



Australian Government

Food and Grocery Code Consultation Paper



Improving commercial relationships in the food and grocery sector

August 2014



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Consultation paper

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PROVIDING YOUR FEEDBACK

A public consultation process will run from 6 August 2014 to 12 September 2014.

There are two ways that you can get involved. You can provide a formal submission in response to this consultation paper or provide brief comments on key issues via the Treasury website. The closing date for submissions and comments is Friday, 12 September 2014.

SUBMISSIONS TO THIS CONSULTATION PAPER

Throughout this paper there are questions to facilitate and focus submissions. These should be used as a guide when submitting a written response, but input is welcome on all of the issues raised in the paper. There is no limit to the length of submissions.

Submissions emailed electronically are preferred. For accessibility reasons, please email responses in a Word or RTF format. An additional PDF version may also be submitted. Treasury will publish your formal submission on the Treasury website, unless you mark it as confidential.

Please provide submissions to:

Website:	www.treasury.gov.au/ConsultationsandReviews/Consultations
Email:	grocerycode@treasury.gov.au
Mail:	Grocery Code Consultation Paper Small Business, Competition and Consumer Division The Treasury Langton Crescent PARKES ACT 2600

PROVIDING COMMENTS VIA THE TREASURY WEBSITE

If you have views on key issues or experiences that you wish to share, but do not want to prepare a formal submission, you are able to submit brief comments via the Treasury website, at www.treasury.gov.au. Comments lodged through this comments facility will not be published.

PROVIDING A CONFIDENTIAL RESPONSE

All information (including name and address details) contained in formal submissions will be made available to the public on the Australian Treasury website, unless it is indicated that you would like all or part of your submission to remain confidential. Automatically generated confidentiality statements in emails do not suffice for this purpose. Respondents who would like part of their submission to remain confidential should provide this information marked as a separate document.

A request made under the *Freedom of Information Act 1982* (Commonwealth) for a submission marked 'confidential' to be made available will be determined in accordance with that Act.

FACTSHEET

The Treasury has released a short fact sheet to provide an overview of this project and key points about the proposed Food and Grocery Code of Conduct.

The fact sheet can be accessed here: www.treasury.gov.au.

For further information

You may send questions or comments to grocerycode@treasury.gov.au.

Enquiries may also be directed to Treasury on 02 6263 1557.

NEXT STEPS FOLLOWING THE PUBLIC CONSULTATION PROCESS

Stakeholder feedback to the public consultation process will inform the Government's consideration of whether the proposed Grocery Code is an appropriate response to concerns within the food and grocery sector. Once the public consultation process is concluded, further targeted consultation may be necessary to clarify any issues or questions which arise from the initial consultation period.

This consultation paper also represents the Government's Early Assessment Regulation Impact Statement (RIS). The RIS process is part of the Government's firm commitment towards better regulation that delivers net benefits for businesses and the community. The objective of the Early Assessment RIS is to inform the Government's decision about how to proceed with the Grocery Code based on evidence and feedback from stakeholders. This will underpin the subsequent Final Assessment RIS, which will build on this document by discussing the results of the consultation process, the evidence that has been gathered and how the final conclusion is reached.

Both the Early and Final Assessment RIS will be published on the Office of Best Practice Regulation's website.

LIST OF ABBREVIATIONS

ACCC	Australian Competition and Consumer Commission
ACL	Australian Consumer Law
AFGC	Australian Food and Grocery Council
CCA	<i>Competition and Consumer Act 2010</i> (Cth)
Grocery Code	Food and Grocery Code of Conduct
IAMA	Institute of Arbitrators and Mediators Australia
IP	Intellectual Property
NFF	National Farmers' Federation
OBPR	Office of Best Practice Regulation
PGICC	Produce and Grocery Industry Code of Conduct
RIS	Regulation Impact Statement

INTRODUCTION

In recent years there has been public debate about whether the activities of the major supermarket chains are harming suppliers, including primary producers, and leading to outcomes that are not in the long term interests of Australian consumers.

On 18 November 2013, Coles, Woolworths and the Australian Food and Grocery Council (AFGC — the representative body for processed food, drink and grocery manufacturers and suppliers in Australia) provided a jointly-developed *Food and Grocery Code of Conduct* (the Grocery Code) to the Australian Government. This was subsequently redrafted to comply with the legislative framework, and a copy is provided at **Attachment A**.

The proposal brought forward by these industry proponents is for the Government to prescribe the Grocery Code as a voluntary industry code under the *Competition and Consumer Act 2010* (CCA). Being a 'voluntary' code means that once a party 'opts-in' they will be legally bound by the requirements of the code. Being 'prescribed under the CCA' means that the Australian Competition and Consumer Commission (ACCC) and private parties can take enforcement action under the CCA for breaches of the code. There are a range of remedies for breaches of a prescribed industry code, including injunctions and compensation for damages.

The Government welcomes this industry-led response. The proposed Grocery Code represents an important step forward for the industry. However, before Government decides to prescribe an industry code, it is essential to undertake extensive public consultation and rigorous analysis to ensure the Code will be effective in establishing a minimum standard of conduct in the industry and that its benefits outweigh the regulatory costs.

The Government seeks input from interested stakeholders. The intent is to improve the quality of commercial relations between retailers and suppliers without imposing unnecessary compliance costs. This will be achieved by a code that is strict enough to limit undesirable retailer behaviour, while allowing sufficient flexibility to support mutually beneficial supply agreements. Well-functioning markets are often supported by regulation that protects the competitive process and provides incentives for innovation and investment, which in turn enhance the wellbeing of all Australians.

Part A of this consultation paper outlines reported problems in the food and grocery sector and the rationale for Government action.

Part B seeks stakeholders' views on the proposed Grocery Code. The Government will need to be satisfied that the proposed Grocery Code would be effective in addressing and resolving concerns about certain types of dealings in the food and grocery sector before taking it forward.

Part C seeks input on whether there is a more efficient and effective way of addressing concerns within the sector than prescribing a code of conduct that retailers can opt-in to.

Alternative approaches identified in **Part C** are:

- A ‘do-nothing’ option which relies upon existing laws, regulations and codes and the ability of suppliers to resolve disputes with retailers. This approach would not preclude an industry Grocery Code. That is, a code which is not prescribed by regulations under the CCA and not subject to enforcement action by the ACCC. The Produce and Grocery Industry Code of Conduct (PGICC) is an example of a non-prescribed voluntary, industry run code.
- A prescribed mandatory Grocery Code, whereby retailers (as defined by regulations) would be compulsorily bound by the Code, rather than opting in. The Franchising Code of Conduct is an example of a mandatory code that is prescribed by regulations under the CCA. The consequences of breaching a mandatory code are the same as those for breaching a prescribed voluntary code.

Part C of the consultation paper also seeks to establish the regulatory impacts of alternative approaches. Stakeholder feedback is needed on the likely regulatory impacts, in order to inform the Government’s decision making and implementation processes going forward.

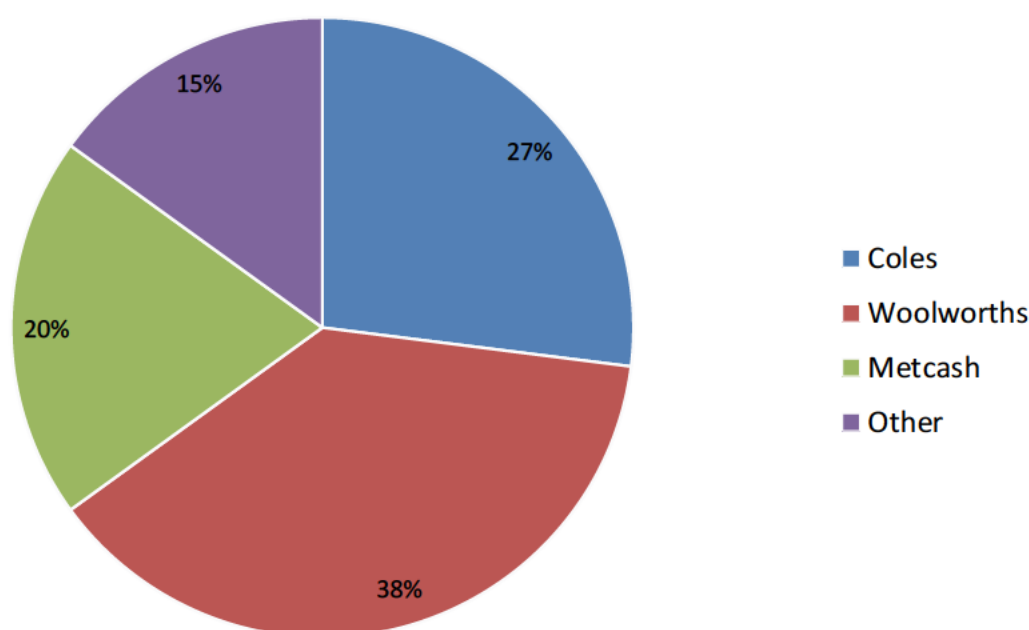
PART A — WHAT IS THE POLICY PROBLEM TO BE SOLVED?

Comparisons across countries suggest that retail grocery markets in Australia are more concentrated than in some other advanced economies.

Coles and Woolworths (the ‘major supermarket chains’) are the largest players in the food and grocery retail market. Other major participants include ALDI, Costco and a number of independent and franchised food and grocery retailers, including those serviced by wholesaler Metcash (further information about these operators is at **Attachment B**). The smallest retailers in the food and grocery retail market are Australia’s convenience stores and corner stores.

Apart from retailers, other key players in the food and grocery sector include a large number of primary producers, food and grocery processors, and manufacturers and wholesalers (collectively referred to in this consultation paper as ‘suppliers’).

GROCERY RETAIL MARKET SHARE IN AUSTRALIA¹



However, there is a range of different estimates of the market share of Coles and Woolworths in different grocery product groups – from approximately 70 per cent for packaged groceries to 50-60 per cent for dairy and deli products; around 50 per cent for fresh meat, and up to 50 per cent for fruit and vegetables, bakery products, and eggs.² In 2012-13 the top two

1 Productivity Commission, *Economic Structure and Performance of the Australian Retail Industry*, Report no. 56, 2011, Canberra, page 37. Note: These figures are for food and liquor, Australian retail market share, major retailers, 2010-11. Measures of market share depend on the definition of market used. Packaged groceries are heavily dominated by Woolworths and Coles; however, they have a less high proportion of market share with respect to fresh groceries.

2 Productivity Commission Inquiry Report into the Economic Structure and Performance of the Australian Retail Industry, No. 56, 4 (2011), page 38.

petrol retailers (Coles Express/Shell, and Woolworths/Caltex) held 48 per cent of retail petrol sales.³

There has been considerable public debate in Australia in recent years about the conduct of retailers during negotiations with suppliers.⁴ This debate has focussed on differences in bargaining power between suppliers and supermarkets (and in some cases between suppliers and wholesalers), and resultant difficulties suppliers may face in negotiating fair trading terms. There are views that grocery suppliers looking to do business in Australia have relatively limited options besides supermarkets to get their product to market, particularly on a national basis.

Due to its relatively small population, and remoteness from centres of global economic activity, Australian markets can tend towards high concentration, with two or three key players and a number of smaller competitors.⁵ In some sectors, this gives key players significant buyer power, known as ‘monopsony power’. Firms may be able to use monopsony power to negotiate lower prices with suppliers or better terms. In the Australian grocery sector, Coles and Woolworths are the dominant buyers and have a degree of monopsony power.⁶

There have been anecdotal claims that some suppliers may have little choice but to accept particular terms for fear of losing contracts, and may similarly be unwilling to complain to the supermarkets, or other bodies to resolve issues or enforce their legal rights during the life of the agreement for fear of retribution.⁷ Some particular concerns reported in recent inquiries include:⁸

- Agreements and understandings that are not in writing or contracts which do not clearly establish the terms which govern the commercial interactions between the parties.
- Unilateral or retrospective contract variation — contracts being changed by retailers without notice or at short notice or those changes being applied retrospectively without supplier consent.
- Late payment by retailers of agreed prices for goods or failure to pay the full amount agreed in respect of the goods.

3 ACCC Report into the prices, costs and profits of unleaded petrol in Australia (December 2013), page lv.

4 This debate has been raised in consultations for the 2008 *Report of the ACCC’s inquiry into the competitiveness of retail prices for standard groceries*; the 2012 Senate Select Committee inquiry into food processing; the 2012 Food Processing Industry Strategy Group report; the former Government’s 2013 National Food Plan; and most recently, by the ACCC in relation to its current investigation of supermarket supplier issues. These issues were noted in Australia’s submission to the OECD Roundtable on Competition Issues in the Food Chain Industry in 2013.

5 Rod Sims, in his 30 October 2013 speech ‘Thoughts on market concentration issues’, stated that “Australia has many markets that are highly concentrated, which is perhaps not surprising given the relative size of our population... supermarkets and liquor are often identified as two such markets”.

6 OECD Policy Roundtable – Monopsony and Buyer Power (2008), document found at: <http://www.oecd.org/daf/competition/44445750.pdf>

7 ACCC, *Report of the ACCC inquiry into the competitiveness of retail prices for standard groceries*, 2008, page 326.

8 ACCC, *Report of the ACCC’s inquiry into the competitiveness of retail prices for standard groceries*, 2008; Senate Select Committee, *Inquiry into food processing report*, 2012; Food Processing Industry Strategy Group, *Final report of the non-Government members*, 2012; and the former Government’s 2013 *National Food Plan*.

