



**CALTEX**

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Caltex Australia

## **Caltex submission on the *Stronger Shipping for a Stronger Economy* reform agenda**

**5 March 2012**

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## Submission by Caltex Australia Limited

5 March 2012

Caltex welcomes the opportunity to further contribute to the development of legislation concerning coastal trading arrangements in Australia.

This submission provides comment on the following exposure drafts released on 20 February 2012 by the Department of Infrastructure and Transport (the Department), including the:

- Coastal Trading (Revitalising Australian Shipping) Bill 2012 (the Coastal Trading Bill);
- Coastal Trading (Consequential Amendments and Transitional Provisions) Bill 2012 (the Consequential Bill);
- Shipping Reform (Tax Incentives) Bill 2012 (the Tax Incentives Bill); and the
- Tax Laws Amendment (Shipping Reform) Bill 2012 (the Tax Amendment Bill).

### 1. Introduction

Caltex is a refiner and marketer of petroleum products in Australia, with operations in all states and territories. Caltex currently supplies over one third of wholesale transport fuels (petrol, diesel and jet fuel) supplied nationally and also accounts for almost a third of Australia's oil refining capacity. It owns and operates two of Australia's seven operating oil refineries, Kurnell in Sydney and Lytton in Brisbane.

Caltex has not been a ship operator since 1997 and, subsequently, internationally charters vessels from the spot tanker market and generally by time charter for coastal cargo movements. Currently, Caltex time charters (leases) two Australian manned petroleum product ships, the Alexander Spirit and the Hugli Spirit. The majority of the coastal shipping Caltex is engaged in is primarily for distribution of petroleum products from our refineries to terminals along the Australian east coast.

Caltex spot charters foreign flagged Aframax and Suezmax crude oil tankers to transport domestic and international crude oil. Currently, there are no Australian flagged crude oil vessels to conduct such voyages.

As outlined in Table 1, Caltex completed 145 voyages in 2011 and shipped 1,800,579mt utilising our two permanent time charter vessels. The number of cargoes would be far in excess of the number of voyages as we load multiple products on each voyage. In 2011, Caltex required a total of 17 crude oil voyages on the Australian coast, as outlined in Table 2.

**Table 1: Total number of petroleum product voyages (2011)**

Destination	Voyages by Hugli Spirit	Voyages by Alexander Spirit	Total voyages
Cairns	15	4	19
Townsville	14	3	17
Mackay	19	3	22
Gladstone	13	3	16
Hobart	1	17	18
Devonport	1	17	18
Inter refinery transfers	10	24	34
Exports - Melbourne	n/a	1	1
<b>Total voyages</b>	<b>73</b>	<b>72</b>	<b>145</b>
<b>Total volume shipped (tonnes)</b>	<b>969,812</b>	<b>830,767</b>	<b>1,800,579</b>

**Table 2: Total number of crude oil voyages (2011)**

<b>Origin</b>	<b>Destination</b>	<b>Total voyages</b>
<b>Hastings</b>	Botany Bay	14
<b>Dampier</b>	Brisbane and Botany Bay	1
<b>Varanus</b>	Botany Bay	1
<b>Varanus</b>	Brisbane	1
<b>Total voyages</b>		17

Caltex's primary objectives are to maintain reliable supply of crude for its two refineries as well as the reliable supply of products for its terminals to meet the demand for fuel in Australia. Crucial to meeting these objectives is having the flexibility to make appropriate adjustments and changes to product movements to minimise any potential disruption to the Australian fuel market.

## **2. Coastal Trading Bills**

### **2.1 Splitting of trade types**

Caltex recognises the objectives of the shipping reform package are to promote and revitalise the Australian shipping industry. However, the legislation as it stands is restrictive and unmanageable in the often unpredictable environment Australian oil refiners operate in. It is essential to take into consideration the commercial realities of industries, like oil refining, which rely on shipping for their supply and distribution operations.

For Caltex, if these reforms do not consider the impact on the normal operating practices of Australian oil refiners then they have the real potential of contributing to fuel supply disruptions throughout Australia.

The proposed licensing regime encompasses many varied business activities and the proposed bills have failed to take into consideration the different operating environment of each industry. This has resulted in proposed regulations being restrictive and the regulations must be tailored to recognise the unique elements of the different trades.

