Public Submission

Re: Horticulture Code

by Brisbane Markets Limited

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1. INTRODUCTION

Brisbane Markets Limited (BML) has what is in excess of a $120 million investment in servicing the supply chain based around the ownership and operation of a Central Market.

Across Australia, Central Market owners such as BML, have in excess of an estimated $500 million investment in Market infrastructure, while Market-based wholesalers (of which there are around 400), and other Market-based tenants have in excess of a further $500 million invested in business assets and infrastructure.

As such, this organisation, like its interstate counterparts, and the many Market wholesaling businesses nationally, have a real concern about the operation of a code and its impact on the industry. The Code does NOT meet the primary objectives underlying the Code, (as detailed by the Centre for International Economics (CIE) in the final Regulation Impact Statement) in that it interferes with commercial relationships right across the wholesaling sector of the industry and it restricts the ability for growers and wholesalers to access flexible trading options. Furthermore, the Code has failed to meet established Government policy regarding the introduction of regulations on business, and remains both distortionary and anticompetitive in its impact.

The process of reviewing of the Code has now seen four calls for submissions in close to a 6-month period, two by the Horticulture Code Advisory Committee and two by the ACCC.

Of increasing concern is the inference being displayed in this review process which appears to pigeonhole all growers and all wholesalers (traders) such that neither is capable of transacting business without the imposition of the prescriptive requirements of the Horticulture Code.

What is even more intriguing is that in introducing the Code, the Government justified regulating an industry sector which its own advisors had told them was highly competitive with relatively low profit margins, while at the same time justifying the exclusion of another industry sector which their own advisors had previously characterised as lacking competition and had even recommended that this other sector should be subject to a mandatory code of conduct.

2. BASIS FOR CODE

The Final Regulation Impact Statement (RIS) compiled by the Centre for International Economics (CIE) drew the following conclusions:

- There is evidence to indicate that the wholesale market is subject to intense competition (RIS Section 2.2 p4)

- The evidence of competition at the wholesale level is reflected in key market outcomes – particularly relatively low profit margins.(RIS Section 2.2 p5)

- The problems of lack of clarity and transparency impact mainly on smaller scale growers – growers who are a long way from the markets, growers who supply infrequently to the markets or who are new entrants, and growers who have found it difficult to overcome information problems in the market. They are “outsiders”. (RIS Section 3 p8)

The CIE estimated that the potential problem transactions make up less that five per cent of total sales of domestically produced fruit and vegetables (RIS Section 3 p8)

The Final RIS (Section 4 p10) states that three primary objectives should underlie the code:

- To address the problem identified
- To avoid unintended side effects, and
- To ensure it is effective

Importantly, the RIS stated (Section 4.2 p10) that in order to avoid unintended side effects, and to minimise the costs of imposing the Code would require:

- Minimising interference in areas where problems do not exist
- Ensuring flexible trading options remain so that
  - There are no prescriptive 'one size fits all' terms and conditions
  - Anti-competitive structures are imposed that might greatly favor one party over another and force some players out of the Market.

The RIS also highlighted that the recommendations of the Red Tape Reduction taskforce were ignored in that the need or justification of having such a Code were never part of the evaluation process.

As stated in the RIS, "a 'no code' option was not considered because of the Government's election commitment". (RIS Section 5 p12)

This position contradicts all public policy statements regarding the effective formulation and introduction of regulations on business, and highlights both the hypocrisy of the prior Federal Government in relation to this issue and the level of political intervention which occurred in delivering on an election promise.

Under Section 7- Impact Analysis, the final RIS highlights that the Code will mainly benefit those growers associated with the 5% of the total sales where they believe there is the potential for problems.

The report goes on to state that the costs of the Code will affect all wholesalers and growers (an estimated 1140 wholesalers inside and outside wholesale markets and approximately 11,100 fruit and vegetable growers throughout Australia).

It states further that "additional requirements and costs brought about by the Code will primarily impact on wholesalers".

