

1982-83

PARLIAMENT OF NEW SOUTH WALES

EIGHTH REPORT

OF THE

PUBLIC ACCOUNTS COMMITTEE

OF THE

FORTY-SEVENTH PARLIAMENT

*(INQUIRY INTO REFERENCE BY THE MINISTER FOR AGRICULTURE
AND FISHERIES TO THE COMMITTEE UNDER THE PROVISIONS OF
SECTION 16 OF THE AUDIT ACT, 1902)*

ORDERED TO BE PRINTED, NOVEMBER, 1983

MEMBERS OF THE COMMITTEE

MR M.R. EGAN, B.A., M.P. (Chairman)

MR J.J. AQUILINA, B.A., Dip. Ed., M.P.

MR J.C. BOYD, M.P.

MR P.E.J. COLLINS, B.A., LL.B., M.P.

MR S.T. NEILLY, AASA, M.P.

TRANSCRIPTS OF EVIDENCE TABLED
TOGETHER WITH THIS REPORT.

CONTENTS

	<u>Page</u>
1. RECOMMENDATIONS	1
2. BACKGROUND TO THE REPORT/SUMMARY	5
3. CONDUCT OF THE INQUIRY	9
4. SUMMARY OF THE BOARD'S ACTIVITIES	10
4.1 Constitution and Establishment	10
4.2 Legislation	11
4.3 Functions of the Board	11
4.4 Operations of the Board	12
4.5 Activities in the 1981-82 Crop Season	12
4.6 Activities in the 1982-83 Crop Season	15
5. ANALYSIS OF THE BOARD'S ACTIVITIES	18
5.1 Forward Contracts	18
5.2 Futures Trading	22
5.3 Illegal Sales	27
5.4 Communication by the Board	29
5.5 Industry Support for the Board	31
5.6 Duties of Board Members	33
5.7 Power to Accumulate Reserves	37
5.8 Future Viability of the Board	38
5.9 Other Legal Issues	39
6. APPENDICES	41
1. Terms of Reference	42
2. Points of Interest	43
3. Submissions Received	44
4. Parties who Presented Evidence	45
5. Trade Creditors of the Board	46
6. Other Creditors of the Board	47
7. Grain Deliveries in Recent Years	48
8. Futures Trading Involving Forward Contracts	49
9. Futures Trading Without Forward Contracts	51

1.

RECOMMENDATIONS

The following recommendations have been specifically framed to apply to all Boards constituted under the Marketing of Primary Products Act, and do not apply only to the Grain Sorghum Marketing Board.

1. Boards continue to be permitted to negotiate forward contracts in the commodity which they were established to regulate.
(Refer page 19)
2. Boards be permitted to negotiate forward contracts in commodities other than that which they were established to regulate only with the approval of the Minister.
(Refer page 19)
3. Forward contracts be related to expected Board receipts, and not to expected production in New South Wales.
(Refer page 22)
4. The Department of Agriculture formulate rules governing futures trading.
(Refer page 22)
5. The rules for futures trading stipulate the commodities in which the Board is permitted to trade.
(Refer page 23)

6. All futures market transactions by a Board be recorded in a register including details of -
 - date of transaction
 - quantity
 - futures delivery month
 - price
 - reason for transaction
 - other party
 - commission
 - broker(Refer page 24)

7. Copies of the Futures Market Register be forwarded monthly to the Auditor General and the Minister for Agriculture for evaluation of the legality and effectiveness of the Board's trading.
(Refer page 25)

8. A summary of futures trading activities be included with each Board's annual statements of account.
(Refer page 25)

9. Bank hedge operations be subject to the same requirements as those recommended for futures market transactions.
(Refer page 26)

10. The vesting provision of the Marketing of Primary Products Act be retained.
(Refer page 29)

11. Boards be given wider powers under the Marketing of Primary Products Act to ensure policing of the vesting provision.
(Refer page 29)

12. Boards provide evidence in their Annual Reports of their activities in respect of policing the vesting provisions of the Act.
(Refer page 29)

13. Boards form Industry Advisory Committees to discuss, evaluate and advise on issues related to domestic marketing. These Committees to include:
 - growers
 - merchants
 - end users
 - government
 - other relevant personnel(Refer page 31)

14. Regular assessments of grower support be made to determine whether the continued existence of the Board is warranted.
(Refer page 33)

15. The duties of members of Marketing Boards be investigated and prescribed in the Marketing of Primary Products Act. The duties to include:
 - a duty to inform growers
 - a duty to do all that is reasonably possible as individuals to see that the Board prospers.(Refer page 36)

16. Any candidates for election to the Board disclose their dealings with the Board for the twelve months prior to each election and that Board members disclose their dealings with the Board annually.
(Refer page 36)

17. Failure of Board members to deliver their grain sorghum to the Board, at times when all marketing activities are vested in the Board, be grounds for their removal and ineligibility for re-election.
(Refer page 36)

18. Boards be permitted under the Marketing of Primary Products Act to accumulate general reserves, subject to development of guidelines by the department governing amounts and types of deductions which can contribute to reserves.
(Refer page 37)

2. BACKGROUND TO THE REPORT/SUMMARY

This Report arises from a reference by the Minister for Agriculture and Fisheries, the Honourable J.R. Hallam, M.L.C., to the Public Accounts Committee to inquire into the administration and operations of the Grain Sorghum Marketing Board and any other matters which affect that Board's efficiency, effectiveness and accountability. (Appendix 1).

Prior to the reference the Minister foreshadowed the introduction of a new Marketing of Primary Products Act to govern the operations of all Marketing Boards constituted under that Act. The Committee accordingly sought to analyse the factors contributing to the Board's precarious financial position, and to formulate recommendations which would be applicable to all Boards. These recommendations have been developed with the aim of minimising the likelihood of another Board repeating the Grain Sorghum Marketing Board's errors.

The operations of marketing boards in New South Wales, other States and the Commonwealth have attracted increasing scrutiny in recent years. Attention has focussed on their failure to disclose certain trading activities (e.g. futures market trading), their methods of determining contracts and claims of their inefficiency and uselessness.

Since the date of the grain sorghum reference another two large rural marketing organizations have reported severe financial shortfalls. These are the Central Queensland Grain Sorghum Marketing Board and the Queensland Graingrowers Association. Their problems also relate to financial losses incurred in both meeting forward contracts and from commodity and financial futures trading operations and bank hedging operations. The proposed recommendations for inclusion in the new Act should clarify the use, limitations and role of futures market trading.

The Grain Sorghum Board's present predicament is the result of several different factors. The principal problem has arisen from the Board's having received insufficient grain sorghum from producers in New South Wales to meet forward contract commitments in both 1981-82 and 1982-83. Losses of approximately \$900,000 were incurred in 1981-82 from purchasing grain sorghum interstate to meet commitments, and losses of approximately \$2.7 million were incurred in 1982-83 in failing to honour contractual commitments.

Recent amendments to the Audit Act have given the Committee the power to initiate its own enquiries. The Committee will therefore be monitoring the future performance of Marketing Boards as measured against objectives and goals.

The volume of grain sorghum forward contracted in 1981-82 indicated that the Board was optimistic, rather than realistic, about the volume to be received. The Board's actions in forward contracting significant volumes in both seasons without either physical stocks or substantial reserves clearly exposed it to substantial risk.

Drought conditions reduced grain sorghum production in both seasons, although production in New South Wales substantially exceeded contracted volume. The real shortfalls were caused by producers (including all producer members of the Board) failing to deliver to the Board. This demonstrates lack of confidence in the Board and its ability to obtain maximum prices for producers.

The Board's futures trading activities did not contribute significantly to its weak financial position. However, these activities had been undertaken without any advice as to the legality of the Board's futures trading operations. The Board has also displayed some reluctance to acquaint growers and other sections of the industry with timely details of all their activities. Indeed the specifics of some activities appear to have been withheld from producers for as long as possible, particularly the method of financing 1981-82 trading losses.

3. CONDUCT OF THE INQUIRY

Notices of the Committee's inquiry and invitations for submissions were placed in selected national, metropolitan and regional press. Interested parties were forwarded a letter outlining the points of particular interest to the Committee in this inquiry (Appendix 2). In addition, the Committee wrote to: all Marketing Boards in New South Wales constituted under the Marketing of Primary Products Act; the major trade creditors of the Grain Sorghum Marketing Board; financial, grain handling, market consulting, and advisory organizations associated directly with the Board's activities; and to the various associations representing grain sorghum trading merchants and producers of grain sorghum.

The Committee ultimately received fourteen submissions relating to this inquiry. The organizations and individuals who made submissions are listed in Appendix 3. Most significantly assisted the Committee in the preparation of its report. From the written submissions received by the Committee, five parties were requested to give oral evidence at the public hearings held by the Committee (Appendix 4).

4. SUMMARY OF THE BOARD'S ACTIVITIES

4.1 Constitution and Establishment

The Grain Sorghum Marketing Board for the State of New South Wales is a body corporate established in 1971 under the provisions of the Marketing of Primary Products Act, following a poll of grain sorghum producers in New South Wales, who voted in favour of the establishment of a Board. Although constituted under Statute the Board is an autonomous organisation and its financial viability is in no way guaranteed by the Government.

The establishment of the Board followed a period of very depressed prices, principally caused by the introduction of wheat delivery quotas in 1969. Also at this time, the Australian Coarse Grain Growers Association developed export markets for grain sorghum, which significantly increased returns to grain sorghum producers. For these reasons growers sought a centralised selling organisation and thus established, by poll, the Grain Sorghum Marketing Board.

The Board comprises seven members, five of whom are elected by producers every three years, and two of whom are nominated by the Minister for Agriculture and Fisheries.

4.2 Legislation

The Board is one of nine Marketing Boards in New South Wales constituted under the Marketing of Primary Products Act, 1927, as amended. This Act provides that grain sorghum produced in New South Wales shall be divested from the producers and become absolutely vested in, and the property of, the Board. Grain sorghum may only be exempted from these vesting provisions at the discretion of the Board, although prior to the 1982-83 season the Board issued exemptions for sales through merchants licensed by the Board. Essentially, then, all grain sorghum in New South Wales must by law be sold to and through the Grain Sorghum Marketing Board.

4.3 Functions of the Board

The functions of the Board, as stated in its submission to the Committee, are:

- "1. To make appropriate and adequate arrangements for the disposal of the New South Wales grain sorghum crop.
2. To arrange for the sale of grain sorghum vested in it or delivered or to be delivered to it, with the object of achieving the highest possible return to producers.
3. To promote the production of grain sorghum in New South Wales and to promote the use of grain sorghum and its products in Australia and overseas.
4. To arrange for the receipt, handling, storage, protection and transportation of New South Wales grain sorghum.
5. To determine and administer quality standards for New South Wales grain sorghum.
6. To arrange financial accommodation to enable the prompt payment of first advance to growers for grain sorghum delivered to the Board and to enable ongoing administrative expenses to be met until seasonal pools can be finalised."

The Committee noted that these functions empowered the Board to deal in no commodity other than grain sorghum.

4.4 Operations of the Board

The Board has developed, over a number of years, a range of grain sorghum marketing alternatives for producers. These alternatives have included:

1. Seasonal pools
2. On-farm storage seasonal pools
3. Brisbane direct deliveries for export
4. Cash price option
5. Licensed merchant system

The first three marketing alternatives are offered by the Board; the fourth is offered by the Board's subsidiary company, the Grain Sorghum Trading Company; and the final alternative is selling to a merchant licensed by the Board. The amounts of grain sorghum handled by each marketing alternative for the last five years are presented in Appendix 7.

4.5 Activities in the 1981-82 Crop Season

(a) Forward contracts - In late December 1981 when the New South Wales grain sorghum crop was progressing well, the Board sold three export cargoes totalling 75,000 tonnes for shipment during March/April/May 1982. No forward domestic contracts were negotiated at this time. The export cargoes were sold to Dreyfus (two) and the Queensland Graingrowers Association (one).

During early 1982 it became apparent that the Board would have difficulty in accumulating sufficient grain to meet its commitments. One shipment of 25,000 tonnes was deferred from March to April at no penalty and at the same time a second cargo was deferred from April to June by selling a June cargo to Pynstorm Pty Ltd and buying an April cargo from the Queensland Graingrowers Association. The Board covered these three contracts by buying a cargo from the Central Queensland Grain Sorghum Marketing Board, buying another cargo from the Queensland Graingrowers Association, and a combination of pool receivals and local cash purchases on behalf of the Board by Gatenby Bros Pty Ltd.

Following completion of the export programme in June 1982, the Board negotiated a forward export commitment of 25,000 tonnes with Mallorca Enterprises Pty Ltd for shipment in June 1983.

(b) Futures trading - The Board has been engaged in futures trading since 1978. This trading involves participation on the corn futures market of the Chicago Futures Market and the bank hedge market in Sydney. The sales and purchases relating to the forward contracts outlined earlier were negotiated at a price relative to Chicago corn futures prices. The prices concerned were expressed in United States currency and the Board's currency exposure was progressively hedged on the Sydney bank hedge market with Westpac Banking Corporation and Elders Finance Pty Ltd.

