



AIP Submission to Senate Inquiry into the Provisions of the Coastal Trading (Revitalising Australian Shipping) Amendment Bill 2017 November 2017

Thank you for the opportunity to provide a submission on the Senate Inquiry into the Provisions of the Coastal Trading (Revitalising Australian Shipping) Amendment Bill 2017.

The Australian Institute of Petroleum (AIP) presents this submission 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 finished petroleum products to seaboard terminals, and the distribution of petroleum products from terminals to 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 refineries or 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 of production 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 with the production 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. There are other Australian sources of crude oil, including from 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 the nature of consumer demand in the regional supply footprint 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 Australian grade low sulphur diesel and occasionally the re-routing of off-specification product for further processing.

In 2016–17, Australia consumed 58 400 ML (mega litres) of petroleum products - or around 160 ML per day – a 9.1 percent increase since 2010-11. Australian refineries produced 25 000 ML of petroleum products, of which around 4.7 percent was exported (excluding LPG). Net imports from over 20 countries accounted for 57 percent (or 33 400 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 (published in 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 percent 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 subsequently 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 (this

has since increased to 90,000 bpd). These ExxonMobil decisions reduced the capacity of the Australian refining sector by 15 percent at the time.

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 closed in 2012 and a project to convert the facility to an import terminal began. Agreement was also reached in 2014 on the sale of Shell's downstream petroleum assets in Australia to Vitol, the world's largest petroleum trader, now operating 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 Energy Geelong are still subject to ongoing intense competitive pressures, including through consideration of changes to federal 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 with crude oil 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.

Movements of finished products from refineries to other major seaboard terminals and to markets not serviced by a local refinery (such as Tasmania and South Australia) will still require a coastal shipping task.

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, particularly during times of supply tightness
- 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 and ease 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). This is particularly important when managing short-term fuel supply disruptions.
 - 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 various markets, particularly during fuel-supply disruptions.
- 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 Amendment Bill.

1. Remove the five-voyage minimum requirement to apply for a temporary licence

AIP supports this amendment. Ensuring secure and reliable 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 products 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. Provide the Minister the power to determine that the movement of certain kinds of cargoes and passengers must be consulted on when applied for under a temporary licence or a variation to a temporary licence

AIP supports this amendment in so far as it is consistent with the intent outlined in the Explanatory Memorandum, at point 43, namely that:

At present, there are no Australian ships operating across a number of sectors in Australian waters, such as oil or gas tankers. It is therefore inefficient and unnecessary to consult all general licence holders for every temporary licence application that is received. This amendment allows the Minister to designate cargo and passenger types where consultation must take place, thereby limiting consultation to those sectors where Australian vessels can provide competition to foreign flagged vessels. This reduces the impost and uncertainty caused to industry due to unnecessary consultation and allows for the more efficient consideration of licence applications.

This pragmatic approach that recognises that there are no Australian flagged liquid fuel or crude oil tankers should provide greater efficiency for Australia's petroleum industry.

3. Streamline the processes for making changes to temporary licences by creating a single 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 extremely challenging 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 so that notifications are only required when voyage details have changed from that approved on the licence

AIP supports this proposal. 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.

5. Amend the tolerance provisions for temporary licence voyages to better reflect industry practice

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. Allow for temporary licences (TL) to be issued in emergency situations

AIP supports this amendment given Emergency Licences have rarely been granted, but our support is contingent on ensuring the inclusion of the amendments 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. Amend the definition of coastal trading to include voyages commencing and concluding at the same port

AIP supports an approach that provides for flexibility in shipping operations for the petroleum industry. This includes moving cargoes from one ship to another at adjacent jetties or at anchor, moving cargoes within the same port, and utilising vessels for floating storage. Such an approach is consistent with international experience.

AIP would be concerned if the reforms to the regime to accommodate a specific industry results in unintended consequences, such as compromising this flexibility for petroleum industry operations. AIP seek clarity on when this provision would apply. If it is intended to apply to a specific industry only (such as recreational vessels) then this should be stated in the legislation for clarity and to ensure no impacts to other industries.

8. Amend the definition of coastal trading to include ships engaged in dry-docking

AIP neither supports nor opposes this amendment.

9. Amend the definition of coastal trading to include voyages between ports and other defined places in Australian waters such as offshore facilities

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

10. Allow vessels to be covered by a coastal trading licence while dry-docking

AIP neither supports nor opposes this amendment.

11. Clarify that applications for a variation to a temporary licence must be made by the temporary licence holder;

While AIP supports this intent, it must be implemented in a manner that ensures efficiency. AIP is concerned that there may be lengthy delays if the vessel is the license holder.

12. Require temporary licence holders to provide a vessel's International Maritime Organization (IMO) number to assist with easy identification of vessels.

AIP agrees that all vessels should have an IMO number. The TL holder can provide the IMO number once a ship has been chartered.

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 approach adopted in the Amendment Bill.