Public Submission to

ACCC Grocery Inquiry by

Brismark

Tuesday 11th March 2008

SUBMITTER'S DETAILS

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BRISMARK AND BRISBANE MARKETS LIMITED BACKGROUND

Brismark is an industry organisation that represents fruit and vegetable wholesalers. Brisbane Markets Limited (BML) is owned by industry and is responsible for the smooth operation and facilities of the Brisbane Produce Market. Both organisations are involved in the promotion of fresh fruit and vegetables.

More than $1 billion of fresh produce was traded through the Brisbane Markets in the 2006/07 financial year, supplied by approximately 8,000 growers.

Six Central Markets exist around Australia as the major wholesale marketing and distribution hub for fresh produce. The total throughput value of Australia's six Central Markets is approximately $5 billion. The responses included in this submission are generally indicative of the situation, which applies in respect of the Central Market system in Australia.

ACCC INQUIRY

The ACCC has indicated it will concentrate the inquiry on various retail grocery product categories including:

- Packaged food;
- Frozen food;
- Fresh meat;
- Fresh fruit and vegetables;
- Dairy products;
- Bakery products;
- Delicatessen items; and
- Packaged non-food items.

The inquiry is only a 'first step' in a robust examination and public discussion of the current market for basic household grocery items.

Broader issues such as industry structure, misuse (abuse) of market power and regulation are salient contextual factors of concern to wholesalers and will be addressed in this submission.

Comments have been provided from a wholesale markets perspective and where appropriate from an industry perspective.

A. STRUCTURE OF THE GROCERY INDUSTRY

Questions on Grocery Wholesaling

Q.10. What have been the major changes to the structure of grocery wholesaling in Australia over the past 5 to 10 years?

Response

The Brisbane Markets have experienced little change in relation to the number of primary wholesalers[1]. There have been other changes relating to structure, for example:

- The development of national wholesalers with selling floors in multiple Central Market locations. This has taken place as a response to the demand placed on wholesalers by the major supermarket chains (MSCs) for national suppliers. Premier Fruits Group and CostaExchange Limited are examples of national wholesaling businesses.
- There has been a significant increase in the number of secondary wholesalers[2] in the Brisbane Markets from 25 in 2002 to 34 in 2008.
- The number of wholesalers servicing MSCs and the quantity of fresh fruit and vegetables supplied to the MSCs has decreased.
- There has been an increase in sales of fresh fruit and vegetables to the food service sector[3].
- Supermarkets have increased their direct purchases from growers[4].
- There was a major rationalisation in the number of independent greengrocers throughout the 10 year period from 1990 to 2000.

Q.11. What factors have driven these changes (such as cost savings from large-scale wholesaling operations, changes to the structure of grocery retailing, mergers and acquisitions, etc.)? What has been the relative importance of these and other factors?

Response

Supermarket policy and changes in consumer behaviour:

- Supermarket Policy: Direct supply, national suppliers and rationalising the number of suppliers.
- Consumer Behaviour: The food service industry is growing rapidly whilst the retail sales of fresh fruit and vegetables are not.

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[1] A Primary Wholesaler sources produce directly from growers for resale.
[2] A Secondary Wholesaler purchases fruit and vegetables from Primary Wholesalers for sale to a variety of customers (e.g. provedores and country order specialists).
[3] This has been the result of the growth in the food retail sector. According to the Department of Agriculture, Fisheries and Forestry (DAFF 2007, p.16), 'growth in food retail during the year was faster in the non-grocery sectors of the market, evidenced by the increases in sales through cafes and restaurants and other outlets over the year'.
[4] DAFF (2005, p.10) has stated that, 'Supermarkets have increased their share of the wholesale market. This seems to reflect efficiencies and benefits obtained from integrating the wholesale distribution and quality control functions as well as other factors'. This trend has not necessarily been a positive for fruit and vegetable wholesalers. An increase in market share of the MSCs has also led to more stringent terms of trade for wholesalers across the Central Markets.

Q.13. How important are economies of scale in grocery wholesaling? What are the sources of these economies of scale? Are economies of scale primarily the result of lower transport costs, lower storage costs, better stock management or the ability to negotiate better deals with suppliers?

Response

The number of Primary Wholesalers has remained fairly stable however they are increasingly specialising in particular lines. Improved cool chain management and the increased use of QA systems have ensured better product quality.

Q.14. What are the most appropriate ways of measuring the shares of grocery wholesalers? Should industry or market shares be measured across all grocery items or for particular product categories (such as packaged food items, bakery, meat, fruit and vegetables, delicatessen products, etc)? If possible please provide quantitative estimates of shares of grocery wholesaling detailing the data sources and any assumptions made in estimating the shares. How have these shares changed over the past 5 to 10 years?

Response

Market share should not be measured across all grocery items. Fruit and vegetables are unique commodities and should be measured separately to packaged food items.

Q.15. Are there any structural differences in grocery wholesaling in metropolitan, regional and country areas? If so, please explain.

Response

A Central Market is the main wholesale fresh fruit and vegetable market serving a state or region. There are six Central Markets in Australia located in Brisbane, Sydney, Newcastle, Melbourne, Adelaide and Perth.

Central Markets provide an efficient and effective wholesale marketing and distribution hub ensuring consumers have ready access to fresh fruit and vegetables. The Central Markets are comprised of many wholesalers, who compete with each other in one location[5]. There are no Central Markets located in any regional or country areas. The transportation networks covering Australia do ensure however that regional and country areas are readily able to be supplied with fresh produce, much of which is still distributed through a Central Market.

[5] Brisbane Markets Limited (2008, website content).

Q.16. ***How profitable are grocery wholesalers?*** *What margins over supply costs do grocery wholesalers achieve? Do these margins differ by size of the wholesaler? If so, how? What rate of return on capital do grocery wholesalers achieve? Has this changed over the past 5 to 10 years?*

Response

In response to Question 16, Sub-Question 1:

- The average rate of return in the wholesaling of fruits and vegetables is estimated at 4%[6].

B. CONSUMER BEHAVIOUR AND CHOICE OF GROCERY RETAILER

Questions on Consumer Behaviour and Consumer Choice of Grocery retailers

Q.22. ***What options or choices of retailer do consumers have to purchase grocery products?*** *How far will customers travel for their groceries? How does this differ by grocery product (packaged food, meat, fruit and vegetables, etc)?* ***How does this differ depending on the type of shopping trip (weekly shop, top-up purchases, etc)?***

Response

In response to Question 22, Sub-Question 1:

- The MSCs, independent grocers, home delivery services and/or grower markets.

In response to Question 22, Sub-Question 4:

- Convenience, service and quality fresh fruit and vegetables seem to be the key determinants with respect to purchases.
- Consumer behaviour has changed insofar as fruit and vegetable purchases are becoming more frequent (top-up) purchases as opposed to once a week purchases. Coupled with a need for better service and quality produce consumers are increasingly choosing to make their top-up fruit and vegetable purchases at independent grocers.

Q.24. How important to consumers is the convenience of purchasing from a retailer offering a broad range of grocery products (meat, fruit and vegetables, packaged products, etc)?

Response

Less important now as consumers move towards more top-up purchases and move away from one weekly shopping trip, but still a significant factor for many shoppers.

[6] DAFF (2005, p.10).

Q.25. How important is price for consumers when they decide where to buy groceries? Does this differ depending on the grocery product?

Response

Price considerations are income dependent[7]. In terms of fruit and vegetables the emphasis for high-income earners is based on the quality of the produce, convenience and service, with price a secondary consideration[8]. Low-income earners are more sensitive to price.

Q.26. How important are factors such as distance of travel, freshness of perishable items, product range, etc? Does this differ depending on the grocery product? If so, how and why?

Response

In terms of fruits and vegetables the key factors are the quality (which is affected by freshness) and convenience. Consumers are demanding consistency of supply, which results in a greater range of products.

Q.27. How do consumers gain information on the pricing of grocery retailers (advertising by grocery retailers, word of mouth, comparisons of key grocery items, etc.)?

Response

Current specials are advertised through media such as newspapers and junk mail. Individual businesses may, over time develop a reputation for competitive pricing. Some industry based media promoters will promote what is in season and what products are the best buy.

[7] Research literature supports this claim; Turrell et al (2003, p.212) have noted that, 'small area variation in the purchase of fruit, vegetables, and grocery foods mainly reflect spatial differences in the socioeconomic composition of the people living in [those] areas'.

[8] Food choice can be influenced by a number of factors, in addition to price or value for money. Some individuals are primarily concerned about the health and nutritional aspects of food and will place greater importance on the nutritional quality of the foods they purchase (French 2003, p.842).

