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18 May 2012

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Dear Dr Chadwick

Jireh International Pty Ltd – Exclusive Dealing Notification N93244

IMPORTANT NOTE

This is a copy of our letter to the ACCC dated 18 May 2012. Information that is commercially sensitive or otherwise confidential to Jireh International Pty Ltd has been redacted. Jireh has instructed us to provide the ACCC with this redacted version of the letter so that it may be placed on the public register.

Although those parts of this letter that have been redacted are not for general publication, Jireh recognises that certain Gloria Jeans Coffee franchisees may have a legitimate commercial interest in that information. Any such Gloria Jeans franchisee should apply directly to Jireh for that information to be disclosed to them, subject to conditions including confidentiality.

All Annexures referred to in this letter are confidential and are excluded from publication.

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1 Preliminary

- 1.1 Further to our conversation with John Rouw of your office on 1 May 2012, we confirm that we act for Jireh International Pty Ltd (**Jireh**), the Australian franchisor of Gloria Jean's Coffees (**GJC**).
- 1.2 Jireh has provided us with a copy of your letter to Fiona Wallwork of Norton Rose Australia dated 16 April 2012, and has instructed us to respond on Jireh's behalf.
- 1.3 This letter contains information that is commercially sensitive and confidential to Jireh. It is provided to the ACCC for the purpose of assisting it with its assessment of the complaints and the public benefits of Jireh's arrangements notified by way of the Exclusive Dealing Notification [REDACTED]
- 1.4 [REDACTED]
- 1.5 Jireh is keen to respond to the complaints outlined in the ACCC's letter. It is important to note, however, that the complaints have been outlined to Jireh in general terms only. Without better and further particulars of each complaint, Jireh can provide the ACCC only with general responses.
- 1.6 As outlined below, Jireh has recently implemented a number of major changes to its food program under a national food strategy called the "New Food Program" (**NFP**). The NFP was introduced to update GJC's food menu offering to maximise efficiencies and thereby improve the overall competitiveness of GJC franchisees in the market. The changes under the NFP, which include the introduction of a new national food menu and the enhancement of GJC's food distribution system, are all within the scope of the notified arrangements outlined in the Notification.
- 1.7 We are instructed to respond to your letter with the following information, provided after due inquiry and to the best of Jireh's knowledge.

2 Complaint Regarding Range of Suppliers and/or Products

- 2.1 The implementation of the NFP has involved a review of Jireh's Approved Products and Approved Suppliers. This has resulted in a reduction in the number of Approved Products in Jireh's food category from [REDACTED] to [REDACTED]. However, there is now a broader variety of available food options for different times of the day, for example new breakfast, lunch and "all-day" items.
- 2.2 Importantly, since the introduction of the NFP, Jireh has increased the number of its Approved Suppliers of food products from [REDACTED] in August 2011 to [REDACTED] as at May 2012.
- 2.3 Jireh's purpose in implementing these changes has been to increase the competitiveness of the GJC business in the market and create a more modern and nationally uniform menu of food items available to consumers. Other objectives include increasing food sales by franchisees; increasing efficiencies; and reducing risks in supply, distribution, food storage, handling and preparation. Ultimately, these changes are aimed at maintaining and enhancing the commercial relevance and competitiveness of GJC franchises by improving the quality and consistency of its food offerings.

- 2.4 To increase efficiencies in the GJC food supply chain, Jireh has also expanded the range of food lines that can be distributed by its approved national distributor, [REDACTED]. While [REDACTED] previously distributed only [REDACTED] products to GJC franchisees, under the NFP it is now able to distribute [REDACTED] food lines to GJC franchisees nationally.
- 2.5 As a result, GJC franchisees can now acquire the majority of Approved Products on the new national food menu from [REDACTED] or, should they choose to, deal directly with the relevant Approved Supplier. There is no requirement for GJC franchisees to use [REDACTED]. Franchisees may choose to deal directly with Approved Suppliers.
- 2.6 The rationalisation of the number of approved food products, along with the expansion of available food lines that can be distributed nationally by [REDACTED], was due to the fact that the existing GJC food regime had become inefficient, costly and difficult to manage efficiently.
- 2.7 For example, before the NFP was rolled out, GJC stores across Australia had access to [REDACTED] food products supplied by [REDACTED] suppliers. Numerous similar items were supplied by multiple suppliers and quality control was difficult to monitor and enforce. As a result, a number of the public benefits intended by the notified conduct (set out at subparagraph 4(a) of the Notification) were not being optimised.
- 2.8 [REDACTED] rollout of the NFP commenced in South Australia in about May 2011, and Jireh is currently in the process of rolling out the NFP with GJC franchisees in other states and territories.

