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Department of Infrastructure and Regional Development
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To whom it may concern

Re: Coastal Shipping Reforms Discussion Paper

Thank you for the opportunity to provide a submission on the Coastal Shipping Reforms Discussion Paper.

The Australian Institute of Petroleum (AIP) presents this submission to the Department on behalf of AIP's core member companies BP Australia Pty Ltd, Caltex Australia Limited, Mobil Oil Australia Pty Ltd and Viva Energy Australia Pty Ltd.

AIP member companies operate across all or some of the liquid fuels supply chain including crude and petroleum product imports, refinery operations, fuel storage, terminal and distribution networks, marketing and retail. Underpinning this supply chain is considerable industry investment in supply infrastructure, and a requirement for significant ongoing investment in maintaining existing capacity. Over the last decade, AIP member companies have invested over $10 billion to maintain the reliability and efficiency of fuel supply meeting Australian quality standards.

Coastal Shipping and Petroleum Products

AIP, and Member Companies, have been actively engaged in the policy discussions relating to Australia's Coastal Shipping regime for many years. Efficient coastal shipping remains important to the industry and Australia because of the ongoing need for transport of crude oil and petroleum products on the coast.

The supply of petroleum products to meet Australia's demand for liquid fuels requires the refining of crude oil at Australian oil refineries and supply of these products to terminals, the import of the finished petroleum products to seaboard terminals, and the distribution of petroleum products from terminals to major commercial customers and service stations.

The involvement of the petroleum industry in coastal trading includes the movement of:

- domestically produced crude oil to Australian refineries
- intermediate products between refineries (though this has diminished in recent years)
- finished products from major distribution terminals to other major seaboard terminals.

While Australia has its own indigenous crude oil production, this has been declining with around 76 percent exported in 2015–16. These crudes are largely unsuitable for Australian refineries to manage their product slate, with the locations of Australian refineries being generally remote from upstream production also contributing to the quantity of exports. Crude oils required to meet the product demand mix in Australian refineries were imported from over 25 countries, but mainly from the Asia-Pacific region (71 percent) including New Zealand and PNG. The remaining third of crude oil imports was sourced from the Middle East (17 percent), Africa (10 percent) and others (2 percent).

Crude oil from Bass Strait is supplied by pipeline to the Altona refinery in Melbourne and the Geelong refinery. However, the production of crude oil from Bass Strait continues to decline as the fields are depleted and the production from Bass Strait is progressively becoming a lighter condensate and unsuitable for processing in Australian refineries in more than small volumes. However, there are still movements of crude oil by ship from Bass Strait to other Australian refineries. Other Australian sources of crude oil include the Cooper Basin fields, and the North West Shelf which are also moved by ship.

There are movements of intermediate products between Australian refineries by ship because of greater capacity to process certain types of inputs and nature of consumer demand in the regional supply foot print of the receiving refinery. Past examples of these intermediate product movements include cracker feeds for processing in a fluidised catalytic cracker, high sulfur gasoil for processing in hydrogen desulfurisation unit to produce diesel and occasionally the re-routing of off-specification product for further processing.

In 2015–16, Australia consumed 55 400 ML (mega litres) of petroleum products - or around 150 ML per day. Australian refineries produced 25 800 ML of petroleum products, of which around 2 percent was exported (excluding LPG). Net imports from over 20 countries accounted for 53 percent (or 31 000 ML) of total consumption. The bulk of imported fuel came from refiners and regional suppliers in Japan and South Korea and imports from India are increasing.

Finished petroleum products are also moved by ship from Australian refineries to other seaboard terminals around Australia. The major regular supply areas from Australian refineries were Northern Queensland, South Australia, North West Western Australian and Tasmania. There have also been irregular movements of finished petroleum products between major metropolitan terminals of finished petroleum products and ad hoc supplies being conducted between major metropolitan terminals in the event of supply disruptions.

The volume of petroleum products shipped locally is in long term decline. The most recent data from the Bureau of Infrastructure, Transport and Regional Economics on Australian Sea Freight 2014-15 (2017) showed a reduction of coastal trading volume for petroleum products from 14.9 million tonnes in 2005-06 to 8.3 million tonnes in 2014-15 (Table 2.8, p 33). This 44% decline in coastal shipping of petroleum products over the period is in the context of a 14% growth in total Australian demand for petroleum products over the same period.

Structural Change in Australian Downstream Petroleum Industry

This reduction in the need for coastal shipping of petroleum products is largely a result of the ongoing rationalisation of the Australian oil refining industry and associated changes to the petroleum distribution system brought about by increasing competition from larger and more efficient refineries in the Asian region.