C. COMPETITION IN GROCERY RETAILING

Questions on Competition in Grocery Retailing

Q.31. ***Does the nature of competition in grocery retailing differ across products groups?*** *Does the nature of competition differ across the types of shopping trips?* ***What elements of the customer offer are important in each product group?***

Response

In response to Question 31, Sub-Question 1:

- Yes. There is more competition in the fresh fruit and vegetable category due to vibrant independent retailing sector. By comparison dry groceries, and to a slightly lesser extent, meat, bakery and delicatessen categories are dominated by the MSCs.

In response to Question 31, Sub-Question 2:

- The quality of fresh fruit and vegetables, convenience, service and price.

Q.32. Who are the major competitors to the MSCs in each of the products groups?

Response

Independent green grocers and the independent retail chains are the main competitors in respect of fresh fruit and vegetables.

Q.33. To what degree do Coles and Woolworths compete against each other? To what degree does the option of shopping at other supermarket chains (e.g. IGA) constrain the conduct of the MSCs? To what degree does the option of shopping at specialist grocery retailers constrain the conduct of the MSCs?

To what degree does the option of shopping at convenience stores constrain the conduct of the MSCs? How does this differ by product group? How does this depend on the type of shopping trip (i.e. weekly or "top-up")?

Response

In relation to fresh fruit and vegetables, Coles and Woolworths do advertise specials and Woolworths invests heavily in its brand image. However, the overall pricing of their fresh produce is generally higher than the independents other than where they are facing direct competition. They rely heavily on the convenience of 'one stop' shopping and are sharpest with their pricing when a competitor is located within walking distance of their store.

The existence of a greengrocer or an independent retail chain store within a close proximity of MSC stores is the best way to promote competitive pricing.

Q.35. What are the grocery pricing policies of the MSCs, and other grocery retailers that operate in more than one location? Do individual supermarket chains set the same product prices across all their stores? If not, are individual product prices determined regionally or store-by-store

How much, if any, pricing discretion is in the hands of the management of individual stores? To what extent, if any, do major national retailers respond at the store or local levels to changes in the grocery prices of local competitors?

Response

The example provided in Table 1 below indicates that supermarkets will compete as aggressively as appropriate so as to confront competitors and either maintain or increase their grocery sales.

Table 1. Joint Committee on the Retailing Sector: Transcript Extract 1

Review Participant	Input to Proceedings
Chair[1]	Did you go to ACCC? Sorry, you are making your opening statement.
Mr Natoli[2]	I went through to the Prime Minister at the time. I wrote to Paul Keating. I got a response from Senator Chris Schacht, who was representing the minister.
Chair	He is on this committee, but he is obviously not here today. Did you actually go to the ACCC?
Mr Natoli	I can remember one day we advertised sultana grapes at $1.79 a kilo, only to find that Big Fresh had them advertised at $1.99 a kilo. What an embarrassment it was for them to be seen in the paper to have a price that was higher than ours, because their policy was that whatever our price was it had to be lower. When I got back from the markets that day, they had already dropped their price to $1.69 and I said, 'Let's have it out. Let's see how far we can take it.' We did and within two hours they had their sultana grapes at 49c a kilo. I paid $1.20 a kilo for those sultana grapes and they were selling them at 49c a kilo. By the end of that afternoon they went up to 69c a kilo.

Notes 1 and 2: (1) The Hon Bruce Baird MP (Committee Chair) and (2) Mr Joseph Anthony Natoli (witness).

Source: Joint Committee on the Retailing Sector (1999b, pp.485-487).

D. COMPETITION IN GROCERY WHOLESALING

Q.42. Are there commercial advantages and disadvantages of vertical integration between grocery retailing and wholesaling? What are these advantages and disadvantages?

Response

There are advantages in vertical integration. The MSCs possess significant distribution centres throughout Australia. The Horticulture Code of Conduct (the Code) applies to wholesalers but does not apply to the MSCs as they are not considered wholesalers.

The fact is that the Horticulture Code regulates and imposes significant costs on one supply chain (being the supply chain utilised by independent greengrocers) when these same regulations and costs are not imposed on another (being the supply chain where the MSCs buy direct from growers).

This situation is anti-competitive.

Q.43. Does the vertical integration of the MSCs impede other players from achieving a competitive scale in grocery wholesaling?

Response

Yes, it does reduce the volume of fruit and vegetables traded through the Central Market system.

Q.44. Can grocery retailers 'bypass' the large grocery wholesalers? If so, how? Does this vary by the type of product or type of retailer?

Response

Yes, grocery retailers can buy directly from a Central Market, an off-market wholesaler, a broker, a secondary wholesaler or a grower directly. They can also source within Australia or overseas and can for some products switch between the two, and do so in a manner which has an obvious and significant impact on supply and demand factors and the resultant price to the producer in Australia.

Q.45. What are the impediments to entry into grocery wholesaling? Is large-scale entry likely?

Response

In terms of the Central Markets individuals with enough capital can become primary or secondary wholesalers. Wholesaling businesses may be set up off market and individuals may act as brokers with very little capital backing.

E. BUYING POWER IN GROCERY SUPPLY MARKETS

Questions on the buying power of grocery wholesalers and retailers

Q.46. Are large grocery wholesalers or retailers able to acquire products from suppliers at lower prices or on better terms than smaller wholesalers or retailers? Does this differ by product type?

Response

The MSCs have less influence on the price of fruit and vegetables due to the existence of the Central Market system. However, the MSCs can enforce tougher trade terms on suppliers due to buying power.

They can also influence the domestic market price by sourcing produce from overseas producers. This has occurred in relation to the likes of tomatoes, (source from New Zealand) with the outcome being a collapse in domestic demand and a sharp reduction in the return price paid to wholesalers/growers.

Q.47. Do grocery wholesalers or retailers with buying power pass on the lower prices they can achieve from suppliers to retailers and consumers?

Response

Supermarket pricing used to reflect the wholesale price. If product oversupply were experienced, supermarkets prices would move downward and thus clear the oversupply in the market bringing a state of equilibrium.

This situation is not always the case in that supermarkets are not tying the wholesale price to the retail price. This means that when there is an oversupply of product in the wholesale market and if supermarkets do not drop their retail price, if the demand from consumers does not increase the oversupply situation continues for longer ensuring the wholesale price remains lower for longer and the MSCs achieve supernormal profits.

Anecdotal evidence provide by some Brisbane Markets wholesalers supports the arguments noted above. One wholesaler indicated that the MSCs have the flexibility to vary their margins and control their profits or losses irrespective with no regard for the price paid to wholesalers. In another instance a wholesaler noted the ability of the MSCs to maintain an oversupply situation in the market.

Q.49. Do suppliers offer the same terms and conditions to all grocery wholesalers or retailers? For example, if a small wholesaler offered to purchase the same volume as a large wholesaler, would the small wholesaler receive the same volume discount?

Response

No. Suppliers to the MSCs do so on the terms developed by those organisations. Primary and secondary wholesalers in the Central Markets may have the capacity to negotiate terms.

Q.50. Is there evidence that large grocery wholesalers have market power as acquirers of products and what are its effects at the retail level?

Response

In Australia there are over 400 Primary Wholesalers operating across the Central Markets in addition to secondary wholesalers, off-market wholesalers, brokers and other purchasers of produce. Therefore unlike the concentrated grocery retail market there is sufficient competition in the wholesale market to make it very unlikely that any individual wholesaler would be able to exercise dominance in the market.

Q.52. Are there other forms of behaviour or conduct by supermarkets in their dealings with producers or suppliers that may indicate market power?

Response

The MSCs have insisted that wholesalers use the QA systems they nominate. Coles supermarkets require the use of SQF 2000[9] while Woolworths require the use of the Woolworths Quality Assurance (WQA) scheme[10]. The consequence for wholesalers wanting to trade with the MSCs is the need to adopt both QA systems and bear the costs involved of doing so.

Suppliers to the MSCs are forced to pay rebates and other fees, they are forced to carry additional pallet hire costs after products are delivered and they are forced to accept 'returns' of product regardless of the circumstances.

Packaging is another area of concern. The MSCs demand that fruit and vegetables are packed using returnable plastic crates (RPCs) or plain black cartons in some instances. Research has taken place to determine the packaging performance of RPCs. The research data was gathered using packaging performance trials in a laboratory setting and actual produce transported from Queensland to Melbourne.

[9] The SQF Program consists of the SQF 1000 Code (for use by primary producers) and the SQF 2000 Code (used mainly by food manufacturers). These Codes are not audit checklists nor are they product or sector codes of practice. Specific procedures, practices, methods and records a supplier must implement to achieve certification are not described. Unlike a code of practice the SQF Codes are general requirements (SQF Institute 2008).

