SmallBusiness NSW Commissioner

Grocery Code Consultation Paper
Small Business, Competition and Consumer Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: grocerycode@treasury.gov.au

Dear Sir/Madam,

Submission to the Food and Grocery Code Consultation Paper

Thank you for giving the Office of the NSW Small Business Commissioner (OSBC) the opportunity to comment on the Food and Grocery Code Consultation Paper (Consultation Paper).

The OSBC was established in mid-2011 to support small businesses throughout NSW. The role of the OSBC is to:

- provide dispute resolution services;
- speak up for small business within government; and
- deliver quality business advice through Small Biz Connect.

The OSBC is focused on improving the operating environment for small businesses within NSW. The OSBC therefore supports measures aimed at improving the quality of commercial relations between large retailers and small suppliers. In particular, the OSBC supports making the commercial relationship between small food and grocery suppliers and large retailers more equitable and less susceptible to being dominated by those retailers due to their superior bargaining power.

Although the introduction of the Code in its proposed form may represent a step in the right direction in improving the commercial relations between large retailers and small suppliers, the existing imbalance in bargaining power, combined with the significant exemptions permitted by the Code, may limit the Code's potential to promote significantly improved relations.

The OSBC has reviewed the Consultation Paper and makes the following specific comments directly relevant to small business suppliers.

➢ **Grocery Supply Agreements (questions 8 and 9)**

The OSBC supports the proposed provisions of the Code which will require retailers to enter into written "Grocery Supply Agreements" (GSAs) and for those GSAs to contain provisions on six fundamental matters. This will go some way to ensuring that the terms which govern the commercial relationships between small suppliers and large retailers are clearly understood by both parties, which is not always the case at present.

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Keeping records of GSAs

The OSBC suggests that consideration be given to increasing the proposed 12 month period that a retailer must keep a copy of each GSA following its termination, perhaps to 24 or 36 months. This will not materially increase the administrative burden on retailers, especially if the GSAs are stored electronically. Increasing this time frame may assist the Australian Competition and Consumer Commission (ACCC) with gathering evidence when undertaking oversight and enforcement activities.

Unilateral and retrospective variations

The OSBC supports the Code's proposed general prohibition on retailers unilaterally and retrospectively varying GSAs. However, in recognition that retailers and suppliers may wish to agree to allow the retailer to make those types of variations, the OSBC supports the Code requiring the terms of such agreements to be expressly included in GSAs.

The OSBC supports the principle that the threshold for exempting retrospective variations should be higher than for unilateral variations, as proposed in the Code. For this reason, we suggest that a retailer should also be required to give reasonable notice to a supplier of a retrospective variation, as is required for unilateral variations. From a technical perspective, this may already be the case, since a retrospective variation made by a retailer without the consent of the supplier is also likely to constitute a unilateral variation.

- **Conduct generally prohibited and exemptions (questions 10, 11 and 12)**

The OSBC welcomes the Code's regulation of retailer conduct that has been the subject of concern in the food and grocery industry. The general prohibition of certain types of conduct proposed in the Code will assist with setting common industry expectations and standards for large retailer conduct.

Conditions and safeguards attached to exemptions

Subject to our comments below, the OSBC supports attaching conditions and procedural safeguards (for the benefit of suppliers) to the exemptions available to retailers from the general conduct requirements. This includes giving retailers the onus of proving that they have met the conditions of a particular exemption.

These features will provide some protection for small suppliers that agree to exemptions in their GSAs with major retailers. At the very least, having the exemption conditions documented in the GSA will give small suppliers an opportunity to understand what they are being asked to agree to.

The overall effect of the exemptions

The Consultation Paper states that the proposed exemptions recognise "the principle that an effective code should avoid imposing unnecessary limitations or intrusions into normal commercial decision making" (p16). The problem, of course, is that the decision making environment in the food and grocery sector is dominated by large supermarkets and characterised by a significant imbalance in bargaining power between those supermarkets and smaller suppliers. The existence of this imbalance was expressed in evidence received by the Senate in its inquiry into the sector (Senate Select Committee on Australia's Food Processing Sector, 2012 *Inquiry into Australia's food processing sector*, p50) (Senate Inquiry).

As currently proposed, the availability of these exemptions (as well as the exemptions to unilateral and retrospective variations to GSAs) is based on agreement being reached with the supplier, and the terms of that agreement being recorded in a GSA. In other words, the exemptions are based on the premise that negotiations take place between a retailer and supplier. Given the superior bargaining power of the large retailers, which often leads to standard form contracts being offered on a "take it or leave it" basis, it is arguable that the premise of negotiations (or at least fair negotiations) taking place will often not be borne out in reality.

The OSBC therefore agrees with the statement in the Consultation Paper that:

> "*there is a risk that the cumulative effect of these exemptions may undermine the ability of the Grocery Code to improve retailer-supplier relations. 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*" (p17).

The overall effect may be that the Code will do little to prevent GSAs from being skewed in favour of large retailers.

