





**Response to Draft Report
Independent Review of the Food and
Grocery Code of Conduct
August 2018**

**NSW Farmers' Association
Level 6, 35 Chandos Street
St Leonards NSW 2065**

T: (02) 9478 1000 | F: (02) 8282 4500
W: www.nswfarmers.org.au | E: emailus@nswfarmers.org.au
 @nswfarmers  nswfarmers

For further information about this submission, please contact:
Kathy Rankin
Policy Director – Business, Economics and Trade
02 9478 1008 | rankink@nswfarmers.org.au

Table of contents

Contents

Table of contents	4
About NSW Farmers.....	5
Executive summary	6
Area for Improvement - Major wholesaler Metcash should become a signatory.....	7
Area for Improvement - New fair dealings provision	9
Area for improvement - An independent adjudicator	11

About NSW Farmers'

A profitable and sustainable New South Wales farming sector

The NSW Farmers' Association is Australia's largest State farming organisation representing the interests of its farmer members.

Farmers across New South Wales produce more than \$15 billion worth of food and fibre every year, representing around one quarter of Australia's total agricultural output. Our state's unique geography means a wide variety of crops and livestock can be cultivated and nurtured. NSW Farmers is Australia's only state-based farming organisation to represent the interests of farmers of all agricultural commodities – from avocados and tomatoes, apples, bananas and berries, through grains, pulses and lentils to oysters, cattle, dairy, goats, sheep, pigs and poultry.

Our focus is not just on issues affecting particular crops or animals – it extends to the environment, biosecurity, water, economics, trade and rural and regional affairs. We also have an eye on the future of agriculture; we are advocates for innovation in agriculture, striving to give our members access to the latest and greatest innovations in research, development and extension opportunities. Our industrial relations section provides highly specialised advice about labour and workplace matters.

Our 100-plus regional branch network ensures local voices guide and shape our positions on issues which affect real people in real communities. Members are the final arbiters of the policies of the Association – through our Annual Conference and elected forums such as Executive Council, members can lobby for the issues which matter to them and their community to become Association policy. Our issue- and commodity-specific Advisory Committees are elected by members to provide specialist, practical advice to decision makers on issues affecting the sector. We are proudly apolitical – we put our members' needs first.

In addition, NSW Farmers has partnerships and alliances with like-minded organisations, universities, government agencies and commercial businesses across Australia. We are a proud founding member of the National Farmers' Federation.

Executive summary

NSW Farmers' welcomes the release of the Draft Report of the Independent Review of the Food and Grocery Code of Conduct.

In general NSW Farmers' supports the 14 recommendations included in the Draft Report and provide additional comment in support of the three main areas of improvement, being:

- Major wholesaler Metcash should become a signatory
- New fair dealings provision that reframes the current good faith provision, and
- An independent adjudicator

Farmers need supply chain certainty. They need a level and fair trading environment, equitable and reliable access to ports, competitive prices for transportation of goods and reliable and affordable supplies of inputs such as fuel and electricity. Domestic and regionally-distributed value-adding opportunities are key to securing enhanced market access to trade our highly sought after goods. Farmers have the capacity to grow the pre- and post-farm gate value of produce, as well as reinvigorating rural communities.

Making the agriculture sector strong is essential to driving greater price competition for consumers and growers alike. When agriculture does well, the broader community does well. Lifting the value of production will better enable farmers to ride out the tougher times and give consumers increasing confidence about the quality of the products they purchase.

Creating farm business confidence is an essential ingredient that will lift the value of production now and into the future. The Food and Grocery Code of Conduct has an important role in removing distortions that exist within the Australian food and grocery sector and by strengthening its application will have a beneficial effect to reduce pressure to agree unfair trading terms, consistency and certainty for supply agreements, and seek to identify and remove anti-competitive behaviour.

Area for Improvement - Major wholesaler Metcash should become a signatory

NSW Farmers' Association supports the proposal that Metcash should become a signatory to the Grocery Code to improve its dealings with suppliers and provide access to equitable dispute resolution processes.

