

2 December 2010

Statement of Issues — Caltex Australia Petroleum Pty Ltd - proposed acquisition of the Mobil assets at the Caltex-Mobil joint fuel terminal in Gladstone

- 1. Outlined below is the Statement of Issues released by the Australian Competition and Consumer Commission (ACCC) in relation to the proposed acquisition of the Mobil assets at the Caltex-Mobil joint fuel terminal in Gladstone (the Mobil assets) by Caltex Australia Petroleum Pty Ltd (proposed acquisition).
- 2. A Statement of Issues published by the ACCC is not a final decision about a proposed acquisition, but provides the ACCC's preliminary views, drawing attention to particular issues of varying degrees of competition concern, as well as identifying the lines of further inquiry that the ACCC wishes to undertake.
- 3. In line with the ACCC's *Merger Review Process Guidelines* (available on the ACCC's website at www.accc.gov.au) the ACCC has established a secondary timeline for further consideration of the issues. The ACCC anticipates completing further market inquiries by 23 December 2010 and anticipates making a final decision on 27 January 2011. However, the anticipated timeline can change in line with the *Merger Review Process Guidelines*. To keep abreast of possible changes in relation to timing and to find relevant documents, market participants should visit the Mergers Register on the ACCC's website at www.accc.gov.au/mergersregister.
- 4. A Statement of Issues provides an opportunity for all interested parties (including customers, competitors, shareholders and other stakeholders) to ascertain and consider the primary issues identified by the ACCC. It is also intended to provide the merger parties and other interested parties with the basis for making further submissions should they consider it necessary.

Background

5. On 15 October 2010 the ACCC commenced a public review of the proposed acquisition, having received a submission from Caltex Australia Petroleum Pty Ltd seeking informal clearance from the ACCC.

The parties

Caltex Australia Petroleum Pty Ltd (Caltex)

6. Caltex is a major refiner-marketer of petrol, diesel and automotive LPG in Australia. It owns the Kurnell refinery in Sydney and the Lytton refinery in Brisbane and has an interest in five fuel terminals throughout Queensland, located in Brisbane, Cairns, Gladstone, Mackay and Townsville.

Mobil Oil Australia Pty Ltd (Mobil)

7. Mobil is a major refiner and wholesaler of petrol, diesel and automotive LPG in Australia. It has previously owned terminals at five locations in Queensland, but each of these terminals has been sold in recent years. Mobil currently owns no terminal assets in Queensland other than the assets at Gladstone that are the subject of the proposed acquisition.

The Transaction

- 8. Caltex and Mobil own adjoining terminals at Port Gladstone in Queensland. These terminals are used to store the petrol and diesel which Caltex and Mobil supply by ship into the Port of Gladstone. The assets at the terminals include tanks, which store fuel, and infrastructure such as pipelines and gantries to allow for the loading and unloading of fuel from these tanks. Fuel is distributed from these facilities to customers in the region by truck.
- 9. Since 1997, Caltex and Mobil have operated their terminals jointly under a joint terminal agreement. Under this joint terminal agreement, the separate assets owned by Caltex and Mobil are operated by one management entity (ie Caltex) and each party has certain rights to use, and host fuel in, the other's assets. Caltex and Mobil separately supply the fuel hosted within the facilities to their own retail sites, wholesale distribution points and customers.
- 10. Mobil is proposing to sell the Mobil assets at the joint fuel terminal to Caltex. The Mobil assets at the Gladstone terminal in Queensland that are the subject of the proposed acquisition include 2 x unleaded petroleum tanks (6,580 KL & 2,140 KL), 1 x premium unleaded petroleum (95) tank (2,750 KL), 2 x diesel tanks (4,420 KL & 3,110 KL) and associated infrastructure. The Mobil assets also include space which is currently or could be made suitable for additional new build tanks.

Industry background

Fuel terminals

- 11. Terminals for storage of refined petroleum products (petrol and diesel) are large facilities commonly located near their sources of supply, either by pipeline from refineries or by pipeline from import facilities, being ports, wharves or berths.
- 12. Import terminals are generally located close to ports and distribute refined petroleum products by pipeline from a berth to a storage facility located within the terminal. The terminal owner will use vehicles owned or contracted by it to supply fuel to its own retail sites, wholesale distribution points and customers.