[10] The WQA scheme involves more than 2,000 suppliers who must adhere to auditing. The WQA standard encompasses food and consumer products supplied by local and international trade partners. The standard encompasses process control, product specifications, good manufacturing practice, cleaning procedures, product identification and traceability, corrective action, evidence of commitment to continuous improvement and other aspects of product supply (Woolworths Limited website 2008).

Research reports commissioned by Horticulture Limited Australia (HAL) and undertaken by Third Party Logistics investigated the impacts of RPCs on participants in the horticulture sector[11].

Third Party Logistics developed an RPC Calculator (model) to review the cost / benefits of plastics crates as an alternative to using cartons. An analysis of the costs / benefits are provided in Tables 2a and 2b below[12].

Table 2a. Third Party Logistics: (Cost)/Benefit Analysis

	Apples	Avocado	Lettuce	Mandarin
Cartons	100,000	300,000	50,000	50,000
$				
Grower	3,718	22,602	38,690	(17,161)
Transporter	(9,859)	(19,276)	(652)	(4,207)
Warehouse/DC	(21,618)	(34,523)	(2,624)	(9,401)
Supermarket	10,166	85,351	11,884	11,124
(Cost) / Benefit	**(17,593)**	**54,154**	**47,298**	**(19,645)**
$ Per Carton				
Grower	0.03	0.11	0.77	(0.41)
Transporter	(0.09)	(0.09)	(0.01)	(0.10)
Warehouse/DC	(0.20)	(0.16)	(0.05)	(0.23)
Supermarket	0.09	0.40	0.24	0.27
(Cost) / Benefit	**(0.16)**	**0.26**	**0.95**	**(0.47)**

Source: HAL (2002, p.4).

Table 2b. Third Party Logistics: (Cost)/Benefit Analysis

	Mango	Orange	Pear	Potato	Tomato
Cartons	50,000	150,000	100,000	200,000	500,000
$					
Grower	(62,528)	(2,052)	(7,026)	(59,528)	(96,152)
Transporter	(5,510)	(12,259)	(8,125)	(20,528)	(33,881)
Warehouse/DC	(15,503)	(9,487)	(10,315)	(55,688)	(51,335)
Supermarket	7,068	18,032	15,131	22,606	132,096
(Cost) / Benefit	**(76,473)**	**(5,766)**	**(10,335)**	**(113,138)**	**(49,272)**
$ Per Carton					
Grower	(1.25)	(0.01)	(0.07)	(0.28)	(0.26)
Transporter	(0.11)	(0.08)	(0.08)	(0.10)	(0.09)
Warehouse/DC	(0.31)	(0.06)	(0.10)	(0.26)	(0.14)
Supermarket	0.14	0.11	0.15	0.11	0.35
(Cost) / Benefit	**(1.53)**	**(0.04)**	**(0.10)**	**(0.53)**	**(0.13)**

Source: HAL (2002, p.4).

The model underpins the data in Tables 2a and 2b which indicates that there are many negative impacts to the use of RPCs including:

[11] HAL (2002, p.3).
[12] Third Party Logistics also noted that while every situation will have a unique set of variables, a number of representative models were produced (HAL 2002, p.3).

Costs

- Black crates and cartons eliminate the intellectual property rights and marketing (branding) that can be achieved through the use of corrugated cardboard packaging.
- Growers investing in the equipment and processing required to use RPCs will become more dependant on the MSCs for business and less able to differentiate their produce. As noted by HAL (2202, p.3):

  '… the closed loop necessary for the effective use of RPCs will further marginalize wholesalers and encourage direct supply'.
- Across the categories examined in Tables 2a and 2b the costs are shifted from the MSCs to other participants in the supply chain. The total supply chain cost using RPCs is higher than using traditional cartons.
- The in-store cost to MSCs is less using RPCs than using traditional cartons.
- Potential for workplace health and safety claims against businesses. The size and weight of RPCs has the potential to injure staff.
- HAL (2002. p.3) provides an example of the costs to industry of crate losses:

  'A 0.5% loss factor is included in the model but the data internationally suggests the loss rate in a season may be up to 15%. If a loss rate of 10 to 15% is fed into the model then all the other costs become meaningless as the cost of using crates becomes prohibitive'.
- Extensive refitting of packing sheds. Another example provided by the HAL report indicates the impact on a tomato grower:

  '…with 40 drop bays on the side of his packing line wants to use crates 385mm wide then the line has to be extended by 4 meters. Apart from the significant cost of extending the machine many packing sheds don't have an extra 4 meters of floor space available'.
- Wholesalers are bearing the cost shift from the retail sector.
- Using RPCs restricts the height of a pallet and is further restricted by the 6 or 12 footprint/layering in order to satisfy the MSCs administration system.

Q.53. How could grocery wholesalers or retailers exercise any market power? ***Could major retailers credibly threaten to 'delist' a product or brand? How would consumers react if their desired brands are not available at their local supermarket?*** *How important is the potential for a grocery retailer to substitute to a private-label or generic brand?*

Do major retailers threaten to import products in preference to local brands and how credible is the threat? What options do suppliers have if this occurs? Where else could suppliers sell their products (other grocery retailers, exports)? What are the consequences at the retail level?

Response

In response to Question 53, Sub-Question 2:

- Yes, suppliers that do not meet the required standards of operation can lose the ability to supply, either for a period or indefinitely.

In response to Question 53, Sub-Question 3:

- Fruit and vegetables are commodities and therefore individual suppliers can lose their ability to supply without any impact on the retailer. Produce is simply sourced elsewhere.

F. COMPETITIVE POSITION OF SMALL AND INDEPENDENT GROCERY RETAILERS

Q.54. What are the major sources of competitive advantage and disadvantage of small and independent retailers (e.g. trading hours, scale of operations, density of retail outlets, location of retail outlets, wholesale prices, product and brand range, customer service, etc.)?

Response

Independent retailers may offer better quality fruit and vegetables, product knowledge, convenience (store locations), product range and price. They can also operate on the value for money basis, with more of a focus on 'lower prices'. The main disadvantage is that they may fall victim to predatory pricing by the MSCs.

Q.56. Are the wholesale prices independent and small retailers pay affected by the wholesale prices the MSCs pay? For instance, if a MSC puts pressure on a supplier to lower its prices will the supplier:

- Attempt to 'make this up' by charging more to other wholesalers and retailers, or
- Reduce the prices it charges other wholesalers and retailers so other wholesalers and retailers can remain competitive with the MSCs?

Response

The MSCs have the capacity to buy a disproportionate amount of fruit and vegetables as part of a sales promotion. In effect this demand can result in a limited supply of product for independent and small retailers, increasing the cost of a particular commodity, which in terms limits the buying power of independent and small grocery retailers.

Conduct of Grocery Retailers

Q.63. Is there evidence of any anti-competitive conduct in grocery retailing? What types of market conduct are of most concern to grocery retailers and wholesalers?

Response

In 1999 the Commonwealth government reviewed industry concentration in the retail sector. The review was conducted by a Joint Select Committee on the Retailing Sector[13].

[13] The terms of reference were narrow and included, 'The Joint Select Committee on the Retailing Sector is asked to inquire into and report on: (a) the degree of industry concentration within the retailing sector in Australia, with particular reference to the impact of that industry concentration on

The example provided in Table 3 provides an insight into the dilemma facing small business owners in the retail sector. Small businesses have a limited capacity to compete with larger competitors and cannot sustain losses.

Table 3. Joint Committee on the Retailing Sector: Transcript Extract 2

Review Participant	Input to Proceedings
Mrs Elson[1]	Does the Retail Traders Association have any evidence of predatory pricing in Tasmania? We have heard in other states that when they do want to, say, get rid of a florist or a deli or something like that, they undercut constantly until they remove that person from the business.
Mr P.Morgan[2]	I can give an example of garden centre. One of our garden centre people was telling me she has a business in a small country town in southern Tasmania. She opened the business from nothing and was operating and going along okay. She had started a business from nothing, which is quite a difficult thing to do, and the business was going quite well. After about three years, the local major store, which had a branch in that town, in early Spring would bring a truck into their carpark and sell pot plants off the back of this truck. That did not drive her out of business, but that was her peak time, and from having quite a good little business, she is now struggling. That sort of thing is right across every area of retail activity - florists, you mentioned, butchers, delicatessens, pharmacy, the ones that Tony has listed. That is the competition. We see it as unfair because we are all individuals. We are stand-alone operators. I have no financial tie-up with any other trader and yet we are being targeted by a big force out there which has lined us up. We see ourselves as under threat and that is why we are so worried.