Under Section 9 – Conclusions, of the final RIS it noted that "written terms of trade in particular provide greater clarity and certainty about transactions".

This position is supported and not in dispute.

The document went on to add that the costs of having the code "'are expected to outweigh benefits because costs are imposed on all participants, whereas benefits will mainly accrue to a limited number of growers".

What one can determine from the Final RIS is that after the CIE's lengthy process of analysis and evaluation, they concluded that

- the Code may benefit those transactions which comprise up to just 5% of the total sales of domestically produced fruit and vegetables,
- the Code will come at a net cost to the industry, and
- the option of having No Code, a Voluntary Code, or indeed, continuing to use the Produce and Grocery Industry Code of Conduct, were never considered because of the political decision by the Government of the day to deliver a Mandatory Code as an election promise.

Against a backdrop of political pork barreling, no case was made to justify the existence of the Code.

The potential for, or existence of, some level of commercial disputation between growers and wholesalers (traders), or the benefits of using documented terms of trade, has never been denied by the wholesaling sector representative organisations. What they do say however, is that these issues could be addressed through other options such as the Produce and Grocery Industry Code of Conduct, or through a more commercial, less prescriptive and more flexible Horticulture Code.

2.1 Growers' Expectations

There is evidence from the comments being made at the public hearings being conducted by the ACCC that many growers who supported the introduction of the Code, "expected more from it".

The Code was never going to be the panacea which some claimed it would be. The Code represents a classic example where the political rhetoric that built people's expectations went well beyond what was ever going to be achievable.

It was a case of a promise that growers would get something for nothing – supporting the code and doing nothing different, would result in them getting better returns.

This was always a hollow promise which defied economic logic.

The premise that by forcing wholesalers to take more risk would leave more money for growers simply defies logic. The very notion which underlies trade and commerce that if wholesalers are going to increase their exposure to risk, they will increase their margin to manage that risk, was completely ignored.

The level of zeal with which certain individuals pursued the outlawing of the "hybrid" transaction, without even seeking to evaluate whether it had a genuine role within the industry, and the preparedness to dismantle and destroy all that is good with the existing way business is done by the majority of growers and wholesalers, must surely border on negligence.

If the code is really about improving contractual clarity and transparency, it should seek to establish a framework which promotes clarity and transparency and leaves it to growers and wholesalers to operate as efficiently and effectively as they can within that framework.

The Code should not outlaw any type of relationship which has shown to be extremely effective for many growers in providing them with a fair, market-based return price for their produce in a manner which is otherwise, lawful, competitive, cost effective and efficient.

If the government wants to impose the desires of a section of the growing industry on all other growers, they should at least give those growers the option to contract out of those otherwise harsh conditions if they so choose – that is to say, if the Code does provide a prohibition on growers and wholesalers agreeing to a method of determining the return price to be paid to the grower, it should allow growers and wholesalers to contract out of that specific requirement by agreement in writing. The current prohibition in the code is removing access to a cost effective and efficient method of doing business that is supported by many, if not the majority of growers.

2.2 Produce and Grocery Industry Code of Conduct

The comment and/or inference has been made on numerous occasions by those seeking to justify the existence of two separate codes, one voluntary and one mandatory, that the voluntary Produce and Grocery Industry Code (PGIC) does not apply to wholesalers. This is incorrect.

Further, other statements which infer that wholesalers have not supported the PGIC because they do not subscribe to it, is also incorrect. There is in fact no mechanism for subscribing to the Code.

The market wholesaling sector has in fact supported the PGIC and is in fact represented on the committee overseeing the Code by the Australian Chamber of Fruit and Vegetable Industries Limited.

Complaints against wholesalers made under the terms of the PGIC were investigated and there was a high level of cooperation between wholesaler representative organisations and wholesalers in seeking to have any issues raised resolved.

The fact is that the PGIC can work as well for the wholesaling sector as it does for the retailing sector.

The industry would benefit from having one single code, and one single disputes resolution framework.