- Unfair allocation of risk — contracts requiring payment for matters outside the control of the supplier such as damage, wastage, and shrinkage (e.g. responsibility for theft and loss in store or for retailers’ accounting errors).
- Pressure to agree and threats of adverse outcomes if suppliers do not agree to requests from retailers, or if suppliers make complaints, for example, threats of:
 - de-listing of products;
 - poorer shelf positioning;
 - varying the volume of stock acquired; or
 - cancelling of supply contracts entirely.
- Requiring suppliers to make payments for in-store promotions, marketing and mark-downs when these promotions are the decision of the retailer rather than the supplier.
- Return of unsold goods to suppliers at the suppliers’ expense, including fresh produce that cannot be resold.
- Requiring the disclosure of cost information that may be commercially sensitive to suppliers.
- Requiring profit gap payments or other additional payments from suppliers over and above agreed trading terms to boost the retailer’s earnings and profit margins.
- Conduct associated with retailer own brand products, including in relation to intellectual property rights and the use of confidential information, and product ranging and shelf-space allocation to further retailers’ own brands.

To the extent that these behaviours are present, they may result in inappropriate types and levels of costs and risks being shifted on to the suppliers. Particularly if these types of retailer behaviours occur unexpectedly or recurrently, they could result in serious detriment to suppliers, particularly smaller ones. This includes: forcing suppliers to bear unnecessary costs; inhibiting the ability of suppliers to plan appropriately for their business; increasing variability of cash flow; and imposing additional financing costs.⁹ In turn, this would detract from the incentive for suppliers to invest, innovate, expand capacity or develop new product lines. Ultimately, some suppliers may be forced out of business as a consequence.

There may also be long term detrimental effects for Australian consumers. Erosion of the supplier base, including restrictions on the ability of suppliers to invest, innovate and expand, may result in higher long-run prices; limited product range and variety; poorer quality products; less intense competition between suppliers; and potentially fewer new products coming to the market. This would not be in the long term interests of Australian consumers and may reduce the efficiency of the grocery sector.

⁹ European Commission, *Green paper on unfair trading practices in the business to business food and non-food supply chain*, 2013.

Separately, primary producers have raised concerns that they are offered unsustainably low prices.¹⁰ Issues relating to farm-gate returns are currently being considered as part of the Government's *White Paper on Australia's Agricultural Competitiveness*, which is proposed for release towards the end of 2014, with an issues paper released on 6 February 2014. The proposed Grocery Code does not seek to deal with the issue of the base prices that suppliers receive for their goods.

The issues being debated are not unique to the Australian food and grocery sector. There has been a similar debate in other nations, with a number of countries inquiring¹¹ into relationships in the food and grocery supply chain. A common feature of those inquiries is the finding of imbalances in bargaining power, with suppliers fearful of making complaints or declining requests from retailers out of concern of adverse consequences, including being delisted as a supplier.¹² A summary of the international experience is provided at **Attachment C**.

Questions:

1. Do the concerns outlined above accurately capture the most acute problems facing the food and grocery sector? Are there other behaviours engaged in by retailers that should be considered?
2. Are there any behaviours of suppliers that should be addressed by the Grocery Code?
3. Do you believe there is a role for Government to intervene in the market to address these concerns?

WHY IS GOVERNMENT ACTION NEEDED?

The Grocery Code has been proposed by industry proponents against the backdrop of this ongoing public discussion. This proposed approach is intended to improve standards of conduct in the food and grocery industry and effectively address the key problems identified.

As a general proposition, industry codes of conduct should aim to address specific problems and set out clear requirements and obligations, rather than aims and ideals.¹³ These obligations should be enforceable and consistent with the broader objectives of the CCA.¹⁴

An effective code should:¹⁵

10 ACCC, *Report of the ACCC's inquiry into the competitiveness of retail prices for standard groceries*, 2008, page 325.

11 European Commission, *Green paper on unfair trading practices in the business to business food and non-food supply chain*, 2013.

12 European Commission, *Green paper on unfair trading practices in the business to business food and non-food supply chain*, and *Summary of Response to the European Commission Green Paper*, 2013, Notes by Japan, United Kingdom to OECD Roundtable on Competition Issues in the Food Chain Industry, 2013, Finnish Competition Authority, *Study on Trade in Groceries: How does buyer power affect the relationship between trade and industry?*, 2012, Ireland, *Joint Committee on Enterprise, Trade and Employment report: Supplier- Retailer Relationships in the Irish Grocery Market*, 2010.

13 The Treasury, *Policy guidelines on prescribing industry codes under Part IVB of the Competition and Consumer Act 2010* (May 2011).

14 Ibid.

15 Ibid.

- identify the industry participants to be covered, and the means by which participants are bound;
- identify the behaviours that should be prevented or required;
- ensure that obligations cannot be avoided; and
- establish clear complaints resolution mechanisms.

More broadly, the Government considers that any regulation of the sector should facilitate the efficient operation of the food and grocery sector, in turn delivering associated benefits to consumers and improving the welfare of Australians.

The Government is keenly aware that any intervention needs to be beneficial overall, and not impose undue regulatory burden. Retailers should continue to have sufficient flexibility to negotiate good deals with suppliers that ultimately benefit consumers. An outcome that is too prescriptive or restrictive may have the unintended effect of resulting in higher retail prices for consumers. Conversely, allowing too much flexibility may mean that the issues of concern outlined above are not addressed.

The intention of any Government action is not to prevent hard bargaining and vigorous competition, but rather, to ensure that market distortions do not compound and have a longer-term detrimental impact on consumers or the grocery sector more broadly.

The Government also wishes to encourage industry-led responses to resolving issues in different sectors where this is feasible. Allowing industry to lead the response to problems in a market can have several benefits, as outlined in the guidelines for developing industry codes of conduct.¹⁶ In particular, prescribing an ‘opt-in’ industry code reinforces that the code has industry buy-in and is not overly prescriptive or burdensome.

The proposed Grocery Code is not the only possible mechanism for regulating relationships in the food and grocery sector. Existing laws, regulations and codes in Australia which are relevant to problems in the food and grocery sector are discussed in Part C of this consultation paper and at **Attachment D**.

¹⁶ Hon. Joe Hockey MP, *Prescribed codes of conduct – policy guidelines*, 1999; The Treasury, *Policy guidelines on prescribing industry codes under Part IVB of the Competition and Consumer Act 2010*, 2011; ACCC, *Guidelines for developing effective voluntary industry codes of conduct*, 2011.

PART B — SEEKING STAKEHOLDER VIEWS ON THE PROPOSED GROCERY CODE AND ITS IMPLEMENTATION

The Government is seeking stakeholder views and feedback on the draft content and text of the proposed Grocery Code at **Attachment A**. The purpose of the Grocery Code is to help regulate standards of business conduct in the grocery supply chain to build trust; to ensure transparency and certainty in commercial transactions to minimise disputes; and to provide an effective, fair and equitable dispute resolution process.

The approach brought forward by industry proponents — Coles, Woolworths and AFGC — is for Government to prescribe the proposed Grocery Code as an industry code under the CCA that retailers can agree to be bound by.

- The proposed Grocery Code would apply to retailers that agree in writing to be bound by the Code. These retailers would be bound by its terms. Under the CCA this is referred to as a voluntary industry code that is prescribed under the regulations. However, for the purposes of this paper it is referred to as an ‘opt-in’ prescribed Grocery Code to avoid potential confusion with voluntary codes that are not prescribed.
- Prescription would mean that, if a retailer that had agreed to be bound by the Code is later found in breach, the ACCC could take enforcement action for a breach of the CCA. A range of remedies would be available, including injunctions, and compensation for damages.

The proposed Code has six parts, as follows:

- **Part 1 — Preliminary:** sets out the Grocery Code’s purpose, definitions, application and transitional arrangements, including an obligation on retailers to offer suppliers the option to vary existing agreements to conform with the requirements of the Grocery Code.
- **Part 2 — Grocery Supply Agreements:** sets out requirements to have and retain written agreements, matters that those agreements must cover, and conditions that must be met before the retailer can enter into or vary agreements with suppliers (to the extent that the exceptions available under the Grocery Code do not apply).
- **Part 3 — Conduct generally:** sets out other standards of conduct, including in relation to payments for wastage, de-listing products, payment terms, product quality and standards, intellectual property rights, and shelf space allocation.
- **Part 4 — Other duties:** includes obligations to act in good faith and provide retailer contact details.
- **Part 5 — Dispute resolution:** sets out the approaches that suppliers are able to take in raising complaints in relation to conduct covered by the Grocery Code.
- **Part 6 — Compliance and reporting:** sets out obligations around compliance training and reporting on compliance with the Grocery Code.

The Government welcomes Coles, Woolworths and the AFGC’s industry-led response but is keen to seek input to ensure that the proposed Grocery Code would be effective in addressing the types of issues outlined in Part A of this paper.

This part of the consultation paper therefore provides an opportunity for stakeholders, particularly others that were not involved in the development of the Grocery Code, to provide their views and feedback on the effectiveness of specific aspects of the proposed Grocery Code.

APPLICATION AND COVERAGE

The Grocery Code applies to ‘retailers’ that opt in, or agree in writing to be bound by it. The Grocery Code defines a ‘retailer’ as a corporation that is: carrying on a supermarket business in Australia for the retail supply of groceries; or carrying on a business of purchasing groceries from a supplier for the purposes of resale to a supermarket business in Australia for the retail supply of groceries. Where a person carrying on a supermarket business in Australia also carries on other businesses, the Code only applies to the supermarket business.

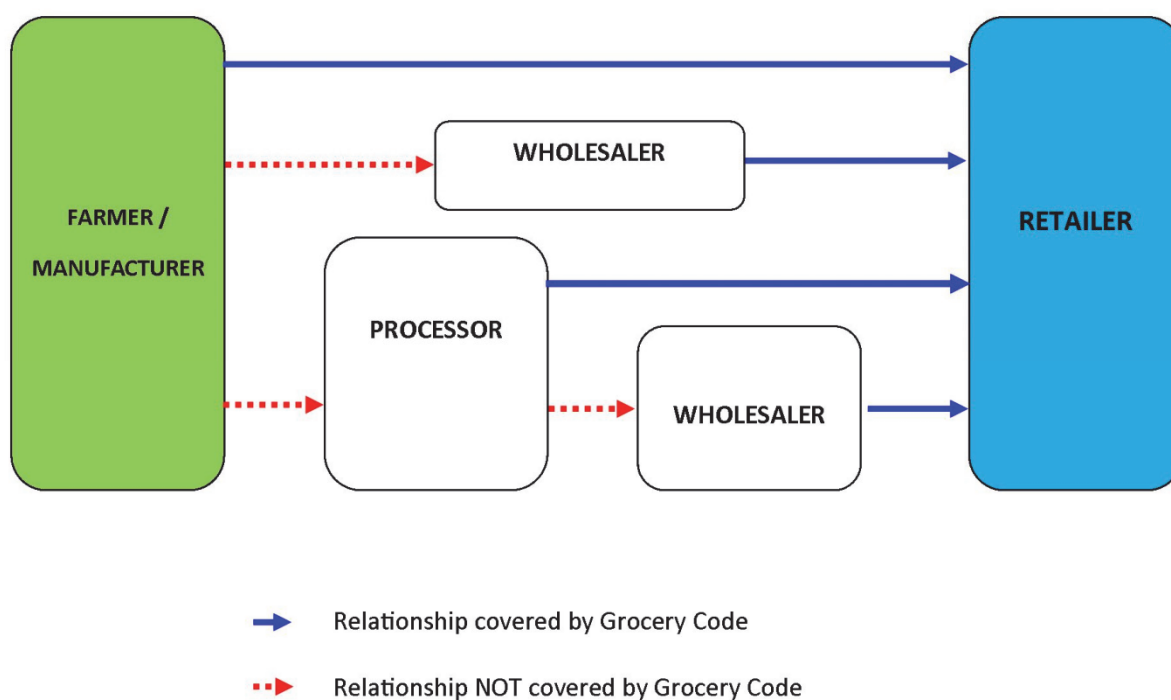
This definition is broad and potentially extends beyond the major supermarket chains and larger wholesalers that are the focus of the proposed Grocery Code, including to intermediaries such as Metcash. Smaller retailers and wholesalers, could also choose to sign up and be bound by the Code. However, as the Code has been predominately designed to reflect supermarket business operations, it may be less applicable or relevant for participants further down the supply chain. A list of non-proponent retailers and wholesalers is provided at **Attachment B**.

‘Supplier’ is defined as a person carrying on (or actively seeking to carry on) a business of supplying groceries to a retailer. This definition is also broad and includes both domestic and international suppliers.

An entity such as a wholesaler could potentially fall within the definition of both ‘retailer’ and ‘supplier’.

The Code only regulates the conduct of retailers and does not extend to bind the actions of suppliers. This approach recognises that while the retailer is to be bound by the Code, this should not have the effect of automatically binding its suppliers as well (particularly in the case where the supplier had no awareness of, or did not support the Grocery Code). Binding suppliers in this way would be inconsistent with the framework for industry codes and would not be legally enforceable if the Grocery Code is regulated on an ‘opt in’ basis for retailers.

Importantly, not all supplier–acquirer relationships in the food and grocery sector would be covered by the Grocery Code. The coverage of the Code only extends to retailers in their direct relationships with suppliers. For example, a farmer supplying directly to a supermarket or wholesaler which meets the definition of a ‘retailer’ under the Grocery Code (and that has agreed to be bound) would be captured by it. However, a farmer supplying to a series of intermediary processors before the goods are supplied to a retailer, would not be within the scope of the Grocery Code.



