



**QUEENSLAND
PRODUCTIVITY
COMMISSION**

**DECISION
REGULATORY
IMPACT
STATEMENT**

**SUGAR INDUSTRY
(REAL CHOICE IN
MARKETING)
AMENDMENT BILL
2015**

November 2015

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EXECUTIVE SUMMARY



The Queensland sugar industry is Queensland's second largest agricultural export industry after beef. It generates around \$2 billion per year in earnings and employs around 16,000 people. There are almost 4,000 cane farming enterprises in Queensland supplying 21 mills, owned by seven different milling companies.

Before deregulation of the industry in 2006, regulation affected almost all aspects of the Queensland sugar industry – from the allocation of cane production areas to the acquisition, marketing and sale of the raw sugar.

In the early 2000's increasing global competition, particularly from Brazil, and several poor seasons, saw sugar industry returns halve from around \$2 billion per year to around \$1 billion per year. A series of reviews found that the regulatory framework at the time was impeding innovation and productivity improvements – with strong recommendations for removing unnecessary regulation and allowing the sector to reorganise itself to flourish.

There is evidence that deregulation has generated improvements. There has been consolidation of farming and milling activities – and significant investment in improving milling. It is also evident that the sector is seeking to add value through the supply chain and through international trading arrangements.

However, it is evident that segments of the industry are at an impasse about agreeing future cane supply agreements. This impasse has arisen from Queensland's three larger millers' decision to cease contracting with Queensland Sugar Limited (QSL) for marketing of export raw sugar from 1 July 2017 and instead market export raw sugar through their own arrangements. Some growers and grower organisations are concerned that this change could adversely affect returns to growers and have indicated the need for Government intervention.

Purpose of the Bill

On 19 May 2015 the Member for Dalrymple, Mr Shane Knuth MP, introduced the *Sugar Industry (Real Choice in Marketing) Amendment Bill 2015* (the Bill) to the Queensland Parliament. The Bill's intent is to protect the interests of Queensland's canegrowers in the State's vitally important sugar industry as mill owners opt out of long-standing sugar marketing arrangements with Queensland Sugar Limited (QSL).¹ To this end, the objects of the Bill are:

- (a) To ensure that a grower has real choice in terms of nominating the marketing entity for on-supply sugar in which they have an economic interest.
- (b) To facilitate the fair and final resolution of any commercial disputes that 'rise between a grower or bargaining representative and a mill owner, including by arbitration'.²

¹ Agriculture and Environment Committee (2015), page v

² Revised Explanatory Notes, Sugar Industry (Real Choice in Marketing) Amendment Bill 2015, Page 1

To achieve this objective, the Bill would require a supply contract to include:

. . . a term requiring the mill owner to have an agreement with a stated entity (the GEI sugar marketing entity) to sell that quantity of the on-supply sugar at least equal to the quantity of the grower economic sugar . . .

Role of the Queensland Productivity Commission (QPC) for the Regulatory Impact Statement (RIS)

On 30 September 2015, the Honourable Curtis Pitt, Treasurer, Minister for Employment and Industrial Relations and Minister for Aboriginal and Torres Strait Islander Partnerships asked us to undertake an independent regulatory (including economic) impact assessment of the Bill. The Queensland Parliament's Agriculture and Environment Committee (AEC) recommended that a regulatory impact assessment be completed prior to the Bill being brought on for the second reading debate.

Regulation can impose significant costs on business and the wider community, so it is important there is a clear rationale and strong case for Government intervention. The purpose of a RIS is to identify the case for government intervention and provide decision makers with the information they need to make an assessment of the benefits and costs of regulatory intervention on the affected stakeholders including business, community, employment, environment and the economy.

Impact assessment

Draft impact assessment

Our draft impact assessment of the Bill concluded that:

- (a) there was no evidence to support a case for market failure in the Queensland sugar industry that would indicate the need for additional Government intervention; and
- (b) that the benefits of additional regulation, as proposed by the Bill, do not outweigh the costs.

We released the Consultation RIS on 30 October 2015 for stakeholder comments and indicated that our assessment of impacts may change in response to issues raised by stakeholders and the presentation of additional information.

Results of stakeholder consultation

We received 12 submissions on the Consultation RIS. The milling sector strongly supported the conclusions of our draft impact assessment. Canegrower organisations on the other hand, consider our conclusions to be flawed. Submissions on our Consultation RIS continue to highlight the impasse between the parties. QSL noted that:

...the optimal outcome to the current sugar marketing impasse is an industry-led enduring commercial resolution acceptable to all parties. However, despite over 18 months of industry discussion and ongoing negotiations between millers and growers regarding this matter, a mutually-agreeable outcome has not yet been achieved.³

Canegrower organisations have expressed strong concerns that our conclusion was:

Around 80% of raw sugar produced in Queensland is exported.

The value of export raw sugar is determined by the world sugar price – for Queensland this is the ICE No.11 price.

Australia is not a price setter in the global market and it is estimated that 99 per cent of the value of raw sugar is set in this way.

Queensland's sugar exports are valued at around \$1.7 billion in an average year.

Around 1 per cent of the value of raw sugar exports is derived from net premiums – around \$14 million per annum to growers and \$7 million per annum to millers.

³ QSL (November 2015), Submission to Queensland Productivity Commission, page 1

at odds with the underlying premise of the National Competition Policy that competition in a properly functioning market will provide the discipline on businesses to continually strive to improve their performance, lift productivity growth and lower costs.... Despite this, the QPC provides no evidence to support its finding that monopoly provision of marketing and pricing services will provide a better outcome than the competitive provision of these same services.⁴

Clearly all parties are concerned about the impact that the impasse in the industry will have on investment by growers and millers, and Australia's international reputation as a marketer of sugar.

No evidence to support a case for market failure in Queensland sugar industry

Growers (and the Bill) are advocating for choice of marketer for that proportion of the raw sugar that they have exposure to in the Cane Price Formula, and which is referred to as Grower Economic Interest (GEI) sugar. Some canegrower groups are also expressing concerns about change that is occurring in the marketing of raw sugar and the move away from the longstanding QSL arrangement. Some grower groups have expressed that the decision of some millers to market raw sugar is 'stripping them of their rights to use QSL' and that the lack of choice implies market failure.⁵

What is market failure?

There is a rationale for regulation where there is market failure. A competitive market is generally characterised with prices that will be close to marginal cost and the firm is incentivised to engage in innovation to seek to lower its costs below that of its rivals and attract customers.⁶ A market failure occurs where there is some structural issues in the industry which do not enable market participants to engage in commercial negotiation and obtain an outcome similar to the result of a competitive market.

Typically, the exercise of choice in how property is managed is attached to ownership. For the Queensland sugar industry, raw sugar marketing occurs after raw sugar has been produced and becomes a tradeable commodity. There is no evidence to suggest that millers do not have clear title over this product. Unless there are significant changes to the traditional Cane Supply Agreement (CSA) arrangements, it is evident that growers do not own, or have an ownership interest, in the raw sugar for which they are seeking choice of marketer. Further, there is no evidence that the Cane Price Formula or the concept of GEI provides any form of legal title in the growers. These arrangements simply recognise that the price the growers obtain for cane is dependent on the price obtained for the sale of manufactured raw sugar.

Since 2006, and with the removal of the single desk seller arrangement in the *Sugar Industry Act 1999* (SIA), millers have the flexibility to choose a marketer for the raw sugar that they produce. As discussed in the body of the Decision RIS, millers exercising their choice to market raw sugar through arrangements outside QSL was envisaged at the time of deregulation, following an orderly transition to the new marketing arrangements. There are now multiple active marketers (including QSL) for Queensland export raw sugar, which is consistent with the development of a competitive market as envisaged by reforms in 2005.

We cannot conclude there is market failure in the Queensland sugar industry because millers are not offering growers choice to determine the marketing arrangements for something they do not own. Nor do we consider that this is inhibiting competition in the market, because the 'market' is the market for the export of raw sugar, which is contestable.

No evidence of abuse of market power

We have also considered whether millers have market power, and if they do, if there is evidence that this is being abused. While some mills may have a degree of market power, there are aspects of the industry and

⁴ CANEGROWERS and ACFA (November 2015). Submission to Queensland Productivity Commission, page 1

⁵ Canegrowers Burdekin (November 2015). Submission to Queensland Productivity Commission, page 3

⁶ Roger Sherman, 'Regulation of Monopoly' (Cambridge University Press, 1989) 17.

current regulation which mitigates against this market power, including the ongoing co-dependent relationship between mills and growers, and the ability for growers to engage in collective bargaining.

We have not been able to identify evidence that any market power, which does exist, is being abused and that would suggest there is need for additional government intervention. We consider the existing legislation:

- supports a pricing negotiation framework which provides an appropriate balance of risk and reward between growers and millers, noting that ten years after deregulation, the Cane Price Formula is still the dominant form of pricing in the sector and growers are authorised to bargain collectively
- allows for millers to provide transparency about pricing and premiums to growers and there is evidence that they are doing so, notwithstanding the evident lack of trust expressed by some growers about the information being provided
- supports investment in the sugar industry, which is important to the long-term economic sustainability of the sugar industry, noting that millers have been investing in mill improvements, which increase overall productivity within the sector.

Even if there were an abuse of market power in the future there are already regulatory options available to growers. For example, it is clear that the unconscionable conduct provisions of the *Competition and Consumer Act 2010* (Clth) (CCA) and recently the unfair contracts regime apply to circumstances of business-to-business contracts. Section 46 of the CCA prohibits an abuse of market power. These options would be open to the growers should contractual arrangements post 2017 be either unconscionable or constitute an abuse of market power, or in certain circumstances are an unfair contract.

Benefits of additional regulation do not outweigh the costs

The Bill proposes to provide growers with the ability to choose a marketer for the GEI proportion of raw sugar, authorises specific anti-competitive conduct as described by the CCA and would provide a framework for pre-contract arbitration.

Our conclusion for the Decision RIS is that potential benefits that may accrue from passage of the Bill, are outweighed by the potential costs and risks. Specifically, the Bill, if enacted:

- (a) interferes with the property rights of millers (assuming the traditional structure of CSAs is retained) and has the effect of conferring an ownership right with growers. We consider that this is a significant form of sovereign risk for millers and would likely reduce the profitability of future sugar mill investment and dampen longer term innovation and productivity compared to no additional regulation
- (b) could reduce the overall returns to the sugar industry. The larger millers have made commercial decisions that they can improve financial outcomes by marketing export raw sugar – the remaining millers have made the commercial decision to market export raw sugar through QSL. There is nothing to suggest that millers – with a commercial incentive to improve returns from their production of raw sugar – are not well equipped to make this decision. Further, to the extent that returns are distributed to growers – it is difficult to see how growers are disadvantaged and the proposals by MSF and Wilmar seem to have sufficient transparency that if a disadvantage were to arise, it would be identifiable to the growers
- (c) could reduce the returns to the industry by adding extra costs. Marketers would need to compete for the business of 4,000 cane producers with costs to attract and retain customers and additional transaction costs. As marketing premiums are still capped by global factors, it is possible that any additional competitive benefits of having growers choose a marketer could be offset by higher costs

- (d) would re-introduce pre-contract arbitration which may lead to both financial (legal) and time loss costs for the industry. Legal costs for an average arbitration are estimated to range between \$1.2 million and \$1.5 million per dispute, with the time to resolve a dispute estimated at 12 – 18 months, with a ‘fast track’ of 9 months. It is not clear that pre-contract arbitration adds additional benefits above the existing mediation arrangements
- (e) could leave parties exposed to action by the Australian Competition and Consumer Commission (ACCC), if the Australian Government does not accept that there is a net benefit from the authorisation of anti-competitive conduct included in the Bill. Clause 8 of the Bill would authorise some additional anti-competitive behaviour. If the Queensland Parliament legislates for a restriction on competition, it must advise the ACCC within 30 days. The Australian Government can disallow the authorisation if the benefits of the anti-competitive conduct do not outweigh the costs. A cost benefit assessment was not completed prior to introduction of the Bill and there is the risk if the Australian Government is not satisfied by the public benefit justification, that parties engaged in anti-competitive conduct would not have the protection of an authorisation.

Attachment 3 summarises the likely impacts on key sugar industry parameters under the Bill option, as well as the base case of 'do nothing'; a mandatory code and a tolling option (where growers contract with millers to crush cane and retain title and control of raw sugar marketing). Under any option, the major influence of the value of cane and raw sugar production continue to be world sugar prices, input costs, and environmental conditions and mill availability.

Conclusion

We have considered in detail the extensive submissions made in response to the Consultation RIS, and made some amendments to the analysis. However, the conclusion of this RIS remains unchanged, specifically:

- (a) there was no evidence to support a case for market failure in the Queensland sugar industry that would indicate the need for additional Government intervention; and
- (b) that the benefits of additional regulation, as proposed by the Bill, do not outweigh the costs.

The Decision RIS concludes that retaining the existing regulatory framework — with no additional regulation — will provide the greatest net benefit to Queensland.

ROLE OF THE QUEENSLAND PRODUCTIVITY COMMISSION



The Queensland Productivity Commission (QPC)'s role is to provide independent advice on complex economic and regulatory issues, and propose policy reforms, with the objective of driving economic growth, lifting productivity, and improving living standards across Queensland. A wide level of open and transparent public consultation will underpin these functions.

The QPC is an independent statutory body established under the *Queensland Productivity Commission Act 2015* (QPC Act).

Our work encompasses three key streams:

- economic reform and policy
- regulatory advice and guidance to departments
- economic research into private and public sector productivity.

Our operation and reporting is independent, with tasks referred to the QPC by the Government.

We are committed to providing a transparent and consultative process to allow all interested stakeholders to participate in inquiry processes.

We operate on the principles of independence, rigour, responsiveness, openness, transparency, equity, efficiency and effectiveness.

ABOUT THE DECISION RIS



Scope

On 30 September 2015, the Honourable Curtis Pitt, Treasurer, Minister for Employment and Industrial Relations and Minister for Aboriginal and Torres Strait Islander Partnerships asked us to undertake an independent regulatory (including economic) impact assessment of the *Sugar Industry (Real Choice in Marketing) Amendment Bill 2015* (the Bill).

The Bill is a Private Member's Bill, and was not subject to the regulatory impact assessment process that would normally be undertaken for Government-initiated legislation. Recommendation 2 of Report No. 6, 55th Parliament Agriculture and Environment Committee (AEC) September 2015 *Sugar Industry (Real Choice in Marketing) Amendment Bill 2015* was:

that the Minister requests his Department of Agriculture and Fisheries to conduct a regulatory impact assessment of the Bill in conjunction with the Queensland Productivity Commission, and that the Minister tables the department's report on this assessment prior to the Bill being brought on for the second reading debate.

Conduct of the regulatory impact assessment

In referring the Bill to us for a RIS, the Treasurer noted that this is not the usual approach to assessment of legislative proposals. However, given our expertise in regulatory review, and independence from Government, it was considered the QPC was best placed to provide advice.

As the Bill is listed for debate in the sitting week starting 1 December 2015, there was urgency attached to the preparation of a RIS to inform the Queensland Parliament's consideration of the Bill.

The timetable for the preparation of the Decision RIS reflected the urgency required, rather than the normal consultation practice set out in the Queensland Treasury RIS System Guidelines (RIS Guidelines).

This Decision RIS has been prepared in accordance with the RIS Guidelines and with the assistance of the Department of Agriculture and Fisheries (DAF).

Key dates

Referral from Treasurer
30 September 2015

Initial submissions
9 October 2015

Release of Consultation RIS
30 October 2015

Due date for submissions
13 November 2015

Decision RIS provided to the Treasurer
25 November 2015

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1 BACKGROUND

1.1 Overview of the Queensland sugar industry

The Queensland sugar industry is located mainly along Australia's eastern coastline, from Mossman in far north Queensland to Rocky Point in south east Queensland. The industry is one of Queensland's largest rural industries and forms a major part of the economy in many coastal regional communities.

The sugar industry represents significant infrastructure investment across rural and regional communities. In Queensland there are around 4,000 cane farming enterprises growing sugarcane on a total of 350,000 hectares annually, supplying 21 mills, owned by seven separate milling companies. The vast majority of cane farms are owned by sole proprietors or family partnerships. The mill ownership structures are a combination of publicly owned entities, privately held companies limited by guarantee, and co-operatives.

Queensland contributes 95 per cent to the nation's raw sugar production. In 2014, 30.8 million tonnes of sugarcane was crushed, producing approximately 4.2 million tonnes of sugar. Total industry revenue was just under \$2 billion, which includes sales from sugar, molasses and electricity exported back into the grid.

Around 80 per cent of the raw sugar produced in Queensland is exported. Australia is the third largest exporter of sugar, after Brazil and Thailand, with around \$1.7 billion in export earnings.

The perishable nature of sugar cane means that it must be processed within 16 hours after harvest. Location and transport costs limit the mills available to growers to process the cane. Due to the 16 hour crushing window, harvested cane must be delivered to mills soon after harvest and growers generally use the services of a miller located close to their farms. In many cases, growers have no alternative mill to supply their cane crop. Millers also require harvested cane to be delivered quickly to their mill as it is not economically feasible to source cane from distant locations.

1.2 History of Queensland's sugar marketing arrangements

Historically, the Queensland sugar industry was highly regulated. Before extensive legislative reform in 2004 and 2005, government regulation controlled almost all aspects of the industry — from the allocation of cane production areas to the acquisition, marketing and sale of the raw sugar product.



1.2.1 Steps toward deregulation of the Queensland sugar industry

Under the *Competition Principles Agreement 1995*, all Australian governments agreed to review restrictions on competition, and regulatory arrangements that contained restrictions on competition, every 10 years. The Queensland sugar ‘single desk’ arrangements were reviewed in 1996.

In 2004, prior to the competition review required for 2006, CANEGROWERS and the Australian Sugar Milling Council (ASMC) signed an agreement committing to the establishment of a working group to progress a new marketing system for bulk raw sugar. Industry agreed to take a pro-active approach to future sugar marketing arrangements, rather than a defensive ‘protection of the status quo’.

At the time the industry was facing a fundamentally changed market situation, because:

- the industry’s historic advantage in efficiency had been eroded, with very low uptake of new technology and practices
- Brazil was emerging as a major new competitor, with a more efficient and commercial export sector – in 2004 alone Brazil increased its cane production by the size of the total Australian industry; and
- the industry remained focused almost entirely on raw sugar exports, and had done little to promote either alternative products from cane or sugar, or to further value-add.

Because of these factors, and several poor seasons, industry returns in the early 2000’s declined from approximately \$2 billion per year, to approximately \$1 billion.

The costs and benefits of the working group’s recommendations were independently evaluated and it confirmed the single desk was hindering the industry from making the changes it needed to remain competitive in the global sugar market by preventing competition in the marketing of raw sugar. Such anti-competitive powers were:

- hindering the industry from embracing opportunities to manage finances and risks of marketing more effectively
- mitigating against opportunities for product diversion from bulk raw sugar
- impeding the take-up of opportunities to install whole-of-chain systems in all operations, preventing the industry from developing a range of commercial marketing skills; and
- negating the need to attract and develop the enterprise and management required to run growth oriented commodity marketing organisations.

1.2.2 2006 deregulation of the Queensland sugar industry

Final deregulation of Queensland’s single desk marketing arrangements for sugar commenced on 1 January 2006. Vesting of raw sugar to QSL was removed and control of raw sugar consequently reverted to millers.

On 13 October 2005, prior to deregulation, the Queensland Sugar Industry and the Queensland Government signed a Memorandum of Understanding (MOU). The MOU included the following statements:

- the working group recommend a commercial, non-legislative based marketing structure for the sugar industry be developed and that it be based on the recommendations of the working group report. The key principles include that QSL would continue to be the industry’s preferred bulk raw sugar export marketing company

- the Australian Sugar Milling Council (ASMC) stated: All members of the ASMC remain committed to working with QSL to assist QSL to retain the preferred marketer by suppliers and customers of Queensland produced bulk raw sugar for export.⁷

When the industry was deregulated, QSL entered into voluntary agreements with the majority of Queensland mills to continue to market their export raw sugar. Under the Raw Sugar Supply Agreements (RSSAs), which QSL has with each of the seven Queensland mill owners, millers supply 100 per cent of their raw sugar production, intended for bulk export, to QSL.

Raw sugar for domestic supply (or exported in bags or containers) is not supplied under the RSSA and marketing can occur independently of QSL.

Today, the SIA imposes few regulations on the sugar industry and facilitates some aspects of production, transport and milling. The principal object of the SIA (section 3) is to

facilitate an internationally competitive, export oriented sugar industry based on sustainable production that benefits those involved in the industry and the wider community.

The SIA continues to require that the relationship between a grower and a miller is governed by CSAs. However, growers and millers are free to negotiate terms relating to the sale of the cane crop.

1.3 Role of Queensland Sugar Limited

QSL is a not-for-profit company in which both growers and millers own shares. Under its constitution, QSL is required to act in the best interests of the sugar industry. As a tax exempt, not-for-profit entity it is not permitted to distribute profits to its members.

QSL is the modern incarnation of the former Sugar Board that was established in 1923 and controlled all Australian sugar exports. Legislation originally required that all sugar be sold to the Sugar Board. In 1991, the Queensland Sugar Corporation (QSC) was established as a statutory authority under the *Sugar Industry Act 1991*, replacing the Sugar Board.

The primary activities undertaken by QSL today include:

- acquiring raw sugar intended for bulk export from Queensland mill owners under the RSSAs
- selling export raw sugar
- chartering shipping for export raw sugar
- financing and hedging activities related to that raw sugar
- sub-leasing, operating and providing storage and handling services at the six bulk sugar terminals; and
- conducting other initiatives considered to be in the best interests of the Queensland sugar industry.

QSL sells raw sugar directly to refiners in a number of countries. Proceeds are pooled for payment purposes and distributed back to mills and growers after being adjusted for marketing costs incurred by QSL. With the pooling of sales proceeds, producers receive an average of prices received from sales of export raw sugar each year.

The arrangements for marketing and export of raw sugar are made between milling companies and QSL under a RSSA. Growers are not a party to the RSSA.

⁷ Burdekin District Cane Growers Limited (November 2015). Submission to Queensland Productivity Commission, page 1

RSSAs acknowledge growers have an ‘economic interest’ in the raw sugar produced from their sugar cane crop — equal to around two-thirds of the raw sugar sold. The miller has the remaining one-third interest. This reflects the historical revenue sharing arrangement which has been in place for the past 100 years — commonly referred to as the Cane Price Formula.

1.4 Role of Sugar Terminals Limited (STL)

Queensland has six bulk sugar terminals — at Cairns, Mourilyan, Lucinda, Townsville, Mackay and Bundaberg — leased from the relevant port authorities by STL under long term leases.

The Queensland sugar industry has storage assets that can store approximately 60 per cent of the state’s total crop. Thus, with sufficient storage it is possible to move sugar sales between futures contracts and maximise revenue in terms of both the net premiums and the overall ICE 11 price able to be achieved. The amount of flexibility Queensland has with its storage is unmatched anywhere else in the world.⁸

Table 2 Queensland bulk sugar terminal capacity vs approximate district sugar production

Bulk sugar terminal	Cairns	Mourilyan	Lucinda	Townsville	Mackay	Bundaberg
Storage capacity	250,000 tonnes	175,000 tonnes	235,000 tonnes	750,000 tonnes	750,000 tonnes	320,000 tonnes
Approximate local sugar production	290,000 tonnes	620,000 tonnes	560,000 tonnes	1,240,000 tonnes	990,000 tonnes	490,000 tonnes
Local sugar production able to be stored	86%	28%	42%	60%	76%	65%

Source: QSL (November 2015) Submission to Queensland Productivity Commission

In 1999, the terminals were separated from QSL's marketing operations but kept in industry ownership through the creation of STL. STL was established as a ‘for profit’ company with 360 million shares: 229.4 million issued to growers (‘G class’) and 130.6 million issued to mill owners (‘M class’). The Brisbane bulk sugar terminal was sold to Wilmar Gavilon in 2009. The ‘G’ class shares were listed on a restricted market on the NSX (National Stock Exchange of Australia).

Trading in STL’s shares is restricted to mill owners for M class and growers for G class — with requirements for growers to sell shares within a reasonable time if no longer actively growing cane. This is intended to ensure that terminal assets remain within industry control. However, millers can purchase G class shares through their farming operations and QSL also has an interest in G class shares.

QSL subleases the terminals from STL and operates them on behalf of the industry. Sublease payments are one of QSL’s major marketing costs and STL’s only material source of income. QSL stores all Queensland raw sugar in the bulk sugar terminals on an open access and cost-recovery basis, including domestic sugar and export sugar for which QSL is not conducting the marketing.⁹

1.5 Recent developments in the Queensland sugar industry

1.5.1 Changing ownership arrangements

Prior to 2006, there had been a significant degree of under-investment in the sugar industry. Since 2006, the industry has attracted significant investment, and as a result of ongoing industry

⁸ QSL (November 2015). Submission to Queensland Productivity Commission, page 3

⁹ QSL (2014). Submission to Senate Committee on Rural and Regional Affairs and Transport

consolidation, many milling companies are now foreign-owned. The scale of global investment in the industry has been substantial and is shown in **Table 2**.

Table 2 Foreign investment in Queensland sugar mills

<i>Company</i>	<i>Details</i>
Wilmar Sugar Australia	Singapore-based Wilmar paid \$1.75 billion for Sucrogen (formerly CSR) in 2010
Tully Sugar Limited	China-based food conglomerate China National Cereals, Oils and Foodstuffs Corporation's made a \$136 million investment in Tully Sugar Limited in 2011
MSF Sugar Limited	Thailand-based Mitr Phol's made an investment of \$313 million in MSF Sugar Limited in 2012.

The Australian sugar milling market is highly concentrated. Wilmar Sugar Australia (Wilmar) accounts for around 55 to 60 per cent of Australia's total raw sugar exports. The next three largest millers — Mackay Sugar Limited, MSF Sugar Limited (MSF) and Tully Sugar Limited (Tully Sugar) — collectively account for about 30 per cent. **Table 3** lists the seven milling companies and the mills they operate. Raw sugar production is largely exported to international customers (around 80 per cent) — predominantly into Asia. The remaining 20 per cent of sugar is refined and consumed domestically.

Table 3 Milling companies and current ownership of mills

<i>Mill ownership</i>	<i>Trading As</i>	<i>Operating mills</i>
Wilmar International Limited (Based in Singapore)	Wilmar Sugar Australia	Macknade Victoria Invicta Pioneer Kalamia Inkerman Proserpine Plane Creek
Grower owned limited company	Mackay Sugar Limited	Mossman Farleigh Marian Racecourse
Mitr Phol Sugar Corp (Based in Thailand)	MSF Sugar Limited	Tableland Mulgrave South Johnstone Maryborough
COFCO (Based in China)	Tully Sugar Limited	Tully
Finasucre (Based in Belgium)	Bundaberg Sugar Limited	Bingera Millaquin
Grower owned, shareholder co-operative	Isis Central Sugar Milling Company Limited	Isis
Family owned and operated	Heck & Sons Limited	Rocky Point

Source: Department of Agriculture and Fisheries

1.5.2 Changing marketing arrangements

In 2010, Queensland cane farmers suffered one of the most extreme weather events in a generation. While the cane was grown, some 5.5 million tonnes of cane was left unharvested due to the wet weather. The total supply shortfall for the 2010 Season was 723,000 tonnes. The supply shortfall resulted in a 'washout' or cancellation of sales contracts and buy-back of previously priced futures positions. The cost of managing cancelled sugar sales and futures buy-back was \$105.5 million, which was allocated to the Shared Pool and then allocated equally across all tonnes in all

pools.¹⁰ This cost was allocated back to the mills and passed on to growers in accordance with the Cane Price Formula (see Section 1.6).

This had the consequence of:

- solidifying growers' views about their economic interest in the sugar, although at the time they argued the mills should meet the full cost of the loss; and
- precipitated millers reviewing their voluntary marketing arrangements with QSL.

In 2012, QSL agreed to a system where Wilmar would sell its economic interest sugar. In 2013 all RSSAs provided millers with the option to buy back their economic interest sugar (around one third) from QSL and then on-sell it to their customers.

In 2013, Wilmar proposed a 'Grower Choice' model which it said would have given growers the ability to choose either the miller, QSL, or both, as the marketer of their economic interest sugar. CANEGROWERS and the Australian Cane Farmers Association (ACFA) rejected Wilmar's proposal due to concerns it would place growers in a weakened negotiating position in the future. Growers were concerned Wilmar might implement

a predatory pricing strategy to lure sufficient volume away from QSL such that the pricing QSL could achieve would be damaged and the price Wilmar would then have to pay for cane would be reduced (and its marketing competitor eliminated).¹¹

In 2014, Wilmar, MSF and Tully Sugar gave notice to QSL that they would not be continuing with their RSSAs beyond 30 June 2017.

1.6 Sugar Pricing

1.6.1 Cane Price Formula

As sugar cane is not a tradeable commodity, the sugar industry developed a 'Cane Price Formula' in 1915 to calculate how the returns (either revenue or losses) of the raw sugar produced would be fairly allocated between both growers and mills.

Today, the price that most growers receive for the sugar cane they provide to the mill continues to be determined by the Cane Price Formula (as shown below).

Cane Price = Net Sugar Price x (0.009¹²) x (CCS – 4) + Constant

where CCS is the 'commercial cane sugar'.

When the Cane Price Formula was developed, it was estimated that grower's total costs and investment in the production of sugar cane — and ultimately raw sugar — was two-thirds of the industry's costs, while miller costs and investment represented one-third.

Therefore, under the Cane Price Formula returns are distributed to growers and mills on a similar basis (2:1). It was also assumed a mill would expect a CCS of 12 (that is, 12 per cent recovery rate of CCS from cane). The Cane Price Formula means that where CCS is greater than 12 (determined when the cane is sampled) this will result in a greater return to growers.

MSF notes that the formula

¹⁰ Wilmar (November 2015). Submission to Queensland Productivity Commission, page 3

¹¹ QSL (2014). Submission to Senate Committee on Rural and Regional Affairs and Transport, page 17

¹² Represents 'milling recovery efficiency'.

in effect splits the revenue from the sale of raw sugar into the revenue to pay for the cane and the revenue the mill needs to operate the sugar mill and to make a profit from its business.¹³

While growers and mills are able to negotiate variations on the formula in their CSAs we understand that the price paid is generally based on:

- the 'net sugar price' (section 1.6.2)
- the recoverable sugar content of the cane - CCS
- a regionally specified 'constant' amount which will vary depending on the mill area¹⁴.

The formula was also designed to provide incentives for growers and mills to operate more efficiently and improve returns. ASMC has noted that growers

now have a range of mechanisms through which they can influence the price of sugar that will ultimately be used in their cane price formula. These include through participation in various mill or QSL pooling arrangements or through agreement with their mills to have their sugar price directly or indirectly hedged via derivatives.¹⁵

1.6.2 Net sugar price

The 'net sugar price' represents the price received from the sale of raw sugar to the world sugar market and determines the aggregate returns to the Queensland sugar industry for both growers and millers. The components of the net sugar price are the:

Raw sugar futures contract price

plus marketing premiums

less marketing costs.

Raw sugar futures contract price

The raw sugar futures contract price refers to the globally traded 'Intercontinental Exchange No.11 raw sugar futures contract price' (ICE No. 11)¹⁶, converted to Australian dollars. ICE No. 11 sets the benchmark for world sugar prices and stakeholders consider that this contributes more than 95 per cent of the net sugar price,¹⁷ although recently this has been close to 99 per cent, as discussed in section 3.3.

Marketing premiums

Marketing premiums are the additional returns over and above the global sugar price and are the sum of a 'physical premium' and a 'polarisation premium.'¹⁸

The physical premium is negotiated between the marketer and the raw sugar customer and is derived from the supply and demand specifics at the time as well as the freight differentials between different supply locations. It may also include the value paid by a customer for accessing higher quality Australian raw sugar compared with alternative products that may be available in the same shipment period.

¹³ MSF (2015). Submission to Agriculture and Environment Committee, page 6

¹⁴ ASMC's submission to the Agriculture and Environment Committee, used a constant of \$0.608 as an indicative example, noting this would be 'different (in the order of cents) from one mill area to the next'.

¹⁵ ASMC (2015). Submission to Agriculture and Environment Committee, page 11

¹⁶ The price for US domestic market sales is determined using ICE No.16 rather than ICE No. 11. These sales comprise a small proportion of all Australian raw sugar exports due to US import quotas.

¹⁷ MSF (2015), Submission to Agriculture and Environment Committee, page 5

¹⁸ Wilmar also note that marketing premiums also include 'spread' gains and losses. Wilmar (November 2015) Submission to the Queensland Productivity Commission, p. 3

The polarisation premium is an additional premium that is essentially a 'quality parameter common to almost all raw sugar export contracts'.¹⁹ Where sugar has a higher 'sucrose purity' (or polarisation) relative to the standard quality benchmark under ICE No. 11, this additional premium is paid.²⁰

Marketing costs

Marketing costs are those costs incurred by the marketer (currently QSL in the main) in the course of completing its sales to customers. These costs include, but are not limited to:

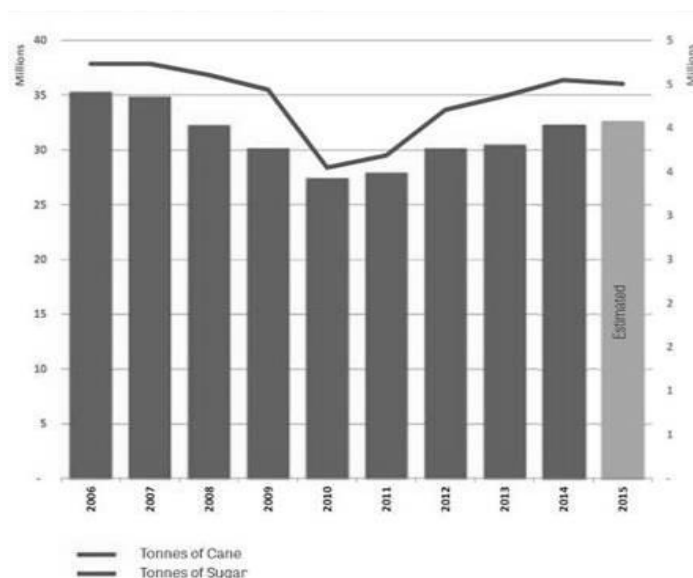
- storing and handling of sugar at bulk sugar terminals (subleased from STL)
- freight and port costs of shipping sugar to customers
- financing advance payment to growers and the administration of pricing pools
- other direct operating costs.

