

Freehills

21 July 2005

Your ref A90973 & A90974
Phone +61 3 9288 1655
Email Emma.Gordon@freehills.com
Doc no Melbourne\004681352

Mr Scott Gregson
A/g General Manager, Adjudication Branch
Australian Competition and Consumer Commission
PO Box 1199
Dickson ACT 2602

By email

Dear Mr Gregson

Applications for authorisations A90973 & A90974 lodged by the Tasmanian Forest Contractors Association Ltd

We refer to your letter of 7 July 2005 to Gunns Limited (**Gunns**) seeking its comments in relation to two related applications for authorisation and interim authorisation (A90973 and A90974) lodged by the Tasmanian Forest Contractors Association Ltd (**TFCA**) and to your telephone conversation with Peter McDonald on 20 July 2005.

We have been instructed by Gunns to provide comments on its behalf in relation to the TFCA's application for interim authorisation. Thank you for this opportunity to respond and for granting a short extension of time in which to make a submission.

This letter provides summary submissions expressing Gunns' serious concerns about the possible grant of the interim authorisation sought by the TFCA. We advise that Gunns also intends to provide a full and detailed submission in respect of the TFCA's substantive authorisation application, at the appropriate time.

1 Interim authorisations sought

The TFCA has sought interim authorisation to allow TFCA members to 'collectively negotiate' the terms and conditions of forestry contracts.

Gunns is extremely concerned at the prospect of the grant of this interim authorisation, taking into account:

- (a) The serious trade practices and competition concerns raised by the conduct, which relates to:
 - (1) the setting of industry-wide contract prices, as is (notwithstanding the TFCA's submission to the contrary):

- specifically contemplated by the negotiation outcomes referred to above, for example:
 - the adoption of a 'transparent' diesel fuel surcharge;
 - the adoption of an indexing model to be used for the annual adjustment of contract rates;
 - the adoption of new rate matrixes;
 - a new clause containing minimum annual contract revenue targets;
 - apparent from the nature of the public benefits said to arise from the conduct, as identified in section 10 of the submission;
- (2) the setting of industry-wide terms and conditions;
 - (3) industry-wide collective boycott activity, which can be used to reinforce price-fixing and other anti-competitive conduct.
- (b) The breadth of the conduct and its industry wide effect, having regard to the fact that it relates to:
- (1) all of the five major wood products companies in Tasmania; and
 - (2) a potentially very high proportion of contractors (on the basis of the stated TFCA 'strong membership' levels which are said to already represent '85%' of the total wood flows produced by forest contractors within Tasmania).

In making this submission, Gunns notes that it is not privy to details of the actual number of contractors who are TFCA members and the proportion of its current contracts held with these contractors.

2 Considerations for the grant of interim authorisation

As indicated in your letter of 7 July 2005, in the absence of special circumstances, interim authorisation is unlikely to be granted where to do so:

- would permanently alter the competitive dynamics of the market; or
- inhibit the market from returning to its pre-interim state if authorisation is later denied.

The ACCC has stated in its guide to authorisations that interim authorisation should only be allowed in exceptional circumstances. We submit that this must be the case because such a decision:

- is made without considering the merits of the application;
- removes substantive legal rights of the parties affected; and
- can result in serious anti-competitive conduct, which may otherwise be subject to proceedings instituted by the ACCC or parties injured by the conduct.

The TFCA has not made out any case for the grant of interim authorisation. Neither has it made substantive submissions in support of the need for an immediate authorisation. The fact that the TFCA would prefer to engage in

prohibited conduct now is irrelevant and interim authorisation should not be granted on this basis. However, Gunns also submits that there are very strong reasons why interim authorisation should not be granted in relation to the application.

Gunns submits that there is a high risk that the interim authorisation sought would permanently alter the competitive dynamics of the market and would inhibit the market from returning to its pre-interim state if authorisation is later denied, for the following reasons:

- (a) The TFCA contemplates that changes negotiated pursuant to authorisation might be incorporated into existing contracts within eight weeks of the conclusion of negotiations (as well as being automatically included in new contracts). In the absence of agreement being reached, the TFCA seeks authorisation of boycott activity.

Accordingly, it appears that the conduct, if authorised, would affect all forestry contracts in Tasmania to which TFCA contractors are party (which, given the stated extent of TFCA membership, as noted above, may be a substantial number). This would include existing contracts which were awarded and negotiated in good faith by the parties following a competitive tender process. Gunns notes that the majority of its ongoing contracts are long term contracts and that attempted renegotiation mid-term would have significant effects (some of which are difficult to predict).