(c) Board receivals - The total quantity of grain sorghum delivered by the Board against the export sales, and later small domestic sales, was 99,471 tonnes. This quantity comprised pool receivals of 12,714 tonnes, local cash purchases of 16,528 tonnes, and interstate purchases of 70,329 tonnes. The local purchases were negotiated by Gatenby Bros Pty Ltd at a commission of \$2 per tonne, while the interstate purchases were made in Queensland from the Queensland Graingrowers Association and the Central Queensland Grain Sorghum Marketing Board.

(d) Financial position - the total net loss incurred by the Board in respect of covering the contract commitments was approximately \$905,500. This amount included a loss of \$325,459 on its currency hedge operations, and a net profit of \$151,269 on its Chicago Futures Market operations, as outlined in the Auditor-General's 1982-83 Report.

The forward contract with Mallorca Enterprises Pty Ltd, for June 1983 delivery, involved a pre-payment of U.S.\$800,000 (which converted to A.\$838,422). This pre-payment was used for financial accommodation by the Board, with the balance of the shortfall being met from the Board's funds. The balance of accumulated reserves held by the Board after final payments to growers relating to 1982 pool deliveries was approximately \$16,405.

4.6 Activities in the 1982-83 Crop Season

(a) Forward contracts - Against a background of anticipated record grain sorghum plantings and expected downward price pressure at harvest, the Board decided, in September 1982, to acquire the New South Wales sorghum crop in the 1982-83 crop season. That is, no grain sorghum would be exempted from the vesting provisions of the Marketing of Primary Products Act.

In addition to the overseas contract of 25,000 tonnes for June 1983 delivery, the Board negotiated in January 1983 a number of forward contracts with various local buyers for delivery from March to July 1983. These forward domestic contracts totalled 43,500 tonnes to the following buyers:

Gatenby Bros Pty Ltd	20,000 tonnes
Inghams Enterprises Pty Ltd	10,000 tonnes
K.M.M. Pty Ltd	5,000 tonnes
Bunge (Australia) Pty Ltd	3,000 tonnes
Gurley Feedlot	2,500 tonnes
Allied Mills Industries Pty Ltd	2,000 tonnes
Peter Schwarz (Overseas) Pty Ltd	1,000 tonnes

(b) Futures trading - The Board again engaged in futures trading activities on the Chicago Futures Market. These activities included transactions on both the corn futures and wheat futures markets. The overseas contract with Mallorca Enterprises Pty Ltd was expressed in United States currency and the Board's currency exposure was hedged on the Sydney bank hedge market, as in the 1981-82 season.

(c) Board receivals - The Board's voluntary pool received zero deliveries, in response to its advertised first advance payment. The Board, through the Grain Sorghum Trading Company, attempted to buy grain sorghum by making cash price offers of \$93 per tonne on-farm in late January 1983, and \$105 per tonne on-farm on 22 February, 1983, to growers. However total purchases were only 1,060 tonnes. The Board announced on 9 March, 1983 that it was not proceeding with its acquisition of the crop, and the system of sale would revert to an exemption system through licensed merchants.

(d) Financial position - The failure of the Board to attract sufficient grain sorghum to meet its forward contract commitments led to large financial claims against the Board by those firms with dishonoured contracts. These claims related to the difference in cost between the contract price and ruling market prices at the time the contracts should have been delivered against. The Board has admitted liability for these claims which total A.\$1,797,182.81 for the dishonoured domestic contracts and U.S.\$806,847.77 for the dishonoured export contract. Full details of individual claims are detailed in Appendix 5.

At current exchange rates, the total liability of dishonoured contracts is approximately A.\$2.7 million. In addition the Board has a liability of \$201,370.63 to various creditors. Full details of sundry creditors are presented in Appendix 6. The total liability of the Board is therefore approximately \$2.9 million.

When giving evidence to the Committee, the Board indicated assets of approximately \$30,000 cash, and an amount of approximately \$60,000 in a Trust Fund, paid by sorghum producers to be used to finance the Board, if its future was assured. The latter amount was subsequently returned to growers following their failure to adequately respond to the Board's appeal.

Clearly the Board's liabilities far exceed its assets, and various schemes of arrangement between creditors and the Board, which allow the Board to continue trading, are currently being negotiated.

The Board's futures trading operations in corn and wheat futures on the Chicago Futures Market resulted in a total net loss of \$143,182.29.

5. ANALYSIS OF THE BOARD'S ACTIVITIES

5.1 Forward Contracts

Forward selling is a routine part of grain trading, both internationally and domestically. It allows buyers to better plan their operations, through determining inputs in advance and sellers to negotiate more efficient arrangements for storage, freight, and shipping programmes.

Contracts for future delivery are usually for a determined quantity with price negotiated on either of two bases:

1. Fixed price
2. Price relative to Chicago Futures Market quotations ("basis trading")

In both cases the contracts are for determined quantities, for delivery at a set time. In the first instance, the price is also set when the contract is signed, while in the second the price is contracted at a premium over a certain Chicago Futures Market price (for example a contract price of 10 cents per bushel premium over July 1984 Chicago Corn Futures price). Usually the buyer has the option to decide which day, between the signing of the contract and the delivery date, the contract price will be set, and the seller advised that day. Thus the exact price is not known when the forward contract is signed, although the method by which it will be determined is known. In both instances the agreed price (be it either fixed or "basis trading") represents a commercial judgement acceptable to both buyer and seller.

The Committee recommends that:

BOARDS CONTINUE TO BE PERMITTED
TO NEGOTIATE FORWARD CONTRACTS
IN THE COMMODITY WHICH THEY WERE
ESTABLISHED TO REGULATE.

BOARDS BE PERMITTED TO NEGOTIATE
FORWARD CONTRACTS IN COMMODITIES
OTHER THAN THAT WHICH THEY WERE
ESTABLISHED TO REGULATE ONLY WITH
THE APPROVAL OF THE MINISTER.

In the 1981-82 season, the Board forward contracted 75,000 tonnes. The Board's justification for this was to take advantage of favourable current prices, which it did not expect to continue until harvest, and that the contracted amount represented only twenty per cent of expected total grain sorghum production in New South Wales.

Expected price movements require organizations to make commercial judgements, and it is usual in normal circumstances for grain sorghum prices to fall at harvest time, so that the Board's decision relating to price appears a sound one.

The decision to relate contracted tonnage to expected production was however erroneous. The relevant variable is not expected production, but rather expected receivals by the Board as not all the grain sorghum produced in the State is received by the Board. The grain sorghum not delivered to the Board will include grain retained on-farm by producers, interstate sales, and illegal intrastate sales (see section 5.3).

The export contract for 25,000 tonnes for shipment in June 1983 negotiated at the end of the 1981-82 season, involved a large pre-payment of A.\$838,422. This was used for financial accommodation by the Board to cover trading losses in that season. This information was not conveyed to growers at that time and the specific manner of financing the trading losses was not known publicly until March 1983.

In January 1983, the Board forward contracted 43,500 tonnes with various domestic buyers at prices averaging \$93 per tonne on farm. The contract price approximated then current market prices. In total therefore the Board had forward commitments of 68,500 tonnes prior to harvest. The Board had announced in September 1982 that it would not be exempting grain sorghum from the vesting provisions of the Act; that is, all grain sorghum entering trade in New South Wales would, legally, be delivered to the Board through its licensed agents.

While the Committee accepts that it was proper for the details of the arrangement to remain confidential, growers should nevertheless have been informed that the Board had entered into a significant forward commitment involving bridging finances.

Pool receipts by the Board in the five seasons prior to 1982-83 are listed in Appendix 7 and were as follows:

1977-78	56,000 tonnes
1978-79	196,795 tonnes
1979-80	6,568 tonnes
1980-81	16,754 tonnes
1981-82	29,241 tonnes

While the Committee does not oppose the principle of forward selling the decisions to forward sell 75,000 tonnes prior to the 1981-82 harvest and 68,000 tonnes prior to the 1982-83 harvest appear to have been somewhat irresponsible because:

- * Recent history showed that receivals by the Board were far less than the commitments entered into in respect of both the 1981-82 and 1982-83 seasons.

- * The Board should have been aware that on 1 December, 1979, the pricing mechanism used by the Australian Wheat Board for wheat used on the domestic market was lifted to export parity. The higher price of domestic wheat clearly would have made grain sorghum more competitive as a stock feed and hence domestic demand for it would normally have been expected to rise, which it did. This factor was cited by one of the Board members in evidence before the Committee as having caused the short supply of sorghum in the 1981-82 season.

- * In respect of the 1982-83 season the Board should have been aware of the likely price escalating effect of the fodder subsidy provided by the Federal Government from 1 September, 1982, well before the forward contracts for the domestic market were negotiated.

- * Having been unable to obtain sufficient grain sorghum from the 1981-82 season the Board should have been less optimistic about its prospects for the 1982-83 season.

The Committee recommends that:

FORWARD CONTRACTS BE RELATED TO EXPECTED BOARD RECEIVALS, AND NOT TO EXPECTED PRODUCTION IN NEW SOUTH WALES.

5.2 Futures Trading

Futures trading is a marketing technique which can provide an increased degree of price insurance, if used as a "price hedging" operation. However, speculation on futures markets can lead to widespread losses or substantial gains in a very short period.

The legality of futures trading by Boards under the current Act has been accepted, following a favourable opinion from a Queen's Counsel. However, the guidelines to be followed have not been developed to any extent. The Wheat Marketing Act was recently amended to allow the Australian Wheat Board to legally engage in futures trading, subject to certain requirements.

The Committee recommends that:

THE DEPARTMENT OF AGRICULTURE FORMULATE RULES GOVERNING ALL FUTURES TRADING.

The legal opinion referred to earlier advised that futures trading was legal in relation to the commodity for which the Board was constituted. The Grain Sorghum Marketing Board's futures trading activities have been on the Chicago Futures Market in corn and wheat futures, because there is no futures market for grain sorghum. The Board has frequently stated that it has legal opinion that its corn futures trading activities are legal under the Act. However, the legal opinion obtained referred only to futures trading in the commodity specified under the Act and not to futures trading in a substitute commodity. To state that the Board's futures trading activities are legal, although no legal opinion has been given, is misleading.

The Committee recommends that:

THE RULES FOR FUTURES TRADING
STIPULATE THE COMMODITIES IN
WHICH THE BOARD IS PERMITTED
TO TRADE.

Futures trading activities can be undertaken to complement normal trading activities in the physical commodity in two situations:

- * where a forward contract has been signed by the Board for future delivery at a price relative to a Chicago Futures Market price ("basis trading").

- * where a Board wishes to take advantage of current favourable prices as a basis for signing forward contracts. This is often referred to as a "hedge" situation.

It is important to stress that futures trading, when appropriately used for price insurance, represents one component of a total price fixing process (the other being the cash market price at time of sale, or contract price at delivery). Therefore, net gains or losses on the Chicago Futures Market in each season must not be viewed in isolation, but considered in relation to prices received for the physical commodity. This process is clearly indicated in Appendices 8 and 9.

It is important that all futures market transactions be evaluated both against the set of trading rules recommended earlier and against the aims or reasons for which the transactions were entered into.

The Committee recommends that:

ALL FUTURES MARKET TRANSACTIONS
BY A BOARD BE RECORDED IN A REGISTER
INCLUDING DETAILS OF:

- DATE OF TRANSACTION
- QUANTITY
- FUTURES DELIVERY MONTH
- PRICE
- REASON FOR TRANSACTION
- OTHER PARTY
- COMMISSION
- BROKER

It is recognized that some of the details which would be contained in this proposed register may be commercially sensitive if publicly available. Therefore access to the register may have to be restricted, although a summary of the transactions would not include such details.

The Committee recommends that:

COPIES OF THE FUTURES MARKET REGISTER BE FORWARDED MONTHLY TO THE AUDITOR GENERAL AND THE MINISTER FOR AGRICULTURE FOR EVALUATION OF THE LEGALITY AND EFFECTIVENESS OF THE BOARD'S TRADING.

A SUMMARY OF FUTURES TRADING ACTIVITIES BE INCLUDED WITH EACH BOARD'S ANNUAL STATEMENTS OF ACCOUNT.

A detailed examination has been made of the Board's futures trading activities since 1979. The maximum net exposure by the Board has been less than two export cargoes (50,000 tonnes) in that time.

The Board's futures trading activities can be described as "selective hedging". That is, the Board does not cover all physical commitments on the Chicago Futures Market, but selects those which it believes will benefit through futures trading. This process involves judgements by the Board as to future movements in prices. Similarly the Board times its transactions around expected price movements, in an attempt to maximise futures profits and minimise futures losses through any futures market price variations.