***Recommendation 1: That the proposed legislation separates shipping trade into three distinct segments: break bulk and general cargo; bulk commodities; and containerised trade, and the temporary licence requirements be tailored to each shipping trade to facilitate, not restrict, their voyage requirements.***

### **2.2 Temporary exclusion of crude oil trade**

Caltex employs spot chartered, foreign flagged Aframax and Suezmax crude oil tankers to transport domestic and international crude oil. There are currently no Australian licensed crude oil Aframax and Suezmax vessels to conduct such voyages and the Department's Regulatory Impact Statement, dated August 2011, states that:

*"The prospect of an Australian registered crude oil carrier on the coast is therefore considered small."*

The requirement to apply for a temporary licence (TL) for a foreign flagged ship when it is well known that there is no local alternative is unproductive for the applicant as well as the Department.

In this circumstance, it would be appropriate for the Minister to exclude crude oil vessels and/or cargoes from requiring TLs under Section 11 of the Coastal Trading Bill until such vessels exist. If this exclusion occurs, Caltex proposes that the voyage notification and reporting requirements for each cargo would still apply to ensure that the objectives of the reforms (ie to increase transparency) are still being achieved.

***Recommendation 2: That the proposed Coastal Trading (Revitalising Australian Shipping) Bill 2012 exclude the need for temporary licences for inter-state crude oil movements under Section 11 until such time that a licensed vessel (Aframax) is brought onto the coast.***

### **2.3 Transition period**

Caltex is still concerned about the uncertainty being created by the transition between the current single vessel permit (SVP) regime and the proposed TL regime due to commence on 1 July 2012. The proposed transitional procedures do not offer sufficient flexibility for our business to continue operations and minimise potential supply disruptions where urgent voyages may be required.

Under the proposed regulations, only one TL application may be made in a 12 month period. If Caltex requires a TL voyage to take place in July 2012, the earliest Caltex can apply for a TL is Monday 2 July 2012 (ie the first business day following the Coastal Trading Bill's enactment).

The proposed legislation outlines that it may take up to 15 business days for the Minister to approve the application, and this is at a minimum. If the 15 business day period is fully utilised by the Minister, an applicant will not know the outcome until 23 July 2012.

However, the outcome of an application may be extended beyond this date if the Minister requests further information to inform their decision and/or a general licence (GL) holder gives notice in response. If either occurs, the 15 business day approval period only begins from the day Caltex provides the additional requested information and/or the Minister is notified of the outcome of negotiations. This creates unnecessary uncertainty with respect to July voyages.

Caltex is aware that SVP applications will be accepted up until 30 June 2012 and has been advised that the current three to four day turn-around for the assessing of SVP applications will increase to 10 days. Caltex has been advised that this is in preparation for the substantial increase in SVP applications, and workload, expected in the lead up to the 30 June closing date. However, this has the potential to leave companies without licences between 30 June 2012 and 23 July 2012 (assuming an application is approved in 15 business days).

To minimise uncertainty and ensure a seamless transition, the government must provide a grace period for companies to adjust and transition to the new arrangements without impacting their commercial trade.

Caltex does not believe that extending the processing time of SVPs to 10 business days is appropriate and suggests the government consider directing additional resources to the processing of SVPs to maintain the current turn-around times and avoid potential disruptions.

Another solution may be for the government to accept SVP applications beyond 30 June 2012, however these permits would only remain valid until their specified expiry date or 31 October 2012 (whichever occurs first). This would coincide with the proposed Consequential Bill, which states that permits issued under the old law and licences granted under the coasting trade regulations will the day that is four months after the new law commences or the day the permit would have expired (whichever occurs first). This would allow both businesses and the Department to adjust to the transition whilst also providing businesses with more certainty around required voyages.

***Recommendation 3: That applications for single vessel permits may be submitted and approved beyond 30 June 2012. These permits would only remain valid up until their specified expiry date or 31 October 2012 (whichever occurs first).***

### **2.4 Shipper may also be applicant**

With respect to Section 28(1) of the Coastal Trading Bill, Caltex proposes that a shipper of the cargo should also be able to apply for a TL. In the first exposure draft, a shipper or shipping

agent could apply, however the second exposure draft now states that only the owner, charterer, master or agent of the vessel can apply.

A shipper is defined as “a person or firm who enters into a contract with a shipowner for the transportation of cargo or passengers for a stipulated period of time, ie a shipowner’s customer”. A charterer is “a person who puts his cargo on a carrier and is responsible for the payment of the transportation service rendered.”

Caltex proposes that a shipper be reinserted into the proposed legislation because depending on the chartering arrangements, Caltex may be either the charterer or the shipper of a voyage. When Caltex uses the spot market, we do not know whether we will be the charterer or shipper of a vessel until we have actually contracted a vessel.

Caltex usually contracts a vessel two to three weeks prior to a voyage and so at the time of submitting a TL application, we will not know the number of cargoes where we will be the charterer or the shipper. This means we risk breaking the law if we apply for a cargo where we end up being the shipper.