Notes 1 and 2: (1) Mrs Kay Elison MP and (2) Mr Paul Francis Morgan, Vice-President, Retail Traders Association of Tasmania (witness).
Source: Joint Committee on the Retailing Sector (1999c, p.556).

Q.64. Is there any evidence of predatory pricing by larger retailers and wholesalers, and if so, is there any evidence of any adverse impact on independent/smaller retailers and wholesalers?

Response

The interaction outlined in Table 4 supports the argument that the MSCs will use pricing as a way to eliminate competition. Moreover, the independent supermarket operator indicated that he was assisted by his suppliers to 'weather' the situation (see Table 4); the MSCs would label the situation 'vigorous competition' (see Table 5).

the ability of small independent retailers to compete fairly in the retail sector; (b) overseas developments with respect to this issue, highlighting approaches adopted in OECD economies; and (c) possible revenue-neutral courses of action by the Federal Government (ie courses of action that do not involve taxation reform)'.

Table 4. Joint Committee on the Retailing Sector: Transcript Extract 3

Review Participant	Input to Proceedings
Mrs Elson[1]	You are an independent grocery chain, aren't you?
Mr Bernardi[2]	I am an independent supermarket, yes.
Mrs Elson	Are you under a banner?
Mr Bernardi	We are under the Davids wholesale supply. How do we compete against the chains or the smaller stores?
Mrs Elson	How are you competing at the moment?
Mr Bernardi	In Forbes, I actually do not have Woolworths figures, but I would be pretty confident in saying that we actually out-trade Woolworths in our town.
Mrs Elson	Do you compete with their prices or try to?
Mr Bernardi	Absolutely. Yes, we do.
Mrs Elson	Do you have any evidence of predatory pricing from the big chain against you?
Mr Bernardi	They ran that advertising campaign for about eight weeks. Apart from that, in our town, no. That is the only thing I have seen.
Mrs Elson	Did it affect your turnover?
Mr Bernardi	It actually didn't. The suppliers were very helpful and they said, 'Look, we know what is going on. It does not cost us very much to help you. We want to see you guys survive'. So we matched most of their prices. But the power that they potentially have - there is nothing to stop them from dropping everything to half price until we are gone. That is the worrying thing'.

Notes 1 and 2: (1) Mrs Kay Elison MP and (2) Mr David Antonio Bernardi (witness).

Source: Joint Committee on the Retailing Sector (1999d, p.746).

Table 5. Joint Committee on the Retailing Sector: Transcript Extract 4

Review Participant	Input to Proceedings
Senator Boswell[1]	In the various submissions we have had, people have said that there is predatory pricing by the majors. Could you tell us what protocols you have that would prevent that? Is it still happening?
Mr Corbett[2]	There are certain laws against predatory pricing. I assure you that our policies in Woolworths are very strongly against that. Perhaps Naum Onikul, who heads up our supermarkets, could add to that.
Mr Onikul[3]	Our pricing is based on a number of issues. Our pricing is based, first of all, on our need to get a return on investment. Our pricing is also based on a need for us to be competitive in the marketplace. When we set a price for any merchandise it is set to be competitive in the marketplace. We compete vigorously in the marketplace with our major competitors. In any marketplace there are a number of other players normally which keep us very competitive. We do not set out to undercut anyone. Our pricing is based on being competitive to deliver to our customers the best value for money in that particular marketplace.

Notes 1, 2 and 3: (1) Senator the Hon. Ron Boswell (Committee Member), (2) Mr Roger Campbell Corbett, Chief Executive Officer, Woolworths Limited (witness) and (3) ONIKUL, Mr Naum, Chief General Manager Supermarket, Woolworths Limited (witness).

Source: Joint Committee on the Retailing Sector (1999a, pp.485-487).

Q.65. Please describe any such conduct (including specific instances) and the effect of the conduct on competition in grocery retailing.

Response

The example cited in Table 1 (pages 9-10) indicates that changes to prices (however small) may lead to greater reductions below cost price.

The impact of predatory pricing outlined in Table 1 does lead to a short-term gain on the part of consumers. The implications in the long-term are negative for the consumer and for competition at the retail level. Once competitors have been eliminated from at the market there is no incentive for supermarket chains to keep prices low.

G. FACTORS INFLUENCING THE PRICING OF INPUTS ALONG THE SUPPLY CHAIN FOR STANDARD GROCERY ITEMS

Questions for Suppliers of Grocery Products

Q.66. What are the major influences on the prices you receive for your produce? How are your prices determined? What proportion of the retail price of the product do you receive?

Response

The major influences on the price of fresh produce are supply, demand and quality of the product.

Q.67. Have the prices you receive for your produce changed over the past 1 to 3 years? What have been the major reasons for any changes in the prices you receive? Have your costs of production changed over the past 1 to 3 years? Have the prices you receive for your produce changed by more or less than your cost of production? Please provide details?

Response

Market wholesalers operate in a spot market where demand and supply determine prices on a daily basis. Supply has been affected by climactic conditions, which have caused price increases.

Q.68. To whom do you sell your produce? What supply arrangements do you have with the buyers of your produce? Do you sell any of your produce to the MSCs? If so, what options do you have if you decided not to sell to the MSCs (other grocery retailers or wholesalers, food processors, exports, etc?)

Response

Market wholesalers sell produce to MSCs, greengrocers, retailers, secondary wholesalers, provedores, independent supermarkets, exporters, cafes, restaurants and the general public. The percentage of trade with the MSCs has reduced over time and has been replaced by increased trade with independent retailers and secondary wholesalers.

Q.69. If the MSCs put pressure on you to lower your prices would you attempt to 'make this up' by charging more to other wholesalers and retailers, or would you also lower your prices to other wholesalers and retailers so they can remain competitive in grocery wholesaling and retailing?

Response

If MSCs are able to negotiate a discount off the market price from their wholesalers/growers, it will not automatically apply to other buyers in the market.

Questions for Wholesalers and Retailers of Grocery Products

Q.70. Do changes in retail grocery prices reflect changes in the prices you pay your suppliers? For example, do retail grocery prices reflect changes in farm gate prices? Please provide details.

Response

As a commodity, fruit and vegetable wholesale prices generally reflect supply and demand. In the past, increases and decreases in wholesale prices were generally reflected in retail prices, however this nexus is becoming more tenuous. Issues such as relative inelasticity of demand for many products, now means that often MSCs do not pass on the reductions in wholesale purchase prices to consumers.

Q.71. Do cost savings in the supply chain flow through to lower retail prices for consumers?

Response

Not always.

Q.72. What is the nature of the supply arrangements you have with suppliers? How are prices determined under these arrangements?

Response

The regulation of trade between growers and wholesalers is governed by the Horticulture Code of Conduct (the Code). However, a significant amount of fruit and vegetable business between growers

and wholesalers is conducted under pre-existing written agreements or between parties that are not subject to the Code

Prices are therefore set through one of two mechanisms; (1) pre-existing contracts or (2) Code based arrangements. Brismark has argued that the manner in which the Code has been drafted is unworkable and if applied to most transactions it would not be possible to process existing market volumes.

To comply with detailed inspections and finalise price negotiations under the Code would lead to build up in the quantity of produce stored within the Central Markets. Any delays in transporting fresh fruit and vegetables will degrade the quality of the produce.

The Code seeks to redefine the definition of a 'merchant' transaction in a manner which takes away the flexibility for a wholesaler of fresh produce to clear large volumes of produce quickly and efficiently, while at the same time returning their grower suppliers a fair 'market' price.

H. IMPEDIMENTS TO EFFICIENT PRICING OF INPUTS ALONG THE SUPPLY CHAIN

Q.73. Is there evidence of market power in the supply of grocery products to retailers or wholesalers? Please identify specifically which grocery products and explain the sources of market power?

Response

As detailed in Tables 1, 3, 4 and 5 of this submission, supermarkets have the latitude to compete as aggressively as they can without breaking the letter of the *Trade Practices Act 1974*.

Q.74. Are there any impediments to cost savings flowing through the supply chain to consumers?

Response

From a wholesaler's perspective there are multiple impediments to cost savings including:

- Cost shifting as noted in Question 52.
- Market power of the MSCs.
- The imposition of unworkable provisions of the Horticulture Code of Conduct
- The data provided in Table 6 indicates that in relation to RPCs, growers, transports and wholesalers have borne a shift in costs from supermarkets.