Activities by the Board on the Chicago Futures Market have involved trading in corn and also in 1983 wheat. The Board has argued that prices of these commodities are directly related to grain sorghum prices. The Committee notes that experienced futures market traders caution against participation in one commodity as a means of hedging prices of a different commodity. The Board's activities must therefore also be viewed with some concern from an operational side.

The Board's currency hedging operations for the past two seasons have been performed on the Sydney bank hedge market. The aim of this has been to protect the Board against devaluation of the Australian currency. The bank hedge market is a recent development, which is widely used in commercial circles to minimise currency fluctuation risks. The Board's general activities in this area appear to be prudent.

The Committee recommends that:

BANK HEDGE OPERATIONS BE SUBJECT
TO THE SAME REQUIREMENTS AS THOSE
RECOMMENDED FOR FUTURES MARKET
TRANSACTIONS.

5.3 Illegal Sales

Prior to the 1982-83 crop season the Board divested control of the marketing of grain sorghum and ran voluntary pools. That is, producers could legally deliver their grain sorghum to the Board's voluntary pool, or sell it to a merchant licensed by the Board. These licensed merchants pay a fee to the Board, which is offset against the Board's administration costs. However, for the 1982-83 crop season the Board decided to enforce its vesting requirement, in an endeavour to prevent a collapse of prices during the expected large harvest.

This does not mean that a Board must at all times enforce the vesting provision, but that the industry is aware that it can be enforced if required. However, in the absence of complementary Commonwealth legislation, section 92 of the Constitution prevents the vesting provision of the Act extending to grain bought by an interstate buyer and moved directly interstate. The major interstate movements of grain sorghum over the past two seasons have been into Victoria and South Australia for the intensive livestock industries.

Intrastate sales of grain sorghum outside the system approved by the Board are however illegal. Such illegal sales include direct sales from producer to producer, direct producer sales to end users, sales to merchants not licensed by the Board, and opportunity sales by, for example, truck drivers.

The degree of illegal trading in grain sorghum is widespread, and the Rural Marketing and Supply Association in evidence to the Committee estimated that over fifty per cent of grain merchants would be unlicensed and thus illegal traders. The Association further stated:

"I think the main illegal activity would concern the unlicensed merchant buying from growers. ... It is not done behind closed doors. He freely advertises in the newspapers that he is a buyer for sorghum."

Such widespread illegal sales must detract from the effectiveness of the Board in achieving its objectives. The Board claimed that it was unable to gather sufficient evidence of illegal trading under the Act to initiate any prosecutions in 1982-83. However, notwithstanding any difficulties that may exist under the current legislation, the Committee is not satisfied that there was any determined effort by the Board to gather evidence and indeed the Board appeared reluctant to pursue the matter.

The Board's decision in March 1983 to reverse its announcement of September 1982 that no sorghum would be exempted from the vesting provisions of the Act, followed its inability to attract sorghum receivals. Thus trade from this time through licensed merchants was legalised. The alternative was to continue to require total acquisition of the crop by the Board, thereby encouraging growers to trade illegally intrastate or to trade legally interstate where their grain sorghum attracted higher prices.

The Committee recommends that:

THE VESTING PROVISION OF THE
MARKETING OF PRIMARY PRODUCTS
ACT BE RETAINED.

BOARDS BE GIVEN WIDER POWERS UNDER
THE MARKETING OF PRIMARY PRODUCTS ACT
TO ENSURE POLICING OF THE VESTING
PROVISION.

BOARDS PROVIDE EVIDENCE IN THEIR
ANNUAL REPORTS OF THEIR ACTIVITIES
IN RESPECT OF POLICING THE VESTING
PROVISIONS OF THE ACT.

5.4 Communication by the Board

The Board's principal means of communication to producers is by way of newsletters. The frequency of these depends on relevant circumstances but appears to average about two per year. The Board has also formed a Licensed Merchant Liaison Committee in an attempt to improve communication with this sector of the industry. On only one occasion has the Board issued an annual report. This serious deficiency must be overcome so that information on all aspects of the Board's operations are publicly available.

Although the Board has communicated with growers, it has not always included full details of activities which have affected or will affect returns to producers. For example, no formal report was given to growers on the trading losses incurred in 1981-82, the source of financing these losses, their effect on grower returns in that and subsequent seasons, and the total loss of Board reserves, until the Board was in extreme financial difficulties in early 1983. This deliberate withholding of information by the Board about its activities and future viability has damaged its acceptability to both producers and users of grain sorghum, at a time when the Board's future is dependent on the support and trust of these individuals and organizations.

Another frequent criticism by various industry groups and the media over the past two seasons has been the persistent unavailability of the Board Chairman to answer questions relating to policies of the Board and their implementation. This has had the effect of eroding public confidence in the Board.

The importance of effective communication by any organization cannot be over-emphasised. In this area some other Boards have formed Industry Advisory Committees with widespread membership including growers, merchants, processors, and Government to act as an advisory group to the Board on issues affecting, and priorities in, domestic grain marketing. These committees are working efficiently in promoting and discussing industry views before Board policy is implemented or amended. Their usefulness would be severely restricted with regard to exports.

The Committee recommends that:

MARKETING BOARDS FORM INDUSTRY
ADVISORY COMMITTEES TO DISCUSS,
EVALUATE AND ADVISE ON ISSUES
RELATED TO DOMESTIC MARKETING.
THESE COMMITTEES TO INCLUDE:

- GROWERS
- MERCHANTS
- END USERS
- GOVERNMENT
- OTHER RELEVANT PERSONNEL

5.5 Industry Support for the Board

The long term future viability of the Board is dependent on the support of the industry, and especially on the support of the grain sorghum producers. The Board has been created under the Act by producers for the benefit of producers and must therefore be funded by producers.

It is clear that in seasons prior to 1981-82 the producers of grain sorghum benefitted by the marketing activities of the Board through higher prices for their product: that is, by finding alternative markets for sorghum the Board prevented over supply on the local market and hence producers effectively obtained a premium on sales.

During both the 1981-82 and 1982-83 seasons the Board again set out to improve returns to producers by forward contracting to sell grain sorghum. In both seasons supply was much lower than expected (and domestic demand greater than expected) and so the prevailing market price at which producers could sell their crops either to licenced or unlicenced merchants was far greater than the price that the Board could realise for grain delivered to its pool. Consequently, producers did not sell to the Board.

It is clear that producers were happy to take the higher prices that resulted from the Board's activities in the years of abundant supplies but were not willing to financially support the Board in years when grain sorghum was in short supply and the Board was over-committed.

The Committee considers that grain sorghum producers have been very short-sighted in their actions. They have shown a distinct preference for short-term profit maximization instead of long-term profitability and stability. If the Board had gone bankrupt because of the failure of growers to support it in difficult seasons it would have been to the detriment of all growers in the longer term.

This problem is one which the Board and the growers will clearly need to resolve if the long term viability of the Board is to be ensured. However, it is possible that the producers' ignorance of the Board's predicament was largely responsible for the lack of support by growers. This will be remedied to some extent by the implementation of the Committee's recommendation in Section 5.4.

The Committee recommends that:

REGULAR ASSESSMENTS OF GROWER
SUPPORT BE MADE TO DETERMINE
WHETHER THE CONTINUED EXISTENCE
OF THE BOARD IS WARRANTED.

5.6 Duties of Board Members

During the 1981-82 and 1982-83 seasons when the Board found itself unable to meet contractual commitments to supply grain sorghum there was a general failure on the part of producers to deliver their product to the Board rather than to licenced merchants.

Not one of the grower members of the Board who had produced receival standard grain delivered his own crop to the Board's pool in the 1981-82 and 1982-83 seasons. It is also clear that a number of grower Board members contracted to sell their own crops to licenced merchants at a time when they knew the Board was desperately short of grain sorghum.

The actions of these Board members cannot be said to have been illegal as they sold their crops to licenced merchants approved by the Board. Further, it is doubtful whether they were in breach of any legal duty as Board members. This view is based on advice received from the Crown Solicitor.

Certainly, the Board members felt that they had no obligation or duty to deliver their crops to the Board. This view is exemplified by the evidence Mr Hamparsum (Board member) gave when asked whether he had an obligation to deliver the grain he had available to the Board, to enable it to meet its commitments. He stated:

"No, I did not ... As the principal of my family company, a grower of sorghum and a board member, I have an option, and a responsibility, in two places. I agree there is a conflict of interest to make a decision to market the grain. In my own case I was well aware of the forward commitments of the board in 1982 and 1983 at all times. However, as a grower, I have to consider the options. I have grain storage, but I do also have commitments in my own business - commitments of money. If I look at two situations where I can market my grain, one is to put it into the government silos".

He went on to say:

" ... No, I did not feel any obligations to deliver grain to the Board's pool, because to have done so would have represented a seriously lower price for my sorghum than I could have obtained through the Board's licensed merchants system".

Although this view was generally supported by all other Board members, one of them (a non-grower) did concede that growers had a moral obligation to support the Board even if this meant delivering their grain to the pool rather than to licensed merchants.

After considering the various arguments the Committee has come to the view that the actions of the Board members are questionable on a number of grounds:

1. In view of the fact that grower Board members were acutely aware of the predicament it seems that they had at least a moral obligation to deliver their grain sorghum to the Board in order to secure the Board's financial survival: that is, if it is assumed that it was in the interests of grain sorghum growers that the Board survive then the Board members were not acting in the interests of the growers by not delivering their grain to the Board's pool.
2. The Board's failure to adequately inform other growers of the Board's predicament meant that the same obligation to deliver to the Board's pool did not apply to most of the growers. Hence, potential support may have been lost.
3. When the Board revoked the vesting provision on 2 March 1983 it did so in the belief that the Board could not attract any grain. A number of growers Board members soon after entered into contracts with licensed merchants for the sale of their own grain sorghum. Clearly, if the revocation was prompted by the self-interest of those Board members, then it would have been a breach of fiduciary duty to the Board on the part of those Board members.

However, while the Committee has been unable to establish any such breach on the part of Board members it is seriously concerned that the Board failed to take any other action at the time of revoking the vesting provision to ensure that financial support from growers was forthcoming. Given that producers again had the option of selling to licensed merchants instead of to the Board, it seems that the licensed merchant system should have been used to subsidise the losses being incurred by the Board due to its failure to attract supplies of grain. For example, the fee charged by the Board for sales through licensed merchants could have been increased. This did not occur.

The Committee recommends that:

THE DUTIES OF MEMBERS OF MARKETING
BOARDS BE INVESTIGATED AND PRESCRIBED
IN THE NEW MARKETING OF PRIMARY PRODUCTS
ACT. THE DUTIES TO INCLUDE:

- * A DUTY TO INFORM PRODUCERS

- * A DUTY TO DO ALL THAT IS REASONABLY
POSSIBLE AS INDIVIDUALS TO SEE THAT
THE BOARD PROSPERS.

ANY CANDIDATES FOR ELECTION TO THE
BOARD DISCLOSE THEIR DEALINGS WITH
THE BOARD FOR THE TWELVE MONTHS PRIOR
TO EACH ELECTION AND THAT BOARD MEMBERS
DISCLOSE THEIR DEALINGS WITH THE BOARD
ANNUALLY.

FAILURE OF BOARD MEMBERS TO DELIVER
THEIR GRAIN SORGHUM TO THE BOARD, AT
TIMES WHEN ALL MARKETING ACTIVITIES
ARE VESTED IN THE BOARD, BE GROUNDS
FOR THEIR REMOVAL AND INELIGIBILITY
FOR RE-ELECTION.

5.7 Power to Accumulate Reserves

Under the present Act all proceeds from the sale of a pool must be disbursed to producers delivering to that pool. This severely limits the scope for Boards to amass accumulated reserves. The Grain Sorghum Marketing Board did not have access to other means, such as Export Market Development Grants, to accumulate general reserves.

The provision of reserves by commercial organizations is normal business practice. They can be used to finance unexpected or extraordinary expenditure necessary to enable that organization's continued existence and operation. The Board could have used reserves to finance purchases to honour contracts in 1982-83 for example, which would have minimised disruption to domestic grain sorghum marketing arrangements.

The Committee recommends that:

BOARDS BE PERMITTED UNDER THE
MARKETING OF PRIMARY PRODUCTS
ACT TO ACCUMULATE GENERAL RESERVES,
SUBJECT TO DEVELOPMENT OF GUIDELINES
BY THE DEPARTMENT GOVERNING AMOUNTS
AND TYPES OF DEDUCTIONS WHICH CAN
CONTRIBUTE TO RESERVES.

The accumulation of general reserves and their expenditure could still be evaluated under the proposed Annual Reports Act. In addition, growers have the opportunity to show their judgement of all Board actions at elections every three years.

5.8 Future Viability of the Board

The Board's future viability is dependent on two contingencies. First, the Board and its financiers must negotiate an arrangement which is acceptable to the Board's creditors and which can be implemented over time. Second, grain sorghum producers must commit themselves to support the Board, to financially assist with the present debt and to continue deliveries to the Board's receival system.

The Committee does not consider that a detailed examination of the proposed scheme to allow the Board to continue operations falls within the Terms of Reference of the current Report.

