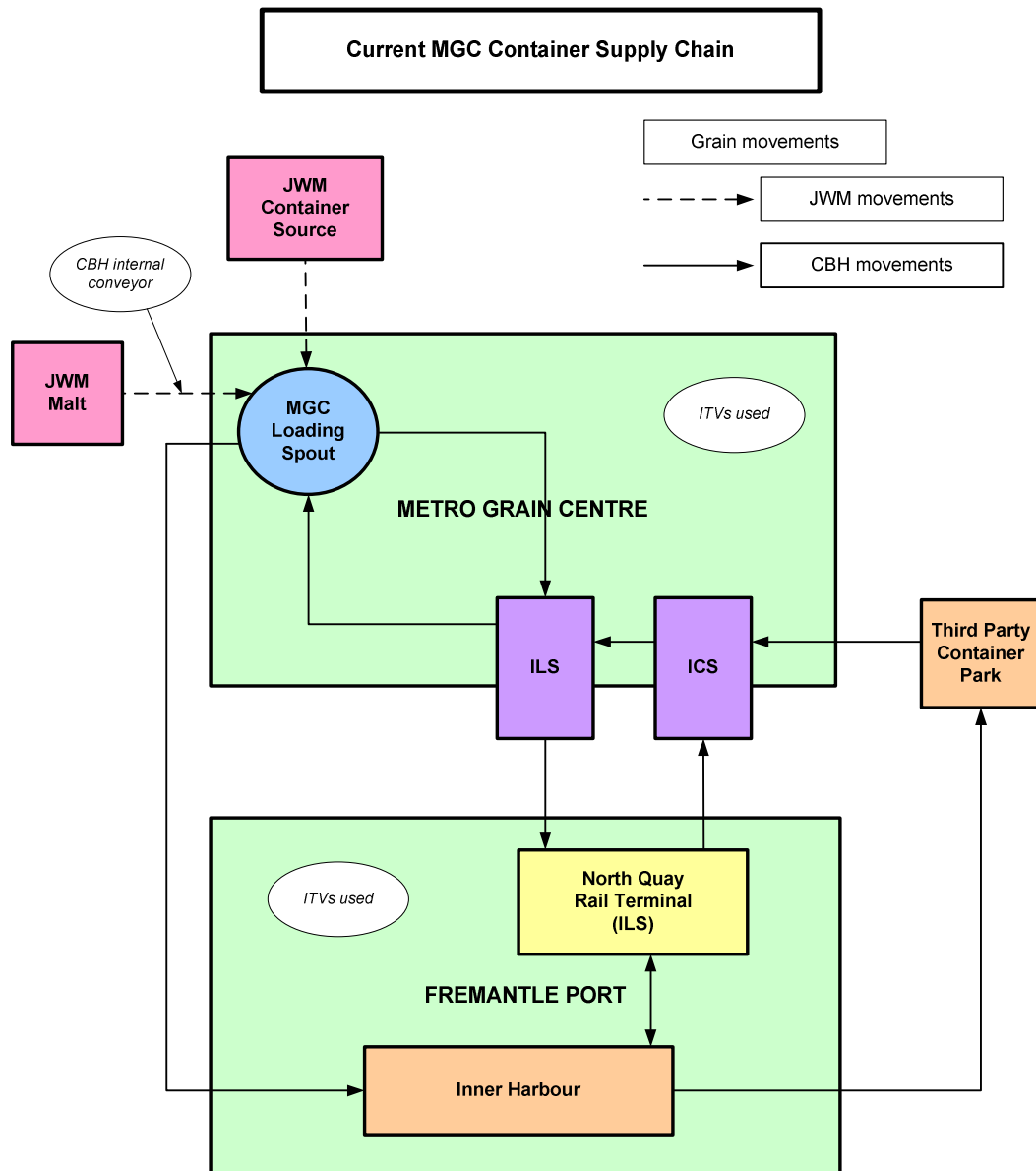
- 2.105 A substantial proportion of Growers whose properties are within 100 kilometres of one of the four ports deliver grain direct to port by road. The Western Australian Strategic Grain Infrastructure Study estimates farm to port deliveries as comprising 19% of receivals at port. In poor or average seasons, the incidents of direct to port deliveries generally increases.
- 2.106 Approximately 30 receival sites in Western Australia are designated “road to rail” sites under the current freight agreement. Grain received at these sites is transported by road to the nearest rail link by the rail operator.

¹⁴ Ibid 38.

Container loading and handling

- 2.107 CBH owns and operates the MGC, which is a specialised grain storage and container loading facility in Forrestfield, Western Australia. The MGC receives grain in bulk by road and rail, stores grain as required and loads grain into containers for non-bulk export or domestic consumption.
- 2.108 Approximately 1,000,000 tonnes of grain per annum can now be loaded by CBH into containers for delivery to both domestic end-users or to the Fremantle port for export. The Marketers organise to have containers made available from their relevant shipping line and CBH then organises to collect, load and transfer the containers back to the relevant destination (a container park for domestic use and the Inner Harbour for shipping).
- 2.109 CBH contracts with Intermodal Link Services (**ILS**), which supplies logistics services for the movement of containers between the Intermodal Container Services (**ICS**) container park (at MGC), the loading spout, the North Quay Rail Terminal (**NQRT**) and the Inner Harbour of Fremantle Port. Approximately 85% of all containers moved by ILS are moved by rail.
- 2.110 ILS contracts with ICS which manages the empty container park at MGC. ICS arranges to receive containers from either NQRT or third parties. ICS receives approximately 85% of all empty containers by rail. ICS transports all of its decommissioned containers by Internal Transit Vehicles (**ITV**) to the ILS premises and then on to the MGC loading spout to be filled, before being taken back to the ILS premises at MGC.
- 2.111 ILS then organises for the full containers to be moved from MGC to NQRT by rail, and then moved from NQRT by ITV to Fremantle Port's Inner Harbour for loading onto ships.
- 2.112 NQRT is located in the greater Fremantle Harbour precinct at Rous Head. NQRT receives containers by both rail and road, and then may distribute:
- (i) full containers to the Inner Harbour of Fremantle Port for loading; or
 - (ii) empty containers to ICS or other third parties.
- 2.113 Marketers and end-users of grain delivered to MGC may choose whether to make their own transport arrangements for moving containers between MGC, NQRT and the port, or whether to have CBH arrange their own transport.
- 2.114 An example of an MGC user that arranges its own transport is Joe White Maltings, whose malting plant adjoins MGC and is served directly by conveyer from MGC storage. After barley has been processed into malt by Joe White Maltings, it is sent back to MGC for packing by CBH. Joe White Maltings then arranges road transport to port.
- 2.115 Figure 2.8 below describes the container Supply Chain, with a focus upon MGC's operations.

Figure 2.8 - Container Supply Chain



Port storage and handling

- 2.116 Once grain arrives in port storage, it is accumulated for loading, pending the vessel's arrival. The Marketer or his agent will instruct CBH to load the cargo (order labour). **[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]** Depending on the actual sale or charterer terms, the stevedore labour will also be booked by the Marketer (or its agent) or the shipping agent (on behalf of the ship owner).
- 2.117 CBH then instructs its port staff that the grain is acceptable to ship. The ship's master issues a notice of readiness to the Marketer upon arrival. Loading is

commenced and completed, and the Marketer (or its agent), shipping agent, and master then exchange statements of fact and times to confirm the key matters relevant to the vessel's call.

- 2.118 The shipper will usually appoint a third party to collect and/or sign shipping documents on their behalf for all bulk shipments. Such documents will include SOF, NOR, Mates Receipts etc. AWB currently appoint Inchcape to act on their behalf. Other shippers appoint CBH to act on their behalf for a modest fee.
- 2.119 The final acquirer (shipper) pays CBH Fobbing fees. Ocean freight and stevedoring charges are paid according to the sale/chartering terms. Sales proceeds from the customer are paid to the marketer. The marketer will pay funds to the grower in a variety of payment methods after deducting costs.

Planning and information flows

- 2.120 As stated above, CBH requests a 12-month forward shipping program from the Marketers, which describes the type and quantity of grain, and approximate time and port from which the grain will be shipped. Forward shipping programs are inherently subject to delay or change but are still useful in assisting in planning for likely shipments. As a result, CBH may receive grain at a port facility that is not for shipping on a specific vessel.
- 2.121 If the vessel is delayed in arrival at the port, passing through Customs, obtaining AQIS phytosanitary clearance or vessel structural surveys, then this may have flow on effects to the shipping stem and the order of berthing of other grain export vessels. Slippage in dates at this point in time could result in detrimental consequences entirely out of CBH's knowledge and control such as
 - (i) the vessel not being loaded before the expiry of the contracted loading date, for example, expiry of Letter of Credit issued (which would mean that the Marketer will not want the ship to be loaded until the Marketer/overseas client has negotiated possible later load dates); and
 - (ii) factors such as quality, quantity, nature of product, fumigation constraints, capacity constraints, lack of loading notice, ships failing survey and weather.

Marketing

- 2.122 Grains are acquired and marketed in a variety of ways. At the farm gate, producers choose whether to:
 - (i) deliver their grain to a national or regional pool;
 - (ii) forward contract for cash;
 - (iii) forward contract into a special pool;
 - (iv) deliver against a pre-existing contract for a special product like AgraCorp Active (which is very similar to a financial product);
 - (v) sell for cash at harvest time;
 - (vi) put into warehousing; or

- (vii) supply themselves into the domestic market (eg domestic mills, seed makers or feedlots).
- 2.123 Producers selling into a pool may either take a distribution pool payment for the wheat, or another financial product, which may include:
- (i) harvest loan;
 - (ii) flexible draw down loan;
 - (iii) advance payment;
 - (iv) percentage of estimated pool return (generally underwritten); and
 - (v) AWB's deferred payment (deferred until July after delivery and a percentage of the July estimated pool return).
- 2.124 Marketing activities differ depending upon the type of grain, and whether the grain is sold into the domestic market or for export. Marketing options help manage the various production and price risks that a Grower faces when deciding to produce grain. For example, producers selling into a pool may either take a payment for the wheat or another grain in the following manner:
- (i) harvest loan;
 - (ii) flexible draw down loan;
 - (iii) advance payment;
 - (iv) percentage of estimated pool return (generally underwritten); and
 - (v) deferred payment (deferred until July after delivery and a percentage of the July estimated pool return).
- 2.125 Domestic grain markets are unregulated, and any person may acquire, accumulate, trade and supply grain to domestic end-users. Export marketing of wheat is currently regulated under Commonwealth legislation, while State legislation currently regulates Barley, Canola and Lupins in Western Australia.

Wheat

- 2.126 Exporting of wheat is regulated by the *Wheat Marketing Act 1989* (Cth) (**WMA**). The WMA establishes the Authority as the continuation of the former statutory entity, the Australian Wheat Board¹⁵, whose staff and trading functions were transferred to AWBL in 1999.
- 2.127 The WMA prohibits wheat exports without the consent of the Authority¹⁶. AWBL's subsidiary – AWBI – is expressly excepted from this prohibition¹⁷. Before granting export consent, the Authority must consult with AWBI¹⁸ and, in

¹⁵ *Wheat Marketing Act* (Cth) 1989, section 4.

¹⁶ *Wheat Marketing Act* (Cth) 1989, section 57(1).

¹⁷ *Wheat Marketing Act* (Cth) 1989, section 57(2).

¹⁸ *Wheat Marketing Act* (Cth) 1989, section 57(3)A.

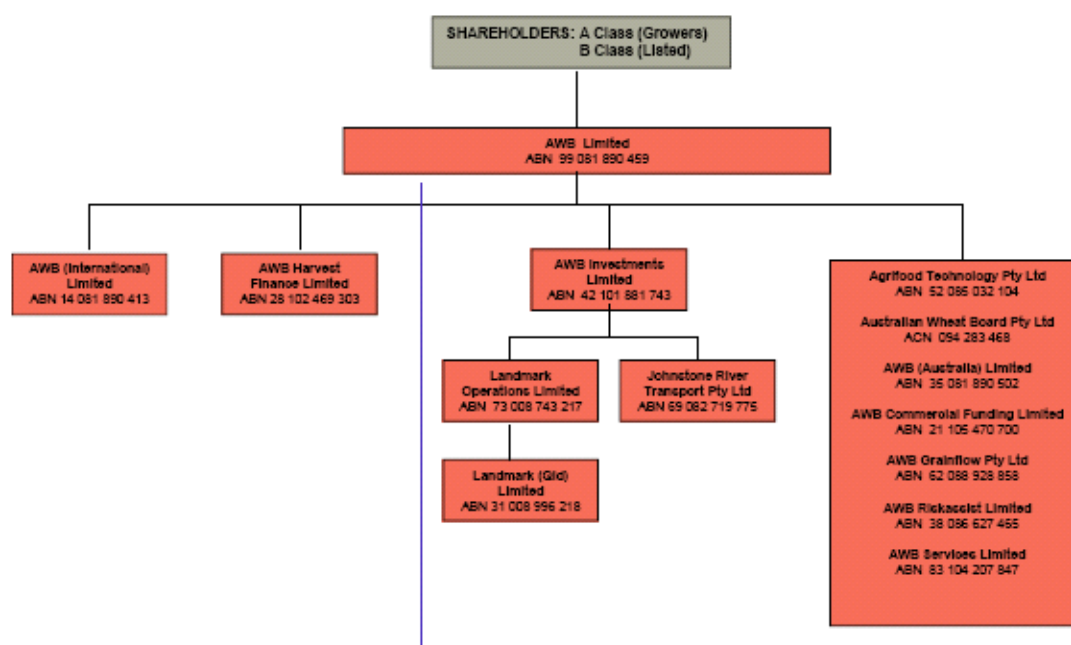
relation to bulk wheat exports, AWBI has the right to veto a decision by the Authority to grant export consent¹⁹.