The level of complaints raised against wholesalers under the PGIC was low and this continues to be the case under the mandatory code.

The PGIC and the disputes resolution framework which exists under the PGIC remain an alternative which simply duplicates the framework under the Horticulture Code.

2.3 Disputes Resolution

One of the claims made by those supporting the introduction of the mandatory Horticulture Code of Conduct was that growers were not prepared to use the numerous dispute resolution frameworks that have been available to them.

In the case of Queensland, this has included:

- *The Farm Produce Marketing Act*

  This Act operated for many years up until its repeal in 2000. The Act provided for the operation of the 'hybrid' style of transaction, prescribed books of account, and established a dispute resolution framework with the existence of Government inspectors.

  After a number of reviews, the Act was repealed as it was shown to have a total compliance cost which exceeded the value of benefits provided.

- *Existing legal structures*

  The option of pursuing dispute settlement through existing legal channels remains available to all within the industry.

- *Magistrates Court – mediation services.*

  A free mediation service has existed in relation to the Magistrates Courts system in operation throughout Queensland. We understand that this option has been rarely, if ever, used in the process of dispute resolution between a grower and a wholesaler.

- *The Brismark code of Practice for Wholesalers*

  Brismark introduced a Code for Practice for wholesalers in 2000. The Code provided for wholesalers to be Accredited as subscribers to the Brismark code. Wholesalers who supported the Code offered their growers documented terms of trade and access to a dispute resolution framework. They paid to be Accredited and these funds were used to promote support for the Code.

  Grower representative organisations failed to give their support for the role of the code as a business tool and the wholesalers who subscribed to the Code reported that it failed to deliver them any commercial advantage.

  Growers maintained a focus on their existing trading relationships and saw little or no merit in delivering a commercial bias towards those wholesalers (traders) who were accredited under the Code. The operation of the Code was suspended by Brismark in 2006.

- *Brismark/Brisbane Markets Limited Disputes Resolution framework*

  Brismark and BML continue to operate a toll free Grower Hotline and a disputes resolution service for growers. This is a free service which involves complaint investigation and access to trained mediators.

  The number of complaints received remains very low, with just seven received and investigated over the past 12 months.

- *Produce and Grocery Industry Code of Conduct*

  As previously discussed, the PGIC existed as a framework for the resolution of disputes between growers and wholesales for a number of years prior to the introduction of the Horticulture Code. The level of complaints raised under the PGIC fell far short of what those advocating a mandatory code said would exist if the mandatory Code became a reality.

  The regular claim has been that only under a legislated arrangement would growers be prepared to lodge their complaints.

  This was never the case under the Farm Produce Marketing Act (Qld), which was repealed after some three reviews over a 10-year period and the conclusion that both the costs of administering the Act and the costs of compliance, could not justify its existence. This was supported by a statement in the final review, that many growers went out of their way to operate outside the requirements of the Act.

It would appear that very little has changed. Industry policy and indeed Government regulations should not be built around anecdotal evidence.

This organisation supports the establishment of a disputes resolution framework, but highlights the need to ensure that the magnitude of the issues which exist are kept in perspective given the size of the industry and the number of transactions which occur.

While the Horticulture Code of Conduct has been in place for over one year, there still has not been any report to the industry by the Horticulture Mediation Adviser appointed under the Code as to the number or nature of commercial complaints which have been received and investigated.

How can industry organisations act to address the issues which are supposed to exist in the industry if there is NO transparency at all in relation to the most fundamental issues, such as the number and nature of commercial complaints actually being made?

2.4 Contractual Clarity and Transparency

The introduction of the Code had a basis in promoting "contractual clarity and transparency".

Little was done to define these terms, but much was made about having wholesalers disclose whether they were operating as an "agent" or a "merchant", and outlawing the so-called "hybrid" transaction.