The question of a Government guarantee to assist the Board out of its current difficulties was raised during the Committee's hearings. However, neither the Board members nor any of the growers' representatives supported this course.

5.9 Other Legal Issues

In the course of the inquiry the Committee developed doubts concerning the legality of a number of procedures adopted by the Board.

The first of these doubts concerns the procedure through which the Board exempted producers of grain sorghum from delivering to the Board's pool thus allowing them to sell their grain sorghum to licensed merchants. The procedures to be followed are given in the Grain Sorghum Marketing Board Regulations, 1972.

The relevant regulations are as follows:

"Exemptions

22. Exemption from the operation of section 11 of the Act may be granted by the Board in the following cases:-
- (a) where the board is of the opinion that acquisition or disposal of any grain sorghum is impractical, uneconomic or otherwise undesirable;
 - (b) where the grain sorghum is grain sorghum required by the producer thereof for his own use within the confines of his own property for live-stock feeding or as seed;
 - (c) where sales of grain sorghum are made in New South Wales by the producer thereof through marketing agents appointed by the Board for that purpose.

Application for exemption under reg.22(a)

23. Application for exemption pursuant to paragraph (a) of Regulation 22 shall be made in such manner as the Board may require.

Requirements for exemption under reg.22(c)

24. No exemption from the operation of section 11 of the Act shall be granted by the Board with respect to any case specified in paragraph (c) of Regulation 22 unless the producer -
- (a) makes application to the Board therefor;
 - (b) has paid all moneys payable by him to the Board;
 - (c) has complied with all the provisions of the Act and these Regulations;
 - (d) agrees with the Board that the grain sorghum in respect of which the desired exemption is to apply shall not be sold by him otherwise than at such prices and in accordance with such terms and conditions as are for the time being approved by the Board."

The Committee has received no evidence that the procedure required by S.24(a) was correctly adhered to although there appears little doubt as to the intentions of the Board. In order that the Board be in a sound legal position in the event of prosecutions for illegal sales it is important that the procedure adopted for exempting grower producers be strictly in accordance with the Act. This is a matter that needs attention although it is not proposed to pursue it further in this Inquiry.

The second concern of the Committee relates to the power of the Board to vest all of the crop during a particular season after some producers have already contracted to sell their crops. This matter too needs further attention.

6. APPENDICES

	<u>Page</u>
1. Terms of Reference from the Minister for Agriculture and Fisheries.	42
2. Points of Particular Interest to the Public Accounts Committee in its Inquiry.	43
3. Written Submissions Received by the Public Accounts Committee.	44
4. Parties who have Presented Oral Submissions Heard by the Public Accounts Committee.	45
5. Trade Creditors of the Grain Sorghum Marketing Board for the State of New South Wales.	46
6. Sundry Creditors of the Grain Sorghum Marketing Board for the State of New South Wales.	47
7. Summary of Grain Handled Through the Grain Sorghum Marketing Board's System (Tonnes).	48
8. Example of Futures Trading when a Forward Contract Involving "Basis Pricing" is held.	49
9. Example of Futures Trading Without a Forward Contract being held.	51

APPENDIX 1: TERMS OF REFERENCE FROM THE MINISTER



Minister for Agriculture and Fisheries
New South Wales

MAE.1258

Mr M.R. Egan, Esq., B.A., M.P.,
Chairman,
Public Accounts Committee,
N.S.W. Legislative Assembly,
Parliament House,
SYDNEY. N.S.W. 2000

12 APR 1983

Dear Mr Egan,

I refer to our discussion of Wednesday, March 23, regarding the activities of Marketing Boards formed under the Marketing of Primary Products Act in relation to the investigation the Public Accounts Committee is currently undertaking regarding reporting requirements of statutory bodies.

As I indicated in our discussion, I have prepared proposals for a new Marketing of Primary Products Act for consideration by Cabinet. Included in the proposals are increased public accountability requirements for Marketing Boards, such as the publication of annual reports, a report to Parliament of the Boards' activities and the possibility of the Minister for Agriculture initiating investigations into Board activities.

During our discussion you asked a number of specific questions concerning the Grain Sorghum Marketing Board. Following our meeting I have received a report on the Grain Sorghum Marketing Board from the Auditor General indicating the Board is in a very difficult financial situation. I believe it would assist me if you could further investigate and report on the Grain Sorghum Marketing Board. Therefore, I seek you to enquire into the administration and operations of the Grain Sorghum Marketing Board and any other matters which affect the Grain Sorghum Marketing Board's efficiency, effectiveness and accountability.

Officers of my Department will be available to assist you in your investigations into the Grain Sorghum Marketing Board. I have also attached a copy of the Auditor General's report on the Board which may assist you in your investigations.

Yours faithfully,

A handwritten signature in dark ink, appearing to read 'J.R. Hallam', with a long horizontal flourish extending to the right.

J.R. HALLAM, M.L.C.,
MINISTER FOR AGRICULTURE & FISHERIES.

APPENDIX 2: POINTS OF PARTICULAR INTEREST TO THE
PUBLIC ACCOUNTS COMMITTEE IN ITS INQUIRY

As you will be aware from recent press advertisements, the Public Accounts Committee has received a reference from the Minister for Agriculture and Fisheries under Section 16D of the Audit Act to inquire into the administration and operations of the Grain Sorghum Marketing Board for the State of New South Wales, and other matters which affect that Board's efficiency, effectiveness and accountability.

The Minister's reference to the Committee arises as a result of the Board's inability to meet contractual obligations and its accumulated financial position. The Committee will therefore be concentrating its investigations on activities undertaken by the Board during the 1981-82 and 1982-83 crop seasons. There are three particular areas the Committee will be examining; namely

- * documentation of the Board's activities during this time.
- * an analysis of the reasons for, and justifications of, these activities.
- * an examination of current reporting requirements and legislation applying to Marketing Boards, and their apparent deficiencies.

The Committee requests your consideration and response to the above issues, together with any additional comments and/or suggestions you may wish to make in relation to the subject matter of the Inquiry.

I thank you in anticipation of your co-operation and look forward to your participation in the Inquiry.

APPENDIX 3: WRITTEN SUBMISSIONS RECEIVED BY THE
PUBLIC ACCOUNTS COMMITTEE

Listed in order of receipt.

Mr H.J. Burke

The Livestock and Grain Producers' Association
of New South Wales

Australian Poultry Industries Association

Grain Sorghum Marketing Board for the State
of New South Wales

Grain and Feed Trade Association of New South Wales

Grain Handling Authority of New South Wales

Gatenby Bros Pty Ltd

Stock Feed Manufacturers' Association of New South Wales

Rural Marketing and Supply Association

The Oats Marketing Board for the State of New South Wales

Australian Grain Exporters Association

Department of Agriculture, New South Wales

Kimpton Grain Company

Westpac Banking Corporation

APPENDIX 4: PARTIES WHO HAVE PRESENTED ORAL
 SUBMISSIONS HEARD BY THE
 PUBLIC ACCOUNTS COMMITTEE

Department of Agriculture, New South Wales

Gatenby Bros Pty Ltd

Grain Sorghum Marketing Board for the State
of New South Wales

The Livestock and Grain Producers' Association
of New South Wales

Rural Marketing and Supply Association

APPENDIX 5: TRADE CREDITORS OF THE GRAIN SORGHUM
MARKETING BOARD FOR THE STATE
OF NEW SOUTH WALES
(AS AT 8 AUGUST, 1983)

<u>CREDITOR</u>	<u>AMOUNT</u>
Gatenby Bros Pty Ltd	A\$ 848,916.00
Inghams Enterprises Pty Ltd	A\$ 420,566.81
K.M.M. Pty Ltd	A\$ 245,900.00
Bunge (Australia) Pty Ltd	A\$ 141,000.00
Allied Mills Industries Pty Ltd	A\$ 97,000.00
Peter Schwarz (Overseas) Pty Ltd	A\$ 43,800.00
Mallorca Enterprises Pty Ltd	U.S.\$ 806,847.77
	<hr/>
TOTAL	A\$1,797,182.81
	U.S.\$ 806,847.77
	<hr/> <hr/>

APPENDIX 6: SUNDRY CREDITORS OF THE GRAIN SORGHUM
MARKETING BOARD FOR THE STATE OF NEW SOUTH WALES
(AS AT 8 AUGUST, 1983)

SUNDRY CREDITORS	AMOUNT (\$)
Central Queensland Grain Sorghum Marketing Board	54,037.50
E.A. Roche Transport	36,599.88
Agroprom Investments Limited	17,500.00
Australian Wheat Board	16,138.48
Conaust (Australia) Pty Ltd	16,067.65
State Wheat Board of Queensland	12,132.22
Agroprom Pty Ltd	11,235.00
Thomas Corson Holdings Ltd	10,660.00
The Treasury, New South Wales	8,000.00
State Rail Authority of New South Wales	5,530.04
Hogg Robinson CCL	3,884.27
United Press International Inc	2,084.95
Jones Lang Wootton	1,832.74
Automail Pty Ltd	1,683.08
Walter Dickson and Co	1,215.00
State Electoral Office	1,024.68
Grain Handling Authority of New South Wales	945.91
Namoi Aero Club	434.16
The Sydney County Council	291.30
Edward Dight and Co Pty Ltd	51.57
Cabcharge Australia Pty Ltd	22.20
	<hr/>
TOTAL	\$201,370.63

APPENDIX 7: SUMMARY OF GRAIN HANDLED THROUGH THE GRAIN SORGHUM MARKETING BOARD'S SYSTEM

(TONNES)

ALTERNATIVE	1978-79	1979-80	1980-81	1981-82	1982-83*
Pool receivals (Excluding Brisbane and on-farm)	167,861	6,417	15,439	11,406	-
Brisbane receivals	28,934	151	-	1,269	-
On-farm receivals	-	-	1,315	38	-
Cash purchases	-	-	-	16,528	1,060
<hr/> Total grain available to the Board to sell	<hr/> 196,795	<hr/> 6,568	<hr/> 16,754	<hr/> 29,241	<hr/> 1,060
Licensed merchants	128,830	100,023	56,050	110,109	43,933
	<hr/> 325,625	<hr/> 106,591	<hr/> 72,804	<hr/> 139,350	<hr/> 44,993

NOTE * Until 31 July, 1983

APPENDIX 8: EXAMPLE OF FUTURES TRADING WHEN A FORWARD CONTRACT INVOLVING "BASIS PRICING" IS HELD

A contract of 25,000 tonnes (100,000 bushels) has been signed at a price of 10¢ premium over July 1984 Chicago Corn Futures price (contract date of price set by buyer). At the date of signing the contract (1 October, 1983) the July 1984 Chicago Corn Futures price is 270¢ per bushel.

(a) Futures price falls to 250¢ per bushel on day buyer sets contract sale (6 May, 1984)

WITHOUT FUTURES TRADING

6. 5.84 Contract Price = 250¢ + 10¢ per bushel
= 260¢ per bushel.
Total Receipts to Board = 260¢ x 100,000
= \$260,000

WITH FUTURES TRADING

1.10.83 Board sells Futures contract for 100,000 bushels at 270¢ per bushel.
6. 5.84 Board buys Futures contract for 100,000 bushels at 250¢ per bushel.
6. 5.84 Nett profit on futures = 20¢ per bushel
6. 5.84 Contract Price = 250¢ + 10¢ per bushel
= 260¢ per bushel

Total Receipts to Board = Contract Price + Futures Profit
= 260¢ + 20¢ per bushel
= 280¢ per bushel
= \$280,000

(b) Futures price rises to 300¢ per bushel on day
buyer sets contract sale (6 May, 1984)

WITHOUT FUTURES TRADING

6. 5.84 Contract Price = 300¢ + 10¢ per bushel
= 310¢ per bushel.
Total Receipts to Board = 310¢ x 100,000
= \$310,000

WITH FUTURES TRADING

1.10.83 Board sells futures contract for 100,000
bushels at 270¢ per bushel.
6. 5.84 Board buys futures contract for 100,000
bushels at 300¢ per bushel.
6. 5.84 Nett loss on futures = 30¢ per bushel.
6. 5.84 Contract Price = 300¢ + 10¢ per bushel.
= 310¢ per bushel.
Total Receipts to Board = Contract Price - Futures Loss.
= 310¢ - 30¢ per bushel.
= \$280,000.

Note: 1. Futures market commissions not included.
This cost is approximately 0.7¢ per bushel.

APPENDIX 9 · EXAMPLE OF FUTURES TRADING WITHOUT
A FORWARD CONTRACT BEING HELD

The Board expects to have available 10,000 tonnes (40,000 bushels) for sale in May 1984. The current price (1 October, 1983) of 300¢ per bushel for Chicago May 1984 Futures is viewed as a price the Board would be happy to receive on the cash market in May 1984.

(a) Price falls to 285¢ per bushel in May 1984

WITHOUT FUTURES TRADING

6. 5.84 Board sells its 40,000 bushels on the cash market at 285¢ per bushel.