- Some of the terminal owner's fuel customers may also receive delivery of purchased fuel at the terminal, allowing them to organise their own logistics.
- 13. The majority of terminals capable of receiving cargos of petroleum products being imported into Australia are owned and operated by BP, Caltex, Mobil and Shell (the **major refiners**) all of which import refined petroleum into Australia.
- 14. There are also a number of other import terminals which are owned and operated by importers or bulk liquid logistics companies that are not related to the major refiners (such as Neumann and Freedom Fuels in Brisbane).

Gladstone region fuel supply

15. A large proportion of the fuel supplied in the Gladstone region is diesel, particularly for use by mining, industrial and transport customers. The Surat-Bowen basin is also located in the Gladstone region and the coal seam methane operations in this area are expected to be a large driver of future diesel demand.

Other market participants

16. There is one other fuel terminal in the Port of Gladstone; a joint fuel terminal operated by Shell and BP at a site adjacent to the Caltex-Mobil terminal. BP, Caltex, Mobil and Shell all supply petrol and diesel fuel to customers from their terminals. There is also a diesel-only terminal owned by Marstel located in the nearby town of Port Alma. Marstel is not a fuel supplier and supplies terminal services to any interested fuel supplier. Gekko Petroleum currently supplies diesel from the Marstel terminal.

Market inquiries

17. On 15 October 2010 the ACCC commenced market inquiries regarding the proposed acquisition. A range of interested parties provided responses, including other suppliers of petroleum products and liquid fuel terminal services.

With and without test

- 18. In assessing a merger pursuant to section 50 of the *Trade Practices Act 1974* (Cth) the ACCC must consider the effects of the transaction by comparing the likely competitive environment post-acquisition if the transaction proceeds (i.e. the "with" position) to the likely competitive environment if the transaction does not proceed (i.e. the "without" or "counterfactual" position) to determine whether the proposed acquisition is likely to substantially lessen competition in any market.
- 19. The ACCC's preliminary view is that the likely counterfactual in this matter is that if the proposed acquisition does not proceed, Mobil would sell the Mobil assets to another fuel supplier.
- 20. If Mobil were to sell the Mobil assets to any party other than Caltex, it would only do so on the condition that the purchaser would enter into a long term hosting agreement with Mobil, with an option or options to extend the agreement, so that Mobil could continue to use the terminal services.

- 21. Mobil has stated that it would seek an initial term of at least three years for this hosting agreement and the ability to extend for at least 15 further years but with a strong preference for at least 25 years.
- 22. At this point in time, Mobil has stated that it would seek to enter a hosting agreement which provided sufficient volume to meet its current demand, plus additional capacity to increase hosting volumes in the future. Mobil would request no minimum throughput. If a minimum take or pay throughput was demanded Mobil would require a lower per litre hosting rate to reflect the higher income certainty.
- 23. Mobil would request no upper limit on throughput but would accept such a limit provided Mobil had the option to secure increased volumes beyond the limit, if and when they were required, by funding necessary capital investment at the terminal. Mobil would require the following minimum throughput:
 - For ULP 55ML p.a.
 - For Diesel 195 ML p.a.
 - For PULP 95 10 ML p.a.
- 24. The existing joint terminal agreement between Caltex and Mobil is subject to a 5-year termination clause. If Mobil were to sell the Mobil assets to any party other than Caltex then Mobil would seek to impose as a condition of sale that the acquirer provide access to Caltex on terms consistent with the joint terminal agreement for at least a 5-year period after acquiring the assets.

The ACCC invites comment on the counterfactual

The ACCC welcomes comment from any market participant as to the viability of the Mobil assets being effectively used by a third party to import and supply fuel.

In particular the ACCC is seeking information about the likely impact of Mobil's proposed condition of sale that an acquirer (other than Caltex) provide access to Caltex on terms consistent with the joint terminal agreement for at least a 5-year period. Specifically, the ACCC is seeking a response to the question of whether an acquirer (other than Caltex) is likely to be able to acquire and viably operate the Mobil assets with such a condition of sale compared to a situation where the condition is not imposed.