2.128 AWB was incorporated on 12 March 1998. It has three subsidiaries which are relevant to the operation the Single Desk (**AWB Group**):

- (i) AWBI – 5 ordinary shares all held by AWB;
- (ii) AWBS – 1 ordinary share held by AWB; and
- (iii) AWB Harvest Finance Ltd (**AWBF**) – 1 ordinary share held by AWB.

2.129 Figure 2.3 is an organisation chart for the AWB Group detailing the operation of the export grain monopoly arrangement known as the “Single Desk”²⁰.

Figure 2.3 – AWB Corporate structure



2.130 AWBI does not have any employees. Rather, AWB provides all functions for AWBI which are necessary for the operation of the Single Desk. The services are provided by AWB under an agreement called the service level agreement (**Service Level Agreement**).

2.131 Under the Service Level Agreement, AWB is remunerated by AWBI as follows:

- (i) a fixed fee which is CPI indexed; and

¹⁹ *Wheat Marketing Act* (Cth) 1989, section 57(3)B.

²⁰ AWB Corporate Structure Diagram (2004) AWB Limited <http://www.awb.com.au/NR/rdonlyres/F1023877-0510-4B75-88B7-3D06A4909E84/0/Corporate_structure_diagram.pdf> at 1 May 2008.

- (ii) an out-performance incentive (**OPI**) under which AWB receives a percentage of the revenue generated by the Single Desk if certain criteria (including Supply Chain costs) are met.
- 2.132 As the OPI is based on certain hurdles, including AWBI's Supply Chain costs not exceeding a maximum level, a key reason for AWB seeking to reduce Supply Chain costs is to achieve the OPI.
- 2.133 AWB controls AWBI via its rights under AWBI's Constitution and through the services it provides to AWBI under the Service Level Agreement. Under the WMA, the Export Wheat Commission (**EWC**) granted AWBI the sole right to market and export wheat via the Single Desk. AWB's subsidiaries, AWBI and AWBF, fund and purchase wheat from local Growers, and market and export that wheat via the Single Desk.
- 2.134 The sections relevant to AWBI's operation of the Single Desk are provided below.
- 2.135 Section 57(1) of the WMA provides that:
 - "A person shall not export wheat unless:*
 - (a) *the [EWC] has given its written consent to the export of the wheat; and*
 - (b) *the export of the wheat is undertaken in accordance with the terms of that consent".*
- 2.136 Section 57(1A) of the WMA exempts AWBI from the prohibition under section 57(1).
- 2.137 Under sections 57(3A) and (3B) of the WMA, the Authority must consult with AWBI prior to providing its consent to a person seeking to export wheat in accordance with section 57(1). The Authority cannot provide its consent without the prior written approval of AWBI. The ability for AWBI to veto the entry of any other parties to the export wheat market was temporarily stripped from AWBI under the *Wheat Marketing Amendment Act 2006* (Cth).
- 2.138 Australian wheat exports are presently regulated by the WMA and the EWC. The present wheat export arrangements came into effect in mid-2007, following amendments to the WMA. These amendments:
 - (i) give the Minister for Agriculture, Fisheries and Forestry the power to appoint a "designated company" to manage the Single Desk for bulk wheat exports. This power came into effect on 1 March 2008 and will sunset on 30 June 2008²¹;
 - (ii) established the EWC on 1 October 2007 to replace the Authority. Under the WMA, the EWC has 3 main functions:
 - (A) controlling bulk wheat exports;

²¹ *Wheat Marketing Act 1989* (Cth), section 3AA.

- (B) monitoring and reporting on the performance of the Single Desk company (AWBI); and
 - (C) administering the non-bulk wheat quality assurance scheme.
- 2.139 On 5 March 2008, an exposure draft of the Wheat Export Marketing Bill 2008 (Cth) (**Proposed Act**) was released for public comment. Changes may be made to the proposed wheat export marketing scheme as a result of public and industry consultations, and the Senate Inquiry by the Rural and Regional Affairs and Transport Committee²². At the time of drafting this submission, the EWC was awaiting the outcome of the consultation process, and further policy advice from the government in relation to the proposed alterations to the wheat export scheme²³. Further detail on the proposed changes is provided in part 6 of this document in relation to the counterfactual analysis.
- 2.140 Under the WMA, the export of wheat by AWBI, and anything done by AWBI under section 57 of the WMA, is to be regarded as being exempt from the provisions of the TPA. In this regard, section 57(6) of the WMA provides that:
- “For the purposes of subsection 51(1) of the Trade Practices Act 1974, the following things are to be regarded as specified in this section and specifically authorised by this section:*
- (a) *the export of wheat by nominated company B [AWBI];*
 - (b) *anything that is done by nominated company B [AWBI] under this section or for the purposes of this section”.*
- 2.141 In its submission to the 2004 Wheat Marketing Review²⁴, AWB stated that “AWBI has no employees and therefore, in order for it to carry out its functions, it contracts various services from AWB Ltd”.
- 2.142 To enable AWBI to undertake its functions (the operation of the Single Desk), AWB provides services to AWBI via the Service Level Agreement. AWBF is also a party to the Service Level Agreement, and AWB provides services to AWBF.
- 2.143 The Service Level Agreement is not a public document. It is therefore not possible to review it or comment on its terms.
- 2.144 The Service Level Agreement commenced on 1 July 1999. Since then, it has been reviewed three times, once in 2001, 2003 and 2006 respectively. The amendments to the Service Level Agreement have changed the manner in which AWB is remunerated for providing services to AWBI.

²² Wheat Export Accreditation Scheme (2008) Wheat Export Commission
<<http://www.ewc.gov.au/WheatExportAccreditationScheme.html>> at 1 May 2008.

²³ Ibid.

²⁴ AWB Ltd, *Submission to the 2004 Wheat Marketing Review* (2004) 2004 Wheat Marketing Review, p.24
<http://www.2004wheatreview.gov.au/documents/283_AWBI.pdf> at 1 May 2008.

- 2.145 The services provided by AWB to AWBI and AWBF under the Service Level Agreement are provided by AWB's wholly owned subsidiary AWBS, at the direction of AWB.
- 2.146 In its submission to the 2004 Wheat Marketing Review²⁵, AWB listed the following services which it provides to AWBI under the Service Level Agreement (**AWB Services**):
- (i) premises services;
 - (ii) core corporate services including:
 - (A) company secretary;
 - (B) internal audit;
 - (C) legal services;
 - (D) human resources and change management;
 - (E) office of the Managing Director – business strategy;
 - (F) accounting and administrative services;
 - (G) IT services; and
 - (H) other services as agreed; and
 - (iii) operational services including:
 - (A) treasury;
 - (B) sales and marketing;
 - (C) risk management;
 - (D) acquisition;
 - (E) logistics;
 - (F) trading;
 - (G) export credit advice and insurance;
 - (H) credit services;
 - (I) public affairs; and
 - (J) other services as agreed.
- 2.147 AWB receives remuneration for providing the AWB Services to AWBI under the Service Level Agreement. When the Service Level Agreement commenced, payments to AWB for the provision of the AWB Services were calculated on a costs plus basis. However, the EWC considered this method was inadequate. From 2001, AWB was paid for providing the AWB Services via the

²⁵ Ibid.

“Performance Based Remuneration Model” (**PBRM**). The PBRM was revised in 2005²⁶.

- 2.148 As the Kronos Report observed²⁷, the majority of AWBL’s income is derived from providing non-contestable services to AWBI or the pool.

Other marketers

Toepfer

- 2.149 Toepfer trades in grain, oilseeds, and feedstuffs. The Toepfer group consists of the headquarters in Hamburg and 42 subsidiaries. Toepfer has offices worldwide, with more than 2,000 employees achieving a sales volume of more than 42 million tonnes annually. Toepfer International, founded in 1979, started with an equity of approximately €55.5 million. Today, the equity amounts to more than €230 million²⁸. Toepfer operates in Australia through Elders Toepfer Grain Pty Ltd. It is unclear what the relationship between Toepfer and Elders is based upon in Australia.

Elders

- 2.150 Elders is positioned to offer grain growers full services in grain, with branches located throughout the grain belt in Australia. This includes the provision of agronomic advice, seed, fertilisers and agricultural chemicals. Elders has a suitably qualified team of specialised grain staff with extensive experience in managing grain pools and forward contract options, grain trading and logistics, grower services and grain accumulation. Elders offers growers a full suite of grain marketing options for a range of commodities, including contracts, cash prices, pooling products, ex-farm and delivered end user options and on-farm storage products²⁹.

Cargill Australia Limited

- 2.151 Cargill Australia Limited (**Cargill**) is an international provider of food, agricultural and risk management products and services. Cargill is a wholly owned subsidiary of Cargill Incorporated, which has over 149,000 employees in 64 countries. Cargill established a presence in Australia in 1968 to service the country’s large grain exports. It has since extended its involvement into several other agricultural industries including oilseed and beef processing, flour milling, grain and cotton trading, and grain storage. Cargill currently sells protein meals and vegetable oils, beef products and cotton lint, and exports food ingredients via Toshoku. In addition, Cargill Risk Management offers a range of risk management products for producers and consumers of commodities. Cargill’s investments in Australia total US\$250 million with an

²⁶ AWB Ltd, *AWB proposes changes in response to 2004 Wheat Review* (24 November 2004) <<http://www.awb.com.au/NR/exeres/8355A31B-FC2E-4FEB-8E81-1CCC66421F62.htm#>> at 1 May 2008.

²⁷ Kronos Corporate Pty Ltd, *Review of Structural Issues in the Australian Grain Market* (2002), 29.

²⁸ Toepfer International (2008), <http://www.acti.de/e_frameset.html> as at 6 May 2008.

²⁹ Elders (2008), <<http://grains.elders.com.au/>> as at 6 May 2008.

annual turnover of approximately US\$500 million. Cargill employs over 1,200 people in Australia³⁰.

GrainCorp Limited

- 2.152 GrainCorp Limited (**GrainCorp**) operates an extensive storage and handling receival network, comprising 286 country receival sites, 9 port terminals, and more than 21 million tonnes of storage capacity. GrainCorp's network provides receival, stock management and bulk/container handling facilities for grain and a range of other commodities – including woodchips, sugar, cottonseed, meals, mineral sands and frozen orange juice concentrate. GrainCorp services customers in domestic (industrial, human consumption, stockfeed, feedlots, maltsters) and export markets. GrainCorp provides contract rail and/or road transport services to millers, maltsters, feedlots, grain traders and growers as well as to GrainCorp business units.
- 2.153 GrainCorp's marketing business operates across Australia trading grains, oilseeds and wool. It offers cash prices, forward prices and pools, and specialist risk management services are available through Agricultural Risk Management Services. GrainCorp markets to a range of domestic and international clients, with an increasing focus on Asia and the Middle East.

ABB Grain Limited

- 2.154 ABB Grain Limited (**ABB**) is a leading Australian agribusiness with a multi-faceted operation and international focus. ABB has historically been involved in grain accumulation and marketing, but now has a more diversified operation which stretches across the entire supply chain. ABB accumulates grain from all grain growing regions across Australia, and trades in all grain commodities³¹.
- 2.155 ABB's supply chain includes operations in storage, handling and logistics. ABB has a significant network of silos and export shipping terminals in South Australia and the eastern states of Australia. ABB also provides a number of value-adding services. ABB's malting division, Joe White Maltings, is one of the world's largest producers of malt with the capacity to produce 500,000 tonnes per annum. The 8 malting plants strategically positioned across Australia include the largest malthouse in the southern hemisphere, which is located in Perth³².

Glencore Grain Pty Ltd (Brooks Grain)

- 2.156 Glencore Grain Pty Ltd, trading as Brooks Grain, is a 100% owned subsidiary of Glencore International AG (**Glencore**), and operates throughout Australia servicing the domestic market and grain exports. Brooks Grain trades in domestic and international markets.

³⁰ Cargill Australia Limited (2007), < http://www.cargill.com.au/about_us.htm as at 6 May 2008.

³¹ ABB Grain Limited (2008), <<http://www.abb.com.au/AboutABB/WhoWeAre/tabid/496/Default.aspx>> at 6 May 2008.

³² Ibid.

- 2.157 Glencore is a privately-owned Swiss company. Together with its subsidiaries, Glencore is a diversified natural resources group with worldwide activity in the mining, smelting, refining, processing and marketing of metals and minerals, energy products and agricultural products. Glencore is engaged in the physical sourcing and marketing of commodities on a global basis, purchasing physical commodities as principal (mostly from producers), and selling and delivering these commodities to industrial consumers (such as car manufacturers, steel mills, public utilities and flour mills). Glencore also provides financing, logistics, marketing and purchasing services to producers and consumers of commodities. These activities are supported by strategic investments in industrial assets relating to Glencore's core physical marketing business³³.

Louis Dreyfus Commodities

- 2.158 Louis Dreyfus Commodities (**LDC**), is an international commodity merchant and processor of agricultural products. LDC has merchandised and traded bulk commodities in international markets since 1851. LDC is present in over 53 countries, and its aggregate average annual gross sales in recent years have exceeded \$20 billion³⁴.
- 2.159 LDC operates from five major regions (Argentina, Brazil, North America, Europe and Asia), and offices in Beijing, Buenos Aires, Delhi, Geneva, São Paulo, Singapore and Wilton (USA) serve as major coordination centres for merchandising activities. LDC is ranked number one in world cotton merchandising and is one of the three largest producers of orange juice. LDC is also a leader in the grains and oilseeds, sugar, coffee, rice, metals, freight and emerging financial trading markets³⁵.
- 2.160 LDC is an affiliate of the Louis Dreyfus Group, an organization of diversified companies privately owned by the Louis-Dreyfus family. The global activities of LDC are vertically integrated under a holding company, Louis Dreyfus Commodities BV, which is based in the Netherlands³⁶.