Total Receipts to Board = 40,000 x 285¢
= \$114,000.

WITH FUTURES TRADING

1.10.83 Board sells futures contract for 40,000 bushels at 300¢ per bushel.

6. 5.84 Board buys futures contract for 40,000 bushels at 285¢ per bushel.

Nett profit on futures = 15¢ per bushel.

6. 5.84 Board sells its 40,000 bushels on the cash market at 285¢ per bushel.

Total Receipts to Board = Cash Sale + Futures Profit
= 285¢ + 15¢ per bushel
= 300¢ per bushel
= \$120,000

(b) Price rises to 315¢ per bushel in May 1984

WITHOUT FUTURES TRADING

6. 5.84 Board sells its 40,000 bushels on the cash market at 315¢ per bushel.

Total Receipts to Board = $315¢ \times 40,000$
= \$126,000.

WITH FUTURES TRADING

1.10.83 Board sells futures contract for 40,000 bushels at 300¢ per bushel.

6. 5.84 Board buys futures contract for 40,000 bushels at 315¢ per bushel.

Nett loss on futures = 15¢ per bushel.

6. 5.84 Board sells its 40,000 tonnes on the cash market at 315¢ per bushel.

Total Receipts to Board = Cash Sale - Futures Loss
= $315¢ - 15¢$ per bushel
= 300¢ per bushel
= \$120,000

- Notes:
1. Futures market commissions not included. This cost is approximately 0.7¢ per bushel.
 2. The usual situation is for the futures price to equate the cash price when both are the same month.

1982-83

PARLIAMENT OF NEW SOUTH WALES

EIGHTH REPORT

OF THE

PUBLIC ACCOUNTS COMMITTEE

OF THE

FORTY-SEVENTH PARLIAMENT

*(INQUIRY INTO REFERENCE BY THE MINISTER FOR AGRICULTURE
AND FISHERIES TO THE COMMITTEE UNDER THE PROVISIONS OF
SECTION 16 OF THE AUDIT ACT, 1902)*

ORDERED TO BE PRINTED, NOVEMBER, 1983

MEMBERS OF THE COMMITTEE

MR M.R. EGAN, B.A., M.P. (Chairman)

MR J.J. AQUILINA, B.A., Dip. Ed., M.P.

MR J.C. BOYD, M.P.

MR P.E.J. COLLINS, B.A., LL.B., M.P.

MR S.T. NEILLY, AASA, M.P.

TRANSCRIPTS OF EVIDENCE TABLED
TOGETHER WITH THIS REPORT.

CONTENTS

	<u>Page</u>
1. RECOMMENDATIONS	1
2. BACKGROUND TO THE REPORT/SUMMARY	5
3. CONDUCT OF THE INQUIRY	9
4. SUMMARY OF THE BOARD'S ACTIVITIES	10
4.1 Constitution and Establishment	10
4.2 Legislation	11
4.3 Functions of the Board	11
4.4 Operations of the Board	12
4.5 Activities in the 1981-82 Crop Season	12
4.6 Activities in the 1982-83 Crop Season	15
5. ANALYSIS OF THE BOARD'S ACTIVITIES	18
5.1 Forward Contracts	18
5.2 Futures Trading	22
5.3 Illegal Sales	27
5.4 Communication by the Board	29
5.5 Industry Support for the Board	31
5.6 Duties of Board Members	33
5.7 Power to Accumulate Reserves	37
5.8 Future Viability of the Board	38
5.9 Other Legal Issues	39
6. APPENDICES	41
1. Terms of Reference	42
2. Points of Interest	43
3. Submissions Received	44
4. Parties who Presented Evidence	45
5. Trade Creditors of the Board	46
6. Other Creditors of the Board	47
7. Grain Deliveries in Recent Years	48
8. Futures Trading Involving Forward Contracts	49
9. Futures Trading Without Forward Contracts	51

1.

RECOMMENDATIONS

The following recommendations have been specifically framed to apply to all Boards constituted under the Marketing of Primary Products Act, and do not apply only to the Grain Sorghum Marketing Board.

1. Boards continue to be permitted to negotiate forward contracts in the commodity which they were established to regulate.
(Refer page 19)
2. Boards be permitted to negotiate forward contracts in commodities other than that which they were established to regulate only with the approval of the Minister.
(Refer page 19)
3. Forward contracts be related to expected Board receivals, and not to expected production in New South Wales.
(Refer page 22)
4. The Department of Agriculture formulate rules governing futures trading.
(Refer page 22)
5. The rules for futures trading stipulate the commodities in which the Board is permitted to trade.
(Refer page 23)

6. All futures market transactions by a Board be recorded in a register including details of -
 - date of transaction
 - quantity
 - futures delivery month
 - price
 - reason for transaction
 - other party
 - commission
 - broker(Refer page 24)

7. Copies of the Futures Market Register be forwarded monthly to the Auditor General and the Minister for Agriculture for evaluation of the legality and effectiveness of the Board's trading.
(Refer page 25)

8. A summary of futures trading activities be included with each Board's annual statements of account.
(Refer page 25)

9. Bank hedge operations be subject to the same requirements as those recommended for futures market transactions.
(Refer page 26)

10. The vesting provision of the Marketing of Primary Products Act be retained.
(Refer page 29)

11. Boards be given wider powers under the Marketing of Primary Products Act to ensure policing of the vesting provision.
(Refer page 29)

12. Boards provide evidence in their Annual Reports of their activities in respect of policing the vesting provisions of the Act.
(Refer page 29)

13. Boards form Industry Advisory Committees to discuss, evaluate and advise on issues related to domestic marketing. These Committees to include:
 - growers
 - merchants
 - end users
 - government
 - other relevant personnel(Refer page 31)

14. Regular assessments of grower support be made to determine whether the continued existence of the Board is warranted.
(Refer page 33)

15. The duties of members of Marketing Boards be investigated and prescribed in the Marketing of Primary Products Act. The duties to include:
 - a duty to inform growers
 - a duty to do all that is reasonably possible as individuals to see that the Board prospers.(Refer page 36)

16. Any candidates for election to the Board disclose their dealings with the Board for the twelve months prior to each election and that Board members disclose their dealings with the Board annually.
(Refer page 36)

17. Failure of Board members to deliver their grain sorghum to the Board, at times when all marketing activities are vested in the Board, be grounds for their removal and ineligibility for re-election.
(Refer page 36)

18. Boards be permitted under the Marketing of Primary Products Act to accumulate general reserves, subject to development of guidelines by the department governing amounts and types of deductions which can contribute to reserves.
(Refer page 37)

2. BACKGROUND TO THE REPORT/SUMMARY

This Report arises from a reference by the Minister for Agriculture and Fisheries, the Honourable J.R. Hallam, M.L.C., to the Public Accounts Committee to inquire into the administration and operations of the Grain Sorghum Marketing Board and any other matters which affect that Board's efficiency, effectiveness and accountability. (Appendix 1).

Prior to the reference the Minister foreshadowed the introduction of a new Marketing of Primary Products Act to govern the operations of all Marketing Boards constituted under that Act. The Committee accordingly sought to analyse the factors contributing to the Board's precarious financial position, and to formulate recommendations which would be applicable to all Boards. These recommendations have been developed with the aim of minimising the likelihood of another Board repeating the Grain Sorghum Marketing Board's errors.

The operations of marketing boards in New South Wales, other States and the Commonwealth have attracted increasing scrutiny in recent years. Attention has focussed on their failure to disclose certain trading activities (e.g. futures market trading), their methods of determining contracts and claims of their inefficiency and uselessness.

Since the date of the grain sorghum reference another two large rural marketing organizations have reported severe financial shortfalls. These are the Central Queensland Grain Sorghum Marketing Board and the Queensland Graingrowers Association. Their problems also relate to financial losses incurred in both meeting forward contracts and from commodity and financial futures trading operations and bank hedging operations. The proposed recommendations for inclusion in the new Act should clarify the use, limitations and role of futures market trading.

The Grain Sorghum Board's present predicament is the result of several different factors. The principal problem has arisen from the Board's having received insufficient grain sorghum from producers in New South Wales to meet forward contract commitments in both 1981-82 and 1982-83. Losses of approximately \$900,000 were incurred in 1981-82 from purchasing grain sorghum interstate to meet commitments, and losses of approximately \$2.7 million were incurred in 1982-83 in failing to honour contractual commitments.

Recent amendments to the Audit Act have given the Committee the power to initiate its own enquiries. The Committee will therefore be monitoring the future performance of Marketing Boards as measured against objectives and goals.

The volume of grain sorghum forward contracted in 1981-82 indicated that the Board was optimistic, rather than realistic, about the volume to be received. The Board's actions in forward contracting significant volumes in both seasons without either physical stocks or substantial reserves clearly exposed it to substantial risk.

Drought conditions reduced grain sorghum production in both seasons, although production in New South Wales substantially exceeded contracted volume. The real shortfalls were caused by producers (including all producer members of the Board) failing to deliver to the Board. This demonstrates lack of confidence in the Board and its ability to obtain maximum prices for producers.

The Board's futures trading activities did not contribute significantly to its weak financial position. However, these activities had been undertaken without any advice as to the legality of the Board's futures trading operations. The Board has also displayed some reluctance to acquaint growers and other sections of the industry with timely details of all their activities. Indeed the specifics of some activities appear to have been withheld from producers for as long as possible, particularly the method of financing 1981-82 trading losses.

3. CONDUCT OF THE INQUIRY

Notices of the Committee's inquiry and invitations for submissions were placed in selected national, metropolitan and regional press. Interested parties were forwarded a letter outlining the points of particular interest to the Committee in this inquiry (Appendix 2). In addition, the Committee wrote to: all Marketing Boards in New South Wales constituted under the Marketing of Primary Products Act; the major trade creditors of the Grain Sorghum Marketing Board; financial, grain handling, market consulting, and advisory organizations associated directly with the Board's activities; and to the various associations representing grain sorghum trading merchants and producers of grain sorghum.

The Committee ultimately received fourteen submissions relating to this inquiry. The organizations and individuals who made submissions are listed in Appendix 3. Most significantly assisted the Committee in the preparation of its report. From the written submissions received by the Committee, five parties were requested to give oral evidence at the public hearings held by the Committee (Appendix 4).

4.2 Legislation

The Board is one of nine Marketing Boards in New South Wales constituted under the Marketing of Primary Products Act, 1927, as amended. This Act provides that grain sorghum produced in New South Wales shall be divested from the producers and become absolutely vested in, and the property of, the Board. Grain sorghum may only be exempted from these vesting provisions at the discretion of the Board, although prior to the 1982-83 season the Board issued exemptions for sales through merchants licensed by the Board. Essentially, then, all grain sorghum in New South Wales must by law be sold to and through the Grain Sorghum Marketing Board.

4.3 Functions of the Board

The functions of the Board, as stated in its submission to the Committee, are:

- "1. To make appropriate and adequate arrangements for the disposal of the New South Wales grain sorghum crop.
2. To arrange for the sale of grain sorghum vested in it or delivered or to be delivered to it, with the object of achieving the highest possible return to producers.
3. To promote the production of grain sorghum in New South Wales and to promote the use of grain sorghum and its products in Australia and overseas.
4. To arrange for the receipt, handling, storage, protection and transportation of New South Wales grain sorghum.
5. To determine and administer quality standards for New South Wales grain sorghum.
6. To arrange financial accommodation to enable the prompt payment of first advance to growers for grain sorghum delivered to the Board and to enable ongoing administrative expenses to be met until seasonal pools can be finalised."

The Committee noted that these functions empowered the Board to deal in no commodity other than grain sorghum.

4.4 Operations of the Board

The Board has developed, over a number of years, a range of grain sorghum marketing alternatives for producers. These alternatives have included:

1. Seasonal pools
2. On-farm storage seasonal pools
3. Brisbane direct deliveries for export
4. Cash price option
5. Licensed merchant system

The first three marketing alternatives are offered by the Board; the fourth is offered by the Board's subsidiary company, the Grain Sorghum Trading Company; and the final alternative is selling to a merchant licensed by the Board. The amounts of grain sorghum handled by each marketing alternative for the last five years are presented in Appendix 7.

4.5 Activities in the 1981-82 Crop Season

(a) Forward contracts - In late December 1981 when the New South Wales grain sorghum crop was progressing well, the Board sold three export cargoes totalling 75,000 tonnes for shipment during March/April/May 1982. No forward domestic contracts were negotiated at this time. The export cargoes were sold to Dreyfus (two) and the Queensland Graingrowers Association (one).

During early 1982 it became apparent that the Board would have difficulty in accumulating sufficient grain to meet its commitments. One shipment of 25,000 tonnes was deferred from March to April at no penalty and at the same time a second cargo was deferred from April to June by selling a June cargo to Pynstorm Pty Ltd and buying an April cargo from the Queensland Graingrowers Association. The Board covered these three contracts by buying a cargo from the Central Queensland Grain Sorghum Marketing Board, buying another cargo from the Queensland Graingrowers Association, and a combination of pool receivals and local cash purchases on behalf of the Board by Gatenby Bros Pty Ltd.