Further information on the value of the premium that is distributed back to growers and millers is detailed in section 3.3.

1.7 Sugar production since deregulation

As shown in Figure 1, Australia's production of cane and raw sugar experienced a decline between 2006 and 2010 – and since 2011 – has gradually increased.

Figure 1: Australian sugar production 2006-2015



Source: CANEGROWERS

Environmental issues have had a significant impact on production over the last decade:

- As part of deregulation, land no longer remained assigned to a mill and growers were able to pursue other agricultural pursuits. Around the same time as deregulation of the sugar industry, the Australian Government was facilitating Forestry Management Investment Schemes (FMIS), and a number of cane farmers sold their farms for forestry plantations. The

¹⁹ Tully Sugar (2015). Submission to Agriculture and Environment Committee, page 4

²⁰ ICE No. 11 references 96 degrees polarisation. Queensland sugar industry typically produces sugar closer to 99 degrees polarisation.

majority of the FMIS have since failed and a number of cane growers have bought back land and have converted the land back into cane.

- In 2007 the sugar mill in the Ord River Irrigation Area (WA) closed, affecting production.
- The cane disease 'Sugarcane Smut' was found in Childers in 2006. In response to this biosecurity threat, the Queensland sugar industry (through government regulations) stopped growing Smut susceptible varieties. Unfortunately, Smut resistant varieties are not as high yielding, and this has had an overall impact on both cane and sugar production particularly for the 2008 and 2009 harvest.
- An unseasonal wet harvest in 2010 which resulted in an approximately 20 per cent of the crop being unharvested. The 2010 decline subsequently impacted the 2011 harvest as there was a significant amount of standover cane (the unharvested cane) which impacted on CCS levels (and therefore raw sugar quantities) as well as harvesting efficiencies.
- Tropical Cyclone Larry (March 2006) and Tropical Cyclone Yasi (2011) severely impacted some of the northern sugar growing districts which affected productivity.

2 CONTEXT FOR THE BILL



The QPC has been asked to complete a RIS for the Bill. Ordinarily, a RIS would be prepared by the government agency proposing the regulation. A clear description of the problem and associated issues would be part of the development of the proposed regulation.

As we have been asked to complete a RIS on a Bill that has already been tabled in the Queensland Parliament, we are relying on publicly available information to best describe the context and the problem the Bill is seeking to address. Our assessment has relied on the report of the AEC; submissions to the AEC; submissions we have received (including on the Consultation RIS) and submissions to the Senate Committee on Rural and Regional Affairs and Transport – *Inquiry into Current and Future Arrangements for the Marketing of Australian Sugar*.

2.1 Sugar Industry (Real Choice in Marketing) Amendment Bill 2015

On 19 May 2015 the Member for Dalrymple, Mr Shane Knuth MP, introduced the *Sugar Industry (Real Choice in Marketing) Amendment Bill 2015* to the Queensland Parliament.

The *Sugar Industry (Real Choice in Marketing) Amendment Bill 2015* — Revised Explanatory Notes (the Revised Explanatory Notes) set out a range of problems the Bill is seeking to address. The following statement appears to best encapsulate the problem the Bill is seeking to address.

To remove any doubt whatsoever, the Bill is to prevent anti-competitive behaviour and promote pro-competitive outcomes. Overall, the Bill is to ensure economic viability for both growers and mill owners, among others, in the Queensland sugar industry.²¹

The AEC concluded the intent of the Bill is

to protect the interests of Queensland's canegrowers in the State's vitally important sugar industry as mill owners opt out of long-standing sugar marketing arrangements with QSL.²²

The following sections set out the issues facing the key stakeholders in the Queensland sugar industry today, and that form the background for consideration of the assessment of the existing situation (the base case), the potential implications of the Bill and alternative options.

2.2 Grower views

The Bill seeks to address a range of concerns expressed by some growers, summarised below.

²¹ Revised Explanatory Notes to the *Sugar Industry (Real Choice in Marketing) Bill*, page 2

²² Agriculture and Environment Committee (2015), page 2

2.2.1 Concern about the imbalance of bargaining power between growers and millers

A central issue of concern is the potential for mills to misuse their monopoly power when negotiating future CSAs. Growers are clearly concerned that under the existing arrangements:

- millers have monopoly power as a result of the sugar cane market being a monopsony²³²⁴²⁵²⁶
- co-dependency does not balance the monopoly power (and mills can, and in recent years have, purchased additional land for cane production)²⁷
- misuse of market power is an unintended consequence of deregulation. When agreement was reached on 2006 deregulation it was on the understanding that millers were not free to independently market and sell the raw sugar²⁸²⁹
- the CCA does not provide sufficient protection for growers from the misuse of market power³⁰³¹
- denying growers the right to have choice about who markets their sugar is evidence of misuse of market power.³²

Growers are also concerned that the imbalance in market power will result in the following impacts:

- growers being unable to obtain 'fair and reasonable terms' for their cane (including GEI)³³³⁴
- in the future growers supplying mills that have opted out of RSSAs will have no choice but to agree to the mill's new terms, including marketer, or leave the industry³⁵
- miller marketing of raw sugar will potentially lead to lower premiums, which are vitally important to growers³⁶
- miller marketing will lower or remove growers share of net premiums.³⁷

2.2.2 Concern about lack of transparency in miller marketing and potential for transfer pricing

Miller marketing is giving rise to a range of concerns for some growers, largely related to the future treatment of premiums. These concerns are related to both issues of market power and the lack of transparency about future premiums. These concerns include:

²³ Tableland Canegrowers Ltd (October 2015). Submission to Queensland Productivity Commission, page 2

²⁴ Canegrowers Herbert River (October 2015). Submission to Queensland Productivity Commission, page 2

²⁵ Burdekin District Cane Growers Limited (2015). Submission to Agriculture and Environment Committee, page 3

²⁶ QSL (2014). Submission to Senate Committee on Rural and Regional Affairs and Transport, page 20

²⁷ QSL (2014). Submission to Senate Committee on Rural and Regional Affairs and Transport, pages 20-21

²⁸ Tableland Canegrowers Ltd (October 2015). Submission to Queensland Productivity Commission, page 1

²⁹ CANEGROWERS and ACFA (2015). Submission to Agriculture and Environment Committee, page 4

³⁰ Canegrowers Herbert River (October 2015). Submission to Queensland Productivity Commission, page 2

³¹ CANEGROWERS and ACFA (2015). Submission to Agriculture and Environment Committee, page 1

³² CANEGROWERS and ACFA (2015). Submission to Agriculture and Environment Committee, page 1

³³ QSL (2014). Submission to Senate Committee on Rural and Regional Affairs and Transport, page 22

³⁴ Invicta Cane Growers Organisation Ltd.(2015). Submission to Queensland Productivity Commission, Attachment 1, page 3

³⁵ QSL (2014). Submission to Senate Committee on Rural and Regional Affairs and Transport, page 2

³⁶ CANEGROWERS and ACFA (2015). Submission to Agriculture and Environment Committee, page 3

³⁷ CANEGROWERS and ACFA (2015). Submission to Agriculture and Environment Committee. Attachment 1, page 13

- lack of transparency leading to millers increasing their slice of the pie at the expense of growers in situations where foreign mill owners also own their own refineries and facilities overseas.³⁸³⁹⁴⁰
- transparency about marketing risks, costs and premiums could effectively be removed to the benefit of the milling company⁴¹⁴²

2.2.3 Clarification of ownership of grower economic interest sugar

The recognition and ownership of grower economic interest (GEI) sugar is a key concern to growers as it relates to their level of influence and control in how raw sugar is marketed.

CANEGROWERS and ACFA noted that the RSSAs that QSL has with each mill acknowledges the price exposure held by their supplying growers, describing the quantity of sugar as Grower Economic Interest (GEI) sugar. In the RSSAs:

*Grower Economic Interest Sugar means Raw Sugar for which Growers, excluding those Growers who are Related Corporate of a Supplier, bear the price exposure under the cane supply or other agreements between the Supplier and the Grower.*⁴³

There does not appear to be full agreement about the level of property right that is implied by GEI or how the form of recognition should be achieved, with growers indicating a range of views from:

- GEI is not necessarily title to a specific batch of raw sugar but it is nevertheless a 'property right'⁴⁴
- our view is that the mill is paid to crush the cane with this compensation, the cane price formula is agreed by millers and growers, through the formula millers are paid by growers to manufacture sugar, after being paid for this service how can millers believe they own the end product⁴⁵

However, growers appear to have a common position about the rights that some more formal recognition of GEI should provide:

- growers are as much entitled as the millers are to have a say in how the raw sugar price is determined (and how the raw sugar is marketed)⁴⁶
- legal title to raw sugar, arising under the current CSAs is not carte-blanche for a mill to expropriate the property rights of every sugar cane grower⁴⁷
- growers should have choice about who markets their GEI sugar.⁴⁸

2.2.4 Concern about the future role of QSL

QSL is well respected by many growers. CANEGROWERS Burdekin has expressed that:

³⁸ Tablelands Canegrowers Ltd (October 2015). Submission to Queensland Productivity Commission, page 2

³⁹ Burdekin District Cane Growers Limited (October 2015). Submission to Queensland Productivity Commission, page 5-6

⁴⁰ Tablelands CANEGROWERS Ltd (2015). Submission to Agriculture and Environment Committee, page 2

⁴¹ Canegrowers Herbert River (October 2015). Submission to Queensland Productivity Commission, page 2

⁴² CANEGROWERS Cairns Region (2015). Submission to Agriculture and Environment Committee, page 1

⁴³ CANEGROWERS and ACFA (2015). Submission to Agriculture and Environment Committee, page 6

⁴⁴ SISL Group (2015). Submission to the Agriculture and Environment Committee, page 3

⁴⁵ CANEGROWERS Burdekin (November 2015). Submission to the Queensland Productivity Commission, page 3

⁴⁶ SISL Group (2015). Submission to Agriculture and Environment Committee, page 3

⁴⁷ SISL Group (2015). Submission to Agriculture and Environment Committee, page 3

⁴⁸ Tablelands Canegrowers Ltd (October 2015). Submission to Queensland Productivity Commission, page 1

QSL is an Australian, not for profit, industry owned, niche marketing company that is the heart of our sugar marketing system, a system which has faithfully served the needs of the Queensland cane industry for over 100 years.⁴⁹

CANEGROWERS Isis commented

Growers have confidence in this system, knowing that QSL's operations always benefit the parties, are transparent, and all the proceeds from the marketing are distributed between growers and millers in accordance with the established agreements regarding the sharing of sugar proceeds.

The QSL marketing model has helped to provide stability and consistency in what is a very volatile marketing environment. This model gives some comfort to growers who struggle through difficult times to maintain their sugarcane production.

We believe if growers lose access to QSL and the benefits this marketing model provides, this will jeopardise the areas planted to sugarcane thereby threatening the viability of the local industry and tonnages available to Isis Mill.⁵⁰

The potential impact on QSL of the decision by the larger millers to discontinue with their RSSAs is also a concern for growers. These concerns include⁵¹:

- a reduction in tonnage through QSL will affect QSL's credit rating and borrowing facilities⁵²
- QSL and millers competing against each other in the same markets for premium quality Australian sugar will result in erosion of the premiums distributed to growers and millers
- millers will use their monopoly market power to substantially damage or eliminate QSL as a competitor and eliminate QSL as the Australian marketer
- loss of transparency will mean growers will not know if they receive the correct price for their sugar⁵³
- loss of security of cane payments, as QSL funds the advance payment system to growers. A replacement would be up to the result of negotiations with millers about CSAs
- concern that QSL's loss of control of terminals will increase costs and lose the benefit of a pooled cost across higher and lower cost terminals
- an inability to manage sugar quality issues, as QSL is able to blend all the sugar to manage quality issues
- a loss of the growers share in 100 per cent of the profits generated from QSL's trading activities.

However, many growers stressed that they are not advocating a return to the single desk arrangement.

2.2.5 Need for an adequate dispute resolution system

Several grower organisations commented that there is no adequate process to resolve deadlocks in negotiations and noted this is especially important given there is no competition for milling services. These concerns include:

⁴⁹ Burdekin Canegrowers (November 2015). Submission to the Queensland Productivity Commission, page 1

⁵⁰ CANEGROWERS Isis (2015), Submission to Agriculture and Environment Committee, page 1

⁵¹ Tableland Canegrowers Ltd (October 2015). Submission to Queensland Productivity Commission, page 2

⁵² Tableland Canegrowers Ltd (2015). Submission to Agriculture and Environment Committee, page 2

⁵³ Canegrowers Herbert River (October 2015). Submission Queensland Productivity Commission, page 2

- collective bargaining by growers has proven ineffective in circumstances where there has been a monopoly miller and no process to resolve deadlocks in negotiations⁵⁴
- there is no statutory or mandatory dispute resolution process in the SIA to assist growers and millers resolve commercial disputes in a mutually beneficial manner when negotiating the terms of a CSA.⁵⁵⁵⁶⁵⁷⁵⁸

2.2.6 Concern about adverse impacts on future investment in Queensland cane farms

Several grower organisations expressed concern that without action to provide grower certainty about GEI and the choice of marketer, numerous growers could leave the industry and/or cease to invest. Particular concerns include:

- the loss of choice and the subsequent uncertainty will not give growers the confidence to expand⁵⁹ and could quite possibly spell the withdrawal of cane land and lessened investment in the local sugar cane industry⁶⁰⁶¹
- absence of certainty could have a negative impact on third party investment given 'it is difficult to imagine any new entrant (whether domestic or foreign) looking favourably at an investment in sugar cane farms where the revenue stream is effectively a 'farm gate' price that can be dictated or manipulated by the activities of a monopoly buyer'⁶²
- continued erosion of grower confidence, especially on top of the current low sugar prices, has fuelled greater competition for land as growers exit the industry and growers are considering planting alternative crops/trees...removal of grower choice in marketing will accelerate the change away from sugarcane production⁶³
- there could be knock on impacts for the regional economies.⁶⁴

2.2.7 Changes sought by growers

The Bill encapsulates the changes being sought by some growers and grower organisations to address the problems they perceive with the existing regulatory arrangements to address the imbalance in market power and absence of grower choice about how GEI is marketed.

2.2.8 Other issues raised in response to the Consultation RIS

In our Consultation RIS, we asked whether there were other grower concerns that should be taken into consideration. We received the following responses:

- Concern was expressed that growers will lose the benefits of QSL, which they note offers buyers a unique niche supplier.⁶⁵
- Wilmar Sugar Australia (WSA) advised CANEGROWERS Burdekin that they will be signing a 15 year contract with a Singaporean trading company to market the raw sugar. Concern that this

⁵⁴ CANEGROWERS and ACFA (2015). Submission to Agriculture and Environment Committee, page 5

⁵⁵ Tableland Canegrowers Ltd (October 2015) Submission Queensland Productivity Commission, page 3

⁵⁶ Burdekin District Cane Growers Ltd (October 2015). Submission Queensland Productivity Commission, page 4

⁵⁷ Burdekin District Cane Growers Ltd (2015). Submission to Agriculture and Environment Committee, page 2

⁵⁸ CANEGROWERS and ACFA (2015). Submission to Agriculture and Environment Committee, page 5

⁵⁹ Bondrogers Farming Pty Ltd (2015). Submission to Agriculture and Environment Committee, page 1

⁶⁰ Tableland Canegrowers Ltd (2015). Submission to Queensland Productivity Commission, page 2

⁶¹ Canegrowers Cairns Region (2015). Submission to Agriculture and Environment Committee, page 2

⁶² SISL Group (2015). Submission to Agriculture and Environment Committee, page 4

⁶³ CANEGROWERS Isis (November 2015). Submission to Queensland Productivity Commission, page 4

⁶⁴ CANEGROWERS Innisfail (2015). Submission to Agriculture and Environment Committee, page 3

⁶⁵ CANEGROWERS Burdekin (November 2015). Submission to Queensland Productivity Commission, page 2

arrangement has the potential to damage the milling company WSA and that Wilmar International could sell the mills once the 15 year lock in contract is in place.⁶⁶

- We did not report the results of a detailed assessment of market structure, market conduct or performance under current structures, those proposed by Wilmar, MSF and Tully post-2017 or under the contestable market environment envisaged in the provisions of the Real Choice in Marketing Bill.⁶⁷

2.3 QSL views

QSL's pricing and marketing model provides four key service areas to members:⁶⁸

<i>Financing</i>	<i>Pricing</i>	<i>Marketing</i>	<i>Logistics</i>
Providing low-cost financing through advance payments to members	Providing knowledge, expertise and experience in managing futures markets	Maximising returns through optimising sales timing and customer premiums	Safe and efficient storage, handling and shipping of raw sugar

QSL considers its pricing and marketing model benefits Queensland growers including:⁶⁹

- through structures like limits on raw sugar which can be forward priced or sold without physical delivery, there is a more cautious approach taken to managing downside risks
- the RSSAs provide some parameters around how QSL markets and prices raw sugar and calculates the returns provided to mill owners (which can then be referred to in CSAs), providing greater certainty and transparency for growers; and
- it does not have the conflict of interests that other international sugar traders do as a result of their non-Australian based trading businesses.

QSL is of the view that changes to current title arrangements are not necessary and that it is possible to implement a Grower Choice system under the current SIA through a commercial arrangement acceptable to all parties.

QSL supports introducing a Grower Choice system where farmers are able to choose who markets their GEI sugar, and that millers would be encouraged to attract economic interest volumes from growers by providing competitive marketing services.

QSL is concerned if no action is taken this will:⁷⁰

- cause uncertainty with negative impacts on grower investment
- impact its ability to actively manage price risk by forward pricing on the ICE No.11 Futures Market; and
- negatively impact some millers – those exiting the current marketing system may potentially face reductions in cane supply.

QSL says that when considering ways to achieve a competitive raw sugar marketing system certain key elements are required including:⁷¹

⁶⁶ CANEGROWERS Burdekin (November 2015). Submission to Queensland Productivity Commission, page 2

⁶⁷ CANEGROWERS and ACFA (November 2015). Submission to Queensland Productivity Commission, page 11

⁶⁸ QSL (2015). Submission to Agriculture and Environment Committee, page 1

⁶⁹ QSL (2014). Submission to the Federal Rural and Regional Affairs & Transport References Committee, page 16

⁷⁰ QSL (2015). Submission to Agriculture and Environment Committee, page 2

⁷¹ QSL (2015). Submission to Agriculture and Environment Committee, page 3

- an obligation for millers and growers to negotiate in good faith regarding the terms on which cane is supplied
- CSAs providing for the cane price to be referable to the market price obtained from a corresponding quantity of raw sugar, and giving the grower the right to choose the entity which will market the GEI
- obligations on millers to publish specified information to growers in relation to their marketing activities; and
- a prohibition on millers discriminating against growers who choose to have an entity other than the mill owner of their affiliates market their GEI.

2.3.1 Other issues raised in response to Consultation RIS

In our Consultation RIS, we asked whether there were other concerns about QSL that should be taken into consideration. Issues raised include the following:

Storage

- The RIS has not recognised or valued the important role QSL’s management of the State’s storage facilities play in Queensland’s raw sugar export marketing system.⁷²
- Under QSL’s current operating system, the storage assets are managed in a pooling environment where this overall benefit can be shared by the entire industry. Unless a commercial agreement can be reached, the operation of the storage assets will not be on a pooled basis beyond the 2016 Season. Therefore some industry participants will not have access to the same amount of storage as they do under the current system. Subsequently, some will not have the same flexibility over the timing of sales and associated pricing on the ICE 11 that they have under the current system. This will result in a direct and negative impact on the return to impacted mill owners and their growers.⁷³

Pricing

- The RIS has incorrectly assumed that QSL will be able to continue to offer pricing services to all growers post-2017. This is not the case, nor is it true of the current arrangement...Cane growers are currently given the ability to choose a pool pricing product to match their risk profile, and have the ability to price sugar at their own discretion on QSL’s pricing book. Whether the range of current services will still be available to all growers beyond 2017 is not guaranteed. As a not-for-profit entity, QSL requires a contractual raw sugar supply commitment and the consequent title that this provides to be able to offer these services.⁷⁴
- The assumption that QSL will be able to continue to offer pricing services to all growers post-2017 is not correct. This is not the case under current arrangements. Presently not all mills offer the full suite of QSL pricing options available to their growers. The range of QSL pricing options made available to growers is exclusively a mill decision.⁷⁵
- QSL also considered that if the current positions of Wilmar, Tully Sugar and MSF do not change, the growers supplying these millers will be prevented from using QSL (a company both growers and millers own) in the 2017 and future seasons.⁷⁶

⁷² QSL (November 2015). Submission to the Queensland Productivity Commission, page 3

⁷³ QSL (November 2015). Submission to the Queensland Productivity Commission, page 3

⁷⁴ QSL (November 2015). Submission to the Queensland Productivity Commission, page 4

⁷⁵ CANEGROWERS and ACFA (November 2015). Submission to Queensland Productivity Commission, page 12

⁷⁶ QSL (November 2015). Submission to the Queensland Productivity Commission, page 4

2.4 Miller views

Unlike some growers and grower organisations, millers generally have not expressed concerns about the existing regulatory framework. They are however, particularly concerned about the impacts on their businesses if the Bill is to be passed. A summary of miller views is provided below.

Millers were generally satisfied that we had accurately reflected their views.⁷⁷⁷⁸⁷⁹

2.4.1 Current regulatory environment is effective

Millers consider that:

- the current regulatory environment of the sugar industry in Queensland is effective⁸⁰
- there are adequate protections under the SIA;⁸¹⁸² and
- any disputes should be resolved through commercial negotiation rather than government intervention.

Millers consider that increases in regulation are not required due to the co-dependent nature between millers and growers⁸³. Wilmar considers

Regulation is not required to achieve the outcome of mills acting in the best interests of cane farmers. This is because millers' investment is highly sensitive to and dependent on cane values. If mills were to seek to reduce payments to growers, mill cane supply would decline and mill profitability would also decline.⁸⁴

Tully Sugar believes that

there is no evidence of market failure in the industry under the current or proposed arrangements and therefore no need for legislated intervention or reregulation of the Sugar Industry⁸⁵.

Millers also consider that appropriate dispute resolution services are already available⁸⁶⁸⁷. Wilmar's submission to the AEC noted that:

- commercial dealings of sugar industry participants are subject to other state and Commonwealth regulation which provide adequate countervailing forces to ensure appropriate conduct of parties⁸⁸
- the SIA authorises grower collective bargaining for the purpose of negotiating CSAs; and
- existing and proposed cane supply contracts already provide a process of discussion and mediation administered by the Australian Commercial Disputes Centre and final and binding arbitration subject to the *Commercial Arbitration Act 2013 (Qld)*.⁸⁹

⁷⁷ ASMC (November 2015). Submission to the Queensland Productivity Commission, page 1

⁷⁸ Wilmar (November 2015). Submission to Queensland Productivity Commission, page 1

⁷⁹ MSF Sugar (November 2015). Submission to Queensland Productivity Commission, page 1

⁸⁰ Wilmar (2015). Submission to Agriculture and Environment Committee, page 6

⁸¹ Tully Sugar Limited (2015). Submission to the Queensland Productivity Commission, page 4.

⁸² MSF Sugar (2015). Submission to the Agriculture and Environment Committee, page 5

⁸³ ISIS Central Sugar Mill Co. Ltd (2015). Submission to the Queensland Productivity Commission, page 3

⁸⁴ Wilmar (2015). Submission to Agriculture and Environment Committee, page 65

⁸⁵ Tully Sugar Limited (2015). Submission to the Queensland Productivity Commission, page 4

⁸⁶ ASMC (2015). Submission to Agriculture and Environment Committee, page 3

⁸⁷ Wilmar (2015). Submission to Agriculture and Environment Committee, page 4

⁸⁸ Wilmar (2015). Submission to Agriculture and Environment Committee, page 7

⁸⁹ Wilmar (2015). Submission to Agriculture and Environment Committee, page 10

2.4.2 Miller marketing will increase premiums

Wilmar states that the benefit of marketing its raw sugar through Wilmar Sugar Trading is its ability to use its scale and expertise to generate higher premiums, which it estimates to be around \$46.4 million per annum compared to marketing raw sugar through QSL.⁹⁰ We note that these estimates have been disputed by QSL.

Wilmar has said it will share any gains with growers, together with a share of any net trading value generated from arbitrage opportunities that arise due to Wilmar Sugar Trading's global sugar trading presence and marketing expertise.⁹¹ It indicated its growers would receive \$36.3 million of these additional premiums.⁹²

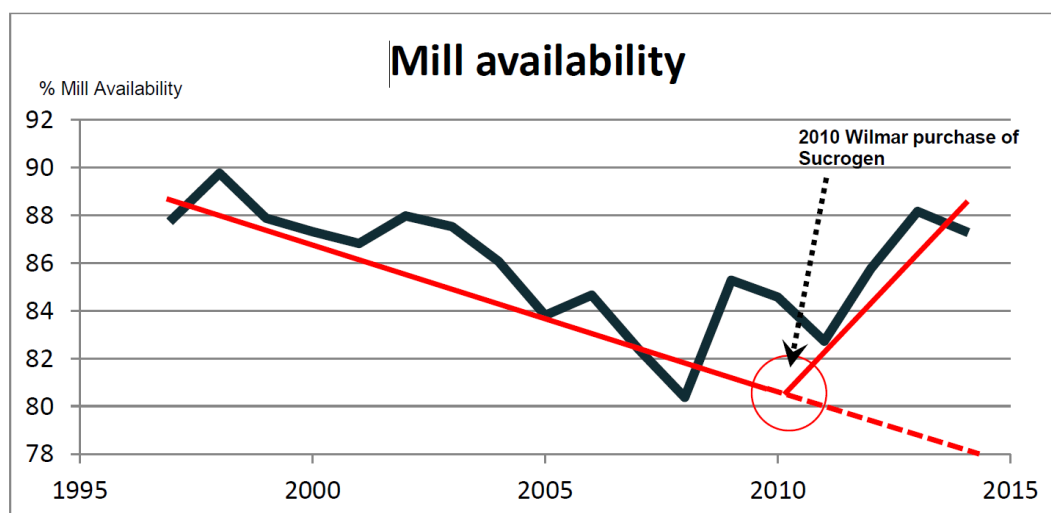
2.4.3 Deregulation has increased investment and innovation in the sugar industry

Millers pointed to the significant re-investment in the sugar industry since 2006 as evidence that the regulatory arrangements post deregulation are effective and generating results.^{93,94}

Wilmar considers that before they entered Queensland in 2010, mill reliability was suffering as a result of significant underinvestment and that its \$530 million investment in upgrading existing assets has improved mill reliability (as shown below in **Figure 2**). This has

equated to shorter season lengths and greater returns to growers due to crushing a higher proportion of cane at increased levels of sugar content. This has also reduced milling costs and increases milling recovery, as losses are reduced through fewer unplanned stoppages.⁹⁵

Figure 2 Wilmar mill availability showing the impacts of reinvestment



Source: Wilmar submission to Queensland Productivity Commission (November 2015)⁹⁶

Wilmar also pointed to deregulation having increased the range of pricing methods and pools available to growers allowing growers to undertake their price risk management independently from the price risk management of their miller.

⁹⁰ Wilmar (October 2015). Submission to Queensland Productivity Commission, page 23

⁹¹ Wilmar (October 2015). Submission to Queensland Productivity Commission, page 22

⁹² Wilmar (October 2015). Submission to Queensland Productivity Commission, page 23

⁹³ Wilmar (October 2015). Submission to Queensland Productivity Commission, page 11

⁹⁴ MSF Sugar (October 2015). Submission to Queensland Productivity Commission, page 11

⁹⁵ Wilmar (October 2015). Submission to Queensland Productivity Commission, page 11

⁹⁶ Wilmar provided a revised graph as part of its November 2015 submission.

The ASMC noted that deregulation in 2006

- *has given the Queensland sugar industry the flexibility to better respond to challenges posed by global market competition... provided the opportunity for individual milling regions to be more commercially responsive and better able to take advantage of niche market opportunities as they arise*⁹⁷
- *delivered ground breaking innovation, with the introduction of forward pricing and price and currency risk management tools... now embraced by approximately 70 per cent of Queensland cane growers*⁹⁸

MSF Sugar noted that:

*Over the past two years, the foreign owners of MSF Sugar have invested around \$240 million of new capital into the Australian operations. In addition to the corollary benefits to the Queensland and local economics, this investment has generated significant improvements in productivity.*⁹⁹

CANEGROWERS and ACFA considered that the miller investment was directed at returning previously rundown assets to the full operational potential and that this has created a distorted perception of new investment.¹⁰⁰

2.4.4 Regulatory intervention would have a negative impact on investment

Millers are very concerned about proposals at the state and national levels for potential regulatory intervention in the sugar industry. Millers consider that further regulatory intervention into the industry would:

- undermine investment and implications for their business
- impair asset values; and
- fundamentally alter the structure and operation of the sugar industry supply chain.

Millers are also concerned with the return of 'pre-contract arbitration', as it 'was removed with the agreement of all industry stakeholders'¹⁰¹ as part of deregulation and did not appear to exist in any other business context between a supplier and a processor/manufacturer.¹⁰²

ASMC also considered that pre-contract arbitration would be an added cost to business, would reduce the motivation for business to negotiate in good faith, and that 'commercial negotiation is going to produce better outcomes than one imposed by an arbitrator'.¹⁰³

2.4.5 Other issues raised in response to the Consultation RIS

ASMC considered the RIS has summarised the views of millers accurately in that the current regulatory environment of the sugar industry in Queensland is effective, that there are adequate protections under the Sugar Industry Act and that any disputes should be resolved through commercial negotiation rather than government intervention.¹⁰⁴

⁹⁷ ASMC (2015). Submission to Agriculture and Environment Committee, page 2

⁹⁸ ASMC (2015). Submission to Agriculture and Environment Committee, page 2

⁹⁹ MSF Sugar (2015). Submission to Queensland Productivity Commission, page 2

¹⁰⁰ CANEGROWERS and ACFA (November 2015). Joint submission to Queensland Productivity Commission, page 12.

¹⁰¹ Wilmar (2015). Submission to Agriculture and Environment Committee, page 4

¹⁰² ASMC cited in Agriculture and Environment Committee (2015), page 20

¹⁰³ ASMC cited in Agriculture and Environment Committee (2015), page 20

¹⁰⁴ ASMC (November 2015). Submission to Queensland Productivity Commission, page 2

2.5 National reviews of sugar industry marketing

2.5.1 Senate Inquiry into Current and Future Arrangements for the Marketing of Australian Sugar

On 4 September 2014, the Australian Senate moved that the current and future arrangements for the marketing of Australian sugar be referred to the Rural and Regional Affairs and Transport Reference Committee for inquiry and report by 27 November 2014.

On 24 June 2015, the Committee provided a report that recommended

*the development and implementation of a mandatory sugar industry Code of Conduct, acknowledging that, provided appropriate stakeholder consultation is undertaken, the work of the Sugar Marketing Code of Conduct Taskforce may provide a foundation upon which a Code of Conduct may be established.*¹⁰⁵

In forming this view, the Committee noted:

- *that any move toward re-regulation would be contrary to the stated policy objectives of both the state and Commonwealth governments. More importantly, the Committee is of the view that any move toward re-regulation of the industry would not be in the best interests of the industry – particularly over the longer term*
- *that cane growers and their representative bodies have very real concerns about the potential which would exist, under new arrangements, for milling companies to misuse their market power.*
- *current ownership structures for sugar are determined by the provisions of CSAs. ... historically, title to sugar had not been an issue because any financial gain from the sale of sugar was shared between growers and millers... under Queensland Government legislation – at the crucial stage of marketing and selling – title to the raw sugar was vested in QSL (and its predecessors)*
- *there is a legal framework which underpins the negotiation of CSAs...the framework includes provisions in relation to:*
 - *access to collective bargaining;*
 - *provisions for unconscionable conduct; and*
 - *misuse of market power.*
- *doubts... about whether the current framework will prove sufficient for growers and millers to work their way through the current impasse and reach agreement on new CSAs and, ultimately, on the future of the industry*
- *not convinced that the existing legal framework is adequate – particularly given that the problems currently facing the industry are in large part due to the imbalance of bargaining power between growers and millers...there is a need for the industry to develop and implement a mandatory Code of Conduct*
- *a mandatory Code of Conduct would provide stakeholders with access to impartial, affordable dispute resolution processes and would go some of the way to addressing the inequities in bargaining power between millers and growers... and should include formal dispute resolution frameworks which support both growers and millers negotiating supply contracts.*

Submissions made to the Senate Committee are publicly available.¹⁰⁶

¹⁰⁵ Senate Select Committee on Rural and Regional Affairs and Transport (2015), page 7

¹⁰⁶ http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Rural_and_Regional_Affairs_and_Transport/Sugar

2.5.2 Sugar Marketing Code of Conduct Taskforce

On 10 December 2014, the Federal Minister for Agriculture, the Honourable Barnaby Joyce MP, announced the establishment of a Sugar Marketing Code of Conduct Taskforce to consult with the sugar industry on a range of issues around marketing and export arrangements for cane growers.