Emerald Group Australia

- 2.161 Emerald Group Australia (**Emerald**) is a commodity management, investment and advisory company. Emerald operates nationally, and has three divisions:
- (i) commodity products: Emerald develops and distributes a range of commodity products to producers and consumers of agricultural commodities to assist in enhancing returns and managing volatility and risk. Emerald's grain marketing activities include an innovative range of grain marketing pools, fixed price contracts, spot pricing and other associated grain marketing alternatives;

³³ Glencore Grain Pty Ltd (2008), <<http://www.glencoregrain.com.au/content.asp?page=58>> at 6 May 2008.

³⁴ Louis Dreyfus Commodities (2008), <<http://www.ldcommodities.com/index.php?nav-about>> at 6 May 2008.

³⁵ Ibid.

³⁶ Ibid.

- (ii) investments: Emerald manages investments in the Australian agricultural commodity sector on behalf of professional investors, specifically focussed on opportunities in the growing Australian grains sector. Emerald operates industry specific investment vehicles that capture unique commodity management and arbitrage opportunities; and
- (iii) advisory: Emerald is a leading advisor to corporate agribusiness through its corporate consulting unit, Kronos Corporate. Emerald specialises in commodity risk and volatility management, commodity procurement, strategy, industry overview, mergers & acquisitions and executive recruitment³⁷.

Tamma Grains

- 2.162 Tamma Grains receives, stores and markets grain. The Tamma Grains facility is located approximately 202 kilometres south east of Perth. It began operations in 1986, purchasing grain from farmers on behalf of local feed mills. Tamma Grains' current storage is approximately 55,000 tonnes. Farmers within a 250km radius deliver grain to Tamma Grains' facility. The towns serviced include Yealering, Kondinin, Kulin, Hyden, Corrigin, Bruce Rock, Southern Cross, Lake Grace, Newdegate and Narembeen.

Barley, lupins and canola marketing

- 2.163 In Western Australia, the export of barley, lupins and canola is regulated under the *Grain Marketing Act 2002* (WA) (**Grain Marketing Act**). The Grain Marketing Act also created the Grain Licensing Authority (**GLA**) as the regulatory body responsible for the issue of licenses to export barley, lupins and canola in bulk shipments from Western Australia. GPPL is the main export license holder under the Grain Marketing Act. In November 2002, the Western Australian government corporatised the Grain Pool business, and CBH acquired the shares in GPPL in an agreed merger based on a similar shareholder base.
- 2.164 GPPL does not have the same degree of statutory monopoly rights as enjoyed by AWBI. The licensing structure under the Grain Marketing Act provides the GLA with the ability to issue additional licenses to export barley, lupins or canola.
- 2.165 The GLA is required to consider two criteria in determining whether to grant or refuse an application for the issue of a further export license:
- (i) whether the main export license holder (GPPL) is receiving a price premium in the market for which a grain trader seeks a license. If a price premium can be demonstrated, the Grain Licensing Authority is to contact GPPL and determine whether the premium will be affected to a significant extent by the additional market applicant. A license cannot be granted if a significant risk exists; and

³⁷ Emerald Group Australia (2008), <http://www.emerald-group.com.au/our_company.php> at 6 May 2008.

- (ii) whether a new license will have any adverse effect on the State's reputation as a grain exporter and on the State's grain industry generally³⁸.
- 2.166 Traders that are granted licences by the GLA under the Grain Marketing Act are referred to in this document as "GLA license holders".
- 2.167 A recent review of the Grain Marketing Act by the Economic Regulation Authority of Western Australia has recommended its repeal, and the deregulation of the export of barley, lupins and canola. That deregulation is recommended to take place by the 2008/09 harvest.

³⁸ RSM Bird Cameron, *Review of the Benefits and Costs of the Operations of the Grain Marketing Act 2002 and the Grain Licensing Authority* (2005), [2.7].

3 CBH's proposed conduct

Overview

- 3.1 Grain Express is a complete and coordinated transport, storage and handling solution that CBH will offer to Growers and Marketers (including AWB, GPPL and GLA license holders) as well as proposed accredited wheat exporters for domestic and export grain.
- 3.2 The key elements of Grain Express are:
- (i) open access to the CBH storage and handling network;
 - (ii) a new structure for freight agreements;
 - (iii) a bundled receival, storage, handling, logistics and transport service;
 - (iv) more flexible and effective receival conditions;
 - (v) improved outturning of grain at defined Destination Sites;
 - (vi) transparent freight, storage and handling fees for Growers and Marketers;
 - (vii) transparent queuing and shipping arrangements;
 - (viii) clarified grain entitlements of Growers and Marketers;
 - (ix) improved quality management services to derive value from information; and
 - (x) a new and more extensive Grower services call centre.
- 3.3 These changes are summarised in the following paragraphs.

Freight agreement structure

- 3.4 Under current arrangements, CBH and Marketers acquire road and rail freight services directly, despite the fact that CBH has custody of grain in its system.
- 3.5 Under Grain Express, CBH will negotiate agreements to acquire bulk grain haulage services from ARG and road haulage carriers. CBH will use the freight services it acquires to move grain in its system between the Receival Point and, depending upon the requirements of the Grower and Marketer:
- (i) one of 10 larger grain storage and loading facilities, where grain may be outturned by the Grower or Marketer (Destination Sites);
 - (ii) the MGC (which is also an Destination Site), where grain may be loaded into containers or outturned for domestic supply;
 - (iii) one of the four port storage and loading facilities (which are also Destination Sites).
- 3.6 To this extent, CBH will replace AWBS and GPPL as the primary grain freight purchaser in Western Australia.

Bundled service

- 3.7 CBH will offer grain receival, storage and handling services to Growers and Marketers on the condition that, CBH will arrange for haulage of that grain to the point where it is outturned from CBH's custody, which may be done at any of the 17 Destination Sites selected by Growers or Marketers.
- 3.8 This condition will be implemented in CBH's contracts with both Growers (who acquire receival and storage services from CBH) and Marketers (which acquire storage and handling services).

Receival conditions

- 3.9 Under current arrangements, a Grower delivers grain to CBH and, in most cases, nominates an acquirer (usually a Marketer), which acquires the grain at the Receival Point. Marketers do not always acquire grain at all Receival Points. Nomination of an acquirer is made on a paper delivery form and frequent errors are made at this point.
- 3.10 In the 2007/2008 harvest, marketing options were selected by Growers at the point of delivery in about 50% of cases. Of those occasions, the details regarding that load need to be corrected about 60% of the time. That is, about 30% of overall deliveries (113,896) required manual adjustment in some fashion due to errors on the Carter's Delivery Form – such as the wrong marketing option selection (eg there may be multiple pool choices for a single Marketer and the wrong selection is made or the wrong payment option is selected). CBH considers that this level of manual intervention is unsustainable.
- 3.11 If an acquirer is not nominated at this point, the grain is held in storage by CBH (a practice called "warehousing") and time-based storage fees may be charged to the Grower.
- 3.12 Under Grain Express, Growers will not be required to make a nomination immediately at the Receival Point. Rather, grain will be received by CBH and the Grower will have 21 days to nominate its chosen acquirer and marketing arrangement.
- 3.13 That choice is made electronically, via CBH's Loadnet system, which lists each of the marketing options offered by the various grain Marketers. The various marketing options will include different transport costs and marketing options for grain, depending upon the point at which the Marketer expects to outturn grain or load it onto a vessel for export. For example, a marketing option may be offered for grain at the nearest Destination Site, or at the relevant downstream port.

Outturns at Destination Site

- 3.14 Under Grain Express, transfer of grain entitlement to Marketers will no longer necessarily occur at the moment grain is delivered at the Receival Point. Instead, each marketing choice on Loadnet provides for a specific point at which the Marketer will outturn the grain. When the Grower nominates a choice of marketing option and outturn point, the Marketer becomes entitled to outturn grain at the nominated Destination Site at that time.

- 3.15 There will be 15 Destination Sites (including the 4 port terminals, the MGC and 10 of the larger country sites). While Growers will be able to outturn grain from a Receival Point where they have warehoused grain, Marketers will only be able to outturn their grain entitlements at an Destination Site.
- 3.16 Marketers that have acquired grain for domestic outturn will be able to change their mind and outturn it at port but they, and not the Grower, will be liable for the transport cost for the movement to port.
- 3.17 Marketers that have acquired grain at port which they wish to outturn at an inland Destination Site can also change their mind in certain limited circumstances.

Transparent billing

- 3.18 Under current arrangements, Marketers quote prices on a port basis, and therefore generally deduct freight charges from Growers' payments. The actual cost under marketing options of carrying a Grower's grain to port is not transparently disclosed.
- 3.19 Under Grain Express, once a Grower has nominated a marketing option, CBH will arrange transport to the nominated Destination Site and invoice the Grower for its services (including a distinct and transparent freight charge) to that point. CBH will not add a profit margin to freight costs.
- 3.20 The Marketer will be charged storage and handling fees for the grain in relation to the Destination Site where it is outturned.

Clarified grain entitlement of owners

- 3.21 Under current arrangements, Marketers acquire grain at the Receival Point and arrange and pay for freight from the Receival Point to the port. Marketers may also seek to influence the movement of particular parcels of grain. However, the commingling of grain in CBH's storage network and the grain entitlement system embodied in the Bulk Handling Act is inconsistent with specific grain "ownership" in the traditional sense.
- 3.22 Grain Express recognises that, because different loads of grain are co-mingled in stacks, it is unrealistic for owners of grain in storage facilities to assert control over individual grain parcels.
- 3.23 Under Grain Express, the entitlement of the owner of grain in CBH's custody is to receive an equivalent quantity, specification and quality of grain at the Destination Site nominated by that owner. This is consistent with the Bulk Handling Act and the practical impossibility of identifying distinct volumes of grain within a co-mingled stack.
- 3.24 Marketers will not be entitled to specific volumes of grain at Receival Points, though CBH's service will still enable Marketers to use quality information to derive value in an efficient manner as described below.

Quality management

- 3.25 CBH performs testing of grain at the Receival Point and at other stages in the Supply Chain. This information is valuable in understanding the quality and other attributes of grain in CBH's system. Testing of grain at the Receival Point provides Growers with a detailed record of the grain they have delivered and also provides Marketers with a quality profile of:
- (i) quality profile of their grain entitlement; and
 - (ii) the total quality profile of all stocks of grain acquired.
- 3.26 Deriving value from grain quality information is an important matter for Growers, CBH and Marketers. Marketers seek to match quality and specification of grain with particular markets.
- 3.27 CBH has a significant investment in quality management by establishing:
- (i) the Australian Grain Centre in 2003 which is a nationally accredited testing laboratory; and
 - (ii) a better farm integrated quality program, which is an on-farm quality assurance program built to meet the internationally recognised SQF code, and is fully HACCP compliant.
- 3.28 Over the next five years, CBH and Western Australian Growers will work together to achieve a supply chain that will provide customers and international governments with the assurance that Western Australia grain is produced to internationally accepted food safety standards.
- 3.29 CBH recognises that Marketers want site level quality information for marketing purposes. However, it does not necessarily follow that it is appropriate for a Marketer to assert control over specific grain parcels or to "mine" co-mingled stacks in order to obtain a greater share of high quality grain than the Marketer has paid for.
- 3.30 To effectively manage these issues and balance logistics efficiency with marketing value derivation, an important component of Grain Express will be a quality management plan with the following elements:
- (i) Marketers will be provided with:
 - (A) full quality (as tested at receival), grade and quantity information for each parcel of grain delivered to their entitlement;
 - (B) weighted average quality of that Marketer's stock by grain and grade at each Destination Site, that will be adjusted based on all transactions in and out of Destination Sites.
 - (ii) Stake holders will be provided with total tonnes received (on a zone and whole-State basis) by grain and grade and its weighted average quality profile;
 - (iii) Marketers may request further testing data (not tested at receival), subject to payment of a fee and CBH's information flow policy, which

prohibits CBH from disclosing Marketers' confidential stock information.

- 3.31 Under Grain Express, CBH will deliver at the nominated Destination Site (most commonly, at port) grain to a specification nominated by a Marketer, provided that the Marketer has sufficient stock of equivalent grain and provided sufficient time before the outturn is required. In order to achieve this, CBH will maintain a rolling profile of the Marketer's grain entitlement, updating the profile as grain is acquired by that Marketer and outturned to that Marketer's specification. Unless it does so under the reservation policy referred to below, Marketers will not generally be able to request the movement of particular parcels of grain. However, they will be able to use information about the quality profile of their grain entitlements to derive value in niche markets.
- 3.32 Marketers will be able to request the movement of particular qualities of grain if engaging in the quality management plan process. Marketers may request CBH to provide a particular quality of grain which will result in CBH reserving internally a stack of grain in order to meet the quality requirements of a Marketer. This will ensure that the grain in the reserve stack is then delivered to that Marketer at the Destination Site. CBH will endeavour to meet these quality requests in accordance with Marketers' pro rata entitlement to grain of that quality. Full guidelines in relation to this quality management process are being developed in conjunction with Marketers.
- 3.33 To ensure that the right balance is struck between Supply Chain efficiency and niche marketing requirements, CBH:
- (i) has appointed a logistics quality manager, who is responsible for meeting quality specifications; and
 - (ii) has commenced working with Marketers to develop quality management plans.

