Independent Review of the Food and Grocery Code of Conduct 2023-24

Consultation Paper February 2024

Metcash Food & Grocery Pty Ltd Submission

Metcash Food & Grocery Pty Ltd (**MF&G**) became a signatory to the Food and Grocery Code of Conduct (**Code**) in September 2020. MF&G continues to support the Code and the principles of good faith, fairness, transparency and clarity governing the trading relationships between suppliers and retailers or wholesalers. MF&G is pleased to submit these responses on the questions in the *Independent Review of the Food and Grocery Code 2023-24 Consultation Paper* (**Paper**). MF&G confirms it consents to this submission being published.

Rather than answer each question individually, MF&G has grouped questions raising similar themes and provides general responses relevant to some or all of those themes.

Mandatory or Voluntary Code

The Code is effective in achieving its stated purpose and objectives as a voluntary Code

MF&G considers that the Code is effective as a voluntary Code in achieving its desired purpose and addressing potential imbalances of market power. As a principles-based voluntary industry code, it allows for and promotes collaboration between industry participants, government (including the Independent Reviewer) and the regulator to foster improvements in culture, relationships and behaviours to the benefit of both signatories and suppliers.

MF&G is committed to remaining a signatory to the Code and as discussed below effectively treats the Code as mandatory in its current form. As such, MF&G has no objection in principle to the Code becoming mandatory in respect of itself or the other current signatories. However, MF&G questions the need for such a change where it would provide no practical benefit to suppliers.

As the Paper notes, the four signatories to the Code together hold ~82% of the Australian market (measured by revenue). These signatories include the two largest businesses, Woolworths and Coles, that hold significant bargaining power, having a combined market share of ~65%. Whilst MF&G is supportive of the Code, given its much smaller position as an acquirer of relevant food and grocery products, it does not consider that is has any or material market power in negotiations with suppliers.

Once each signatory has signed up to the Code, the Code provisions are legally binding on those signatories and all suppliers to them are automatically given the benefit of the Code provisions. MF&G signed up to the Code in September 2020 and, for all purposes since, has considered the Code 'mandatory' given its legally binding nature.

Although it is possible that MF&G or other signatories could withdraw from being signatories to the Code given its voluntary nature, the practical and commercial reality is that the signatories will not. With one minor exception no signatory has withdrawn since becoming a signatory to the Code.[1]

[1] Only one small retailer, About Life Pty Ltd, has signed and then withdrawn from the Code in circumstances where the Independent Review of the Food and Grocery Code of Conduct Final Report issued in September 2018 (**2018 Final Report**) encouraged About Life Pty Ltd to consider whether it would be appropriate for them to continue to be part of the Code should the changes recommended in that Report be implemented.

MF&G is committed to its participation in a voluntary Code and expects that other signatories will take a similar position. MF&G considers that there is little prospect of current signatories withdrawing from the Code and, consequently, limited utility in making the Code mandatory. In this regard it notes the following:

- MF&G has seen tangible benefits and improvements from becoming a signatory to the Code in its relationships with suppliers. Other signatories have also spoken of these benefits.
- Each of the signatories has invested significant resources in implementing policies, procedures and systems to ensure compliance with the Code and has entered into Code compliant grocery agreements with suppliers. These policies, procedures and systems have now been embedded into ways of working as 'BAU' (business as usual).
- There would be significant reputational risk for any signatory withdrawing from the Code. This may include damage to relationships with suppliers, political fallout, and likely increased regulatory scrutiny on that withdrawing signatory. Withdrawal may, in fact, trigger action by the Government to make the Code mandatory.

Extension of the Code to apply to smaller wholesalers and retailers.

MF&G does not consider that there is any basis to impose a mandatory code on smaller wholesalers and retailers.

Broadening the Code to smaller wholesalers and retailers will do little to address the fundamental objective of the Code, that is, to address imbalances of market power between supermarkets and their suppliers. In circumstances where MF&G does not have market power in negotiations with suppliers, there can be no basis to conclude that there is a market power concern in the relationship as between suppliers and smaller retailers.