Table 6. Third Party Logistics: (Cost)/Benefit Analysis

	Orange	Pear	Potato
Cartons	100,000	200,000	500,000
$			
Grower	(7,026)	(59,528)	(96,152)
Transporter	(8,125)	(20,528)	(33,881)
Warehouse/DC	(10,315)	(55,688)	(51,335)
Supermarket	15,131	22,606	132,096
(Cost) / Benefit	**(10,335)**	**(113,138)**	**(49,272)**
$ Per Carton			
Grower	(0.07)	(0.28)	(0.26)
Transporter	(0.08)	(0.10)	(0.09)
Warehouse/DC	(0.10)	(0.26)	(0.14)
Supermarket	0.15	0.11	0.35
(Cost) / Benefit	**(0.10)**	**(0.53)**	**(0.13)**

Source: HAL (2002, p.4).

Q.75. What are the consequences for suppliers of any market power of grocery wholesalers or retailers in the acquisition of grocery products (e.g. lower prices to suppliers, transfer of risk and/or costs to suppliers, decreased incentive for investment and innovation along the grocery supply chain, etc.)?

Response

In terms of the example noted under Question 52, the MSCs have shifted costs directly to wholesalers and growers as a consequence of the MSCs seeking efficiencies within their operations. The data provided in Tables 2a, 2b and 6 provide support for the argument that the supermarkets have opted to shift packaging costs along the supply chain. The following issues should be noted:

- Wholesalers that wish to trade with MSCs have been forced to adopt food safety systems dictated by the MSCs regardless of existing systems;
- Wholesalers are forced to pay various rebates and fees to the MSCs;
- Wholesalers are forced to accept 'returns' from MSCs; and
- Wholesalers are forced to bare additional pallet hire costs when dealing with the MSCs.

Q.78. What impact, if any, does the presence of direct supply agreements have on the level of competition in the markets for those individual products?

Response

The MSCs have specific requirements in regard to size, quality etc. This is to be expected however, the direct supply of product from a grower to an MSC can reduce the level of the most saleable product in the Central Markets, and the level of demand that would otherwise exist. This can result in circumstances where market prices may be reduced. As MSCs regularly set their prices with reference to the Central Markets, even their suppliers may be disadvantaged as a result.

I. HORTICULTURE CODE OF CONDUCT

Q.81. What has been the impact (if any) of the Code on market behaviour along the supply chain for horticultural products?

Response

The Code was developed to achieve three broad aims:

- Provide contractual clarity and transparency providing clear market signals to all parties;
- Identify whether a wholesaler is acting as an agent or a merchant; and
- Include effective and affordable dispute resolution processes to avoid costly litigation.

The Code has not met the objectives above and has impacted within the industry as follows:

- When the Code was made public its first impact was to spur many wholesalers and growers into formalising existing trading arrangements. This provided contractual clarity and transparency outside the auspices of the Code. However, the major motivation to enter into such arrangements was not only the satisfaction by both growers and wholesalers with established trading arrangements but also the recognition that the new regulations were in many cases unsuitable or unworkable. For those wholesalers with pre-Code contracts this has ameliorated the potentially debilitating affects of the Code in its present form. For other wholesalers and growers however, they operate in the untenable position of having to breach the Code to maintain an effective commercial relationship.
- The second impact of the Code has been the lengthy and expensive exercise of developing various legal documents and promulgating them throughout the industry. Brismark alone spent tens of thousands of dollars on legal advice to produce template contracts in the impossibly short time allowed for by the Government. Their implementation has been a tortuous episode punctuated by lengthy negotiations with the ACCC. There are still growers that are unwilling to meet the contractual requirements of the Code and the struggle to achieve compliance continues.
- The ongoing impact of the Code has been a massive increase in paperwork associated with purchases of products made under the Code.
- As noted above, many transactions are covered by pre-Code contracts and are exempt from the paperwork requirements. Some Market wholesale transactions are excluded because a third party has been interposed between the grower and the wholesaler. Where the Code does apply some wholesalers and growers have adopted fixed price contracts. This avoids the necessity to agree prices in writing on a transaction by transaction basis. Fixed price arrangements are transparent but do not provide the “clear market signals” sought by advocates of the Code.

- Another impact has been a culling by some wholesalers of smaller, less profitable suppliers. Where pre-Code contracts were not in place wholesalers have had to weigh up the impact of the additional cost of doing business with smaller, less professional growers. The practice by some growers of sending produce unannounced to wholesalers on spec has also been curtailed.
- This outcome was foreshadowed by the Centre for International Economics (CIE) in the Mandatory Horticulture Code of Conduct Regulation Impact Statement as follows:

  ‘Option 6 (being the option adopted by the Government) may cause some smaller growers and those that supply the market infrequently to be disadvantaged. Wholesalers have said they will offer lower prices to these growers, or refuse to deal with them, to defray the additional risks involved in trying to off-load lower quality produce or smaller consignments’.
- The question of whether the Government should have an actual role in rationalising the horticulture industry through the imposition of regulations such as the Code was not addressed to by the Government when introducing the Code.
- The overall effect of the Code on transparency and clarity of trade has been mixed. Contractual relationships are now documented and terms of trade are more clearly available. However the adoption of fixed price contracts and the pricing of produce before the market is open have weakened market signals to the growing sector.
- In its Regulation Impact Statement the CIE stated that there was “an under supply of important information, particularly in regard to prices obtained and prices paid by traders in the marketplace”. This situation has been exacerbated by the nature of the contractual requirements of the Code.
- For these reasons Brismark supports the use of documented terms of trade, but opposes the restrictive trading requirements of the existing Code.
- For further information see Appendices 1 and 2. These are submissions by Brismark and Brisbane Markets Limited to the Horticulture Code Committee regarding the operation of the Code.

It is important that the ACCC acknowledges the call from the horticulture industry for amendments to the Code which extend beyond the issue of scope and the inclusion of retailers buying direct from growers.

The Code as it stands is unworkable and any review or move to amend the Code must include changes to the existing provisions which make it unworkable.

Q.82. What would be the impact on market behaviour along the supply chain for horticultural products if retailers and other major buyers were also included in the Code?

Response

Firstly it is important to note that there are potentially differing objectives which would need to be addressed if coverage of the Code was extended.

The existing Code has three broad aims. In relation to the MSCs the first and the last dot point still apply. However, a fourth aim would also need to be added relating to providing a framework which worked to minimize the potential for the misuse of market power.

For a level playing field and as a minimum regulations which exist to provide either a 'safety net' or framework within which governs commercial transactions which must apply to all players. However, the use of regulation must take into account the very different functions of the various players. Retailers buy discrete quantities of produce; the Central Markets are clearing houses and accept the produce supplied by growers. Therefore the requirements for documented terms of trade, returns of produce, dispute resolution and so on should apply equally but the issue of price setting must allow for the different functions mentioned above.

A Central Market is qualitatively different to a retail operation insofar as demand and supply play a critical role in price setting; in a spot market negotiating a price fruit or vegetables before the market opens is not a viable option for a wholesaler or grower. Under current Code arrangements a wholesaler would tend err on the side of caution and set as low a price as possible to minimise the their risk of making a loss on their consignments.

Prior to the introduction of the Code grower organisations including the Horticulture Australia Council and National Farmers Federation argued that price averaging and discretionary pricing was unacceptable. These organisations stated that the Code "distorted price signals and growers being unable to gauge the true value of their produce".

The same groups are now complaining about the impact of the Code on grower owned co-operatives and the practice of price averaging and pooling of produce. They have conceded that the Code requirements are too stringent for their constituents and now want special "exemptions" for certain parties. This organisation opposes any ad-hoc amendments to the Code which work to make it more anti-competitive.

Industry Coverage

In 1999, the Joint Select Committee on the Retailing Sector recommended a mandatory Code to regulate the retail chains. The 2003 Report of the Review of the Retail Grocery Industry Code of Conduct (Buck Report) recommended a mandatory Code covering the entire industry including

grocery retailers and processors. Submissions by Horticulture Australia Council and National Farmers Federation also called for a Code, which applied to all parties including retailers, exporters and processors.

The inclusion of retailers, processors and exporters to the Code would have the effects outlined above and ensure as level a playing field as possible; a qualitatively different position than exists at present. However, a case exists to allow Central Market wholesalers more latitude in price setting. Brismark opposes any other elements in the Code, which do not apply equally to all parties. Exemptions or exclusions that give commercial advantages to one group or sector, which are not available to others in the industry, will distort the market.

Q.83. Would such an inclusion improve the effectiveness of the Code?

Response

The major obstacles to an equitable application of the Code are the price setting mechanism and industry coverage.