On 25 June 2015, the Taskforce recommended that a Mandatory Code of Conduct be adopted for the sugar industry that addressed the following key points:

- a mechanism to distribute relevant interests in the quantities of sugar obtained from cane between growers and millers
- a link between the price paid for cane and the selling price of sugar
- the ability to choose marketing services
- non-discriminatory provisions
- a mechanism to resolve disputes.¹⁰⁷

Submissions to the Taskforce are not publicly available.

¹⁰⁷ <http://www.georgechristensen.com.au/taskforce-recommends-sugar-code-of-conduct/>

3 PROBLEM IDENTIFICATION AND POLICY OBJECTIVES



The objective of any regulatory action is to improve situations for business, community and government that cannot be improved through existing business and social institutions and mechanisms. A RIS should clearly set out the objectives of the regulatory proposal in terms of what is to be achieved, and any constraints on the objectives should be identified.

Amongst other things, a RIS needs to consider:

- *the issue(s) that need to be addressed, including identifying the extent of market failure which suggest the need for intervention*
- *what is causing the problem(s)?*
- *what is the size of the problem?*
- *who is affected?*
- *what is the probability of the problem occurring?*
- *what are the risks and consequences of maintaining the status quo (taking no action).*

This Chapter sets out the policy objectives of the Bill and tests the case for some form of regulatory intervention in the Queensland sugar industry. In particular we have considered the extent to which market failure may be present in the Queensland sugar industry. We also make an estimate of the size of the issue.

We consider the risks and consequences of taking no action in Chapter 4.

3.1 Policy objectives

The clause 3 of SIA states that the object of the Act is:

to facilitate an internationally competitive, export oriented sugar industry based on sustainable production that benefits those involved in the industry and the wider community.

The stated intention of the Bill is to prevent anti-competitive behaviour and promote pro-competitive outcomes; and ensure economic viability for both growers and mill owners in the Queensland sugar industry.

In this context, the Bill proposes to amend the SIA with the objectives of:¹⁰⁸

- (a) providing growers (and their representatives) with a new right to a statutory arbitration process to resolve contractual and pre-contractual disagreements related to supply contracts.
- (b) prescribing terms that must be included in a grower, miller supply contract

¹⁰⁸ Agriculture and Environment Committee Report 2015, page 17

- (c) establishing growers economic interest (GEI) (proportion of raw sugar for which they bear a sale price exposure)
- (d) allowing growers to nominate their choice of marketing entity for their proportion of GEI sugar.

Strictly speaking, the matters indicated in (a) to (d) would be considered a policy response rather than policy objectives themselves. To prepare the RIS, we have considered it necessary to identify the underlying policy objectives behind the measures set out in the Bill.

Seeking to understand the underlying objectives is consistent with the statutory interpretation approach (particularly used when there is no objects clause) of seeking to identify the ‘mischief’ the legislation is responding to.

Taking into account the objectives of the Bill, the objects clause of the SIA, and the issues identified by stakeholders we consider the policy objectives the sugar industry regulation is seeking to achieve are:

- to ensure a pricing framework where there is an appropriate balance of risk and reward between growers and millers
- to ensure that there are appropriate protections for growers and millers to prevent against the abuse of market power
- to ensure a regulatory framework that supports investment and innovation in the sugar industry and supports the long-term economic sustainability of the sugar industry.

We have used these objectives to consider the potential policy and regulatory responses.

Stakeholder responses to the Consultation RIS

We received the following responses to our draft impact assessment:

- QSL considers the policy objective not expressly mentioned in the RIS is to increase competition for provision of raw sugar marketing services.¹⁰⁹
- CANEGROWERS and ACFA said they supported the Real Choice in Marketing Bill because they consider it delivers on the policy objective of establishing a regulatory structure that prevents the misuse of market power, addresses market failure and establishes a competitive market. This overarching policy objective is consistent with National Competition Policy and strengthens the policy objectives identified and used by QPC.¹¹⁰

We have considered the issue of competition for the provision of raw sugar marketing services in more detail in section 3.5.

3.2 Framework for assessing regulatory impacts

As regulation can impose significant costs on business and the wider community, it is important that there is a clear rationale and strong case for introduction for any new regulation. Even where regulation may be successful in addressing a particular market failure, it might also involve costs that mean that overall it is not worthwhile.

Key questions to support government action include:

¹⁰⁹ QSL (2015). Submission to Queensland Productivity Commission. Page 4

¹¹⁰ CANEGROWERS and ACFA (November 2015). Submission to Queensland Productivity Commission, page 8

- Is there a market failure? This includes assessment of whether there are abuses of market power?
- Is the rationale for intervention clear? For example is there clear evidence of market failure?
- Is it reasonable to assume that the benefits of intervention will exceed the costs?

The RIS Guidelines state that the most common types of market failure are: incomplete property rights; market power; incomplete information; and missing and incomplete markets.¹¹¹ For this RIS, the key issues that need to be considered to establish a case for regulatory intervention are:

- What is the estimated value of net premiums to growers?
- Are there property rights in the Queensland sugar industry that are not being appropriately recognised?
- Do millers in the Queensland sugar industry have market power?
- Is there evidence that market power is being abused?
- Is there insufficient transparency between millers and growers that would give rise to millers not distributing net premiums to growers in accordance with the CSAs?
- Is there evidence that the dispute resolution arrangements in the Queensland sugar industry are not being effective in balancing the interests of growers and millers?
- Are changes needed to the SIA to promote competition in sugar marketing?

Each of these issues is considered below.

3.3 Value of premiums

A key objective of the Bill is to ensure that Queensland growers are receiving their share of the net premiums that arise from the sale of raw sugar. Net premiums form part of the CSA arrangements.

As discussed in section 1.6 the globally traded ICE No.11 contributes at least 95 per cent to the net sugar price, with Wilmar noting that five year average data from QSL(2009 to 2013 seasons) shows the net marketing premium is appropriately 1 per cent of the net sugar price.¹¹²

The component of the net sugar price which is linked to the world sugar price (and has the greatest impact on the price growers receive for sugar cane under the cane price formula) does not appear to change irrespective of who owns or markets the raw sugar (although some growers are concerned that a change of marketer may affect futures trading flexibility and returns.¹¹³ This is further discussed in section 4.2.2).

While premiums are an important component of the net sugar price and ultimately returns to the industry (comprising approximately 8 per cent of the net sugar price),¹¹⁴ 'net premiums' (premiums less marketing costs) are likely to comprise around one and perhaps up to five per cent of the net

¹¹¹ Queensland Treasury (2013) Regulatory Impact Statement System Guidelines, page 53

¹¹² Wilmar (November 2015). Submission to Queensland Productivity Commission, page 5

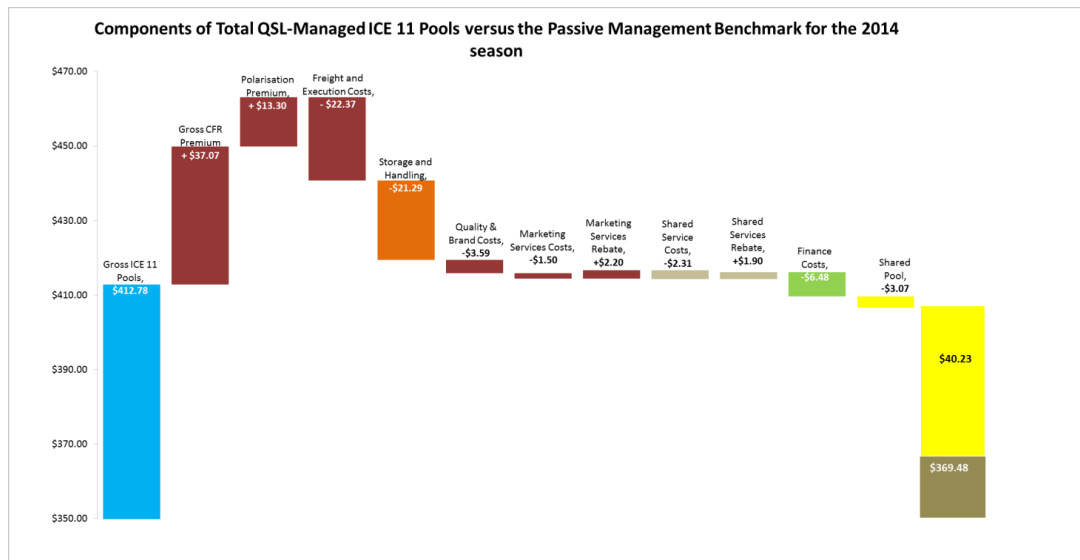
¹¹³ QSL and CANEGROWERS/ACFA consider that the marketer sets the timing of exposure of pricing on ICE 11 and optimises the sales against the right futures contract, and that it requires skill to manage variations in exposure risk. QSL (2015) Submission to the Queensland Productivity Commission, pages 4-5. CANEGROWERS and ACFA (November 2015), Submission to the Queensland Productivity Commission, page 16.

¹¹⁴ Wilmar (October 2015). Submission to Queensland Productivity Commission, page 6

sugar price. We do note, however, that premiums are likely to be considered more important to smaller cane farming operations than larger operations.¹¹⁵

CANEGROWERS and ACFA noted that all revenues and costs associated with QSL’s marketing activities are, in addition to the raw sugar futures price, shared between both growers and millers through the operation of ‘shared pools.’ In addition, they state that ‘the shared pool receives in excess of \$250 million in revenue and defrays a similar amount in costs each year’¹¹⁶, and that optimising each component of premiums and minimising each element of costs is ‘a significant management task’.¹¹⁷ Figure 3 shows how market premiums offset the costs of exporting raw sugar.

Figure 3 Components of Total QSL-Managed ICE 11 Pools versus the Passive Management Benchmark for the 2014 Season



Source: QSL (November 2015)

Millers consider that the recent net premiums achieved above the global sugar price, were small in comparison to the net sugar price. MSF considers that the

Year on Year difference between the ICE11 raw sugar price and Psugar [net sugar price] will be plus/minus \$5 per tonne of raw sugar.¹¹⁸

If the range provided by MSF is correct, based on estimated production of 4.2 million tonnes of raw sugar per annum¹¹⁹, net premiums represent (in aggregate across the industry) a range of plus or minus \$21 million per annum. Assuming that this is distributed between growers and millers at a ratio of 2:1, the value of the net premium to growers is approximately \$14 million per annum.

Table 4 Estimated value of net premiums to growers based on 2014 raw sugar production

Raw sugar production (tonnes)	4,200,000
Net premium per tonne	\$5.00
Total value of net premium	\$21,000,000
% of grower return	66.67%
Value of grower net premium	\$14,000,000

¹¹⁵ Canegrowers Rocky Point (2015). Submission to the Queensland Productivity Commission, page 3

¹¹⁶ CANEGROWERS and ACFA (2015). Submission to the Agriculture and Environment Committee, page 9

¹¹⁷ CANEGROWERS and ACFA (2015). Submission to the Queensland Productivity Commission, page 3

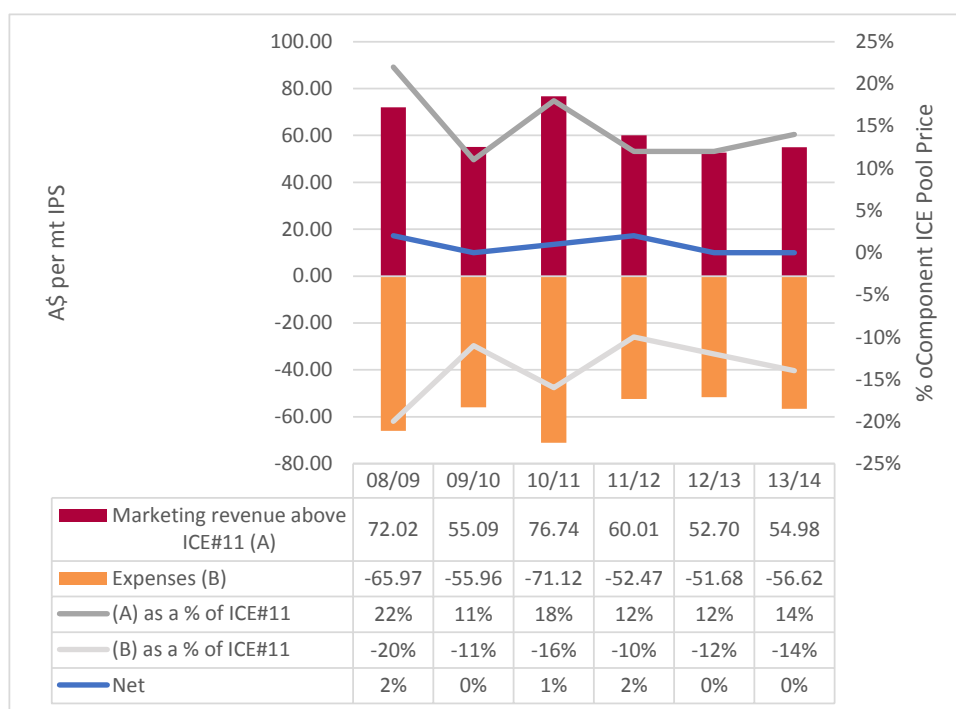
¹¹⁸ MSF (2015). Submission to Agriculture and Environment Committee, page 14

¹¹⁹ Based on an estimated 4.2 million tonnes of raw sugar produced in Queensland in 2014

Figure 4 shows QSL’s marketing revenue above ICE No.11 for the period 2008-09 to 2013-14.¹²⁰ It shows the variability in net premiums over the period has ranged between \$7.54 per tonne raw sugar and (\$1.66) per tonne raw sugar over the period 2008-09 to 2013-14:

- at \$7.54 per tonne raw sugar, the net premium is approximately \$31.67 million, with growers share being (2:1) \$21.1 million¹²¹
- at (\$1.66) per tonne raw sugar the net premium (loss) is approximately (\$6.97) million with growers share being (2:1) (\$4.65) million.

Figure 4 QSL marketing revenue above ICE No, 11 2008-09 to 2013-14



Source: QSL submission to Senate Inquiry

QSL has noted that given the size of recent marketing revenue and costs (with marketing revenue ranging between \$52.70–\$76.74 above the ICE No. 11 price and expenses of between \$51.68–\$71.12 per tonne of raw sugar):

that marketing performance and costs can have a substantial influence on the ultimate return achieved by growers.

However, ASMC’s submission to us states that

while the marketing premium is an important element of the payment made to growers for sugarcane, it is vastly outweighed by the impact of variation in ICE11 and CCS variability¹²²

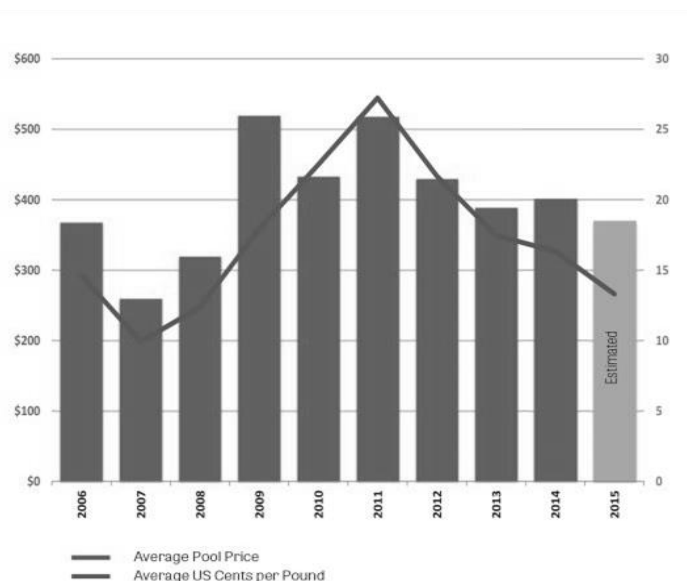
While under the net sugar price formula a \$1 movement in net premiums will have the same effect as a \$1 movement in ICE No. 11 prices, we note that the variations of the ICE No. 11 price (Figure 5) are likely to be larger than net premiums.

¹²⁰ QSL (2014). Supplementary submission to the Senate Select Committee on Rural and Regional Affairs and Transport, page 4

¹²¹ This is based on 100 per cent of raw sugar production of 4.2 million tonnes of raw sugar (both domestic sales and exports) and could be considered an ‘upper bound.’

¹²² ASMC (October 2015). Submission to Queensland Productivity Commission, page 15

Figure 5 World Sugar Prices 2006 - 2014



Source: CANEGROWERS Australia¹²³

This variability, combined with the fact that net premiums comprise a small percentage of the net sugar price, is likely to result in changes to the net premium having less of an impact on returns to growers and mills compared to other factors such as the ICE No. 11 price.

This is demonstrated from the results of our analysis of the sensitivity of key variables to the returns to both growers and millers. Compared to an initial baseline¹²⁴ we have estimated that, under the cane price formula, a 1 per cent (refer to table below):

- Change in net premium, from \$7.54¹²⁵ per tonne to \$7.6154 per tonne, would increase aggregate grower returns by approximately \$0.19 million per annum.
- Increase in ICE No. 11, from \$423.40¹²⁶ per tonne to \$427.63 per tonne, would increase aggregate grower returns by approximately \$10.56 million.
- Appreciation of the Australian dollar against the US dollar (which then impacts the ICE No. 11 price ultimately passed through to the net sugar price) would reduce aggregate grower returns by approximately \$10.46 million while a 1 per cent depreciation would increase grower returns by approximately \$10.67 million.
- Change in CCS, from 13 to 13.13, will increase aggregate grower returns by approximately \$15.53 million.
- Increase in annual cane production, from 30.8 million tonnes to 31.108 million tonnes, will increase aggregate grower returns by approximately \$10.94 million.

These results are summarised in **Table 5**.

¹²³ http://www.canegrowers.com.au/page/Industry_Centre/industry-focus/statistics-facts-figures/ accessed 13 October 2015

¹²⁴ Assuming a baseline scenario of ICE No. 11 = \$423.40, Net premium = \$7.54, CCS = 13 and constant = 0.608.

¹²⁵ A \$7.54 net premium achieved by QSL in 2011-12 appears to be the largest between 2008-2009 and 2013-2014

¹²⁶ ICE No.11 based on March 2016 futures contract price, as stated on QSL website 6 October 2015.

Table 5 Sensitivity of returns from sale of export raw sugar

<i>Variable</i>	<i>Baseline value</i>	<i>Amended value</i>	<i>Difference in returns (\$M)</i>
Net Premium (per tonne)	\$7.54	\$7.6154	0.19
ICE NO. 11 (per tonne)	\$423.40	\$427.63	10.56
Appreciation in AUD/USD (converted to ICE No. 11 price, per tonne)	\$423.40	\$419.21	(10.46)
Depreciation in AUD/USD (converted to ICE No. 11 price, per tonne)	\$423.40	\$427.68	10.67
CCS	13.00	13.13	15.53
Annual Cane Production (m tonne)	30.8	31.108	10.94

Source: Queensland Productivity Commission

While no stakeholders disputed our sensitivity analysis, we note the ASMC in its submission on the Consultation RIS stated that:

In addition, the points being made through the use of the aggregate levels in the examples (Table 5 and the discussion following Figure 5) could be enhanced through the addition to the values described on a per-tonne-of-sugarcane basis as set out below based on the Queensland sugarcane crop in 2011 of 26,329,304 tonnes:

- *Change in net premium from \$7.54 per tonne (of sugar) to \$7.6154 per tonne, would increase aggregate grower returns by approximately \$0.19 million per annum **or by less than one cent per tonne of cane***
- *Increase in ICE No. 11, from \$423.40 per tonne (of sugar) to \$427.63 per tonne, would increase aggregate grower returns by approximately \$10.56 million or by **forty cents per tonne of cane.***¹²⁷

3.4 Are there property rights in the Queensland sugar industry that are not being appropriately recognised?

As set out in section 2.2.3, there are varying views amongst growers about the extent to which growers have a level of ownership of the raw sugar produced by mills. CANEGROWERS Burdekin expressed that:

*Much has been made as to who owns the sugar in the current marketing debate. The only legal reference on this point is contained with the CBL CSA and is as follows: 6.3 Risk and title: Title and risk in the Cane shall pass to Wilmar Sugar immediately upon delivery of the Cane to Wilmar Sugar at the Delivery Point.*¹²⁸

and

*our view is that the mill is paid to crush the cane with this compensation, the cane price formula is agreed by millers and growers, through the formula millers are paid by growers to manufacture sugar, after being paid for this service how can millers believe they own the end product?*¹²⁹

What is the legal position?

The title to Queensland cane and raw sugar products is agreed through the terms of commercial contracts. Under the existing contracts, growers pass title of cane to millers at point of delivery to the mills. Millers pass title of the raw sugar to QSL at the point of delivery to QSL (under the RSSAs) and QSL sells raw sugar to international buyers, with title transferring on delivery. The existing relationships are shown in **Figure 6**.

¹²⁷ ASMC (November 2015). Submission to the Queensland Productivity Commission, page 2

¹²⁸ CANEGROWERS Burdekin (November 2015). Submission to Queensland Productivity Commission, page 7

¹²⁹ CANEGROWERS Burdekin (November 2015). Submission to Queensland Productivity Commission, page 3

Figure 6 Title transfers across the sugar supply chain



In some instances, mills purchase back raw sugar from QSL for their own marketing. The first step toward millers marketing raw sugar has been for some millers to amend the contract arrangements with QSL in order to purchase that proportion of the raw sugar produced in their mills and that they derive their profits from, back from QSL.

The AEC noted that Wilmar had termed this sugar Miller Economic Interest (MEI) sugar – which it had defined as raw sugar for which it has nominal price exposure. The defining of MEI has resulted in the consequential development of the phrase GEI sugar to refer to raw sugar that is not MEI sugar. The AEC also noted Wilmar’s position that the concept of GEI sugar does not imply any transfer of rights to any party.¹³⁰

In our Consultation RIS we said that we understand that the term ‘GEI’ has been used to express recognition that the Cane Pricing Formula works in a way so that growers obtain approximately two thirds of the final price and the millers one third of the final price.¹³¹ We also considered that it is recognition that the grower's actual revenue is a proportion of the final price.

We note that Wilmar disputed the premise that title to raw sugar is currently conferred to the miller through operation of a contractual arrangement between millers and growers. It said

*The miller owns the sugar because they created it and in the absence of any legal agreement between the miller and the grower to the contrary, ownership of the raw sugar resides with the miller who produces it. The miller doesn't gain title to the sugar because of an agreement with the grower.*¹³²

We consider this to be consistent with our conclusion that the current arrangements could be amended by way of agreement on a tolling arrangement.

However, we have not seen anything to suggest that legal title does not transfer to the miller and that the miller produces a different product than that delivered to it by the growers. That is recognising that they have an interest in the final price is neither a legal title nor ownership interest. We do not see evidence that the Cane Price Formula is a proxy for a tolling arrangement as is implied by CANEGROWERS Burdekin.¹³³

Of course the contractual arrangements between growers and millers post 2017 may be different in respect of legal title. It is by no means certain that a collective negotiation will result in the growers providing 100 per cent of the legal title to the millers, ie. they could seek to negotiate a

¹³⁰ AEC (2015), page 9

¹³¹ Wilmar considered that this is fundamentally incorrect, as millers and growers receive different net sugar prices, based on the price risk management decisions they make independently of each other. These decisions affect the ICE#11 price, which is approximately 99 per cent of the net sugar price. The net marketing premium from the physical sale of raw sugar makes up the remaining 1 per cent. Wilmar (November 2015). Submission to the Queensland Productivity Commission, page 5

¹³² Wilmar (November 2015). Submission to Queensland Productivity Commission, page 5

¹³³ CANEGROWERS Burdekin (November 2015). Submission to Queensland Productivity Commission, page 3

tolling arrangement. However, all the material we have received suggests that this is the most likely outcome.¹³⁴

In almost all other industries, a product is sold (and title transferred) at the time that the person who will process that product takes possession of the product. The courts have recognised this general principle. For example:

- In *Clough Mill Ltd v Martin*¹³⁵ the court found that a clause which purported to retain legal title in yarn that was supplied by the mill had been incorporated, or used as material for, other goods and that despite the attempt to retain title, title in the newly manufactured goods are owned by the manufacturer of those goods;¹³⁶ and
- In *Borden (UK) Ltd v Scottish Timber Products*¹³⁷ the court found that absent a specific contractual term to the contrary the supplier of resin which was used in manufacturing chipboard had no legal title to the chipboard.¹³⁸

It is necessary to consider whether the use of the concept of GEI in the pricing formula had a clear intent for the parties to actually vest legal title in the growers. In our view, the use of the concept of GEI was not intended to vest legal title in the growers but merely to recognise that the price the growers obtain is dependent on the price obtained for the ultimate product.

To change this position would require the industry to convert to a pure ‘tolling’ structure. We consider that would require a significant re-writing of CSAs, including the pricing provisions. In tolling circumstances, pricing is usually determined by a cost build up with a return on processing and related assets. As the entity who undertakes the tolling does not have any legal or property interest in the product being tolled, it takes no price risk in respect of the product. In the circumstances of the sugar industry, this would require the growers to take all of the risk in respect of the final price, and indeed on the costs of processing.

Despite the view presented by CANEGROWERS Burdekin, there is nothing that suggests that the Cane Price Formula has ever operated as a tolling arrangement and that growers have been paying the mills to manufacture sugar. We note the submission from CANEGROWERS/ACFA that indicates a similar conclusion in respect of the historic ownership arrangements:

***Title to raw sugar is determined by what is in the supply agreement.** Historically, growers have been comfortable with cane supply agreements prepared in the context of raw sugar supply agreements that together provide for title in the delivered cane to pass to the miller and the title in sugar upon manufacture and delivery to the delivery point (usually the nearby bulk sugar terminal) to pass to QSL. QSL, the industry owned not for profit marketer, then undertook the marketing for all interested parties. Growers and millers together shared in the risks and rewards associated with the sale of the sugar.*

If QSL is removed and the mill takes this function, it is not clear that growers will be comfortable with the same title arrangements. Growers may want to explore retention of title issues and/or tracing sale proceeds and/or associated trust issues in supply contracts. Mills, on the other hand, take a different view. Some mills have distributed a proposed cane supply agreement for 2017 and subsequent seasons which continue title in cane transferring to the mill and title in sugar retained

¹³⁴ Wilmar disputed the premise that title to raw sugar is currently conferred to the miller through operation of a contractual arrangement between millers and growers. It said the miller owns the sugar because they created it and in the absence of any legal agreement between the miller and the grower to the contrary, ownership of the raw sugar resides with the miller who produces it. The miller doesn’t gain title to the sugar because of an agreement with the grower. We consider this to be consistent

¹³⁵ [1984] 3 All ER 982.

¹³⁶ Ibid at 989.

¹³⁷ [1979] 3 All ER 961.

¹³⁸ Ibid at 966, 970, 973, 974.

by the mill, with growers having no say in marketing issues. For example, Wilmar seeking to link the provision of raw sugar marketing services with the provision of sugarcane milling services, has advised these provisions are not negotiable.¹³⁹ While we note CANEGROWERS/ACFA view that the Bill does not change the title arrangements in the supply chain, our conclusion in section 4.3.2 is that the Bill would have the effect of removing one of the legal rights attached to property.

Based on the information we have, and on the existing CSAs, we see no evidence of market failure due to there being absence of legal title for growers for the control of sugar for which there is a GEI. Further, we are not aware that a tolling arrangement has been proposed by growers. We are also not aware of any legal or regulatory impediments that would prevent such a tolling arrangement being negotiated between relevant parties.

3.5 Is there market failure arising from the marketing of raw sugar?

There is a rationale for regulation where there is market failure. A competitive market is generally characterised with prices that will be close to marginal cost and the firm is incentivised to engage in innovation to seek to lower its costs below that of its rivals and attract customers.¹⁴⁰ A market failure occurs where there are some structural issues in the industry which do not enable market participants to engage in commercial negotiation and obtain an outcome similar to the result of a competitive market.

3.5.1 Is the coupling of sugar production and marketing activities anti-competitive?

A number of the grower organisation submissions have stated that there is a need for regulation because mills are refusing to negotiate around marketing services. CANEGROWERS and ACFA have stated that:

Exercising their monopoly power in cane processing, mills are refusing to negotiate around the provision of marketing services. By coupling sugar production and marketing activities in this way, mills are engaging in anticompetitive behaviour. They are denying growers' rights and preventing them from exploring competitive offers and being able to engage the sales and marketing services of others.

The only way to address the imbalance in market power between the mills and growers and provide some level of grower choice in sugar marketing is the introduction of some light form of regulation. Amending the Sugar Industry Act 1999 to require that cane supply contracts contain provisions to enable growers' choice in how their economic interest sugar is priced and sold would restore commercial balance between growers and the mills they supply.¹⁴¹

Typically, the exercise of choice is attached to ownership. Raw sugar marketing occurs after raw sugar has been produced and becomes a tradeable commodity. There is no evidence to suggest that millers do not have clear title over this product.

As discussed in section 3.4, unless there are significant changes to the traditional CSA arrangements, it is evident that growers do not own, or have an ownership interest, in the raw sugar for which they are seeking choice of marketer. Further, there is no evidence that the concept of GEI provides any form of legal title in the growers but simply recognises the price the growers obtain is dependent on the price obtained for the ultimate product.

3.5.2 Marketing considerations at the time of deregulation in 2006

We have considered the views expressed that:

¹³⁹ CANEGROWERS and ACFA (November 2015). Submission to Queensland Productivity Commission, page 11

¹⁴⁰ Roger Sherman, 'Regulation of Monopoly' (Cambridge University Press, 1989) 17.

¹⁴¹ CANEGROWERS and ACFA Submission (October 2015). Joint submission to Queensland Productivity Commission, page 2

In 2005-06 when the Beattie Government at the behest of the Federal Government deregulated the industry as a trade-off for the \$444 million restructure package, (growers had NO CHOICE) other than to accept the package) the one thing Beattie insisted on was that all mill owners sign and the continuation of the QSL marketing arrangements (other than for domestic sugar). And the millers did, including CSR/Sucrogen. When Wilmar took over Sucrogen's sugar assets they agreed to maintain the marketing arrangements!!¹⁴²

The MOU is referenced in the Explanatory Notes to the *Sugar Industry Amendment Bill 2005*, which showed the intention of the Government for an orderly transition to the new marketing arrangements:

The MOU recognises that while the Queensland Government intends to pursue its policy to remove regulatory encumbrances from the sugar industry, it is committed to support an orderly transition from legislative to contractually-based marketing arrangements for bulk export sales.

It is recognised that, in moving to a new marketing system, the key to success is for all parties to work towards delivering greater flexibility and enhanced outcomes whilst continuing the benefits and synergies of presenting a coordinated face to Queensland's bulk raw sugar customers. The peak industry bodies have committed to working with Queensland Sugar Limited to assist it to remain the preferred marketer.

Following the signing of the MOU in October 2005, the Queensland Government moved ahead to prepare the necessary legislative amendments that will enable the introduction of the new sugar arrangements commencing with the 2006 crop. This will be accomplished by way of commercially negotiated contractual arrangements between participating mill owners and Queensland Sugar Limited (QSL) for the export of bulk raw sugar for an initial period of three years.¹⁴³

Since 2006, and with the removal of the single desk seller arrangement in the SIA, millers have the flexibility to choose a marketer for the raw sugar produced. As discussed further in the Decision RIS, millers exercising their choice to market raw sugar through arrangements outside QSL was envisaged at the time of deregulation, following an orderly transition to the new marketing arrangements.

There are now multiple active marketers (including QSL) for Queensland export raw sugar, which is consistent with the development of a competitive market as envisaged by reforms in 2005.

It also seems that the marketing arrangements that are emerging today, were foreseen and considered at the time of deregulation in 2005 and 2006. In June 2005, the Centre for International Economics (CIE) provided a report to the Queensland Government on the likely economic costs and benefits of the Working Group's proposals for the Queensland sugar industry. CIE noted that exactly which companies end up marketing Queensland sugar is difficult to predict.¹⁴⁴ However, CIE made the following observations about the potential implications for millers and growers:

Sugar milling companies and the competitive pressures they could apply

Three milling groups, CSR¹⁴⁵ Mackay Sugar and Bundaberg Sugar, currently control about three quarters of the Queensland industry's raw sugar output. The remaining quarter is produced by seven independent mills. Each of the big three owns several mills and could enter the market drawing on supplies dedicated from those mills. ...

The three large milling groups could readily enter the market following deregulation were QSL unable to meet their expectations. Each could enter as buyers of raw sugar for domestic and export manufacture in their own facilities. CSR and Mackay could also operate as merchants of raw sugar for export, while Bundaberg might export its raw sugar through another operation within its international network.

¹⁴² Cristaudo, Alf (2015). Submission to Queensland Productivity Commission, page 1.

¹⁴³ Sugar Industry Amendment Bill 2005 - Explanatory Notes, page 2

¹⁴⁴ CIE (2005), page 42

¹⁴⁵ Now Wilmar Sugar Australia

The seven independent mills do not have ownership links with domestic refining and probably have less expertise and financial backing to act as competitive merchants in their own right. They could, however, add value for some small but highly profitable niche market situations. Rocky Point (organically grown sugar), Mulgrave (Plantation White sugar) and Maryborough (High Pol brand sugar) already have capacity in these regards. The independents could also mill cane on a toll basis for growers or other interests who would sell into other markets, sell to or through major world commodity traders, or develop long term contractual relationships with QSL or other Australian marketers.¹⁴⁶

Growers

Repealing statutory backing for QSL should also, in the longer term, allow for the development of a wide range of marketing options that would introduce a desirable degree of dynamism into the ways in which sugar is processed, stored and sold on both domestic and export markets. Contractual arrangements between mills and QSL would be only part of these, but important parts. They would allow greater scope for negotiating skills to be developed by all parties, even going back to growers if they were able to sell their own sugar milled for them on a toll basis (as analogously occurs in the cotton industry).¹⁴⁷

The CIE Report envisaged that growers would need to negotiate marketing of raw sugar in the context of a tolling arrangement. The intent of the 2005 amendments to the SIA was not that growers be provided with marketing rights by way of statutory intervention by the Government.