The authorised parties (ie owner, master, and agents) have never been involved in Caltex’s SVP applications under the existing regime. They would not be able to apply for a TL application under the proposed regulations because Caltex uses spot vessels, which means there is a different vessel, owner, master and possibly a different agent for each cargo. Therefore, it is not possible for these parties to apply for a 12 month TL, which requires a minimum of 10 voyages.

***Recommendation 4: That a shipper may also apply for temporary licences, in addition to the owner, charterer, master or agent of the vessel.***

## **2.5 Duration of general licence**

As outlined, Caltex currently time charters two Australian manned product ships, the Alexander Spirit and the Hugli Spirit, to undertake coastal trade. These two vessels undertake the majority of Caltex’s coastal movements of petroleum products, which are part of Caltex’s planned supply chain.

It is understood that these vessels will be eligible for a GL for a period of five years under the proposed Consequential Bill.

Caltex requests that the GLs extended to these vessels be commensurate with the remaining term of the time charter agreements that Caltex has entered into. For one of these vessels this period extends beyond the proposed five year period.

***Recommendation 5: That the period a transitional general licence is valid under the proposed Coastal Trading (Consequential Amendments and Transitional Provisions) Bill 2012 is equal to the greater of five years or the length of the commercial agreement between two parties (ie shipowner and shipper/charterer).***

## **2.6 Notification of vessel availability**

One of the objectives of the coastal trading reforms is to improve transparency and increase the availability of information within the Australian shipping industry. The coastal trading legislation as it stands places a majority of the onus on TL applicants to provide information regarding their voyage requirements. However, the same requirement is not extended to GL holders. As a result, the legislation will result in asymmetrical information in the marketplace, whereby GL holders have access to more information than TL applicants and/or holders.

The proposed legislation seems to place more emphasis on GL holders contesting TL applications rather than promoting direct discussion/negotiation between the parties on an ongoing basis. This can cause conflict between the parties and may result in financial loss for the TL applicant in some cases.

Section 28(2) of the proposed Coastal Trading Bill states that the Department will publish on its website approved TL applicants' voyage requirements for a 12 month period, including the number of voyages; the dates of voyages; the name and International Maritime Organisation identification number; the volume of cargo the vessel is capable of carrying; kinds and volume of cargo expected to be carried; and the ports where cargo is expected to be taken on board and expected to disembark.

However, Section 17(2) of the same Bill states that the Department will publish on its website with respect to approved GL holders: the relevant general licence number; the holder of the licence; the holder's business name and address; the vessel to which the licence relates; and the period of the licence.

To overcome the asymmetry of information, the Department should ensure that once a GL application has been approved, information pertaining to the volume of cargo the GL holder's vessel(s) is capable of carrying is also available on the website. GL holders should also be required to make publicly available the dates they are available to undertake voyages and from which ports. The Department should provide a mechanism for this information to be made publicly available to facilitate trade within the Australian shipping industry.

Making this information about GL holders available will also reduce the time taken for information sharing during any future negotiations following a notice in response, which must take place within two business days. As a consequence of not providing up-to-date information with respect to vessel capacity, dates and ports, the GL holder should be excluded from giving notice in response to a TL application and variation. This will encourage GL holders to participate in the information sharing process.

TL applicants may be forced into a commercially sensitive situation if a GL holder gives notice in response to an application. For example, specific voyage and vessel details are required in applications and to meet these requirements a TL applicant may have already entered into a contractual arrangement for a voyage using an approved and vetted foreign flagged vessel.

If one or more GL holders provide notice in response, the TL applicant is required to negotiate with each holder of a GL. These negotiations must take place and be completed within two days after the TL applicant receives a copy of each notice. While these negotiations take place, there is the prospect that the foreign flagged vessel may be contracted to undertake alternate voyages by other parties. This increases the commercial risk for TL applicants and, as a result, the proposed Bill will potentially force adverse commercial outcomes on TL applicants.

In addition, if an applicant has negotiated with a holder of a GL in accordance with the process in Section 32 in relation to a particular voyage, the GL holder may not give a notice in response. This would encourage applicants to negotiate well in advance with GL holders but if unsuccessful could not delay a subsequent granting of a TL.

The availability of information with respect to GL holders will increase transparency within the industry for all parties. It will also allow TL holders and applicants to be aware of current vessel capacities and availability to determine if their needs can be met locally. This will limit administrative burden, increase transparency, improve timeliness of information, and help to minimise uncertainty for businesses.