Changes to structure of ownership, custody and transportation

- 3.34 The proposed changes to the Supply Chain will create a substantially different contractual structure in relation to the provision of transport services for grain in Western Australia. These changes will affect the contractual relationships between:
- (i) rail carriers, CBH and Marketers;
 - (ii) road carriers, CBH and Marketers;
 - (iii) Growers and CBH; and
 - (iv) Marketers and CBH.
- 3.35 Under Grain Express, CBH will become the head contractor for transport services required to transport grain in CBH's custody from country storage to port and between CBH sites.
- 3.36 From the carriers' perspective, this will simplify the contractual position and the path of instructions and information. Instead of dealing with several parties

(and possibly a greater number, if AWB's monopoly position is revoked), carriers will only need to negotiate with CBH.

- 3.37 An independent 'Freight Fund' will be established in the main rail and road export agreements. The Freight Fund will be based on the mechanics of the previous 'Rapid Rail Loading Fund' which was set up under the 1996 Western Australian rail agreement. Whilst CBH will manage and administer the Freight Fund, all cash flows in and out of the fund will be independently audited by external auditors. All transactions will be transparent. An annual financial report will be provided to the National Agricultural Commodities Marketing Association (**NACMA**), WAFF and PGA, which will detail the financial position of each year's freight collections and payments. In addition:
- (i) CBH's goal is to have a single set of annual freight rates;
 - (ii) by 1 November each year, CBH Operations will aim to notify the market of the coming year's freight rates. Marketers will be able to post prices at desired Destination Sites net of freight. A freight estimate will be provided earlier than the date of the fixed freight rate;
 - (iii) road freight rates will be calculated using a distance matrix and a based dedicated fleet, net tonnes per kilometre (**NTKS**), including an expected proportion of the more expensive 'spot tender' work;
 - (iv) the risk of fuel price changes may be hedged (for no profit) to avoid the need for monthly fuel rate adjustments;
 - (v) all domestic Destination Site choices are to be quoted a road freight rate based on the NTKS matrix, rather than the differences between Grower freight deductions;
 - (vi) essential and extraordinary harvest movement cost estimates will now be fully incorporated into the visible freight rates³⁹;
 - (vii) an administration and audit, early payment discount and bad debt recovery estimate will be incorporated into the freight rates;
 - (viii) an interest charge to cover the delay in receipt of receival charges caused by Grain Express may be incorporated into the freight rates. Freight interest earned from freight collection upfront will be returned to the Freight Fund; and
 - (ix) a risk premium will be incorporated into the freight rates to cover evolving harvest estimates.
- 3.38 It is intended that deductions to freight rates will be made from any previous years' surpluses (plus interest earned, plus any rail volume rebate) to reduce future years' freight rates in a rolling manner. For example, a \$2 million Freight Fund surplus may be reallocated at 60% in Year 1, 35% in Year 2 and 5% in

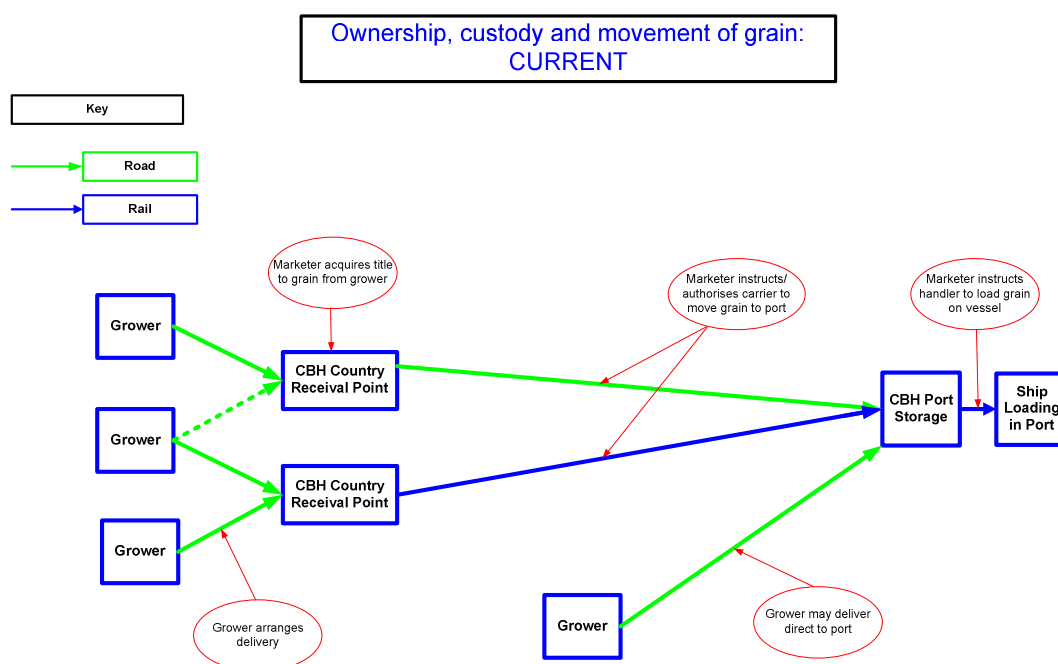
³⁹ This ensures that freight costs, such as the cost of the dedicated fleet, will be transparently charged and disclosed to supply chain participants. One of the existing sources of inefficiency in the current system is that CBH is partially absorbing dedicated fleet costs, which effectively transfers supply chain costs to CBH members, with no reference to the actual use of the supply chain by those members.

Year 3. This has the effect of insuring against future bad harvests, and reducing what would otherwise be inflated rates in poor years. The Freight Fund would have the effect of smoothing freight rates.

3.39 Figure 3.1 below describes the current bulk grain export Supply Chain in terms of the ownership, custody and movement of grain. Note that:

- (i) the Marketer acquires grain at the Receival Point, at the same time that CBH takes custody;
- (ii) the Marketer acquires rail and road services between the Receival Point and the Port (or other destination. Presently, AWB asserts that this confers upon it the ability to control the movement of grain between the Receival Point and Port.

Figure 3.1 – Ownership, custody and movement in current bulk grain Supply Chain



3.40 Figures 3.2 and 3.3 below describe the Grain Express export grain Supply Chain in terms of the ownership, custody and movement of grain. Notable changes from the current Supply Chain include:

- (i) Marketers will no longer acquire transport from carriers;
- (ii) CBH will supply receival and transport services to Growers up to the point of delivery to Marketers (at an Destination Site, which may be the Port); and
- (iii) CBH supplies storage and handling and transport services to Marketers from the Receival Point to the Destination Site; and

- (iv) if a Marketer wishes outturn grain at a different Destination Site to that nominated at the time of sale (say, for example to a Port Destination Site), CBH supplies transport services to the Marketer from the Destination Site to Port and charges those fees to the Marketer.

Figure 3.2 - Ownership, custody and movement in Grain Express: Example 1 –
Grower chooses price at Destination Site

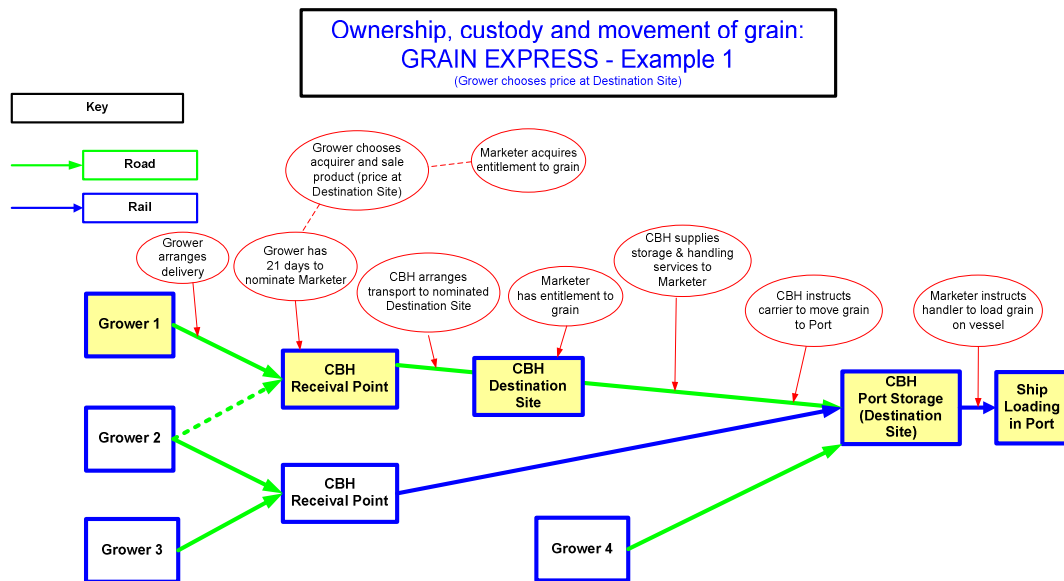
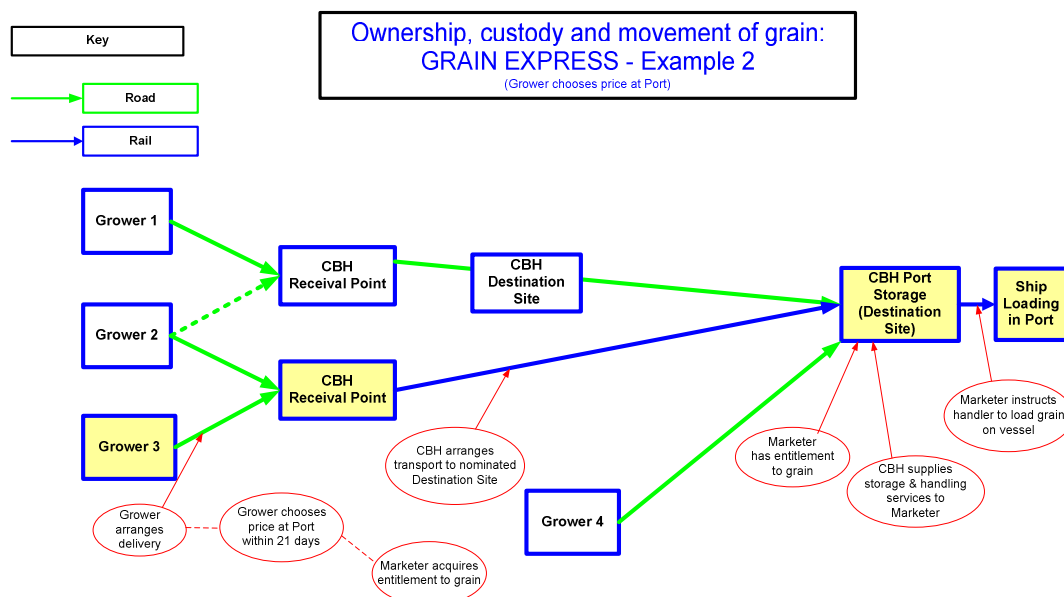


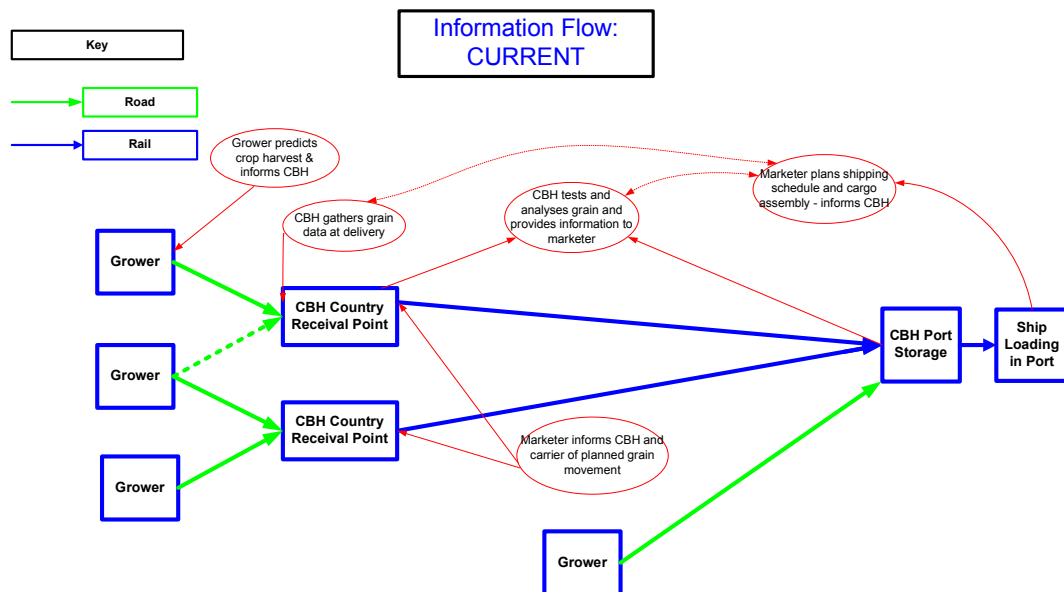
Figure 3.3 - Ownership, custody and movement in Grain Express: Example 2 –
Grower chooses price at Port