3.5.3 There is not market failure because millers are not providing growers with choice of marketer

We cannot conclude there is market failure in the Queensland sugar industry because millers are not offering growers choice to determine the marketing arrangements for property they do not own. Nor do we consider that millers, or the existing regulatory framework is inhibiting competition in the marketing of raw sugar, because the marketing of export of raw sugar, is contestable.

3.6 Do millers have 'market power'?

One of the key issues underlying the Bill is the clear concern of growers that millers have 'market power' and that this power is either being abused (or has the potential to be abused).

To make our assessment of market power, we have considered Section 46 of the CCA which prohibits a corporation, which has a substantial degree of power in a market from taking advantage of that power for the purpose of:

- eliminating or substantially damaging a competitor
- preventing the entry of a person into any market; or
- deterring or preventing a person from engaging in competitive conduct in any market.

Section 46 sets out a number of provisions, to identify the nature of market power. Relevantly, section 46(3C) provides that a corporation may have market power even though:

- it does not substantially control the market; or
- the corporation does not have absolute freedom from constraint by the conduct of competitors or persons to whom or from whom the corporation supplies or acquires goods or services.

¹⁴⁶ CIE (2015), page 39-40

¹⁴⁷ CIE (2005), page 21

The concept of market power is, in essence, the power to behave in a market not constrained by competitors who can often be observed by the ability to increase prices or decrease service levels.¹⁴⁸ A common example of a corporation with market power is where the corporation is able to provide contracts or agreements on a ‘take it or leave it’ approach.

Table 6 shows the 21 Queensland sugar mills and the extent to which there may be an alternative.

Table 6 Milling companies and mills

<i>Milling company</i>	<i>Ownership</i>	<i>Mills</i>	<i>Alternative</i>
Wilmar International Limited	Private - Wilmar	Macknade Victoria Invicta Pioneer Kalamia Inkerman Proserpine Plane Creek	Some growers in Proserpine and Plane Creek seem to be close enough to supply grower cooperatives such as Farleigh or Marian
Mackay Sugar Limited	Grower-owned company	Mossman Farleigh Marian Racecourse	
MSF Sugar Limited	Private - Mitr Phol Sugar Corporation (Thai)	Tableland Mulgrave South Johnstone Maryborough	Some Tableland and Mulgrave growers could supply Mossman Maryborough could supply Isis
Tully Sugar Limited	Private - COFCO (China)	Tully	
Bundaberg Sugar Limited	Private - Finasucre (Belgium)	Bingera Millaquin	Some Bingera and Millaquin growers could supply Isis
Isis Central Sugar Milling Company Limited	Grower-owned company	Isis	
Heck & Sons Limited	Family owned and operated miller	Rocky Point	

Due to the fact that the quality of sugar cane declines from the time that the cane is cut and must be processed as soon as possible¹⁴⁹, combined with transportation costs making longer distance travel uneconomical, it is generally thought that sugar cane can only be transported for not more than approximately 100 kms. In fact there is evidence that competitive substitution can happen over this range as the Tableland growers moved their mill from Tablelands to Mossman which was over 100 kms away.¹⁵⁰¹⁵¹ We also note that the ACCC has previously estimated a 50km radius, although the basis for this assessment was not made publicly available.¹⁵²

Both BSL and ICSM have indicated their view that in some regions competition for cane supply can be high.

Growers however, dispute the notion that an alternative mill is available. CANEGROWERS and ACFA state that:

¹⁴⁸ Queensland Wire Industries Pty Ltd v Broken Hill Pty Co Ltd (1989) 167 CLR 177 at 188; Melway Publishing Pty Ltd v Robert Hicks Pty Ltd (2001) 205 CLR at [67].

¹⁴⁹ See, for example, Canegrowers Cairns Region (2015), *Submission to the Agriculture and Environment Committee*, page 1.

¹⁵⁰ Canegrowers Tableland (2015), *Submission to the Agriculture and Environment Committee*, page 1.

¹⁵¹ We note that the Mossman Mill had spare crushing capacity at the time.

¹⁵² <http://registers.accc.gov.au/content/index.phtml/itemId/1003357/fromItemId/751043>

- mill capacity and timing harvest constraints limit competition¹⁵³
- cane delivery and railway systems are designed to provide a particular mill.¹⁵⁴

We note that moving to an alternative mill is only likely to be the case where a miller is operating under full capacity and it is economical to move to an alternative mill. This will vary between mill areas.

The growers are also concerned that the inability to choose their milling company gives rise to market power. However, even in respect of mills which have no competitive alternatives, we consider that this potential market power is mitigated by a number of factors:

- The relationship between growers and millers is co-dependent. Mills need a certain supply of cane to be viable. Mills are also constrained to largely source from their local area. Our understanding is that mills have excess capacity so it is in their interest to encourage growers to continue to grow sugarcane. In many areas growers have demonstrable alternatives for land use (for example sugarcane complementary crops).¹⁵⁵ Once land is lost to other activities it may be difficult to get it back for sugar cane production. Due to the co-dependency it is difficult to see that mills can act without constraint in the way which is usually seen in true monopsony situations.
- Growers are statutorily authorised under the SIA to collectively negotiate with the mills. Several grower collectives negotiate on behalf of growers. Statutory authorisations are effective to authorise conduct that would otherwise be 'exclusionary conduct'.¹⁵⁶ This means statutory authorisation allows growers to collectively make a decision that none of the cane growers will provide product to the miller until the miller agrees to the terms and conditions requested by the growers.

Burdekin District Cane Growers noted there are substantial hurdles to switching crops including the need for substantial investment, the need to develop an export market and the need for substantial infrastructure.¹⁵⁷ We acknowledge that investment may be required to change crops but in some cases large investment may not be required and the change can occur quite quickly, for example changing to complementary/break crops.

We have also considered that there have been a number of previous reviews which have almost unanimously formed the conclusion that the relationship between the growers and millers is interdependent and co-dependent. The Hildebrand Report concluded:

Millers and farmers are therefore jointly reliant in each mill area for profitable outcomes, and each must be profitable for economic sustainability of the mill area.¹⁵⁸

Our conclusion is that some millers have a degree of market power, but not all millers have market power. In some areas there appears to be an alternative mill option, with a level of competition. We also noted an interdependent and co-dependent relationship between growers and millers, which should act as a countervailing balance against the misuse of market power.

The presence of market power by itself does not imply that there is a need to regulate. Instead, policy makers need to consider the degree, if any, that market power is being abused as part of the case for considering additional regulation.

¹⁵³ CANEGROWERS and ACFA (November 2015). Submission to Queensland Productivity Commission, page 5

¹⁵⁴ CANEGROWERS and ACFA (November 2015). Submission to Queensland Productivity Commission, page 5

¹⁵⁵ MSF Sugar(2015), Submission to the Agriculture and Environment Committee , page 7

¹⁵⁶ This is unlike authorisations that are available from the ACCC. The ACCC in authorising conduct which might otherwise be cartel conduct has generally refused to authorise "exclusionary conduct".

¹⁵⁷ Burdekin District Cane Growers Limited (November 2015). Submission to Queensland Productivity Commission, page 2

¹⁵⁸ Hildebrand, Clive (2002), page 13.

3.7 Is there evidence of abuse of market power?

3.7.1 Claims by growers

The growers have made a number of claims that there have been, or may be, abuses of market power. Examples which have been raised in previous submissions include the following:

- failed negotiations between Mitr Phol owned Tableland Mill and the growers in that region¹⁵⁹
- the finding of Chesterman QC in 1997 that the miller in a particular dispute offered too little and had not taken into account the difficulties facing the grower¹⁶⁰
- the Rocky Point negotiations which were only settled after input from a mediator and covered a range of issues including the Miller being non-transparent as to the deal that they had done with Golden Circle, not paying the growers on time, not providing enough time for growers to respond to an offer and the Miller not sharing the premium with the growers¹⁶¹ Canegrowers Rocky Point further submission considered that its growers have been subjected to miller marketing abuse by the denial of industry standard for payments of sugar premiums, US Quote and Sugar Quality Bonuses since Rocky Point Mill has sold outside of QSL. It considered the move by Rocky Point mill to market outside of QSL was a deliberate action to negate the transparency offered under QSL, allowing the miller financial reward by reducing the grower share.¹⁶²
- the Tully cane growers state that there was a difficult negotiation for the CSA expiring at the end of the 2013 season and that Tully Sugar refused to honour its agreement in relation to dispute resolution and left the growers in a position where they were not able to get a Collective Cane Supply Contract and the individual growers had to sign an Individual Cane Supply Contract.¹⁶³ The submission states that there is an imbalance in the market power, however it does not explain how the Individual CSAs were less desirable than the Collective CSAs
- Burdekin District Canegrowers states that Wilmar Sugar, on 16 August 2012, presented as a fait accompli a contractual document which changed the net sugar price and that Wilmar Sugar stated that it was 'not proposing to negotiate the new FPPA'.¹⁶⁴ The submission further states that Wilmar Sugar only 'begrudgingly' agreed to some amendments after persistent requests.¹⁶⁵ Burdekin District Cane Growers state that the new FPPA does not have any transparency in relation to the calculation of the net sugar price.¹⁶⁶

To form a view about whether there is evidence of abuse of market power, and by extension evidence of market failure, we have considered each of these claims.

3.7.2 Consideration of miller behaviour

Previous negotiations on the Wilmar Proposal

There have been numerous negotiations over the years in the sugar industry. One example is the 2013 negotiations around a proposal put forward by Wilmar.

¹⁵⁹ Canegrowers Tableland (2015). Submission to the Agriculture and Environment Committee, page 1

¹⁶⁰ Canegrowers Rocky Point (2015). Submission to the Agriculture and Environment Committee, page 2

¹⁶¹ Canegrowers Rocky Point (2015). Submission to the Agriculture and Environment Committee, page 3

¹⁶² Canegrowers Rocky Point (November 2015). Submission to the Queensland Productivity Commission, page 1

¹⁶³ Tully Cane Growers Limited (2015). Submission to the Agriculture and Environment Committee, page 3

¹⁶⁴ Burdekin District Cane Growers Limited (October 2015). Submission to the Queensland Productivity Commission, page 6

¹⁶⁵ Burdekin District Cane Growers Limited (October 2015). Submission to the Queensland Productivity Commission, page 6-7

¹⁶⁶ Burdekin District Cane Growers Limited (October 2015). Submission to the Queensland Productivity Commission, page 7

On 30 July 2013 Wilmar issued a document titled 'Wilmar's Grower Choice Marketing Proposal' (Wilmar Proposal). The key elements of that proposal included the following:

- provide growers choice on a year-by-year basis about whether to nominate all or a portion, of their notional sugar exposure to be sold from QSL to Wilmar for marketing by Wilmar
- for any grower-nominated volume which is marketed by Wilmar, Wilmar would pay growers an additional premium of US 0.15c per lb (which is approximately AU\$3 to \$3.50 per tonne of sugar) over and above the 'Shared Pool Element' achieved by QSL
- all grower pricing and pooling options to remain unchanged
- subject to the Wilmar Proposal receiving enough support by industry stakeholders to enable its adoption for the then 2014 season Wilmar will increase the term of its RSSA with QSL from 3-4 years to 5-6 years.

As we understand, the Wilmar Proposal did not affect a number of other functions that QSL provides for the industry, including:

- storage and handling at the bulk sugar terminals
- management of the pooling and pricing options available to millers and growers
- facilitating financing for the industry and paying advances. To facilitate this function the Wilmar Proposal continued with the current structure whereby Wilmar would continue to supply QSL with 100 per cent of the RSSA export sugar which it mills. The purpose of this was to allow QSL to take title, and therefore have the collateral to raise financing for the industry. This last element seems to be a significant benefit to the industry.

The Wilmar Proposal included an element of Wilmar paying the growers a 'Premium' of approximately AU\$3—AU\$3.50 per tonne of sugar. The Wilmar Proposal contains a slide which shows the history of the Shared Pool Element (also referred to as the premium) as having moved over the last 5 years between \$1 and \$6.50 per tonne of sugar. The premium reached its peak in 2011 at \$6.50 and has been in significant decline from 2011–2013. At the time of the Wilmar Proposal there was a forecast premium of negative \$1 per tonne. Therefore, the offer of an additional premium of between \$3 and \$3.50 would seem to have been reasonable.

Wilmar's presentation on proposed model dated 25 June 2015

Wilmar proposed another model on 25 June 2015 which would apply to the post 2017 contractual arrangements.

The essential elements of the 2015 Proposal are as follows:

- the recognition of GEI in the pricing formula
- growers can continue to use QSL to forward price their cane, or other appropriately qualified third party pricing manager
- dispute resolution provisions in the CSA incorporating final and binding arbitration
- pre-contract mediation to assist in commercial negotiations
- price reports to growers showing what price the downstream product was sold for
- sales reports for growers showing them the product was sold, to whom it was sold, how much was sold and at what price;
- seasonal audit of all sugar sales to deliver transparency. Audit to be conducted by one of the big four accountancy firms with a right for growers to review the audit with the auditors.

We note that the main concerns raised by growers in respect of this Wilmar Proposal are the lack of transparency, conflicts of interest and lack of choice in marketing the grower's economic interest in the crop.¹⁶⁷ Wilmar also notes that it has not received any feedback of specific concerns with the details of the proposal or the draft CSA.¹⁶⁸

The Wilmar proposal does not provide for grower choice of marketer, however we do not see evidence of the growers claim that there remains a lack of transparency and there are conflicts of interest (essentially arising because the private miller may sell it to a related body corporate).

In respect of the absence of grower choice in the proposal, the growers are effectively asking to be given property type rights in a product which they do not own. A refusal by the owner of a product to give away property type rights in that product, does not constitute a misuse of market power as it is not of itself inherently unreasonable. We are also not aware of anything that would prevent growers and Wilmar agreeing a different form of property rights for the CSAs, and a tolling arrangement being entered into. Although Burdekin District Canegrowers noted that the growers were not being offered a tolling arrangement, there is nothing to prevent the parties reaching a commercial agreement where the growers take all of the pricing risk and the millers toll the sugar cane.

We do not consider that the absence of choice for growers in marketing in the Wilmar Proposal (2015) or draft CSA (2015) to be evidence of an abuse of market power by Wilmar.

MSF Sugar pricing model

MSF Sugar has established a Grower Pricing Reference Panel which has visibility and transparency of all of the physical marketing activities undertaken by MSF Sugar. MSF Sugar states that the pricing can be independently audited.¹⁶⁹ MSF Sugar also state that in the Maryborough and Mulgrave areas, when given a choice to nominate QSL or MSF, 91 per cent elected to stay with MSF.¹⁷⁰

MSF Sugar has an 'Improved Pricing and Pooling Model' which is described in some detail in its submission to AEC¹⁷¹. Therefore the submission by growers that MSF Sugar has provided no visibility on its pricing model does not seem to be correct. Importantly, all pools run by MSF Sugar are open to audit and the Grower Pricing Reference Panel has input into the scope of the audit, the choice of the auditor and is able to view sales premiums, freight, sales timing, sales customer choice and futures allocation.¹⁷²

3.7.3 Conclusion on evidence of an abuse of market power

There is clearly a degree of distrust between the growers and the millers and negotiations are difficult. However, the absence of trust is not an indication of an abuse of market power. There are however, other measurable indications that there is no existing abuse of market power as follows:

- no evidence that for those mills without competitive alternative, that the growers are not being paid in accordance with the same formula as prior to deregulation¹⁷³

¹⁶⁷ CANEGROWERS and ACFA (October 2015). Submission to Queensland Productivity Commission, Attachment 3, pages 18-19

¹⁶⁸ Wilmar (November 2015). Submission to the Queensland Productivity Commission, page 7

¹⁶⁹ MSF Sugar (2015). Submission to the Agriculture and Environment Committee, page 10

¹⁷⁰ MSF Sugar (2015). Submission to the Agriculture and Environment Committee, page 10

¹⁷¹ MSF Sugar (2015). Submission to the Agriculture and Environment Committee, page 17

¹⁷² MSF Sugar (2015). Submission to the Agriculture and Environment Committee, page 17

¹⁷³ MSF Sugar (2015). Submission to the Agriculture and Environment Committee, page 5

- no evidence that the current contractual arrangements for private mills and grower owned mills are different. The fact that the current contractual arrangements for private mills and grower owned mills are the same or similar was noted by a number of submissions.¹⁷⁴ If there was a current abuse of market power in respect of contractual arrangements, we would expect to see a difference in the contractual arrangements between private and grower owned mills. Although this is not directly relevant to contractual arrangements beyond 2017, it is relevant to the extent that there is no observable abuse of market power currently and in light of the elements of the MSF and Wilmar proposals particularly around transparency, it is not clear that an assumption should be made that there will be an impending abuse of market power
- the 2013 Wilmar Proposal seems to have been a reasonable proposal on the basis that it provided growers with a choice on a year-by-year basis about whether to nominate QSL or Wilmar, it provided a premium level which seems reasonable when the variation in premiums is taken into account and assisted the industry in broader ways such as continuing to sell the raw sugar to QSL to enable QSL to raise finance and provide premiums; and
- the MSF Sugar pricing model and the Wilmar Proposal 2015 seem to be a reasonable balance and, for example, seem to provide for almost complete transparency in respect of the premium. A number of the submissions from growers make the allegation that they are concerned that private millers may engage in ‘price transfer’ meaning that they will sell the raw sugar to their affiliated refiners not at market price. The MSF Sugar pricing model and the Wilmar Proposal 2015 seem to address this issue.

We note there appears to be issues which have arisen in commercial negotiations between growers and miller in the Rocky Point region that require further investigation. As QPC has not received any submissions from Rocky Point mill, it is unable to draw any conclusions on this issue. However, it should be noted that we do not believe these issues are indicative of wider issues throughout the sugar industry in Queensland.

Despite the evident absence of trust, our conclusion is there is no evidence of a significant or wide-spread abuse of market power.

This conclusion does not preclude an abuse of market power in respect of the post 2017 contractual arrangements. However, based upon the various proposals that have been put to growers it is clear that there is a co-dependent relationship between the growers and the millers and that the millers are aware that this is the case.

Even if there were an abuse of market power in the future there are a number of current regulatory options available to growers. For example, it is clear that the unconscionable conduct provisions of the CCA apply to circumstances of business-to-business contracts. There is also section 46 of the CCA which prohibits an abuse of market power.

After 12 November 2016, the CCA will prohibit an unfair term of a contract where:

- the contract is a standard form contract;
- one of the parties to the contract has less than 20 employees; and
- the upfront price (the price which can be calculated at the time of entering into the contract) is less than \$1,000,000 (assuming the contract is for more than 12 months) or \$300,000 (if the contract is less than 12 months).

¹⁷⁴ Burdekin District Canegrowers Ltd (November 2015). Submission to Queensland Productivity Commission, page 3.

A term is unfair if it causes a significant imbalance in the parties' right and obligations, is not reasonably necessary to protect the legitimate interests of the party benefiting from the term and causes detriment to the other party.

These options would be open to the growers should contractual arrangements post 2017 be either unconscionable, constitute an abuse of market power or, in some circumstances, an unfair term.

3.8 Is there sufficient transparency for growers?

It appears that one of the reasons underlying the proposal for grower choice of marketer is concern about the future of QSL and its role in providing transparency. The AEC's Report cites the ACFAs evidence to the Parliamentary hearing, specifically:

*We need QSL to be there as a benchmark, as an alternative pricer and marketer of our sugar.*¹⁷⁵

In section 2.2.2, we noted grower concerns that a move to miller marketing could mean that:

- transparency about marketing risks, costs and premiums could effectively be removed – to the benefit of the milling company
- lack of transparency leading to millers increasing their 'slice of the pie' at the expense of the growing sector in situations where foreign mill owners also own their own refineries and facilities overseas.

There can be a case for government regulation where there is evidence of information asymmetry and the absence of sufficient information means that participants in a market are at a disadvantage in their dealings compared to the other party.

We have carefully considered whether there is evidence of market failure in the provision of information to growers, which would suggest the need for a regulatory intervention to increase transparency.

In sections 3.7.2 we set out the information that Wilmar and MSF are proposing to provide to growers in their mill regions. This information appears to be comprehensive and would appear to provide the information that growers would need to form a view on whether the premiums that should be being paid to growers, is in fact being paid. It would also allow comparison of the premium and cost performance from year to year.

We have also considered the extent to which those matters have been incorporated in the draft CSA which was circulated by Wilmar in late 2014/early 2015. The CSA proposed by Wilmar includes comprehensive pricing mechanisms and reporting requirements.

The Wilmar draft CSA sets out a reporting, transparency and audit framework at Schedule 7.

Wilmar is required to provide monthly reports to growers setting out details of net pool pricing (including marketing and other costs), forecast adjustment amounts and timing of payments to growers.¹⁷⁶ An example of this report is set out at Annexure A-1 in Schedule 7 of the CSA. Wilmar is also required to provide an end of season report.¹⁷⁷ This report is required to set out comprehensive details of the net pool pricing for each pricing mechanism and allocation amounts for the relevant season. This should enable the grower to determine whether they are gaining the appropriate price for the sugar cane.

¹⁷⁵ Agriculture and Environment Committee (2015), page 9

¹⁷⁶ Clause 2.3 of Schedule 7 of the draft CSA.

¹⁷⁷ Clause 2.4 of Schedule 7 of the draft CSA.

Further clause 4.1 of the draft CSA provides that Wilmar must engage one of the big four accounting firms as an independent auditor to conduct an audit of the annual report and the information used to prepare the report. In addition to this, clause 5 of Schedule 7 allows a grower to request a further audit by another big four accounting firm to determine the accuracy of the annual report and supporting material. Auditors have duties under various statutes and Codes of Ethics to provide an independent opinion.

We also note the views of Bundaberg Sugar Limited, one of the three millers who intend to remain with QSL, that it is possible to develop appropriate transparency arrangements with growers. Specifically:

we have a good working relationship with local growers and have developed over recent years a mechanism to provide transparency to the determination of a domestic sugar price which is a component in deriving a final cane price for growers. The issues involved were very similar to those being debated by Wilmar and their growers, given the lack of transparency on pricing of 'GEI' sugar passing through the refining process.

By negotiation with our growers, we developed a system which mirrors the export sugar price determined by QSL. Should QSL cease to exist in the future, then transparent mechanisms similar to those existing with QSL could be implemented with a new marketer of export sugar. Further, should it eventuate that there is no export sugar, then it is believed that transparency could be achieved utilising some proxy (agreed with growers) for the physical marketing returns which currently are a component of sugar price. Other components of the sugar price are transparent and auditable. Alternatively, some other method of determining a cane price for growers could be possible.¹⁷⁸

Both QSL and CANEGROWERS/ACFA considered that all companies providing marketing services to growers should have an obligation to publish specified information to those growers in relation to their marketing activities to explain how those marketing choices are reflected in their returns. This information should include:

- *past marketing performance, including factors that provide material context for that performance, such as the volume marketed, marketing, pricing, hedging and other risk strategies adopted, sugar quality and seasonal factors*
- *details of the terms on which any trading with related or affiliated refineries occurs*
- *a summary of marketing, pricing and strategies to be utilised, including how the marketing of the relevant Australian raw sugar will form part of any wider international sugar trading activities conducted, and*
- *any administration fees, commissions, profit margins or other amounts to be charged by the mill owner in connection with marketing and/or pricing of Grower Economic Interest sugar.¹⁷⁹¹⁸⁰*

Several submissions, commented on the audit trail proposed by Wilmar and MSF and said they do not overcome the issues associated with a lack of transparency, including the opportunity large, multinational companies have to move profit from one entity to another in intercompany and related party transactions.

Submission also noted that QSL publishes full details of the risk management approach taken in each of its pools and the progressive pricing performance of each of these pools on its website, which is something not provided by Wilmar and MSF¹⁸¹¹⁸². We do not consider marketers of raw sugar should be required to publish details of their risk management strategies on websites. In

¹⁷⁸ Bundaberg Sugar Ltd (2015). Submission to Agriculture and Environment Committee, page 5

¹⁷⁹ QSL (November 2015). Submission to Queensland Productivity Commission, page 7

¹⁸⁰ CANEGROWERS and ACFA (November 2015). Submission to Queensland Productivity Commission, page 13

¹⁸¹ Tableland CANEGROWERS (November, 2015). Submission to the Queensland Productivity Commission, page 2

¹⁸² CANEGROWERS and ACFA (November 2015). Submission to the Queensland Productivity Commission, page 13

most cases risk management strategies are proprietary and strategic information to be shared with their customers in a non-public forum, and do not consider this to be evidence of an absence of transparency.

Based on the information available, there seems to be no strong evidence that millers are not, or will not, provide the information that growers need to make informed decisions regarding marketing risks, costs and premiums, and to show that growers are indeed being paid net premiums in accordance with the CSAs.

We also note the Australian Tax Office's transfer pricing rules, which use internationally recognised methods to discourage international profit sharing. They require all multinational businesses operating in Australia to:

price related party international dealings according to what truly independent parties acting independently would reasonably be expected to have done in the same situation. Pricing for international dealings between related parties should reflect a fair return for the activities carried out in Australia, the Australian assets used (whether sold, lent or licensed), and the risks assumed in carrying out these activities¹⁸³.

3.9 Are the existing dispute resolution arrangements effective?

An effective dispute resolution process is important given the potential market power within the sugar industry. Sugar The Way Forward (2003) noted that these arrangements

provide a mechanism to ensure that market failure cannot occur in a monopoly buyer situation and unfair agreements cannot be forced.¹⁸⁴

Some growers have indicated that the existing dispute resolution arrangements are insufficient protection against misuse of market power and there needs to be a mechanism for resolving deadlocks in the negotiation of CSAs.¹⁸⁵¹⁸⁶

They note that the current dispute resolution mechanism, which is a requirement of CSAs under the SIA, is post contractual and so only applies once a contract has been signed. It does nothing to ensure that a grower, with little market power, can negotiate on equal terms with a mill.¹⁸⁷

QSL noted the current impasse about the terms of which cane should be supplied in the 2017 season and onwards and the fact that there has been no avenue to successfully resolve that impasse to date is evidence that existing dispute resolution mechanisms are ineffective¹⁸⁸. CANEGROWERS and ACFA point to the unsatisfactory resolution of disputes between growers and mill owners in the Tully, Wilmar, MSF and Rocky Point areas.

We also note that pre-contractual dispute resolution was removed from the sugar industry regulatory framework as part of the 2004 reforms. The Hildebrand Review (2002) found that arbitration was costly and impeding investment and innovation and noted that

It is not desirable that arbitration becomes a customary way to avoid the responsibility that should accompany local leadership in genuine negotiation at the mill area level, for the good of participants in that mill area.¹⁸⁹

¹⁸³ Australian Tax Office – International Transfer Pricing – Introduction to concepts and risk management <https://www.ato.gov.au/Business/International-tax-for-business/In-detail/Transfer-pricing/International-transfer-pricing---introduction-to-concepts-and-risk-assessment/>

¹⁸⁴ Queensland Government (2003), page 48

¹⁸⁵ CANEGROWERS and ACFA (October 2015). Joint submission to the Queensland Productivity Commission, page 4

¹⁸⁶ Tablelands Canegrowers Ltd (October 2015). Submission to the Queensland Productivity Commission, 2-3

¹⁸⁷ CANEGROWERS and ACFA (October 2015). Joint submission to the Queensland Productivity Commission, page 4

¹⁸⁸ QSL (November 2015). Submission to Queensland Productivity Commission, page 8.

¹⁸⁹ Clive Hildebrand (2002), page 14

CANEGROWERS/ACFA considers the modern dispute resolution process provided for in the Commercial Arbitration Act 2013 is different to the arbitration process reviewed in the 2002 Hildebrand Review and is designed to be an efficient, effective and low cost means of resolving commercial disputes.

The 2002 Memorandum of Understanding between the Federal and Queensland Governments identified the statutory bargaining system as one of the areas that appear to:

impede increased competitiveness and efficiency, and are detrimental to cultural change and innovation.¹⁹⁰

We note that some growers have pointed to the failure of millers to agree to grower choice of marketer as evidence of failure of the dispute resolution mechanisms. Given the legal title in the CSAs, we do not consider that millers having not agreed to provide choice in marketing of sugar in which they hold title is an indication of an ineffective dispute resolution mechanism.

Despite the evident lack of trust amongst some stakeholders, since deregulation there has been no significant developments that would alter these conclusions on the potential negative impacts of statutory arbitration.

Given our conclusion that there is currently no evidence of an abuse of market power occurring in Queensland in the sugar industry, we consider the current dispute resolution mechanisms are adequate in terms of addressing any imbalance in market power. Therefore, we consider that there would need to be a strong case to justify introducing more arbitration beyond the existing arrangements, especially given the potential high costs involved. These costs are discussed in Section 4.3.5.

3.10 Conclusion

As we set out in Section 3.1, we consider that the regulatory arrangements for the sugar industry should be able to meet the objectives of:

- ensuring a pricing framework where there is an appropriate balance of risk and reward between growers and millers
- ensuring that there are appropriate protections for growers and millers to prevent against the abuse of market power
- ensuring a regulatory framework that supports investment and innovation in the sugar industry and supports the long-term economic sustainability of the sugar industry.

We have considered a range of issues that have been raised by stakeholders that there is a market failure within the industry that is preventing the achievement of these objectives. Having addressed each of these concerns we have not been able to identify specific evidence of market failure which would point to a conclusion of a need for additional regulation.

¹⁹⁰ Memorandum of Understanding between the Federal and Queensland Governments, The Commonwealth and Queensland Working Together for the Sugar Industry and Communities 2002.

4 ASSESSMENT OF POTENTIAL OPTIONS



The purpose of a RIS is to assess the potential impacts of a regulatory proposal on different groups within business, community and government, to identifying whether the net change in welfare associated with the recommended regulatory proposal means the community as a whole would be better off with a regulatory proposal compared to the ‘do nothing’ option.¹⁹¹

The RIS Guidelines indicate that where possible, and appropriate, a RIS should assess the benefits and costs of a regulatory proposal quantitatively. This allows for a clearer comparison both across and between options, and supports independent validation of results. However, in some circumstances it may not be possible to assign a monetary value to some benefits and costs and when benefits and costs cannot be considered quantitatively, the benefits and costs of regulatory options should still be compared and assessed using a qualitative framework.

For this RIS, we have sought to quantify impacts as far as possible. However, there is a limited amount of publicly available quantitative data, so we have applied a more qualitative approach to the impact assessment process. Given the nature of the regulation being considered, our view is that a cost benefit assessment (even if the data was reliable) would not change the qualitative assessment we have made of the costs and benefits.

4.1 Why is assessment of options important?

A RIS must consider all relevant options to allow the decision maker to make an informed decision as to whether the benefits of the proposed regulation outweigh the costs, and to understand how stakeholders are impacted. This comparison is always made in comparison to the ‘do nothing’ option.

For this RIS, we are considering the impacts on growers, millers, QSL, STL and the broader economic and employment impacts of the Bill. We have also assessed the other options which could achieve the same policy objectives.

4.1.1 Public benefit assessment required for authorisation of anti-competitive conduct

The Competition Principles Agreement includes an agreement that regulation should not restrict competition unless it can be demonstrated that:

- the benefits of the restriction as a whole outweigh the costs; and
- the objectives of the legislation can only be achieved by restricting competition.

¹⁹¹ Department of Prime Minister and Cabinet (2014), The Australian Government Guide to Regulation

This assessment is essential where a regulatory proposal seeks to authorise anti-competitive conduct which, without a legislated exemption or other legal authority, would contravene Part IV of the CCA.

Use of a legislation exemption under section 51 of the CCA must be supported by evidence that there is a clear public benefit and that there are no other ways the policy objective can be achieved. Without this justification, a regulation may be overturned by the Commonwealth Government.

In this instance, clause 8 of the Bill specifically authorises anti-competitive conduct that would occur if parties were to comply with provisions of the Bill. A statutory authorisation is necessary to prevent the ACCC taking action against any parties that may engage in anti-competitive conduct in complying with legislation.

4.1.2 Options for consideration

The Bill is one of a number of options that have been proposed by stakeholders to deal with the impasse that seems to be evident in the Queensland sugar industry.

We note that under any option, the Queensland sugar industry will continue to be a price taker in the internationally competitive sugar market, with the price for raw sugar produced in Queensland determined by external factors. Between 95-99 per cent of the price of the sugar is determined by the international market.

Marketers of Queensland produced raw sugar have the ability to negotiate premiums, although these still are negotiated within the international market, so are influenced by global factors of supply and demand. Marketers also have the capacity to manage costs. In this respect, any option needs to ensure that marketers have the commercial flexibility and incentive to maximise net premiums.

The options being considered for this RIS are those that have been proposed by stakeholders either to the Queensland Parliament or considered at the Australian Government level.