Relationships covering the supply and retail of alcohol would not be covered by the Grocery Code as drafted. Stakeholder views are sought on whether there are differences in the supply chain for alcohol which warrant its exclusion or whether coverage of the Code should be extended.

The Code does not specify an end date for its operation, or when it will be reviewed. However, codes of conduct that are prescribed under the CCA are typically reviewed at least every five years in consultation with industry, consumers and business. Treasury is the Department responsible for undertaking the review.¹⁷

When the Grocery Code will apply

If a retailer agrees to be bound by the Grocery Code they must ensure that all **new agreements** entered into with suppliers (including international suppliers) after that date must fully comply with the Code.

The Code provides transitional arrangements for grocery supply agreements entered into by retailers before the Code commenced (pre-existing grocery supply agreements). The Code will not apply to the supply of groceries under pre-existing grocery supply agreements immediately. The time that the Code will apply will depend on whether a retailer opts-in to the Code within the first six months of the Code commencing.

- If a retailer opts-in within the first six months after the Code commences, the Code will apply to all pre-existing grocery supply agreements from 12 months after the Code commenced.
- If a retailer opts-in more than six months after the Code commences, the Code will apply to all pre-existing grocery supply agreements from 6 months after the retailer opted-in.

¹⁷ The Treasury, *Policy Guidelines on Prescribing Industry Codes under Part IVB of the Competition and Consumer Act 2010* (May 2011).

In either case, if the retailer varies a pre-existing grocery supply agreement so that it complies with the Code within 12 months after the Code commences, the Code applies from when the agreement is so varied.

This transitional application of the Code is supported by a requirement for retailers to offer suppliers the option to vary these agreements to conform to the requirements of the Grocery Code within 6 months after the retailer is bound by the Code. If the supplier accepts the offer, the retailer must implement the variation within 6 months after the offer is accepted.

Questions:

4. Does the Grocery Code make it clear who the Code applies to and the scope of relationships in the food and grocery sector that it will cover?
5. Are the definitions for 'retailer' and 'supplier' sufficient to allow the Grocery Code to capture the types of supply chain relationships that present the most problems?
6. Should relationships relating to the supply of alcohol be covered? Why/why not?
7. Is the timing allowed for retailers to transition pre-existing grocery supply agreements to new agreements that conform to the Code appropriate?

GROCERY SUPPLY AGREEMENTS

The proposed Grocery Code introduces the concept of 'Grocery Supply Agreements.' This is the term given to any agreement between a retailer and supplier for the supply of groceries. The Grocery Code requires that such agreements must be in writing, clearly setting out standards of behaviour for a range of transactions between the parties.

The particular terms and conditions of each Grocery Supply Agreement will be determined by negotiation between the relevant retailer and supplier in each case, and may differ between retailers, or between suppliers to the same retailer.

However, the Grocery Code identifies a range of fundamental matters that must be specified in any Grocery Supply Agreement:

1. any requirements the retailer has in respect of the delivery of groceries;
2. any circumstances in which the retailer may reject the groceries;
3. the period within which the retailer must pay the supplier for the groceries and the circumstances in which any payment, or part of a payment, may be withheld or delayed;
4. the term of the agreement — if the agreement is intended to operate for a limited time only;
5. any quantity and quality requirements relating to the groceries — in clear terms; and
6. the circumstances in which it may be terminated — if the agreement provides for termination by one or more parties to it.

The Grocery Code also places limits around the circumstances under which a retailer is allowed to enter into or vary a Grocery Supply Agreement. This includes issues on:

- **Payments for shrinkage** — a retailer must not enter into a Grocery Supply Agreement that requires the supplier to make payments as compensation for shrinkage (such as theft, loss and accounting errors that occurs after the retailer has taken possession of the groceries).
- **Unilateral variations to Grocery Supply Agreements** — a retailer must not vary a Grocery Supply Agreement without the supplier's consent.
 - However, a retailer can still do this if the Grocery Supply Agreement between the parties provides for it and clearly sets out the change of circumstances that will allow for such variation; and the basis for calculating the adjustment for variations that involve changes in volume of supply. Reasonable notice is also required to be given to the supplier.
- **Retrospective variations to Grocery Supply Agreements** — a retailer must not vary a Grocery Supply Agreement retrospectively.
 - However, a retailer can still do this if the Grocery Supply Agreement between the parties provides for it and clearly sets out the change of circumstances beyond the retailer's control that justifies the variation; and the basis for calculating the adjustment for variations that involve changes in volume of supply.

A distinction in respect of unilateral versus retrospective variations is that for unilateral variations, it is not necessary for the changes in circumstances set out in the agreement to be 'beyond the control of the retailer'. This may reflect the view that retrospective variations can involve greater uncertainty for suppliers, whereas unilateral variations by the retailer may be regarded as a necessary business practice in certain cases.

Questions

8. Do you agree with the six fundamental matters listed for inclusion in all Grocery Supply Agreements? Are there other matters that should also be considered?
9. Should there be a higher threshold for exempting retrospective variations than unilateral variations in Grocery Supply Agreements?

CONDUCT GENERALLY

The Grocery Code contains further provisions to regulate forms of retailer conduct, including:

- **Payments for wastage** — a retailer must not require a supplier to make any payment to cover any wastage (spoilage or goods becoming unfit for sale) of groceries incurred at the premises of the retailer (or its contractor or agents).
 - However, a retailer can require such a payment if: the wastage is due to the supplier's negligence and the Grocery Supply Agreement clearly sets out what constitutes negligence; or the Grocery Supply Agreement sets out the basis of such a payment.

- **Circumstances for payments as a condition of being a supplier** — a retailer must not require a supplier to make any payment as a condition of stocking or listing the supplier’s grocery product.
 - However, a retailer can require such a payment if: the payment relates to a promotion; or the groceries have not been stocked, displayed or listed during the past year in a quarter or more of the retailer’s stores and the payment reflects a reasonable estimate of the costs and risks of stocking those products.
- **Payment for better positioning** — a retailer must not require a supplier to make any payment to secure better positioning or an increase in allocation of shelf space.
 - However, a retailer can require such a payment if: the Grocery Supply Agreement provides for such a payment; and the payment is reasonable having regard to the additional benefits to the supplier and the costs and risks to the retailer. This may occur even where the supplier may not have requested better positioning of their product.
- **De-listing** — a retailer may only de-list a supplier’s grocery product (that is, remove a product from the retailer’s product range) in accordance with the Grocery Supply Agreement and for genuine commercial reasons.
 - The Grocery Code sets out examples of what may constitute ‘genuine commercial reasons’. It also states that ‘genuine commercial reasons’ do not include ‘punishment for a complaint, concern or dispute raised by a supplier’.

Prior to de-listing, a retailer must provide reasonable written notice, including reasons for de-listing, and inform the supplier of their right to have the retailer’s decision reviewed.

- However, reasonable notice is not required where ‘time is of the essence’ or where there are persistent supply issues from the supplier.
- **Payments from retailers to suppliers** — a retailer must pay a supplier for all grocery products delivered and accepted in accordance with the Grocery Supply Agreement, within a reasonable timeframe set out in the agreement.
 - A retailer must not offset any amount against this payment unless the supplier has given written consent.
 - : However, a retailer can offset an amount if this has been provided for under the Grocery Supply Agreement.
 - A retailer must not require a supplier to contribute to the retailer’s costs of: a buyer’s visit to the supplier; artwork or packaging design; consumer or marketing research; opening or refurbishing of a store; or hospitality for the retailer’s staff.
 - : However, a retailer can require a supplier to make these payments if it has been provided for under the Grocery Supply Agreement.
- **Promotional and in-store support** — a retailer must not require a supplier to fund the retailer’s costs of promotion.

- However, a supplier can require a supplier to fund such costs if it has been provided for under the Grocery Supply Agreement. Even if the supplier agrees, the retailer may only hold the promotion after it gives the supplier reasonable written notice.

The Grocery Code also includes obligations on retailers in relation to the quantities of promotional stock they order; what they will do in the event that they over-order promotional stock; and the circumstances in which they may cancel or reduce their orders of promotional stock with the supplier's written consent.

- However, in relation to cancelling or reducing promotional order, a retailer is not required to obtain the supplier's written consent if reasonable written notice is given or compensation is provided for any net costs, losses, or expenses incurred as a direct result of the retailer's failure to give reasonable notice of the cancellation or reduction.

- **Product quality and standards** — a retailer must provide any fresh produce standards or quality specifications to a supplier in clear, unambiguous and concise written terms. The retailer must accept all fresh produce delivered in accordance with the standards; and the retailer may only reject the produce if it fails to meet the standards.

In addition, any labelling, packaging and preparation requirements must be communicated in clear, unambiguous and concise written terms; and reasonable written notice of any changes to the requirements must be provided. A retailer must also make any claims for damaged grocery produce or shortfalls within a reasonable time, no later than 30 days after delivery to the retailer.

- **Changes to supply chain procedures** — a retailer must not require a supplier to make any material change to supply chain procedures.

- However, a retailer may make material changes to the supply chain procedure where the retailer gives reasonable notice; or compensates the supplier for any net losses incurred as a direct result of the retailer's failure to give reasonable notice of the change. (A supplier can agree to waive its right to receive this compensation.)

- **Business disruption** — a retailer must not threaten business disruption or termination of an agreement without reasonable grounds.

- **Intellectual property rights** — a retailer must respect the intellectual property rights held by the suppliers in relation to grocery products; and in developing or producing their own brand products, must not infringe the intellectual property rights of a supplier.

- Conversely, the supplier's treatment of the retailer's intellectual property rights is also an important consideration under the Grocery Code. The supplier's actions in relation to the retailer's intellectual property rights will be taken into account during any dispute resolution process (including mediation or internal review) relating to a breach of this provision.

- **Confidential information** — a retailer must only use a supplier's confidential information for the purpose for which it was disclosed, and must only disclose that information to those that 'need to know'. Retailers must establish systems to ensure compliance with this obligation.

- **Transfer of intellectual property rights** — a retailer must not require a supplier to transfer or exclusively license any intellectual property right held by the supplier in

relation to a grocery product as a condition or term of supply of an equivalent own brand product.

- **Allocation of shelf space** — a retailer must publish or provide brand product ranging and shelf allocation principles, act in accordance with them, and keep them up-to-date.

Retailers must also:

- within a reasonable time before conducting a range review, provide clear written notice of the purpose of the range review and the key criteria governing ranging decisions, and following the conclusion of a range review, allow a reasonable amount of time to discuss outcomes; and
- apply the shelf-space allocation principles without discrimination.

Questions

10. Do you believe that these requirements under the Grocery Code will help address the range of problematic issues that can arise during the relationship between retailers and suppliers?
11. Do you believe that the exceptions accompanying the requirements are necessary to provide sufficient commercial flexibility while maintaining appropriate procedural safeguards?
12. Will the exemptions significantly reduce the effectiveness of the Code in addressing critical supply chain concerns?

Discussion

It is clear that while the Grocery Code establishes a broad range of restrictions on the behaviour of retailers in their dealings with suppliers, many of these restrictions are accompanied by exemptions which permit the behaviour to occur under certain conditions.

Rather than an outright prohibition, retailers are permitted to take certain actions that would otherwise be prohibited, provided that they meet certain requirements (such as giving reasonable notice) or clearly setting out terms and conditions that would allow such action to be taken in the Grocery Supply Agreement between the parties.

On the one hand, there are arguments that such exemptions are appropriate and necessary to reflect practical commercial realities and facilitate workable business interactions between the parties. This approach recognises the parties' freedom to contract wherever doing so is mutually beneficial and provides suitable flexibility to allow the parties to conduct business efficiently. This also recognises the principle that an effective code should avoid imposing unnecessary limitations or intrusions into normal commercial decision making.¹⁸

A benefit of the Grocery Code is to require that relevant terms and conditions are clearly and unambiguously set out, in writing, in the Grocery Supply Agreement. This will help improve transparency for both parties and ensure that there is a common understanding between them as to their risks and benefits, and rights and obligations during the business relationship. Combined with oversight and enforcement by the ACCC, it is argued that this approach strikes the appropriate balance in regulation to benefit the sector as a whole.

¹⁸ The Treasury, *Policy guidelines on prescribing industry codes under Part IVB of the Competition and Consumer Act 2010* (May 2011).

On the other hand, there is a risk that the cumulative effect of these exemptions may undermine the ability of the Grocery Code to improve retailer-supplier relationships. Given the concerns about the imbalance of bargaining power between suppliers and retailers, there is a possibility that some of the exemptions built into the Grocery Code may deliver outcomes that are practically no better for suppliers.

Permitting retailers to take certain actions that would otherwise be prohibited, provided that they include relevant terms and conditions in the Grocery Supply Agreement, may operate to simply shift the pressures of the imbalance of bargaining power between the parties to be more heavily felt during the initial negotiation stage. While this may go some way towards giving suppliers a better awareness and understanding of the risks before they decide to enter into contracts with retailers, it may limit the effectiveness of the Code in improving the business relationship between the parties. There may be other alternative ways to achieve flexibility (discussed below).

It is worth noting that some of the types of terms and conditions that are covered by the Grocery Code might be able to be characterised as ‘unfair contract terms’. The Government is committed to extending the existing protections for consumers against unfair contract terms in standard form contracts, to small businesses. More information is provided in the consultation paper, *Extending Unfair Contract Term Protections to Small Business*, available at www.treasury.gov.au.