NSW Farmers' members have considerable concern for the implications of market concentration in the food and grocery sector. In particular the growing gap between the farm gate value of food and the price paid by consumers at the supermarket indicates that the capture of value in the food supply chain is dominated by the major participants in the supermarket trade.

In response to these concerns NSW Farmers supports a mandatory code for all major supermarkets that has a broader remit than that presently embodied within the code. However, it is critical that the Code's provisions apply to all supermarkets in regulating the retailer – supplier relationship to protect primary producers who are either direct suppliers, or alternatively supply food processors and wholesalers who in turn supply retailers.

Not with standing these concerns, NSW Farmers recognises the role of the Food and Grocery Code in developing the rules required to ensure that the market power exercised by the major supermarket chains does not impede the ability of the market to return value to the farm gate.

The ACCC has the capacity to enforce compliance against the Code by signatories to the Code. Therefore, unless all major supermarkets are required to participate in the Code and comply with the provisions, the Code will be less effective in restraining the use of market power with regard to costs and risks faced by suppliers caused by unfair practices that these retailers are able to undertake.

On this basis achieving adequate participation of the supermarket sector is crucial to ensuring that the Code operates in a manner that is satisfactory to the farming industry, and meets the code's objectives to build and sustain trust and cooperation throughout the grocery supply chain.

In response to the Government's initial consultation on a draft code, NSW Farmers' recommended that after the commencement of the code a review be undertaken to determine the proportion of retailers that had become signatories to the code. The reasoning was to enable the consideration of whether nonparticipation, particularly where driven by strategic avoidance, was hindering the positive impact that the code was having on the market; and if so provide the basis for mandating the code.

Additionally it is important to note that due to the high market concentration in the supermarket sector, the concerns of the behaviour of the major supermarkets are not limited to the aspects to be regulated by the code. This includes issues such as misuse of market power, unconscionable conduct and the use of unfair contract terms that are not provided for within the code.

There are general truths about the industry regardless of the commodity produced – farmers are 'price takers', they are captive to market and climate forces beyond their direct control and long

supply chains leave them vulnerable when something goes wrong 'beyond the farm gate'. Many of the issues relating to competition policy, pricing and regulation rest at a Commonwealth level; regulation of food safety, biosecurity and funding for supply-chain related infrastructure is largely the responsibility of state and territory governments.

Farmers recognise that the price paid by a consumer varies significantly from the price paid to them at a wholesale level. There are many and varied reasons for this – some additional costs are necessary to enable treatment of the raw product for human consumption (for example the pasteurisation of milk). Some value adding and packaging is required for a product; in addition, the retailer will have their own costs which they will need to recoup. However unless all supermarkets are included in the Code, there remains a lack of transparency on the pricing of retail goods. A general competition imbalance between large retailers and (generally) small growers does not assist in this regard.

Area for Improvement - New fair dealings provision

NSW Farmers' Association supports reframing the good faith provision to focus on fair dealings between the parties.

Delay in settling invoices is an issue across all sectors of the economy. Maintaining a healthy cash flow situation is vital to business continuity, supplier certainty and business confidence. Small and medium enterprises however, often bear a disproportionately high burden from long delays in the settling of invoices. This practice is unfair.

The NSW Farmers believes that there is a strong relationship between farm-gate prices paid to farmers and the final retail price, if the commodity supply chain is competitive. In uncompetitive markets the relationship between farm-gate and retail prices breakdown. This is more to do with the ability of the processor or the retailer not to pass on the economic surplus of the transaction down the supply chain or to the consumer. Farmers, as price takers, tend have the weakest bargaining position in the supply chain.

Competitive retail markets are a necessary but insufficient measure to ensure a closer link between retail and farm-gate prices. The retail market for fresh food or groceries can be competitive, but if certain stakeholders within the supply chain have substantial market power, the economic surplus from the sale of fresh food and groceries will not find its way to the farmer. There does not have to be a contravention of market power regulatory provisions for the link between farm-gate and retail prices to break down. This has been demonstrated in the dairy supply chain, and by the recent ACCC report into the dairy industry. The subversion of price signals in the supply chain is a market failure that leads to poor economic and social outcomes.