Information flows

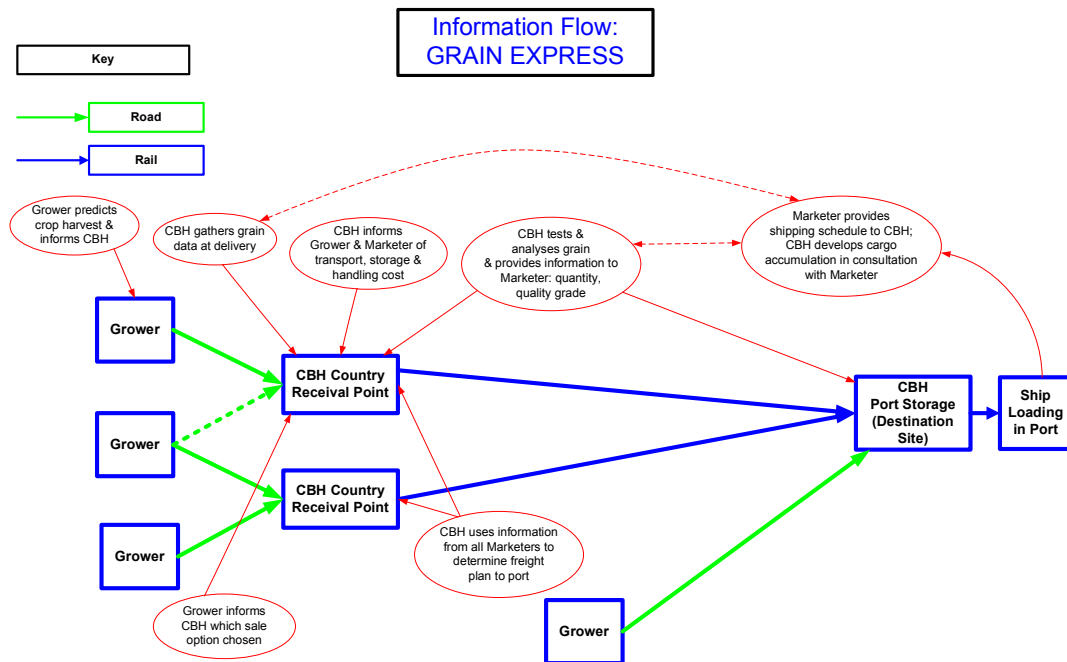
- 3.41 The impact of CBH's proposed changes may be described in terms of the movement of information (which is key to both competitive neutrality and efficiency), and the organisation of logistics planning. The following paragraphs and diagrams show how the proposed changes provide decision makers with better information and ensure that those in control of the Supply Chain have a real stake in reducing costs and promoting efficiency.
- 3.42 Because CBH is the central hub for grain load and vehicle movement information, it will be in a unique position to align this data in order to:
- (i) better coordinate the interaction of transport and handling; and
 - (ii) provide Marketers and transporters with accurate and disaggregated information regarding the freight costs involved in moving grain.
- 3.43 Because CBH is the collector and custodian of the detailed information concerning the location, quality and other attributes of grain across the entire Supply Chain, it is the ideal entity to plan the accumulation of grain for export shipping, according to the specifications of the Marketer.
- 3.44 In the current system, Marketers asserts control over cargo accumulation, and use contractual and financial power over transporters to do so. Each Marketer has access to some, but not all, relevant information and lacks information about the stocks and outturn plans of other participants. Marketers have no ability to appreciate the impact of grain movements upon other members of the Supply Chain.
- 3.45 If, in the future grain Supply Chain, there will be several bulk wheat Marketers and each of these asserts control over site accumulation, a substantial administrative and logistical burden will arise for CBH as it attempts to reconcile the potentially conflicting accumulation plans of multiple export wheat Marketers. The proposed changes enable CBH to develop and implement site accumulation plans with the benefit of near-perfect information over the entire Supply Chain. Marketers will have the opportunity to contribute to the accumulation plan.
- 3.46 Another feature of the proposed Supply Chain is the ability of CBH to provide greater information to transporters and Growers. Under the present structure, AWBS does not provide load-by-load information to enable transport invoices to be reconciled with specific parcels of grain. As a result, there is sub-optimal transparency which prevents Supply Chain participants from properly analysing Supply Chain costs.
- 3.47 Information flows are part of the picture, but in Supply Chain logistics, it is also important to examine the impact of changes upon the structure and timing of planning. Figure 3.13 below describes the key planning steps in the current Supply Chain.
- 3.48 Figure 3.4 below, describes the flow of information in the current export grain Supply Chain.

Figure 3.4 - Information flows in the current Supply Chain



- 3.49 Note that, as this diagram illustrates, CBH occupies the central position in that it is the common party to the great majority of information exchanges occurring within the system. Marketers have information on their own shipping requirements and grain haulage but they cannot see the whole Supply Chain and have no idea how ad hoc grain movements affect other participants.
- 3.50 Note also that Growers do not have access to information about Supply Chain costs, including freight costs for specific movements of grain. This affects their marketing and delivery decisions.
- 3.51 Carriers are receiving distinct (and potentially conflicting) information from CBH and Marketers.
- 3.52 Figure 3.5 below, describes the flow of information in the Grain Express export grain Supply Chain.

Figure 3.5 - Grain Express information flows



3.53 In Grain Express,:

- (i) Marketers (including GPPL) do not have access to the confidential information of other Marketers;
- (ii) Growers have accurate and transparent information about Supply Chain costs;
- (iii) CBH has a complete set of information regarding grain outturn requirements in the entire system;
- (iv) carriers receive instructions and information only from CBH;
- (v) Marketers price grain according to where they want it outturned, not where it is delivered;
- (vi) Marketers will be able to trade grain unencumbered at Destination Sites with confidence;
- (vii) in Grain Express, all Marketers gain access to CBH port terminals for the outturn of bulk grain.

Financial structure

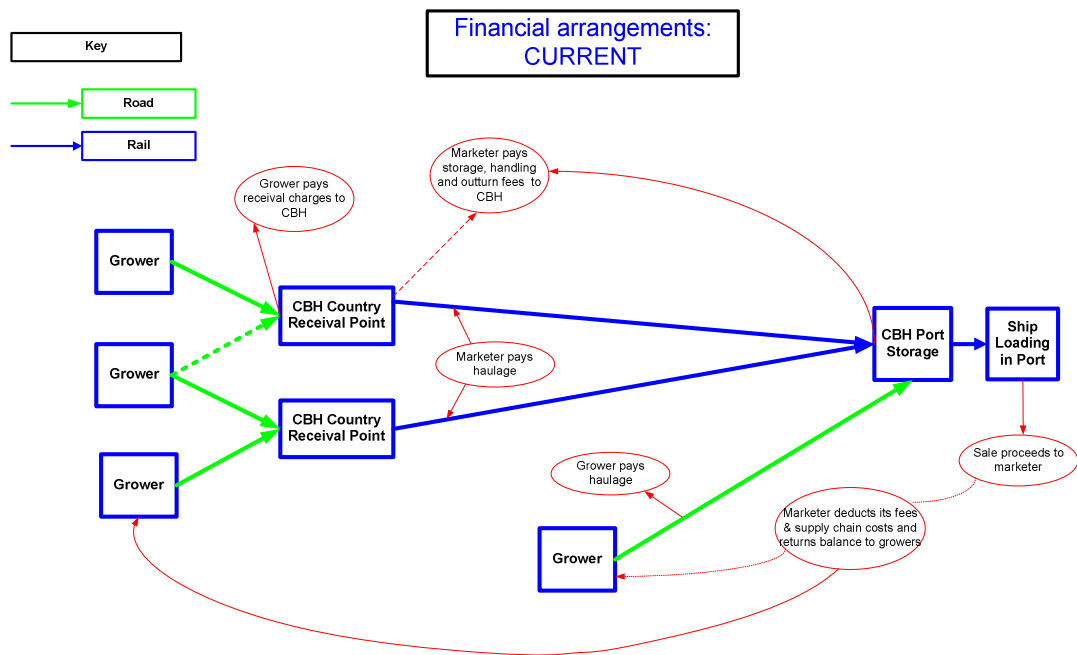
3.54 The key changes to the flow of money under Grain Express include:

- (i) CBH will incur freight costs and then invoice Growers or Marketers for movement of their grain in a transparent cost-recovery basis; and
- (ii) Growers will not have freight and logistics costs deducted from payments but instead, will be invoiced for grain movements up to the Destination Site (in most cases, this will be the port).

3.55 Instead of Marketers retaining control of carriers through its position as the party controlling payments for freight services, CBH will control the payment of freight invoices. CBH will require payment for those services pursuant to Regulation 19(1)(b) of the Bulk Handling Regulations, which requires a Warrant Holder to “*bear any transport charges incurred in respect of grain obtained from [CBH]*”.

3.56 Figure 3.6 below describes financial arrangements in the current Supply Chain.

Figure 3.6 - Financial arrangements in current bulk grain Supply Chain (timing of payments)

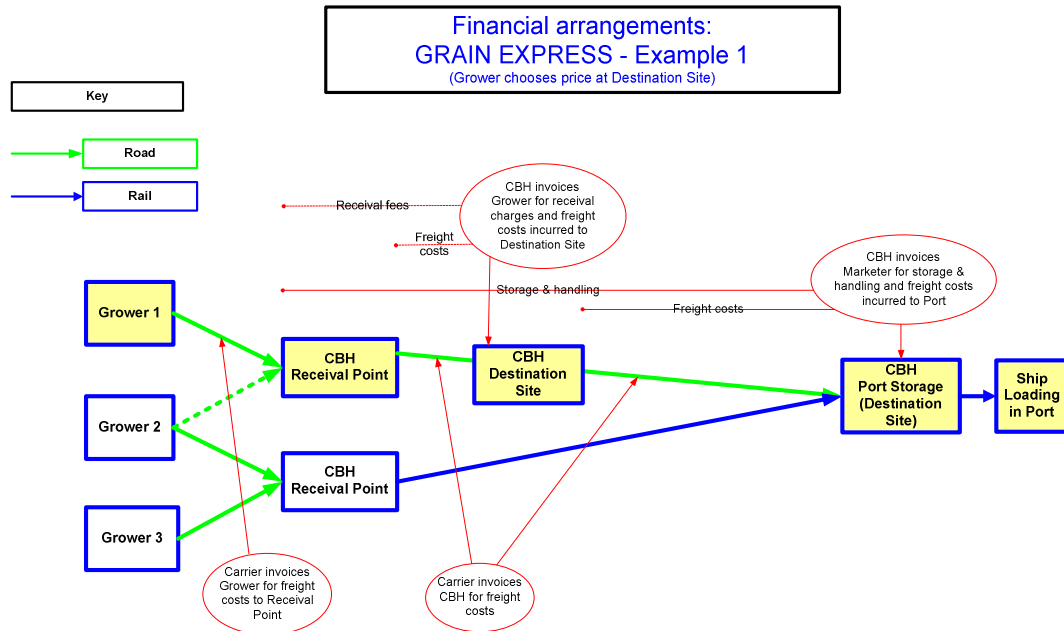


3.57 Note that transport, storage and handling fees are charged to the Marketer, which deducts them from payments to Growers. This structure lacks transparency and fails to assist Growers in making marketing and delivery decisions.

3.58 Figure 3.7 below describes financial arrangements in the Grain Express Supply Chain. Note that, by contrast with the current structure:

- the Growers have a choice of marketing options, and in the example shown, opts for a price on the basis that the Marketer may outturn at an inland Destination Site;
- the Grower is charged a receival fee and is also invoiced for freight to the Destination Site; and
- the Marketer decides to change the outturn point to port and is invoiced freight to port (note, however, that in the elapsed time, the Marketer bears the risk of a change in freight rates).

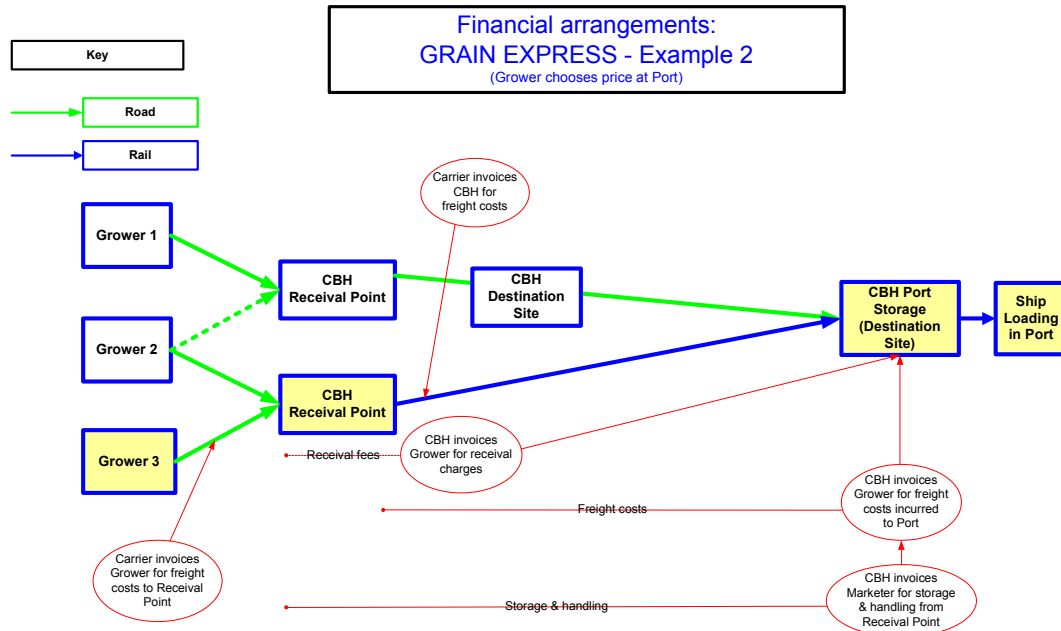
Figure 3.7 - Financial arrangements in Grain Express: Example 1 – Grower chooses price at Destination Site



3.59 Figure 3.8 below describes financial arrangements in the Grain Express Supply Chain if the Grower chooses a price at port. In this illustration:

- (i) the Grower is charged a receival fee and is also invoiced for freight to the Destination Site at port;
- (ii) the Marketer is invoiced for time-based storage from the nomination date and handling fees from the Destination Site to the port.