Following completion of the export programme in June 1982, the Board negotiated a forward export commitment of 25,000 tonnes with Mallorca Enterprises Pty Ltd for shipment in June 1983.

(b) Futures trading - The Board has been engaged in futures trading since 1978. This trading involves participation on the corn futures market of the Chicago Futures Market and the bank hedge market in Sydney. The sales and purchases relating to the forward contracts outlined earlier were negotiated at a price relative to Chicago corn futures prices. The prices concerned were expressed in United States currency and the Board's currency exposure was progressively hedged on the Sydney bank hedge market with Westpac Banking Corporation and Elders Finance Pty Ltd.

(c) Board receivals - The total quantity of grain sorghum delivered by the Board against the export sales, and later small domestic sales, was 99,471 tonnes. This quantity comprised pool receivals of 12,714 tonnes, local cash purchases of 16,528 tonnes, and interstate purchases of 70,329 tonnes. The local purchases were negotiated by Gatenby Bros Pty Ltd at a commission of \$2 per tonne, while the interstate purchases were made in Queensland from the Queensland Graingrowers Association and the Central Queensland Grain Sorghum Marketing Board.

(d) Financial position - the total net loss incurred by the Board in respect of covering the contract commitments was approximately \$905,500. This amount included a loss of \$325,459 on its currency hedge operations, and a net profit of \$151,269 on its Chicago Futures Market operations, as outlined in the Auditor-General's 1982-83 Report.

The forward contract with Mallorca Enterprises Pty Ltd, for June 1983 delivery, involved a pre-payment of U.S.\$800,000 (which converted to A.\$838,422). This pre-payment was used for financial accommodation by the Board, with the balance of the shortfall being met from the Board's funds. The balance of accumulated reserves held by the Board after final payments to growers relating to 1982 pool deliveries was approximately \$16,405.

4.6 Activities in the 1982-83 Crop Season

(a) Forward contracts - Against a background of anticipated record grain sorghum plantings and expected downward price pressure at harvest, the Board decided, in September 1982, to acquire the New South Wales sorghum crop in the 1982-83 crop season. That is, no grain sorghum would be exempted from the vesting provisions of the Marketing of Primary Products Act.

In addition to the overseas contract of 25,000 tonnes for June 1983 delivery, the Board negotiated in January 1983 a number of forward contracts with various local buyers for delivery from March to July 1983. These forward domestic contracts totalled 43,500 tonnes to the following buyers:

Gatenby Bros Pty Ltd	20,000 tonnes
Inghams Enterprises Pty Ltd	10,000 tonnes
K.M.M. Pty Ltd	5,000 tonnes
Bunge (Australia) Pty Ltd	3,000 tonnes
Gurley Feedlot	2,500 tonnes
Allied Mills Industries Pty Ltd	2,000 tonnes
Peter Schwarz (Overseas) Pty Ltd	1,000 tonnes

(b) Futures trading - The Board again engaged in futures trading activities on the Chicago Futures Market. These activities included transactions on both the corn futures and wheat futures markets. The overseas contract with Mallorca Enterprises Pty Ltd was expressed in United States currency and the Board's currency exposure was hedged on the Sydney bank hedge market, as in the 1981-82 season.

(c) Board receivals - The Board's voluntary pool received zero deliveries, in response to its advertised first advance payment. The Board, through the Grain Sorghum Trading Company, attempted to buy grain sorghum by making cash price offers of \$93 per tonne on-farm in late January 1983, and \$105 per tonne on-farm on 22 February, 1983, to growers. However total purchases were only 1,060 tonnes. The Board announced on 9 March, 1983 that it was not proceeding with its acquisition of the crop, and the system of sale would revert to an exemption system through licensed merchants.

(d) Financial position - The failure of the Board to attract sufficient grain sorghum to meet its forward contract commitments led to large financial claims against the Board by those firms with dishonoured contracts. These claims related to the difference in cost between the contract price and ruling market prices at the time the contracts should have been delivered against. The Board has admitted liability for these claims which total A.\$1,797,182.81 for the dishonoured domestic contracts and U.S.\$806,847.77 for the dishonoured export contract. Full details of individual claims are detailed in Appendix 5.

At current exchange rates, the total liability of dishonoured contracts is approximately A.\$2.7 million. In addition the Board has a liability of \$201,370.63 to various creditors. Full details of sundry creditors are presented in Appendix 6. The total liability of the Board is therefore approximately \$2.9 million.

When giving evidence to the Committee, the Board indicated assets of approximately \$30,000 cash, and an amount of approximately \$60,000 in a Trust Fund, paid by sorghum producers to be used to finance the Board, if its future was assured. The latter amount was subsequently returned to growers following their failure to adequately respond to the Board's appeal.

Clearly the Board's liabilities far exceed its assets, and various schemes of arrangement between creditors and the Board, which allow the Board to continue trading, are currently being negotiated.

The Board's futures trading operations in corn and wheat futures on the Chicago Futures Market resulted in a total net loss of \$143,182.29.

5. ANALYSIS OF THE BOARD'S ACTIVITIES

5.1 Forward Contracts

Forward selling is a routine part of grain trading, both internationally and domestically. It allows buyers to better plan their operations, through determining inputs in advance and sellers to negotiate more efficient arrangements for storage, freight, and shipping programmes.

Contracts for future delivery are usually for a determined quantity with price negotiated on either of two bases:

1. Fixed price
2. Price relative to Chicago Futures Market quotations ("basis trading")

In both cases the contracts are for determined quantities, for delivery at a set time. In the first instance, the price is also set when the contract is signed, while in the second the price is contracted at a premium over a certain Chicago Futures Market price (for example a contract price of 10 cents per bushel premium over July 1984 Chicago Corn Futures price). Usually the buyer has the option to decide which day, between the signing of the contract and the delivery date, the contract price will be set, and the seller advised that day. Thus the exact price is not known when the forward contract is signed, although the method by which it will be determined is known. In both instances the agreed price (be it either fixed or "basis trading") represents a commercial judgement acceptable to both buyer and seller.

The Committee recommends that:

BOARDS CONTINUE TO BE PERMITTED
TO NEGOTIATE FORWARD CONTRACTS
IN THE COMMODITY WHICH THEY WERE
ESTABLISHED TO REGULATE.

BOARDS BE PERMITTED TO NEGOTIATE
FORWARD CONTRACTS IN COMMODITIES
OTHER THAN THAT WHICH THEY WERE
ESTABLISHED TO REGULATE ONLY WITH
THE APPROVAL OF THE MINISTER.

In the 1981-82 season, the Board forward contracted 75,000 tonnes. The Board's justification for this was to take advantage of favourable current prices, which it did not expect to continue until harvest, and that the contracted amount represented only twenty per cent of expected total grain sorghum production in New South Wales.

Expected price movements require organizations to make commercial judgements, and it is usual in normal circumstances for grain sorghum prices to fall at harvest time, so that the Board's decision relating to price appears a sound one.

The decision to relate contracted tonnage to expected production was however erroneous. The relevant variable is not expected production, but rather expected receivals by the Board as not all the grain sorghum produced in the State is received by the Board. The grain sorghum not delivered to the Board will include grain retained on-farm by producers, interstate sales, and illegal intrastate sales (see section 5.3).

The export contract for 25,000 tonnes for shipment in June 1983 negotiated at the end of the 1981-82 season, involved a large pre-payment of A.\$838,422. This was used for financial accommodation by the Board to cover trading losses in that season. This information was not conveyed to growers at that time and the specific manner of financing the trading losses was not known publicly until March 1983.

In January 1983, the Board forward contracted 43,500 tonnes with various domestic buyers at prices averaging \$93 per tonne on farm. The contract price approximated then current market prices. In total therefore the Board had forward commitments of 68,500 tonnes prior to harvest. The Board had announced in September 1982 that it would not be exempting grain sorghum from the vesting provisions of the Act; that is, all grain sorghum entering trade in New South Wales would, legally, be delivered to the Board through its licensed agents.

While the Committee accepts that it was proper for the details of the arrangement to remain confidential, growers should nevertheless have been informed that the Board had entered into a significant forward commitment involving bridging finances.

Pool receipts by the Board in the five seasons prior to 1982-83 are listed in Appendix 7 and were as follows:

1977-78	56,000 tonnes
1978-79	196,795 tonnes
1979-80	6,568 tonnes
1980-81	16,754 tonnes
1981-82	29,241 tonnes

While the Committee does not oppose the principle of forward selling the decisions to forward sell 75,000 tonnes prior to the 1981-82 harvest and 68,000 tonnes prior to the 1982-83 harvest appear to have been somewhat irresponsible because:

- * Recent history showed that receivals by the Board were far less than the commitments entered into in respect of both the 1981-82 and 1982-83 seasons.

- * The Board should have been aware that on 1 December, 1979, the pricing mechanism used by the Australian Wheat Board for wheat used on the domestic market was lifted to export parity. The higher price of domestic wheat clearly would have made grain sorghum more competitive as a stock feed and hence domestic demand for it would normally have been expected to rise, which it did. This factor was cited by one of the Board members in evidence before the Committee as having caused the short supply of sorghum in the 1981-82 season.

The legal opinion referred to earlier advised that futures trading was legal in relation to the commodity for which the Board was constituted. The Grain Sorghum Marketing Board's futures trading activities have been on the Chicago Futures Market in corn and wheat futures, because there is no futures market for grain sorghum. The Board has frequently stated that it has legal opinion that its corn futures trading activities are legal under the Act. However, the legal opinion obtained referred only to futures trading in the commodity specified under the Act and not to futures trading in a substitute commodity. To state that the Board's futures trading activities are legal, although no legal opinion has been given, is misleading.

The Committee recommends that:

THE RULES FOR FUTURES TRADING
STIPULATE THE COMMODITIES IN
WHICH THE BOARD IS PERMITTED
TO TRADE.

Futures trading activities can be undertaken to complement normal trading activities in the physical commodity in two situations:

- * where a forward contract has been signed by the Board for future delivery at a price relative to a Chicago Futures Market price ("basis trading").

- * where a Board wishes to take advantage of current favourable prices as a basis for signing forward contracts. This is often referred to as a "hedge" situation.

It is important to stress that futures trading, when appropriately used for price insurance, represents one component of a total price fixing process (the other being the cash market price at time of sale, or contract price at delivery). Therefore, net gains or losses on the Chicago Futures Market in each season must not be viewed in isolation, but considered in relation to prices received for the physical commodity. This process is clearly indicated in Appendices 8 and 9.

It is important that all futures market transactions be evaluated both against the set of trading rules recommended earlier and against the aims or reasons for which the transactions were entered into.

The Committee recommends that:

ALL FUTURES MARKET TRANSACTIONS
BY A BOARD BE RECORDED IN A REGISTER
INCLUDING DETAILS OF:

- DATE OF TRANSACTION
- QUANTITY
- FUTURES DELIVERY MONTH
- PRICE
- REASON FOR TRANSACTION
- OTHER PARTY
- COMMISSION
- BROKER

It is recognized that some of the details which would be contained in this proposed register may be commercially sensitive if publicly available. Therefore access to the register may have to be restricted, although a summary of the transactions would not include such details.

The Committee recommends that:

COPIES OF THE FUTURES MARKET REGISTER BE FORWARDED MONTHLY TO THE AUDITOR GENERAL AND THE MINISTER FOR AGRICULTURE FOR EVALUATION OF THE LEGALITY AND EFFECTIVENESS OF THE BOARD'S TRADING.

A SUMMARY OF FUTURES TRADING ACTIVITIES BE INCLUDED WITH EACH BOARD'S ANNUAL STATEMENTS OF ACCOUNT.

A detailed examination has been made of the Board's futures trading activities since 1979. The maximum net exposure by the Board has been less than two export cargoes (50,000 tonnes) in that time.

The Board's futures trading activities can be described as "selective hedging". That is, the Board does not cover all physical commitments on the Chicago Futures Market, but selects those which it believes will benefit through futures trading. This process involves judgements by the Board as to future movements in prices. Similarly the Board times its transactions around expected price movements, in an attempt to maximise futures profits and minimise futures losses through any futures market price variations.

Activities by the Board on the Chicago Futures Market have involved trading in corn and also in 1983 wheat. The Board has argued that prices of these commodities are directly related to grain sorghum prices. The Committee notes that experienced futures market traders caution against participation in one commodity as a means of hedging prices of a different commodity. The Board's activities must therefore also be viewed with some concern from an operational side.

The Board's currency hedging operations for the past two seasons have been performed on the Sydney bank hedge market. The aim of this has been to protect the Board against devaluation of the Australian currency. The bank hedge market is a recent development, which is widely used in commercial circles to minimise currency fluctuation risks. The Board's general activities in this area appear to be prudent.