Codes of conduct

Through industry codes of conduct, the Commonwealth Government (through the ACCC) can investigate unfair payment terms and can, where a breach of competition policy occurs, consider remedies at law. There are many industry codes of conduct which exist across the agriculture sector – recently, the ACCC recommended the adoption of a mandatory code of conduct for the dairy industry. The horticulture industry now has a mandatory code of conduct, with a voluntary code having first been put in place in 2007. At present, a review is taking place into the Food and Grocery Code of Conduct, a voluntary code which regulates trade between supermarkets and their suppliers.

NSW Farmers notes the recent commentary on the food and grocery code by Graeme Samuel AC, the independent chair of the review into that code. Mr Samuel suggested that this code should be applied on a mandatory basis¹. While codes of conduct assist in the regulation of trading arrangements, there remains an enormous power imbalance between small and medium tier suppliers and multi-billion dollar supermarkets, and their supply chains – all the 'good faith' negotiation provisions in the world cannot prevent the abuse of market power between a farmer with a time-sensitive crop or product seeking a buyer of those goods at a fair price.

¹ Ex-ACCC boss Graeme Samuel recommends major changes to grocery code of conduct, Australian Financial Review, 23 May 2018 <http://www.afr.com/business/manufacturing/exacc-boss-graeme-samuel-recommends-major-changes-to-grocery-code-of-conduct-20180523-h10fms>

Horticulture

The now-mandatory Horticulture Code of Conduct provides a good case study in point. The Code requires a grower to enter into an agreement (known as a Horticulture Produce Agreement (HPA)) with the person purchasing or trading their produce (defined as either an agent or merchant, respectively). The Code itself outlines generally-agreed terms, and requires the parties to the HPA to negotiate arrangements such as payment terms, the price paid, the method of delivery and the manner in which produce can be rejected. Ambiguities in the Code have created tension between grower groups and industry bodies, each seeking to ensure fair terms for their respective members.

Importantly, the Code does not specify the precise timeframe in which the person/party buying the produce is required to pay for it – rather, the Code simply requires that the parties agree on the payment terms in writing in the HPA. While the Code assumes that the parties will negotiate such arrangements ‘in good faith’, the reality is that a much larger trader will generally specify payment terms which advantage the trader over a much smaller grower.

The ambiguity in the definition of key terms in the Code is a key warning to other industries seeking to enact codes of conduct – either voluntary or mandatory. Codes of conduct seek to address trading imbalances – however, to fairly address these imbalances, fair definition of essential terms must form the foundation of the code, rather than be left to negotiation between parties of varying size and power.

Area for improvement - An independent adjudicator

NSW Farmers' Association supports the proposal for an independent adjudicator with the power to resolve individual complaints, make binding decisions and award compensation.

Growers have expressed concern and frustration about the enforcement of codes particularly when significant power imbalances exist between them. Notwithstanding the operation of dispute resolution mechanisms under the codes, growers in particular, have expressed hesitation in raising concerns about commercial agreement for fear of retribution. While the ACCC has established an anonymous hotline to allow growers to refer potential unfair terms for investigation, growers fear the loss of contracts and sales pathways for their product if they raise concern about the terms of trade.

Moving produce from paddock to plate in an efficient and timely manner is essential to product quality, freshness and food safety. New South Wales has some of the longest agricultural supply chains in the country, with GrainGrowers Limited finding that transport costs can account for up to 40 per cent of farmers' post-gate costs.

Agricultural supply chains have changed. Historically, locally-grown produce was picked, packed and distributed at local distribution centres throughout regional areas. Increasingly however, produce is picked locally and sent to more centralised packing and/or distribution centres, often located long distances from the place it was grown. These 'value added' products are then shipped back to the regional areas where they were grown and sold to consumers at a price significantly above the farm-gate price paid to the farmer.

Producing food and fibre to the increasingly exacting standards of consumers is a daily challenge for our farmers. It does not come without cost to them and their business. This is a cost which, all too often, is not recognised by the consumer when they purchase a blemish-free product at their local supermarket.