3 Complaint Regarding Price Competitiveness with Prior Suppliers and Products

- 3.1 It is not possible to respond in detail to the claim that Approved Suppliers and/or Approved Products are not price competitive with previous suppliers without particulars of the specific suppliers and/or products concerned. In general terms, however, Jireh notes that to the extent that some franchisees may now pay slightly more for some product types:
- (a) price is only one aspect of competition – Jireh has sought to ensure that franchisees have access to high quality products at a *reasonable price* as *quality* and *value* are central to the GJC brand;
 - (b) further, the same prices are now available uniformly across the entire franchise network, rather than some franchisees enjoying lower prices while others bear the cost of reduced buying power and other lost efficiencies; and
 - (c) the current Approved Suppliers and Approved Products better ensure that the public benefits intended by the notified conduct (including those set out at subparagraph 4(a) of the Notification) are maximised.

4 Complaint Regarding Requirement to Buy Equipment Outside Notified Arrangements

- 4.1 Jireh is not aware of any equipment other than the ovens mentioned in your letter to which this complaint may relate.
- 4.2 A component of NFP is the introduction of a line of [REDACTED] food items that are oven cooked in the store at or close to the time of purchase by customers (**Oven**

Cooked Food). There is currently no requirement for GJC franchisees to offer Oven Cooked Food to customers.

- 4.3 As it must be cooked in-store, those franchisees choosing to offer Oven Cooked Food in their stores need to have use of a suitable oven. Jireh selected the "Merrychef" oven as an Approved Product by conducting a trial and comparison of two potentially suitable units: [REDACTED] and Merrychef. Jireh selected Merrychef on the basis of it offering a number of desirable features, such as an easy to use touch pad; the sensory qualities of its cooked products; a menu program easily obtained by users and readily uploadable via USB port; and its overall serviceability.
- 4.4 Ice & Oven Technologies Pty Ltd is the exclusive distributor of the Merrychef oven in Australia and has been approved by Jireh as an Approved Supplier.
- 4.5 Franchisees may choose to either purchase or rent the Merrychef oven. [REDACTED]
- 4.6 It follows from the above that franchisees are not, as a matter of fact, required to buy ovens:
- (a) The need for the use of an oven, be it by way of purchase or rental, is not compulsory and is completely at the discretion of each franchisee.
 - (b) Jireh does not sell Oven Cooked Food to franchisees for resale to the public.
 - (c) Even where a franchisee chooses to sell Oven Cooked Food and therefore requires the use of an oven, the approved equipment may be either bought from Ice & Oven, or alternatively rented (and then, if desired by the franchisee, bought) [REDACTED]
- 4.7 As such, the arrangements regarding the Merrychef oven do not constitute third line forcing under sections 47(6) or 47(7) of the *Competition and Consumer Act 2010* (Cth). However, to the extent that the ACCC forms the contrary view that the arrangements amount to third line forcing, the conduct is clearly within the scope of the notified arrangements as outlined in the Notification.
- 4.8 Properly construed, the notified arrangements described in paragraph 2 of the Notification clearly include Jireh requiring franchisees to purchase "equipment" from Approved Suppliers. Subparagraphs 2(a) and 2(b) are to be read conjunctively. The term "equipment" is expressly included in the definition of "Products" set out at subparagraph 2(b). In the context in which the term is used, an oven such as the Merrychef clearly meets that description. Equally, subparagraph 2(a) includes reference to "associated items" which, in the context of the whole of paragraph 2, may be construed as including equipment such as ovens necessary for the preparation of "certain food products".
- 5 Complaint Regarding Approval of Suppliers**
- 5.1 We understand the complaint about Approved Suppliers to be that certain suppliers have not been authorised, despite them meeting the criteria set out in clause 6.9 of the GJC Franchise Agreement current as at December 2007 and partially reproduced in the Notification.

5.2 Again, it is difficult to respond to this complaint without details of the actual supplier and the request for its approval. However, to assist the ACCC's consideration of this matter further information regarding the number of approval applications Jireh has received and approved is set out at paragraphs 13.5 to 13.7 below.

6 Question 1: Have the supply arrangements for franchisees covered by notification N93244 changed since 2007?

6.1 As outlined above, in broad terms the supply arrangements authorised under the Notification have not changed to date. In particular, GJC franchisees are still required under their Franchise Agreements to purchase certain products from Jireh or its Approved Suppliers.

6.2 As anticipated in the Notification and in GJC Franchise Agreements, changes have from time to time been made to the list of Approved Products and Approved Suppliers. However, a larger than usual number of changes have recently been, and continue to be, implemented in accordance with the NFP.