Possible alternative for achieving commercial flexibility

No disadvantage test

A possible alternative approach may involve applying a no disadvantage test. That is, to allow the retailer to rely on an exemption provided for in the Grocery Supply Agreement and engage in certain conduct so long as it does not result in the supplier being materially disadvantaged.

This may require any costs imposed on the supplier due to the retailer’s exercise of an exemption to be factored in during initial negotiations on the supply agreement or possibly compensation being offered at the time the exempted conduct is engaged in.

This approach attempts to maintain commercial flexibility to the extent it is mutually beneficial, while offering safeguards against conduct that may be considered inconsistent with the minimum industry standards.

OTHER DUTIES

Obligation to deal lawfully and in good faith

The proposed Grocery Code provides that a retailer must at all times deal with suppliers lawfully and in good faith, including by:

- conducting its trading relationships with suppliers without duress and in recognition of the suppliers’ needs for certainty regarding the risks and costs of trading, particularly in relation to production, delivery and payment issues; and
- entering into Grocery Supply Agreements that acknowledge the retailer’s obligation to deal with suppliers lawfully and in good faith in accordance with the Grocery Code.

Good faith is a concept that has been recognised in Australian common law. The principle of good faith has been developed by the courts over time and in recent years some courts have accepted the duty to act in good faith as an implied term in the performance of contracts. While there is no definitive meaning of good faith, there has been considerable jurisprudence and legal commentary surrounding it, with guiding principles such as honesty, cooperation, reasonableness and fairness, often cited to assist in determining the obligation on a case-by-case basis. There are a range of alternative ways in which an obligation to act in good faith could be considered in the Code.

The options for a good faith obligation

1. Good faith as a stand-alone provision applying to retailers only (as currently drafted)

The current approach places an obligation on retailers to act in good faith at all times during their dealings with suppliers, but does not place a reciprocal duty on suppliers. This is because the proposed Code has been designed to apply only to retailers (that agree to be bound) and not suppliers. This is similar to the mandatory *UK Groceries Supply Code of Practice*, which influenced the development of the proposed Australian Code and includes an obligation that retailers conduct trading relationships with suppliers in good faith (further information is at **Attachment C**).

It may be argued that it is appropriate to only impose this obligation on retailers in light of previous inquiries into the grocery retailer sector that found that problematic behaviours that may involve a lack of good faith are typically attributed to retailers with superior bargaining power rather than suppliers. Further, any assessment of whether a retailer has acted in good faith would take into account surrounding circumstances, which may include the conduct of suppliers as well.

The proponents – Coles, Woolworths and the AFGC – have concerns that this one-sided obligation is contrary to equitable principles of mutual good faith in dealings and could result in unintended consequences that may undermine the mutual trust, fairness and commitment that underpin the Code's objective of improving commercial relationships. The proponents prefer that options that balance obligations on both parties be considered.

2. Good faith as an interpretative provision

This approach could involve incorporating the principle of good faith within the introductory purpose clause of the Code (clause 2). An addition to this clause could include 'the purpose of this code is to ensure dealing in good faith at all times between retailers and suppliers in respect of any matter arising under or in relation to a grocery supply agreement or this code.'

This provision could assist in interpreting other Code provisions where there may be ambiguity or multiple interpretations. In such cases, those provisions would have the benefit of being interpreted in a manner that is consistent with the principles of good faith. However, this provision does not create any separate or distinct obligations on retailers or suppliers that would be enforceable by the courts for a breach.

The options for a good faith obligation (continued)

3. Revised good faith provision that takes account of the supplier's conduct

This approach would retain the obligation on retailers only (as with option 1) but would direct the courts to also take into account whether the relevant supplier had acted in good faith during its determination of whether the retailer had breached the good faith obligation. It should be noted the proposed Code already considers the supplier's conduct during dispute resolution procedures, which allows a retailer to refuse to investigate or attend mediation (or arbitration) if they find that the supplier has not acted in good faith.

This may provide a further mechanism for balancing the obligation between the parties while retaining the current' structure of the Code as applying only to retailers. However, this may complicate enforcement by requiring that the ACCC and courts weigh up the conduct of the parties to determine whether the retailer has breached its good faith duty.

4. Redesign the Code to bind retailers and suppliers in respect of good faith

The proposed Code is currently designed to apply only to retailers that choose to opt-in. There is no mechanism for suppliers to opt-in and become bound by the Code. However, the Code could be redesigned to also allow suppliers to opt-in and agree to be bound by a similar good faith provision tailored to apply to them. This approach would provide a mutual obligation on both parties to act in good faith in their dealings with one another. Such an approach would only be effective to the extent that suppliers choose to opt-in.

5. Good faith as a contractual term in Grocery Supply Agreements

A further approach could involve the Code specifying that a contractual term be included in all Grocery Supply Agreements that retailers and suppliers must deal with each other in good faith. This would be legally enforceable under general contract law. However, as it would no longer be an obligation under the Code itself, a breach of good faith would not be enforceable by the ACCC. Further, there is some support for the view that a duty of good faith is already an implied term in all contracts at common law in any case.

Questions

13. Will the inclusion of a duty to act in good faith improve commercial relationships in the sector?
14. Should this obligation only apply to retailers, or do suppliers also engage in behaviours lacking in good faith that warrant them being covered by this obligation as well? Which option is most appropriate?
15. Would compliance with the duty of good faith lead to increased or decreased compliance costs?

DISPUTE RESOLUTION

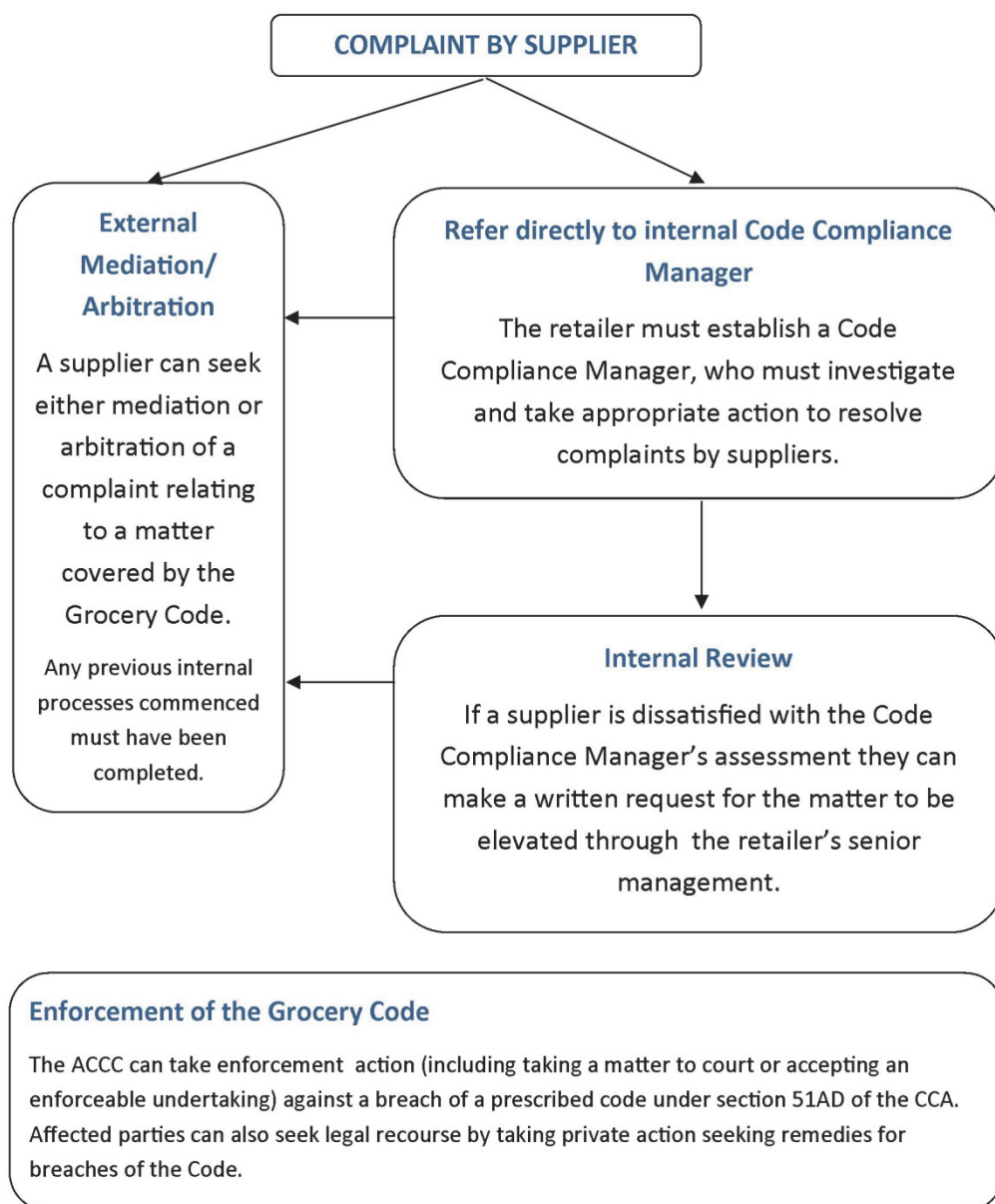
Establishing clear and effective dispute resolution mechanisms has been a key benefit and recognised success story of other industry codes. A structured arrangement to allow the parties to resolve their disputes in a timely and cost effective manner without jeopardising business relationships is an important component of the proposed Grocery Code.

The proposed Grocery Code aims 'to provide an effective, fair and equitable dispute resolution process for raising and investigating complaints and resolving disputes arising between retailers and suppliers'. The processes outlined in the Grocery Code are only intended to be used when suppliers raise complaints – there is no equivalent process for retailers to raise complaints.

The draft Grocery Code sets out internal and external dispute resolution arrangements for suppliers to lodge complaints and seek to have their disputes with retailers resolved. It is open to suppliers to choose the type of dispute resolution option that best meets their needs.

Dispute resolution arrangements

The diagram below outlines the dispute resolution process under the proposed Grocery Code.



Referral of complaints to Code Compliance Manager

A supplier may refer complaints relating to a matter covered by the Grocery Code to a retailer's code compliance manager, who has responsibility for investigating the complaint and determining what action must be taken, if any, in response to the complaint.

Internal review

If the supplier is not satisfied with the outcome of the investigation by the code compliance manager, they may request in writing that the matter to be elevated through senior levels of management.

Mediation or arbitration

A supplier may seek either mediation or arbitration of a complaint or dispute relating to a matter covered by the Grocery Code, but only after any previous internal review process initiated by them has been or should have been completed. A supplier is able to take a complaint directly to mediation or the ACCC, and is not required to first engage in internal dispute resolution. The Institute of Arbitrators and Mediators Australia (IAMA) Mediation Rules will apply to all mediation and arbitration processes commenced under the Grocery Code. The IAMA rules will also determine the allocation of any associated costs of mediation or arbitration.

If a mediator or arbitrator is not agreed to by the parties within 10 days then one will be appointed.

In providing for less adversarial mechanisms for a supplier to raise a complaint with a retailer, the Grocery Code offers a clear and more structured process that may improve a supplier's access to justice.

Supplier access to dispute resolution mechanisms

In order for retailers to become obliged under the Code to take part in dispute resolution processes, it is necessary for suppliers to meet some basic conditions. For the internal dispute resolution process, if the code compliance manager makes an initial finding that the supplier's complaint is 'vexatious, trivial, misconceived or lacking in substance' they must notify the supplier in writing of this, but are not required to investigate the matter further. The supplier can progress the matter for internal review with the retailer's senior management or choose to go directly to external arbitration and mediation.

Similar threshold conditions also exist before the retailer becomes obligated to take part in external arbitration and mediation. If the retailer has made a determination that the supplier's complaint is 'vexatious, trivial, misconceived, or lacking in substance' or that the supplier has not 'acted in good faith' then the retailer does not have to attend the arbitration or mediation.

There may be concerns that the current proposed arrangement places unnecessary constraints on the ability of suppliers to access suitable dispute resolution mechanisms under the Code. This approach places the decision-making power in relation to commencing dispute resolution processes (including mediation) firmly with the retailer. As suppliers may already be hesitant about bringing complaints forward to retailers, this approach may undermine the goal of improving the commercial relationship.

Questions

16. Do you agree with the threshold conditions in the Code that suppliers must meet in order to trigger the retailers' obligation to take part in mediation or arbitration? What impact could this have on the accessibility of the dispute resolution mechanisms in the Code?
17. Would the dispute resolution mechanisms under the Code 'provide effective, fair and equitable dispute resolution processes'?
18. How should each party allocate costs of dispute resolution?

Enforcement

Breaches of prescribed industry codes are a breach of the CCA and are subject to many of the remedies available under the CCA, including:

- compensation or damages for the amount of any loss or damage;
- injunctions to restrain a body corporate from engaging in conduct in breach of a code;
- requiring corrective advertising or the disclosure of information;
- setting aside or varying relevant contracts; or
- requiring money to be refunded.¹⁹

Currently the CCA does not allow a pecuniary penalty to be imposed for a contravention of an industry code, nor does it allow regulations to be made prescribing pecuniary penalties in respect of a contravention of an industry code. The CCA also currently does not allow the ACCC to issue an infringement notice in respect of a contravention of an industry code. However, it should be noted that the Government's current reforms to the Franchising Code propose to introduce pecuniary penalties (up to \$51,000) and allow the ACCC to issue infringement notices (\$8,500 for a body corporate and \$1,700 in any other case) for contravention of a civil penalty provision of that code, and this necessitates amending the CCA.