Market definition

- 25. The ACCC's preliminary view is that the relevant market in relation to the proposed acquisition is the market for the supply of petrol and diesel terminal services in the Gladstone region that are capable of being supplied by ship. Petrol and diesel terminal services involve the storage of the relevant fuel and associated services relating to the loading (by ship) and unloading (by truck) of that fuel.
- 26. The ACCC generally considers that petrol terminal services and diesel terminal services are in the same market. This is due to the potential for supply sided substitutability between the two fuels. It is technically possible to store either diesel or petrol in the same storage tank, provided the tank is properly cleared

between changing fuel types. In some cases technical modifications must be made, for instance the storage tank will require a floating roof to store petrol but not diesel and there are different fire safety issues for each fuel. Relevantly to this assessment, port authorities may also place different restrictions on the shipping and handling of gasoline and diesel which can limit or eliminate the possibility of supply-side substitution between the two fuels in certain instances.

- 27. Terminal services are an important input into the supply of wholesale fuel. Having access to terminal facilities gives wholesale suppliers the ability to source and import their own fuel, which gives them a stronger negotiating position with other wholesale suppliers. In addition, terminal access can enable wholesale suppliers to supply fuel into the area at a lower cost than they could if they had to rely on wholesale fuel acquired from competing fuel suppliers. Thus, issues which impact on the supply of terminal services in the Gladstone region have important flow on effects to wholesale and, ultimately, retail fuel markets in the Gladstone region.
- 28. The ACCC considers that the Gladstone region market is likely to include the terminals located at Port Alma. However, the ACCC notes that the relevant port authority currently imposes restrictions which prevent petrol being stored at terminals in Port Alma.
- 29. Some market participants indicated that the market may also include terminals located at Bundaberg. The ACCC is seeking further information on the suitability of Bundaberg as a supply point into the Gladstone region.
- 30. The ACCC considers that the Gladstone region market is not likely to include the terminals located at Mackay or Brisbane. Market inquiries to date indicate that terminals located at Mackay and Brisbane do not provide close substitute services for services provided by the terminals located in the Gladstone region, due to the high cost of transporting fuel by truck to the Gladstone region from Mackay or Brisbane. Market inquiries suggested that transportation from these locations is primarily done in unusual circumstances to meet particular customer or supply requirements.
- 31. The ACCC is seeking further information in relation to the geographic delineation between the Gladstone region market and adjacent petrol and diesel terminal services markets.

The ACCC invites industry comments on the above market definition

The ACCC welcomes any comments from market participants regarding the ACCC's preliminary views on market definition. In particular the ACCC seeks views in relation to whether fuel terminal services located in Bundaberg, Brisbane and Mackay should be regarded as close substitutes for fuel terminal services in Gladstone and Port Alma.

Statement of issues

32. For the purposes of this Statement of Issues, the issue identified in this matter falls within the category of an "issue of concern".

Issue of concern

33. The ACCC's preliminary view is that the proposed acquisition is likely to substantially lessen competition in the market for the supply of import-capable petrol and diesel terminal services in the Gladstone region. In particular, the ACCC is concerned that acquisition of the Mobil assets by Caltex will substantially reduce competition by foreclosing the likelihood of effective entry by independent fuel suppliers into the Gladstone region market for the foreseeable future.

Barriers to entry and expansion

- 34. The ACCC considers that barriers to entry into and expansion within the relevant market are substantial and that if the proposed acquisition proceeds, entry or expansion on a scale sufficient to provide a competitive constraint on existing fuel suppliers is not likely within the foreseeable future.
- 35. Market inquiries to date indicate that one barrier to entry and expansion is a lack of suitable land for establishing a import-capable terminal in the Gladstone region. There is currently no land available for the development of a new fuel terminal at the Port of Gladstone. While the Gladstone port authority does propose to reclaim over 150 ha of land as part of the Fisherman's Landing Northern Expansion Project, the timing of this development and its suitability for use as a fuel terminal is presently unclear.
- 36. In addition, market inquiries suggest that new entry at such a "greenfield" site is prohibitively costly and involves significant sunk costs in both tankage and associated infrastructure, including shipping berths, pipelines, loading gantries and site facilities. Greenfields entry is also difficult without an existing customer base in the region as fuel terminals require a certain amount of throughput to be economically viable.
- 37. There is land available for the development of additional terminal services at Marstel's terminal in Port Alma. However, market inquiries suggest that this terminal has a number of restrictions which limit its use as a supply point for petrol and diesel in the Gladstone region. These limitations include safety restrictions currently imposed by the Port Authority which prohibit the hosting of petrol at that site and draught restrictions limiting the size of ships which are able to dock at the port. These restrictions mean that Port Alma is unable to be used as an entry point for petrol retailing in the Gladstone Region and limit the competitiveness of Port Alma as a supply point for commercial and wholesale diesel fuel.