***Recommendation 6a: That general licence holders be required to make publicly available their vessel names, capacities and availability with respect to dates and ports in order to be eligible to give a notice in response.***

***Recommendation 6b: If an applicant has negotiated with a holder of a general licence in accordance with the process in Section 32 of the Coastal Trading (Revitalising Australian Shipping) Bill 2012 in relation to a particular voyage, the GL holder may not give a notice in response.***

## 2.7 Updating of temporary licence details

In addition to time charters, Caltex undertakes coastal trade by utilising the services of foreign vessels on an ad hoc basis as requirements arise. These events are mostly unplanned and occur in response to changes in the company's operations or external factors, such as power cuts and extreme weather events.

Part of optimising our supply chain and having an efficient operation requires the daily balancing of supply and demand across our refineries and terminals. This balancing occurs throughout the supply chain and includes movement of crude oil imports, intermediary products, and finished transport fuels.

The supply balancing occurs on a daily basis as a result of changes in manufacturing outputs, varying yields from different feed stocks, production units coming online or going offline, market demand variances and changes to shipping timetables.

Given the variable and unpredictable nature of our operations, 'unplanned' movements will always occur and are a business reality for Caltex. In some cases these requirements are urgent and timely movement of product can be critical to the continued operation of the refineries and maintaining continuity of supply to the market.

As Australia is a net importer of transport fuels, Caltex always has a number of imports on the water and a variety of foreign vessels calling at terminals and refineries at any one time. These vessels therefore often present the most timely and cost effective way to manage unplanned and unforeseen coastal movements.

Given the variable nature of our operation it is not possible for Caltex to nominate the proposed coastal trade for the coming 12 months which will be undertaken by foreign vessels because this is not known nor planned more than three months in advance.

For the same reasons, Caltex is not in a position to provide the information required under Section 28(2) of the Coastal Trading Bill to apply for a TL. What can be provided is an estimate of the coastal trade movements under a TL system based on historic data and provide in a TL application the Department with the following indicative information:

- cargo type;
- type of vessels required;
- estimated number of cargoes by type; and
- ports of operation (but not specific load and discharge ports).

Caltex proposes that this information be updated and submitted to the Department on a monthly basis as the specific details become known.

Furthermore, it is then proposed that the specifics of each voyage will be made available at the time Caltex 'goes to market' for a vessel to ship the product. These details would include

- load port;
- discharge port;
- three to five day loading date range (laycan);
- cargo type;
- vessel type required; and
- quantity.

This information would only be made available to registered Australian ship owners and it is envisaged that these updates would be conducted by way of 'updating' the original temporary licence under the relevant section.

If a movement is required that does not comply with the originally approved TL (eg different ports or cargo types) then a variation to the licence, as specified in the legislation, would be required. However, it is proposed that any variations are decided within three business days.

Caltex undertakes crude and product movements any day of the week, irrespective of business days. To minimise potential disruptions to planned voyages, the seven business days provided to the Minister to decide upon a variation should be reduced.

***Recommendation 7a: That the application process for a temporary licence, outlined in Section 28 of the Coastal Trading (Revitalising Australian Shipping) Bill 2012, be revised to increase flexibility and provide for 'unplanned' shipping movements that occur in Australian shipping.***

***Recommendation 7b: That the required information for a temporary licence application may be indicative, with the ability to provide monthly updates once specific details become known.***

***Recommendation 7c: That when specific details pertaining to voyages are known and the temporary licence holder enters the market to contract a vessel, that these details are also updated on the licence and are only made available to registered Australian shipowners.***

***Recommendation 7d: That a variation would be required when a coastal trading movement is not covered by the original TL. These variations should be decided within three business days.***

## **2.8 Minimum of 10 voyages is impractical**

Additionally, Section 28(2) states that there is a minimum of 10 voyages per licence, which is not practical or reasonable. Caltex currently undertakes more than 10 voyages in a calendar year because of our purchases of Australian crude oil.

However, if in future Caltex purchased less local crude oil there could be less than 10 voyage requirements in a calendar year. In this case, Caltex would not be able to apply for a TL even though there were no GL vessels available to carry crude oil. For example, Caltex undertook three SVP product ship voyages in 2010 and two in 2011. These voyages were critical to maintaining supply availability or refinery production. In addition, there were 38 coastal movements of crude oil in 2010 and 17 in 2011.

If this requirement remains in place, then Caltex will consider not purchasing Australian crude oil in the future. Already, Caltex chose not to bid for the last term Cooper Basin Crude contract on the basis of uncertainty around the proposed shipping reforms.