Questions:

19. Is the range of remedies available for breaches of the Grocery Code appropriate?
20. Should penalties be included in this opt-in Code that can be enforced by a court?
21. Should the ACCC be empowered to issue infringement notices for contraventions of this opt-in Code under the CCA?

CONCLUSION TO PART B

The Government welcomes Coles, Woolworths and the AFGC's industry-led response to the considerable public debate in recent times about negotiation arrangements in the food and grocery sector. The Government is nonetheless keen to seek input to ensure that the proposed Grocery Code would be effective in addressing supply chain concerns. We look forward to hearing your views.

¹⁹ *Competition and Consumer Act 2010* (Cth), section 51ADC.

Questions

22. Does the proposed Grocery Code clearly set out the issues in the food and grocery sector that it seeks to address? Does it include clear requirements and obligations to address these issues?
23. Does the Code cover the key issues that it should cover in order to achieve its aims of regulating standards of business conduct, ensuring transparency and certainty in commercial transactions and building trust and cooperation in the sector?
24. Are there any unintended consequences that may arise from the operation of the proposed Grocery Code?

PART C — WHAT ARE THE POLICY OPTIONS BEING CONSIDERED? WHAT ARE THE LIKELY COSTS AND BENEFITS?

The Government has a variety of options for achieving the policy objectives outlined in Part A. This part of the consultation paper considers and seeks views on the relative regulatory impacts of these different options.

OPTION 1: STATUS QUO

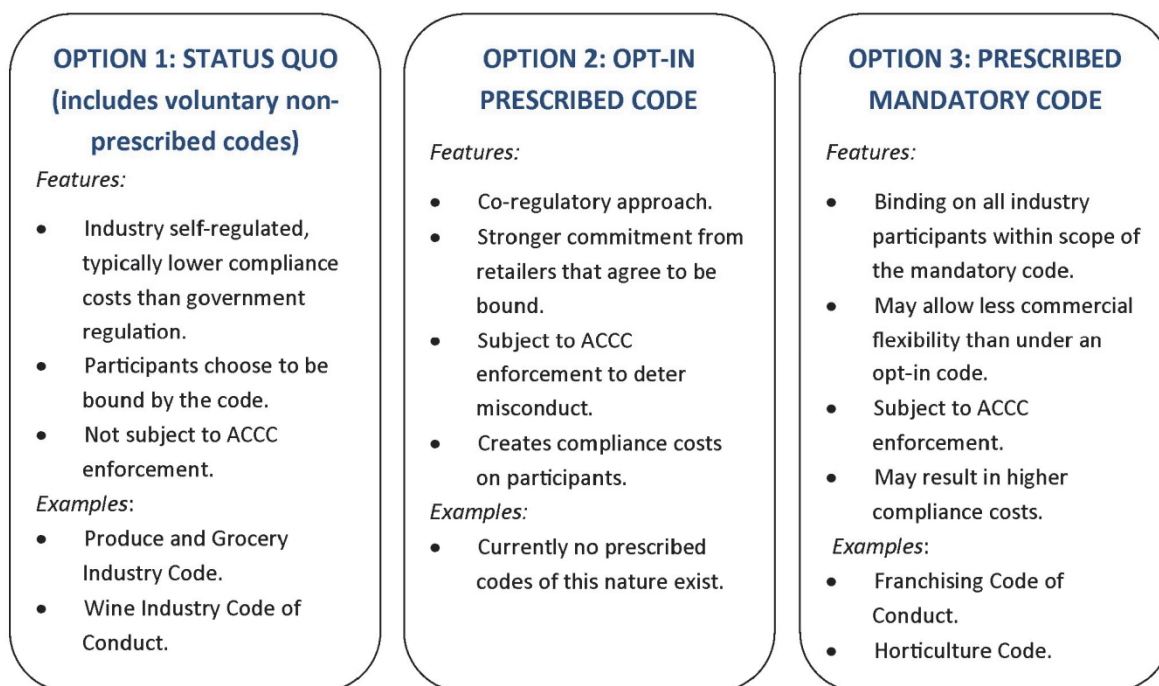
Involves maintaining the ‘status quo’ and relying upon existing laws, regulations and codes. This option would not preclude a code of conduct being implemented by the industry outside of the CCA.

OPTION 2: OPT-IN PRESCRIBED CODE

Involves prescribing a Grocery Code, whereby a retailer chooses whether or not to be bound by the Code. Retailers that agree to be bound by the Code would then be legally required to comply with it.

OPTION 3: MANDATORY PRESCRIBED CODE

Involves prescribing a mandatory Grocery Code, whereby a retailer (as defined by regulations) would be legally bound by the Code.



Option 1 — the status quo

Under option 1, existing laws and codes would be relied upon for addressing concerns in the food and grocery sector. As such, this option would involve no additional regulatory intervention by the Government.

Relationships in the food and grocery sector are currently subject to the following non-prescribed and prescribed codes of conduct:

- the Produce and Grocery Industry Code of Conduct (PGICC) — a non-prescribed voluntary, industry run code;
- the Australian Wine Industry Code of Conduct — also a non-prescribed voluntary industry code; and
- the Horticulture Code of Conduct — this is a mandatory code prescribed under the CCA.

These codes are, however, unlikely to address all of the issues outlined in Part A of this consultation paper:

- The Australian Wine Industry Code of Conduct and the Horticulture Code of Conduct cover different relationships in the supply chain — the Australian Wine Industry Code of Conduct addresses issues between grape growers and winemakers, and the Horticulture Code of Conduct addresses issues between growers and traders of fresh horticultural produce. The Horticulture Code of Conduct deliberately excludes relationships with processors and retailers.
- The PGICC is significantly more limited than the proposed Grocery Code in terms of coverage and scope. Further, the PGICC Administration Committee has not met since 2011 and a number of parties to the PGICC have withdrawn their support.

Relationships in the food and grocery supply chain are also governed by:

- the economy wide provisions of the CCA, including the Australian Consumer Law (ACL);
- the common law, which governs contractual dealings (including the concept of good faith); and
- intellectual property protection mechanisms.

Existing codes and laws are outlined and discussed in more detail in **Attachment D**.

However, the issues discussed in Part A of this consultation paper have remained issues of concern despite these existing competition, consumer, contract and intellectual property law regimes. Option 1 would still allow for the sector to implement the proposed Grocery Code as a non-prescribed code. The current non-prescribed voluntary code (the PGICC), for example, has failed to address the concerns outlined in Part A.²⁰

If the Grocery Code were implemented by industry as a non-prescribed code, this could result in some costs to industry e.g. costs of updating the current self-regulatory scheme, changes to dispute resolution processes and ongoing costs associated with monitoring of compliance. However, these are still likely to be lower than costs associated with a prescribed code.

A non-prescribed code would not be subject to ACCC enforcement, meaning that the ACCC would not be able to take complaints, investigate breaches and enforce compliance with the code.

Maintaining the status quo could avoid some costs to the sector and to the ACCC associated with prescribing a code (for example, the costs of implementation, compliance monitoring and enforcement action under the prescribed code).

On the other hand, to the extent that the existing laws, regulations and codes outlined above are ineffective—and because there is a risk that retailers and suppliers would not fully comply with the proposed Grocery Code in the absence of prescription—the problems outlined in Part A of this paper would persist.

Given the ongoing debate about supply chain issues in the sector, there may be concerns from industry that the current ‘status quo’ arrangements have not been effective in improving the business relationships between retailers and suppliers. Stakeholder feedback is sought on the effectiveness of these existing ‘status quo’ processes and whether further Government intervention is warranted.

²⁰ Senate Select Committee, *Inquiry into food processing report*, 2012.

Questions:

25. Please provide any views on the effectiveness or otherwise of current industry codes and existing laws in addressing concerns identified in Part A of this paper.
26. If the proposed Grocery Code were to be prescribed, what should be the future of the PGICC, the Australian Wine Industry Code of Conduct and the Horticulture Code? Please provide reasons for your views.
27. What are the costs and benefits associated with maintaining the status quo?

Option 2 – Opt-in Prescribed Grocery Code

This consultation paper has focused primarily on the proposal by Coles, Woolworths and the AFGC for the Grocery Code to be prescribed on an opt-in basis.²¹

Under this approach, retailers could agree to be bound by the Code. Once they had agreed to be bound, they would have to deal with their suppliers in accordance with the Code. Retailers would be able to cease being bound by giving notice in writing to the ACCC but conduct during the period signed up would still be covered by the Code.²²

A Grocery Code that is prescribed on an opt-in basis could deliver the following benefits:

- There may be a stronger commitment for signatories to comply with the spirit and substance of the code than if it is mandated, because participants in the supply chain volunteer of their own accord to address undesirable behaviours in the sector.
- Establishes a clear and structured low cost alternative dispute resolution process that can assist the parties to resolve disputes before they become ‘toxic’ and damaging to the business relationship. This may help parties to avoid the need for costly legal action.
- There would be an opportunity to test whether retailers voluntarily agree to be bound and any additional costs associated with prescribing a mandatory code (as outlined below) could be avoided.
 - Prescription of a code in a voluntary form would not preclude the Government from prescribing a mandatory code at a future time.
- Relative to the non-prescribed codes that are already in place, there would be a higher likelihood of compliance and in turn issues in the sector being addressed, because prescription would result in:
 - the ACCC’s audit power being able to be brought to bear;
 - a range of remedies being available to a court in the event that a breach of the Code is found; and

²¹ For the purposes of Part IVA of the CCA, under section 51ACA a voluntary industry code binds a person who has agreed, as prescribed, to be bound by the Code and who has not subsequently ceased, as prescribed, to be bound by it (see also section 51AE). This is referred to as an ‘opt-in’ prescribed Grocery Code for the purposes of this paper to avoid potential confusion with voluntary codes that are not prescribed.

²² Opting-out would prevent the firm from incurring any public law sanction for future conduct, but it would remain responsible under public law for the period of time under which it was bound.

- the ACCC or private parties being able to take action seeking these remedies.

Indeed, a key purpose of prescribing an industry code of conduct is to strengthen a non-prescribed code where there is concern that it would not be able to meet its objectives.²³

On the other hand, a prescribed Grocery Code that retailers agree to be bound by would give rise to the following costs:

- Costs for retailers involved in transitioning to and then complying on an ongoing basis with the new regulatory regime, such as the need for legal advice and education of staff regarding the regime, and record keeping and reporting. Estimates of these compliance costs and the assumptions underlying them are included in **Attachment E**.
 - These compliance costs would only be faced by those retailers that agree to be bound by the code.
 - A level of compliance costs would also be faced under a mandatory code.
- The opt-in nature of the Code means there is always a risk that retailers that agree to be bound up-front may, at a later date, decide to cease being bound by the Code by giving written notice to the ACCC, or that retailers causing the types of problems the Code seeks to address do not opt-in to the Code.
 - As noted above though, if this were the case, the Government could consider the need for a mandatory code.
- Costs to Government in terms of implementation, compliance monitoring and enforcement action.
 - These costs would also be faced under the mandatory code option.

Questions:

28. Would the benefits of prescribing a code on an opt-in basis outweigh the costs? Why do you consider this to be the case?
29. Are the compliance cost estimates associated with Option 2, and the underlying assumptions that have been used to estimate them (as outlined in **Attachment E**) accurate?

Option 3 – Mandatory Prescribed Grocery Code

The third option the Government is considering is the prescription of a mandatory code of conduct under the CCA. This option would be a change from Government facilitating an industry-led response, to Government specifying the scope and effect of regulations to the sector. If the Government were to pursue a mandatory code, it is possible that the code would look different from the current proposed opt-in Grocery Code.

The key difference between prescribing a mandatory code, versus prescribing an opt-in code, is that a mandatory code applies to all parties that fall within the scope of the code, not just those that agree to be bound.

A mandatory code prescribed under regulations could deliver the following benefits:

²³ ACCC, *Guidelines for developing effective voluntary industry codes of conduct*, July 2011.

- Relative to a non-prescribed code or a prescribed opt-in code, greater certainty that all appropriate supply chain relationships in which there are issues will be covered, because compliance would be mandatory.
 - However, if the code is imposed by the Government, retailers may be less supportive of it and less willing to comply because, they have not voluntarily agreed to be bound.

On the other hand, prescription of a mandatory code would give rise to the following costs:

- Higher compliance costs if the mandatory code were given broad scope, for example, if the current broad definition of ‘retailer’ were retained. This is because a larger number of businesses would be required to comply with the mandatory code’s obligations.
 - Having said this, the scope of the code could be designed narrowly. For example, the definition of ‘retailer’ could be narrowed such that only those entities for whom there is evidence of supply chain issues would be obligated to comply. If this were the case, compliance costs may be much the same as or only slightly higher than for an opt-in prescribed code.
- There is a potential for regulation to be applied to retailers in a manner that reduces the commercial flexibility of retailers and suppliers under a mandatory code approach compared to the proposed opt-in Grocery Code. The resultant increase in regulatory burden for these retailers may not be offset by any associated increase in benefits to the suppliers that deal with them, or consumers generally.
- Potentially higher costs to Government in terms of implementation, compliance monitoring and enforcement action than for a opt-in prescribed code.

Questions:

30. Would the benefits of prescribing a mandatory code outweigh the costs, or vice versa? Why do you consider this to be the case?