Figure 3.8 - Financial arrangements in Grain Express: Example 2 – Grower chooses price at Port



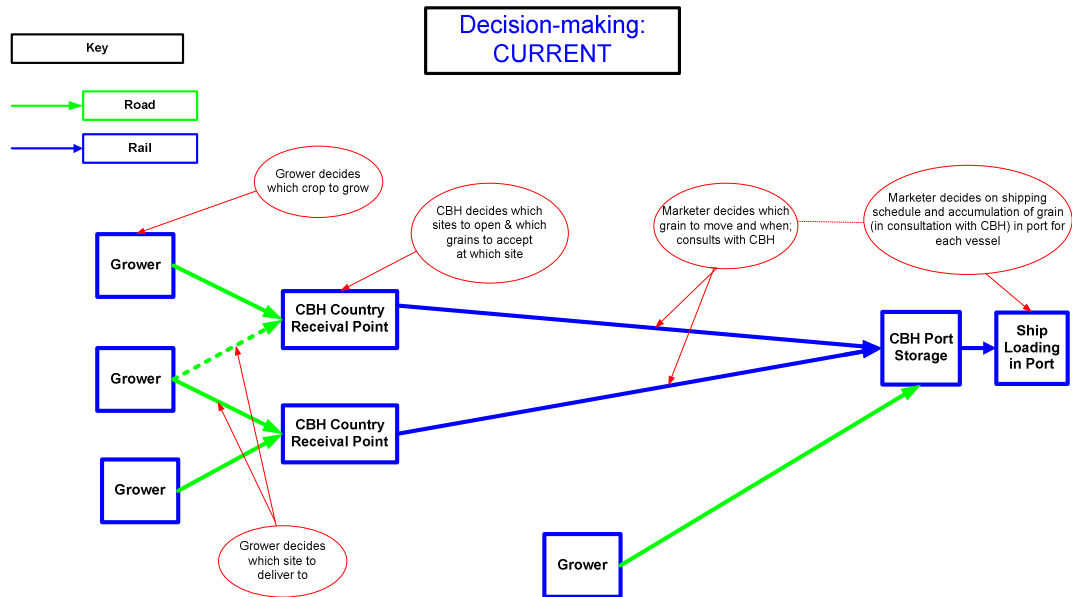
Decision-making

3.60 Decision-making is closely related to the contractual structure, financial structure and information flows. Figure 3.9 below describes decision-making in the current Supply Chain.

3.61 Note that:

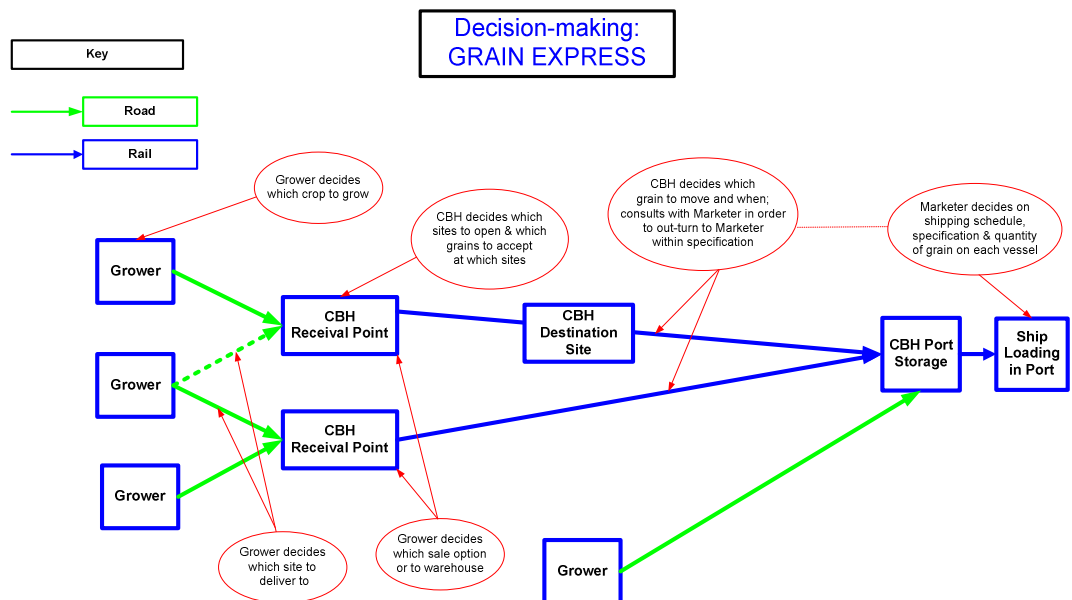
- (i) the Marketer purports to determine cargo assembly, despite its lack of knowledge of the complete Supply Chain, including:
 - (A) other Marketers' movements from the same sites;
 - (B) the available stocks of grain in CBH storage at Port
 - (C) transport resources available, versus transport resources already in use; and
 - (D) fumigation protocols.
- (ii) CBH will potentially have to deal with conflicting instructions from multiple Marketers in an interdependent system.

Figure 3.9 - Decision-making in the current Supply Chain



3.62 Figure 3.12 below describes decision-making in the Grain Express Supply Chain. Note that CBH, which is in possession of information concerning the stocks of all parties, the shipping schedules of the Marketers and the forecasts of Growers, makes the cargo accumulation and transport decisions.

Figure 3.10 - Decision-making in Grain Express



4 Characterisation of conduct

Summary of characterisation

- 4.1 CBH submits that the correct characterisation of the Grain Express conduct is that it is “full line forcing” that falls within section 47(2) of the TPA. In substance, CBH will offer to supply storage and handling services on the condition that Growers or Marketers acquire Supply Chain coordination services from CBH and, to the extent that grain remains in CBH’s custody, that they acquire transport services from CBH (through its nominated carrier).

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5 Relevant markets

Approach to market definition

- 5.1 An appropriate approach to market definition in relation to proposed exclusive dealing begins with a consideration of the goods and services that are subject to the relevant conduct.
- 5.2 As the ACCC has previously noted, in some cases it is not essential to define relevant markets with precision. CBH submits that this is such a case, because the effect of the relevant conduct on relevant markets and the claimed public benefits do not materially differ with the possible alternative market definitions. CBH’s conduct will have effect throughout Western Australia and the most relevant services to be considered in this notification (storage and handling) are equally affected in each of the port zones and in all places in which services are supplied (Receival Points, Destination Sites and Port Facilities). The claimed public benefits are similarly derived and distributed across the entire grain Supply Chain in Western Australia.
- 5.3 To assist the ACCC in applying the statutory tests, CBH summarises the relevant services and their substitutes and then states some assumed roughly defined markets for the purpose of analysis. In doing so, we note the definition of a market in section 4E of the TPA and explained in the QCMA⁴⁰ case, in which the Tribunal stated:

“We take the concept of a market to be basically a very simple idea. A market is the area of close competition between firms or, putting it a little differently, the field of rivalry between them. (If there is no close competition there is of course a monopolistic market.) Within the bounds of the market there is substitution – substitution between one product and another, and between one source of supply and another, in response to changing prices. So a market is the field of actual and potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long run, if given a sufficient price incentive. Let us suppose that the price of one supplier

⁴⁰ Re Queensland Cooperative Milling Association Limited (1976) 25 FLR 169 at 190.

goes up. Then on the demand side buyers may switch their patronage from this firm's product to another, or from this geographic source of supply to another. As well, on the supply side, sellers can adjust their production plans substituting one product for another in their output mix or substituting one geographic source of supply for another. Whether substitution is feasible or likely depends ultimately on customer attitudes, technology, distance and cost and price incentives."

- 5.4 In relation to CBH's proposed conduct, the relevant services may be divided into categories as follows:
- (i) grain trading;
 - (ii) grain storage and handling;
 - (iii) transport (including bulk rail and road); and
 - (iv) Supply Chain logistics and management.

Grain storage and handling

- 5.5 Geographically, grain storage and handling services are supplied within the State of Western Australia or, on a narrower view, within each of the four port zones. Grain from Western Australia is rarely, if ever, stored and handled using facilities outside the State.
- 5.6 Storage and handling facilities may be categorised as follows:
- (i) country receival and storage facilities;
 - (ii) larger, primary storage and handling facilities; and
 - (iii) port storage and ship loading facilities.
- 5.7 From the demand side, Growers and Marketers approach the services supplied by means of these facilities in different ways. Growers determine which receival point to deliver grain to based upon the quality of their grain, the service available and price of receival charges at each site. To this extent, country sites within a reasonable road haulage radius would be regarded by Growers as substitutes.
- 5.8 Marketers view the storage and handling infrastructure from the perspective of their own grain stocks and shipping requirements.. They acquire storage and handling services from CBH according to these requirements and are supplied with services at Receival points, Destination Sites and Port Storage and Loading Facilities.
- 5.9 CBH owns the up-country network of facilities and the port storage and loading infrastructure across the entire State. At present, there appears to be no real likelihood of duplication of those facilities by a new entrant, though it is conceivable that country storage facilities might be economic to duplicate.

Freight haulage

- 5.10 In the ACCC's Determination in relation to the Export Grain Logistics Joint Venture⁴¹ in eastern Australia, the ACCC examined competition issues in transport in terms of the State-based markets for grain rail freight, on the basis that:
- (i) in eastern Australia, rail freight is the foremost means of transporting bulk grain, especially for export;
 - (ii) over 95% of all export grain is moved by rail;
 - (iii) road haulage is not substitutable with rail for the transport of bulk grain over medium to long distances, due to the high volumes involved and relative speed of rail for bulk grain movement.
- 5.11 In Western Australia, there is evidence that in some circumstances, road services are substitutable and price-competitive with rail. The picture is also complicated by the fact that 42 of the 200 receival sites in Western Australia are off-rail, served exclusively by road.
- 5.12 The Western Australian Strategic Grain Infrastructure Study of 26 April 2005 states that:
- (i) approximately 17% of CBH's country receivals over the past five years have been at road sites;
 - (ii) Grower deliveries by road direct to ports amount to 17-19% of total receivals;
 - (iii) road access to ports other than Kwinana is very good;
 - (iv) five year average road site mode tonnages have increased at a greater rate than rail over the period from 1995/9 to 2000/04 and are projected to gain a slightly increased share in the future;
 - (v) the average haul distance for Western Australian grain on rail is 290 kilometres, almost double the average haul from road sites. Of the total farm to port (and domestic consumer) task, rail currently accounts for approximately 70% of all NTKS;
 - (vi) road freight is now competitive with rail on price, if not scale, in most areas of the State⁴².
- 5.13 Grain Express aims to provide a positive and sustainable environment which fosters investment in Western Australian grain transport service providers. The proposal aims to avoid the chaotic situation that occurred in New South Wales and Victoria over the last 12 months, which culminated in the rail service

⁴¹ C2004/1418.

⁴² Western Australia Strategic Grain Infrastructure Study (2005), 33.

provider (Pacific National) announcing its withdrawal from the grain storage network in December 2007⁴³.

- 5.14 We therefore conclude that in Western Australia, while rail has traditionally been the primary means of transport used for bulk grain, road has become increasingly competitive and must be considered in one or more of the following ways:
- (i) as an external constraint upon players in a State-based rail market;
 - (ii) as a close substitute in a converged State-based bulk grain transport market; or
 - (iii) as a close substitute in a number of regional or point to point bulk grain transport markets within each port zone.
- 5.15 On any of these views, it is clear that the monopoly above-rail provider, QR, has a significant power. Road, due to its lower barriers to entry, provides a constraint in many areas, but in some areas, there is no substitute for rail.

Export grain marketing

- 5.16 Grain trading involves the acquisition of grain or rights to grain by Marketers, end-users and other parties seeking to derive revenue or address risk exposure by trading in grain.
- 5.17 Due to the legislative and regulatory regimes in place in relation to bulk export grain, there is some degree of separation between trading in various grains. The core services appear closely related, being comprised of acquisition, sale and the provision of related financial services.
- 5.18 Geographically, the proposed conduct is likely to have influence only within Western Australia. Many participants in grain trading operate nationally and the services supplied by grain trading entities also have an international aspect, because grains are global commodities and traders are strongly constrained by global pricing.
- 5.19 However, for the purpose of this analysis, it is appropriate to consider competitive effects by reference to a national market for trading in grain.

Relevant markets

- 5.20 To the extent that this submission addresses competition effects, it does so in terms of:
- (i) markets for the supply of country grain receipt, storage and handling services in Western Australia, or alternatively, in each of the four port zones in Western Australia;

⁴³ ABC News, *Pacific National to sell or close rail freight business* (2007) <<http://www.abc.net.au/news/stories/2007/12/12/2116312.htm>> at 5 May 2008.

- (ii) markets for the supply of bulk grain road haulage services in Western Australia, or alternatively, in each of the four port zones in Western Australia;
- (iii) markets for the supply of bulk grain rail haulage services in Western Australia, or alternatively, in each of the four port zones in Western Australia; and
- (iv) grain trading markets, which may include:
 - (A) a market in Western Australia for the acquisition and supply of wheat; and
 - (B) the market in Western Australia for the acquisition and supply of coarse grains;

As the ACCC noted in its determination in the Export Grain Logistics Authorisation, these markets may have international and domestic components.