The Committee recommends that:

BANK HEDGE OPERATIONS BE SUBJECT
TO THE SAME REQUIREMENTS AS THOSE
RECOMMENDED FOR FUTURES MARKET
TRANSACTIONS.

The degree of illegal trading in grain sorghum is widespread, and the Rural Marketing and Supply Association in evidence to the Committee estimated that over fifty per cent of grain merchants would be unlicensed and thus illegal traders. The Association further stated:

"I think the main illegal activity would concern the unlicensed merchant buying from growers. . . . It is not done behind closed doors. He freely advertises in the newspapers that he is a buyer for sorghum.'

Such widespread illegal sales must detract from the effectiveness of the Board in achieving its objectives. The Board claimed that it was unable to gather sufficient evidence of illegal trading under the Act to initiate any prosecutions in 1982-83. However, notwithstanding any difficulties that may exist under the current legislation, the Committee is not satisfied that there was any determined effort by the Board to gather evidence and indeed the Board appeared reluctant to pursue the matter.

The Board's decision in March 1983 to reverse its announcement of September 1982 that no sorghum would be exempted from the vesting provisions of the Act, followed its inability to attract sorghum receivals. Thus trade from this time through licensed merchants was legalised. The alternative was to continue to require total acquisition of the crop by the Board, thereby encouraging growers to trade illegally intrastate or to trade legally interstate where their grain sorghum attracted higher prices.

The Committee recommends that:

THE VESTING PROVISION OF THE
MARKETING OF PRIMARY PRODUCTS
ACT BE RETAINED.

BOARDS BE GIVEN WIDER POWERS UNDER
THE MARKETING OF PRIMARY PRODUCTS ACT
TO ENSURE POLICING OF THE VESTING
PROVISION.

BOARDS PROVIDE EVIDENCE IN THEIR
ANNUAL REPORTS OF THEIR ACTIVITIES
IN RESPECT OF POLICING THE VESTING
PROVISIONS OF THE ACT.

5.4 Communication by the Board

The Board's principal means of communication to producers is by way of newsletters. The frequency of these depends on relevant circumstances but appears to average about two per year. The Board has also formed a Licensed Merchant Liaison Committee in an attempt to improve communication with this sector of the industry. On only one occasion has the Board issued an annual report. This serious deficiency must be overcome so that information on all aspects of the Board's operations are publicly available.

Although the Board has communicated with growers, it has not always included full details of activities which have affected or will affect returns to producers. For example, no formal report was given to growers on the trading losses incurred in 1981-82, the source of financing these losses, their effect on grower returns in that and subsequent seasons, and the total loss of Board reserves, until the Board was in extreme financial difficulties in early 1983. This deliberate withholding of information by the Board about its activities and future viability has damaged its acceptability to both producers and users of grain sorghum, at a time when the Board's future is dependent on the support and trust of these individuals and organizations.

Another frequent criticism by various industry groups and the media over the past two seasons has been the persistent unavailability of the Board Chairman to answer questions relating to policies of the Board and their implementation. This has had the effect of eroding public confidence in the Board.

The importance of effective communication by any organization cannot be over-emphasised. In this area some other Boards have formed Industry Advisory Committees with widespread membership including growers, merchants, processors, and Government to act as an advisory group to the Board on issues affecting, and priorities in, domestic grain marketing. These committees are working efficiently in promoting and discussing industry views before Board policy is implemented or amended. Their usefulness would be severely restricted with regard to exports.

The Committee recommends that:

MARKETING BOARDS FORM INDUSTRY
ADVISORY COMMITTEES TO DISCUSS,
EVALUATE AND ADVISE ON ISSUES
RELATED TO DOMESTIC MARKETING.
THESE COMMITTEES TO INCLUDE:

- GROWERS
- MERCHANTS
- END USERS
- GOVERNMENT
- OTHER RELEVANT PERSONNEL

5.5 Industry Support for the Board

The long term future viability of the Board is dependent on the support of the industry, and especially on the support of the grain sorghum producers. The Board has been created under the Act by producers for the benefit of producers and must therefore be funded by producers.

It is clear that in seasons prior to 1981-82 the producers of grain sorghum benefitted by the marketing activities of the Board through higher prices for their product: that is, by finding alternative markets for sorghum the Board prevented over supply on the local market and hence producers effectively obtained a premium on sales.

During both the 1981-82 and 1982-83 seasons the Board again set out to improve returns to producers by forward contracting to sell grain sorghum. In both seasons supply was much lower than expected (and domestic demand greater than expected) and so the prevailing market price at which producers could sell their crops either to licenced or unlicenced merchants was far greater than the price that the Board could realise for grain delivered to its pool. Consequently, producers did not sell to the Board.

It is clear that producers were happy to take the higher prices that resulted from the Board's activities in the years of abundant supplies but were not willing to financially support the Board in years when grain sorghum was in short supply and the Board was over-committed.

The Committee considers that grain sorghum producers have been very short-sighted in their actions. They have shown a distinct preference for short-term profit maximization instead of long-term profitability and stability. If the Board had gone bankrupt because of the failure of growers to support it in difficult seasons it would have been to the detriment of all growers in the longer term.

This problem is one which the Board and the growers will clearly need to resolve if the long term viability of the Board is to be ensured. However, it is possible that the producers' ignorance of the Board's predicament was largely responsible for the lack of support by growers. This will be remedied to some extent by the implementation of the Committee's recommendation in Section 5.4.

The Committee recommends that:

REGULAR ASSESSMENTS OF GROWER
SUPPORT BE MADE TO DETERMINE
WHETHER THE CONTINUED EXISTENCE
OF THE BOARD IS WARRANTED.

5.6 Duties of Board Members

During the 1981-82 and 1982-83 seasons when the Board found itself unable to meet contractual commitments to supply grain sorghum there was a general failure on the part of producers to deliver their product to the Board rather than to licenced merchants.

Not one of the grower members of the Board who had produced receival standard grain delivered his own crop to the Board's pool in the 1981-82 and 1982-83 seasons. It is also clear that a number of grower Board members contracted to sell their own crops to licenced merchants at a time when they knew the Board was desperately short of grain sorghum.

The actions of these Board members cannot be said to have been illegal as they sold their crops to licenced merchants approved by the Board. Further, it is doubtful whether they were in breach of any legal duty as Board members. This view is based on advice received from the Crown Solicitor.

Certainly, the Board members felt that they had no obligation or duty to deliver their crops to the Board. This view is exemplified by the evidence Mr Hamparsum (Board member) gave when asked whether he had an obligation to deliver the grain he had available to the Board, to enable it to meet its commitments. He stated:

"No, I did not ... As the principal of my family company, a grower of sorghum and a board member, I have an option, and a responsibility, in two places. I agree there is a conflict of interest to make a decision to market the grain. In my own case I was well aware of the forward commitments of the board in 1982 and 1983 at all times. However, as a grower, I have to consider the options. I have grain storage, but I do also have commitments in my own business - commitments of money. If I look at two situations where I can market my grain, one is to put it into the government silos".

He went on to say:

" ... No, I did not feel any obligations to deliver grain to the Board's pool, because to have done so would have represented a seriously lower price for my sorghum than I could have obtained through the Board's licensed merchants system".

Although this view was generally supported by all other Board members, one of them (a non-grower) did concede that growers had a moral obligation to support the Board even if this meant delivering their grain to the pool rather than to licensed merchants.

After considering the various arguments the Committee has come to the view that the actions of the Board members are questionable on a number of grounds:

1. In view of the fact that grower Board members were acutely aware of the predicament it seems that they had at least a moral obligation to deliver their grain sorghum to the Board in order to secure the Board's financial survival: that is, if it is assumed that it was in the interests of grain sorghum growers that the Board survive then the Board members were not acting in the interests of the growers by not delivering their grain to the Board's pool.
2. The Board's failure to adequately inform other growers of the Board's predicament meant that the same obligation to deliver to the Board's pool did not apply to most of the growers. Hence, potential support may have been lost.
3. When the Board revoked the vesting provision on 2 March 1983 it did so in the belief that the Board could not attract any grain. A number of growers Board members soon after entered into contracts with licensed merchants for the sale of their own grain sorghum. Clearly, if the revocation was prompted by the self-interest of those Board members, then it would have been a breach of fiduciary duty to the Board on the part of those Board members.

However, while the Committee has been unable to establish any such breach on the part of Board members it is seriously concerned that the Board failed to take any other action at the time of revoking the vesting provision to ensure that financial support from growers was forthcoming. Given that producers again had the option of selling to licensed merchants instead of to the Board, it seems that the licensed merchant system should have been used to subsidise the losses being incurred by the Board due to its failure to attract supplies of grain. For example, the fee charged by the Board for sales through licensed merchants could have been increased. This did not occur.

The Committee recommends that:

THE DUTIES OF MEMBERS OF MARKETING
BOARDS BE INVESTIGATED AND PRESCRIBED
IN THE NEW MARKETING OF PRIMARY PRODUCTS
ACT. THE DUTIES TO INCLUDE:

- * A DUTY TO INFORM PRODUCERS

- * A DUTY TO DO ALL THAT IS REASONABLY
POSSIBLE AS INDIVIDUALS TO SEE THAT
THE BOARD PROSPERS.

ANY CANDIDATES FOR ELECTION TO THE
BOARD DISCLOSE THEIR DEALINGS WITH
THE BOARD FOR THE TWELVE MONTHS PRIOR
TO EACH ELECTION AND THAT BOARD MEMBERS
DISCLOSE THEIR DEALINGS WITH THE BOARD
ANNUALLY.

FAILURE OF BOARD MEMBERS TO DELIVER
THEIR GRAIN SORGHUM TO THE BOARD, AT
TIMES WHEN ALL MARKETING ACTIVITIES
ARE VESTED IN THE BOARD, BE GROUNDS
FOR THEIR REMOVAL AND INELIGIBILITY
FOR RE-ELECTION.

5.7 Power to Accumulate Reserves

Under the present Act all proceeds from the sale of a pool must be disbursed to producers delivering to that pool. This severely limits the scope for Boards to amass accumulated reserves. The Grain Sorghum Marketing Board did not have access to other means, such as Export Market Development Grants, to accumulate general reserves.

The provision of reserves by commercial organizations is normal business practice. They can be used to finance unexpected or extraordinary expenditure necessary to enable that organization's continued existence and operation. The Board could have used reserves to finance purchases to honour contracts in 1982-83 for example, which would have minimised disruption to domestic grain sorghum marketing arrangements.

The Committee recommends that:

BOARDS BE PERMITTED UNDER THE
MARKETING OF PRIMARY PRODUCTS
ACT TO ACCUMULATE GENERAL RESERVES,
SUBJECT TO DEVELOPMENT OF GUIDELINES
BY THE DEPARTMENT GOVERNING AMOUNTS
AND TYPES OF DEDUCTIONS WHICH CAN
CONTRIBUTE TO RESERVES.

The accumulation of general reserves and their expenditure could still be evaluated under the proposed Annual Reports Act. In addition, growers have the opportunity to show their judgement of all Board actions at elections every three years.

5.8 Future Viability of the Board

The Board's future viability is dependent on two contingencies. First, the Board and its financiers must negotiate an arrangement which is acceptable to the Board's creditors and which can be implemented over time. Second, grain sorghum producers must commit themselves to support the Board, to financially assist with the present debt and to continue deliveries to the Board's receival system.

The Committee does not consider that a detailed examination of the proposed scheme to allow the Board to continue operations falls within the Terms of Reference of the current Report.

The question of a Government guarantee to assist the Board out of its current difficulties was raised during the Committee's hearings. However, neither the Board members nor any of the growers' representatives supported this course.

5.9 Other Legal Issues

In the course of the inquiry the Committee developed doubts concerning the legality of a number of procedures adopted by the Board.

The first of these doubts concerns the procedure through which the Board exempted producers of grain sorghum from delivering to the Board's pool thus allowing them to sell their grain sorghum to licensed merchants. The procedures to be followed are given in the Grain Sorghum Marketing Board Regulations, 1972.

The relevant regulations are as follows:

"Exemptions

22. Exemption from the operation of section 11 of the Act may be granted by the Board in the following cases:-
 - (a) where the board is of the opinion that acquisition or disposal of any grain sorghum is impractical, uneconomic or otherwise undesirable;
 - (b) where the grain sorghum is grain sorghum required by the producer thereof for his own use within the confines of his own property for live-stock feeding or as seed;
 - (c) where sales of grain sorghum are made in New South Wales by the producer thereof through marketing agents appointed by the Board for that purpose.

Application for exemption under reg.22(a)

23. Application for exemption pursuant to paragraph (a) of Regulation 22 shall be made in such manner as the Board may require.

Requirements for exemption under reg.22(c)

24. No exemption from the operation of section 11 of the Act shall be granted by the Board with respect to any case specified in paragraph (c) of Regulation 22 unless the producer -
- (a) makes application to the Board therefor;
 - (b) has paid all moneys payable by him to the Board;
 - (c) has complied with all the provisions of the Act and these Regulations;
 - (d) agrees with the Board that the grain sorghum in respect of which the desired exemption is to apply shall not be sold by him otherwise than at such prices and in accordance with such terms and conditions as are for the time being approved by the Board."