CONCLUSION TO PART C

Part C of this consultation paper has considered what the regulatory impacts of prescribing an opt-in code may be and how these compare to alternative approaches.

In summary, these alternative approaches include firstly, a ‘do-nothing’ option whereby existing laws, regulations and codes are relied upon and suppliers enforce their rights at private law against retailers, and secondly, prescribing a mandatory code.

Stakeholder feedback is sought in order to inform the Government’s final approach in this matter.

An estimate of the compliance costs associated with prescribing an opt-in code is provided in **Attachment E**. The Government is seeking views on these cost estimates and the assumptions underlying them.

ATTACHMENT A: PROPOSED GROCERY CODE

To obtain a copy of the exposure draft of the Grocery Code please visit the Treasury website at:

www.treasury.gov.au/ConsultationsandReviews/Consultations/2014/Improving-Relationships-Food-Grocery-Sector.

ATTACHMENT B: KEY NON-PROPONENT RETAILERS AND WHOLESALERS

As noted in Part A, other key organisations at the retail and intermediary levels of the supply chain include:

- ALDI – similarly to Coles and Woolworths, ALDI operates at both the wholesale and retail level.²⁴ ALDI is known as a low cost operator, is growing, and has a targeted product range.²⁵ A large proportion of ALDI’s product range is retailer own brand products.²⁶
- Costco – a more recent entrant to the market than ALDI, Costco is also a low cost operator, and operates its retail outlets in a ‘warehouse club’ format, whereby a membership is required to make purchases. Goods are sold in bulk or large scale to individuals as well as small to medium sized businesses.²⁷
- Metcash – is Australia’s largest wholesaler that supplies and distributes groceries and alcohol to the majority of independent supermarket operators, most of whom operate relatively small stores (though there are a number of large-format independent supermarkets).²⁸ Metcash’s retail channels include IGA Supermarkets, Supa IGA, IGA Express, Foodworks and Lucky 7 convenience stores.²⁹ Packaged grocery distribution is undertaken through Metcash’s twelve distribution centres; and the company also distributes fresh food products to its retail partners via ten fresh produce warehouses.³⁰

These retailers and wholesalers do not necessarily adopt business models that are the same as those of Coles and Woolworths, and the degree of buyer power that they have in their relationships with suppliers may differ.³¹

24 ACCC, *Report of the ACCC’s inquiry into the competitiveness of retail prices for standard groceries*, 2008.

25 ALDI offers a product range of about 900 lines, compared with larger retailers, such as Coles, who stock closer to 30,000 lines. Reference – ACCC, *Report of the ACCC’s inquiry into the competitiveness of retail prices for standard groceries*, 2008, page 43.

26 ACCC, *Report of the ACCC’s inquiry into the competitiveness of retail prices for standard groceries*, 2008, page 475.

27 IBISWorld Company Report, Costco Wholesale Australia Pty Ltd, 1 September 2013, page 4.

28 ACCC, *Report of the ACCC’s inquiry into the competitiveness of retail prices for standard groceries*, 2008.

29 IBISWorld Company Report, Metcash Limited, 30 April 2013, page 4.

30 IBISWorld Company Report, Metcash Limited, 30 April 2013, page 4.. Fresh produce sold at these independent supermarkets is also sourced directly from suppliers, or via wholesale markets. ACCC, *Report of the ACCC’s inquiry into the competitiveness of retail prices for standard groceries*, 2008.

31 See chapter 15 of ACCC, *Report of the ACCC’s inquiry into the competitiveness of retail prices for standard groceries*, 2008, for an overview of differences in the evidence available at that time of the major supermarket chains’ and Metcash’ buyer power in different supply chain relationships.

ATTACHMENT C: THE INTERNATIONAL EXPERIENCE

Concerns about trading relationships between supermarkets and suppliers are not unique to the Australian grocery market.

In October 2013, the OECD Competition Committee discussed competition issues in the food chain industry. Submissions from 32 countries (including Australia) were received. These submissions are available on the OECD's website.³²

UNITED KINGDOM

In 2008, an inquiry into the UK grocery market by the then UK Competition Commission (UKCC) raised concerns about the exercise of buyer power by grocery retailers. To address the concerns identified in the report, the UKCC established a new, mandatory Groceries Supply Code of Practice (GSCOP), which came into effect on 4 February 2010 and replaced the former Supermarkets Code of Practice.

The GSCOP covers the eight major supermarket chains operating in the UK and all other retailers with groceries turnover in excess of £1 billion per year. The GSCOP includes provisions about fair dealing (including an obligation on retailers to deal with suppliers in good faith), prohibitions on retrospective changes to terms of supply, procedures for customer complaints and de-listing, the burden of proof on retailers for 'requests', and compliance and enforcement, including dispute resolution and binding arbitration procedures and the requirement that retailers have in-house compliance officers. In this way, suppliers are automatically covered by the protections provided by the code but do not have any reciprocal obligations under the code.

Some of the criticisms that have been reported in relation to the GSCOP include its enforceability and effectiveness, its associated compliance costs, the overall increase in regulatory burden for businesses and the effects of the code's prohibitions on commercial flexibility.

Key features of the GSCOP include prohibitions on: payments for shrinkage; delays in payments; and imposing obligations to contribute to marketing costs. Retailers are also prohibited from making retrospective adjustments to terms and conditions of supply.

The GSCOP also imposes obligations on retailers to appoint a code compliance officer, maintain written records of all agreements with suppliers, and supply information to the Competition and Markets Authority (formerly the Office of Fair Trading) as required. The dispute resolution system provides for arbitration with the associated costs borne by the designated retailer.

In June 2013, the UK set up an independent regulator, the Grocery Code Adjudicator, to enforce compliance with the GSCOP. It ensures that large supermarkets treat their direct suppliers lawfully and fairly.

³² <http://www.oecd.org/daf/competition/competition-issues-in-food-chain.htm>

The Adjudicator's statutory functions are to:

- investigate confidential complaints from any source about how supermarkets treat their suppliers;
- make recommendations to retailers if a complaint is upheld;
- require retailers to publish details of a breach of the code;
- in the most serious cases, impose a fine on the retailer; and
- arbitrate disputes between retailers and suppliers.

EUROPEAN UNION

In the European Union (EU), a number of recent developments relating to food and agricultural commodity markets in the EU and worldwide have prompted a response from policymakers. These developments include:

- asymmetries in the transmission of price changes throughout the supply chain in many EU member states, such as retail prices increasing whilst product/commodity prices are declining; and
- rising concerns about the bargaining power of retailers in their commercial relationships with suppliers and the perceived existence of unfair trading practices due to factors including the increased concentration of retailers and private label products.

Following the food price crisis in 2008-09, the European Parliament has called for action against alleged unfair trading practices by retailers in relation to their suppliers, farmers or small industry manufacturers. Additionally, food manufacturers and, to some extent, consumer associations have claimed that there has been a deterioration of choice and innovation in recent years.

Responding to this pressure, an Expert Platform on B2B Contractual Practices within the High Level Forum for a Better Functioning Food Supply Chain was established to work on a solution. In November 2011, all operators in the supply chain (through their European Associations) agreed on a code of good practice. This was a voluntary initiative. In December 2012, all operators (except farmers) agreed on an implementation mechanism. During 2013, participants worked to implement the code of good practice, maintaining dialogue with a farmers' association.

The *Vertical relationships in the Food Supply Chain: Principles of Good Practice* (principles of good practice) recognise that unfair practices may occur throughout the food supply chain and that stakeholders have a willingness to address those practices in a consensual and effective way. Stakeholders that developed the principles believe that they 'provide a framework for doing business that respects contractual freedom and ensures competitiveness, trust and continuity, all required for business development, innovation and the three pillars of sustainability.'

Contracting parties agree to operate according to the following general principles:

1. **consumers** — parties should consider consumer interests and the overall sustainability of the supply chain in their B2B relations;

2. **freedom of contract** – parties respect each other’s right to contract freely according to their own strategy and management policy; and
3. **fair dealing** – parties should deal with each other reasonably, in good faith and with professional diligence.

The principles of good practice operate on the following specific principles:

1. **written agreements** – agreements should generally be in writing and express terms clearly and transparently, covering as many relevant and foreseeable elements as possible;
2. **predictability** – any unilateral change must have been agreed in advance and agreements should outline the process for discussing any necessary changes to implement the agreement or due to unforeseeable circumstances;
3. **compliance** – agreements must be complied with;
4. **information** – the exchange of information should be done in strict compliance with competition and other applicable laws, with parties taking reasonable care to ensure information is accurate and not misleading;
5. **confidentiality** – confidentiality of information is to be respected;
6. **responsibility for risk** – each party should bear their own risks; and
7. **justifiable request** – parties shall not use threats to obtain an unjustified advantage or to transfer an unjustified cost.

To assist parties, the principles of good practice include a table outlining examples fair and unfair practices.

ITALY

The food industry in Italy has been the object of public and political concerns, focusing on both volatile practices and relationships between market players along the industry supply chain.

Although the Italian food retail sector has experienced a notable consolidation process over the last 15 years, the three top retailers account for less than 35 per cent of the total value, unlike the UK, Germany, France and Spain where the shares of the three top retailers are equal to or higher than 55 per cent.

Two key factors could indicate the existence of buyer power in the Italian food retail sector:

- retailers have increased their bargaining power by forming ‘super-alliances’ (collaborative purchasing by chains of retailers); and
- retailer concentration can be high at a local level.

To better understand the competition issues in the sector, the Italian Competition Authority (ICA) undertook two market surveys. The first, published in 2007, looked at the food distribution chain, specifically in the fruit and vegetable sector; the second, completed in 2013, examined the large retail sector. Findings of the 2013 survey included that:

- food producers are confronted with complex and long negotiations;
- suppliers are often requested to deliver goods to retailers before an agreement is formalised; and

- retailers sometimes unilaterally vary contracts.

The last chapter of the survey focused on buyer power. Buyer power can be seen in positive terms in that 'powerful' retailers obtain better purchasing conditions and pass on the benefits to consumers. However, it can also be seen as detrimental to competition and consumer welfare in the long term.

A recent provision (Article 62 of law no. 27 of March 2012 (*Discipline of commercial relations relating to the sale of agricultural food products*)) introduced into Italian legislation could prove helpful to curb buyer power in vertical relationships within the agricultural food chain. It is designed to prevent unfair conduct and requires contracts to be formalised in writing. A number of unfair commercial practices, such as imposing unfair price conditions and applying objectively different conditions to equivalent transactions, are forbidden. The ICA has been given an enforcement role for this provision, including surveillance and fining powers. The ICA continues to monitor developments in the food sector.

OTHER COUNTRIES

Other jurisdictions (in addition to the United Kingdom and European Union) are choosing to adopt codes of conduct. The Irish Government plans to introduce regulations establishing a code of conduct in the grocery sector, following the introduction of the Competition and Consumer Bill on 31 March 2014, which empowered the Minister to make regulations about procedures that must be followed in commercial relationships in the grocery goods sector. The code may regulate contractual relations between retailers and distributors, as well as upstream suppliers. It may aim to prohibit certain practices currently engaged in by retailers (mainly the large retailers).

In August 2013, the Spanish Government enacted legislation based on a mixed model of regulation and self-regulation in commercial relations. It covers food contracts and abusive commercial practices, with self-regulation through a voluntary Code of Best Trading Conduct in food contracting, and a food chain watchdog.

A number of countries address similar concerns about buyer power in the food supply chain by legislation. In some cases it is by means of general competition legislation. In others it is specific to the grocery sector or a particular stage of the supply chain (such as between suppliers and retailers, or the supply of agricultural products).

In Japan a general prohibition applies to abuse of superior bargaining position as part of regulation of unfair trading practices. Specific conduct is designated as unfair and amongst other things includes unjust price reductions (which in one prosecution by the regulator involved the retailer reducing payments to the supplier as a result of a mark downs by the retailer), delays in payment, requests for monetary contributions and requesting other economic benefits such as intellectual property rights.

A number of countries have legislation that focuses on dealings between suppliers and retailers. Lithuania's legislation applies to the unfair practices of retailers (not just supermarkets). It aims at an appropriate balance between the interests of the suppliers and large retailers. It limits the use of market power by large retail undertakings enjoying a significant market power, and is enforced by the Competition Council. Latvia similarly regulates the use of a dominant position in retail trade generally, via amendments in 2008 to its competition laws. The statutory provision regulates relations between retailers and suppliers in the food and non-food chain considering retailers' buyer power and the suppliers' dependence in the relevant procurement market.

The Russian Federation and Hungary both have a combination of general provisions and those specific to food production and distribution. In Hungary's case this followed the failure of a non-binding code of conduct for big retail chains, with legislation covering not only retailers with significant market power but all types of retailers, for example, small convenience stores.

Those countries with legislation that is sector-specific include France (the agricultural sector) and Italy (food and agricultural products).

ATTACHMENT D: EXISTING REGULATION OF RELATIONSHIPS IN THE FOOD AND GROCERY SECTOR

THE PRODUCE AND GROCERY INDUSTRY CODE OF CONDUCT (PGICC)

The Produce and Grocery Industry Code of Conduct (PGICC) is a non-prescribed voluntary, industry run code established in 2000 as the Retail Grocery Industry Code of Conduct in response to a Joint Parliamentary Inquiry into the changing retail market environment and its implications for trading. The PGICC takes the form of a voluntary set of guidelines aimed at promoting fair trading practices in the produce and grocery industry. The PGICC covers vertical transactions within the produce and grocery industry supply chain and guides the conduct of businesses within the industry. The PGICC is intended to cover all participants (except consumers) in the Australian produce and grocery industry, including growers, processors, wholesalers, distributors and retailers.³³ It also provided a dispute resolution mechanism through the Produce and Grocery Industry Ombudsman (ombudsman).³⁴

The Produce and Grocery Industry Code Administration Committee (PGICAC) administered and monitored the operation of the PGICC. It was chaired by an independent Chairman, and committee members paid the costs of the Chairman and were responsible for promoting the code.