In terms of transparency, all efforts to give a greater commercial meaning to this area were cut from early drafts of the Code. Transparency in the fruit and vegetable industry should also be about disclosure of issues relating to product quality, food safety, product specifications and communications along the supply chain, however, no specific mention is made of these fundamental issues in the Code.

This organisation supports the use of documented terms of trade. We support those terms of trade providing contractual clarity in relation to payment terms, the nature of the relationship, how return prices will be determined, and the use of a dispute resolution framework.

A documented method of determining a return price is both clear and transparent, with an audit trail available to evidence the transaction.

2.5 Unintended consequences of Over-Regulation

While the Code may well have a purpose of protecting "outsiders", as described by the CIE, the one major unintended consequence of having overly-prescriptive and inflexible regulations, as contained in the current Code, is significant.

With the costs of compliance and an increased risk in doing business with those who may fit into the category of "outsiders", one inevitable consequence is that many wholesalers will simply stop doing business with them.

The outcome may well be that the Code which was supposed to protect them will be the regulatory imposition which results in them being forced out of business.

2.6 Role of Central Markets

One issue which appears to be regularly overlooked in the debate over the Horticulture Code is that of the role of the Central Markets and Central Market Wholesalers.

While the major retailers are in a position to order specified quantities of fresh produce so as to meet their projected needs, they also retain the right under their terms of trade, to cancel orders as they see fit, reject produce – largely as they see fit, and to order more or top up from a Central Market as they see fit.

It needs to be understood that both the supply and demand for fresh produce can fluctuate dramatically from day to day because of an array of factors ranging from prevailing conditions influencing consumer buying patterns, to natural disasters affecting production and supply, product imports, other demands diverting consumer expenditure on food (eg major events, school terms etc).

Central Markets operate with three main functions, being:

- A clearing house for the available volumes and specification of produce supplied
- A marketing hub – where demand is concentrated in a single location, and
- A distribution hub – where transport efficiencies can be achieved for the receival and dispatch of produce.

A wholesaler (trader) is not operating like a major retailer. They are unlikely to have discreet order quantities which will meet their needs. They are operating in a marketplace where they are seeking to match supply volumes with demand.

While the majority of wholesalers do work to manage the supply volumes they receive from their growers, they are operating in a competitive environment, whereby the supply situation across the Market is not known until the market conditions are unfolding and trading is underway.

For many lines of produce, there may be anywhere between tens and hundreds of growers supplying product to numerous wholesalers within a Market. Furthermore, for some lines, there is also the increasing presence of imported product.

In a very volatile market, such as mangoes, the season can open at a high price as limited volumes of product come onto the market. The risk at this stage is that growers wanting to gain the benefit of early high prices pick their crop too early (fruit too immature). This will inevitably result in product quality issues.

As the mango season progresses, there is often a rapid drop in prices as more product comes into the market. Without strict product quality controls by growers, the market will often become glutted with mixed qualities of product.

Growers will often oversupply their wholesaler, or if their usual wholesaler will not accept their excess volumes, they will find another wholesaler who will.

The mango season is relatively short and growers have a limited time in which to harvest, pack and market their product. Growers have their own financial commitments and there is an obvious underlying desire to market as much product as they can in an effort to maximise their returns.

In a very volatile market, and with what can be a week to 10 days between a mango being harvested in say North Queensland, shipped to market (up to three days), ripened and made available for sale, the market price for the produce could have risen or slumped (most likely the latter) by as much as 70-90%.

For any wholesaler to agree on a price for the product prior to receipt – ie up to some 3-10 days before the product is going to be available for sale, will obviously mean that the wholesaler will be very conservative in their pricing.

For example, the wholesaler may offer $15/tray, subject to confirmation of quality, for mangoes to be available for sale in a week, when the prevailing market is $40/tray. This is how volatile the market is and this is the reality which those growers who want on farm pricing, fail to recognise or accept.

In this situation, the vast majority of growers will reject the on-farm offer price, and seek to retain the existing arrangement, being a return price which reflects the prevailing market price. The prevailing market price may well only be $10 - $20 per tray, when the product is actually sold.