The Code must be amended so as to provide a framework which promotes good commercial practice. It should not exist as a means to make illegal a commercial relationship which is otherwise lawful. This is what the current Code does with the way it redefines the meaning of a “merchant” transaction. The Code must also be amended so that it provides an effective framework which applies to all sectors of the Horticulture Industry supply chain.

Extending the Code to the MSCs, processors and exporters would have the effect of redressing the current inequity under current Code arrangements.

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Submission to the Horticulture Code Committee

Preamble

On 20 November 2007 the Chairman of the Horticulture Code Committee released a call for industry's views on the impact and effectiveness of "the Code". Industry input received by 25 January will be considered at the second Committee meeting to be held in February 2008.

The list of industry issues discussed at the first Committee meeting on the 14th November is nearly identical to a list of concerns outlined in a media release by Horticulture Australia Council on 8th November.

In the interests of fairness and a commercially sensible outcome it is hoped that favoured access and consideration provided to several peak grower associations during the development of the Horticulture Code does not extend to the review process. On this basis Brismark is pleased to provide the following submission.

1.0 THE IMPACT OF THE CODE INCLUDING THE EXTENT TO WHICH IT IS IMPROVING TRANSPARENCY AND CLARITY OF TRADE

In the lead up to the Code those advocating its introduction called for a system which would:

- provide contractual clarity and transparency providing clear market signals to all parties;
- identify whether a wholesaler is acting as an agent or a merchant; and
- include effective and affordable dispute resolution processes to avoid costly litigation.

When the Code was made public its first impact was to spur many wholesalers and growers into formalising existing trading arrangements. This provided contractual clarity and transparency outside auspices of the Code. However, the major motivation to enter into such arrangements was not only the satisfaction by both growers and wholesalers with established trading arrangements but also the recognition that the new regulations were in many cases unsuitable or unworkable. The large number of pre-code contracts has ameliorated the potentially debilitating affects of the Code in its present form.

The second impact of the Code has been the lengthy and expensive exercise of developing various legal documents and promulgating them throughout the industry. Brismark alone spent tens of thousands of dollars on legal advice to produce template contracts in the impossibly short time allowed for by the Government. Their implementation has been a tortuous episode punctuated by lengthy negotiations with the ACCC. There are still growers that are unwilling to meet the contractual requirements of the Code and the struggle to gain compliance continues.

The ongoing impact of the Code has been a massive increase in paperwork associated with purchases of products made under the Code.

As noted above, many transactions are covered by pre-code contracts and are exempt from the paperwork requirements. Some transactions are exempt because a third party has been interposed between the grower and the wholesaler. Where the Code does apply some wholesalers and growers have adopted fixed price contracts. This avoids the necessity to agree prices in writing on a transaction by transaction basis. Fixed price arrangements are transparent but do not provide the "clear market signals" sought by advocates of the Code.

Another impact has been a culling by some wholesalers of smaller, less profitable suppliers. Where pre-code contracts were not in place wholesalers have had to weigh up the impact of the additional cost of doing business with smaller, less professional growers. The practice by some growers of sending produce unannounced to a wholesaler on spec has also been curtailed.

This outcome was foreshadowed by the Centre for International Economics (CIE) in the Mandatory Horticulture Code of Conduct Regulation Impact Statement as follows:

> *"Option 6 (being the option adopted by the Government) may cause some smaller growers and those that supply the market infrequently to be disadvantaged. Wholesalers have said they will offer lower prices to these growers, or refuse to deal with them, to defray the additional risks involved in trying to off-load lower quality produce or smaller consignments."*

The question of whether the Government should have an actual role in rationalising the horticulture industry through the imposition of regulations such as the Code, was not responded to by the Government when introducing the Code.

The overall effect of the Code on transparency and clarity of trade has been mixed. Contractual relationships are now documented and terms of trade are more clearly available. However the adoption of fixed price contracts and the pricing of produce before the market is open have weakened market signals to the growing sector.

In its Regulation Impact Statement the Centre for International Economics stated that there was "an under supply of important information, particularly in regard to prices obtained and prices paid by traders in the marketplace".

This situation has been exacerbated by the nature of the contractual requirements of the Code.

For these reasons Brismark supports the use of documented terms of trade, but opposes the restrictive trading requirements of the existing Code.

2.0 HOW GROWERS AND WHOLESALERS PERCEIVE THE CODE

Larger, more professional growers perceive the Code as being an unnecessary impost interfering with long standing trading arrangements.

Wholesalers perceive the Code as being unworkable in its present form and as noted above, have taken action to ameliorate its impact.

Brismark's position regarding the code is supported by grower research, such as the extracts from the most recent Roy Morgan Research survey, as attached.

The Roy Morgan Survey, which looked into growers' views of the code, was conducted from a database of some 3,500 growers and 604 respondents in April 2007.

It highlighted a moderate level of grower awareness of the code with the majority of growers opposing the exclusions of supermarket chains, exporters and processors. It also showed that:

- 67% of growers support amendments to the code so as to allow a merchant transaction where the return price paid to the grower is based on the sale price achieved by the wholesaler (only 18% of growers were opposed to this position).
- 90% of growers think that it is important to have an effective Central Market system.
- In terms of importance, the code issue was ranked last out of a list of nine topical industry issues.

The survey results again highlight that growers do not see the code as important and if there is to be a code, they want it amended so as to provide for greater flexibility, and in particular, the ability for wholesalers (traders) to operate as a merchant and establish a return price which is based on the sales price achieved by the wholesaler less a documented and agreed margin.

Significantly, the recent dumping of Growcom chairman, Paul Ziebarth, by the members of that organisation, also highlights that growers are not supportive of the current Code, or the adversarial policy position regarding the Code, which had been advocated by Growcom and the Horticulture Australia Council.

3.0 OPTIONS AND PRACTICAL ACTIONS THAT WILL SUPPORT THE EFFECTIVE OPERATION OF THE CODE

Those responsible for the review of the Code must understand the operations and functions of the Central Markets if “practical actions” are to be possible. The current situation has come about as a result of political decisions by parties unqualified in their understanding of the Markets. Only by comprehending the volume of transactions, the constraints of time and resources and the functions to be performed by a Central Market, can workable outcomes be achieved.

In conducting a review of the code, it must be understood that the Central Markets have always been predominantly a spot market, where supply and demand set the price and prices fluctuate rapidly. They can be compared to markets for shares, commodities and currency and must not be confused with the discreet order quantity scenario enjoyed by other sectors of the economy including the retail chains.

The requirements under the Code that merchant prices are set prior to the opening of the market change its very nature from a spot market to one in which wholesalers trade in “futures”.

Such an outcome weakens market signals to growers and exposes wholesalers to greater risk. This increased risk in turn demands a greater return to the risk taker and will lessen returns to growers.

It must also be understood that wholesalers cannot physically negotiate prices in the time between the receipt of produce and the opening of trade. Receipt of product generally begins at 2.00am and trade commences at 6.00am. The sheer volume of transactions makes making agreements in writing impossible. If wholesalers attempted to agree prices on delivery for all produce entering the Markets the system would collapse.

That is why the State-based Farm Produce Marketing legislation allowed for price setting on merchant transactions after the produce received had been made available for sale. It is also why many wholesalers and growers entered into pre-code contracts.

It is also a fact that many wholesalers are unable to comply with the Code requirements for agency transactions. Wholesalers who source multiple grades and sizes of products from many different growers and combine those lots to fill complex orders cannot meet agency reporting requirements in a cost effective manner. This is a major reason why some wholesalers are not prepared to consider trading with growers on an agency basis.

Prior to the introduction of the Code grower organisation including the Horticulture Australia Council and National Farmers Federation argued that price averaging and discretionary pricing was unacceptable. They stated that it “distorted price signals and growers being unable to gauge the true value of their produce”. The same groups are now complaining about the impact of the Code on grower owned co-operatives and the practice of price averaging and pooling of produce. They have conceded that the Code requirements are too stringent for their constituents and now want special "exemptions" for certain parties.

The issues faced by co-operatives are magnified in the Central Markets by the greater volumes and complexities found there. If credence is given to concerns about the effect of the Code on co-operatives greater credence must be given to concerns about the effect on wholesalers.

When the functions and logistics of the Central Markets are understood the “practical actions” required to support the operations of the Code are clear.