Extension of unfair contract term protections to small businesses

Some exemptions allowed by the Code may be characterised as unfair contract terms. If such terms are contained within standard form contracts offered to small business suppliers, it is possible that they may be captured by the Federal Government's proposed extension of unfair contract term protections to small businesses.

Whether this may offer an alternative means of redress for small suppliers who, because of their inferior bargaining power, cannot negotiate GSAs offered on a "take it or leave it" basis, will depend on the terms of any unfair contract protections that may be extended to small businesses, and the legal interaction between the Code and those statutory protections. We suggest that further consideration be given to these issues, pending the outcome of the Federal Government's consideration of this matter.

"No disadvantage" test

The OSBC believes there is merit in applying a "no disadvantage" test to a retailer's reliance on an exemption provided for in a GSA. This test would support the intention of limiting undesirable retailer behaviour while allowing sufficient flexibility to support *mutually* beneficial supply agreements.

For example, the proposed exemption allowing retailers to require a supplier to make a payment for better positioning or more shelf space, even if the supplier does not request better positioning or more shelf space, would be more acceptable to small suppliers if such a requirement was measured against the standard of whether the supplier is materially disadvantaged or not from having to make such a payment.

- **Good faith obligations in the Code (questions 13, 14 and 15)**

The OSBC supports the inclusion in the Code of a duty on retailers to act in good faith. The most appropriate option, in the OSBC's view, is for good faith to be retained as a stand-alone provision in the Code applying to retailers only.

This is appropriate because it is the conduct of large retailers that is sought to be improved through the introduction of the Code. Further, as acknowledged in the Consultation Paper, any assessment of whether a retailer has acted in good faith will take into account surrounding circumstances, which may include the conduct of suppliers.

If compliance with the duty of good faith leads to increased compliance costs for large retailers, this is likely to be offset by improved and more productive retailer-supplier relationships, and fewer disputes.

- **Dispute resolution mechanisms in the Code (questions 16, 17 and 18)**

Access to external dispute resolution mechanisms

Allowing retailers to avoid attending arbitration or mediation if they determine that a supplier's complaint is "vexatious, trivial, misconceived, or lacking in substance" or that the supplier has not "acted in good faith" unfairly places the decision-making power in relation to commencing dispute resolution processes firmly with the retailer.

This may discourage suppliers from using the dispute resolution processes under the Code, especially given that there is evidence that many small suppliers are hesitant to raise complaints at all.

For example, the Senate Inquiry "heard repeatedly throughout its inquiry that food manufacturers were reluctant to speak publicly about specific instances of abuse of market power by the major supermarkets. The committee encountered a genuine reluctance for witnesses to come forward and give evidence on these matters, even on a confidential basis" (Senate Inquiry, p52-53).

The ACCC, in its recent investigation into allegations that supermarket suppliers were being treated inappropriately by the major supermarket chains, also found that suppliers were reluctant to speak out because of what they perceived may be the consequences of providing information to the ACCC (ACCC Media Release no. 102/14, *ACCC takes action against Coles for alleged unconscionable conduct towards its suppliers*, 5 May 2014).

For this reason, consideration should be given to having an independent third party, namely a mediator or arbitrator, determine whether a complaint is vexatious etc as a preliminary or initial step when handling a dispute referred to them by a supplier under the Code.

The costs of mediation/arbitration

From the perspective of small suppliers, the cost of mediation or arbitration should be as low as possible. If mediation or arbitration is too costly, this will discourage small suppliers from using the external dispute resolution processes available under the Code. Any difficulty a small supplier may have in contributing to the costs of mediation or arbitration should also be considered.

Given its experience with offering both informal and formal dispute resolution processes for small businesses which are widely used by NSW small businesses, the OSBC would be willing to discuss this aspect further with The Treasury.

➢ **Policy options being considered**

The OSBC supports the prescription of the Code as a mandatory code of conduct under the *Competition and Consumer Act* 2010 (Cth). This is because by covering all retailers, it would provide greater certainty and consistency in the relationships between suppliers and retailers.

If the Code were to be retained as an opt-in code, as currently proposed, there is a risk that major retailers (other than Woolworths and Coles) may choose not to opt-in, or to withdraw their participation at a later date, causing uncertainty and inconsistency in supplier-retailer relationships.

We assume that Woolworths and Coles will opt-in given that they, together with the Australian Food and Grocery Council, have drafted and brought forward the proposed Code. The Consultation Paper, however, contains no indication that those two retailers have in fact expressed an intention to opt-in. Given their combined 65% share of the grocery market, if the Code was implemented as an opt-in code and Woolworths and Coles did not opt-in, that would undoubtedly undermine industry support for the Code.

Should you wish to further discuss any of the issues raised in this submission please contact Georgos Papanastasiou, Assistant Advisor, Advocacy on (02) 8222 4833 or georgos.papanastasiou@smallbusiness.nsw.gov.au.

Yours sincerely

Robyn Hobbs OAM
Small Business Commissioner

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