Furthermore, the fact is that an 'agency' transaction gives a grower NO certainty at all as to the price they will receive.

The reality is that the existing 'hybrid' transaction offered the best outcome in most situations as it offers both growers and wholesalers the most cost efficient and effective transaction-based outcome.

The option of having terms of trade documentation that gives clarity to the "sale price less a margin" option offers the best outcome for growers in meeting the objectives of the Code and the needs of the industry.

3. ANALYSIS OF ISSUES

3.1 Reluctance of Growers to Complain

The claim that growers are reluctant to complain for fear of some form of commercial retaliation as retribution has been around for over a decade.

It was used by some grower representative organisations to argue against the repeal of State-based Farm Produce Marketing legislation in the 1990's – when this legislation was shown to have a cost which far outweighed the benefits. It has also been used as an argument as to why industry self-regulation would not work, and now it is being used to justify the fact that very few commercially-based complaints are being lodged under the Horticulture Code.

This excuse has been shown to be used whenever there is an inability to substantiate the anecdotal claims being made by these grower representative organisations.

At some point, those who continue to make this claim must be held accountable.

If there are commercially-based complaints, they must be raised in a timely and factual manner so that they can be appropriately investigated. After the past three years of debate regarding this issue in relation to the Code, unless the anecdotal claims being made are not able to be fully substantiated, they should now be totally discounted.

3.2 Reluctance to Regulate Retailers, Processors and Exporters

If the Code is about promoting better commercial practice, and is to do so fairly and equitably, a single Code should exist and it should apply to the first point of sale, no matter whom the grower is doing business with. As such, the Code would serve to establish good commercial practices, and those same practices would apply across the entire industry. This is both simple and fair.

It is grossly unfair and inappropriate that under the Code, a wholesaler (trader) is not allowed to accept returns from the buyer of produce and return the title for those goods to the grower for reasons such as the product being outside the required specifications. Other parties exempt from the code are allowed to do this, and do so frequently.

The Code is imposing a set of commercial standards on wholesalers (traders) that is now much higher, and much more onerous than what applies to retailers, exporters or processors buying direct. There is NO basis to justify this anticompetitive situation.

There has been no significant analysis of what growers' views are in relation to this issue. The views of those organisations which oppose this type of arrangement are continually shown not to be the views of mainstream growers.

The most comprehensive insight into what growers want is reflected in the results of the Roy Morgan Research Survey which looked into growers' views of the code. It was conducted from a database of some 3,500 growers and 604 respondents in April 2007.

The survey 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 with the balance being unsure).**
- 90% of growers think that it is important to have an effective Central Market system.
- In terms of importance, the Horticulture Code of Conduct issue 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.

The survey is the most comprehensive analysis undertaken to date of the views of growers on this issue.

3.3 Concerns for Compliance Costs

It is of significant interest that one of the arguments raised by the ACCC to maintain the exclusion of retailers from the Code is the potential to impose unnecessary compliance costs.

Why should compliance costs be an issue when it concerns retailers but not an issue when it involves wholesalers (traders)?

The final Regulation Impact Statement prepared by the CIE identified that the Code would benefit up to an estimated 5% of transactions. That leaves a massive 95% of that are incurring compliance costs for no benefit.

Why is the Code being imposed in a "one size fits all" manner, which is both inefficient and costly in how it targets the perceived problem?

This approach is contrary to what was recommended by the CIE.

If compliance costs are to be considered as a factor in determining the scope of the Code, there is a significant and a very persuasive argument which supports the Code applying to all businesses which purchase fresh produce from a grower, but with the grower and that party having the ability to contract out of certain provisions of the Code through the terms of their Horticulture Produce Agreement.

3.4 Should the Code impose a cessation date on pre-existing contracts?

Pre-existing agreements allowed the significant percentage of growers who saw little or no merit in the Code avoid its application.