7 Question 2: If the supply arrangements have changed, can Jireh provide an updated submission to the ACCC on the benefits and detriments resulting from the notified conduct that addresses the changes in the conduct?

7.1 As outlined above, in broad terms the supply arrangements contemplated by the Notification have not changed. However, Jireh acknowledges that the implementation of the NFP brings with it a number of amendments to the list of Approved Products and Approved Suppliers.

7.2 As mentioned at paragraph 8 below, Jireh intends to lodge an updated exclusive dealing notification with the ACCC that will better articulate the public benefits and any detriments arising from these changes.

7.3 In addition to the benefits outlined above and those set out in the Notification, Jireh considers that the NFP will provide the following public benefits:

- (a) Market competitiveness of the GJC business will be enhanced;
- (b) Franchisees will now have access to a greater number of Approved Suppliers;
- (c) Franchisees will now have access to a wider variety of food options including new breakfast, lunch and all-day food items that were previously unavailable;
- (d) Franchisees will also have greater access to better quality food items at a reasonable cost;
- (e) The greater consistency and quality of food items sold across GJC franchises will improve the general customer experience and the competitiveness of the GJC brand;
- (f) The NFP will improve food storage, handling and preparation procedures which will result in higher quality, consistency and safety of food sold to consumers;
- (g) The NFP will decrease wastage of food products which will result in greater cost efficiencies that can be passed on to consumers in the form of lower prices;

- (h) Increased efficiencies in the food supply chain which will increase convenience for franchisees and reduce transaction costs;
- (i) For those GJC franchisees that operate outside of the major city areas, the expansion of the new food lines available under the NFP will increase their access to new food items, improving the variety of food products available to consumers in those areas;
- (j) Increased availability of healthy food options for consumers, including products with higher nutritional value and a greater range of additive-free items. For example, as part of the NFP Jireh has introduced new food lines with reduced salt and sugar content and the reduced use of food preservatives and additives.
- (k) A national product offering and increased volumes will provide greater buying power for Jireh which will result in volume discounts that can be passed on to consumers in the form of lower prices.

7.4 There will be no significant public detriments that arise from these changes.

8 Question 3: Will Jireh be lodging any further notifications for exclusive dealing, related to requirements placed on Gloria Jean's franchisees, for the ACCC's consideration?

8.1 Yes. Jireh considers it worthwhile to prepare and lodge an updated Exclusive Dealing Notification that is more "reader friendly" and which more clearly articulates the information provided about the relevant notified conduct and the arguments, facts and evidence in support of the notification. It intends to do so shortly.

9 Question 4: How and on what basis have the current suppliers been selected? For example, was there a tender process, consultation with franchisees or some other approach taken?

9.1 Approval of the Merrychef oven is addressed above at paragraph 4

9.2

9.3 Jireh has a formal process for selecting food and beverage products from Approved Suppliers. This process is necessarily detailed and rigorous in order for Jireh to ensure that any food products sold at GJC franchised outlets meet minimum quality, safety and consistency standards.

9.4 First, the need for a new product or supplier must be identified as filling a perceived gap in or otherwise adding meaningful value to the GJC franchise network's food offering.

9.5 The approval process is based primarily on a review of a prospective supplier's product/s and whether they meet Jireh's standards, having regard to attributes such as appearance, taste, nutritional value and cost.

9.6 Once a need for a product or supplier is identified, the following steps are taken:

(a)

- (b) [Redacted]
- (c) [Redacted]
- (i) [Redacted]
- (ii) [Redacted]
- (iv) [Redacted]
- (d) [Redacted]
- (e) [Redacted]
- (f) [Redacted]

9.7 Once an Approved Supplier's products are integrated into the supply chain, Jireh has a strict monitoring system in place to ensure that quality and safety standards are being continually met. Jireh has appointed a dedicated Quality System Administrator who is responsible for managing Approved Supplier quality standards post-approval.

10 Question 5: How and when were these changes first communicated to franchisees and how will they be implemented, for example is there a transitional period?

10.1 Jireh first announced the proposed rollout of the NFP to GJC franchisees in early 2011 at a series of roadshows that Jireh conducted with GJC franchisees across Australia. At these roadshows, GJC franchisees were informed [Redacted] As part of this, Jireh informed franchisees about the NFP [Redacted]

10.2 The dates of the franchisee roadshows in early 2011 are as follows:

- (a) 31st March – WA & NT;
- (b) 1st April – SA;
- (c) 5th April – VIC;

- (d) 6th April – QLD;
- (e) 7th April – NSW/ACT; and
- (f) 12th April – TAS.