Two of the main Australian crudes that require coastal movements are Cooper Basin crude and Gippsland crude. Both of these crudes are consumed entirely within Australia and because of this there are limited buyers for these crudes. These crudes have high value to domestic refineries due to favourable freight economics and good quality. They are less valuable to overseas refineries due to unfavourable freight economics and are rarely exported. If Caltex did not buy these crudes, their value would be eroded due to the need to find export markets, which could lead to less revenue for Australian crude oil producers and reduced tax receipts for the government.

While it may not be the intent of the proposed regulation, it appears through its design that for a TL holder to make a variation to their licence, the variation must also be for a minimum of 10 voyages. If so, this is an impractical requirement. For example, if a charterer is nearing the end of their 12 month TL, they could more than likely have less than 10 approved voyages remaining on their licence. In such a circumstance, the TL holder would be unable to vary their licence, placing them in an untenable situation.

***Recommendation 8: That the requirement for a minimum of 10 voyages per temporary licence application, and variation, be removed from Section 28(2)(a) of the Coastal Trading (Revitalising Australian Shipping) Bill 2012.***



## 2.9 Urgent temporary licences

As outlined, Caltex operates two refineries as well as numerous sea board fuel terminals around Australia. A fundamental part of our operation is the use of import vessels on an ad-hoc basis to move intermediary or finished products between refineries and terminals. These decisions are often made with a few days notice as our operational groups respond to variations in the supply chain. The product type, parcel size, or date of the required movement, are generally not known in advance due to the large number of variables in the supply chain.

Due to this operating environment, Caltex has identified need for the proposed Coastal Trading Bill to include the provision of urgent TLs. These licences would be used in times when unusual, unplanned and unforeseen events have caused a disruption to the regular pattern of business and an urgent requirement has presented to move products on the Australian coast. All relevant information required for approval under a normal TL will be provided but the approval period for an urgent TL must be a maximum of two business days.

An application for an urgent TL would need to provide the information criteria specified in Section 28(2) of the proposed legislation, however there would be no provision for a GL holder to give notice. If the proposal for an urgent TL is accepted, the legislation would need to include criteria with respect to what circumstances constitute the need for an urgent TL.

To demonstrate the necessity for urgent TLs, Caltex has included the following case studies and real life scenarios to clearly demonstrate the often unpredictable operating environment of the Australian oil refining industry.

### **Case Study 1 – The Savannah:**

Caltex purchases and imports fuel oil from Singapore for sale in the domestic marine market. An import was planned using the Savannah, a foreign vessel, to import fuel oil into Brisbane and Sydney. To complete the cargo a parcel of LSWR (intermediary feedstock) was purchased for Sydney.

The Savannah loaded from 31 January to 2 February 2012. The vessel then steamed for Australia, with the estimated time of arrival in Brisbane as 21 February.

On 11 February, Lytton Refinery had an unplanned shutdown. Over the following days a number of units could be restarted, but the restart of the Fluidised Catalytic Cracker Unit (FCCU) was delayed while a number of operational issues were dealt with.

Despite the FCCU not being operational, the feedstock for the FCCU accumulates while the other refinery units are online and functioning. On Friday 17 February, it was identified that we would need to “export” FCCU feed from Lytton if we wanted to keep the refinery online and producing diesel and jet fuel.

The Savannah was identified as an appropriate and capable vessel to transfer the FCCU feed from Lytton to our Kurnell Refinery. The timing of the “export” allowed Lytton to continue operation of the refinery’s other units and ensure there were no disruptions to the supply of diesel or jet fuel.

Loading of FCCU feed on the Savannah commenced Thursday 23 February, four business days after the requirement was identified. Loading would have commenced a day earlier except for congestion at the Lytton Refinery products wharf.

In this instance, if we had not been able to use the Savannah in this “unplanned” manner, due to the TL application, variation, and voyage notification requirements, we would have had to slow or stop the refinery.

This would have resulted in the significant shortage of diesel and jet fuel in Queensland in the short term. This would also have added significantly to the cost of the incident for Caltex,

subsequently increasing the total cost of manufacturing petroleum products in Australia versus importing the finished products.

#### **Case Study 2 – Flexible and cost efficient supply chain:**

Caltex has recently entered into a time charter agreement for the Everhard Schulte. The vessel will be used to import fuel oil into Lytton and Kurnell and export clarified oil from these two locations. The vessel will be on a permanent cycle moving these two products.

It is highly likely there will be times when it will be efficient and economically desirable for Caltex to use this vessel to transfer products between its two refineries. Although there is no current plan for this to occur, in the same way the Savannah was required the Everhard Schulte could also be called upon at short notice.

Given Caltex pays a flat time charter rate for the vessel, the additional cargo can be transferred at limited additional cost. This is beneficial in ensuring our supply chain operations are cost efficient and economical.