An extension of the Code to smaller participants would impose a significant regulatory burden and cost on small businesses and negatively impact their ability to effectively compete against dominant vertically integrated chains. In circumstances where there are broad community concerns regarding the competitiveness of a grocery sector dominated by the two largest retailers, the extension of the Code to smaller participants could have the perverse effect of entrenching or extending the market power of the biggest retailers by imposing additional costs on smaller retailers.

On a practical level, determining the appropriate threshold test will be extremely difficult; any quantitative test may not accurately reflect market power, whether nationally or in any given geographic market or in respect of particular goods.

If the test were to be based on turnover (i.e. wholesalers or retailers are caught by a mandatory Code if their turnover exceeds a stated threshold), the turnover would need to be specific to the particular goods covered by the Code and even if that could be determined, it does not necessarily mean that the retailer will be purchasing a significant quantity of those goods direct from suppliers to have any substantive buying power. In this regard, it is noted that independent retailers, including those supplied by MF&G, can purchase products through wholesalers or directly from suppliers. The proportion of sales of a product acquired through direct supply can change on a month-to-month basis. As such, a test based on turnover will bear no correlation to an independent retailer's bargaining power vis-à-vis suppliers and so may not accurately reflect any market power or any imbalance of power between that retailer and its suppliers and potential for abuse of that power. This was recognised in the 2018 Final Report, where on page 22 it stated:

> *…the Review also notes that [a] quantitative measure may not necessarily be demonstrative of significant market power, particularly in circumstances where there are a number of participants in the market which offer alternative routes for suppliers to bring their products to market.*

An alternative to a pure revenue threshold would be a market share threshold (recognising the relationship between revenue and market share). Retail market share would be an appropriate measure to be applied to both wholesalers and retailers as, ultimately, purchases made by wholesalers are sold at the retail level of the market and a wholesaler's proportion of retail sales can be a proxy of market power, if any, in relationships with suppliers.

If a market share percentage was used, MF&G submits that a market share of 20% may be appropriate. This reflects the ACCC's guidelines for the proposed combined market share at which the ACCC recommends that parties submit potential acquisitions to the ACCC for review. This, presumably, reflects a view by the ACCC that market power concerns are very unlikely to arise where market shares are below 20%. The ACCC's thresholds in a merger review context suggest it is very unlikely that the activities of independent retailers and smaller wholesalers could give rise to market power concerns. As such there is no basis for the extension of the Code to such persons. It is noted that on any calculation MF&G's percentage of retail supply is materially below 10%.

MF&G is not advocating potential thresholds with a view to not being bound by the Code. MF&G's position is that if the Code were to become mandatory there must be a correlation as between relevant thresholds and the likely existence of a meaningful imbalance of power between wholesalers/retailers and suppliers. On any reasonable basis that threshold could not apply to independent retailers.

MF&G acknowledges that it is an important access point for suppliers to reach independent retailers and is a route to market alternative to the dominant retail chains for suppliers. In fact, it is a cornerstone of MF&G's strategy to provide an effective and efficient route-to-market choice for suppliers through our independent partner network. As noted above, MF&G is committed to remaining a signatory to the Code given the benefits it delivers for our relationships with suppliers. If the Code were made mandatory, and a quantitative measure were adopted which did not apply to MF&G, it would still seek to be bound by the Code. MF&G considers, as a result, that there should still be avenue for other participants to voluntarily become a signatory to the Code should they wish to do so.

Putting to one side the position of MF&G in respect of the application of the Code to its own activities, if the threshold test is set too low and extends to retailers with a smaller market share, it would have a detrimental impact on the independent retailer sector and affect the overall competitiveness of the sector. MF&G is concerned that it would:

- require retailers to incur increased regulatory compliance costs;
- create barriers to entry for new retailers to enter the market;
- create an uneven playing field between those retailers that fall within the ambit of the Code and those that don't;
- create uncertainty for those retailers that are on the cusp of the threshold and may come in or out the Code; and
- create a fragmented independent network operating on different conditions, and different levels of regulation and compliance.