The ACCC invites industry comment on the above barriers to entry and expansion

In particular, the ACCC seeks views in relation to the viability of new entry in the medium term using the land proposed to be reclaimed in the Port of Gladstone.

The ACCC also seeks comment on the commercial viability of using the terminal at Port Alma to supply diesel customers in the Gladstone region.

Removal of a potential competitor

- 38. The ACCC has previously found that one of the characteristics of wholesale petrol markets that have the potential to restrain competition and restrict downward pressure on wholesale petrol prices are the impediments faced by suppliers other than the major refiners (**independent suppliers**) in obtaining access to suitable terminal capacity to import refined fuel. For the reasons outlined above, the Gladstone region suffers from this impediment. Large scale importing by independent suppliers is not possible for petrol and limited in scope for diesel due to restrictions at the Port Alma terminal.
- 39. Ownership of the Mobil assets by an independent supplier may facilitate greater access to terminal services in the Gladstone region. A new entrant acquiring the Mobil assets is likely to seek to maximise throughput at that terminal and, without a large existing customer base, may look to provide hosting services to other suppliers at a competitive rate. In this way, acquisition of the Mobil assets by an independent supplier may increase competition for the supply of fuel terminal services.
- 40. The ACCC also considers that independent access to an import capable terminal in the Port of Gladstone has the potential to significantly improve competitive outcomes and increase customer choice in wholesale petrol and diesel markets in the Gladstone region. This effect in turn may affect competition in retail markets for petrol and diesel, as more vigorous wholesale competition could lead to increased retail competition.
- 41. The ACCC notes that retail sites in the Gladstone region are ultimately reliant on one of the four major refiners for the supply of petrol. The ACCC also notes that there is a gap between the petrol and diesel terminal gate prices (**TGP**) offered by major refiners in Brisbane and those offered in Gladstone. Market inquiries suggest that the size of this gap may not be justified by cost differences in supplying wholesaler customers in the two locations.
- 42. In the absence of the proposed acquisition, the ACCC considers that it is likely that an independent supplier would acquire the Mobil assets and that the sale of the Mobil assets represents one of the only opportunities for independent suppliers to effectively enter the Gladstone region market for the foreseeable future. It is the ACCC's preliminary view that increased competition from entry by independent suppliers could put downward pressure on wholesale prices in the region, leading to better outcomes for petrol and diesel users in the Gladstone region.

The ACCC invites comment on the existing state of competition for the supply of wholesale and retail petrol and diesel in the Gladstone region

In particular, the ACCC seeks views on whether, and to what extent, access to the Port of Gladstone by independent fuel suppliers would improve competitive outcomes for retail, wholesale and commercial customers in the Gladstone region.

¹ Report of the ACCC inquiry into the price of unleaded petrol (December 2007).

The ACCC also seeks views on whether, and to what extent, the difference in the TGP charged by the major refiners in Brisbane and Gladstone can be explained by cost differences in supplying wholesale customers in the two locations.

ACCC's future steps

- 43. The ACCC will finalise its view on this matter after it considers the market responses invited by this Statement of Issues.
- 44. The ACCC now seeks submissions from market participants on each of the issues identified in this Statement of Issues and on any other issue that may be relevant to the ACCC's assessment of this matter.
- 45. Submissions are to be received by the ACCC no later than 23 December 2010. The ACCC will consider the submissions received from the market and the merger parties in light of the issues identified above and will, in conjunction with information and submissions already provided by the parties, come to a final view in light of the issues raised above.
- 46. The ACCC intends to publicly announce its final view by 27 January 2011. However the anticipated timeline may change in line with the *Merger Review Process Guidelines*. A Public Competition Assessment for the purpose of explaining the ACCC's final view may be published following the ACCC's public announcement.