Table 7: Options in respect of regulation of the Queensland sugar industry

<i>Option</i>	<i>Description</i>
Option 1: Do nothing – no legislative change	No change to the regulatory framework that was implemented at the time of the 2006 industry deregulation. This means that legal title to raw sugar is determined by the commercial agreements, as are pricing negotiations for the supply of cane In the absence of any changes the nature and form of CSAs, millers would make the commercial decision to market the raw sugar they produce themselves, or enter into a market agreement with alternative market (which may include QSL or another marketer(s)).
Option 2: Legislative change, as set out in the Bill	The legislative changes set out in the Bill are:

Option	Description
	<p>(a) providing growers (and their representatives) with a new right to a statutory arbitration process to resolve contractual and pre-contractual disagreements related to supply contracts (adding a new section 33A). prescribing terms that must be included in a grower, miller supply contract</p> <p>(b) establishing growers economic interest (GEI) (proportion of raw sugar for which they bear a sale price exposure)</p> <p>(c) allowing growers to nominate their choice of marketing entity for their proportion of GEI sugar.</p> <p>We note that the State LNP has proposed the <i>Sugar Industry (Facilitating Grower Choice) Amendment Bill 2015</i>¹⁹², which has a similar set of objectives.</p>
<p>Option 3: Sugar Industry Code of Conduct Regulation</p> <p>Mandatory Code of Conduct (Australian Government Taskforce)</p>	<p>Burdekin District Cane Growers Ltd has proposed a Sugar Industry Code of Conduct Regulation with detailed drafting.</p> <p>The Australian Government's Sugar Industry Code of Conduct Taskforce proposed a mandatory code created under the CCA. The matters proposed for inclusion are:</p> <p>(a) a mechanism to distribute relevant interests in the quantities of sugar obtained from cane between growers and millers</p> <p>(b) a link between the price paid for cane and the selling price of sugar</p> <p>(c) the ability to choose marketing services</p> <p>(d) non-discriminatory provisions</p> <p>(e) a mechanism to resolve disputes</p>
<p>Option 4: Tolling</p>	<p>Some stakeholders have suggested a tolling arrangement, where growers contract with millers for processing and retain title and responsibility for marketing raw sugar. It has also been proposed that miller processing could be made subject to a third party access regime.</p>

4.2 Option 1 – Base case – no additional legislation

Option 1 would see no changes to the SIA meaning that legal title to raw sugar is determined by the outcome of commercial agreements. The current regulatory framework reflects the regulatory parameters developed as part of the 2006 deregulation arrangements.

These parameters, aspects of which reflect the recommendations of numerous reviews commissioned by both the Queensland and Australian Government, include:

- while a grower may only supply cane to a mill if the grower has a CSA with the mill, growers and mills are free to commercially negotiate the CSA's terms
- the ability (and authorisation for competition legislation) for growers to collectively negotiate with a miller in the making and varying of a CSA
- a CSA must state a process for dispute resolution and that the parties must attempt to resolve the dispute by using the process
- final offer arbitration is prohibited
- millers can choose who markets raw sugar they produce (that is, there is no single desk).

Given the announcements of Wilmar, MSF and Tully Sugar not to renew their RSSAs with QSL beyond 1 July 2017, the base case for consideration is in two parts.

¹⁹²[http://debfrecklington.com.au/documents/Exposure%20Draft%20Sugar%20Industry%20\(Facilitating%20Grower%20Choice\)%20Amendment%20Bill%202015.pdf](http://debfrecklington.com.au/documents/Exposure%20Draft%20Sugar%20Industry%20(Facilitating%20Grower%20Choice)%20Amendment%20Bill%202015.pdf)

Wherever possible, we have sought to make an assessment of the base case for stakeholders pre and post 1 July 2017. As agreements are still to be reached between some growers and some millers beyond 1 July 2017, we have assumed that the proposals that have been presented by the relevant millers to growers become the base case.

A description of the relationship between the various parties is reflected in **Table 8**.

Table 8: Assumed roles of Queensland supply chain participants – pre and post 1 July 2017

<i>Stakeholder</i>	<i>Pre 1 July 2017</i>	<i>Post 1 July 2017</i>
Growers	<p>CSA arrangements with millers. Title transfers on delivery of cane to mill.</p> <p>Growers paid for sugar on the terms set out in CSAs. Most CSAs include the Cane Price Formula which provides for a roughly 2:1 distribution between growers and millers.</p>	<p>CSA arrangements with millers. Title transfers on delivery of cane to mill, unless growers and millers negotiate alternative agreement.</p> <p>We are unaware of any alternative agreements.</p> <p>Growers paid for sugar on the terms set out in CSAs. Most CSAs include the Cane Price Formula which provides for a roughly 2:1 distribution between growers and millers.¹⁹³</p> <p>Growers continue to have the ability to manage their sugar price exposure</p>
Millers	<p>Millers contract with QSL for marketing of raw sugar.</p> <p>Some millers have commenced the purchase of raw sugar from QSL and commenced the marketing of raw sugar.</p> <p>MSF has marketed a proportion of its raw sugar since 2006</p>	<p>Millers make the commercial decision to market the raw sugar they produce themselves, or enter into a market agreement with alternative marketer (which may include QSL or another marketer(s).</p> <p>Wilmar has announced plans to market raw sugar directly.</p> <p>MSF and Tully have yet to indicate an alternative marketer.</p> <p>ISMC, Mackay Sugar Limited and Bundaberg Sugar Limited have indicated they will remain with QSL for the 2017 season.</p>
QSL	<p>QSL provides the following services:</p> <ul style="list-style-type: none"> • acquiring raw sugar intended for bulk export from Queensland millers under RSSAs • selling the raw sugar acquired to international customers • chartering shipping for the raw sugar acquired • financing and hedging activities related to raw sugar (with growers having a choice to use QSL or alternative arrangement) 	<p>QSL would continue to provide the following services:</p> <ul style="list-style-type: none"> • acquiring a proportion of raw sugar intended for bulk export from the three millers for the 2017 season • selling the raw sugar acquired to international customers • chartering shipping for the raw sugar acquired • financing and hedging activities related to raw sugar (with growers having a choice to use QSL or alternative arrangement)¹⁹⁴

¹⁹³ We note Wilmar's submission to the QPC, October 2015 (page 3) indicates that Wilmar is not seeking to change how cane growers are paid for the product they supply to mills, it is not seeking to change the process by which cane supply agreements are negotiated and it is not seeking to change the existing mechanisms which provide growers with the ability to make decisions that determine 99 per cent of the net sugar price on which the price of their cane is based.

¹⁹⁴ QSL considers that the full range of pricing products is at the discretion of the miller and that production risk management as currently managed by QSL, is not contemplated by the scenario. QSL (2015), Submission to the Queensland Productivity Commission.

Stakeholder	Pre 1 July 2017	Post 1 July 2017
	<ul style="list-style-type: none"> sub-leasing, operating and providing storage and handling services at STL. 	<ul style="list-style-type: none"> sub-leasing, operating and providing storage and handling services at STL.
STL	Terminals managed by QSL, based on a cost recovery only basis.	STL has a number of options including: <ul style="list-style-type: none"> continuing to engage QSL to manage the terminals under the sublease operating the terminals itself – achieved by purchasing equipment from QSL and employing QSL’s terminal employees. Alternatively, STL could engage another terminal operator individual terminals could be sold or subleased to milling companies

4.2.1 Option 1 – base case millers

Under the CSAs, returns to growers and millers are determined by the Cane Price Formula. As millers receive a share of the net premiums, millers have a strong incentive to maximise the net price for raw sugar, including minimising marketing costs.

In Chapter 3, we estimated an average net premium range for Queensland’s sugar of \$21 million per annum, of which \$7 million would be earned by millers and \$14 million earned by growers, based on a net premium of \$5.

For the base case (particularly post 1 July 2017) we have assumed that millers who have made the decision to cease using QSL for the marketing of raw sugar have done so because they have made a commercial decision that an alternative marketing strategy would increase the overall net premiums earned from raw sugar produced by their mills.

We have sought to consider the potential implications for millers marketing their own raw sugar and millers who have indicated that they plan to continue holding RSSAs with QSL, at least for the 2017 season.

Millers marketing their own raw sugar

Wilmar has indicated its primary reason for making the decision to market 100 per cent of the raw sugar it produces is to increase the returns that both it and growers receive. Wilmar says that in marketing its MEI in the 2012 and 2013 seasons:

Wilmar’s net sugar price, including marketing premiums, was \$45 per tonne higher than on average was achieved for growers under the QSL system. Wilmar’s marketing premiums were approximately 60 per cent higher than QSL returned over the same period, about \$11 better per tonne of sugar... and that its growers would be around \$36 million per year better off post 1 July 2017.¹⁹⁵

CANEGROWERS and ACFA have indicated their concerns to us that Wilmar’s proposed marketing arrangements, as provided to growers in their ‘New Marketing Partnership’ information update dated 8 April 2014, will ‘dilute the returns growers will receive from trading profits’. CANEGROWERS and ACFA also considered that Wilmar has provided no empirical evidence to support assertions of increased premiums or assumptions used.¹⁹⁶

¹⁹⁵ Wilmar (October 2015) Submission to Queensland Productivity Commission, page 13

¹⁹⁶ CANEGROWERS and ACFA (November 2015) Submission to the Queensland Productivity Commission, page 14

We have been provided with an Ernst and Young (EY) audit report on Wilmar’s actual returns. This confirms Wilmar’s statements that it was able to achieve higher returns than in the QSL system in the 2012 and 2013 years. We note that there may be different risk profiles or levels of forward pricing between Wilmar and QSL.¹⁹⁷ However, we have no reason to consider that Wilmar has not achieved the indicated returns and in the future would not have the commercial incentive to maximise the returns from marketing of raw sugar.

In response to the claim that Wilmar’s proposed marketing arrangement will negatively affect grower returns, it appears, based on supplementary information provided by Wilmar to us that the 50 per cent referred to by CANEGROWERS is based on arbitrage returns rather than either net premiums or ICE No.11 returns that are currently paid to growers. Whilst we note that only 50 per cent of these arbitrage returns appear to be distributed to growers, rather than the usual two-thirds distributed to growers on the basis of cane payment arrangements, Wilmar states that ‘these benefits are not available to growers in the current QSL system, because QSL does not trade any material quantity of other origin sugar’.^{198,199}

Assuming that all the elements included in net premiums (including spread gains on Australian sugar) under the proposed framework are the same as under QSL, there is no evidence to suggest that net premiums would be any lower than QSL, and could well be higher under a Wilmar marketing scenario.

In its response, QSL said it:

does not agree with the use of Wilmar’s pricing claims in a bid to justify the QPC’s claim that “there is no evidence to suggest that net premiums would be any lower than QSL and could well be higher under a Wilmar marketing scenario”. Past performance does not guarantee future performance.

As recognised in the RIS, Wilmar and QSL’s results are based on very different risk profiles. Wilmar’s increased risk profile (which it can easily bear over a large volume of globally traded sugar) will create material risks and volatility of return for growers, an issue which appears to have been glossed over in the RIS.²⁰⁰

We have considered the QSL view, but have no information that would support a position that QSL provides consistently higher returns than would occur through an alternative arrangement.

Neither MSF nor Tully have made public estimates about the net premiums they might achieve, although we note that MSF has been marketing at least some proportion of its raw sugar since 2006. We can only assume that this decision was made because MSF considered the net premiums it could generate would be in excess of those that QSL (or an alternative marketer) might have been able to achieve.

Millers selling raw sugar to QSL for marketing

Three millers (ICSM, Bundaberg and Mackay Sugar Limited) have indicated they will remain with QSL as their marketer, at least for the 2017 season. None of these millers in submissions either to us or the AEC have indicated concerns that their net premiums in the 2017 season will be impacted. We note millers appear to have been silent on the matter.

¹⁹⁷ Wilmar (November 2015) Supplementary Information to Queensland Productivity Commission, page 9

¹⁹⁸ Wilmar (October 2015) Supplementary Information to Queensland Productivity Commission, page 2

¹⁹⁹ QSL strongly refutes the claim that Other Origin benefits “are not available to growers in the current QSL system, because QSL does not trade any material quantity of other origin sugar”. QSL considers it has the same capability and tools available as Wilmar to achieve Other Origin trading results in the market – only the appetite for risk and the transparency of their Other Origin sugar activities differs between the two entities. QSL (November 2015). Submission to Queensland Productivity Commission, page 8

²⁰⁰ QSL (November 2015). Submission to Queensland Productivity Commission, page 8

Accordingly we have assumed that the net premiums will be at least comparable to the pre-1 July 2017 base case. We would, however, welcome any additional evidence from millers that this is not the case.

Overall, we conclude that under the base case, the millers will be no worse off from 1 July 2017 and may well be better off if they are able to outperform QSL in net premiums.

4.2.2 Option 1 – base case growers

Some growers have expressed concern they will be worse off if the raw sugar, for which they have price exposure is marketed by a marketer chosen by the miller and they have no choice of their marketer. While chapter 3 estimated that 95-99 per cent of the cane price the growers receive for their cane crop is impacted by the world price for sugar, CANEGROWERS / ACFA noted there is an interaction between marketing decision and pricing activities.

We note that Queensland growers generally have been given the ability by their millers to manage their price risk through a variety of pricing pools. As far as we are aware, this arrangement will not change post 1 July 2017.

Variety of pools

Both Wilmar and MSF appear to offer growers a variety of pricing pools catering to different risk profiles to manage their ICE No. 11 exposure. The range of pools available appears similar to the range currently offered by QSL. We note that although Tully has not yet detailed their pricing options available to growers post 2017, it has previously stated that it will enable growers to continue to price risk independently of the mill.²⁰¹

Pricing

While Wilmar has stated that growers may choose to forward price using QSL (or another suitably qualified third party)²⁰² we note that the details of such an arrangement have yet to be negotiated with QSL.

We also note QSL's view that:

Queensland cane growers are currently given the ability by their miller to choose a pool pricing product to match their risk profile, and have the ability to price sugar at their own discretion on QSL's pricing book. Whether the range of current services will still be available to all growers beyond 2017 is not guaranteed.

As a not-for-profit entity, QSL requires a contractual raw sugar supply commitment and the consequent title that this provides to be able to offer these services. If the current positions of Wilmar, Tully Sugar and MSF do not change, the growers supplying these millers will be prevented from using QSL (a company both growers and millers own) in the 2017 and future seasons.²⁰³

This position appears to be a commercial decision taken by QSL, rather than one which reflects any legal or contractual requirement. Prior to deregulation of QSL in 2006, the Industry Working Group on *Proposal to Introduce a New Marketing System for the Queensland Sugar Industry* considered that:

The relationship between the marketing company and suppliers²⁰⁴ would be governed by contractual arrangements. Although the terms of those contractual arrangements would be

²⁰¹ Tully Sugar Limited (2014). Submission to Senate Select Committee on Rural and Regional Affairs and Transport, page 6

²⁰² Wilmar (October 2015). Submission to Queensland Productivity Commission, pages 16-17

²⁰³ QSL (November 2015). Submission to Queensland Productivity Commission, page 4

²⁰⁴ The SIA defines **supplier** for sugar, means a person who immediately before the sugar is manufactured, owns the sugar cane from which the sugar is manufactured.

matters to be determined between the suppliers and the marketing company, it is envisaged that there could potentially be at least two main types of contracts with suppliers:

- *a Sale of Goods contract where ownership of the bulk raw sugar passes to the marketer in accordance with the terms of the contract; or*
- *a Principal/Agent contract where the marketer is vested with full contractual capacity and authority to market and sell bulk raw sugar on behalf of the supplier.*

In the transformation to responsive marketing, it is expected that these contractual arrangements would provide greater flexibility and a wider portfolio of options and services for participants.²⁰⁵

This suggested that it was envisaged that QSL would develop a broader range of product offerings, and that not all offerings would require that the ownership of title be required to pass to QSL. We are not convinced that the management of pricing pools requires title of raw sugar, although it would change the nature of some of the services offered by QSL. We also note that ultimately the range and nature of product offerings must be a commercial decision for QSL.

We also understand that there are other third parties that can provide these functions without the need for transfer of title.²⁰⁶

However, we also consider that even in the absence of growers being offered the option of QSL as a price manager, we note that millers have proposed to continue to allow growers to price risk through forward contracts independently of the mill and participate in a range of pricing pools that suit their risk appetite. We consider this provides choice for a significant proportion of the price exposure growers are exposed to through the ICE 11 pool.

From this perspective we consider the base case provides growers with considerable autonomy to manage their revenues according to their appetite for price risk, irrespective of the ultimate marketer of raw sugar.

We consider that the world sugar price, along with input prices, are the largest contributors to the viability of cane production and the net premiums, while important, are not likely to be the major contributor to a growers investment decision in cane production.

In respect of the net premiums, we note Wilmar's submission that it is not seeking to change how cane growers are paid for the product they supply to mills, it is not seeking to change the process by which cane supply agreements are negotiated, and it is not seeking to change the existing mechanisms which provide cane growers with the ability to make decisions that determine 99 per cent of the net sugar price on which the price of their cane is based.²⁰⁷

QSL and CANEGROWERS / ACFA consider that pricing and marketing cannot be done in isolation. However, we understand that in the instances where a grower elects to price using QSL (or a third party), provided there is adequate communication (when required) between the pricing manager and the marketer, there is no reason why a pricing manager's hedging decisions and instructions cannot be provided to the marketer for execution.²⁰⁸ In addition, we consider that there is no reason a miller, who has a strong incentive to maximise the net price received for raw sugar, will not be able to also manage futures positions and generate spread gains for both themselves and growers.

Given our conclusion that millers should be no-worse off pre and post 1 July 2017, we can only conclude that growers will be no worse off post 1 July 2017. If marketers (including miller

²⁰⁵ Industry Working Group (2005). Proposal to Introduce a New Marketing System for the Queensland Sugar Industry, page 7

²⁰⁶ Mackay Sugar (2014). Submission to the Senate Select Committee on Rural and Regional Affairs and Transport, page 2

²⁰⁷ Wilmar (October 2015). Submission to Queensland Productivity Commission, page 13

²⁰⁸ Wilmar notes that it has previously facilitated pools in Queensland managed by third-party managers on behalf of growers. Wilmar (November 2015). Submission to the Queensland Productivity Commission, p. 1

marketers) are able to market in a manner that increases net premiums then growers may be slightly better off.

Other Revenue

QSL also notes that all profits from additional corporate activities (such as of other materials at terminals) are passed back to members.²⁰⁹ However, no information was provided as to the size of this revenue and therefore the impact this may have on growers outside QSL post 1 July 2017.

4.2.3 Option 1 – base case QSL

Under its constitution, QSL is required to act in the best interests of the sugar industry. Its' main activities include:

- acquiring raw sugar intended for bulk export from Queensland mill owners under RSSAs
- selling and chartering shipping for that raw sugar to international customers
- financing and hedging activities related to the raw sugar
- sub-leasing, operating and providing sugar storage and handling services at the six bulk sugar export terminals
- other initiatives considered to be in the best interests of the Queensland sugar industry.

As it is owned by grower and millers, QSL works on behalf of growers and millers to export raw sugar to international refineries.

Marketing

QSL consider, over the past few years that Wilmar has been looking for ways to remove it from the marketing of Queensland raw sugar. For example, it was initially proposed that QSL should subcontract Wilmar to conduct all of its marketing operations. QSL says that having failed to convince other mill owners of that position, Wilmar has threatened on numerous occasions to provide a notice to terminate its RSSA.²¹⁰

In 2017, QSL will see a portion of its marketing function transfer to the following mills who have indicated a preference to find an alternate marketer for their raw sugar: Wilmar, MSF Sugar and Tully Sugar.²¹¹

Some stakeholders have noted concern for the viability of QSL as a result.

Tully Sugar commented that it assessed the impact of the withdrawal of the largest suppliers to the QSL export marketing system and determined that the loss of major suppliers would fundamentally change the QSL offering. In announcing its decision to withdraw, Tully Sugar noted that the withdrawal of Wilmar and MSF Sugar meant that QSL:

loses more than seventy per cent of its critical export mass and its competitive advantage. This represents unacceptable risks to our business and our growers.

In addition, Tully Sugar submitted that it is seeking to replace the services that are currently being provided by QSL.²¹²

Further, CANEGROWERS noted that Bundaberg, Isis and Mackay Sugar Limited, the millers remaining with QSL for the 2017 season have delayed their decision of whether to continue with

²⁰⁹ QSL (2015). Submission to the Queensland Productivity Commission, page 10

²¹⁰ QSL (2014). Submission to Senate Select Committee on Rural and Regional Affairs and Transport, pages 10-11

²¹¹ QSL (2015). Submission to Senate Select Committee on Rural and Regional Affairs and Transport, page 3

²¹² Tully Sugar. Submission to Agriculture and Environment Committee, page.3

QSL until 15 December 2015 and that there is a risk that the continuing mills will withdraw from QSL at the conclusion of the 2017 season.²¹³ CANEGROWERS also noted the changing market profile will have consequences for all growers, both inside and outside QSL.²¹⁴

The AFCA requested a speedy resolution to the state and federal processes due to a concern over the future of QSL as there has been a history in the industry of neglecting organisations until they fall.²¹⁵

Three mills have chosen to remain with QSL. We note ICSM and Bundaberg Sugar do not support the Bill.²¹⁶ Further, neither mill has noted concern respecting QSL's ability to market its raw sugar with the loss of the three other mills.

Mackay Sugar notes that despite other sugar suppliers giving notice to withdraw supply from QSL, Mackay Sugar has opted to remain with QSL as a joint exporting marketing body of the growers, Bundaberg Sugar and ISCM.²¹⁷

We note QSL's view that it provides a different value proposition in its approach to raw sugar marketing, in comparison to other raw sugar marketers such as Wilmar. QSL notes that growers value its approach as it can offer a more cautious approach to managing downside risks; whereas global agribusinesses (which are heavily exposed to trading risks) have very different appetites for risk.²¹⁸ Mills are provided with a choice to pursue the marketing option which matches their risk appetite.

We note Tully Sugar's comment that QSL has lost its critical export mass and its competitive advantage. Given thirty per cent of the market have chosen to remain with QSL, it is difficult to conclude whether the 'critical mass' threshold has indeed been met. While it is difficult to predict whether the three remaining millers will choose to remain with QSL after the 2017 season, we consider that for the 2017 season, there is reason to believe QSL's marketing function will remain viable given the choice of the three remaining mills to form a joint exporting body.

Non-marketing functions

Given some mills' choice to pursue alternate marketing arrangements, it is apparent there will be a change in QSL's servicing model with respect to raw sugar marketing.

QSL notes that as a result of its structure, purpose and not for profit nature, it has opened up competition in the raw sugar industry in a way that a purely profit driven entity in its position would not have. For instance QSL notes it has:

- structured the RSSAs as relatively short term arrangements, with three year rolling terms
- provided open access to the six bulk sugar terminals that it operates, at cost-recovery rates to all raw sugar mill owners, irrespective of whether the relevant raw sugar is being marketed by QSL, ensuring that access to storage and handling facilities is not a barrier to entry while QSL is the operator of the terminals
- agreed to amend the RSSAs that it had entered with mill owners, to give mill owners the option to market their 'supplier economic interest sugar' from the 2014 Season onwards.²¹⁹

²¹³ AEC (2015) page 4

²¹⁴ CANEGROWERS and ACFA (November 2015). Submission to Queensland Productivity Commission, page 7

²¹⁵ AEC (2015) page 4

²¹⁶ Bundaberg Sugar, page.1; ICSM, page.1-2;submissions to Agriculture and Environment Committee (2015)

²¹⁷ Mackay Sugar Limited (2014). Submission to Senate Select Committee on Rural and Regional Affairs and Transport, page 1

²¹⁸ QSL(2014), Supplementary submission to Senate Select Committee on Rural and Regional Affairs and Transport, page.16

²¹⁹ QSL (2014). Submission to the Senate Select Committee on Rural and Regional Affairs and Transport, page. 11

QSL has noted that under its current operating system, the storage assets are managed in a pooling environment where this overall benefit can be shared by the entire industry. QSL has also expressed concern that

Unless a commercial agreement can be reached, the operation of the storage assets will not be on a pooled basis beyond the 2016 Season. Therefore some industry participants will not have access to the same amount of storage as they do under the current system. Subsequently, some will not have the same flexibility over the timing of sales and associated pricing on the ICE 11 that they have under the current system. This will result in a direct and negative impact on the return to impacted mill owners and their growers.²²⁰

We note that some millers may also have similar access to storage (compared to its raw storage volumes) post 1 July 2017.²²¹

In **Table 9**, we set out how reduced marketing volumes may result in changes to the remainder of QSL's functions.

Table 9: Comments regarding QSL's non-marketing service functions

<i>Service function</i>	<i>Stakeholder comments</i>	<i>QPC comments</i>
Storage, handling and logistics	<p>QSL notes that it can provide storage, handling and logistics services without the customer mill supplying it information about the ultimate customer for the raw sugar (ie marketing). QSL also notes that the industry (with the exception of Wilmar), supports QSL continuing to provide storage and handling services at the bulk sugar terminals ²²²</p> <p>The QPC's assumption that QSL's loss of marketing volumes will not necessarily result in a change to QSL providing storage, handling and logistic services is incorrect. The tonnage in QSL's marketing system is directly linked to the threshold volume required to retain the STL sub-lease, as detailed in the 'Access to Bulk Sugar Terminals' section of the table. It should also be noted that as QSL is a not-for-profit operator, it can be assumed that any alternate STL operator would do so at a cost incorporating margins that would be passed on to growers and millers. Judging by the National Competition Council's draft decision regarding shipping channel services at the Port of Newcastle, third-party access regimes will not provide appropriate protection against increases in price in the way the RIS seems to assume they would.²²³</p>	<p>Ultimately the management of storage, handling and logistics services is a matter for STL (which is jointly owned by growers, millers and QSL). The third party access regime that applies in Queensland, is the <i>Queensland Competition Authority Act 1997</i> (QCA Act). The National Competition Council previously found the application of the third party access regime for the Dalrymple Bay Coal Terminal to be effective.</p> <p>We have no reason to consider that an effective Queensland regime could not be developed for sugar terminals, if necessary.</p>

²²⁰ QSL (November 2015). Submission to Queensland Productivity Commission, page 3

²²¹ Wilmar (November 2015). Supplementary Submission to Queensland Productivity Commission, page 4

²²² For example, QSL says the MSF have not had a contract to provide raw sugar to it and MSF continues to benefit from QSL's other services at cost. In addition, QSL notes that the industry (with the exception of Wilmar), supports QSL continuing to provide storage and handling services at the bulk sugar terminals. QSL (2015). Supplementary submission to Senate Select Committee on Rural and Regional Affairs and Transport, page 5

²²³ QSL (November 2015). Submission to Queensland Productivity Commission, page 8

<i>Service function</i>	<i>Stakeholder comments</i>	<i>QPC comments</i>
Access to Bulk Sugar Terminals	<p>QSL noted that it currently provides and will continue to provide open access to the sugar terminals for entities that compete with it in export markets.²²⁴</p> <p>Tully Sugar notes that it does not believe changes to marketing arrangements will impact on access to essential infrastructure.²²⁵</p>	<p>We understand there is a threshold volume of sugar that is to be handled and stored at each terminal for QSL to retain its sublease with STL to the six sugar terminals.</p> <p>If STL terminates the sublease, it may negotiate with other parties to provide the service at the terminals.</p>
Pricing and price risk management <ul style="list-style-type: none"> QSL provides pricing products to millers and growers Includes QSL managed pools, individual forward pricing and miller managed pricing pools. 	<p>Mackay Sugar notes that to a large degree, growers and millers are able to manage their own risks relating to the underlying sugar futures price as well as currency. This is achieved via a range of market based products that are provided by a range of service providers, including banks, QSL and millers.²²⁶</p> <p>The deregulation of sugar marketing has seen a number of cane pricing mechanisms being developed to allow individual or smaller collective groups of growers to directly price their cane by pricing on the international raw sugar market (ICE No, 11). However growers have also had the choice to remain in a large collective pricing pool if that is their wish (as was the situation in the regulated environment).²²⁷</p>	<p>It appears that QSL is one of many players capable of providing pricing and price risk management.</p> <p>Should QSL continue to add value to customers in providing pricing, and price risk management, it will likely remain competitive in this space.</p>
Financing <ul style="list-style-type: none"> QSL provides payment to millers on receipt of sugar at the bulk sugar terminal and is often in advance of sugar being sold, or being paid for by the customer. 	<p>QSL is accessing its syndicated facility agreement to fund the industry's advances program.</p> <p>Wilmar exiting from QSL's marketing function lead to an immediate \$1 million increase in financing costs due to the necessity of using the syndicated debt facility.²²⁸</p>	<p>We note that QSL's submission to the AEC did not raise concerns about the impact of financing costs on the operation of the business.</p>

We have not been able to identify any direct evidence that suggests QSL will not remain a viable entity beyond 1 July 2017, noting:

- its remaining mill customers are supportive of QSL and have not expressed concern over its ability to market their respective raw sugar despite a reduction in volume
- corollary functions such as financing and pricing will be buoyed by the retention of the marketing function (albeit if reduced)
- provision of logistics and port access, should STL retain this agreement, will continue to provide industry value.

²²⁴ QSL (2015), Supplementary submission to the Senate Select Committee on Rural and Regional Affairs and Transport, page 5

²²⁵ Tully Sugar (2014). Submission to the Senate Select Committee on Rural and Regional Affairs and Transport, page 5

²²⁶ Mackay Sugar (2014). Submission to the Senate Select Committee on Rural and Regional Affairs and Transport, page 2

²²⁷ Mackay Sugar (2014). Submission to the Senate Select Committee on Rural and Regional Affairs and Transport, page 3

²²⁸ QSL Media Release "QSL Retracts Standard & Poor's Rating", Friday 4 July 2014 (<http://www.qsl.com.au/news-media/qsl-retracts-standard-poors-rating>)

As noted above, the remaining millers have yet to indicate if they will continue their relationship with QSL after 2017. Should the remaining mills choose alternate marketing agents, it's likely that QSL's service functions may be limited to the provision of logistics, and potentially provision of access to the bulk sugar terminals if:

- the threshold volumes have not been breached resulting in a sublease termination
- the sublease agreement can be renegotiated on different terms between QSL as a single operator and STL.

4.2.4 Option 1 – base case STL

Growers and QSL have indicated concerns that a move to miller marketing, and away from QSL marketing could give rise to STL ceasing to use its existing cost recovery model i.e. no returns included in current storage and handling provision services. Ultimately the pricing arrangements for STL will be an STL shareholder decision, with millers, growers and QSL as joint shareholders.

We also note there are already protections through the QCA Act and the CCA that would prevent misuse of monopoly power in restricting access to the service provided by these facilities.

While QSL suggested that the CCA may not be effective,²²⁹ we are unconvinced by the position and continue to note that STL's industry ownership arrangements are a relevant consideration in terms of the industry agreeing a pricing arrangement.

4.2.5 Option 1 –economic base case

As the economic base case, we have assumed the following:

- Cane production, both pre and post 1 July 2017, is most likely to be influenced primarily by world sugar prices (as this flows through to cane prices under the cane price formula), inputs costs (such as electricity, water and fuel), and environmental conditions (such as favourable weather and crop quality). This is unlikely to change, post 1 July 2017, as net premiums appear unlikely to be significant enough to make any major impact on a decision to invest in cane production.
- Raw sugar production is expected to be heavily influenced by cane production, the quality of the cane delivered to the mill, and the efficiency of the miller. A change of marketer is unlikely to have any discernible impact on raw sugar production. This is unlikely to change materially, post 1 July 2017.
- World raw sugar prices, both pre and post 1 July 2017, will continue to be set by the world market (predominantly the globally traded ICE No. 11).
- Net premiums currently move between a range of approximately plus or minus \$5 per net tonne. Average net premiums are presumed to be at least maintained under either QSL or an alternative marketer. Some millers may be able to achieve a higher net premium from alternative marketing of raw sugar.
- Investment in cane production (a new grower or a grower planning to expand cane production) will be influenced primarily by world sugar prices (as this flows through to cane prices under the cane price formula), inputs costs (such as electricity, water and fuel), and whether there is suitable cropping land available, close to a mill. A change of marketer post 1 July 2017 is considered unlikely to have any discernible impact on investment in cane production.

²²⁹ QSL (November 2015). Submission to Queensland Productivity Commission, page 8.

- Investment in mills, both pre and post 1 July 2017, is most likely influenced by forecast world sugar prices, input costs, the level of cane production within an appropriate radius of the prospective mill area, world sugar consumption and broader economic conditions.
- Employment in the sugar industry is estimated to be 16,000 people. Post 1 July 2017, no material change in employment is expected.

This is summarised below in **Table 10**.

Table 10 Base case assumptions for sugar industry

	<i>Pre 1 July 2017</i>	<i>Post 1 July 2017</i>
Cane production	Most likely influenced by forecast world sugar prices, input costs, and environmental conditions and mill availability.	Change of marketer is unlikely to change the influences of cane production.
Raw sugar production	Most likely influenced by cane production volumes and quality, mill availability and miller efficiency	Change of marketer likely to have minimal impact on raw sugar production
World raw sugar price (ICE No.11)	Set by world market	Set by world market
Net premiums	Average range of plus or minus \$5/net tonne raw sugar	Average net premiums are presumed to be at least maintained under either QSL or alternative marketer. Some millers may be able to achieve a higher premium from alternative marketing.
Investment in cane production	Most likely influenced by forecast world sugar prices, input costs and availability of suitable cropping land	Continue to be influenced by forecast world sugar prices, input costs and availability of suitable cropping land
Investment in mills	Most likely influenced by forecast world sugar prices, input costs, and cane production in mill area	Continue to be influenced by forecast world sugar prices, input costs, and cane production in mill area
Employment	Estimated 16,000	No material change in employment expected under any marketing changes

4.3 Option 2 – Sugar Industry (Real Choice in Marketing) Amendment Bill

4.3.1 Description

The explanatory notes, tabled with the Bill in May 2015 stated the policy objectives of the Bill were to provide cane growers with the right to have real choice in who sells and prices GEI sugar and addresses the imbalance of market power between mill owners and growers.

In July 2015, replacement explanatory notes were tabled, broadening the objectives as follows:

- to ensure a grower has a real choice in terms of nominating the marketing entity for on-supply of sugar in which they have an economic interest
- to facilitate a fair and final resolution of any commercial disputes that arise between a grower or bargaining representative and a mill owner including by arbitration.