This cost, uncertainty and disruption would make it even more difficult for those retailers to effectively compete with the dominant integrated chains.

The MF&G position is consistent with the findings of the 2018 Final Report, where on page 22 it stated:

> *The Review does not believe there is benefit from capturing smaller retailers under the Grocery Code, as it would impose disproportionately more regulatory costs on small organisations. … A small retailer should consider whether the additional compliance costs outweigh the benefits.*
>
> *The Review's opinion is that the combined coverage of the existing signatories and Metcash's participation will be adequate for addressing the key problems in the current market.*

Effectiveness of the Code and power imbalance

MF&G considers that the Code is generally effective in achieving its stated objectives and addressing issues arising from potential power imbalances. It is both principles based with a sensible degree of some prescriptive elements and allows parties to work constructively together to improve relationships between suppliers and wholesalers/retailers. An overly prescriptive approach may undermine prospects of industry participants working together constructively to resolve issues and/or promote legalistic technical responses to issues that arise which, in the view of MF&G, may undermine effectiveness.

After becoming a signatory to the Code, MF&G has made significant improvements to its supply documents, including policies and procedures, as well as its supply practices to the benefit of its relationships with suppliers. Through its constructive engagement with the ACCC, MF&G further refined its policies, procedures and systems to ensure better compliance with the Code and instil good discipline and practices in its dealings with suppliers.

MF&G does not support any changes to the Code which would result in differing standards applying to different suppliers. This would simply create greater complexity and uncertainty regarding its application and increase the regulatory burden without offering any real benefit. The Code was designed to assist smaller suppliers. In this regard larger suppliers with their own bargaining power are, in some respects, unintended beneficiaries of the Code. Small suppliers are already adequately protected and so there is no need for additional requirements to apply where greater power imbalances exist.

MF&G notes however that the Code is one-way with all obligations imposed on the retailer/ wholesaler with no reciprocal obligations on or allowances for actions of the supplier. If the Code is made mandatory, there should be some reciprocal obligations for the suppliers who benefit from the Code. For example, suppliers should also be required to act in good faith (which is the cornerstone principle setting expectations regarding the foundation on which the relationship be based). Certain other reasonable requirements should equally apply to suppliers regardless of any perceived power imbalance. For example, while there are specified time periods for the retailer/wholesaler to respond or provide notices in a timely manner, there is no reciprocal requirement on the supplier. In the case of price increase negotiations, delays by the supplier when negotiating price increases may result in MF&G having to notify the Independent Reviewer that the price increase negotiations have not been concluded within 30 days. While it is not a Code requirement to negotiate and agree price increases within 30 days (rather, simply to notify the supplier whether the price increase proposal is accepted, accepted in part or not accepted within

that period), this reporting of negotiations that extend beyond 30 days can create negative perceptions of the wholesaler/retailer, when the cause of the delay may be the supplier. Whether or not an obligation is imposed on the supplier under a mandatory Code, this issue for the wholesaler/retailer could also be addressed by excluding from the period delays caused by the supplier.

Excluding Fresh Produce and Liquor from the Code

MF&G considers that the Code is better suited to dry grocery / packaged goods/merchandise products. As such MF&G queries whether it would be more effective excluding fresh produce, meat and dairy from the Code.

There are unique issues and community concerns in those sectors, as well as unique supplier contracting arrangements which don't always fit 'neatly' with the Code's 'one size fits all' provisions. These sectors may be better addressed by a code of conduct specifically designed to address those issues to the extent relevant conduct is not otherwise covered by the Horticultural Code of Conduct and Dairy Code of Conduct.