Under the proposed legislation, Caltex would be required to nominate the cargo, quantity and date the movement was going to occur in a TL. These details are not known with any certainty until the requirement for a transfer presents itself.

#### **Case Study 3 – Events beyond Caltex's control:**

At approximately 1900hrs on Tuesday 12 July 2005, the 132kv power supply to Kurnell Refinery was cut due to an accident involving Energy Australia during their upgrade work to the electricity supply to Kurnell. One of the steel electricity towers collapsed bringing down the transmission lines. This resulted in a total refinery shutdown except for one unit that was maintained on minimum rates.

By the 16 July most of the refinery units had been brought back online at varying production rates.

As a result of the unplanned outage there was an immediate requirement to import finished products to ensure security of supply to the New South Wales market.

Having reviewed the stocks and planned imports it was identified on the 18 July an urgent import of jet fuel would be required to maintain supply to Sydney Airport. A cargo and vessel were organised to load in Melbourne on 21 July and deliver jet fuel into Sydney 24 July.

There were many other actions taken around this time, but this particular element required a fast response to secure the vessel that fortunately was in Melbourne and available at the time of the event.

This case study highlights how unplanned events result in prompt and unplanned requirements for coastal shipping of petroleum products within very short time frames. Caltex's quick response to resolving this unplanned incident ensured that we could maintain jet fuel supply to Sydney Airport and the airport was able to maintain its regular operations.

#### **Case Study 4 – Severe weather event:**

In January 2011, Caltex loaded a cargo of approximately 83,000mt of Kutubu crude oil on board the Pacific Virgo (a foreign vessel) at Kumul, Papua New Guinea with the intention of fully discharging the cargo at Caltex's Lytton refinery.

On 5 January, the vessel arrived at Lytton and commenced discharge of the crude oil and

was estimated to complete discharge early on 7 January.

A severe storm hit Brisbane, at around 2113hrs on the 5 January, causing an electrical trip to a refinery unit which resulted in a total shutdown of the refinery. It was anticipated that the refinery would be totally shutdown for approximately five days and partially shutdown (ie only a number of units operational) for a further five days after that.

By the following morning of 6 January, the Pacific Virgo had discharged about 61,000mt of crude oil, with about 22,000mt remaining on board. The vessel was given instructions to stop discharging. During this day, refinery management determined that it was not operationally feasible to complete the discharge of the Pacific Virgo at Lytton as it was likely there would be insufficient ullage (unfilled space) available at the Lytton refinery to partially discharge the next incoming crude cargo (on the vessel the Knock Clune) which was due in four days time.

If we did not transfer sufficient volume off the Knock Clune cargo, we would also not be able to berth the cargo at our Kurnell refinery due to the berth draft limit in Botany Bay. This would leave the Kurnell refinery at risk of running out of crude if there were any delays to start-up of the Lytton refinery, which would shorten product supply to the Sydney market, as well as further exacerbate our ability to supply the already tight Queensland market.

As a result, the decision was made to commence returning approximately 33,000mt of the already discharged Kutubu crude oil onto the Pacific Virgo, and thus move a total of about 55,000mt of Kutubu crude to Kurnell. At the time this decision was made, all efforts were being directed to keeping production feasible at our Kurnell refinery and making the Lytton refinery operational again.

It was subsequently established that a SVP was required for this unplanned coastal move and a full explanation was provided to the Department. The following is an excerpt from the response we received from the Department:

*“Understand market supply imperatives for Sydney and Queensland markets required Caltex to reload and transfer 33,000mt of crude in addition to the 22,000mt already on board to deliver a total of 55,000mt to the Kurnell refinery. The exceptional circumstances at the Lytton refinery reflect an operational necessity for Caltex to maintain production from the Kurnell refinery in the public interest.”*

It should be noted that the decisions relating to this coastal move were made in a matter of hours due to the nature of the event, which also came at considerable cost to Caltex.

These case studies clearly demonstrate the unpredictable nature of the Australian oil refining industry and reveal that the proposed legislation is not workable from Caltex’s perspective.

Local refining in Australia is a trade exposed industry and faces the challenges of a strong Australian dollar and high operating costs. For manufacturing of petroleum products to be viable in Australia, refiners must be able to optimise their supply chains and maximise the utilisation of the vessels they have already committed to. The case studies outlined above provide real life examples of unplanned shipping movements that are required within the normal operating environment of a refinery.

The inability to effectively move products in a timely manner during unplanned events will negatively impact reliability of supply of transport fuels nationally.

The proposed changes to the shipping legislation present a material degradation of flexibility and cost efficiency within Caltex’s supply chain. The proposed legislation will have a potential adverse impact on the viability of our refinery operations.