Table 11 describes how the Bill would change the way parties do business if enacted.

Table 11 Impacts of the Amendment Bill on key stakeholders in the sugar industry

<i>Stakeholder</i>	<i>Base Case</i>	<i>Bill</i>
Growers	CSA arrangements with millers. Title transfers on delivery of cane to mill. Growers paid for sugar on the terms set out in CSAs. Most CSAs include the Cane Price Formula which provides for a roughly 2:1 distribution between growers and millers.	A new section is proposed that outlines the mandatory terms that must be included in a contract between the growers and mill owner, including: <ul style="list-style-type: none"> • terms establishing GEI in the proportion of raw sugar for which they have price exposure • growers provided a choice to nominate their preferred marketing entity for their GEI. A new section is proposed which provides growers, or their representatives or millers, the right to trigger a statutory arbitration process to resolve contractual and pre-contractual disagreements about supply contracts.
Millers	Millers contract with QSL for marketing of raw sugar. Some millers have commenced the purchase of raw sugar from QSL and commenced the marketing of raw sugar.	The Bill introduces statutory pre-contractual arbitration for growers to trigger in negotiation of supply contracts. See above section on mandatory terms that must be included in a supply contract between growers and miller.
QSL	QSL provides the following services: <ul style="list-style-type: none"> • acquiring raw sugar intended for bulk export from Queensland millers under RSSAs • selling the raw sugar acquired to international customers • chartering shipping for the raw sugar acquired • financing and hedging activities related to raw sugar (with growers having a choice to use QSL or alternative arrangement) • sub-leasing, operating and providing storage and handling services at STL. 	The Bill does not propose changes to the service functions performed by QSL
STL	Terminals managed by QSL, based on a cost recovery only basis.	The Bill does not propose changes to the service functions performed by QSL

4.3.2 Option 2 legal impacts – interference with property rights

Millers have expressed concern that the Bill will have the effect of vesting the title to raw sugar in somebody other than the mill owner that produced it ²³⁰ due to the fact that millers may lose the right to determine where they market raw sugar.

For example millers note that provisions of the Bill will force a miller to enter into an agreement with a marketing body²³¹ and is thus inconsistent with the voluntary marketing arrangements that have existed since 2006.

Section 4 of the *Legislative Standards Act 1992* sets out the meaning of fundamental legislative principles and includes the following:

- does not adversely affect rights and liberties of individuals;²³² and
- does not compulsory acquire property unless there is fair compensation. ²³³

²³⁰ Agriculture and Environment Committee (2015), page 23

²³¹ Agriculture and Environment Committee (2015), page 23

²³² Section 4(2)(a) of the Legislative Standards Act 1992.

²³³ Section 4(3)(i) of the Legislative Standards Act 1992.

To the extent that the Bill limits the ability of the millers to sell any raw sugar to which it has legal title then the Bill interferes with the property rights of the millers.

One complexity which arises in the current circumstances is that it is not clear what the post 2017 contractual arrangements will look like. To the extent that the Bill only implies a new term into future contractual arrangements then it is arguable that there has not been an 'acquisition' of a previously held property right. This is because at the time that the contract would be entered into there would be an additional term required by legislation.

However, based on the information we have reviewed it is likely that future CSAs will still provide millers with legal title to the sugar cane. Assuming that, the Bill, if enacted, will have the effect of removing one of the legal rights attached to property.

4.3.3 Option 2 legal impacts – Singapore-Australia Free Trade Agreement (SAFTA)

Millers have expressed concern that aspects of the Bill may be in possible contravention of aspects of the SAFTA. Specifically, Wilmar's submission to us and the AEC, provided legal opinion that the Bill could be a possible contravention of Chapter 8 of the SAFTA:

as such, re-regulation of the Queensland sugar industry affect the ownership rights of millers over their manufactured product, could result in a need for effective and adequate compensation under the terms of the SAFTA.²³⁴

Wilmar's rights under the FTA

Chapter 8 of the FTA protects and promotes investments of investors of each country. Australia must provide certain protections to investments made by Singapore investors.

Article 11 prohibits expropriation or nationalisation without compensation. It provides:

"Neither Party shall nationalise, expropriate or subject to measures having effect equivalent to nationalisation or expropriation (hereinafter referred to as "expropriation") the investments of investors of the other Party unless such a measure is taken on a non-discriminatory basis, for a public purpose, in accordance with due process of law, and upon payment of compensation in accordance with this Article."

In addition to this, Article 4 sets the minimum standard of treatment in customary international law which includes fair and equitable treatment and full protection and security.

Our initial view is that, on balance, Wilmar may not be able to demonstrate that the enactment of the Bill has resulted in a breach of the FTA because there has been no expropriation of its investment, nor has there been a breach of fair and equitable treatment. Having said that, Wilmar may still commence a claim against Australia if it believes that it has an arguable case under the FTA.

4.3.4 Option 2 legal impacts – authorisation of anti-competitive conduct under the CCA

Subsections 47(6) and (7) of the CCA prohibit third-line forcing. For example, s 47(6)(a) prohibits a corporation from supplying goods to a person on the condition that the person will acquire goods or service of a particular kind from another person. Conversely, s 47(7)(a) prohibits a corporation from refusing to supply goods to a person because the person has not agreed to acquire goods of a particular kind from another person. The Bill can be said to have the effect of a grower(s) supplying sugar cane to a miller on the condition that the miller acquires marketing services from a particular person (being the nominated marketer).

²³⁴ Wilmar (2015). Submission to Agriculture and Environment Committee, page 23

Another potential competition law issue would arise if the growers agreed amongst themselves that each of them would nominate the same marketer. This is because section 45 of the CCA prohibits a corporation from entering into a contract, arrangement or understanding which contains an exclusionary provision.

An ‘exclusionary provision’ is defined in section 4D of the CCA as an agreement, arrangement or understanding between competitors which contain a provision that has the purpose of preventing, restricting or limiting:

- (a) the supply of goods or services to, or the acquisition of goods or services from, particular persons or classes of persons; or
- (b) the supply of goods or services to, or the acquisition of goods or services from, particular persons or classes of persons in particular circumstances or on particular conditions;

by all or any of the parties to the contract.

It is at least arguable that the Bill is facilitating an agreement between the growers (some of whom are competitive with each other) which has the purpose of limiting the supply of sugar cane to millers in particular circumstances (that is, where the miller has not agreed to accept the nomination of the growers).

Exclusionary provisions are cartel conduct and are considered a serious breach of the CCA.

It is also a criminal offence under section 44ZZRF to make an agreement between competitors which has the purpose of limiting the supply of goods or services to a third party. It is also arguable that the Bill is facilitating conduct which would otherwise be in breach of this provision. [This provision has criminal consequences including jail terms for parties to the agreement.]

Finally, section 45 prohibits contracts, arrangements or understandings which have the purpose or effect of substantially lessening competition. A collective agreement between growers which forces a miller to acquire marketing services from a nominated marketer is likely to substantially lessen competition if the agreement is between a significant number of the growers. For example, if all of the growers agreed that all (or a significant proportion) of raw sugar should be marketed by the same entity then this is likely to prevent a new entrant into the market for the marketing of raw sugar. When there is only one market participant, the raising of barriers to entry so that no other person is likely to enter the market, is likely to have at least the effect of substantially lessening competition.

Section 51(1)(b) states that in deciding whether a person has contravened Part IV, anything done in a State that is specifically authorised by a State Act must be disregarded. The same provision of the Competition Code is to the same effect. In reliance on both the CCA and Competition Code provisions, clause 8 of the Bill would insert a new section 238 which would authorise things to be done in relation to supply contracts under proposed section 33B.

As set out in Section 41.1, use of a legislation exemption under section 51 of the CCA must be supported by evidence that there is a clear public benefit and that there are no other ways the policy objective can be achieved. Without this justification, a regulation may be overturned by the Commonwealth Government and there is nothing to prevent the ACCC taking action against any parties that may engage in anti-competitive conduct in complying with legislation.

A public benefit assessment of the net benefits of authorising the proposed anti-competitive conduct was not undertaken prior to introduction of the Bill.

4.3.5 Option 2 legal impacts – pre-contractual arbitration

Pre-contractual dispute arbitration could provide growers with added protection against misuse of market power during negotiations of cane supply agreements. It helps to redress any imbalance in market power by resolving deadlocks during negotiations.

However, the degree of benefit to be gained will depend on the extent of the misuse of market power. Given our conclusion that there is currently no evidence of an abuse of market power occurring in Queensland in the sugar industry, we consider it is likely that the benefits of pre-contract arbitration, over and above the existing mediation arrangements, are likely to be modest.

However, it is likely that canegrowers and millers would face additional financial and time costs associated with arbitration disputes. Given the evident lack of trust between the parties, numerous disputes are possible, especially if growers pursue individual cases.

We have taken into consideration that disputes could be related to the distribution of net premiums. However as previous studies (undertaken pre-deregulation) indicate arbitration may impact on costs and productivity and so could have a negative impact on the overall size of returns to all industry stakeholders (especially given there will be no capacity to influence the world sugar price).

We note that arbitration cases can be costly to administer. We understand that an arbitration process has an average time frame of between twelve and eighteen months and the likely legal costs for each party could be in the range of \$1.2 million and \$1.5 million (not taking into account discounted rates).

This assumes that the parties would appoint only one arbitrator and that the *Commercial Arbitration Act 2013* would apply. If the growers commence the arbitration as a group, similar to the concept of a class action, and they are represented by the same lawyer. The estimate may be higher if the applicants have slightly different individual positions which would need to be considered. Unless there is already an arbitration agreement in place, the parties could agree upon a fast tracked timetable, which would on average be around nine months.

We note that in the telecommunications industry a negotiate/arbitrate process was adopted by Parliament and then abandoned. The reasons for abandonment included: the extensive amount of arbitrations which were being run by the owner, Telstra, the processes were time consuming (sometimes taking years), in the later years, judicial review had been sought in respect of almost all final arbitration determinations made by the ACCC and there were multiple steps at which procedural matters could be challenged.

The Hildebrand report (2002) considered pre-contract negotiations and noted that:

... time spent in aggressive conflict between co-dependent parties as sheer waste.

Overall, we consider that the potential benefits of pre-contractual arbitration are likely to be outweighed by the costs.

We consider that if there was an abuse of market power in the future, there are a number of existing regulatory options available to growers. For example, it is clear that the unconscionable conduct provisions of the CCA apply to circumstances of business-to-business contracts and section 46 of the CCA prohibits an abuse of market power. However, if in the future significant evidence emerged of abuse of market power the adequacy of the available dispute resolution process would need to be reassessed.

4.3.6 Option 2 economic impacts – millers

The Bill introduces sovereign risk for millers to the extent that it has the effect of removing one of the millers' rights to property for the raw sugar its produces that is currently conferred by way of a contractual agreement.

It is impossible to estimate the economic impact that this sort of change would have on miller investment, including future confidence to invest in Queensland. Queensland would be considered a safe, stable economy in which to invest as evidenced by the increase in investment since deregulation. Given the three largest millers have a global presence, we consider that a legislative change in this way would make Queensland a less desirable investment destination, compared with other jurisdictions.

Should the Bill proceed, we would expect to see a reduction in mill investments (including mill improvements), relative to the base case. It would be reasonable to assume that in a capital constrained environment these companies would move capital into other parts of their firms particularly if they had the capacity to control all other aspects of their supply chain.

There are some millers who consider they will be able to get a better financial outcome than QSL, and with the operation of the Bill may lose this ability. Wilmar has estimated the potential loss of value at being \$46 million per annum above the returns currently achieved from the export of raw sugar.²³⁵ We note that some of this additional value is attributable to changing trading behaviour in the world sugar price and would be able to be captured if the Bill is enacted.

It is difficult to predict what the marketing behaviour of millers and marketers would be if the Bill is enacted. If these potential benefits of marketing are as Wilmar suggests, it would be anticipated that millers would still have an incentive to compete for market share. However, making marketing choice available to growers (as opposed to marketing choice for millers) would not be costless. Having marketers compete for the business of 4,000 cane producers would increase marketing costs of attracting and retaining customers, and combined with higher transaction costs, would be costly.

To the extent that premiums are still capped by global factors, at least some of the additional benefits of having growers choose a marketer could be offset by higher costs to manage the system, and depending on grower and marketer behaviour, the sugar industry could be worse-off.

4.3.7 Option 2 economic impacts – growers

Growers in their submissions to both QPC and AEC have largely expressed support for being provided the choice to nominate their preferred marketing entity for GEI, as expressed in the Bill.

Passage of the Bill would provide growers with the ability to nominate a choice of marketer over raw sugar from which they derive economic interest.

While growers would consider the choice of marketer as a benefit, there is the potential scenario that their preferred marketing entity may not maximise the amount received from a miller's raw sugar production. While we have estimated the value of average net premiums to growers is around \$14 million per annum, any additional premiums are likely to be considered important to smaller cane farming operations.

There is a potential opportunity cost of growers receiving a lower premium than what could be achieved by the miller choosing the form of marketing.

²³⁵ Wilmar (October 2015) Submission to Queensland Productivity Commission, page 22

In section 3.8 we noted that transparent information on marketing risks, costs and premiums assists growers making an informed decision on choice of marketing entity.²³⁶

4.3.8 Option 2 economic impacts – QSL

Implementation of the Bill would result in QSL gaining the opportunity to compete in the market for the grower’s economic interest. The addition of more marketing volume would act to reduce the risk that QSL has reached a ‘critical mass’ as coined by Tully Sugar, wherein it no longer enjoys economies of scale in its financing and potentially pricing and price risk management functions.

Additional marketing volume may also lend leverage to QSL that it retains its sublease with STL as it will be less likely to breach the volume threshold wherein STL can consider termination.

4.3.9 Option 2 economic impacts – STL

STL has a number of options including:

- continuing to engage QSL to manage the terminals under the sublease
- operating the terminals itself – achieved by purchasing equipment from QSL and employing QSL’s terminal employees. Alternatively, STL could engage another terminal operator
- individual terminals could be sold or subleased to milling companies.

It is difficult to determine the particular impacts on STL, as the potential composition of marketers of raw sugar is unknown.

4.3.10 Option 2 – economic impacts for sugar industry

The likely impacts of the Bill on the sugar industry are set out below. As discussed earlier, the largest impact is likely to be on future milling investment as it would be anticipated that the Bill would reduce future incentives for investment.

Table 12 Summary of impacts of the Bill

	<i>Option 1 - Base Case — Do nothing (Post 1 July 2017)</i>	<i>Option 2 — Bill</i>
Cane production	Change of marketer is unlikely to change the influences of cane production.	Change of marketer is unlikely to change the influences of cane production.
Raw sugar production	Change of marketer likely to have minimal impact on raw sugar production in the short term. May increase production longer term if marketing improvements if yields higher return.	Perceptions of sovereign risk may lower mill investment leading to lower mill availability and raw sugar production.
World raw sugar price (ICE No.11)	Set by world market	Set by world market
Net premiums	Average net premiums are presumed to be at least maintained under either QSL or alternative marketer. Some millers may be able to achieve a higher premium from alternative marketing.	Average net premiums are presumed to be at least maintained under either QSL or alternative marketer. Some millers may be able to achieve a higher premium from alternative marketing.
Investment in cane production	Continue to be influenced by forecast world sugar prices, input costs and availability of suitable cropping land	Continue to be influenced by forecast world sugar prices, input costs and availability of suitable cropping land

²³⁶ Under the Bill, all prospective marketing entities, including QSL, would need to provide this information to growers to ensure that premiums were not reduced.

	<i>Option 1 - Base Case — Do nothing (Post 1 July 2017)</i>	<i>Option 2 — Bill</i>
Investment in mills	Influenced by forecast world sugar prices, input costs, and cane production in mill area	May result in reduction in mill investment if millers perceive better returns on capital from other parts of international businesses.
Employment	No material change in employment expected	Potential reduction if reduced mill investment

4.4 Option 3 –Code of Conduct

An alternative to legislative change to the SIA, would be the implementation of a Code of Conduct. Two alternatives have been proposed:

- Sugar Industry Code of Conduct Regulation²³⁷; or
- Mandatory Code of Conduct – under Section 51AE of the CCA. Mandatory codes set out the responsibilities and expectations of participants in a market through a set of principles or guidelines.

Mandatory codes can be more efficient than legislation and may improve the public image of an industry. Mandatory codes prescribed under the CCA, do not require additional legislation to develop. There are mandatory codes in place for Horticulture, Bulk Wheat Port Terminals, Franchising, Fuel and Unit Pricing.

The Burdekin District Cane Growers Ltd has provided detailed drafting for a Sugar Industry Code of Conduct, and as discussed in Section 2.5, the Senate recommended the development of a mandatory industry code, and the Australian Government’s Sugar Industry Code of Conduct Taskforce subsequently indicated a number of matters that could be included in a Code. Some stakeholders state that any code of conduct would need to be mandatory.²³⁸

The Sugar Industry Code of Conduct, and the Mandatory Code include:

- a mechanism to distribute relevant interests in the quantities of sugar obtained from cane between growers and millers
- a link between the price paid for cane and the selling price of sugar
- the ability to choose marketing services
- non-discriminatory provisions
- a mechanism to resolve disputes – the Sugar Industry Code of Conduct proposes both mediation and pre-contract arbitration.

In practice, a Sugar Industry Code of Conduct or Mandatory Code of Conduct could include any number of matters to provide a framework for the negotiation between stakeholders. However, in this circumstance, we have assumed that the provisions in the Sugar Industry Code of Conduct would be applied.

While the legal mechanisms for implementation of the Code(s) are different, the practical effect of the Sugar Industry Code of Conduct is essentially the same as the Bill. For this RIS, we have

²³⁷ Burdekin District Cane Growers Ltd (2014). Submission to Agriculture and Environment Committee – Appendix 2

²³⁸ Canegrowers Rock Point (2015) Submission to Queensland Productivity Commission, page 7

assessed the legal and economic impacts of a Code of Conduct to be similar to those presented for the Bill (see Section 4.3). The ASMC supported this conclusion.²³⁹

In comparison to the passage of a Bill, we note that a Mandatory Code of Conduct is likely to result in larger initial costs to industry to develop. However over the longer term a mandatory code is likely to be less costly to adopt and administer than legislation as well as being easier to amend in the event of unforeseen circumstances. A mandatory code under the CCA would also see the ACCC acting as an arbitrator in any dispute resolution cases that arise.

The impacts of a mandatory code of conduct are summarised in **Table 13**.

Table 13: Impacts of code of conduct

	<i>Option 1 - Base Case — Do nothing (Post 1 July 2017)</i>	<i>Option 3 — Code of Conduct</i>
Cane production	Change of marketer is unlikely to change the influences of cane production.	Change of marketer is unlikely to change the influences of cane production.
Raw sugar production	Change of marketer likely to have minimal impact on raw sugar production in the short term. May increase production longer term if marketing improvements if yields higher return.	Perceptions of sovereign risk may lower mill investment leading to lower mill availability and raw sugar production.
World raw sugar price (ICE No.11)	Set by world market	Set by world market
Net premiums	Average net premiums are presumed to be at least maintained under either QSL or alternative marketer. Some millers may be able to achieve a higher premium from alternative marketing.	Average net premiums are presumed to be at least maintained under either QSL or alternative marketer. Some millers may be able to achieve a higher premium from alternative marketing.
Investment in cane production	Continue to be influenced by forecast world sugar prices, input costs and availability of suitable cropping land	Continue to be influenced by forecast world sugar prices, input costs and availability of suitable cropping land
Investment in mills	Influenced by forecast world sugar prices, input costs, and cane production in mill area	May result in reduction in mill investment if millers perceive better returns on capital from other parts of international businesses.
Employment	No material change in employment expected	Potential reduction if reduced mill investment

4.5 Option 4 – Tolling agreement between growers and millers

Option 4 is for growers to contract with millers for toll crushing services, where growers would take ownership of all raw sugar and pay millers for the full cost of crushing services and have full control of the marketing of raw sugar products.

To protect against the potential abuse of market power, QSL has suggested the following options to allow for a regulatory body to set the toll crushing prices:

- amend the third party access regime under Part 5 of the QCA Act and Part IIIA of the CCA.
- provide for a specific access regime in the SIA.

²³⁹ ASMC (November 2015). Submission to Queensland Productivity Commission, page 1

QSL noted the intent of its proposed alternatives is to ensure that the terms of access to the crushing services of the mills (and related transport and logistics services) – which are in a monopoly position – can be regulated.²⁴⁰

4.5.1 Option 4 legal impacts – no impediments to negotiating a commercial agreement

In Chapter 3, we noted there are no legislative or regulatory impediments to parties negotiating a toll crushing agreement. However, a toll crushing arrangement would change the relationship between growers and millers and the contractual arrangements would need to change to reflect the different risk and pricing arrangements.

4.5.2 Option 4 legal impacts – declaration of mills for third party access not an option under existing legislation

We note that QSL has proposed declaring the mills, in order to provide third party access to the ‘cane crushing services’. Under section 72(2)(b) the QCA Act – Meaning of a service – a service does not include:

...the use of intellectual property of intellectual property or a production process (except to the extent that the use is an integral, but subsidiary, part of the service.

We consider ‘cane crushing’ to be a production process, which falls outside the long established definition of a service eligible for declaration under the QCA Act. Similarly, under the CCA definitions, ‘service’ means a service provided by a facility, but does not include the supply of goods, or the use of intellectual property, or the use of a production process (except to the extent that it is an integral but subsidiary part of the service.

Amendment to these acts to allow for processing process to be regulated would represent a major move away from the established third party access arrangements.

4.5.3 Option 4 economic impacts – millers

The introduction of a tolling arrangement would likely lead to millers negotiating a charge to growers on a per tonne of cane basis, to cover the operating cost of processing and a commercial return on the assets employed in crushing.

We note Wilmar’s position that a commercial tolling arrangement may see the costs to growers increase.²⁴¹ We have not undertaken a regulatory analysis of the numbers presented by Wilmar, however, it is not an unreasonable assumption that the costs borne by growers would increase. Specifically, a tolling price would be expected to remain stable from year to year, as millers would neither receive the upside returns from high sugar prices or the downside risks and would need to earn returns solely from crushing activities.

Current or prospective mill owners are also likely to consider the amount of tolling charges received from growers in determining whether to invest in new and existing mill infrastructure. If these charges are not sufficient to earn a commercial return, this could reduce mill investment. This may limit increases in raw sugar production and mill innovation. On the other hand, well designed contractual arrangements could continue to provide mill owners with the incentive to innovate.

While we have noted that the existing State and Commonwealth third party access arrangements would not capture mill production, we also consider that the co-dependent relationship between millers and growers would provide a natural limit on the prices that could be charged for crushing.

²⁴⁰ QSL (2014) Submission to Senate Rural and Regional Affairs and Transport Committee, page 29

²⁴¹ Wilmar (October 2015) Submission to Queensland Productivity Commission, pages 26-27

4.5.4 Option 4 economic impacts – growers

Option 4 would see growers take on all price, marketing and cost risks, including the costs of toll crushing. Growers would continue to have the revenues set through world prices, so any gains to growers would need to come from improving marketing premiums relative to those earned by the existing marketing arrangements or reducing costs of production across the raw sugar supply chain.

A toll crushing arrangement would see a move away from the Cane Price Formula and require the negotiation of a cost contract with each of the mills involved – and potentially means 21 separate arrangements and cost arrangements.

We would expect the implementation costs for new toll crushing arrangements to be high, given the need to agree efficient operating and maintenance costs, assets values and returns. There are well established methods for establishing these estimates, however, it is noted that where they are regulated it can be a costly and time consuming process to have stakeholders agree what is the efficient base.

Option 4 is likely to impose significantly higher transaction costs than either the existing arrangements or the Bill/Code options and require either new intermediaries to manage the supply chain or growers to become more actively involved in the management of all aspects of their supply chains.

4.5.5 Option 4 economic impacts – QSL

The introduction of a tolling arrangement would likely see QSL continue to have an opportunity to compete in the market for raw sugar. There is the potential that QSL would gain additional marketing volume compared to the base case provided it is able to offer an attractive marketing product compared to alternative marketers. QSL may also take on a more active supply chain management role, although this would need to be a commercial decision of the growers.

The addition of more marketing volume would act to reduce the risk that QSL had reached a ‘critical mass’ as coined by Tully Sugar, wherein it no longer enjoys economies of scale in its financing and potentially pricing and price risk management functions.

Additional marketing volume may also lend leverage to QSL that it retains its sublease with STL as it will be less likely to breach the volume threshold wherein STL can consider termination.

4.5.6 Option 4 economic impacts – STL

Terminals are currently managed by QSL under a cost recovery only basis. Under a tolling arrangement, QSL could still negotiate with STL for the sub-leasing and operating of terminals.

Other options are available to STL however including the operating the terminals itself or engaging an alternative terminal operator (marketing entity or otherwise).

4.5.7 Option 4 economic impacts – sugar industry production assumptions

Our assumptions on the economic implications of Option 4 are set out in **Table 14**.

Table 14: Impacts on sugar industry production under tolling option

	<i>Option 1 - Base Case — Do nothing (Post 1 July 2017)</i>	<i>Option 4 — Tolling</i>
Cane production	Influenced by forecast of world sugar prices, input costs and environmental conditions and mill availability.	Influenced by forecast of world sugar prices, input costs and environmental conditions and mill availability.

	<i>Option 1 - Base Case — Do nothing (Post 1 July 2017)</i>	<i>Option 4 — Tolling</i>
Raw sugar production	May increase production longer term if miller marketing improvements prove to yield consistently higher return, noting that this is still a small proportion of the final price.	Raw sugar production unlikely to change unless the tolling arrangements lead to a reduction in mill investment relative to the existing model where millers make the commercial decision to invest.
World raw sugar price (ICE No.11)	Set by world market	Set by world market
Net premiums	Average net premiums are presumed to be at least maintained under either QSL or alternative marketer. Some millers may be able to achieve a higher premium from alternative marketing.	Average net premiums are presumed to be at least maintained under either QSL or alternative marketer. Millers may exit marketing sugar, which would reduce competition in marketing.
Investment in cane production	Continue to be influenced by forecast world sugar prices, input costs and availability of suitable cropping land	Continue to be influenced by forecast world sugar prices, input costs and availability of suitable cropping land Returns to cane production are likely to be more volatile from year to year as cane crushing costs would be largely fixed (although linked to the volume of production) and sector would face higher transaction costs.
Investment in mills	Influenced by forecast world sugar prices, input costs, and cane production in mill area.	The level of mill investment would depend on the commercial terms negotiated with growers.
Employment	No material change in employment expected	Potential reduction if reduced mill investment

5 CONSULTATION



Public consultation is a critical part of any regulatory development process. In line with regulatory best practice principles, there should be effective consultation with affected key stakeholders at all stages of the regulatory cycle.

In Queensland, the development of a RIS is a two stage process, consisting of a:

- Consultation RIS – is a draft RIS publicly released to provide interested stakeholders with information to allow informed debate
- Decision RIS – which considers the submissions received during consultation and is designed to inform and recommend a final policy decision.

In developing this RIS, we called for initial submissions from stakeholders. Submissions from ten organisations were received as part of this process.

We have also taken into account the information provided by stakeholders as part of recent inquiries into these matters by both the Queensland Parliament Agriculture and Environment Committee and the Australian Senate’s Regional and Rural Affairs and Transport References Committee.

Due to the urgency attached to inform the Queensland Parliament’s consideration of the Bill, submissions to the Consultation RIS closed on **13 November 2015**.

These submissions have been published on our website and were considered in the development of the Decision RIS. **Appendix B** provide a summary of comments received and our considerations of these matters.

We provided the completed Decision RIS to the Government on **25 November 2015**.

6 SUMMARY OF IMPACTS AND PREFERRED OPTION



Good practice regulation would suggest that the regulatory option that provides the greatest net benefit to the community overall, including the consideration of the option of no additional intervention, should be implemented. Further, if regulation restricts competition or authorises anti-competitive conduct, it must be demonstrated that:

- the benefits of the restriction as a whole outweigh the costs; and
- the objectives of the legislation can only be achieved by restricting competition.

Use of a legislation exemption under section 51 of the CCA must be supported by evidence that there is a clear public benefit and that there are no other ways the policy objective can be achieved. Without this justification, a regulation may be overturned by the Commonwealth Government. Clause 8 of the Bill specifically authorises anti-competitive conduct. A statutory authorisation is necessary to prevent the ACCC taking action against any parties that may engage in anti-competitive conduct in complying with legislation.

Our conclusions on the net benefits of the options that would meet the objectives of the Bill are set out below.

6.1 Summary of impacts and assessment of net benefits

In **Appendix C**, we have provided an assessment of the likely impacts of each option considered on growers, millers, QSL, STL.

6.1.1 Option 1 – Base case – no additional legislation

The base case is to make no additional changes to the SIA, with protections from anti-competitive behaviour included in the CCA.

In Chapter 3, we concluded that there was no evidence of market failure in the Queensland sugar industry, having specifically considered the appropriate recognition of property rights, market power and the potential abuse of market power by mill owners, and whether growers and millers have sufficient transparency about pricing and premiums to provide for balanced negotiations.

We cannot conclude there is market failure in the Queensland sugar industry because millers are not offering growers choice to determine the marketing arrangements for something they do not own. Nor do we consider that this is inhibiting competition in the market, because the ‘market’ is the market for the export of raw sugar, which is contestable.

We consider the regulatory arrangements for the Queensland sugar industry should be able to meet the objectives of:

- ensuring a pricing framework where there is an appropriate balance of risk and reward between growers and millers

- ensuring there are appropriate protections for growers and millers to prevent against the abuse of market power
- ensuring a regulatory framework that supports investment and innovation in the sugar industry and supports the long-term economic sustainability of the sugar industry.

There is evidence the existing regulatory framework has supported investment in the Queensland sugar industry, including investment to improve mill availability. It also supports the development of new models of marketing export raw sugar, as was envisaged prior to deregulation.

The most likely impact of the no change scenario is that growers and millers will be no worse off, and with some millers pursuing models that could increase the returns to the sector. To the extent that these improvements increase raw sugar production and/or increase net premiums these benefits are generally distributed to growers on a 2:1 ratio, consistent with the Cane Price Formula.

While concern has been raised about QSL's potential viability by some growers, this has not been raised by the millers who have indicated they will remain with QSL for the 2017 season. These millers have not supported a change to the existing arrangements. STL would continue to provide bulk storage facilities, although we note that STL has not formed a view on the future arrangements that would apply.

Given our conclusion that there is no evidence of market failure that would indicate a need for additional regulation, our conclusion for the Decision RIS is that retaining the existing regulatory framework — with no additional regulation — will provide the greatest net benefit to Queensland.

In reaching this conclusion, we are very aware of the protracted impasse within the industry. However, we do not consider that this should be resolved by amending the legislative arrangements as proposed by the Bill (Option 2).

6.1.2 Option 2 - Regulation as proposed by the Bill

The Bill's objectives are:

- to ensure a grower has a real choice in terms of nominating the marketing entity for on-supply of sugar in which they have an economic interest
- to facilitate a fair and final resolution of any commercial disputes that arise between a grower or bargaining representative and a mill owner including by arbitration.

The Bill's stated intent is to prevent anti-competitive behaviour and promote pro-competitive outcomes and to ensure economic viability for both growers and mill owners, among others, in the Queensland sugar industry.

Our assessment is that the Bill has a number of legal and economic impacts that would mean that any benefits from offering grower (rather than miller) choice of market, are outweighed by the cost. Specifically, the Bill

- interferes with the property rights of millers, assuming the existing structure of CSAs is retained. This is likely to reduce the profitability of future sugar mill investment and dampen longer term innovation and productivity compared to no additional regulation
- could reduce the overall returns to the sugar industry. The larger millers have made commercial decisions that they can improve financial outcomes by marketing export raw sugar – the remaining millers have made the commercial decision to market export raw sugar through QSL. There is nothing to suggest that millers – with a commercial incentive to improve returns from their production of raw sugar are not well equipped to make this decision. Further, to the extent that returns are distributed to growers – it is difficult to see

how growers are disadvantaged and the proposals by MSF and Wilmar seem to have sufficient transparency that if a disadvantage were to arise, it would be identifiable to the growers

- could reduce the returns to the industry by adding extra costs. Marketers would need to compete for the business of 4,000 cane producers with costs to attract and retain customers and additional transaction costs. As marketing premiums are still capped by global factors, it is possible that any additional competitive benefits of having growers choose a marketer could be offset by higher costs
- re-introduction of pre-contract arbitration may lead to both financial (legal) and time loss costs for the industry. Legal costs for an average arbitration are estimated to range between \$1.2 and \$1.5 million per dispute, with the time to resolve disputes estimated at 12 – 18 months, with a ‘fast track’ of 9 months. It is not clear that pre-contract arbitration adds additional benefits above the mediation arrangements
- could leave parties exposed to action by the ACCC, if the Australian Government does not accept that there is a net benefit from the authorisation of anti-competitive conduct included in the Bill. Clause 8 of the Bill would authorise some additional anti-competitive behaviour. If the Queensland Parliament legislates for a restriction on competition, it must advise the ACCC within 30 days. The Australian Government can disallow the authorisation if the benefits of the anti-competitive conduct do not outweigh the costs. A cost benefit assessment was not completed prior to introduction of the Bill and there is the risk if the Australian Government is not satisfied by the public benefit justification that parties engaged in anti-competitive conduct would not have the protection of an authorisation.

From an economic perspective, relative to the base case, we have assumed that average premiums are at least maintained comparative to the pre 1 July 2017 case.

The economic analysis indicates the Bill is unlikely to have material impacts on most parts of the sugar industry in Queensland — the notable exception being investment in the milling sector. The impact on property rights implied in the Bill introduces sovereign risk into the sector. We consider this will make Queensland a less attractive investment than alternative options, particularly for companies with the option to invest across a range of countries and agri-businesses.

