



9 July, 2009
Your Ref: 37959
Our Ref: QL09/253

Ms Sue Philp
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Australian Competition and Consumer Commission
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Dear Ms Philp

Transport Workers Union of Australia SA/NT Branch – Application for authorisation A91146 – interested party consultation

Thank you for your invitation to comment on the above application, as outlined in your correspondence of 29 June, 2009.

The Parmalat Group (*Parmalat*) in Australia, comprising Parmalat Australia Ltd (*PA*) and Parmalat Food Products Pty Ltd (*PFP*) oppose the Transport Workers Union of Australia SA/NT branch (*TWU*) application for authorisation A91146 (*the Application*). In summary, the grounds for this opposition are:

1. The Application fails to provide evidence that there is sufficient public benefit to outweigh the public detriment;
2. The Application fails to correctly identify relevant market characteristics; and
3. The Application fails to correctly identify the future with and without the proposed arrangement.

Also PFP, in purchasing the divestment business of National Foods Limited (*NFD*) pursuant to the undertaking given by NFD to the Australian Competition and Consumer Commission (*the Commission*) will, in South Australia, become the franchisor of the franchised distribution formally operated by Dairy Farmers. Parmalat intends to continue to have products in South Australia delivered via a franchised distribution network. Parmalat is yet to complete the acquisition of the divestment business. As a consequence, the granting of the Application prior to the Parmalat taking ownership of and operating the divestment business for a reasonable period of time would appear to be premature and possibly prejudicial to Parmalat's business.

If, despite these matters, the Commission was to approve the Application and grant the authorisation, there are several aspects that Parmalat believe require clarification before this was to occur.

The Application fails to provide evidence that there is sufficient public benefit to outweigh the public detriment.

Many of the benefits set out in section 6 of the Application are either not benefits but statements of intention or appear to be benefits that accrue to distributors rather than the public.

Fairness in the Negotiating Process

It is submitted that fairness in the negotiating process is already achieved through:

- (i) The provisions of the Franchising Code of Conduct, particularly those that apply to franchisors;
- (ii) The unconscionable conduct provisions of the Trade Practices Act 1974 (Cth) (the Act); and
- (iii) The probable application of the new 'unfair contracts' legislation.

The claimed benefit is an improvement in the distributors bargaining position, and it is then claimed that this will lead to *"improved service and other public benefits"*. These are not specified.

It appears that the only benefit sought through the Application is the improvement in the distributors bargaining position. That is a benefit to the distributors and not to the public.

Compliance with Statutory Requirements

Section 6.2 of the Application claims that collective bargaining will eliminate incentives for the parties to *"cut corners"* with respect to statutory requirements. Parmalat has various processes in place, which are reviewed regularly, to ensure statutory and regulatory compliance. All responsible businesses do. It is submitted that the oversight by the various regulatory authorities that exist in Australia, and specifically in South Australia combined with the penalties that apply, provide far more incentive to ensure compliance with statutory and regulatory requirement than collective bargaining can or will. The claimed public benefit appears to be illusory.

Efficiency of Operations

The claimed benefits of efficiency of operations in section 6.3 of the Application do not appear to accrue to the public. In one sentence it is claimed there has been *"the effect of reducing transport costs and the total costs to vendors"*. It is then claimed that *"increases in ...delivery fees have been absorbed by*

processor price increases". If transport costs have fallen, why have delivery fees been increased?

Also If distributor margins have increased, and this has been absorbed by processor price increases then surely the increased processor prices are a detriment to the public rather than a benefit.

Continued Viability of Independent Distribution Sector

No substantive evidence is provided to support the claim that the Application will lead to the continued viability of the independent distribution sector. The claim also ignores the relevant market factors that:

- (i) Increased supermarket home branding and market shares are changes that are occurring in the market throughout the country and not just in South Australia; however
- (ii) There are various methods available to processors to distribute their products to customers/ retailers and ultimately to consumers, of which an independent distributor network is just one. From the processor point of view, for the distribution of packaged milk, to date, the independent distributor network has provided the most effective method of distribution. Despite this, changes to the market have forced changes on both the processors and distributors. Part of this change has been the rationalisation of distributors as processors seek to ensure that the independent distributors they contract with are of sufficient size and have sufficient economies of scale to withstand the continuing changes in the market.