***Recommendation 9: That an urgent temporary licence category be introduced into the proposed Coastal Trading (Revitalising Australian Shipping) Bill 2012. The information required for a temporary licence application would be provided but the approval period must be a maximum of two working days.***

## 2.10 Statutory defence

A possible solution for the unplanned requirement to undertake an urgent voyage without a TL, completing a variation, or submitting the required voyage notification, may be the inclusion of a statutory defence in the Coastal Trading Bill for undertaking such action.

Caltex is aware of existing Commonwealth legislation (ie the *Fuel Quality Standards Act 2000*) that takes into consideration the reality that a shortfall in the supply of a fuel may occur and that such shortfalls have the potential to be a serious threat to the interests of consumers, or economic and regional development. The following is an excerpt from the *Fuel Quality Standards Act 2000*:

### ***“Division 3—Approvals***

#### ***Subdivision A—Grant of approval***

##### ***13 Grant of approval***

***(1) The Minister may grant to any person an approval in writing that varies a fuel standard or a fuel quality information standard in a specified way in respect of specified supplies of the fuel by:***

***(a) that person; or***

***(b) any other specified person (a regulated person).***

***(2) Subject to subsection (3), the Minister may grant a type of approval under subsection (1), known as an emergency approval, if the Minister is satisfied that:***

***(a) a shortfall in the supply of a fuel will exist within two weeks; and***

***(b) the shortfall will have a serious impact on:***

***(i) the interests of consumers; or***

***(ii) economic or regional development; and***

***(c) the shortfall will not reasonably be met by one or more persons (other than the applicant for the approval), either separately or together; and***

***(d) granting the approval will enable, or assist in enabling, the shortfall to be met or mitigated; and***

***(e) the shortfall will exist because of exceptional circumstances.”***

Caltex proposes that the government consider including a statutory defence into the proposed regulations to allow oil companies to minimise any potential disruption of fuel supply to consumers, industry and the economy as a whole.

The criteria outlined in the *Fuel Quality Standards Act 2000* may provide a starting point for considering and developing criteria that may be included in the coastal trading legislation with respect to an urgent licence and/or statutory defence.

The legislation could also incorporate a complementary approach to urgent voyages. For example, if an urgent voyage was required, the first approach would be to apply for an urgent TL. However, if the urgent voyage cannot be delayed by two business days until an urgent TL is approved, then the statutory defence may be used to defend the action of undertaking an urgent voyage without a licence.

***Recommendation 10: That a statutory defence for undertaking an urgent voyage without a temporary licence be introduced into the proposed Coastal Trading (Revitalising Australian Shipping) Bill 2012.***

## 2.11 Comments by third parties

The proposed Coastal Trading Bill now provides third parties with the opportunity to provide comment on TL applications and that the Minister may have regard to these comments when deciding an application (Section 33).

Third parties are not privy to commercial negotiations between two parties and should not be able to generically state that an application would directly affect themselves or their members.

Caltex proposes that if third parties continue to be given the opportunity to provide comment on a TL application or variation, then third parties should only be given this opportunity when a GL holder gives notice in response to the application and/or variation. If a GL holder does not give notice in response then third parties should have no basis for being able to claim they would be directly affected.

***Recommendation 11: That third parties only be given the right to provide comment on a temporary licence application, or variation, if a general licence holder has given notice in response.***

## **2.12 Emergency licences**

With respect to Section 51(4) of the Coastal Trading Bill, Caltex proposes that applications for emergency licences (EL) must be decided within one business day to reflect the likely time pressure and critical circumstances that would exist if the conditions for an EL applied.

***Recommendation 12: That the Minister must decide on an application for an emergency licence within one business day.***

## **2.13 Investigative powers**

Caltex notes that the investigative powers detailed in Part 5 of the proposed Coastal Trading Bill seem to be disproportionate to the objectives of the Act, which includes promoting, facilitating and enhancing the Australian shipping industry.

***Recommendation 13: That the investigative powers outlined in the Coastal Trading (Revitalising Australian Shipping) Bill 2012 be revised to become more fair and balanced with respect to the legislative enforcement needed to promote, facilitate and enhance the Australian shipping industry.***

# **3. Tax Incentives Bill and Tax Laws Amendment Bill**

## **3.1 Income tax exemption**

As it stands, only certain vessels are eligible for the income tax exemption (ITE) and Section 10 of the Tax Incentives Bill sets out the necessary requirements that need to be met in order to qualify. Specifically, Section 10(4) outlines that certain vessels will not be eligible if they fall within the list of excluded assets.