6 The factual/counterfactual analysis

Overview

- 6.1 As the ACCC is aware, the Grain Express project will be implemented in the context of substantial change and uncertainty in the Australian grain industry. This creates challenges in addressing public benefit and competition effects, because the counterfactual is difficult to determine.
- 6.2 Australian wheat exports are presently regulated by the WMA and the EWC. However, new wheat export marketing arrangements and legislation are presently under consideration by the government. An assessment of the nature of these changes and their likely effect is necessary for the purpose of determining the appropriate approach to take to the counterfactual analysis.
- 6.3 On 5 March 2008, an exposure draft of the Proposed Act was released for public comment. Changes may be made to the proposed wheat export marketing scheme as a result of public and industry consultations, and the Senate Inquiry by the Rural and Regional Affairs and Transport Committee⁴⁴. At the time of drafting this submission, the EWC was awaiting the outcome of the consultation process, and further policy advice from the government in relation to the proposed alterations to the wheat export scheme⁴⁵.

Current wheat export arrangements

- 6.4 As mentioned above, Australian wheat exports are presently regulated by the WMA and the EWC. The present wheat export arrangements came into effect in mid-2007, following amendments to the WMA. These amendments:
- (i) give the Minister for Agriculture, Fisheries and Forestry the power to appoint a “designated company” to manage the Single Desk for bulk wheat exports. This power came into effect on 1 March 2008 and will sunset on 30 June 2008⁴⁶; and
 - (ii) established the EWC on 1 October 2007 to replace the Authority. Under the WMA, the EWC has 3 main functions:
 - (A) controlling bulk wheat exports;
 - (B) monitoring and reporting on the performance of the Single Desk company (AWBI); and
 - (C) administering the non-bulk wheat quality assurance scheme.
- 6.5 There are 2 categories of export wheat under the WMA – bulk export wheat, and non-bulk export wheat. Non-bulk export wheat refers to wheat that is

⁴⁴ Export Wheat Commission, *Export Wheat Accreditation Scheme* (2008) <<http://www.ewc.gov.au/WheatExportAccreditationScheme.html>> at 1 May 2008.

⁴⁵ Ibid.

⁴⁶ *Wheat Marketing Act 1989* (Cth), section 3AA.

exported in a bag or container that is capable of holding not more than 50 tonnes of wheat⁴⁷.

- 6.6 Under the WMA, the export of bulk wheat requires valid consent from EWC. Section 57(1) of the WMA provides that a person cannot export bulk quantities of wheat unless the EWC has first given its written consent to that export. Before giving its consent, the EWC must first consult the AWBI, as the designated Single Desk company, and obtain its consent in writing to the export⁴⁸.
- 6.7 One important change to the WMA in 2007 concerned the export of non-bulk wheat. Since 27 August 2007, the WMA deregulated the export of non-bulk wheat. This means that the export of wheat in bags and containers does not require the consent of the EWC. However, wheat which is exported in bags or containers must comply with the non-bulk wheat quality assurance scheme which is specified in the WMA⁴⁹.

Proposed changes to wheat export arrangements

- 6.8 The exposure draft of the Proposed Act was released for public comment on 5 March 2008. The Proposed Act is intended to replace the WMA which is currently in force.

Purpose of Proposed Act

- 6.9 Section 3 of the Proposed Act provides a simplified outline of the Proposed Act's intended operation. It states that:
- (i) the Proposed Act sets up a system for regulating exports of wheat (other than wheat in bags or containers);
 - (ii) exporters of wheat must be accredited under the wheat export accreditation scheme (**Scheme**);
 - (iii) an exporter will not be eligible for accreditation unless the exporter is a company that satisfies the eligibility criteria set out in the Scheme;
 - (iv) the eligibility criteria include being a fit and proper company;
 - (v) an accredited wheat exporter must comply with conditions of accreditation (including reporting conditions).
 - (vi) a new body, Wheat Exports Australia (**WEA**), will administer the Scheme in place of the present EWC;
 - (vii) WEA will have power to:
 - (A) obtain information from accredited wheat exporters; and
 - (B) direct the audit of an accredited wheat exporter.

⁴⁷ Wheat Export Marketing Bill 2008 (Cth), section 6(2).

⁴⁸ *Wheat Marketing Act 1989* (Cth), section 57(3A), (3B).

⁴⁹ *Wheat Marketing Act 1989* (Cth), section 66, 67.

- (viii) the Minister may direct WEA to carry out an investigation;
- (ix) WEA will report to Growers on an annual basis.

Accredited wheat exporter

- 6.10 Pursuant to section 6(1) of the Proposed Act, wheat exporters must be accredited under the Scheme in order to export wheat. Section 6(3) provides that it is an indictable offence to export wheat without being an accredited wheat exporter.
- 6.11 Section 6(2) provides that accreditation under the Scheme is only required for the export of wheat which is not in a bag or a container capable of holding more than 50 tonnes of wheat.
- 6.12 Pursuant to section 10, accreditation under the Scheme is not transferable.

Eligibility for accreditation

- 6.13 Section 11(1) sets out the requirements for accreditation under the Scheme. A company is not eligible for accreditation unless:
 - (i) the company is registered as a company under Part 2A.2 of the *Corporations Act 2001* (Cth) (**Corporations Act**), and
 - (ii) the company is a trading corporation to which paragraph 51(xx) of the Constitution applies;
 - (iii) WEA is satisfied that the company is a fit and proper company, having regard to 17 individual criteria.

Key difference between current and proposed wheat export arrangements

- 6.14 The key difference between the current and proposed wheat export arrangements is the requirement under the Proposed Act that a company must be accredited by WEA (as the regulator) in order to export bulk wheat. Accreditation is not required under the current scheme – the consent of the EWC is all that is necessary at present to export bulk wheat.
- 6.15 The eligibility criteria for accreditation under the scheme⁵⁰ covers a broad range of matters, such as financial resources available to the company and whether the company's directors have been convicted of an offence. Meeting and/or demonstrating the criteria for accreditation may result in greater costs for companies seeking to export bulk wheat than is presently the case with seeking EWC consent to bulk exports. However, the trade-off in relation to accreditation appears to be that, once accredited, a company will no longer have to seek the regulator's consent each time it wishes to export wheat in bulk.
- 6.16 It is likely that further fundamental differences between the current and proposed schemes will become apparent when the terms of the Proposed Act have been finalised.

⁵⁰ Wheat Export Marketing Bill 2008 (Cth), section 11.

Implications for the Supply Chain

- 6.17 It is difficult to predict with any degree of certainty the precise impact the proposed amendments to the wheat export marketing arrangements may have on the Grain Express project. This is because the Proposed Act has not yet been finalised, and is likely to be subject to further alterations in any event.
- 6.18 However, based on the terms of the Proposed Act as it presently stands, there may be several implications for the efficiency of the Supply Chain if the present structure is unchanged. As is described in the earlier summary of the Supply Chain, the current structure positions AWBS as the major acquirer of freight services under industry agreements and a central figure in Supply Chain coordination.
- 6.19 If, as appears likely, the Single Desk will be partially deregulated, resulting in several bulk wheat exporters in competition, the Supply Chain coordination task will increase in complexity. CBH considers that, if multiple export licences are issued, and each licence holder asserts control over grain movements between silo and port, the inefficiency in the current task will increase exponentially when licence holders require grain movements without reference to the efficiency of the Supply Chain as a whole. In addition, if each licence holder acquires freight independently:
- (i) the freight rates for the total task may increase, due to each acquirer lacking volume;
 - (ii) it is unlikely that the fixed cost component of the freight task can be insured, as no participant will be able to guarantee any volume of grain on the network;
 - (iii) possible grain leakage from rail serviced sites to move by road, therefore continuing to weaken the confidence of the rail operator to invest in the grain network leading to road congestion and environmental and social impacts; and
 - (iv) supply chain bottlenecks may develop as a result of each marketer potentially seeking grain from different storage sites.
- 6.20 The second implication concerns the access test in relation to port terminal services which is set out in section 20 of the Proposed Act.
- 6.21 Pursuant to section 11(1)(e) of the Proposed Act, one criterion for eligibility for accreditation under the Scheme is that if the company applying for accreditation (or a related body corporate) is a provider of a port terminal service, WEA must be satisfied that the company or the related body corporate passes the access test (set out in section 20) in relation to that service.
- 6.22 CBH, as a related body corporate of GPPL, would therefore be required to pass the access test in section 20. Under the access test, an access undertaking must be in place under Division 6 of Part IIIA of the TPA after 1 October 2009.

- 6.23 Pursuant to the Bulk Handling Act, CBH is presently required to provide open and fair access to all of its customers at its ports and facilities. As this submission makes clear, Grain Express will create greater structure and certainty around this obligation, with CBH formalising its ring-fencing structure and standardising terms and conditions. In substance, Grain Express will satisfy much of the rationale for regulated access to its services. However, unlike the proposed access undertaking requirement, Grain Express will facilitate access to all of CBH's services.

Circumstances without the conduct

- 6.24 The current industry rail freight agreement was due to expire in October 2007 but was extended by 12 months, pending the outcome of the Government's proposed changes to the export licensing structure.
- 6.25 If, as seems possible, the Single Desk model is eroded, with the result that several large Marketers share the export wheat task, the demands of the coordination function will grow in complexity. If this occurs, CBH submits that the current model will not be sustainable. The following things are likely to result:
- (i) AWB will not regard its current position as a principal party to the industry transport arrangements as sustainable;
 - (ii) It is not clear whether AWB would continue to assert the right to direct ad hoc grain movements, at the potential expense of its competitors; and
 - (iii) other Marketers will seek to put in place their own arrangements, with the result that several Marketers may exert influence over grain movements.
- This would be akin to several people trying to steer the same vehicle, each in a different direction. With no single party willing to commit volumes to the rail freight provider, charges for rail will inevitably increase, and branch lines may close.
- 6.26 This submission assumes that, without the notification, Marketers will acquire freight services from carriers directly, and will continue to substantially determine or influence cargo assembly decisions.
- 6.27 In short, this submission posits that, without the authorised conduct, Marketers are likely to continue to assert control or strong influence over the movement of grain in CBH's custody.
- 6.28 With the likely increase in the number of export wheat Marketers in the next year, central and efficient coordination of the grain supply chain is urgently required.
- 6.29 The consequences of inaction will be serious, and possibly permanent. Immediate consequences of retaining the status quo for the coming harvest will include not only a continuation of the current inefficiencies but a substantial

escalation in them as CBH and ARG struggle to deal with the competing demands of multiple large scale Marketers and Growers.

- 6.30 The industry rail freight agreement will expire in October 2008, having already been extended by one year from its original expiry in 2007. As the March 2008 report of the 2008 GIG Report states, the rail network is barely viable and leakage of the grain task to road further deteriorates the relative competitiveness of the rail network. Once closed, rail lines are rarely recommissioned. The 2008 GIG Report concludes:

“With the deregulation of grain marketing resulting in fragmentation of the supply chain tasks and without significant urgent actions inevitable closure of the entire 2300 kilometre grain branch line network will result.”

Circumstances with the conduct

- 6.31 If the notification is not revoked, and CBH proceeds to implement Grain Express, CBH will occupy the Supply Chain coordination role for all grain held in its custody.
- 6.32 This enables CBH to take four important steps:
- (i) CBH will negotiate haulage agreements with carriers with a high level of confidence in relation to expected volumes of grain. While new entry in storage and handling remains as possible as it always has been, such a change would take time. CBH may therefore project forward volumes in the short to medium term with some confidence;
 - (ii) CBH will be able to acquire insurance to protect against the risk of the fixed cost component of freight rates becoming unaffordable in low harvest years;
 - (iii) CBH is in a position to deal on a non-discriminatory and commercially congruent fashion with multiple Growers and Marketers, while offering Growers and Marketers the benefit of the high volume haulage rates CBH has negotiated with carriers; and
 - (iv) CBH will ensure that all their contracted transporters comply with quality assurance requirements to protect Growers and Marketers within the Supply Chain. Having the full Supply Chain covered under a HACCP-accredited system provides confidence to all stake-holders.
- 6.33 The likely outcomes of Grain Express in terms of competition, efficiency and public benefit are addressed in the following sections.

7 Public benefits

- 7.1 The TPA does not define the term “benefit to the public”, although it does provide that the ACCC will regard the following as public benefits:
- (i) a significant increase in the real value of exports; and
 - (ii) a significant substitution of domestic products for imported goods⁵¹.
- 7.2 The ACCC must also take into account all other matters that relate to the international competitiveness of any Australian industry⁵².
- 7.3 The Australian Competition Tribunal has defined public benefit as including:
- “anything of value to the community generally, any contribution to the aims pursued by society (in the context of trade practices legislation) the achievement of the economic goals of efficiency and progress.”*⁵³
- 7.4 The ACCC’s Draft Guidelines for Authorisation⁵⁴ state that the ACCC considers that all efficiency gains constitute public benefits. However, in determining how much weight will be given to efficiency benefits, the ACCC will consider:
- (i) has sufficient evidence been presented concerning the size of the benefit?
 - (ii) is the gain sufficiently certain?
 - (iii) will gains be offset by losses also resulting from the conduct?
 - (iv) who are the beneficiaries of the gains?
- 7.5 On this last point, there is an issue as to whether gains to producers (and their shareholders) should be given the same weight as gains passed through to consumers. The ACCC’s Draft Guidelines state that:
- “Cost savings arising from increases in productive efficiency constitute public benefits, as the community at large has an interest in resource savings because these savings are released for use elsewhere in the economy.”*

Types of benefit

- 7.6 The primary public benefits produced by the proposal concern the increased efficiency of the Supply Chain. These efficiencies are likely to have a direct and beneficial impact on Australia’s exports⁵⁵. The ACCC acknowledged that

⁵¹ *Trade Practices Act 1974* (Cth), section 90(9A)(a).