In 2003, Australia had eight operating refineries with the capacity to supply over 95 per cent of Australia's liquid fuels demand. The Australian Government's Cleaner Fuels Program that commenced in 2001 required a progressive tightening of fuel standards to deliver urban air quality benefits and facilitation of more advanced motor vehicle technologies. The Australian refiners were required to spend over $3 billion by 2010 in order to stay in business and resulted in the refineries operating with significantly less flexibility.

As a result of the capital requirements to meet these fuel specifications, ExxonMobil announced the mothballing of the Port Stanvac refinery in Adelaide in 2003 and in 2009 the facility was subsequentially decommissioned. The Cleaner Fuels program also caused the de-rating of the ExxonMobil Altona refinery in Melbourne reducing from 135,000 barrels per day to 82,000 bpd. These ExxonMobil decisions reduced the capacity of the Australian refining sector by 15 percent.

During the mid-2000s a supply surplus began to emerge in the Asian region as a result of large scale refinery construction programs in India and China. This surplus was exacerbated by the Global Financial Crisis which saw the emergence of a global overcapacity in the supply of refined petroleum products. The Australian refining industry faced an unprecedented level of competition from larger and more efficient Asian export refineries leading to significant financial losses in 2008, 2011 and 2012.

In response, Shell's Clyde refinery in Sydney was converted to an import terminal in 2012. Agreement was also reached in 2014 on the sale of the remainder of the Shell downstream petroleum assets in Australia to Vitol, the world's largest petroleum trader, under the name Viva Energy Australia.

Further rationalisations included the closure of Caltex's Kurnell refinery in Sydney, which was converted into Australia's largest fuels import terminal in the fourth-quarter 2014, and the closure of BP's Bulwer Island refinery in Brisbane in mid-2015, which was also converted into a fuels import terminal.

The remaining Australian refineries, BP Kwinana in Western Australia, Caltex Lytton in Brisbane, ExxonMobil Altona in Melbourne and Viva Geelong will still be subject to ongoing intense competitive pressures, including through consideration of changes to fuel standards to reduce the sulfur content in unleaded petrol.

The fundamental restructuring of the Australian refining industry has significant implications for fuel distribution and consequently the volume and type of coastal shipping needed to move the fuel around the country.

The coastal shipping task going forward

The total crude oil requirements of Australian refineries have reduced substantially as domestic refinery capacity has reduced and the proportion of Australian crude oil used in Australian refineries continues to decline. As a result, the requirement of coastal shipping to supply Australian refineries will also substantially decline. For this reason, AIP considers there is no likelihood of a General License (GL) crude oil tanker entering coastal shipping in Australia.

The reduction in refining capacity has also meant a reduction in refinery transfers of intermediate products between Australian refineries. There are also no opportunities for intra-company transfers as each company has only one refinery. Moreover, there do not appear to be any economic refining models that would support the transfers of intermediate products between remaining Australian refineries on a regular basis. With the various refinery closures, a greater proportion of Australian petroleum products demand is now supplied by imports which have displaced shipments from Australian refineries particularly to the Northern areas of Australia.

Key shipping issues for the downstream petroleum industry

AIP and Member Companies support amendments to the shipping regulatory regime that:

- reduce the cost impost of coastal shipping on Australian refineries which in turn increase their ability to compete against direct imports and improve the competitive position of Australian refineries
- help deliver cheaper freight costs for fuel supplies
- create greater choice and flexibility in options to supply fuel to the significant number of terminals around Australia
- reduce administration costs for industry and government
- significantly reduce the complexity of rules relating to shipping of petroleum products in Australia
- facilitate supply chain operations that best meet fuel supply needs in regional markets across Australia.

In particular, AIP and Member Companies believe that:

- Vessels used by the petroleum sector must have the flexibility to deliver and/or move petroleum (crude oil and petroleum products) to and between any Australian port (i.e. both inter and intra-State cargo movements).
    - Current legislation makes it exceedingly difficult (because of relatively lengthy approval times and the complex approval process, as well as excessive paperwork) for Australian fuel suppliers to make short term decisions necessary to optimise the Australian fuel supply chains in ways that can best meet emerging fuel supply needs in Australia.
- Contestability is provided through the competitive shipping market – it is in the interest of business that cargo is moved at least cost.
    - Current legislation creates a significant administrative burden for the petroleum industry and Government with no practical purpose since there are no Australian registered petroleum tankers available to contest proposed coastal trading voyages.
- Foreign vessels used by the petroleum industry to pick up crude oil and condensate from FPSOs in Australian waters and deliver that cargo to an Australian port, and petroleum tankers used to store crude oil or petroleum products on a temporary basis in Australian waters (as a form of temporary fuel storage during refinery maintenance periods) must be exempted from the 'importation' provisions of the Customs legislation, in the same way as all other foreign vessels used by the downstream petroleum industry.
    - Current legislation does not properly address these operational issues and as a result imposes significant unintended consequences and costs on the petroleum industry, and constrains potential options to optimise the fuel supply chain operations in Australia and hence fuel supply security. In the case of FPSO production, the current provisions actively discourage the use of Australian crude oil and condensate in Australian refineries.