For example:

- In relation to milk, it is predominantly only Coles and Woolworths that negotiate directly with dairy farmers. Coles and Woolworths enter into in long term supply contracts for the milk (up to 10 years) for the majority of the supply, leaving the smaller market participants with effectively no bargaining power/leverage in relation to the balance of the supply. These contractual arrangements should sit wholly within the Dairy Code of Conduct which can deal with market peculiarities.

- Given the dynamic supplier contracting arrangements for meat and fresh produce, the protections under the Code (e.g. ranging and delisting and price negotiations) are largely not applicable to these products. While MF&G does purchase some meat and fresh produce, it understands that seasonal contracts are generally only entered into by Coles and Woolworths. The balance of the market is very fragmented with a large number of participants. MF&G's buying terms are short in length, with supply susceptible to fluctuations in price. Similar to the Dairy Code, the Horticultural Code of Conduct is better placed to protect suppliers having regard to the peculiarities of the market and contracting arrangements and could be amended if required to address any emerging issues in these sectors.

MF&G considers that the Code should not be extended to include alcoholic beverages. The structure of the liquor industry is very different in nature to the grocery industry. While noting the presence of larger national retailers, there are very important and significant differences between the liquor and grocery industries:

- The beer market is predominantly supplied by two large multinational firms with significant countervailing market power.

- Retailers are not the primary means for suppliers of alcoholic products to reach the domestic consumption market, with wholesalers/buying groups and the on-premise market providing significant alternative routes to market.

- The export market provides another alternative avenue for suppliers.

Expanding the Code to include alcohol products may also add undue complexity, where existing provisions of the Code may not be fit-for-purpose in light of the different nature of the liquor versus grocery industries. Furthermore it is not apparent how certain concerns, for example in respect of the growth of private label wines, would be addressed by any extension of the Code.

Dispute Resolution Provisions and Potential Detrimental Effects if the Code is made Mandatory

MF&G has previously made submissions regarding the dispute resolution provisions of the Code. MF&G does not intend to repeat those submissions here and remains of the view that:

- Since signing the Code and through its constructive engagement with the Independent Reviewer as well as the ACCC, MF&G has strengthened and clarified its dispute resolution procedures.
- MF&G's dispute resolution policy clearly sets out the options available to a supplier in the event of a dispute, how to escalate the dispute, and the availability of the Code Arbiter for Code-related disputes.
- Internal protocols implemented by MF&G, whereby the Executive General Manager Merchandise oversees all significant decisions relating to any suppliers who make a complaint to the Code Arbiter for a period of 12 months from the complaint to ensure decisions are made for valid commercial reasons and not for retribution, provides meaningful protection against fear of retribution by a supplier making a complaint over and above the Code provisions that seek to address this (e.g. the Code expressly includes retribution for past complaints and disputes as a consideration relevant to assessing whether a wholesaler/retailer has acted in good faith).
- A lack of formal complaints to Code Arbiters should not be seen as evidence that the dispute resolution provisions in the Code are not effective. MF&G encourages suppliers to raise issues directly with MF&G and most complaints and disputes can be satisfactorily resolved in this manner. MF&G recognises that some suppliers may nevertheless still be reluctant to do so, and hence has authorised its Code Arbiter to talk and meet with any supplier who, while they may not wish to make a formal complaint, wishes to discuss conduct by MF&G team members, and to use such information to provide MF&G with information to assist it addressing any potentially emerging issues. The intention is to provide an additional less confrontational and formalistic avenue for a supplier to raise issues, and has been utilised by MF&G's suppliers.

The Code could be amended to require specific consideration of decisions by a named executive for a period following a complaint to the Code Arbiter and improved access to the Code Arbiter (processes which MF&G has voluntarily adopted as noted above) to further address issues around fear of retribution.

MF&G notes the outcome of the recent independent review of the dispute resolution provisions of the Code that:

- there is broad ongoing support within the grocery industry for retaining the current dispute resolution framework;
- the current framework should be given more time to work; and
- the low number of disputes that have used the current framework does not necessarily mean that it is not working, particularly as suppliers have reported relatively low numbers of serious disputes in the Independent Reviewer's 2021-22 annual survey.