We consider the potential benefits of the Bill to growers are marginal at best in comparison to the costs and risks that would be faced by millers and the industry from potential loss of future investment. It is also not apparent that policy objectives implied by the Bill cannot be achieved without additional legislation, particularly legislation that includes the authorisation of anti-competitive conduct under the CCA.

A number of grower responses to our Consultation RIS said our draft conclusion was at odds with the objectives of the National Competition Policy.²⁴²

As a general statement, we agree with CANEGROWERS and ACFA about the overarching objective of the National Competition Policy, about the role of competition in a properly functioning market. In a properly functioning market, a change of ownership arrangements between parties should occur by way of commercial negotiation.

However, in this case, the Bill is seeking to create a competitive market by removing one of the benefits of property from millers and transferring it to growers. We are not aware of any

²⁴² CANEGROWERS and ACFA (November 2015). Submission to Queensland Productivity Commission, page 7

circumstance where the National Competition Policy had the intention of creating a market by statutorily removing ownership rights from one party and transferring them to another.

As discussed above in section 4.3.7, the Bill goes further, and then allows growers to engage in anti-competitive conduct that would otherwise be prohibited under the CCA.

While there is clearly an impasse between the parties about the marketing arrangements, we cannot conclude that an intervention of this form is warranted. We also note that this is in contrast to the conclusion formed by the Senate Committee and the Federal Taskforce on a Mandatory Code for Conduct for Sugar Marketing, however, we do not see evidence that the interference in property rights was considered as part of these deliberations.

Our conclusion for the Decision RIS is that potential benefits that may accrue from passage of the Bill, are outweighed by the potential costs and risks.

6.1.3 Option 3 - Code of Conduct

We have considered the option of a code, as described by the Sugar Industry Code of Conduct Regulation proposed by the Burdekin and the Sugar Industry Mandatory Code of Conduct Taskforce. A code can be developed by the industry under section 51AD of the CCA. We consider that economic impacts of a code of conduct would be of a similar to the Bill, depending on the matters included in the Code. Our conclusion for the Decision RIS is that potential benefits from a Code of Conduct are outweighed by the potential costs and risk.

6.1.4 Option 4 - Tolling arrangement

A tolling arrangement, where growers take ownership of all raw sugar and pay millers for the full cost of crushing services and have full control of the marketing of raw sugar products would represent the change for the sugar industry. It would mean that growers take on all price, marketing and cost risk (including for crushing).

There is nothing to prevent a tolling arrangement being negotiated between millers and growers (noting our view that neither the QCA Act nor CCA allow for third party access regulation). However, negotiation of new arrangements would be costly. Growers and millers would need to agree the efficient costs of operating and maintain mills, the value of mill assets, the return on mill assets and a framework for investment in mill assets. This would require all parties to co-operate in the development of what would be, a very different model of sugar production in Queensland.

Moving to a tolling arrangement would need to be achieved by commercial agreement amongst the parties. Our conclusion for the Decision RIS is that potential benefits from implementation of a tolling arrangement would need to be carefully considered against the additional costs and risks of negotiating new arrangements.

6.2 Conclusion

Our conclusion is that the case for additional regulation of the Queensland sugar industry, at this point in time, has not been established.

While there is an evident lack of trust between certain parts of the sugar industry we do not consider there is evidence of market failure, or that the existing legislative framework means that issues cannot be resolved through commercial negotiations.

We consider that retaining the existing regulatory framework, with no additional regulation, will provide the greatest net benefit to Queensland, and that there are sufficient protections already in place to protect against misuse of market power.

However, if there was a change in circumstances, particular evidence of market failure, including abuse of market power, this conclusion would need to be reviewed.

GLOSSARY

A

AEC	Agriculture and Environment Committee
ACFA	Australian Cane Farmer's Association
ASMC	Australian Sugar Milling Council

B

BSL	Bundaberg Sugar Limited
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C

CCA	<i>Competition and Consumer Act 2010</i>
CCS	Commercial Cane Sugar
CSA	Cane Sugar Agreements

F

FMIS	Forestry Management Investment Schemes
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G

GEI	Growers Economic Interest
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I

ICSM	Isis Central Sugar Milling Company Ltd.
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M

MEI	Millers Economic Interest
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Q

QSC	Queensland Sugar Corporation
QSL	Queensland Sugar Limited

R

RIS	Regulatory Impact Statement
RSSA	Raw Sugar Supply Agreement

S

SIA	Sugar Industry Act
STL	Sugar Terminals Limited

APPENDIX A: SUMMARY IMPACT TABLES

	Option 1 – Base Case		Option 2 – Bill	Option 3 – Mandatory Code	Option 4 - Tolling
	Pre 1 July 2017	Post 1 July 2017	(compared to post 1 July 2017 base case)		
<i>Growers</i>					
Supply agreements	CSA with millers. Most CSAs include the Cane Price Formula which provides for a roughly 2:1 distribution between growers and millers.	CSA with millers. Most CSAs include the Cane Price Formula which provides for a roughly 2:1 distribution between growers and millers.	CSA with millers. Most CSAs include the Cane Price Formula which provides for a roughly 2:1 distribution between growers and millers.	CSA with millers. Most CSAs include the Cane Price Formula which provides for a roughly 2:1 distribution between growers and millers.	Growers negotiate processing agreements with millers and retain title through the production process.
Management raw sugar price exposure	Growers have ability to manage 99% of price exposure through pools offered by QSL or third party.	Growers have ability to manage 99% of price exposure through pools offered by QSL or third party.	Growers have ability to manage 99% of price exposure through pools offered by QSL or third party.	Growers have ability to manage 99% of price exposure through pools offered by QSL or third party.	Growers have ability to manage 99% of price exposure through pools offered by QSL or third party.
Title	Title transfers on delivery of cane to mill.	Title transfers on delivery of cane to mill, unless growers and millers negotiate alternative agreement.	Title transfers on delivery of cane to mill. Growers provided a choice to nominate their preferred marketing entity for GEI. This has similar effect to providing legal title as growers control extends beyond delivery.	Title transfers on delivery of cane to mill. Growers provided a choice to nominate their preferred marketing entity for GEI. This has similar effect to providing legal title as growers control extends beyond delivery.	Growers retain title through the production process.
Net premiums	Net premiums earned through QSL shared pools	Net premiums earned through miller marketer, QSL or alternative market (at commercial decision of miller)	Net premiums earned through miller marketer, QSL or alternative market (at commercial decision of grower)	Net premiums earned through miller marketer, QSL or alternative market (at commercial decision of grower)	Net premiums earned through QSL or alternative market (at commercial decision of grower)
		Potential for increase in net premiums for distribution to growers.	Potential for increase in net premiums for distribution to growers. Likely higher transaction costs.	Potential for increase in net premiums for distribution to growers. Likely higher transaction costs	Potential for increase in net premiums for distribution to growers. Likely higher transaction costs
Arbitration			Ability to trigger both contractual and pre-contractual arbitration. Arbitration may provide benefits but increase legal and time costs. Legal costs estimated to range between \$1.2 M and \$1.5 M per dispute. Time to resolve dispute estimated at 12 – 18 months, with a ‘fast track’ of 9 months.	Ability to trigger both contractual and pre-contractual arbitration. Arbitration may provide benefits but increase legal and time costs. Legal costs estimated to range between \$1.2 M and \$1.5 M per dispute. Time to resolve dispute estimated at 12 –	

				18 months, with a 'fast track' of 9 months.	
<i>Millers</i>					
Marketing arrangements	Millers make the commercial decision to market the raw sugar they produce themselves, or enter into a market agreement with alternative marketer (which may include QSL or another marketer(s). Most millers contract with QSL for marketing of export raw sugar under RSSAs	Millers make the commercial decision to market the raw sugar they produce themselves, or enter into a market agreement with alternative marketer (which may include QSL or another marketer(s). Wilmar, MSF and Tully Sugar have announced they will manage their own marketing of raw sugar exports. ISMC, Mackay Sugar Limited and Bundaberg Sugar Limited have indicated they will remain with QSL for the 2017 season.			
Legal title	Title to raw sugar passes to QSL under RSSAs.	Title to raw sugar retained by millers marketing themselves Title to raw sugar passes to QSL under RSSAs for relevant millers	Millers would be required to enter into contracts to supply marketers with raw sugar as nominated by growers.		
		Millers make the commercial decision to market the raw sugar they produce themselves, or enter into a market agreement with alternative marketer (which may include QSL or another marketer(s). Wilmar has announced plans to market raw sugar directly. MSF and Tully have yet to indicate an alternative marketer. ISMC, Mackay Sugar Limited and Bundaberg Sugar Limited have indicated they will remain with QSL for the 2017 season.	Potentially interferes with property rights under future CSAs (if miller holds legal title) Potential costs to administer and facilitate grower's choice in preferred marketing entity for GEI May result in reduction in mill investment Opportunity cost of potentially lower premiums Both contractual and pre-contractual arbitration, which cannot be triggered by a mill. Arbitration may lead to both financial (legal) and time costs. Legal costs estimated to range between \$1.2 M and \$1.5 M per dispute. Time to resolve dispute estimated at 12 – 18 months, with a 'fast track' of 9 months.	Costs to design and operate under Code. If Code is poorly implemented, further costs could be incurred. Potentially interferes with property rights under future CSAs (if miller holds legal title) Potential costs to administer and facilitate grower's choice in preferred marketing entity for GEI May result in reduction in mill investment Opportunity cost of potentially lower premiums A mechanism to resolve disputes. Arbitration may lead to both financial (legal) and time costs. Legal costs estimated to range between \$1.2 M and \$1.5 M per dispute. Time to resolve dispute estimated at 12 – 18 months, with a 'fast track' of 9	

				months. ACCC as mediator may reduce costs.	
<i>QSL</i>					
QSL services	<p>QSL provides the following services:</p> <ul style="list-style-type: none"> acquiring raw sugar intended for bulk export from Queensland millers under RSSAs selling the raw sugar acquired to international customers chartering shipping for the raw sugar acquired financing and hedging activities related to raw sugar (with growers having a choice to use QSL or alternative arrangement) sub-leasing, operating and providing storage and handling services at STL 	<p>QSL would continue to provide the following services:</p> <ul style="list-style-type: none"> acquiring raw sugar intended for bulk export from the three millers for the 2017 season selling the raw sugar acquired to international customers chartering shipping for the raw sugar acquired financing and hedging activities related to raw sugar (with growers having a choice to use QSL or alternative arrangement) sub-leasing, operating and providing storage and handling services at STL 	<p>Potential increase in supply (compared to post 1 July 2017 base case) depending on growers nominating QSL as preferred marketing entity.</p>	<p>Potential increase in supply (compared to post 1 July 2017 base case) depending on growers nominating QSL as preferred marketing entity.</p>	<p>Likely QSL provides the following services:</p> <ul style="list-style-type: none"> acquiring raw sugar intended for bulk export from Queensland growers under RSSAs selling the raw sugar acquired to international customers chartering shipping for the raw sugar acquired financing and hedging activities related to raw sugar (with growers having a choice to use QSL or alternative arrangement) sub-leasing, operating and providing storage and handling services at STL
<i>STL</i>					
Terminal management	<p>Terminals managed by QSL, based on a cost recovery only basis.</p>	<p>STL has a number of options including:</p> <ul style="list-style-type: none"> continuing to engage QSL to manage the terminals under the sublease operating the terminals itself – achieved by purchasing equipment from QSL and employing QSL’s terminal employees. Alternatively, STL could engage another terminal operator 	<p>STL has a number of options including:</p> <ul style="list-style-type: none"> continuing to engage QSL to manage the terminals under the sublease operating the terminals itself – achieved by purchasing equipment from QSL and employing QSL’s terminal employees. Alternatively, STL could engage another terminal operator individual terminals could be sold or subleased to milling companies 	<p>STL has a number of options including:</p> <ul style="list-style-type: none"> continuing to engage QSL to manage the terminals under the sublease operating the terminals itself – achieved by purchasing equipment from QSL and employing QSL’s terminal employees. Alternatively, STL could engage another terminal operator individual terminals could be sold or subleased to milling companies 	<p>Likely that Terminals managed by QSL, based on a cost recovery only basis.</p>

		<ul style="list-style-type: none"> individual terminals could be sold or subleased to milling companies 			
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APPENDIX B: SUMMARY OF LIKELY IMPACTS ON SUGAR INDUSTRY UNDER ALTERNATIVE REGULATORY OPTIONS

	<i>Option 1 - Base Case — Do nothing</i>		<i>Option 2 — Bill</i>	<i>Option 3 — Mandatory Code</i>	<i>Option 4 — Tolling</i>
	<i>Pre 1 July 2017</i>	<i>Post 1 July 2017</i>	<i>(compared to post 1 July 2017 base case)</i>		
Cane production	Influenced by forecast world sugar prices, input costs, and environmental conditions and mill availability.	Change of marketer is unlikely to change the influences of cane production.	Change of marketer is unlikely to change the influences of cane production.	Change of marketer is unlikely to change the influences of cane production.	Influenced by forecast of world sugar prices, input costs and environmental conditions and mill availability.
Raw sugar production	Most likely influenced by cane production volumes and quality, mill availability and miller efficiency	Change of marketer likely to have minimal impact on raw sugar production in the short term. May increase production longer term if marketing improvements yields higher return.	Perceptions of sovereign risk may lower mill investment leading to lower mill availability and raw sugar production.	Similar to the Bill	Unchanged unless the tolling arrangements lead to a reduction in mill investment relative to the existing model where millers make the commercial decision to invest.
World raw sugar price (ICE No.11)	Set by world market	Set by world market	Set by world market	Set by world market	Set by world market
Net premiums	Average range of plus or minus \$5/net tonne raw sugar Assumed \$21 M per annum raw sugar distributed <ul style="list-style-type: none"> • \$14 M to growers • \$7 M to millers 	Average net premiums are presumed to be at least maintained under either QSL or alternative marketer. Some millers may be able to achieve a higher premium from alternative marketing.	Average net premiums are presumed to be at least maintained under either QSL or alternative marketer. Some millers may be able to achieve a higher premium from alternative marketing.	Similar to the Bill	Average net premiums are presumed to be at least maintained under either QSL or alternative marketer. Millers may exit marketing sugar, which would reduce competition in marketing.
Investment in cane production	Influenced by forecast world sugar prices, input costs and availability of suitable cropping land	Continue to be influenced by forecast world sugar prices, input costs and availability of suitable cropping land	Continue to be influenced by forecast world sugar prices, input costs and availability of suitable cropping land	Continue to be influenced by forecast world sugar prices, input costs and availability of suitable cropping land	Continue to be influenced by forecast world sugar prices, input costs (including tolling and transaction costs) and availability of suitable cropping land. Greater volatility returns.

	<i>Option 1 - Base Case — Do nothing</i>		<i>Option 2 — Bill</i>	<i>Option 3 — Mandatory Code</i>	<i>Option 4 — Tolling</i>
Investment in mills	Influenced by forecast world sugar prices, input costs, and ability to lift productivity	Influenced by forecast world sugar prices, input costs, and cane production in mill area	May result in reduction in mill investment if millers perceive better returns on capital from other parts of international businesses.	Similar to the Bill	The level of mill investment would depend on the commercial terms negotiated with growers.
Employment	Estimated 16,000	No material change in employment expected	Potential reduction if reduced mill investment	Similar to the Bill	Unknown

APPENDIX C: STAKEHOLDER SUBMISSIONS SUMMARY TABLE

	Submission points	QPC Response	References	How RIS changed
2.1 Are there any other grower concerns that we should take into consideration?				
1	Growers will lose the benefits of QSL, which they note offers buyers a unique niche supplier.	We have considered this issue in section 4.2.2 of the Decision RIS.	CANEGROWERS Burdekin, p. 2	No change to the RIS.
2	Wilmar Sugar Australia (WSA) advised CANEGROWERS Burdekin that they will be signing a 15 year contract with a Singaporean trading company to market the raw sugar. This separate company is a “for profit” taxable company that is privately owned. We have been unable to obtain details of the ownership of this company and we have been unable to obtain details on its financial standing. Wilmar Sugar Australia has advised that they will be signing a 15 year contract with this separate company. We have grave concerns that this arrangement has the potential to damage the milling company, Wilmar Sugar Australia, and we are concerned that Wilmar International could in fact sell the mills and Wilmar Sugar Australia once this 15 year lock in contract is in place.	Noted. We do not consider potential future ownership arrangements to be a relevant consideration for the marketing matter.	CANEGROWERS Burdekin, p. 2	No change to the RIS.
3	QPC has not reported the results of a detailed assessment of market structure, market conduct or performance under current structures, those proposed by Wilmar, MSF Sugar and Tully post-2017 or under the contestable market environment envisaged in the provisions of the Real Choice in Marketing Bill.	Discussed in section 3.5 of the Decision RIS.	CANEGROWERS and ACFA, p. 11	Please see section 3.5 of the RIS for discussion.
4	In discussions with grower representatives, Wilmar Sugar executives have made it clear that they believe the cane payment formula skews the cane payment arrangements in favour of growers.	Noted. We have seen no evidence that there have been changes to the formula since deregulation that would disadvantage growers.	CANEGROWERS and ACFA, p. 12	No change to the RIS.
5	The decision taken to withdraw from QSL and takeover marketing of GEI sugar appears to be the first step in a wider strategy. With market power heavily favouring Wilmar and without recourse to a robust pre-contractual dispute resolution process, it will be difficult for growers to effectively counter such a development.	The choice in marketing lies with the owner of the raw sugar, the miller. There are measures in place to level the playing field in the negotiation of cane supply agreements between the miller and the grower including: <ul style="list-style-type: none"> growers permitted to collectively bargain the co-dependent relationship between millers and growers. 	CANEGROWERS and ACFA, p. 12	No change to the RIS.

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
6	<p>Some mill owners have invested in mill infrastructure since the changes in ownership have been directed at returning previously run down (heavily depreciated mill assets) to their full operational capacity. This investment has included the replacement of defunct equipment, updating of operating systems and in many cases much needed repairs and maintenance. The result has been to return mill reliability to accepted industry standards, restore mill recovery and avoid the longer season lengths that were caused by mill breakdowns and unplanned stoppages.</p> <p>While this restoration of previously run down mill assets is welcome, it has created a distorted perception of 'new investment'.</p> <p>Other mill owners have not made similar investments, instead electing to continue a regime of underinvestment in mill infrastructure and below standard operating performance.</p>	<p>Ultimately, the decision to invest (or not) in mill infrastructure is a commercial decision of the millers.</p> <p>The consultation RIS concluded that it appears the existing legislation supports investment in the sugar industry. We noted that millers have been investing in mill improvements, which increase the overall productivity within the sector.</p> <p>We also considered that if enacted, the Bill would interfere with the property rights of millers which would likely reduce the profitability of future mill investment and dampen longer term innovation and productivity (compared with existing legislation).</p>	CANEGROWERS and ACFA, p. 12	No change to the RIS.
7	<p>The QPC is indicating that the Grower Choice model would be detrimental to Miller investment in efficiency and mill improvements, with \$500m being spent Since deregulation in 2006 in this area. How are these numbers relevant to the proposal when most of this investment (maintenance or capital) was made while QSL managed the majority of the marketing activities. Furthermore the QPC have failed to understand that when foreign companies made commitments to invest in Australian Milling assets the majority of the sugar was being marketed by QSL, with the largest of these companies giving an undertaking to the FIRB that it would continue with the current market arrangements.</p>	<p>We note there has been an increase in mill investment since deregulation when the current regulatory framework was introduced, and that QSL was the marketer at the time.</p> <p>We consider that legislation that has the effect of interfering with property rights represents a significant sovereign risk, which would have the effect of dampening future investment.</p>	CANEGROWERS Herbert River, p. 1	No change to the RIS.
8	<p>Over the past two years, the foreign owners of MSF Sugar have invested around \$240m of new capital into the Australian operations. In addition to the corollary benefits to the Queensland and local economies, this investment has generated significant improvements in productivity</p>	Noted.	MSF Sugar, p. 2	No change to the RIS.
9	<p>There is no alternative land use. In a 2007 CSIRO Future Use of the Rocky Point Cane Landscapes Report, it was found that there are no viable agricultural alternatives to sugar cane. Under the South East Queensland Regional Plan, we are zoned agricultural with no other land uses available.</p>	<p>Noted.</p> <p>We acknowledge that Alternative uses will depend on the land, climate and economic factor of each region.</p>	Canegrowers Rocky Point, p. 4	No change to the RIS.
10	<p>Burdekin District Cane Growers Ltd noted that the RIS fails to investigate the cost of transporting sugar cane 100 km and provided some average cost data. Where sugar cane was transported 120 km from the Tableland to Mossman the cost of transporting by road was \$15 - \$18 per tonne. A grower is likely to receive \$36/tonne of cane (using a \$386/tonne IPS sugar gross). They note that a grower's costs of production are around \$32 - \$35/tonne of cane without additional</p>	<p>In most cases the mill pays for the transport costs but we understand there could be a renegotiation of the terms of the CSA with some of the transportations costs passed to growers.</p>	Burdekin District Cane Growers Ltd, p. 2	No change to the RIS

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
	transport cost. They conclude that the cost of transporting cane 100km are prohibitive and the RISs conclusions that there is extensive competition for 12 mills is incorrect. The vast majority of growers do not in fact have a choice of miller.	We have used the 100km benchmark as there is evidence of this occurring. Irrespective of the number of mills which do not have a competitive alternative, we consider that any potential abuse of market power is mitigated by the co-dependent relationship between growers and millers. We also consider the growers are statutorily authorised under the SIA to collectively negotiate with the mills – we consider this also mitigates the potential for the abuse of market power.		
11	Burdekin District Cane Growers conclude that without substantial investment there is limited opportunity for growers to grow an alternative crop. They consider that growers would need to develop an expert market for an alternate crop and there would need to be substantial infrastructure.	Noted. We acknowledge there are costs associated with moving to another crop, however this would need to be balanced against the possible gains. There are also complementary crops and break crops used in the sugarcane industry. These are unlikely to require significant investment. ²⁴³	Burdekin District Cane Growers Ltd, p. 2	No change to the RIS.
12	The decision to supply sugar to QSL is exclusively a mill decision. For example, growers supplying MSF Sugar’s Maryborough and Mulgrave mills can presently chose between MSF Sugar and QSL as the marketer of their GEI sugar. This choice has been effectively removed for the 2017 and future seasons. In practice, MSF Sugar has made the ability of its supplying growers to return to QSL unnecessarily complex, while easing the transitional arrangement for growers electing to switch from QSL to MSF Sugar. This is an example of a mill misusing its market power.	Noted. We note in section 3.4 of the Consultation RIS that the decision to supply sugar to QSL is exclusively a mill decision. We also note that growers in MSF Sugar’s Mulgrave and Maryborough regions have voted 91% in favour of MSF’s pricing model.	Canegrowers and ACFA, p. 12	No change to the RIS.
13	Burdekin District Cane Growers argue that collective bargaining is irrelevant and fails to redress the imbalance in bargaining power because of the level of farm debt in QLD and that sugar cane must be harvested each year otherwise it deteriorates. Growers have to supply sugar cane each year. They note that Wilmar Sugar can as easily refuse to consider commercial terms advocated by a bargaining representative, as it can an individual grower.	We consider a mill owner, similar to the grower, has a significant financial incentive to see cane harvested and milled. Evidence has not been provided demonstrating a mill has refused to enter into cane supply agreements that have been negotiated by a collective, or an individual grower.	Burdekin District Cane Growers Ltd, p. 3	No change to the RIS.

²⁴³ <https://www.daf.qld.gov.au/plants/field-crops-and-pastures/sugar/complementary-crops>

	Submission points	QPC Response	References	How RIS changed
2.2 Are there any other QSL issues we should take into consideration?				
14	<p>Storage –</p> <p>The RIS has not recognised or valued the important role QSL’s management of the State’s storage facilities play in Queensland’s raw sugar export marketing system.</p> <p><i>The Queensland sugar industry has storage assets that can store approximately 60% of the state’s total crop. Thus, with sufficient storage it is possible to move sugar sales between futures contracts and maximise revenue in terms of both the net premiums and the overall ICE 11 price able to be achieved. The amount of flexibility Queensland has with its storage is unmatched anywhere else in the world.</i></p> <p><i>Under QSL’s current operating system, the storage assets are managed in a pooling environment where this overall benefit can be shared by the entire industry. Unless a commercial agreement can be reached, the operation of the storage assets will not be on a pooled basis beyond the 2016 Season. Therefore some industry participants will not have access to the same amount of storage as they do under the current system. Subsequently, some will not have the same flexibility over the timing of sales and associated pricing on the ICE 11 that they have under the current system. This will result in a direct and negative impact on the return to impacted mill owners and their growers.</i></p>	<p>Noted and reflected in Section 2.3 of the Decision RIS.</p> <p>We consider that the future operation of the storage assets is a commercial decision for millers, QSL, STL and its industry shareholders to negotiate.</p>	QSL, p.3	QSL’s comments have been reflected in the RIS in section 2.3.
15	<p>Pricing Services –</p> <p>The RIS has incorrectly assumed that QSL will be able to continue to offer pricing services to all growers post-2017. This is not the case, nor is it true of the current arrangement...Cane growers are currently given the ability to choose a pool pricing product to match their risk profile, and have the ability to price sugar at their own discretion on QSL’s pricing book. Whether the range of current services will still be available to all growers beyond 2017 is not guaranteed. As a not-for-profit entity, QSL requires a contractual raw sugar supply commitment and the consequent title that this provides to be able to offer these services.</p>	Please see discussion at section 4.2.2 of the RIS.	QSL, p.4	RIS amended at section 4.2.2.
16	The assumption that QSL will be able to continue to offer pricing services to all growers post-2017 is not correct. This is not the case under current arrangements. Presently not all mills offer the full suite of QSL pricing options available to their growers. The range of QSL pricing options made available to growers is exclusively a mill decision.	See Section 4.2.2 of the RIS.	CANEGROWERS and ACFA, p. 12	RIS amended in section 4.2.2.
17	Under current arrangements and those proposed by Wilmar, MSF Sugar and Tully post-2017, growers do not have an ability to supply GEI sugar to QSL. The decision to supply sugar to QSL is exclusively a mill decision. For example, growers supplying MSF Sugar’s Maryborough and	It is our understanding that legal title transfers to the miller upon processing of the cane. We consider	CANEGROWERS and ACFA, p. 12	No change to the RIS.

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
	Mulgrave mills can presently chose between MSF Sugar and QSL as the marketer of their GEI sugar. This choice has been effectively removed for the 2017 and future seasons.	the marketing decision lies with the miller as owner of the raw sugar.		
18	Consistent with National Competition Policy, a contestable market created by the Real Choice in Marketing Bill will provide growers with an opportunity to make a wider range of choices for both the pricing and marketing of GEI sugar, including an ability to use the marketing and pricing services of QSL – a company that they own. In practice, MSF Sugar has made the ability of its supplying growers to return to QSL unnecessarily complex, while easing the transitional arrangement for growers electing to switch from QSL to MSF Sugar. This is an example of a mill misusing its market power.	See sections 3.5 and 6.1.2 of the Decision RIS.	CANEGROWERS and ACFA	No change to the RIS.
2.3 Are there any other miller issues we should take into consideration?				
19	ASMC believes that the QPC RIS has summarised the views of millers accurately in that the current regulatory environment of the sugar industry in Queensland is effective, that there are adequate protections under the Sugar Industry Act and that any disputes should be resolved through commercial negotiation rather than government intervention.	Noted.	ASMC, p. 2	No change to the RIS.
3.1 Have we appropriately described the policy objectives the Bill is seeking to achieve?				
20	QSL considers the policy object not expressly mentioned in the RIS is to increase competition for provision of raw sugar marketing services.	Noted. In our Decision RIS, we note there are now numerous marketers marketing raw sugar in addition to the incumbent (QSL).	QSL, p.4	Please see discussion in the RIS at section 3.5 noting there are new entrants providing marketing services.
21	In section 3.1 (a) related to the proposed pre contractual arbitration process the Consultation RIS states that This trigger would not be available to mill owners or other affected parties such as QSL. Wilmar note that the 'trigger' that is only available to growers is in relation to giving a notice requiring the mill owner to use reasonable endeavours to negotiate a supply agreement within a stated period.	Noted. The proposed new section 33A (3) (under clause 6 of the Bill) that states If the grower or mill owner refers a dispute about a proposed term of the intended supply contract to arbitration... The RIS has been clarified to reflect this point.	Wilmar, p. 4	The RIS has been amended.

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
	Wilmar goes on to note that under the proposed new section 33A (3) of the Act either a grower or a miller can refer a dispute about a proposed term of the intended supply contract to arbitration.			
22	CANEGROWERS and ACFA support the Real Choice in Marketing Bill because it delivers on the policy objective of establishing a regulatory structure that prevents the misuse of market power, addresses market failure and establishes a competitive market. This overarching policy objective is consistent with National Competition Policy and strengthens the policy objectives identified and used by QPC.	See section 3.5 and 6.1.2 of the Decision RIS.	CANEGROWERS and ACFA, p. 12	The RIS has been clarified.
3.2 Have we made the correct assumptions about the average net marketing premiums that are achieved by QSL competed the ICE No 11. Benchmark price?				
23	QSL believes that looking at net premiums compared to a benchmark ICE11 price gives the full picture of the importance of the marketing function....it risks seriously underestimating the price impact of a marketer's decisions. It is the role of the marketer to optimise the sales against the right futures contract to maximise the level of the ICE11 price able to be achieved. "The QSL system provides a mechanism where a certain amount of exposures against each futures contract for a season are fixed in a set ratio. This mechanism allows growers and millers to make choices with regard to ICE 11 risk for up to 65% of their anticipated production, without having to worry about the actual sales mix of futures contracts used. The remaining 35% is managed on behalf of all participants in a communal pool currently known as the QSL Harvest Pool. This pool's purpose is to manage changes in production up to a set limit and to optimize the mix of actual futures contracts to achieve the best ICE 11 price on behalf of all participants."	Noted.	QSL, p.4-5	Additional information is included in the RIS.
24	QPC appears to have overlooked the importance of the remaining 95 to 99 per cent of revenues and the essential interaction between the physical sales and futures market activities in price risk management and maximising the total value from raw sugar sales. The net premium is an arithmetic calculation netting more than \$250 million in revenue collections against approximately \$240 million of marketing costs each year. It masks the reality that there is a significant management task in optimising each of the components of the premium and minimising each of the elements of costs, as outlined in CANEGROWERS and ACFA submission made at the commencement of the QPC risk assessment.	Noted. We are aware of the importance of maximising marketing premiums and the role they play in maximising overall returns to the industry.	Canegrowers and ACFA, p. 3	Additional information included in section B.3 of the RIS.
25	On page 21 the Consultation RIS states that the globally traded ICE No. 11 contributes at least 95 per cent to the net sugar price, with Wilmar estimating it has been closer to 99 per cent over the last five years. Wilmar remarked that five year average data from QSL, from the 2009 to 2013	Noted.	Wilmar, p. 5	RIS amended (section 3.3) to note that this is

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
	seasons, shows the net marketing premium is approximately 1 per cent of the net sugar price. They note the QSL data is shown in figure 4 of the RIS			based on QSL data.
26	ASMC agrees with the assumptions made around net marketing premiums. The points being made through the use of the aggregate levels in the examples could be enhanced through the addition to the values described on a per-tonne-of-sugarcane basis.	Noted.	ASMC, p. 3	Additional information included in the RIS section 3.3.
27	The audit trail proposed by Wilmar Sugar and MSF Sugar does not overcome the issues associated with a lack of transparency, including the opportunity that large, multinational companies have to move profit from one entity to another in intercompany and related party transactions.	Noted. Page 32 of the RIS notes the Australian Tax Office's transfer pricing rules regarding related party international dealings. We also note the transparency measures being proposed by millers in their proposals appear to adequately address any concerns about related party transactions.	CANEGROWERS and ACFA, p. 12	Additional information on marketing and pricing included in section 3.3 of the RIS.
28	QPC in section 3.3 states the premiums comprise 8% of the net sugar price but then minimises the premiums importance by deducting the marketing costs, to conclude the net premiums are only 1% perhaps up to 5%. Premiums are not gained specifically to offset the costs of exporting raw sugar. Marketing costs exist independently and should be applied to the ICE 11 price. When the premiums are viewed in isolation the value is in excess of \$250 million per annum; not the \$21 million claimed in the (QPC) Consultation Regulatory Impact Statement (RIS). To subtract the costs from the premiums is nonsense. The costs exist whether with or without the premiums. It is false economics to produce document that draw any relationship between market premiums and costs (these can vary significantly from year to year).	It is acknowledged that many of the significant marketing costs such as storage, handling and freight costs will need to be paid irrespective of the value of any premium achieved. However the choice of marketer can influence both and ultimately both need to be included to derive the total returns to be shared between millers and growers.	Canegrowers Isis, p. 2	No change to the RIS.
29	It is almost certain that the costs will increase significantly under the marketing arrangements proposed by mills. There will be additional costs in keeping the sugar segregated, maintaining separate stockpiles, managing storage levels, higher freight costs due to using smaller ships, and generally higher costs due to loss of economies of scale, Costs could double and be passed on to growers. At the same time, the value of premiums to growers will be foregone because mills will not pursue them when dealing with related entities.	As noted in the Consultation RIS under the CSAs, returns to growers and millers are determined by the Cane Price Formula. As millers receive a share of the net premiums, millers have a strong incentive to maximise the net sugar price, including minimising marketing costs. We have assumed that millers who have made the decision to cease using QSL for the marketing of raw sugar have done so because they have made a	Canegrowers Isis, p. 2	No change to the RIS.