The Application fails to acknowledge that a continuing viable independent distributor network is also in the processors as well as the distributors interest. Parmalat has invested considerable resources in the development of its franchise network and will continue to do so because of its belief that a successful group of franchised distributors is a benefit to both parties. Collective bargaining of itself is not sufficient to ensure the viability of the independent distribution sector. There needs to be a commitment by the distributors and the processors to the sector. The Application cannot of itself deliver such a commitment and as such, fails to provide a benefit, either to the public or to the distributors.

Rationalisation of business is likely to continue, as it has in other states. However, if the Application is successful and rationalisation, where necessary, is resisted, it would be hard to argue that the maintenance of otherwise unviable businesses is a benefit to the public.

Reduction in Transaction Costs

The argument concerning reduced transaction costs in section 6.5 of the Application appears to be ignorant of clause 11 of the Franchising Code of Conduct (*the Code*). This requires that franchisors ensure that franchisees

obtain appropriate legal, accounting and business advice. Failure to do so is a breach of section 51AE of the Act.

Even if the Application is approved, those processors, such as Parmalat, who have implemented a franchising model, are required to act in accordance with the Code and to deal with each franchisee individually. The introduction of collective bargaining and the need to deal with the TWU as well as individual franchisees may actually add to the transaction costs rather than reduce them.

Better Information.

The claim that *“the TWU will be able to negotiate on the basis of more comprehensive and accurate market information”* appears to be an alleged benefit to the distributors and not to the public.

Improvement in Health and Safety

Distributors are not the only people to face increased levels of work and higher stress levels as a consequence of a changing market and increased regulatory requirements concerning safety. The Application appears to be suggesting that collective bargaining will be able to overcome market and regulatory forces that affect the dairy industry.

Dispute Resolution/Opt Out Clause/ No Boycotts

The matters set out in sections 6.8,6.9 and 6.10 of the Application are statements of intent and show no public benefit whatsoever.

Rationalisation

The Application makes various claims concerning rationalisation. The principal claims are:

- (i) *“processor rationalisation of the distributor network had a significant effect on the vendor system as it forced twenty five vendors who either did not want to get bigger or lacked the capital to enlarge their businesses to sell at ‘bargain basement prices”*
- (ii) In Fairness in the Negotiating Process the Application also states *“This is reflected in the decline in numbers and profitability of milk rounds since deregulation, as vendors have been forced to accept oppressive contractual terms which strongly favour the processors”*
- (iii) However in Efficiency in Operations it is claimed that *“Collective negotiations (A90927) allowed the consolidation and the increase in the average size of rounds”*

The first two claims appear to be contradicted by the third. It is unclear what, if anything was actually achieved by collective bargaining in the rationalisation process.

Market Assessment

The market assessment contained in the Application also appears erroneous. Parmalat submits that the two relevant markets in South Australia are the market for the supply of milk and dairy products to retailers and the market for the supply of products to consumers.

The background provided in sections 1 and 2 of the Application also appears to omit several relevant factors which are set out below.

There has been a reduction in the number of franchisees/distributors in the Industry, due to the following factors including:

- (i) The increasing influence and market share of major supermarket groups and independent grocery sites.
- (ii) Cross Docking (direct delivery to supermarket warehouses rather than to individual stores) for major grocery (supermarket) and petrol & convenience accounts. (Including house-brands), with a growth of 56 % since 1999.
- (iii) Sale of franchises/distributor businesses due to the expenses associated with compliance issues. (Cold Chain, HACCP and Transport Chain of Responsibility)
- (iv) Reluctance by some franchisees/distributors to accommodate change including updated IT requirements.

Franchisee rationalisation was required to accommodate and provide a stable platform for franchisee viability, territory expansion and sales growth and optimal financial return for those businesses. Furthermore, where franchisees exit a business, the sale price of the business is based upon the current commercial value of the business.

Another aspect of industry change is the emergence of national and state buying groups, such as Metcash, and the need for processors to meet the requirements of this sector of the market.

To accommodate this, processors have implemented cartage fees (delivery fees) on 'bulk, centrally or processor billed' products which are delivered to major customers by distributors. While the delivery fee may be less than the margin previously made by the distributor on those products, the fee also recognises that the distributor is no longer required to maintain credit accounts for those customers and that the risk of customer default, as well as the account keeping costs have passed to the processor. Additionally, payment from these major customers is usually longer than that of other distributor customers, and this is another cost that is transferred from the distributor to the processor.