MF&G supports those conclusions. The Government's response included support for an expanded toolkit for Code Arbiters to allow them to mediate disputes to increase options available for efficient and effective dispute resolution. MF&G supports this recommendation and considers that it will further improve the dispute resolution provisions in the Code.

MF&G is concerned about the impact of a mandatory Code on the dispute resolution provisions. The 2018 Final Report noted that:

> *…if compulsory arbitration with binding decisions was implemented under a mandatory code framework, constitutional issues may arise. Forcing retailers or wholesalers to be subject to determinations about the existing legal rights and obligations … is generally regarded as an exercise of judicial power. The compulsion of an entity to be bound by conclusive determinations on the law is a function exclusively reserved to the courts. If a mandatory Grocery Code were to give this function to an arbiter, it may be invalid as it risks infringing the separation of powers doctrine under the Constitution*.

As noted above, MF&G considers that the case for making the Code mandatory has not been made out. This is especially so where the introduction of a mandatory Code may result in the Code Arbiter dispute resolution process under the Code, which has broad ongoing industry support, being rendered void. The loss of a process which provides an accessible option for suppliers to address concerns may be lost for no discernible benefit.

Compliance and Enforcement

MF&G notes the ACCC's submission in February 2023 to the review of the Code's dispute resolution provisions where it advocated in favour of penalties for non-compliance and to extend the ACCC's infringement notice powers to include the Code.

MF&G understands the initial appeal of the ACCC's submissions on the basis that the risk of enforcement proceedings would improve compliance outcomes. However, MF&G has real concerns that the introduction of a penalty regime, in the absence of evidence of widespread and intentional non-compliance with the Code, would significantly alter the relationship as between Code participants. It is concerned that changes to the compliance regime may result in a legalistic and potentially antagonistic approach which would not improve industry outcomes. MF&G considers that working collaboratively with suppliers, industry bodies, its Code Arbiter, the Independent Reviewer and the ACCC has produced effective outcomes for all participants. It should not be assumed that positive aspects of the Code and its implementation would not be lost if a penalty regime were imposed.

MF&G considers that the ACCC's powers under section 51ADD of the *Competition and Consumer Act 2010* (Cth) are an effective enforcement tool. MF&G's experience is that the compliance check process is positive and constructive. It concurs with the ACCC that the ACCC takes a targeted approach to its audits under the Code in order to minimise the extent of any burden and that its audit work has contributed to embedding and improving a culture of compliance with the Code.[2]

Through the compliance check process, MF&G has worked with the ACCC to further improve its policies, procedures and practices. MF&G has developed further detailed protocols and training on particular issues to more successfully embed compliance as BAU. Interaction with the ACCC under the current regime has advanced MF&G's goals of continuous improvement and compliance for the benefit of our suppliers. MF&G is concerned that a regime where the ACCC moved from a

[2] 2018 Final Report, p. 48.

compliance and improvement partner to an active enforcer would undermine cooperation and result in sub-optimal outcomes. The current relationship with the ACCC is yielding benefits for all participants, a change in that relationship should not be assumed to improve compliance outcomes.

In this regard MF&G notes the following:

- The imposition of infringement notices or penalties does not, in itself, resolve or redress disputes or complaints of suppliers.
- Given existing signatories have implemented trading terms, policies, procedures and systems to ensure compliance with the obligations under the Code, any alleged infringements are likely to be specific to the facts and circumstances of a particular dealing with a supplier, which are better dealt with by dispute resolution between the parties.
- Substantial pecuniary penalties and infringement notices are already available to the ACCC in relation to conduct involving suppliers, including in respect of unconscionable conduct, false and misleading representations etc. and unfair contract terms.
- A move to an enforcement regime would require court orders and court proceedings at considerable public cost. This is not an appropriate use of public funds where efficient outcomes are being generated through other processes.

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