The PGICAC has not met since 2011. Its membership was producer, wholesaler and retailer representatives including the National Farmers' Federation, the Victorian Farmers' Federation, the Australian Chamber of Fruit and Vegetable Industries Limited, the National Association of Retail Grocers of Australia, the Australian Retailers Association, the Coles Group and Woolworths Limited.

The Australian Dairy Farmers resigned its membership on 27 January 2009 and the AFGC and the NFF resigned on 3 March 2009. The Horticulture Australia Council was officially closed in May 2010.

As the PGICAC has not met since 2011 and it is not clear if the remaining members still support the code, the PGICC could be considered to be no longer functioning.

The code addressed four issues:

- Produce standards and specifications³⁵ – produce standards and specifications (where available) are to be negotiated before a supply contract is entered into, and communicated in clear, meaningful and accurate terms. Produce may only be rejected based on these standards and specifications (or other objective criteria) – reasons for rejection must be provided;
- Contracts³⁶ – terms and conditions of supply contracts are to be negotiated between retailers and suppliers in clear, concise, meaningful and accurate terms; contracts are to include terms relating to dispute resolution; and the use of written agreements is encouraged;

³³ PGICC, clause 3.

³⁴ PGICC, clause 2.

³⁵ PGICC, clause 5.

³⁶ PGICC, clause 6.

- Product labelling, packaging and preparation³⁷ – suppliers will supply produce that is labelled and packaged in accordance with Australian and New Zealand labelling and packaging requirements; retailers will communicate labelling and packaging requirements clearly and accurately at the time of ordering; and retailers will provide reasonable notice of changes to individual labelling and packaging requirements; and
- Notification of acquisitions³⁸ – industry participants will notify the ACCC of any acquisitions.

The ombudsman provided mediation services for the produce and grocery industry in accordance with the PGICC.³⁹ Under the PGICC, parties first contact the other person and try to resolve the dispute. If the dispute cannot be resolved then the ombudsman will appoint a mediator from a panel of mediators to mediate the dispute. The dispute resolution service is open to anyone in the produce and grocery supply chain, regardless of whether they are part of an endorsing organisation.

As a voluntary code the PGICC provided high-level principles. The PGICAC considered that the strength of the PGICC was its ability to bring leaders along the supply chain together.

The PGICC was developed in response to the 1997 report which recommended a mandatory code. In its response, the then government supported the development of a voluntary code, stating that ‘The operation and effectiveness of the Code would be independently reviewed after three years of operation, or sooner if the Government believes circumstances warrant an earlier review. Should a review or developments indicate an unsatisfactory participation level, the Government could then pursue the option of a mandatory Code.’

The voluntary code was reviewed by Neil Buck in 2004. In his report, ‘Report of the Review of the Retail Grocery Industry Code of Conduct’ Mr Buck recommended the government take steps to implement a principles based code of conduct. In its July 2004 response the then government acknowledged that a lack of clarity in the relationship between some market participants caused problems, but noted that it did not consider that a mandatory code of conduct, which would impose additional regulation and compliance costs along the supply chain, would necessarily address these concerns. The then government indicated that if problems remained it would consider the appropriateness of mandating a Code, or parts of a Code, in law.

The PGICC has been criticised due to limited awareness of the code, a lack of industry support, and a lack of reporting responsibilities and protection from commercial retaliation.

Any effective voluntary code, whether not prescribed or prescribed, would need to address these issues.

THE AUSTRALIAN WINE INDUSTRY CODE OF CONDUCT

In December 2008, the voluntary Wine Industry Code of Conduct was launched. This code was developed by the Winemakers’ Federation of Australia and the Wine Grape Growers Association. Wine grape purchasers are able to become signatories to the code, and once they do, agree to comply with the code in their commercial dealings with grape growers.

³⁷ PGICC, clause 7.

³⁸ PGICC, clause 8.

³⁹ See PGICC, clause 10.

The code has two main aims:⁴⁰

- to establish a common Australian wine grape supply contract framework; and
- to provide a dispute resolution system to manage disagreements which arise over price or quality assessments.

Through its business, Dorrien Winemaking, Woolworths is a signatory to the Wine Industry Code. The Government understands that Coles does not purchase grapes directly from grape growers and is therefore not eligible to sign on to the code.

THE HORTICULTURE CODE OF CONDUCT

The Horticulture Code was introduced by the Howard government in 2007 following grower concerns over a number of years about the need to improve commercial transparency in fresh fruit and vegetable wholesale markets. At the time, growers and wholesalers could not agree on a voluntary code, so the government agreed to prescribe a mandatory code of conduct under the CCA.

The Horticulture Code applies to all growers and traders of horticulture produce, but not to parties that purchase horticulture produce for retail, export or processing.⁴¹

The purpose of the code is:

1. to regulate trade in horticulture produce between growers and traders to ensure transparency and clarity of transactions; and
2. to provide a fair and equitable dispute resolution procedure for disputes arising under this code or a horticulture produce agreement.

The code seeks to ensure transparency and clarity of transactions by requiring:

- parties to trade under written agreements (horticulture produce agreements);
- that traders (who may be agents or merchants) publish their terms of trade⁴² and only trade as either an agent or a merchant under one horticulture produce agreement;⁴³ and
- particular minimum terms to be included in a horticulture produce agreement.⁴⁴

If a dispute arises, parties to the code may use the procedure set out in the code or another dispute resolution procedure of their choosing. If either party chooses to use the procedure outlined in the code, the Horticulture Mediation Adviser can provide mediation services.

⁴⁰ The Australian Wine Industry Code of Conduct (November 2011), p. 2.

⁴¹ Horticulture Code, regulation 2.

⁴² Horticulture Code, clause 4.

⁴³ Horticulture Code, clause 7. Clause 7 states that a trader cannot act as both an agent and a merchant under one horticulture produce agreement. Prior to the introduction of the Horticulture Code, there was concern among growers that traders were minimising their risk and maximising their returns through the use of both agency and merchant models (see, for example, *Implications of the Australian Competition and Consumer Commission recommendations to amend the Horticulture Code of Conduct* (August 2009), p. 15). This is the issue that clause 7 seeks to address.

⁴⁴ Horticulture Code, clause 9.

Where one party begins the dispute resolution procedure set out in the code, the other party must participate in that procedure.

In 2008 the ACCC made a number of recommendations to improve the operation and effectiveness of the Horticulture Code. A number of these recommendations sought to extend the scope of the Horticulture Code, including to:

- regulate first point of sale transactions of horticulture produce between a grower and a retailer, exporter or processor; and
- regulate first point of sale transactions between a grower and a trader in horticulture produce in relation to agreements made before 15 December 2006.⁴⁵

These (and other) recommendations were met with strong and differing views within the industry.

Following the ACCC review, the then Minister for Agriculture appointed the Horticulture Code of Conduct Committee to consider the implications of implementing the ACCC's recommendations. The committee undertook extensive consultation with industry in the preparation of its report, which was made publicly available on 1 November 2009. In its report, the committee noted that business practices of the horticulture industry vary widely and that the implementation of the recommendations was expected to standardise practices throughout the industry. The committee predicted that this could be met with initial resistance, but it believed the industry would benefit from improved efficiencies and transparency in the long run.

No formal Government response has been issued in relation to the ACCC's review.

THE COMPETITION AND CONSUMER ACT 2010 AND THE AUSTRALIAN CONSUMER LAW

The object of the CCA is to 'enhance the welfare of Australians through the promotion of competition and fair trading and provision for consumer protection'.⁴⁶

Specifically of relevance to relationships in the food and grocery supply chain, the CCA prohibits a corporation with a substantial degree of market power from taking advantage of that power for a proscribed anti-competitive purpose.⁴⁷ The proscribed purposes listed in the CCA include eliminating or substantially damaging a competitor, preventing entry of a person in a market, and deterring or preventing a person from engaging in competitive conduct in a market.⁴⁸

In addition, the following general protections within the Australian Consumer Law (ACL) are of relevance to relationships in the food and grocery supply chain:

⁴⁵ If a trader and a grower have a written agreement entered into before 15 December 2006 (the date the regulations were registered), the Horticulture Code does not apply, unless the agreement has been varied since the commencement day of the code. Anecdotal evidence suggests that this exception applies to a large majority of relationships in the horticulture sector that would otherwise be covered by the code.

⁴⁶ CCA, s. 2.

⁴⁷ CCA, s. 46.

⁴⁸ CCA, s. 46.

- A person must not, in connection with the supply or possible supply of goods or services to a person (other than a publicly listed company), engage in conduct that is unconscionable.⁴⁹ A court will determine on a case-by-case basis what is unconscionable, and may take into account a number of matters to determine whether or not there has been a breach.⁵⁰
- Protections currently apply in relation to unfair contract terms. These provisions apply to all businesses which use standard form contracts in their dealings with *consumers*.⁵¹ The Government has been consulting on extending these protections to small businesses, and whether standard form contracts relating to *acquisition from* a small business (that is, as well as *supply to* a small business) should be covered. This may be relevant, for example, where large supermarkets contract directly with suppliers using standard form contracts. More information is available from the Treasury website.⁵²

In May 2014, the ACCC instituted proceedings in the Federal Court of Australia against Coles alleging that Coles engaged in unconscionable conduct in contravention of the ACL.

The ACCC alleges that in 2011, Coles developed a strategy to improve its earnings by obtaining better trading terms from its suppliers. The ACCC action alleges that this involved unconscionable conduct towards 200 of its smaller suppliers through providing misleading information to suppliers, using undue influence and unfair tactics and taking advantage of its superior bargaining position by, amongst other things, seeking payments when it had no legitimate basis for seeking them.

The ACCC is seeking pecuniary penalties, declarations, injunctions and costs through the legal proceedings. These proceedings arise from a broader investigation by the ACCC into allegations that supermarket suppliers were being treated inappropriately by the major supermarket chains. That broader investigation is continuing.⁵³

REVIEW OF COMPETITION POLICY

On 27 March 2014, the Minister for Small Business announced the final terms of reference for the Government's 'root and branch' review of competition policy. This is an independent review led by Professor Ian Harper and an expert panel.

The Harper Review has a broad remit. It is examining the competition framework, which is a vital part of a strong economy that drives continued growth in productivity and living standards.

49 Section 21 of the ACL.

50 Section 22 of the ACL. The matters a court may take into account include the relative strength of the bargaining positions between the parties; the extent to which the supplier was willing to negotiate the terms and conditions of any contract with the customer; the terms and conditions of the contract; whether, as a result of conduct engaged in by the business, the customer was required to comply with conditions that were not reasonably necessary for the protection of the legitimate interests of the supplier; whether the supplier has a contractual right to vary unilaterally a term or condition of a contract between the supplier and the customer; and the extent to which the supplier and the customer acted in good faith.

51 Section 23 of the ACL.

52 www.treasury.gov.au/ConsultationsandReviews/Consultations/2014/Small-Business-and-Unfair-Contract-Terms.

53 www.accc.gov.au/media-release/accc-takes-action-against-coles-for-alleged-unconscionable-conduct-towards-its-suppliers.

The review has scope to look at the competitiveness of key markets, including grocery markets and whether regulatory changes are necessary to enhance competition outcomes for consumers.

Further information about the Harper Review is available at <http://competitionpolicyreview.gov.au/>.

THE COMMON LAW AND FAIRNESS IN CONTRACTUAL DEALINGS

There appears to be broad acceptance in Australian case law that the obligation to act in 'good faith' requires parties to a contract to:

- perform all things necessary to enable other parties to a contract to enjoy the benefits of the contract; and
- act honestly and not arbitrarily or capriciously in exercising any discretionary powers under the contract.

While the meaning of 'good faith' remains difficult to definitively express, it appears that the obligation is focused on the actions of parties in exercising their express rights and discretions and is therefore focused on procedural rather than substantive fairness.

There are different views about whether the duty of good faith is implied by law in all contracts, or in certain kinds of contracts, or implied by fact in certain specific situations, or is better seen as a general principle for interpreting contracts.

The High Court has not ruled decisively on this matter and at this stage it has provided little guidance on the inclusion or application of the duty of good faith in contractual arrangements.

INTELLECTUAL PROPERTY PROTECTIONS IN AUSTRALIA

Intellectual property (IP) is protected in Australia through a number of mechanisms. The key mechanisms of relevance to the food and grocery industry are:

- the *Copyright Act 1968*;
- the *Patents Act 1990*; and
- the *Trade Marks Act 1995*.

Copyright protections in Australia are automatic. Some IP rights, such as ownership of confidential material, are not governed by legislation and must be enforced through the common law.

The above laws may apply to protect retailers' and suppliers' IP for their branded products.

ATTACHMENT E: BUSINESS COST CALCULATOR, REGULATORY BURDEN AND COST OFFSET ESTIMATE

Table 1 includes estimates of the compliance costs and regulatory offsets associated with prescribing the proposed Grocery Code as an opt-in code.