The Committee has received no evidence that the procedure required by S.24(a) was correctly adhered to although there appears little doubt as to the intentions of the Board. In order that the Board be in a sound legal position in the event of prosecutions for illegal sales it is important that the procedure adopted for exempting grower producers be strictly in accordance with the Act. This is a matter that needs attention although it is not proposed to pursue it further in this Inquiry.

The second concern of the Committee relates to the power of the Board to vest all of the crop during a particular season after some producers have already contracted to sell their crops. This matter too needs further attention.

6. APPENDICES

	<u>Page</u>
1. Terms of Reference from the Minister for Agriculture and Fisheries.	42
2. Points of Particular Interest to the Public Accounts Committee in its Inquiry.	43
3. Written Submissions Received by the Public Accounts Committee.	44
4. Parties who have Presented Oral Submissions Heard by the Public Accounts Committee.	45
5. Trade Creditors of the Grain Sorghum Marketing Board for the State of New South Wales.	46
6. Sundry Creditors of the Grain Sorghum Marketing Board for the State of New South Wales.	47
7. Summary of Grain Handled Through the Grain Sorghum Marketing Board's System (Tonnes).	48
8. Example of Futures Trading when a Forward Contract Involving "Basis Pricing" is held.	49
9. Example of Futures Trading Without a Forward Contract being held.	51

APPENDIX 1: TERMS OF REFERENCE FROM THE MINISTER



Minister for Agriculture and Fisheries
New South Wales

MAE.1253

Mr M.R. Egan, Esq., B.A., M.P.,
Chairman,
Public Accounts Committee,
N.S.W. Legislative Assembly,
Parliament House,
SYDNEY. N.S.W. 2000

12 APR 1983

Dear Mr Egan,

I refer to our discussion of Wednesday, March 23, regarding the activities of Marketing Boards formed under the Marketing of Primary Products Act in relation to the investigation the Public Accounts Committee is currently undertaking regarding reporting requirements of statutory bodies.

As I indicated in our discussion, I have prepared proposals for a new Marketing of Primary Products Act for consideration by Cabinet. Included in the proposals are increased public accountability requirements for Marketing Boards, such as the publication of annual reports, a report to Parliament of the Boards' activities and the possibility of the Minister for Agriculture initiating investigations into Board activities.

During our discussion you asked a number of specific questions concerning the Grain Sorghum Marketing Board. Following our meeting I have received a report on the Grain Sorghum Marketing Board from the Auditor General indicating the Board is in a very difficult financial situation. I believe it would assist me if you could further investigate and report on the Grain Sorghum Marketing Board. Therefore, I seek you to enquire into the administration and operations of the Grain Sorghum Marketing Board and any other matters which affect the Grain Sorghum Marketing Board's efficiency, effectiveness and accountability.

Officers of my Department will be available to assist you in your investigations into the Grain Sorghum Marketing Board. I have also attached a copy of the Auditor General's report on the Board which may assist you in your investigations.

Yours faithfully,

A handwritten signature in dark ink, appearing to read 'J.R. Hallam', with a long horizontal flourish extending to the right.

J.R. HALLAM, M.L.C.,
MINISTER FOR AGRICULTURE & FISHERIES.

APPENDIX 2: POINTS OF PARTICULAR INTEREST TO THE
PUBLIC ACCOUNTS COMMITTEE IN ITS INQUIRY

As you will be aware from recent press advertisements, the Public Accounts Committee has received a reference from the Minister for Agriculture and Fisheries under Section 16D of the Audit Act to inquire into the administration and operations of the Grain Sorghum Marketing Board for the State of New South Wales, and other matters which affect that Board's efficiency, effectiveness and accountability.

The Minister's reference to the Committee arises as a result of the Board's inability to meet contractual obligations and its accumulated financial position. The Committee will therefore be concentrating its investigations on activities undertaken by the Board during the 1981-82 and 1982-83 crop seasons. There are three particular areas the Committee will be examining; namely

- * documentation of the Board's activities during this time.
- * an analysis of the reasons for, and justifications of, these activities.
- * an examination of current reporting requirements and legislation applying to Marketing Boards, and their apparent deficiencies.

The Committee requests your consideration and response to the above issues, together with any additional comments and/or suggestions you may wish to make in relation to the subject matter of the Inquiry.

I thank you in anticipation of your co-operation and look forward to your participation in the Inquiry.

APPENDIX 3: WRITTEN SUBMISSIONS RECEIVED BY THE
PUBLIC ACCOUNTS COMMITTEE

Listed in order of receipt.

Mr H.J. Burke

The Livestock and Grain Producers' Association
of New South Wales

Australian Poultry Industries Association

Grain Sorghum Marketing Board for the State
of New South Wales

Grain and Feed Trade Association of New South Wales

Grain Handling Authority of New South Wales

Gatenby Bros Pty Ltd

Stock Feed Manufacturers' Association of New South Wales

Rural Marketing and Supply Association

The Oats Marketing Board for the State of New South Wales

Australian Grain Exporters Association

Department of Agriculture, New South Wales

Kimpton Grain Company

Westpac Banking Corporation

APPENDIX 4: PARTIES WHO HAVE PRESENTED ORAL
 SUBMISSIONS HEARD BY THE
 PUBLIC ACCOUNTS COMMITTEE

Department of Agriculture, New South Wales

Gatenby Bros Pty Ltd

Grain Sorghum Marketing Board for the State
of New South Wales

The Livestock and Grain Producers' Association
of New South Wales

Rural Marketing and Supply Association

APPENDIX 5: TRADE CREDITORS OF THE GRAIN SORGHUM
MARKETING BOARD FOR THE STATE
OF NEW SOUTH WALES
(AS AT 8 AUGUST, 1983)

<u>CREDITOR</u>	<u>AMOUNT</u>
Gatenby Bros Pty Ltd	A\$ 848,916.00
Inghams Enterprises Pty Ltd	A\$ 420,566.81
K.M.M. Pty Ltd	A\$ 245,900.00
Bunge (Australia) Pty Ltd	A\$ 141,000.00
Allied Mills Industries Pty Ltd	A\$ 97,000.00
Peter Schwarz (Overseas) Pty Ltd	A\$ 43,800.00
Mallorca Enterprises Pty Ltd	U.S.\$ 806,847.77
	<hr/>
TOTAL	A\$1,797,182.81
	U.S.\$ 806,847.77
	<hr/> <hr/>

APPENDIX 6: SUNDRY CREDITORS OF THE GRAIN SORGHUM
MARKETING BOARD FOR THE STATE OF NEW SOUTH WALES
(AS AT 8 AUGUST, 1983)

SUNDRY CREDITORS	AMOUNT (\$)
Central Queensland Grain Sorghum Marketing Board	54,037.50
E.A. Roche Transport	36,599.88
Agroprom Investments Limited	17,500.00
Australian Wheat Board	16,138.48
Conaust (Australia) Pty Ltd	16,067.65
State Wheat Board of Queensland	12,132.22
Agroprom Pty Ltd	11,235.00
Thomas Corson Holdings Ltd	10,660.00
The Treasury, New South Wales	8,000.00
State Rail Authority of New South Wales	5,530.04
Hogg Robinson CCL	3,884.27
United Press International Inc	2,084.95
Jones Lang Wootton	1,832.74
Automail Pty Ltd	1,683.08
Walter Dickson and Co	1,215.00
State Electoral Office	1,024.68
Grain Handling Authority of New South Wales	945.91
Namoi Aero Club	434.16
The Sydney County Council	291.30
Edward Dight and Co Pty Ltd	51.57
Cabcharge Australia Pty Ltd	22.20
	<hr/>
TOTAL	\$201,370.63

APPENDIX 7: SUMMARY OF GRAIN HANDLED THROUGH THE GRAIN SORGHUM MARKETING BOARD'S SYSTEM

(TONNES)

ALTERNATIVE	1978-79	1979-80	1980-81	1981-82	1982-83*
Pool receivals (Excluding Brisbane and on-farm)	167,861	6,417	15,439	11,406	-
Brisbane receivals	28,934	151	-	1,269	-
On-farm receivals	-	-	1,315	38	-
Cash purchases	-	-	-	16,528	1,060
<hr/> Total grain available to the Board to sell	<hr/> 196,795	<hr/> 6,568	<hr/> 16,754	<hr/> 29,241	<hr/> 1,060
Licensed merchants	128,830	100,023	56,050	110,109	43,933
	<hr/> <hr/> 325,625	<hr/> <hr/> 106,591	<hr/> <hr/> 72,804	<hr/> <hr/> 139,350	<hr/> <hr/> 44,993

NOTE * Until 31 July, 1983

APPENDIX 8: EXAMPLE OF FUTURES TRADING WHEN A FORWARD CONTRACT INVOLVING "BASIS PRICING" IS HELD

A contract of 25,000 tonnes (100,000 bushels) has been signed at a price of 10¢ premium over July 1984 Chicago Corn Futures price (contract date of price set by buyer). At the date of signing the contract (1 October, 1983) the July 1984 Chicago Corn Futures price is 270¢ per bushel.

(a) Futures price falls to 250¢ per bushel on day buyer sets contract sale (6 May, 1984)

WITHOUT FUTURES TRADING

6. 5.84 Contract Price = 250¢ + 10¢ per bushel
= 260¢ per bushel.
Total Receipts to Board = 260¢ x 100,000
= \$260,000

WITH FUTURES TRADING

1.10.83 Board sells Futures contract for 100,000 bushels at 270¢ per bushel.
6. 5.84 Board buys Futures contract for 100,000 bushels at 250¢ per bushel.
6. 5.84 Nett profit on futures = 20¢ per bushel
6. 5.84 Contract Price = 250¢ + 10¢ per bushel
= 260¢ per bushel

Total Receipts to Board = Contract Price + Futures Profit
= 260¢ + 20¢ per bushel
= 280¢ per bushel
= \$280,000

(b) Futures price rises to 300¢ per bushel on day
buyer sets contract sale (6 May, 1984)

WITHOUT FUTURES TRADING

6. 5.84 Contract Price = 300¢ + 10¢ per bushel
= 310¢ per bushel.
Total Receipts to Board = 310¢ x 100,000
= \$310,000

WITH FUTURES TRADING

1.10.83 Board sells futures contract for 100,000
bushels at 270¢ per bushel.
6. 5.84 Board buys futures contract for 100,000
bushels at 300¢ per bushel.
6. 5.84 Nett loss on futures = 30¢ per bushel.
6. 5.84 Contract Price = 300¢ + 10¢ per bushel.
= 310¢ per bushel.
Total Receipts to Board = Contract Price - Futures Loss.
= 310¢ - 30¢ per bushel.
= \$280,000.

Note: 1. Futures market commissions not included.
This cost is approximately 0.7¢ per bushel.

APPENDIX 9: EXAMPLE OF FUTURES TRADING WITHOUT
A FORWARD CONTRACT BEING HELD

The Board expects to have available 10,000 tonnes (40,000 bushels) for sale in May 1984. The current price (1 October, 1983) of 300¢ per bushel for Chicago May 1984 Futures is viewed as a price the Board would be happy to receive on the cash market in May 1984.

(a) Price falls to 285¢ per bushel in May 1984

WITHOUT FUTURES TRADING

6. 5.84 Board sells its 40,000 bushels on the cash market at 285¢ per bushel.

Total Receipts to Board = 40,000 x 285¢
= \$114,000.

WITH FUTURES TRADING

1.10.83 Board sells futures contract for 40,000 bushels at 300¢ per bushel.

6. 5.84 Board buys futures contract for 40,000 bushels at 285¢ per bushel.

Nett profit on futures = 15¢ per bushel.

6. 5.84 Board sells its 40,000 bushels on the cash market at 285¢ per bushel.

Total Receipts to Board = Cash Sale + Futures Profit
= 285¢ + 15¢ per bushel
= 300¢ per bushel
= \$120,000

(b) Price rises to 315¢ per bushel in May 1984

WITHOUT FUTURES TRADING

6. 5.84 Board sells its 40,000 bushels on the cash market at 315¢ per bushel.

Total Receipts to Board = 315¢ x 40,000
= \$126,000.

WITH FUTURES TRADING

1.10.83 Board sells futures contract for 40,000 bushels at 300¢ per bushel.

6. 5.84 Board buys futures contract for 40,000 bushels at 315¢ per bushel.

Nett loss on futures = 15¢ per bushel.

6. 5.84 Board sells its 40,000 tonnes on the cash market at 315¢ per bushel.

Total Receipts to Board = Cash Sale - Futures Loss
= 315¢ - 15¢ per bushel
= 300¢ per bushel
= \$120,000

- Notes:
1. Futures market commissions not included. This cost is approximately 0.7¢ per bushel.
 2. The usual situation is for the futures price to equate the cash price when both are the same month.