Caltex seeks clarification on the inclusion of 'barge' in the definition of excluded vessels (Section 10(4)), as there is a distinction between a 'dumb barge' and 'motorized barge' in the shipping industry.

A 'dumb barge' is a long, large and, usually, flat bottom vessel used for the transport of freight such as coal, finished steel, iron ore, grain, gravel, etc. It is generally designed with absence of its own means of mechanical propulsion and is required to be towed or pushed by other craft, such as a tug boat. This can be distinguished from a 'motorized barge' where it can operate without the assistance of a tug boat and can be used for the transportation of product on coastal voyages or offshore.

In addition, there is a differentiation of barges based on size/capacity and capability as some barges can and do operate on open waters, similar to tankers vessels.

***Recommendation 14: That the definition of 'excluded vessels' in Section 10(4) of the Shipping Reform (Tax Incentives) Bill 2012 be clearer on the type of barges that are specifically excluded, and that any barge capable of open ocean operations and with a cargo capacity greater than 750mt be included in the definition.***

### 3.2 Seafarer tax offset (refundable tax offset)

With respect to Schedule 3 of the Tax Amendment Bill, Caltex seeks clarification on whether the '91 days or more' includes days on a ship's overseas voyages where it is in 'ballast', ie a vessel is sailing empty to its next loading port or on a return journey back to an Australian port.

Caltex also seeks further clarification on the amount of the seafarer tax offset a company is entitled to. According to Section 61-710 of the Tax Amendment Bill, this is calculated using the formula:

$$\text{Gross payment amounts} \times 27\%$$

Where the 'gross payment amounts' means the total amount of withholding payments covered by Section 12-35 or Section 12-60(1) in Schedule 1 of the *Taxation Administration Act 1953* payable by the company in the income year.

These payments are salary, wages and allowances paid to Australian seafarers who are employed to undertake overseas voyages on certified vessels. It also includes payments to individuals employed under a labour hire arrangement.

The 27% refundable tax offset is available to employers, however there is confusion about whether this includes annual leave accrued while the individual is at sea. On average, seafarers have an arrangement where for every day they work at sea, they accrue one day's leave. If the 50% proportion of leave is not taken into account, in effect the refundable tax offset translates to be only a 13.5% offset instead of 27%.

In addition, the policy intent of providing this refundable tax offset is to encourage companies to employ and build the pool of Australian seafarers for the Australian shipping industry. Hence, the refundable tax offset should be competitive with other countries (eg UK has a full tax offset for the individual) to ensure companies are encouraged to employ Australian seafarers.

Effectively, the ITE granted to qualifying companies is a tax deferral regime with a clawback of the tax benefit upon distribution of profits to the company's shareholders.

The tax benefit provided at the company level is effectively taken away via either a dividend withholding tax for non-resident shareholders at up to 30% depending on the residency of the recipient, or no franking credit for resident shareholders.

By not having deemed franking credits or dividend exemption this will detract the attractiveness of investment by local and overseas investors.

Given that the reform package aims to "make the Australian shipping industry more internationally competitive and facilitate Australian competition on international routes" and it also is "designed to reform and revitalise coastal shipping in Australia to create a competitive environment attractive to investors", to flow through the tax benefits to shareholders in the form of deemed franking credits and dividend exemption will make it more attractive to investors both locally and internationally.

***Recommendation 15: That the Tax Laws Amendment (Shipping Reform) Bill 2012 define whether the word 'voyages' includes the journey when the vessel is in ballast and whether these days are counted in the criteria of at least 91 days.***

***Recommendation 16: That the Department clarify that the 'gross payment amounts' used to calculate the refundable tax offset are salary, wages and allowances paid to Australian seafarers with no exclusion of the leave component of their remuneration.***

***Recommendation 17: That the government review whether the refundable tax offset is competitive with other countries to ensure that companies will be encouraged to employ Australian seafarers.***

***Recommendation 18: That the tax benefits extend to shareholders in the form of deemed franking credits and dividend exemption, which will make it more attractive to investors both locally and internationally.***

#### **4 Conclusion**

Caltex understands that the government intends to revitalise the Australian shipping industry through these coastal trading reforms. However, the oil refining industry operates in a volatile environment and refineries do not always produce planned volumes. Despite this, Caltex focuses on the safe and reliable supply of petroleum products to the Australian market.

To maintain safe and reliable supply, Caltex believes that the proposed legislation must take into consideration the needs of Australian industry. Caltex believes that the proposed regulations need to become more flexible to minimise the potential for supply disruptions and ensure these regulations do not unnecessarily impose restrictions on the normal operating environment of Australian industries.