The compliance cost estimates assume that Coles, Woolworths, ALDI, Costco and Metcash agree to be bound by the proposed Grocery Code. Unless otherwise stated, the same assumptions have been applied in developing cost estimates for each of these businesses. (Where appropriate, different assumptions have been made for 'larger retailers' and 'smaller retailers' — the table notes the cost categories for which this has been applied.)

The Government is seeking views on whether the compliance cost estimates, and the underlying assumptions that have been used to estimate them (as outlined in Table 2) are accurate; and if they are not, what the appropriate cost categories and assumptions should be.

Table 1: BCC and offsets

Option 1	
Option name	Opt-in prescribed code of conduct — retailer costs
Option description	Prescription of an opt-in code of conduct via regulations under section 51AE of the CCA. Under section 51AD of the CCA, a person must not contravene, in trade or commerce, 'an applicable industry code'. Breaches of prescribed codes are a breach of the CCA and are subject to many of the remedies available under the CCA. The ACCC is responsible for enforcing prescribed codes of conduct, hence, complaints about non-compliance that cannot be resolved through the dispute mechanisms in a prescribed code can be directed to the ACCC.
Businesses affected	5
	Total cost for all businesses
Start up cost	\$53,594.16
Ongoing compliance cost per year	\$1,535.20
	\$7,676.00

Average Annual Compliance Costs (from Business as usual)

Costs	Business	Community Organisations	Individuals	Total Cost
Total by Sector	\$34,473.08	\$	\$	\$34,473.08
Cost offset	Business	Community Organisations	Individuals	Total by Source
Agency	\$34,473.08	\$	\$	\$34,473.08
Within portfolio	\$	\$	\$	\$
Outside portfolio	\$	\$	\$	\$
Total by Sector	\$34,473.08	\$	\$	\$34,473.08

Proposal is cost neutral? yes no

Proposal is deregulatory? yes no

Balance of cost offsets (\$8,574,444.42)

Note: a regulatory offset has been identified from within the Treasury portfolio. This offset relates to the Franchising Code reforms.

The following assumptions underlie the compliance cost estimates in the above tables.

Table 2: assumptions underlying estimates of compliance costs — retailers

Compliance cost	Query	Estimate
Provision of written notice		
<p>Providing written notice</p> <p>Occurs under the following obligations:</p> <ol style="list-style-type: none"> 1. Delisting. 2. Delisting — providing written notice of final decision after review. 3. Cancelling/reducing orders of stock for promotion — seeking Suppliers' written consent. 4. Cancelling/reducing orders of stock for promotion — providing reasonable notice of the cancellation/reduction. 5. In the event of failure to meet fresh produce standards provision of written notice of reasons for rejection. 6. In the event of changes to packaging, preparation etc standards, the provision of reasonable written notice, in certain circumstances. 7. In the event of requiring changes to supply chain procedures, the provision of reasonable written notice. 8. In the event of a range review, providing Suppliers with written notice. 	<p>Time it would take to undertake the task of providing written notice.</p>	<p>0.25 hours⁵⁴</p>
<p>Labour cost associated with providing written notice</p> <p>Occurs under the obligations listed above.</p>	<p>Hourly rate of the staff member that would undertake the task of providing written notice.</p>	<p>\$30.40 per hour⁵⁵</p>
<p>Occurrence of provision of written notice</p> <p>Occurs under the obligations listed above.</p>	<p>How many times per year written notice would be provided.</p>	<p>30 per annum⁵⁶</p>
<p>Number of staff members engaged in providing written notice</p> <p>Occurs under the obligations listed above.</p>	<p>Number of staff members in the organisation that undertake the task of providing written notice.</p>	<p>1 staff member⁵⁷</p>

⁵⁴ Assumes a standard form of notice is adopted and emailed.

⁵⁵ Assumes the task of sending the email is undertaken by an administrative assistant; ABS labour rates in RIS guidelines state that this is the appropriate hourly rate.

⁵⁶ Assumes that an event requiring that notice be provided to any particular supplier arises once a year; assumes each retailer has a relationship with 30 suppliers.

⁵⁷ Assumes one staff member would be responsible for emailing of notices.

Compliance cost	Query	Estimate
Confidential information obligation compliance		
Establishing systems to ensure compliance with confidential information obligation Start-up cost	Time it would take to establish these systems. Hourly rate of the staff member that would establish the systems. Number of staff members in the organisation that would undertake the task of establishing the systems.	40 hours ⁵⁸ \$43.70 per hour ⁵⁹ 1 staff member
Monitoring compliance with above systems	Time it would take to monitor compliance with above systems. Hourly rate of the staff member that would undertake the compliance monitoring. How many times per year compliance monitoring would take place. Number of staff members in the organisation that would be responsible for monitoring compliance.	2.5 hours ⁶⁰ \$34.20 per hour ⁶¹ 2 per annum ⁶² 1 staff member
Product ranging and shelf space allocation principles		
Publication of product ranging and shelf allocation principles Start-up cost	Time it would take to develop and publish these principles. Hourly rate of the staff member undertaking the task. Number of staff members in the organisation that would be involved in developing and publishing the principles.	40 hours ⁶³ \$43.70 per hour ⁶⁴ 1 staff member
Updating product ranging and shelf allocation principles from time to time	Time taken to update the principles. Hourly rate of the staff member that updates the principles. How many times per year the principles are updated. Number of staff members in the organisation involved in updating the principles.	8 hours ⁶⁵ \$43.70 per hour ⁶⁶ 1 per annum ⁶⁷ 1 staff member

58 Assumes this task will take 1 week of full time work (8 hour days, 5 day week).

59 Assumes someone with some form of professional/technical skills (for example, in business processes) will be required to undertake this task; ABS labour rates in RIS guidelines state that this is the appropriate hourly rate.

60 Assumes that the task of checking that the organisation has complied with its systems is undertaken twice a year and takes two and a half hours.

61 Assumes a manager/professional is *not* needed for this task; have therefore adopted ABS economy wide non-managerial hourly rate in RIS guidelines for this wage rate.

62 Assumes that checking that the organisation has complied with its systems takes place twice per year.

63 Assumes that it takes five days of full-time work (eight hour days) to first develop and publish these principles.

64 Assumes someone with some form of professional/technical skills will be required to undertake this task (for example, marketing skills); ABS labour rates in RIS guidelines state that this is the appropriate hourly rate.

65 Assumes task takes one day of full time work.

66 Assumes person of similar standing updates the principles as the person that developed them in the first place.

67 Assumes principles are reviewed and updated once per year.

Compliance cost	Query	Estimate
Record keeping and reporting		
Code Compliance Manager record keeping of complaints ⁶⁸	Time it would take to keep a record of a complaint. Hourly rate of the staff member responsible for keeping records. Number of times per year record is made. Number of staff members in the organisation that would be responsible for keeping these records.	1/2 hour ⁶⁸ \$43.70 per hour ⁷⁰ 12 per annum ⁷¹ 1 staff member
Code Compliance Manager reporting six-monthly	Time it would take to prepare this report. Hourly rate of the staff member responsible for preparing the report. How many times per year the report will be prepared. Number of staff members in the organisation that would be responsible for preparing the report.	4 hours ⁷² \$43.70 per hour ⁷³ 2 per annum ⁷⁴ 1 staff member
Dispute resolution — complaints handling manual		
Development of a written complaints handling procedure ⁷⁵ Start-up cost	Time it would take to develop a complaints handling procedure. Hourly rate of the staff member undertaking the task. Number of staff members in the organisation that would be responsible for developing the procedure.	24 hours ⁷⁶ \$43.70 per hour ⁷⁷ 1 staff member

68 These records must be provided to the ACCC at least every 6 months (or upon written request), or the ACCC must be allowed to inspect them; assume no additional costs associated with doing this.

69 Assumes it takes half an hour to make a record of a complaint.

70 Assumes someone with some form of professional/technical skills will be required to undertake this task (assume it is the Code Compliance Manager); ABS labour rates in RIS guidelines state that this is the appropriate hourly rate.

71 Assumes a complaint is made which requires an update to the records to be made once per month.

72 Assume that it takes half a day of full-time work to pull together this report.

73 Assumes someone with some form of professional/technical skills will be required to undertake this task (assume it is the Code Compliance Manager); ABS labour rates in RIS guidelines state that this is the appropriate hourly rate.

74 6 monthly preparation specified in the proposed Grocery Code.

75 This must also be provided to the ACCC — costings assume that there are no additional costs associated with providing this document to the ACCC.

76 Assumes that it takes three days of full-time work (eight hour days) to first develop this procedure.

77 Assumes that someone with some form of technical skills will be required to undertake this task (assume it is the Code Compliance Manager); ABS labour rates in RIS guidelines state that this is the appropriate hourly rate.

Compliance cost	Query	Estimate
<i>Dispute resolution — complaints handling manual (continued)</i>		
Annual update/reviewing of complaints handling procedure ⁷⁸	Time it would take to review and update this procedure. Hourly rate of the staff member that would review and update. How many times per annum a review and update would take place. Number of staff members in the organisation that would undertake the review and update.	4 hours ⁷⁹ \$43.70 per hour ⁸⁰ 1 per annum ⁸¹ 1 staff member
<i>Compliance training</i>		
Initial compliance training Start-up cost	Time it would take to undertake the training. Hourly rate of those staff member(s) undertaking the training. Number of staff members in the organisation that would take part in the training.	1 hour \$34.20 per hour ⁸² 500 staff members (large) 9 staff members (small) ⁸³
New starter and re-fresh compliance training	Assumes that the organisations procure an online product which facilitates online training (that is, an online training module).	\$35,000

⁷⁸ This must be provided to the ACCC at least every 6 months (or upon written request), or the ACCC must be allowed to inspect it. Costings assume that there are no additional costs associated with providing this document to the ACCC.

⁷⁹ Assumes task takes half a day of full time work.

⁸⁰ Assumes someone with some form of professional/technical skills will be required to undertake this task (assume it is the Code Compliance Manager); ABS labour rates in RIS guidelines state that this is the appropriate hourly rate.

⁸¹ Annual reviewing specified in the proposed Grocery Code.

⁸² Assumes that on average, these staff members are paid a non-managerial wage; have adopted ABS economy wide non-managerial hourly rate in RIS guidelines for this wage rate.

⁸³ Number of staff assumed for the smaller organisations based on pro-rata scaling down of number of staff assumed for larger businesses. Scale down based on comparison of differences in overall staff numbers of Coles and Woolworths as compared to Costco and Metcash.

ATTACHMENT F: WHO WILL BE CONSULTED AND HOW?

CONSULTATION PRINCIPLES

- Consultation is purposeful and clearly defined in order to obtain stakeholder views on the effectiveness of the proposed Grocery Code and inform the Government's decision on whether to take it forward as an opt-in code prescribed under regulations under the *Competition and Consumer Act 2010* (the CCA).
- Feedback and views will be sought from a broad range of stakeholders including: grocery supply chain participants (including small, medium and large businesses); legal bodies; consumer advocates; other interest groups; and relevant government agencies.
- Adequate time will be provided to allow participants to fully consider the issues and provide considered responses.
- Flexible mechanisms will be made available to stakeholders to allow them to provide feedback without the need to submit a formal submission and in a form that is more suitable to them.

PROCESS FOR CONSULTATION

- An exposure draft of the Grocery Code and associated consultation paper will be released for a period of five weeks for public feedback. Stakeholders will be able to make formal written submissions or may choose to provide brief comments via the Treasury website. This process may be supplemented by stakeholder meetings or roundtables, particularly with parties not directly involved in the drafting and preparation of the proposed Code.
- Based on stakeholder feedback on the draft Code, the Government may decide to progress towards prescribing the Code under the CCA. This process would likely involve further targeted stakeholder consultation, which may result in the Code being revised to reflect public feedback. Importantly, stakeholder views will continue to play an important role in informing subsequent Government decision making processes towards prescribing the Code into law.

EFFECTIVE ENGAGEMENT WITH SMALL BUSINESS AND THE PUBLIC

It is important that the consultation is accessible to small businesses and the general public. To make the issues as understandable and accessible as possible a number of steps will be taken:

- The key issues for consultation will be summarised in a 2 page fact sheet to help stakeholders navigate the key issues as simply as possible.
- There will be a facility for interested parties to provide written submissions in response to the consultation paper, or alternatively to leave a short comment on the proposed Code, using the 'electronic submissions' option on the Treasury website. This will help encourage submissions from stakeholders who may view formal submissions as too labour intensive or official.
- A five week timeframe will be provided to give sufficient time for stakeholders to develop submissions and raise enquiries.

STAKEHOLDERS

An initial listing of stakeholders is provided below.

Food and grocery sector organisations and industry bodies

- ALDI
- Australasian Association of Convenience Stores
- Australian Chamber of Commerce and Industry
- Australian Food and Grocery Council
- Australian Industry Group
- Australian National Retailers Association
- Australian Retailers Association
- AUSVEG
- Coles
- Convenience and Mixed Business Association Inc (CAMBA)
- CostCo
- Foodworks
- Harris Farm Markets
- Master Grocers Australia
- Metcash
- National Association of Retail Grocers of Australia
- National Farmers' Federation
- Southern Sydney Retailers Association
- WA Independent Grocers Association
- Woolworths

Consumer bodies

- Choice
- Consumer Action Law Centre
- Consumers SA
- Queensland Consumers' Association
- Consumers' Federation of Australia

Small business

- Council of Small Business of Australia (COSBOA)
- Australian Small Business Commissioner

Government

- Australian Competition and Consumer Commission
- Attorney General's Department
- Department of Agriculture
- Department of Industry
- The Department of the Prime Minister and Cabinet