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
		commercial decision that an alternative marketing strategy is in their commercial interests to maximise returns from raw sugar production.		
30	<p>There is no evidence that all growers would continue to have an option to manage their sugar price exposure with the existing suite of pricing options currently available from both QSL and the miller marketer.</p> <p>The present flow of title from grower to miller to QSL enables the marketer to offer price risk management options to both growers and millers... to manage their ICE No.11 pricing independently of each other using pricing mechanisms and pools offered by QSL and the mills. The futures transactions associated with these mechanisms are settled in the context of physical sales using QSL's pricing platform. This hedge settlement mechanisms removes the need to cash settle futures market transactions and with it uses sugar as collateral for the transaction, minimising exposure of the marketer's balance sheet regarding these transactions and the financing advance payments for raw sugar and sugarcane.</p>	<p>We consider QSL does not need title in order to price sugar. Rather, they could become a third party pricing agent and continue to operate the pools – the physical execution would not lie with them, but with the holder of the product (most likely the miller).</p> <p>We note that QSL's decision about product offerings and corporate form is a commercial decision for QSL's Board and its shareholders.</p> <p>We also note the 2005 CIE Report considered that moving to a 'for profit' company may provide benefits for QSL and in the industry.²⁴⁴</p>	Canegrowers and ACFA, p. 3	The RIS has been amended to clarify our view.
31	QSL's pricing platform also enables growers, where they elect to use the QSL platform, to manage their futures price exposure on QSL's account rather than their own. This frees up capital throughout the industry for other activities.	Noted. We note that Wilmar also proposes to allow growers to manage their exposure on Wilmar's account. ²⁴⁵	Canegrowers and ACFA, p. 3	No change to the RIS.
3.3 Is it correct that CSAs for mills without competitive alternatives are the same or similar to CSAs with grower cooperatives? If not, what are the differences and are they advantageous or disadvantageous to growers?				
32	It is true that Cane Supply Agreements across Queensland contain broadly similar provisions. However it is not fair to assume, as QPC has, that these agreements offset the market power mills have over growers or the ability of mills to influence the net price of sugar including in the calculation of the cane price. A clear illustration of the misuse market power is the behaviour of WH Heck and Sons in the calculation of sugar price and in the deductions made to that price in the determination of a net sugar price to in the cane payment formula, a formula that is consistent with the formulae used in other mill areas.	<p>In our Consultation RIS we noted that we may be able to conclude that mills have abused their market power if there was evidence of a difference in contractual arrangements between private and cooperative mills.</p> <p>There may be issues in the Rocky Point region that require further investigation to ascertain whether there has been an abuse of market power. However, it should be noted that we do not believe</p>	CANEGROWERS and ACFA, p. 13	The RIS has been amended to note that an alternative mill must have capacity available.

²⁴⁴ CIE (2005). Unshackling Queensland Sugar - prepared for the Queensland Government.

²⁴⁵ Wilmar (2015). Supplementary Submission to Queensland Productivity Commission, page 2

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
		these issues are indicative of wider issues throughout the sugar industry in Queensland.		
33	Another illustration of growers' frustration at the mills misuse of market power is the decision taken by many of the growers formerly supplying MSF Sugar's Tableland Mill to supply cane to Mossman Mill, owned by Mackay Sugar. The growers' decision was made because MSF Sugar denied growers' a fundamental choice, the option of having their GEI sugar marketed and priced by QSL, not because of other provisions of the proposed cane supply agreement. This grower decision could only have been made because the Mossman Mill was operating well below capacity (a point that appears to have been overlooked in QPC's market assessment).	We note the comment regarding the Mossman mill and have amended the RIS to note that for growers to be able to move to an alternative mill, there must be spare capacity.	CANEGROWERS and ACFA, p. 13	The RIS has been amended to reflect the issue of spare capacity.
3.4 Is there information that miller marketers should be providing but are not?				
34	<p>QSL and CANEGROWERS/ACFA consider all companies providing marketing services to growers should have an obligation to publish specified information to those growers in relation to their marketing activities in order to explain to growers how those marketing choices are reflected in their returns. The information should include:</p> <ul style="list-style-type: none"> • Past marketing performance, including factors that provide material context for that performance, such as the volume marketed, marketing, pricing, hedging and other risk strategies adopted, sugar quality and seasonal factors • Details of the terms on which any trading with related or affiliated refineries occurs • A summary of marketing, pricing, and strategies to be utilised, including how the marketing of the relevant Australian raw sugar will form part of any wider international sugar trading activities conducted • Any administration fees, commissions, profit margins or other amounts to be charged by the mill owner in connection with marketing and/or pricing of Grower Economic Interest sugar. 	<p>Both Wilmar and MSF proposals appear to allow for sufficient information to be provided to growers on details of transactions, strategies and various fees. We note, however, Tully does not appear to have yet developed its marketing proposals for 2017 and beyond.</p> <p>With regards to past performance, we note MSF appears to have successfully marketed outside QSL for a number of years and continues to have grower support in the Mulgrave and Maryborough mill areas.</p>	QSL, p.7 CANEGROWERS and ACFA, p. 13	No change to the RIS.
35	The audit trail proposed by Wilmar Sugar and MSF Sugar does not overcome the issues associated with a lack of transparency, including the opportunity that large, multinational companies have to move profit from one entity to another in intercompany and related party transactions.	<p>The submission does not explain why the audit provisions proposed by MSF Sugar and Wilmar are not adequate to address concerns of transparency, therefore we cannot draw a conclusion on this issue.</p> <p>We consider an audit report to be a well-recognised approach for providing assurance.</p>	Canegrowers and ACFA, p. 13	No change to the RIS.

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
36	Growers supplying MSF Sugar's Mulgrave mill have observed that, although making several promises to growers, MSF Sugar has not yet provided grower representatives with unfettered access to its auditor or enabled formal grower input into determining the scope of the audit.	Noted. We note MSF Sugar's use of a grower pricing/reference panel. MSF Sugar noted in its submission that the panel has visibility and transparency of all the physical marketing activities undertaken, involving the activities being independently audited.	CANEGROWERS and ACFA, p. 14	No change to the RIS.
3.5 In terms of transparency, are there any aspects of the MSF's Pricing Model that are insufficient? If so, what aspects and why?				
37	No responses received			
3.6 In terms of transparency, are there any aspects of the Wilmar 2015 Proposal that are insufficient? If so, what aspects and why?				
38	Taking both QPC questions 3.5 and 3.6 together, it is a concern that grower pricing representatives supplying both Wilmar mills and MSF Sugar mills are considerably less skilled in matters of marketing and pricing than the experts in those areas employed by the respective companies. Growers' ability to challenge the market assessments or complex price and currency risk management techniques and tools is likely to be limited.	Based on the information available, there seems to be no strong evidence that millers are not, or will not, provide the info that growers need to make informed decisions on marketing risks, costs and premiums, which demonstrate the growers are indeed being paid net premiums in accordance with the CSAs.	CANEGROWERS and ACFA, p. 14	No change to the RIS.
39	The long term success of Wilmar and MSF Sugar's pricing models relies on competition. In the absence of a contestable environment there will be little discipline on the companies to contain their costs, innovate or otherwise improve their product and service offering.	Millers have a strong commercial imperative to minimise costs and maximise their performance in a globally competitive sugar market. We consider the market for marketing Queensland raw sugar is contestable. Of note, since deregulation, marketers of raw sugar in Queensland have increased from a sole provider (QSL), to include Wilmar, MSF and Tully.	CANEGROWERS and ACFA, p. 14	No change to the RIS.
40	Wilmar has also committed to ensure any related party transactions are on an arms-length basis. Under the terms of Wilmar's draft legal agreements, it is obliged to provide to a certifying auditor evidence to demonstrate all related party transactions are conducted on this arms-length basis, where they form any part of any cost, expense or revenue amount used in determining net pool prices. Similar information is also provided by Wilmar to the Grower Transparency Group.	Noted.	Wilmar, p. 6	No change to the RIS.
3.7 Is there any further information and evidence we could take into account that would suggest existing dispute resolution mechanisms are ineffective and are giving rise to market failure?				

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
41	<p>It is clear to everyone in industry that: 1. There is currently a dispute and impasse about the terms of which cane should be supplied in the 2017 Season and onwards, and 2. There has been no avenue to successfully resolve that impasse to date.</p> <p>Even if the QPC takes the view that the refusal to engage with grower choice is not evidence of a market failure (which in competition terms is a refusal to acquire cane unless growers acquire marketing services) it is clear that the existing dispute resolution mechanisms have failed industry. Any other conclusion simply ignores the reality of the current situation.</p>	<p>One of the main aims of dispute resolution mechanisms is to ensure that there are appropriate protections for growers and millers to prevent against the abuse of market power. Given our conclusion that there is no evidence of an abuse of market power in the sugar industry, it is not clear that pre-contract arbitration, which may lead to costs for the industry, adds additional benefits above the existing mediation arrangements.</p> <p>In instances where the impasse is caused by refusal of millers to allow growers choice of marketer we consider that the absence of choice for growers in marketing is not evidence of an abuse of market power.</p>	QSL, p.8	No change to the RIS.
42	<p>ASMC agrees there is no evidence of ineffectiveness. Cane Supply Agreements generally describe a stepped process for dispute resolution that involves mediation between the parties with scope to move to arbitration if the dispute can't be settled through the mediation process- generally the mediator will not be the arbitrator and all agreements have provision for an independent appointment of a suitable arbitrator. These provisions reflect best practice commercial arrangements.</p>	Noted.	ASMC, p. 4	No change to the RIS.
4.1 Have we correctly described the likely impacts on stakeholders under Option 1?				
43	<p>Premium assumptions - QSL does not agree with the use of Wilmar's pricing claims in a bid to justify the QPC's claim that "there is no evidence to suggest that net premiums would be any lower than QSL and could well be higher under a Wilmar marketing scenario". Past performance does not guarantee future performance.</p> <p>As recognised in the RIS, Wilmar and QSL's results are based on very different risk profiles. Wilmar's increased risk profile (which it can easily bear over a large volume of globally traded sugar) will create material risks and volatility of return for growers, an issue which appears to have been glossed over in the RIS.</p>	Noted. RIS amended to clarify QSL's view.	QSL, p.8	RIS amended to clarify.
44	<p>Other origin sales ability - QSL strongly refutes the claim that Other Origin benefits "are not available to growers in the current QSL system, because QSL does not trade any material quantity of other origin sugar". QSL has the same capability and tools available as Wilmar to</p>	Noted. RIS amended to note QSL's view that it has tools and capability, to achieve Other Origin trading results in the market.	QSL, p.8	RIS clarified.

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
	achieve Other Origin trading results in the market – only the appetite for risk and the transparency of their Other Origin sugar activities differs between the two entities.			
45	<p>Table 9 – Storage, handling and logistics – The assumption that QSL’s loss of marketing volumes may not necessarily result in a change to QSL providing storage, handling and logistic services is incorrect. The tonnage in QSL’s marketing system is directly linked to the threshold volume required to retain the STL sub-lease.</p> <p>“It should also be noted that as QSL is a not-for-profit operator, it can be assumed that any alternate STL operator would do so at a cost incorporating margins that would be passed on to growers and millers. Judging by the National Competition Council’s draft decision regarding shipping channel services at the Port of Newcastle, third-party access regimes will not provide appropriate protection against increases in price in the way the RIS seems to assume they would.”</p>	<p>Noted. However, we consider that ultimately, the management of storage, handling and logistics services is a matter for STL (which is jointly owned by growers, millers and QSL).</p> <p>We note QSL’s comment respecting alternate STL operators, however, we have not assumed a third party access regime would be implemented.</p>	QSL, p.8	The RIS has been amended to include QSL’s comment.
46	Table 9 – Pricing and risk management – The RIS fails to acknowledge that the majority of Queensland growers will not be able to access QSL’s pricing and price risk products, so there will be no competition in this space and as a result, the range and cost of products and price risk tools offered to growers may be affected.	<p>As set out in section 4.2.2 of the Decision RIS, we are not convinced that the management of pricing pools requires title of raw sugar, although it would change the nature of some of the services offered by QSL. We also note that ultimately the range and nature of product offerings must be a commercial decision for QSL.</p> <p>We also understand that there are other third party marketers that can provide these functions without the need for transfer of title.</p>	QSL, p.9	Please see discussion in section 4.2.2 of the RIS.
47	Table 7 – Option 1 – Fails to acknowledge that growers supplying Wilmar, Tully Sugar and MSF will no longer be able to access QSL for marketing services.	Noted. See section 4.2.2 of the Decision RIS.	QSL, p.9	No change to the RIS.
48	<p>Table 8 – Growers</p> <ul style="list-style-type: none"> The post-July 2017 scenario does not seem to take into account the major change that QSL will no longer have Raw Sugar Supply Agreements with certain millers, which means that growers from those millers will not have the ability to manage their price exposure via QSL It does not reflect the smaller range of competitive pool offerings if QSL is not an option for all growers 	Noted.	QSL, p.9	RIS amended to note QSL’s views.

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
	<ul style="list-style-type: none"> It does not reflect the scenario that the full range of pricing products to meet different risk profiles, as currently offered to growers by QSL and millers, will be offered at the discretion of the miller and may not be made available to all growers Production risk management as currently managed by QSL is not contemplated by the scenario 			
49	Table 8 – Millers - There is no certainty that QSL will be able to supply any services post-2018, as there are no further Raw Sugar Supply Agreements in place for any miller regions.	Noted. It will be up to the remaining individual millers to negotiate future RSSA's with QSL.	QSL, p.9	No change to the RIS.
50	Table 8 – QSL – The post July-2017 scenario does not correctly reflect that the services QSL can offer will only be for growers and millers in mill regions which have agreed to continue their Raw Sugar Supply Agreement.	Noted.	QSL, p.9	Section 4.2 of the RIS amended.
51	<p>The likely impacts put forward by QPC assume millers will act in a fair and equitable manner post-QSL. Based on the evidence provided in this submission, there is no guarantee that millers will act in a fair and equitable manner post-QSL.</p> <p>The evidence in Rocky Point clearly shows that additional legislation is necessary to ensure millers do not take advantage of their monopoly position.</p>	We note there appears to be issues which have arisen in commercial negotiations between growers and miller in the Rocky Point region that require further investigation. As QPC has not received any submissions from Rocky Point mill, it is unable to draw any conclusions on this issue. We do not believe these issues are indicative of wider issues throughout the sugar industry in Queensland.	Canegrowers Rocky Point, p. 5	No change to the RIS.
52	With the loss of sugar notified to QSL for 2017, QSL's viability will be under threat. Without QSL there would be no yardstick, and with no way to reintroduce the QSL baseline once gone, monopoly millers also become monopoly marketers.	<p>Based on the evidence presented, we have not been able to conclude that QSL will no longer exist post 2017.</p> <p>We also note in the absence of growers being offered the option of QSL as a price manager, we note that millers have proposed to continue to allow growers to price risk through forward contracts independently of the mill and participate in a range of pricing pools that suit their risk appetite. We consider this provides choice for a significant proportion of the price exposure growers are exposed to through the ICE 11 pool.</p>	Canegrowers Rocky Point, p. 7	Please see discussion in section 4.2 of the RIS

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
53	It is false to presume that any current CSA arrangements relating to marketing will continue to exist in the future under the mills' proposed changes without the passing of the... Bill.	We consider marketing of sugar is covered in agreements between millers and their marketers, not the CSA's.	Canegrowers Isis, p.1	No change to the RIS.
54	We believe our growers will be reluctant to invest given the mills' proposal to remove grower choice. The continued erosion of grower confidence, especially on top of the current low sugar prices, has fuelled greater competition for land as growers exit the industry.	Noted. We consider that grower investment will continue to reflect estimates about future returns to cane production, which is affected by the world sugar price and input costs.	Canegrowers Isis, p. 4	No change to the RIS.
55	Both MSF Sugar and Tully sugar separately cited the change in QSL's tonnage and market profile that would occur as a result of Wilmar's decision to withdraw from the QSL as a key reason for their decision to also give notice of their intention to withdraw from QSL from the end of the 2016 season. QSL's changing market profile will have consequences for all growers; both those who supply mills that are exiting QSL and those that supply mills remaining with QSL.	Noted. We consider this is discussed in Section 3.5 of the RIS.	Canegrowers and ACFA, p. 7	No change to the RIS.
56	<p>Wilmar has not provided any evidence to support its assertion that the premiums it achieves would be higher under its model than those premiums QSL is able to achieve. Wilmar's claims are based on a number of market assumptions. No account appears to have been taken of Wilmar's published result that show in FY2014 Wilmar's sugar milling business made a \$13.7 million loss and for the first half of 2015 Wilmar's global trading business has made a loss of \$105.5 million.</p> <p>A standard caveat made by many providers of financial services and advice is that past performance does not guarantee and may not be guide to future performance.</p>	Noted. We consider that all milling companies have a commercial incentive to maximise their overall performance.	Canegrowers and ACFA, pp. 14-15	No change to the RIS.
57	QPC has assumed that mills have made the decision to exit QSL solely on basis that their alternative marketing strategy will increase their net premiums and that with no change to cane payment structure the full impact will be passed on to growers leaving them no worse off. In this narrow assessment no account has been taken of the imbalance in market power between mills and growers, multinational mills' ability to manipulate the net sugar price included in the cane payment calculation and no account of the impact on the smaller GEI sugar marketing task following the withdrawal of Wilmar, MSF Sugar and Tully Sugar from QSL will have on QSL's ability to extract value.	<p>No evidence has been provided demonstrating that multinational mills' may manipulate the net sugar price include in the cane payment calculation.</p> <p>We note that the marketing decision lies with the owner of legal title of the raw sugar, the miller.</p>	Canegrowers and ACFA, pp. 14-15	No change to the RIS.
58	<p>Taken at face value Wilmar claims the lost opportunity cost of the Real Choice in Marketing Bill is \$46 million per year in premium value over the QSL return if they marketed all the sugar produced in their mills. Wilmar supports its assertion with three assumptions:</p> <ul style="list-style-type: none"> • Wilmar "assumes" an arbitrage benefit of 20pts. • Wilmar "assumes" a volume leverage benefit of 30pts. 	Noted. While we have noted Wilmar's estimates, we have not used the Wilmar estimates in our analysis.	Canegrowers and ACFA, pp. 14-15	No change to the RIS.

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
	<ul style="list-style-type: none"> Wilmar “assumes” a 50pt benefit arising from Wilmar’s superior marketing performance to QSL. <p>Wilmar provides no empirical evidence to support either its assertions or its assumptions.</p>			
59	<p>Wilmar claims that the benefits of trading other origin sugars “are not available to growers in the current QSL system, because QSL does not trade any material quantity of other origin sugar.” This Wilmar statement is factually incorrect. QSL has the same capability and tools available as Wilmar to achieve other origin trading results in the market. The key difference is the approach to risk taken by the two companies. QSL reports that in the 2015 financial year its other origin trading activities added \$4.9 million in value. Unlike the Wilmar model, 100 per cent of this value is paid to QSL’s supplying mills and shared with growers through the cane payment arrangements.</p>	<p>We have amended the RIS to note QLS’s views.</p>	<p>Canegrowers and ACFA, pp. 14-15</p>	<p>RIS has been amended to note QSL’s views.</p>
60	<p>In accepting Wilmar’s unsupported assertion that it will be able to create additional value by marketing additional volumes of sugar, QPC has “assumed” that the loss of volume will not necessarily result in a diminution in the value of QSL’s marketing activities. QPC has also “assumed” that QSL’s loss of marketing volumes will not necessarily result in a change to the costs of managing and operating the industry’s bulk raw sugar storage, handling and logistic services.</p> <p>Both MSF Sugar and Tully Sugar, cited the change in market profile and associated change in QSL’s risk profile that would follow Wilmar’s withdrawal from QSL as key reasons underpinning their own decisions to withdraw from QSL. The actions taken by these two companies suggest QPC’s assumptions about QSL’s post-2017 marketing ability are misplaced.</p> <p>QSL is a not-for-profit industry owned company that manages these industry owned facilities. If the loss of volume marketed by QSL caused STL to terminate the current bulk storage and handling operating arrangements, it appears likely that an alternative operator would include a profit margin in their pricing structure. This would be passed on to millers and growers, increasing the underlying cost structure compared with the current not-for-profit operating basis.</p>	<p>Noted. However we consider that ultimately the management of storage, handling and logistics services is a matter for STL.</p>	<p>Canegrowers and ACFA, pp. 14-15</p>	<p>No change to the RIS.</p>
61	<p>QPC assume that the majority of Queensland growers will be able to access QSL’s pricing and price risk management options. As noted, not all mills offer their growers the full range of QSL pricing options under current structures. Growers’ access to QSL’s price offerings is at the discretion of mills. In the absence of the necessary agreements between QSL and mills, QPC’s assumption this will occur post-2017 appears misplaced. Until the three mills who have indicated a desire to stay with QSL have signed new agreements to do so, QSL’s ability to operate post-2018 remains uncertain.</p>	<p>We consider that even in the absence of growers being offered the option of QSL as a price manager, we note that millers have proposed to continue to allow growers to price risk through forward contracts independently of the mill and participate in a range of pricing pools that suit their risk appetite. We consider this provides choice for a</p>	<p>Canegrowers and ACFA, pp. 14-15</p>	<p>Please see discussion at p. 4.2.2 of the RIS.</p>

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
		significant proportion of the price exposure growers are exposed to through the ICE 11 pool.		
62	Wilmar note that the Consultation RIS states that legal title to raw sugar is determined by the outcome of commercial negotiations (page 37) and add that this assumes that the miller's title to raw sugar is conferred by agreement with another party. Wilmar received legal advice from Minter Ellison: When raw sugar is first brought into existence in a sugar mill, the title to the sugar will, absent any agreement to the contrary, reside with the miller that produced it.	Noted.	Wilmar, p. 8	Please see discussion in section 3.4 of the RIS.
63	The Consultation RIS (page 40) cites the QSL submission to the Senate Select Committee on Rural and Regional Affairs and Transport (pages 10-11). The RIS notes that it was initially proposed that QSL should subcontract Wilmar to conduct all of its marketing operations. QSL says that having failed to convince other mill owners of that position, Wilmar has threatened on numerous occasions to provide a notice to terminate its RSSA. Wilmar note that QSL was amenable to such a concept and in 2012, voluntarily entered into an agreement with Wilmar to explore a phased transition to a marketing model whereby QSL would subcontract physical marketing and trading of all Queensland sugar to Wilmar.	Noted.	Wilmar, p. 9	No change to the RIS.
64	The Consultation RIS (page 41) notes that we consider that QSL provides a different value proposition in its approach to raw sugar marketing, in comparison to other raw sugar marketers such as Wilmar. QSL notes that growers value its approach as it can offer a more cautious approach to managing downside risks. Wilmar challenge this assertion noting that any suggestion growers would be forced to accept higher risk in their pricing management as a result of Wilmar's proposed marketing arrangements is incorrect. They note that under their draft legal agreements growers can use a third party pricing manager, such as QSL, to forward price and their proposed model offers growers pools with varying risk profiles.	Noted. RIS has been amended to clarify it is QSL's view that it provides a different value proposition.	Wilmar, p. 9	RIS amended in section 4.2.3.
4.2 Is there any further information and evidence we should consider as part of the base case of no additional legislation?				
65	No responses received.			
4.3 Are there any returns to growers under the QSL model that are not provided to growers under the millers' proposed marketing models?				
66	Yes. These include: <ul style="list-style-type: none"> As a not-for-profit entity, QSL is able to offer a wide range of pricing pools based on industry need, rather than solely commercial considerations. The variance in returns 	We consider that even in the absence of growers being offered the option of QSL as a price manager, we note that millers have proposed to continue to allow growers to price risk through forward	QSL, p.10	RIS amended to note that QSL currently receives profits from

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
	<p>against each of these pools can be significant. There is no guarantee that such a portfolio of pools will be available for growers to manage price risk in the future in the absence of the QSL model.</p> <ul style="list-style-type: none"> • 100% of QSL's other-origin trading profits are passed on to our Members, as are the profits from additional corporate activities, such as storage of other materials at the QSL-operated BSTs. This is not what is proposed by Wilmar. • As a result of our tax-exempt status, QSL is able to provide high-quality marketing, finance, pricing and logistics services for no fee or margin on a cost-recovery basis, representing significant savings for our Members. 	contracts independently of the mill and participate in a range of pricing pools that suit their risk appetite. We consider this provides choice for a significant proportion of the price exposure growers are exposed to through the ICE 11 pool.		additional corporate activities.
67	<p>The millers' proposed models do not provide growers with a contestable environment for the total price exposure. QPC assumes the world market price risk is managed within the fixed exposures offered to the various ICE No.11 raw sugar futures contracts. This simple assumption does not take account of the skill required to manage variations in the exposure risk arising from the interaction of changes in production estimates, changes in shipping patterns that reflect changing customer needs; those driven by changing market dynamics arising from competitor actions and the need to both optimise and operate within the industry's fixed raw sugar storage capacity.</p> <p>These interactions mean the variance in price from the future market price exposure alone can be very large... QSL's different pools offer different risk profiles for the management of this price volatility. The value captured by QSL managing the price risk arising from the uncertainty in production estimates, changes in shipping patterns and efforts to capture maximum value from raw sugar price spreads are included in QSL's Harvest Pool.</p> <p>As noted, QSL has the same capability and tools available as Wilmar to achieve other origin trading results – only the appetite for risk varies between the two entities. Wilmar provides no evidence to support its assertion that with larger volumes it would outperform QSL.</p> <p>As an industry owned not-for-profit company QSL acts in the interests of its grower and miller members, returning 100% of profits it makes in the payments it makes for the raw sugar it purchases in accordance with the terms of the raw sugar supply agreements it holds with each of its supplying mills.</p>	Noted. Please refer to our response to QSL comments above and our response to question 3.2.	CANEGROWERS and ACFA, p.16	Additional information included in section 3.3 of the RIS.
4.4 Have we correctly described the likely impacts on stakeholders under Option 2?				
68	Reject the notion that miller investment will suffer under option 2, but in the absence of same grower investment is likely to reduce.	Noted. We consider that the sovereign risk (ie. interference with property rights) associated with passage of the Bill to be significant.	Canegrowers Rocky Point, p. 7	

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
69	<p>Tablelands notes that the QPC conclusion that the benefits of additional regulation do not outweigh the costs contradicts the National Competition Policy, which advocates competition to provide the incentives to lift productivity, reduce costs and improve performance.</p> <p>They also note that grower choice in marketing will force all marketing players to offer a contestable, strong product (page 2).</p> <p>The contestable market envisaged in the Real Choice in Marketing Bill will provide the competitive discipline of market forces to ensure competitive offerings are made to growers, including incentives to reduce the cost of the services and incentives to encourage innovation in those offerings (Tablelands submission page 2).</p>	See section 3.5 and 6.1.2 of the RIS.	Tableland CANEGROWERS Ltd., p. 1	Please see discussion in the RIS, sections 3.5 and 6.1.2.
70	Mills claim deregulation has increased investment and innovation. Future grower investment in farms can only be guaranteed by maintaining grower choice in how the raw sugar price is determined and by providing certainty in how grower returns are calculated in the future.	Noted.	Canegrowers Isis, p. 1	No changes to the RIS.
71	CANEGROWERS Isis disputes completely the premise that grower choice could reduce returns to the industry by adding extra costs. CANEGROWERS Isis advances that the benefits of competition from two or more marketers will always outweigh the costs by capturing the freight differentials and other physical and quality premiums not identifiable under the millers' proposal.	See section 3.5 of the RIS.	Canegrowers Isis, p. 4	Please see discussion at section 3.5 of the RIS.
72	The QPC has correctly identified a number of risks with the proposed Bill, including the potential for reduced overall returns to the sugar industry through added costs.	Noted.	ASMC, p. 1	No change to the RIS.
73	A number of provisions in the Bill if enacted would be unworkable and would entrench such instability into the industry supply chain that could quickly lead to the demise of the industry	Noted.	ASMC, p. 2	No change to the RIS.
74	The Bill... establishes a contestable market for pricing and marketing services. It does not preclude mills from offering competitive services and offers. It also allows growers to select the offering put forward by the mill, where that offering is backed by a record of strong performance, when choosing who they will select to market their GEI sugar.	See section 3.5 of the RIS.	Canegrowers and ACFA, p. 8	Please see discussion at section 3.5 of the RIS.
75	<p>What about the interference with the property rights of QSL? Wilmar does have the title of the sugar but it is only for a blink of time in the process. Wilmar does have the title for about 24 hours before it is delivered to the bulk sugar terminal when title is transferred to QSL.</p> <p>We struggle to see how Wilmar can feel aggrieved and how they can feel their manufactured sugar has been stolen or expropriated.</p>	See sections 3.4 and 3.5 of the RIS.	CANEGROWERS Burdekin Ltd, p. 5	Please see discussion at sections 3.4 and 3.5 of the RIS.

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
76	QPC have not correctly described the likely impacts on stakeholders under Option 2. QPC assumes the Real Choice in Marketing Bill will constrain competition in the provision of marketing services and that the introduction of a mechanism to resolve deadlocks in commercial negotiations between growers and mills will add more costs than benefits. These assumptions are not an accurate reflection of either the intent of the Bill or of the Commercial Arbitration Act 2013.	Under option 2 in the Consultation RIS, we noted: <ul style="list-style-type: none"> that based on the information we have reviewed it is likely that future CSAs will still provide millers with legal title to the sugar cane. Assuming that, the Bill, if enacted, will have the effect of removing one of the legal rights attached to property the Bill would have the effect of allowing the following anti-competitive activities: third-line forcing, cartel conduct and has the effect of substantially lessening competition the Bill will introduce sovereign risk for millers. 	Canegrowers and ACFA, p. 17	No change to the RIS.
77	Wilmar believes it can demonstrate that the Bill will contravene SAFTA because it can be argued that the Bill would result in an indirect expropriation of Wilmar's property (raw sugar).	Noted. We have considered the Wilmar legal advice, but have not amended the conclusion in the Decision RIS.	Wilmar, p. 9	No change to the RIS.
78	Legal advice Wilmar has received concludes that the miller owns the sugar because they created it in the absence of any legal agreement between the miller and the growers to the contrary, ownership of the raw sugar resides with the miller who produces it.	Legal issues around ownership of raw sugar are considered in section 3.4 of the Decision RIS.	Wilmar, p. 2	No change to the RIS.
4.5 Is there any further information and evidence we should consider as part of our impact assessment of Option 2?				
79	No responses received.			
4.6 Have we correctly described the likely impacts on stakeholders under Option 3?				
80	Any code of conduct would need to be mandatory.	Noted.	Canegrowers Rocky Point, p. 7	No change to the RIS.
81	Endorses the QPC's observation that the option of a code of conduct... could have similar economic impacts for the sugar industry to those arising from the proposed Bill.	Noted.	ASMC, p. 1	No change to the RIS.
4.7 Is there any further information and evidence we should consider as part of our impact assessment of Option 3?				
82	No responses received.			

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
4.8 Have we correctly described the likely impacts on stakeholders under Option 4?				
83	“Toll Crush” could be connected to the value of cane in a similar method to that which already exists to protect the investment by a Mill. Our view is that it would be virtually the same as GEI.	Option 4 of the Decision RIS describes a toll crushing arrangement. We do not consider this to be the same as the concept of GEI, because under a toll crushing arrangement growers would pay a negotiated price for crushing and then take all price and marketing risk.	Canegrowers Rocky Point, p. 7	No change to the RIS.
84	Burdekin District Cane Growers note that It is extremely clear that millers will not negotiate a toll crushing arrangement. They argue that millers are unwilling to consider any other commercial arrangement (including toll crushing) and that this is a fundamental purpose of the Bill.	We are not aware that there have been failed commercial negotiations on a toll crushing arrangement.	Burdekin District Cane Growers Ltd, p. 3	Please see discussion at section 3.5 of the RIS.
4.9 Is there any further information and evidence we should consider as part of our impact assessment of Option 4?				
85	No responses received.			
Preferred options				
86	QPC risks making the growing sector and their assets unviable by leaving them vulnerable to the monopoly power of the mills. It is illogical to even contemplate the suggestion that if the QPC got it wrong that it could be fixed up with a review. Passage of the Bill is the only way to protect grower interests.	Noted.	Canegrowers Isis, p. 4	No change to the RIS.
87	ASMC and its members agree with the conclusions of the QPC’s Consultation RIS that there is no evidence to support a case for market failure in the Queensland sugar industry, and that benefits of additional regulation do not outweigh the costs.	Noted.	ASMC, p. 1	No change to the RIS.
88	The sugar industry needs to work through the current discussion regarding marketing arrangements without the continued adverse impact that political interference is bringing to confirming the future marketing arrangements.	Noted.	ASMC, p. 2	No change to the RIS.
89	The assessment is not consistent with the findings of two broad ranging and comprehensive federal reviews of the Australian industry’s sugar industry marketing system is at odds with the underlying premise of the National Competition Policy that competition in a properly functioning market will provide the discipline on businesses to continually strive to improve their performance, lift productivity growth and lower costs.	Discussed in sections 3.5 and 6.1.2 of the Decision RIS.	Canegrowers and ACFA, p. 1	Please see discussion in sections 3.5 and 6.1.2 of the RIS

	<i>Submission points</i>	<i>QPC Response</i>	<i>References</i>	<i>How RIS changed</i>
	The QPC seems to proffer a view that growers would be better off under a less competitive and more prescriptive, mill discretionary environment.			
90	The Bill... is designed to increase competition in the marketing and pricing of sugar. It does not as the QPC suggests reduce competition. This pro-competitive approach to remedying a market imbalance is consistent with National Competition Policy and provisions that authorise the introduction of additional competition in this space are likely to be accepted by the Federal Government.	Discussed in section 6.1.2 of the Decision RIS.	Canegrowers and ACFA, p. 9	Please see discussion at section 6.1.2 of the RIS

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