Produce marketing plays an enormous, and beneficial, role in the ability of our farmers to sell to domestic and international consumers. However, increasingly exacting standards also come with additional implementation costs. There is also an expectation that a farmer will simply absorb increasing costs to achieve higher quality, while the consumer continues to pay the same, or even lower, prices for the same goods in their supermarket or local supplier.

Consumers need to recognise that there is a price to pay for quality produce, both in the quality of the end product and for the processes and procedures involved in nurturing the product, be it animal or plant. Consumer expectations around animal welfare and chemical use, for example, require investments by farmers in alternative approaches to dealing with welfare practices and the use of chemicals.

Increasing quality expectations

Supermarkets and major retailers, on behalf of their customers, demand ever increasing quality of the produce they stock. While industry has developed quality assurance standards and guidelines

for fresh produce, consumers are generally presented with the ‘pick of the crop’ when they head down the aisle of their local supermarket.

Increasing the quality of food produced comes with added on-farm costs. Producing wheat with higher protein requires a farmer to consider investing in fertilizer, farmers in frost-prone areas will invest in equipment which will mitigate the risk of frost damage to fruit and vegetables. Blemish-free fruit requires attention to detail around pests, including that fruit does not fall to the ground before it is packed for distribution and to added care, and cost, during the harvest period.

Supermarkets and major traders will generally only take so-called ‘Number 1s’, referring to the highest quality fruit – what a farmer does with any fruit of a lesser quality is essentially left to the farmer to resolve.

Objective measurements of quality

A component of the price paid to producers is based on compliance with fixed specifications, both food safety regulations and purchasers specifications. The purchaser sets a certain product specification that is designed to ensure that the product adheres to regulatory and consumer expectations. Compliance with these specifications is determined through the purchaser testing the product. Consequently there is concern amongst producers that there is little transparency or accountability for these grading regimes.

For the sale of livestock direct to the processor (‘over-the-hooks’ transactions) and the sale of raw milk by farmers to dairy processors there are a series of tests and measurements conducted to determine the quality of the product supplied. The producer is paid accordingly. Poor results in these measurements have a significant impact on the final price received. Currently there is limited transparency around these tests and there is poor capacity for farmers to be able to dispute the results.

To enhance transparency in this area NSW Farmers has been advocating for a greater use of objective measurements and technology. This technology offers the potential for the quality of the product to be consistently determined and for any concerns to be openly investigated. It is vital that this technology is supported and that it is the preferred means of demonstrating regulatory compliance.

Regulation of agriculture

In 2017 the Productivity Commission released an investigation into the Regulation of Agriculture. It noted that in general, regulation adds costs and compliance burden on the economy. It noted that striking the right balance between necessary and burdensome regulation is essential to the efficient operation of the sector. The Commission also considered the necessity of regulation in agriculture, noting that the sector broadly supported necessary regulation.

There are many types of regulation which affect agriculture. This includes regulations governing the movement of on-farm machinery on roads, through to the safe handling of animals, food safety practices in packing sheds, industrial practices, management of the environment and the use of chemicals, and animal medicines.

Regulation, at a high-level, adds compliance costs in time, money and effort. When done properly, it can also assist a farmer to achieve a high price for their goods. For example, regulations governing the definition of ‘organic’ assist growers of organic produce to receive a price premium for their product. The strict regulation of what does and does not constitute organic offers an incentive for farmers to determine whether this is a farming system they are prepared to adopt and invest in.

As a matter of principle, regulation should only be implemented where there is a clear need. While accepting the need for regulation, NSW Farmers believes that some regulations are designed to hinder the operation of farm businesses, rather than assist them to grow and prosper.

An independent arbiter

Given the unequal bargaining power within food supply chains, and concerns about competition and abuse of market power, the establishment of a commissioner or advocate for the farming sector, with legislated authority to address the following is supported:

- code compliance on unfair payment terms;
- advocacy on behalf of the farming sector on competition and abuse of power matters; and
- analysis and monitoring of farm-gate and retail prices on a basket of goods to assess the competitiveness within supply chains.