AIP comments on proposed Legislative Amendments

In broad terms, AIP is supportive of the proposed changes outlined in the discussion paper. AIP also raises a number of other issues for consideration.

1. <u>Remove the five-voyage requirement for a Temporary Licence (TL)</u>

    AIP supports this amendment. Ensuring secure supplies of fuel to the Australian market is of paramount importance to AIP members. Key to this supply security is the capacity to complement domestically refined fuels (including diesel, gasoline, and jet fuel) with imported cargos of refined product. Similarly, it is important that cargos of crude oil are able to be efficiently delivered to refineries. These shipments of crude or refined product are normally booked only months in advance, with these bookings often adjusted regularly.

The capacity for the industry to be able to divert or redirect these cargoes to other terminals in times of need is also important. It is not unusual for shipments to be required to be redirected during weather events, shifts in demand, or unplanned refinery outages, but this has not always been possible, without at least considerable expense, under the current regime. The proposed changes should allow the industry to operate in an environment more reflective of market reality.

2. Streamline the licensing process where no General Licence (GL) vessels are available

   AIP supports this proposal and is pleased that the discussion paper specifically references the fact that there are no Australian flagged vessels capable of carrying petroleum products. The amendment should significantly reduce the red tape burden which currently serves no purpose in reflecting and dealing with market realities in the petroleum industry.

3. Streamline the TL variation process

   AIP supports this amendment. As previously noted, it is not unusual for companies to require a redirection of petroleum vessels due to unforeseen circumstances, such as a supply disruption. In these circumstances, companies need a prompt and efficient response in the movement of cargoes, which has largely not been supported under the current regime.

   AIP members have previously provided Government with case studies (invariably commercial in confidence) where such a response has not been possible due to the constraints of the current regulatory system. Experience has shown that once a vessel has commenced its voyage, the regulatory barriers have made it almost impossible to redirect that vessel. Furthermore, time delays have also led to the imposition of unnecessary costs or an inability to address a petroleum market shortfall.

4. Amend voyage notification requirements

   AIP supports this amendment, as consistent with the aforementioned concerns, current arrangements have resulted in costly delays and have only served as a red tape burden for the petroleum industry.

5. Amend the tolerance provisions

   AIP supports the intent of the amendments in principle that the tolerance limit for loading dates be extended to 30 days and removal of the volume tolerance provisions in their entirety. Such an approach would better reflect the market reality which is constantly changing and requiring regular re-assessment.

6. Replace the current three-tier regime with two tiers

   AIP supports this amendment given Emergency Licences have rarely been granted, but our support is contingent on the final form of the proposed amendment, and on the inclusion of amendments proposed to streamline the TL variation process, to ensure they deliver the intended outcome and to ensure sufficient flexibility in vessel movements to respond to petroleum market realities.

7. Extend the geographical reach of the Coastal Trading Act

   AIP supports this amendment. AIP expects that the amendment would more readily provide for the supply of Australian crude oils to some Australian refineries.

8. Allow dry-docking

   AIP neither supports nor opposes this amendment

9. Minor technical amendments

   AIP has no view on these proposals.

Additional Amendments

AIP, while supportive of the amendments identified in the discussion paper, proposes additional actions to support more efficient operations of Australia's coastal shipping regime. In particular, AIP supports a fulsome national approach led by the Federal Government to remove the overlap between State and Federal regulation. Similarly, AIP also supports reforms that would more readily allow for intra-state voyages allowing product movement from port to port. AIP also supports amendments that would allow industry to submit variations to load port or discharge port on approved voyages to further assist in responding to energy security issues. AIP members have provided detailed commercial in confidence cases studies in support of these proposals.

Training Options

Given there are currently no Australian flagged vessel able to be engaged to transport crude oil or refined petroleum products, nor is this situation likely to change in the foreseeable future, AIP is not in a position to provide feedback on the issues raised in the discussion paper. AIP, however, would urge caution to ensure that any new training arrangements do not impose new costs or levies that would ultimately be passed on customers, including the downstream petroleum sector.

Conclusion

AIP welcomes the efforts of Government to amend the coastal shipping regulatory regime in a manner which better reflects the market realities for petroleum companies and the need to be highly flexible and efficient. AIP supports the proposed amendments and encourages Governments to continue working together to streamline the system and remove unnecessary red tape.

Please do not hesitate to contact me on 02 6247 3044 or via email at pgniel@aip.com.au should you wish to discuss further any matter raised in this submission.

Yours sincerely

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