⁵² *Trade Practices Act 1974* (Cth), section 90(9A)(b).

⁵³ *Re Queensland Co-operative Milling Association Ltd* (1976) 25 FLR 169.

⁵⁴ February 2006.

⁵⁵ *Trade Practices Act 1974* (Cth), section 90(9A) requires the ACCC to regard a significant increase in the real value of exports as a benefit to the public.

efficiencies of this kind were to be regarded as public benefits in its determination to authorise the Export Grain Logistics joint venture.

7.7 As Appendix 1, the Synergies report concludes, the proposed conduct will result in a range of benefits, including:

- (i) more efficient grain delivery and handling at Receival Points, including:
 - (A) increased speed of receival, leading to deferred capital expenditure and more efficient investment;
 - (B) better information on marketing options and more time to decide on those options for growers;
 - (C) reduced errors in nomination of marketing options by growers; and
 - (D) increased automation of the receival process;
- (ii) better coordination of storage and handling, including:
 - (A) reduced opening of bulkhead storages;
 - (B) better use of labour force (less mobilisations, reduced overtime and better rostering);
 - (C) reduced loss by division;
 - (D) reduced risk of phosphine resistance;
- (iii) improved efficiency of transport task, including:
 - (A) enhanced rail efficiency, with increased use of unit trains;
 - (B) below rail cost savings through better utilisation, such as possible deferred capital expenditure;
 - (C) certainty of volume on rail;
 - (D) insurance risk sharing;
 - (E) simplified operational interface between carrier and CBH;
 - (F) better negotiation capacity;
 - (G) greater transparency of costs to Growers; and
 - (H) a real likelihood of preserving the viability of the rail network;
- (iv) enhanced port efficiency, including:
 - (A) better utilisation of infrastructure; and
 - (B) reduced demurrage;
- (v) dynamic efficiency gains, which improve the prospect of efficient investment in infrastructure in future; and
- (vi) better marketing decisions for Growers and Marketers.

- 7.8 Grain Express will better align the incentives of the suppliers of Supply Chain services with Growers. CBH, a Grower owned cooperative at the operational centre of the Supply Chain, has a clear incentive to reduce Supply Chain costs. This fact is illustrated by the commitment of CBH to pass freight costs to Growers and Marketers in a transparent form without adding a profit margin.
- 7.9 These benefits are referred to in Part 5 of the Synergies Report, and the sources and primary evidence also stated in that report.

Causation of benefits

- 7.10 CBH considers that each of the benefits referred to above, and in the Synergies Report, are likely to flow from the Grain Express conduct and that, without the Grain Express conduct, it is unlikely that these benefits could be achieved.
- 7.11 This is because:
- (i) the efficiencies rely on the coordination function being assumed by a single entity;
 - (ii) the best entity to perform that function is the one in physical possession of the grain, which has a complete set of information over the entire Supply Chain;
 - (iii) without the bundling element of Grain Express, Marketers are likely to continue to acquire freight in their own right. With multiple Marketers, the freight task is fragmented and the coordination task is unachievable.
- 7.12 **[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]**
- 7.13 **[CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]**
- 7.14 An issue of particular significance in this respect is the preservation of network pricing for the rail freight task. Network pricing recognises the value of capturing volume on rail and the risk that, when volume is moved to road, the rail system risks being uneconomic as a whole, and road, while initially competitive, will quickly cost the same if not more, including in community detriment⁵⁶.

⁵⁶ Western Australia Grain Infrastructure Group, *A Window of Opportunity – Full Report* (2008).

8 Effect on competition

- 8.1 This notification is made on the basis that CBH's proposed conduct may contravene section 47 of the TPA. However, for several reasons, CBH does not consider that Grain Express, as it is planned to be implemented, will raise serious competition concerns.
- 8.2 This section of the document examines the likely effect of CBH supplying its storage and handling services on condition that Marketers also acquire transport and logistics services supplied by CBH (using sub-contractors for the transport portion of the services).
- 8.3 In general, the effects of bundling or full line forcing conduct in trade or commerce may be positive or negative for competition, depending upon a range of factors including:
- (i) the structure of relevant markets;
 - (ii) the goods or services in the bundle; and
 - (iii) the pricing and costs of the bundle and its component parts.
- 8.4 Bundling may be beneficial or pro-competitive in some circumstances⁵⁷. In other circumstances, bundling may form part of an entry-deterrence, or market leverage strategy, and create long term anti-competitive effects.
- 8.5 In this case, the proposed conduct has several features that are of particular relevance to its likely effect upon competition.
- 8.6 Firstly, CBH, as a cooperative supplying services to its members, has no incentive to profit maximise to the detriment of Growers. CBH's charges are levied in the following ways:
- (i) Growers are charged receival fees at the discharge grid;
 - (ii) Marketers are charged storage, handling and outturn charges. These charges are passed on to Growers because Marketers deduct them from pool payments or the proceeds of sale.
- 8.7 Therefore, CBH raising prices to Marketers simply raises costs for Growers. As a result, and despite its ownership of most of the storage and handling infrastructure in Western Australia, CBH does not derive supra-competitive profits. On the contrary, CBH is driven by its Grower members to reduce the cost of its services and has achieved the lowest grain storage and handling charges in Australia over a sustained period. **Annexure O** contains two graphs which compare the grain Supply Chain costs in Australian States in 2004/05 and the projected costs for 2007/08.
- 8.8 CBH does not propose to charge additional fees for Supply Chain management and logistics services. This is because CBH considers that any additional

⁵⁷ As the ACCC noted in its Information Paper, *Bundling in Telecommunications Markets* (2003), 5: "Bundling can be beneficial for both consumers and the carrier or CSP supplying the services if it results in significant efficiencies and pro-competitive benefits".

costs incurred in performing this role will be offset by the savings from efficiencies in a more coordinated and integrated Supply Chain.

Issues arising from bundling and Supply Chain integration

- 8.9 CBH's proposed conduct would effectively place it in control of:
- (i) the negotiation of transport contracts for the grain Supply Chain task in relation to grain in CBH's custody; and
 - (ii) the provision of storage, handling, transport and logistics services for most, if not all, grain Marketers in Western Australia.
- 8.10 As a cooperative whose fees represent costs for its members, not only does CBH have no incentive to derive monopoly rents in storage and handling, it will undertake not to add any additional fee or margin in relation to its provision of transport and logistics services.
- 8.11 As an entry-deterrence strategy, the proposed conduct would have no real effect in Western Australia. The Grain Express conduct does not prevent new entrants from building competitive storage or port loading facilities. Nor does the Grain Express conduct prevent Marketers from outturning their grain from CBH's custody at a nominated point, and making their own transport and port loading arrangements. In this sense, Grain Express does not foreclose entry.
- 8.12 As the Synergies Report recognises, the bundling of freight, storage and handling services may in fact provide an opportunity for competitive entry for entrants that may be capable of optimising the trade-offs in the competing supply chain.

Freight market effects

- 8.13 For the purpose of this document, we have defined conservatively narrow road and rail freight markets, yet as the Synergies Report notes, there is a real argument that road and rail are close substitutes in a number of areas. The 2008 GIG Report provides further information on this issue, and notes that road has the benefit of what is effectively a subsidy because many of the real costs of road haulage are not charged to carriers.
- 8.14 There is no prospect of any leverage of power by CBH from a storage and handling market into a bulk grain freight market. CBH proposes to acquire and then offer freight services purely as an incident to delivering Supply Chain efficiency.
- 8.15 CBH owns virtually no infrastructure for the provision of transport services, and does not intend to acquire such a capability. CBH does not propose to charge any additional fee or derive any margin on the transport services it will acquire from carriers. These transport costs will be passed on to Growers and Marketers transparently and without additional cost.
- 8.16 The current industry-based multi-lateral contracts capture a substantial proportion of the Western Australian rail and road freight tasks in the south

west of the State. This contract expires on 31 October 2008 and the parties are currently negotiating a new agreement.

- 8.17 The most direct impact of Grain Express in freight markets will emerge from CBH having increased concentration as an acquirer of haulage in both rail and road⁵⁸. In rail, this increased buy-side concentration is unlikely to lead to concerns because:
- (i) ARG is itself a virtual monopoly;
 - (ii) CBH, ARG and all supply chain participants have a shared interest in preserving the viability of the rail network.
- 8.18 Road carriers are concerned with the long term viability of their businesses, which are currently exposed to substantial risk from grain task volatility and the potential for further risk from the fragmentation of the task. Grain Express will receive the support of road carriers because it provides a model that preserves competition “for the market”, which enables a successful tenderer for a zone contract to plan capital expenditure and secure reliable labour resources.
- 8.19 CBH submits that Grain Express will have a net positive effect on competition in freight markets, because central control of the freight task will maximise competitive tension between road and rail and may also facilitate competitive entry in rail.

Export grain marketing

- 8.20 Assuming that the structure of the Single Desk changes and multiple export grain licences are issued, there would be considerable incentive for incumbent Marketers (such as AWB) to move grain in such a manner as to raise rivals’ Supply Chain costs. This is made more likely if Marketers influence the movement of grain in CBH’s custody. CBH submits that, in such a post-Single Desk environment, it is essential that grain movements are controlled by a single entity, and that Marketers are not in a position to engage in strategic conduct in grain movements to the detriment of their competitors.
- 8.21 Grain Express achieves this, by ensuring that CBH moves grain with the goal of “whole of Supply Chain” efficiency, rather than the narrow self-interest of a single Marketer. Therefore, CBH submits that Grain Express will have pro-competitive effects in grain marketing, by creating a level playing field between Marketers.
- 8.22 CBH is vertically integrated and for this reason, it is important for any proposal that extends the extent of CBH’s supply chain influence to address the potential for CBH to:
- (i) disclose confidential information to GPPL; or
 - (ii) discriminate against the marketing competitors of GPPL (for example, by delivering preferential terms and conditions).

⁵⁸ Note that concentration does not increase if the status quo is the counterfactual but is assumed to increase relative to the without case if grain marketing is further deregulated.

- 8.23 These risks may be effectively dealt with using appropriate information flow and arm's length dealing structures to address decision-making, implement non-discriminatory terms and conditions for users of the system and ensure that information flows are appropriately controlled. These issues are the subject of the measures detailed in Appendix 2. To summarise those measures, CBH will have the following policies in place:
- (i) an information flow policy, which restricts the flow of confidential information between CBH and its related marketing entities, GPPL and AgraCorp Pty Ltd;
 - (ii) standard terms and conditions of supply for storage and handling services; and
 - (iii) a policy of access to CBH's services on non-discriminatory terms and conditions to all Marketers.

9 Glossary

Term	Definition
AQIS	Australian Quarantine and Inspection Service
ARG	Australian Railroad Group
Authority	Wheat Export Authority
AWB	AWB Limited
AWB Group	Refers to the three subsidiaries of AWB Limited: <ul style="list-style-type: none"> • AWB (International) Limited • AWB Services Ltd • AWB Harvest Finance Limited
AWBF	AWB Harvest Finance Limited
AWBI	AWB (International) Limited
AWBS	AWB Services Ltd
AWR	Australia Western Railroad Pty Ltd
Bulk Handling Act	<i>Bulk Handling Act 1967 (WA)</i>
Bulk Handling Regulations	Bulk Handling Act Regulations 1967 (WA)
CBH	Cooperative Bulk Handling Pty Ltd
Cooperative Act	<i>Companies (Co-operative) Act 1943 (WA)</i>
Corporations Act	<i>Corporations Act 2001 (Cth)</i>
EWC	Export Wheat Commission
GIG	Grain Infrastructure Group
2008 GIG Report	Grain Infrastructure Group, <i>A Window of Opportunity – Full Report</i> (March 2008)
GLA	Grain Licensing Authority
GLA license holders	Traders who have been granted licences by the GLA under the Grain Marketing Act
GPPL	Grain Pool Pty Ltd
Grain Marketing Act	<i>Grain Marketing Act 2002 (WA)</i>
HACCP	Hazard Analysis and Critical Control Points
ICS	Intermodal Container Services
ILS	Intermodal Link Services
ITV	Internal Transit Vehicles
MGC	Metro Grain Centre
NACMA	National Agricultural Commodities Marketing Association
NOR	Notice of Readiness

NQRT	North Quay Rail Terminal
NTKS	net tonnes per kilometre
PGA	Pastoralists and Graziers Association of Western Australia Inc
Proposed Act	Wheat Export Marketing Bill 2008 (Cth)
QR	Queensland Rail
SOF	Statement of Facts
SQF code	Safe Quality Food code
TPA	<i>Trade Practices Act 1974</i> (Cth)
WAFF	Western Australian Farmers Federation Inc
WEA	Wheat Exports Australia
WMA	<i>Wheat Marketing Act 1989</i> (Cth)

10 Appendices

- 1 Synergies Economic Consulting Report**
- 2 Ring-fencing Arrangements and Policy**

11 Annexures

- A** – CBH’s Standard Terms and Conditions of Supply to Marketers
- B** – Carter’s Delivery Form
- C** – CBH’s Data Transmission Guidelines
- D** – Number of Commodities and Grade Segregations Handled
- E** – [CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]
- F** – [CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]
- G** – [CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]
- H** – [CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]
- I** – Export Accumulation Guidelines
- J** – [CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]
- K** – [CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]
- L** – [CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]
- M** – Road Movement Authority
- N** – [CONFIDENTIAL MARKET SENSITIVE INFORMATION REMOVED]
- O** – CBH Presentation – WEA Total Real Supply Chain Costs