- (b) Gunns introduced its current competitive tendering practice approximately ten years ago in order to alleviate the problems arising with the previous uncompetitive central pricing system and in order to ensure its ability to remain internationally competitive (in the competitive environment described below). It believes its tendering processes to have been, and to continue to be, successful in meeting these aims. For example, its contracting processes are flexible in that contracts are tailored to reflect the particular circumstances of each contractor, rather than applying a 'one size fits all' approach.

It is Gunns' belief that introducing collective negotiation would fundamentally undermine its contracting practice which has developed in accordance with competitive imperatives and changes in industry dynamics. It is Gunns' view that the introduction of collective bargaining would permanently affect the operation of the market and is extremely concerned that the TFCA appears to be advocating a return to the anti-competitive practices of 15 years ago.

Dealings between wood product companies and forestry contractors have not been subject to heavy handed regulation in the past and there has been no significant recent structural changes to warrant a return to practices that existed before the acceptance of competition laws.

- (c) Wood products companies continue to face intense international and domestic competition in selling their products (some of which are commodities). An increase in input costs, particularly forestry contracting costs, which can constitute up to 50% of the final product cost, would significantly and immediately affect their ability to compete effectively and put at risk their ongoing viability. It would also have a direct and

immediate effect upon prices to consumers in domestic downstream markets.

Gunns submits that there are no special circumstances that would merit the grant of the interim authorisation sought and, in particular, notes that:

- (a) It is not the case that the interim authorisation application arises in connection, for example, with regulatory or policy reform. Neither has it arisen in response to changes in industry practice. Gunns' current practice of contracting following a competitive tender process has been in place for some ten years.
- (b) Gunns is unaware of any time imperative upon the TFCA's push for the introduction of collective negotiation. For example, Gunns does not have any substantial number of contracts up for re-tender or renegotiation in the near future and is not aware of any other impending bulk contract negotiation in the industry.
- (c) As noted by the TFCA in its submission, the position of forestry contractors has been considered by the Tasmanian Government, leading to the development of the Forestry Fair Contracts Code in 2003. In the past, the Tasmanian Government has not moved to introduce more heavy handed industry-wide regulation.

3 Other matters

There are other matters which also suggest that interim authorisation should not be granted:

- (a) The extent of the effect of the authorised conduct is unclear. For example, the matters which TFCA committees may nominate to be the subject of collective negotiation (and, accordingly collective boycott) are expressly not limited to those matters identified in section 11 and may extend to 'new concepts and bargaining positions' as 'deemed necessary' by the relevant TFCA committees.

The proposed conduct involves a potentially very large number of unidentified contractors across a broad range of forestry services (ranging from planting trees, managing trees, harvesting trees, timber transportation and land clearing services).

- (b) Serious questions arise as to the TFCA's ability to substantiate the public benefits which it asserts to arise from the conduct:

- **Safety**

There is nothing to suggest that collective negotiation of the type contemplated by the proposed authorisation would increase safety. In this regard, Gunns refers to the high level of safety regulation in the industry and the significance placed by Gunns (and it believes, other wood product companies) upon safety certification requirements and past records when assessing and awarding tenders.

- **Employment and training**

There is no evidence put forward to suggest that efficient and well performing contractors face increased difficulty in attracting and keeping employees in a competitive environment.

- Transaction costs

The involvement of the TFCA in contractual negotiations is, in fact, likely to add another layer of administrative cost for wood products companies. Companies will continue to have to deal with individual contractors on-site, in administering contracts and (as suggested by the TFCA) in negotiating individual contract prices. It seems probable that industry transaction costs would increase under the proposed arrangements.

- Industry sustainability

Far from assisting industry sustainability, the end of competitive tender arrangements in favour of a return to centralised contracting via collective negotiation, would, in Gunn's view, permanently affect the operation of the market and undermine its ability to continue to meet strong domestic and international competition.

In light of the above matters, Gunns submits that the interim authorisations sought by the TFCA should not be granted in any form. There must be a full assessment of anti-competitive detriments and alleged public benefits before such significant price fixing and exclusionary conduct is contemplated in an industry that has long moved away from anti-competitive practices in response to international and domestic market conditions. Gunns would welcome any opportunity to further discuss its concerns about the applications for interim authorisation with the ACCC.

If you have any queries or wish to discuss this matter further, please do not hesitate to contact me on 03 9288 1628 or Peter McDonald on 03 9288 1597.

Yours faithfully
Freehills



Bob Baxt
Partner