The increase in the number of major customers moving from distributor billed to processor billed has not originated with the processors. These major customers are growing, and as part of the ongoing trading relationship with them they have various requirements that their suppliers are obliged to meet in order to keep trading with them. These include the need for one supplier invoice, not one invoice from each distributor that supplies them. In addition, many require either electronic ordering, electronic invoicing or both. This means that the processor and the distributor need to have compatible IT platforms, and given the number of distributors involved, it makes commercial sense that a standard platform is used.

The Future

As well as incorrectly identifying public benefits, the Application's other principal shortcoming is its failure to recognise the impact the introduction of franchising has had and will continue to have on the distribution sector of the dairy industry. Parmalat has operated franchises in Queensland for a number of years, has recently successfully introduced franchising to its Victorian operations, and currently has a limited number of existing South Australian franchisees.

Parmalat believes that franchising has and will continue to deliver:

- (i) Proven, market successful business systems;
- (ii) Practical and moral support to franchisees;
- (iii) A focus on customer service standards by both franchised distributors and Parmalat; and
- (iv) Through the Parmalat Leadership Council, a forum to discuss and resolve matters of concern to both franchisees and Parmalat.

A key concept of franchising is that the franchisor/processor and the franchisees/distributors need to work together to ensure the mutual success of their businesses. Direct communication and negotiation between the franchisor and its franchisees, without the involvement of third parties achieves this. Where the involvement of a third party is required, the Code has mediation provisions.

As well, Parmalat remains committed to maintaining and growing its brands in Australia. Parmalat's strong, direct relationships with its franchisees are a key part of protecting and building the sustainability of those brands. This also provides the franchisees with brands and products that will strengthen their businesses.

Retailers demand a consistent and reliable means of supply. As part of this franchisees and processors need to work together to achieve this.

The future with collective bargaining fails to recognise and may hinder direct communication between franchisees and the franchisor. It also overlooks various provisions in the Code. Collective bargaining may have been

appropriate prior to the introduction of franchising, with a market comprising independent distributors. The structure and discipline that franchising brings to both the franchisor and the franchisee works to negate the need and usefulness of collective bargaining. The success of such systems is substantially dependant on the relationship between the franchisor and the franchisees. If the relationship is not working effectively, this is something the parties need to work at themselves. Collective bargaining may actually hinder the development of good relations between the parties, and this is of no benefit to the public.

In addition, the extra layer of dealings required by the Application is likely to result in increased costs to processors who may seek to recover those costs through increased product prices. This is ultimately a detriment to the consumers of milk and dairy products in South Australia.

Matters Requiring Clarification

If despite the matters contained in this submission, it is intended that the authorisation sought in the Application is to be granted, Parmalat believes that the TWU, as occurred with Authorisation A90927, should confirm the following:

1. that the TWU will negotiate separately with National Foods and Parmalat;
2. that any authorisation only extends to new and not existing agreements between Parmalat and its franchised distributors;
3. that any authorisation only extends to existing franchise distributors and not to those distributors who have ceased being distributors prior to the authorisation being granted or who cease being distributors during the authorisation period;
4. that Parmalat is free to, as it sees fit:
 - a. offer new agreements to distributors, if it in its sole discretion, elects to;
 - b. agree or refuse to agree to terms proposed by the TWU for any new agreement, and that Parmalat cannot be compelled to negotiate with the TWU;
 - c. negotiate, refuse to negotiate, and/or cease to negotiate with the TWU or with any collective bargaining groups of distributors represented by the TWU; and
 - d. approach, negotiate and contract with distributors on an individual basis, at any time and whether or not they are part of any collective group represented by the TWU, if the distributor notifies Parmalat that it wishes this to occur.
5. all distributors are free at any time:

- a. to join or withdraw from any collective bargaining group represented by the TWU; and
 - b. to enter into new agreements with Parmalat on such terms as they consider appropriate, regardless of the TWU's view on such contracts;
6. The TWU and distributors are required to refrain from disclosing the terms of any agreement or proposed agreement between a processor and distributors to another processor or distributors to whom that other processor has offered contracts; and
7. Parmalat has clarity about which distributors are represented by the TWU. In the case of non-members of the TWU, it is assumed that they will not be represented by the TWU unless they give positive consent to this, rather than being required to "opt out".

For and on behalf of
Parmalat Australia Ltd and Parmalat Food Products Pty Ltd



Fabio Genitrini
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