The CIE in its Regulation Impact Statement stated a number of objectives required to provide an efficient market. Of particular relevance is the following:

"Ensure costs of marketing remain efficient and competitive by ensuring flexible trading options remain and:

- *Transacting parties can negotiate mutually advantageous arrangements to take advantage of individual economic strengths and circumstances;*
- *There are no prescriptive, ‘one-size-fits-all’ set of terms and conditions;*
- *Producer and consumer prices are not adversely impacted;*
- *Anti-competitive structures are not imposed that might force some players out of the market; and*
- *Existing efficient market arrangements that already achieve the desired objectives can continue unrestricted."*

Later in the report, the CIE warned *"being too prescriptive hinders market flexibility in that market participants' tastes and preferences are not accounted for. Most importantly such arrangements can become a barrier to competition and result in economic costs with little or no public benefits."*

The lofty goals of the CIE were subsequently bastardised through the political interference of peak grower bodies. The resulting restrictive arrangements must be changed to redress the economic burden now weighing upon Central Market wholesalers and their suppliers.

The negative impacts of the Code can be remedied and the original objectives promoted by allowing greater flexibility in the method of price setting. Determining the price by reference to the price for which the goods are on sold provides the following benefits:

- Contractual clarity and transparency is maintained
- Market signals to growers are improved
- Price disputes will be eliminated
- Administration costs will be reduced
- The functions of the market as a price setter and clearing house for varying quantities and standards of product will be restored
- Grower returns will be improved
- Logistic bottlenecks will be addressed

The details of the necessary amendments to the Code as proposed by Brismark and BML are included in Appendix 1.

Peak grower organisations have previously argued against this solution on grounds of transparency, clarity and risk. However, the method described delivers the greater transparency than Code compliant merchant transactions and less risk to the grower than Code compliant agency transactions.

Brismark will however, continue to oppose any amendments to the Code which do not apply equally to all parties. There must not be any exemptions or exclusions which give commercial advantages to one party which are not available to others.

For this reason, Brismark is opposed to the proposed amendments supported by the Horticulture Australia Council and Growcom. The proposed amendments included in Attachment 1 will apply equally to all parties and facilitate the flexibility which they are seeking for packhouses and certain other marketing intermediaries.

4.0 OPTIONS TO INCREASE AWARENESS OF THE CODE AND ITS REQUIREMENTS

An enormous effort has been put into the promotion of the Code both before and after its implementation. Despite this effort, participation in the process by individual growers has been underwhelming. Information sessions have been poorly attended and willingness to comply with Code requirements is low. We contend that this outcome is not due to a lack of awareness but a lack of interest. It clearly demonstrates that many growers do not share the views advocated by several peak bodies and that they wish to continue under pre-code trading arrangements.

Brismark opposes the ongoing allocation of government funds to continue to promote the code, given the long lead time and the significant costs already incurred.

5.0 GENERAL ISSUES RELATING TO THE CODE INCLUDING THE PROVISION OF AN ANNUAL REPORT ON THE COMMITTEE'S ACTIVITIES

5.1 Dispute Resolution

In the lead up to the Code advocates called for an effective and affordable dispute resolution processes to avoid costly litigation. They argued that growers were being treated unfairly but were not in a position to pursue their grievances. They championed the need for a process that would address this alleged situation.

A number of grower organisations went on to claim that the existence of the Code would open the door for an estimated "1,000" complaints annually.

The fallaciousness of these claims is demonstrated by the ongoing absence of disputes under new and existing dispute resolution processes.

- The Produce and Grocery Industry Ombudsman reported a total of six mediations nationwide from July 2006 to June 2007.
- The Horticulture Mediation Advisor appointed under the Code has refused to provide us with any information relating to disputes under the Code however we are unaware of any mediations involving our members.

We call for greater transparency in relation to the reporting of disputes by the Horticulture Mediation Advisor.

Reality has continued to highlight a low level of disputes within the fresh produce industry. What is very evident however, is that of the disputes that do occur, a major contributing factor has been the lack of national grade standards for fresh produce. This issue is not specifically addressed by the Code, highlighting the significant hypocrisy of a Code which while having an objective, the provision of "contractual clarity and transparency" fails to provide for the most fundamental issue of ensuring a consistent and published standard of what constitutes Class 1/Class A produce.

5.2 Retail Chains

In the lead up to the Code, Growcom argued that the inclusion of the retail chains was not necessary because they were already signatories to a voluntary Code and had transparent trading arrangements. However, in their October 2007 submission to the Review of the Produce and Grocery Industry Code of Conduct, they have argued for further regulation on retail chains. They listed a number of major concerns including:

- Prices and other terms and conditions;
- Disputes relating to prices/returns;
- Quality and handling of rejected produce, including returning purchased, ripened (or packages) produce; and
- Slow payment or failure to pay.

Growcom's submission reveals two significant concessions.

Firstly, the retail chains should be included in any horticulture Code. Indeed, as Brismark has consistently argued, market dominance and the issue of abuse of market power by the retail majors was the catalyst for the long chain of events which led to the introduction of the Code.

In 1999, the Joint Select Committee on the Retailing Sector recommended a mandatory Code to regulate the retail chains. The Report of the Review of the Retail Grocery Industry Code of Conduct (Buck Report) recommended a mandatory Code covering the entire industry including grocery retailers and processors. Submissions by Horticulture Australia Council and National Farmers Federation also called for a Code which applied to all parties including retailer, exporters and processors.

The Code in its present form compounds the structural deficiencies of the Australian retail market. The report of the Joint Select Committee described the abuses that can result from the huge market share enjoyed by a retail duopoly. The Code imposes additional costs that are passed on to businesses that rely on the Central Markets. Independent green grocers struggling to survive against the corporate bears cannot avoid Code costs that major supermarkets do not pay.

The second revelation from Growcom's submission was that a lack of contractual "transparency" was not the root cause of grower's complaints. The issues listed above were previously ascribed to the wholesaling sector as justification for a mandatory code. Linking the same complaints to the "transparent" retail chains contradicts that argument.

The more important transparency issue relates to market signals. Excessive retail margins highlighted frequently in the media have broken the nexus between purchase price and selling price in relation to fresh fruit and vegetables. Whereas in past oversupply situations could be relieved by lower retail prices the practice of supermarkets not passing on lower prices prolongs gluts and lessens returns to growers.

Brismark calls for retailers, processors and exporters to be included under the coverage of any mandatory Code, so that there are no distortionary impacts which disadvantage certain sectors of the fresh produce industry.

Proposed changes to the Code to achieve a workable outcome:

1. **Amend clause 9(4)(a) to read:**

   (a) *If the price of horticulture produce will be:*

   (i) *agreed before or upon delivery of produce to the merchant; or*

   (ii) *determined pursuant to a method of calculating the return price set out in the agreement or a method agreed to in writing between the merchant and the grower before delivery of produce to the merchant.*

2. **Amend clause 25(1)** by the addition of the phrase "subject to subclause 3", and as follows:

   Subject to subclause 25(3), the price that is to be paid by the merchant for the purchase of the grower's produce must only be an amount not a method for calculating an amount.

3. **Amend subclause 25(2)** by adding the words " *Subject to subclause 25(3)*" as follows:

   Subject to subclause 25(3), the amount must be agreed in writing between the merchant and the grower either before, or immediately upon, delivery of the produce to the merchant

4. **Add a new subclause 25(3) (4) and (5)** as follows:

   25(3) The price that is to be paid by the merchant for the purchase of the grower's produce may be determined pursuant to a method for calculating an amount, provided that:

   (a) the method is agreed to between the merchant and the grower in writing before delivery of the produce to the merchant;

   (b) the method clearly defines how the return price will be determined;

   (c) the method does not permit the merchant to exercise any discretion in the determination of the price for the product; and

   (d) in addition to the reports to be given to the grower under subclause 28(1), the merchant agrees to provide under the agreement, upon written request by the grower within a reasonable period following delivery of the produce, reasonable documentation supporting the calculation of the price in accordance with the method.

   25(4) Where the requirements of subclause 25(3) are not complied with for a method, the agreement will be deemed to be void and:

   (a) the grower and the merchant must immediately agree in writing on a price for the purchase of the grower's produce; and

   (b) in the event that the merchant and grower do not agree on a price in writing, then there shall deemed to be a horticulture dispute and the price shall be determined under a dispute resolution procedure.

   25(5) A failure to comply with subclause 25(3) with respect to a method is a breach of this Code.

BRISBANE

MARKETS

BRISBANE MARKETS LIMITED

Submission – January 2008

Horticulture Code Committee

1.0 Impact of the Code

The Code has increased the cost of operating as a wholesaler (trader), it has increased variability in pricing, has introduced new administrative requirements, and for many growers, has increased the risk and cost of doing business.

There were numerous growers and wholesalers who did act prior to 15 December 2006 to put in place supply agreements so as to facilitate a trading relationship outside the Code. This was the only opportunity available to adopt more flexible arrangements than those prescribed by the Code.