- 10.3 Following these initial communications, GJC franchisees have been provided with regular updates about the progress of the [REDACTED]. They have also been provided with regular email updates about the upcoming rollout of the NFP in their areas.
- 10.4 Prior to the rollout of the program in each State, GJC franchisees were notified by State Operations Managers of the new rollout and were invited to attend briefing sessions to try the food items on the new menu and receive further training on how to handle and prepare the new food items.
- 10.5 The rollout of the NFP commenced in May 2011 [REDACTED] by South Australian GJC franchisees. Since then, the NFP has been progressively and successfully rolled out with franchisees in other States and Territories across Australia. Jireh expects the rollout of the NFP to be fully implemented approximately within the next [REDACTED]

11 Question 6: Does Jireh receive a rebate or fee or other benefit from suppliers to franchisees?

- 11.1 Since before 2007, Jireh has received rebates and other similar financial benefits from a number of companies that supply goods and services to Jireh and GJC franchisees. [REDACTED]
- 11.2 A list of the names of the companies who provided rebates and other similar financial benefits to Jireh in the previous financial year is included in the Disclosure Document that Jireh provides to all prospective GJC franchisees.

- 11.3 [REDACTED]

12 Question 7: If Jireh does receive a rebate or fee or other benefit from suppliers:**a. What is the value of the benefits and how are they structured?**

12.1 Rebates received from Jireh's Approved Suppliers are calculated based on an agreed percentage, [REDACTED] of total sales revenue. [REDACTED].

b. Are franchisees informed of such payments and, if so, how and when?

12.2 Yes. Currently, a list of all companies that have provided Jireh with a rebate or other financial benefit in the previous financial year is included in the Disclosure Document provided by Jireh to all prospective GJC franchisees. The Disclosure Document also states that Jireh and its associates may, from time to time, receive a rebate or other financial benefit from the supply of goods or services to GJC franchisees, which it may or may not share indirectly with franchisees.

12.3 [REDACTED] Rebates and financial benefits from suppliers are described in clause 9.1(j) & (k) of the Disclosure Document and a list of companies that have provided Jireh with a rebate or other financial benefit is contained in Appendix 5 of the Disclosure Document.

12.4 The list in Appendix 5 of the Disclosure Document does not include a number of Approved Suppliers identified in Jireh's response in paragraph 11.3 above, as these suppliers only commenced providing Jireh with a rebate after July 2011. Jireh is currently amending the Disclosure Document to include these Approved Suppliers on the list of companies that provided Jireh with a rebate or financial benefit in the 2011/2012 financial year.

c. How will any such benefits be used?

12.5 Rebate payments are incorporated into and form part of Jireh's general revenue.

12.6 As with all additional revenue sources, the receipt of rebates contributes to Jireh's ability to avoid significant and/or frequent increases of franchisee fees. GJC franchisee fees have not increased since at least 2007.

d. How do the current benefit arrangements, if any, compare with the situation when Jireh notified its conduct in 2007? For example, have they increased in proportion or total?

12.7 [REDACTED]

13 Question 8: Can franchisees sell products in addition to the goods required to be obtained from suppliers Jireh has nominated?

13.1 As outlined above, GJC franchisees cannot sell food products that are not from an Approved Supplier. Jireh has been aware that in the past a number of franchisees were selling food products that were not Approved Products or acquired from Approved Suppliers, contrary to the terms of their Franchise Agreement with Jireh.

13.2 The requirement that all food products sold by GJC franchisees be Approved Products is necessary for ensuring that Jireh maintains strict quality control standards

with respect to the food products sold at GJC retail outlets, amongst other things to maintain the value of the GJC brand.

a. Is clause 6.9 or a similar arrangement still in place in the Gloria Jean's franchise system? If so, will it be continued? If it is no longer in place and/or is not to be continued, why not?

13.3 Yes. [Redacted]

13.4 [Redacted]

b. How many times have franchisees sought approval to use alternative suppliers? How many times has approval been given?

13.5 Since the Notification was lodged in 2007, Jireh has received [Redacted] requests from GJC franchisees seeking written approval to obtain food products from a non-Approved Supplier. Jireh approved the vast majority of these requests.

13.6 During the period 2008 to 2011, Jireh approved the following suppliers following a franchisee request for approval:

- [Redacted]

13.7 During the same period, there were [Redacted] occasions where Jireh refused to approve a supplier following a franchisee request for approval, [Redacted]

[Redacted]:

(a) [Redacted]

(b) [Redacted]

(c) [Redacted]

[Redacted]

Yours sincerely

Johnson Winter & Slattery