Those growers with pre-existing contracts who now want the Code to apply can simply terminate that contract.

There is no justification or need to provide for a cessation date on these agreements unless the Code is amended to provide the ability for parties to contract out of the prescriptive provisions of the Code which remove flexibility and impose significant compliance costs.

To unilaterally apply a cessation date, without giving growers any other alternatives, reflects a big brother attitude which is not only archaic, but for those who entered into those agreements because they already had an excellent working relationship with their wholesaler (trader), it takes away the only option they had in avoiding the costly and inflexible requirements of the Code.

3.5 Should the Code be amended to allow a method or formula by which to establish a return price to growers?

Yes. The Code should be amended so as to provide a template which promotes good commercial practice. It should not prescribe the nature of the commercial relationship.

The Code should be amended so as to require that all parties involved in purchasing product from a grower are required to have documented terms of trade, and that they are subject to a standard disputes resolution framework.

The Code should prescribe that their terms of trade should specify:

- payment terms
- how and when the return price will be calculated or determined
- the product quality specifications to apply how product returns.

3.6 Should the Horticulture Code permit additional services?

Wholesalers (traders) must be allowed to provide additional services.

This is part of the commercial value they offer in the supply chain, with services extending from:

- warehousing
- quality checking
- picking and sorting
- repacking
- payment advances

- marketing initiatives
- marketing services
- distribution services
- food safety services

Any notion that wholesalers (traders) only exist to on-sell product is both out of date and irrelevant given the demands and needs of the industry.

The majority of wholesalers provide a differing range of value-added/additional services that form part of their service offering to and the commercial relationship they have, with their suppliers.

To even contemplate regulating to restrict any business from providing services which add value to their service offering or which assist them to compete in a highly competitive market is anticompetitive an highly distortionary.

The Code has no role in limiting and restricting the competitive nature of the industry which ensures growers have access to a diverse range of service offerings in a highly competitive market.

3.7 Should Market Credit Services offer collection services for growers?

It is unclear what the Issues Paper is proposing in relation to the operation of Market Credit Services. Whether these services offer collection arrangements for growers would appear to be a commercial decision that each Credit Service would need to make.

3.8 Agency transactions

There remains questions as to whether a mandatory code can over-ride agency law. Whether a wholesaler wants to be an agent or not, depends on a number of commercial considerations including:

- Costs – the additional costs of administering agency transactions
- Demand – the demand from growers for a wholesaler (trader) to operate as an agent
- Risk to intellectual property – disclosure of a buyer's details to a grower can lead them to having to compete with the grower who may use the information to bypass the wholesaler and sell direct to those buyers
- Commercial reality – if growers really wanted agency arrangements and were prepared to pay for it, there would be more wholesalers (traders) operating as agents now. The lack of agents within the industry says one thing – there is a lack of demand for agents, and those who do want it, are NOT prepared to pay for it.

3.9 Application of the Code to grower owned co-operatives / packhouses.

The Code should contain no exclusions. If the document was properly drafted as a tool to promote better commercial practices across the fruit and vegetable industry, it would be equally relevant to all.

Many grower packhouses are not cooperatively owned, and many have a very strong position in terms of their negotiating power with their grower suppliers.

Clearly, a portion of the complaints and misunderstandings that occur within the industry relate to the grey area which can exist when one grower is marketing both their own and other growers' produce.

3.10 Extension of the Code beyond the first point of sale

There has been no case presented for industry consideration and debate regarding the extension of the Code beyond the first point of sale.

For the Code to apply to transactions between one wholesaler (trader) and another or between wholesalers (traders) and retailers, would add a further dimension of complexity and cost.

This organisation opposes any extension of the Code beyond the first point of sale, that being the first transaction between a grower and a wholesaler (trader), retailer, exporter or processor.

3.11 Pooling of Produce and Price Averaging

There is justification to support the pooling of produce of a similar grade/specification and/or price averaging in respect of produce of a similar grade/specification.

This flexibility should be allowed under the Code.