With time, the contractual obligations required under the Code may yield some positive outcomes however, it not hard to conclude that far better outcomes could have been achieved by a more commercially focussed code.

While the Code has been promoted as being a "safety net", it fails in this capacity by allowing no flexibility for parties to contract out of some of the more inflexible and costly requirements which it prescribes. It is not a 'safety net' at all – it is a set of prescriptive regulations which applies to all businesses within one sector of the horticulture industry. It applies irrespective of the size, professionalism and commercial competency of the parties involved.

Other shortcomings with the Code are now seeing those growing sector organisations that lobbied for the Code, seeking limited exemptions for certain parties but not others, a proposal which would add further to the distortionary impact of the Code and its anti-competitive impact. Any moves which further disadvantage certain parties, while favouring others, is totally inappropriate and is opposed by this organisation. Any amendments to increase flexibility under the Code, must apply equally to all traders.

2.0 How do growers and wholesalers perceive the Code

The majority of growers and wholesalers still have a negative attitude towards the Code.

From a grower's perspective, those who favour regulation and who have been unable to establish an effective commercial relationship with their wholesaler/s believe the Code does not go far enough and want more onerous regulations.

This however, is a minority of growers, being those who still believe the Government has a role and responsibility in regulating business transactions.

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Those growers who have an effective commercial relationship are now facing extra costs with little or no commercial benefit.

Those growers who use the Markets as a dumping ground (eg numerous direct suppliers) are using the Code as a means of trying to regulate the relationships they have with their wholesalers to their own advantage when they, as a group, should be given no special protection as they have no commitment to the Central Markets as a supply chain.

Many growers remain reluctant to execute Horticulture Produce Agreements, particularly when they see little or no commercial benefit in doing so, and/or have previously had an effective working relationship with their wholesaler which they do not want to change.

The wholesaling sector generally continues to perceive the Code negatively, which is not unexpected given the manner in which the Code was introduced, how many of the recommendations of the Centre for International Economics (CIE) as contained in the Regulatory Impact Statement) were ignored, and how the issue was politically manipulated by key grower organisations supportive of the Code.

The requirement to have documented terms of trade so as to improve "contractual clarity" is supported by BML and the vast majority of wholesalers however, the current code imposes other requirements which introduce costs, remove flexibility, reduce market signals and reduce the efficiency of the supply chain.

In this regard, the code has failed to achieve most of the objectives which were used by the Minister for Agriculture, Fisheries and Forestry, Peter McGauran, to justify its existence.

The Code as it stands, represents a failed and flawed policy response following an inadequate, biased and politically influenced review process.

3.0 Options and actions that will support the effective operation of the Code.

To be meaningful in supporting the adoption of better commercial practices throughout the horticulture industry, the code must be amended so as to establish guiding principles that promote good commercial practice, rather than dictating inflexible and unworkable arrangements which turn businesses (growers and wholesalers) away from the Code and force them to operate in breach of its provisions. These guiding principles should be built around the elements of:

- Wholesalers (Traders) having documented terms of trade
- These terms of trade providing a contractual basis to the commercial relationship between wholesalers and growers with a requirement that they disclose:
  - The nature of transactions, ie Agent/Merchant
  - The payment terms applicable
  - The quality/grade standards applying
- Providing for a dispute resolution framework

Brisbane Markets Limited and Brismark have jointly proposed a small number of changes to the Code that will promote its effective operation. A copy of these proposed amendments which will facilitate increased flexibility and reduce the compliance costs associated with the Code, is attached for your reference.

Importantly, amendments need to be made to the Code to allow growers and wholesalers the opportunity to agree to and document commercial arrangements which may assist them in gaining greater flexibility and/or reduce the transaction costs of doing business.

4.0 Options to increase awareness of the Code and its requirements

Given this issue has been running for over three years, any person with a need/desire to know about the Code should be well aware of it.

Surveys of growers conducted by Roy Morgan Research, and through the industry magazine, Fresh Source, have continued to highlight that growers do not support the current code or see justification for it. The fact is that most growers have a good relationship with their Market wholesalers and are far more concerned about the issues of water, overproduction, cheap foreign imports and the domination of the industry by the retail chain duopoly.

While the results of these surveys have been criticised by the staunch supporters of the Code, they themselves have done nothing to quantify growers views regarding the Code or to substantiate the counter claims which they make.

Those grower organisations, which saw the Code as being so important, should now be held accountable and be responsible for justifying the need for the Code and promoting the Code to their constituents. They should not receive any further Government funding to do this.

5.0 General Issues relating to the Code

5.1 Red Tape Reduction

Regulation and red tape have increased over the past five years despite a Federal Government Productivity Commission review of the Regulatory Burden on Business.

The Productivity Commission was directed by the Treasurer to review the regulatory burden imposed on a range of primary industries, including agriculture. The benefits of slashing government red tape and the associated increased productivity were highlighted as offering a potential $100 billion benefit to Australia's economy

The Banks Report (January 2006) was specific about the recommended process to be followed to halt the dramatic growth in business regulations that has occurred over the past decade. However, many of the Banks Report recommendations were ignored by the Federal Government and in 2006/07, more regulation was introduced.

As a result, the opportunity was lost for the Federal Government to introduce into the horticulture industry a fair, commercial and cost-effective Horticulture Code of Conduct.

5.2 Regulation Impact Statement (RIS)

When the final RIS used by the Federal Government to justify the introduction of the Mandatory Horticulture Code of Conduct was finally released as a public document (many months after the decision to introduce the Code was made by the Federal Government), it raised more questions than it answered. The final RIS as submitted by the Minister for Agriculture, Fisheries and Forestry, had reduced in content by some 80% when compared to the draft document circulated to the industry some 12 months beforehand.

Of significant concern were conclusions drawn which, far from supporting the introduction of the Code, raised concerns about the cost to the Industry, its failure to benefit the broader industry, and its threat to the competitive nature of the industry.

Importantly, it needs to be noted that in producing the RIS, the CIE was NOT required to assess the need of justification for such a Code.

The final recommendations included in the RIS were never subject to industry analysis or review and the Code implemented by the Federal Government, fails to recognise the role or manner of operations of Central Markets as a clearing house for the fresh produce industry.

The impact of supply and demand on pricing, the low level of complaints within the industry, and the very good commercial relationships, which exist between many growers and wholesalers, were not recognised at all, with the Code being a one size fits all approach to regulating the wholesaling sector of the fresh produce industry.

This kind of approach has been criticised by numerous Federal Government reviews of business red tape – but conveniently ignored in relation to the Horticulture Code of Conduct.

5.3 Code Review

The application of the existing Horticulture Code should be deferred until a further detailed and objective review is conducted into the manner in which the code was introduced, the justification for it and the provisions it contains. The whole process of how the code was introduced is clouded by political intervention and bias, a process which occurred in direct contravention of the Federal Government's own policy guidelines as recommended by the Red Tape Reduction Taskforce and with reference to a Regulation Impact Statement (RIS) document which not only changed dramatically from the draft document review by the industry to the final version submitted with a substantial reduction in content. It also saw a code introduced in direct conflict to some of the key recommendations and conclusions contained in the RIS.

Clearly, there is a strong argument which says the code as introduced represents poor and inappropriate policy making and that for the good of the Horticulture Industry, there must be an immediate and concerted effort to replace it with something which is more commercial, more flexible and more appropriate in promoting good commercial practice.

6.0 Conclusions

The Code offers some potential benefits in relation to promoting the use of terms of trade documentation and in providing for a dispute resolution mechanism. Beyond this however, the Code is too prescriptive and inflexible to add value for the majority of businesses within the industry.

In view of the ongoing failure of the Code to contribute positively and significantly to the commercial relationships between growers and traders, BML is calling for the Minister for Agriculture, Fisheries and Forestry to:

1. Suspend the application of the existing Horticulture Code of Conduct pending a further detailed enquiry into the need for and nature of any Code of Conduct in the fresh produce industry.
2. That the Centre for International Economics be engaged to review and resubmit their final Regulation Impact Statement document based on new, clear and objective terms of reference which ask them to investigate and report on:
   - i) The justification and/or need for such a Code.
   - ii) The alternatives available to mandatory industry Codes of Conduct and the relative merits of each, and
   - iii) The recommended content of any voluntary/mandatory Code, if such a Code is justified.
3. Appoint an industry Committee, including representatives from DAFF and the ACCC as well as industry representatives, to progress a detailed analysis of the need for such a Code and make further recommendations to the Minister regarding the subsequent amendment and/or repeal of the Code as appropriate as an urgent and negotiated industry-based outcome.

Andrew Young
Chief Executive Officer

January 2008