MSF Sugar

30 January 2017

Mr David Hatfield
Director, Adjudication Branch
Australian Competition and Consumer Commission
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CANBERRA ACT 2601

By e-mail: adjudication@accc.gov.au

Dear Mr Hatfield

Re – A91558 - Queensland Cane Growers Organisation Ltd – submission on draft determination

Thank you for the invitation to make a submission in respect of the draft determination issued by the Commission on 15 December 2016 in respect of Queensland Cane Growers Organisation Ltd's (**'Applicant'**) application to the Commission for authorisation (A91588) (**'Draft Determination'**).

Summary

MSF Sugar remains of the view that the authorisation proposed in the Draft Determination, despite some modifications from the Applicant's original application, should not be made. We are concerned that the Draft Determination does not set out, in unambiguous terms, the precise conduct that is proposed to be authorised, and raises a risk that growers, millers, and marketers will not be certain of the boundaries of collective bargaining.

We also have concerns about the characterisation of certain elements of the industry in the Draft Determination, including growers' actual interest in cane and its by-products once sold to millers, and the commercial dynamics of cane supply agreements. Finally, there are a number of factual inaccuracies in the Draft Determination we wish to draw the Commission's attention to.

The submission below details these concerns.

1 Identifying the precise conduct to be authorised

1.1 MSF Sugar is concerned that there is a risk of ambiguity and uncertainty in relation to the scope of application of the proposed authorisation. This concern comes from a potential overlap, or lack of clarity, on state-wide collective conduct that is proposed to be authorised and state-wide collective conduct that is proposed not to be authorised.

1.2 Paragraph 218 of the Draft Determination sets out the conduct and the scope of application that the Commission proposes to grant authorisation in respect of.

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Departing from the original three-tiered authorisation sought by the Applicant, the Commission in paragraph 218 proposes to limit the scope of application:

(a) for collective bargaining of cane supply agreements and related contracts with millers and marketers – to growers "who supply cane to any mill that has the same owner";

(b) for information sharing to facilitate the adoption of best practice in contract terms – to growers across all districts regardless of mill ownership commonality; and

(c) for Canegrowers (head office) to provide information and services to local Canegrowers companies to support their local collective negotiations, including drafting contracts and dispute resolution practices.

1.3 The Commission, in paragraphs 5, 83, 102, 153, 158, 169, 199, and 214 of the Draft Determination, refers to the clarification it received from the Applicant on 18 November 2016 that the Applicant "does not seek authorisation to negotiate single state-wide cane supply and related agreements".[1] Repeated reference is also made in the Draft Determination to the Applicant's clarification that it does not seek to "assume the direct principal bargaining role", but to provide "advice and assistance to local Canegrowers companies."[2]

1.4 To this end, the Draft Determination in paragraph 222 specifically excludes from the conduct it proposes to authorise "Canegrowers collectively negotiating a single state-wide Cane Supply Agreement or related agreements with processors or sugar marketers." It also excludes "Canegrowers (head office) assuming the principal bargaining role in any collective negotiations." [3]

1.5 MSF Sugar submits that the proposed conduct in paragraph 218 of the Draft Determination, set out in 1.2(b) and 1.2(c) above, is in potential conflict with the conduct the Commission specifically proposes not to authorise in paragraph 222 of the Draft Determination, set out in 1.4 above.

1.6 This is because the state-wide information sharing, and state-wide provision of contract negotiation services by the Applicant that the Draft Determination proposes to authorise is likely to have the same or similar effect that authorising the Applicant to assume the direct principal bargaining role, or to negotiate state-wide agreements, would have.

1.7 The distinction between the Applicant "assuming the principal bargaining role" and the Applicant operating behind the scenes to "provide information and services" to growers in support of their collective negotiations risks being one of semantics, and, MSF Sugar submits, does not have the certainty sufficient for authorisation.

1.8 Further, the Applicant's clarification to the Commission on 18 November 2016 highlights the lack of certainty in the boundaries of the conduct proposed to be authorised. The Applicant, as summarised in the Draft Determination, represented to the Commission that "in most instances the collective negotiations are conducted by the local Canegrowers company and the miller".[4] We assume that the remainder of the negotiations take place at a broader, potentially state-wide level, and submit that the qualification that "most", not "all", of negotiations would be done at

[1] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 5. Other references to this clarification include the phrases "does not propose to centralise negotiations for the negotiation of a single-state wide cane supply and related agreement" (paragraph 153), and "does not intend to negotiate and enter into a single state-wide Cane Supply Agreement" (paragraph 199).
[2] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraphs 5, 83, 153, and 214.
[3] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 222.
[4] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 83.

this local level speaks to the uncertainty embodied in this element of the proposed authorisation. For the Commission to be satisfied that the public benefits of authorisation outweigh the public detriments, we submit that it should necessarily be satisfied of the basis on which all, not most, of the particular conduct will be carried out.

1.9 It is not clear how the conduct authorised in paragraph 218 of the Draft Determination would, when implemented, result in outcomes that would be substantively different from those that would result from the conduct which is specifically proposed not to be authorised in paragraph 222 of the Draft Determination.

1.10 Where the Applicant and its members are authorised to share information on the terms of cane supply agreements, and where Canegrowers' head office is authorised to assist local member organisations in their contract negotiations, it seems a highly likely result that standardisation will occur. As such, there is a real risk that the conduct proposed to be authorised will effectively result in the single state-wide approach to negotiation that is specifically excluded from authorisation in paragraph 222.

1.11 While MSF Sugar remains of the view that the authorisation should not be granted at all, we submit that this particular issue could be remedied by specifically limiting authorisation to Canegrowers members who supply cane to mills with common ownership (and then, in relation to those commonly owned mills only).

1.12 Further, the Applicant's clarification to the Commission on 18 November 2016 highlights the lack of certainty outlined above. The Applicant, as summarised in the Draft Determination, represented to the Commission that "in most instances the collective negotiations are conducted by the local Canegrowers company and the miller".[5] We assume that the remainder of the negotiations would then take place at a broader, potentially state-wide level, contradicting the Applicant's purported exclusion of it assuming the principal bargaining role, or of conducting state-wide negotiations.

1.13 For the Commission to be satisfied that the public benefits of authorisation outweigh its public detriments, we submit that it should necessarily be satisfied of the basis on which all, not most, of the particular conduct will be carried out. On that basis, we submit that the Commission should be wary of granting an authorisation on the understanding that the Applicant does not "intend" to carry out an activity,[6] particularly where the Applicant appears to have expressly contradicted that intention.

2 Characterisation of GEI sugar and by-products from processing

2.1 The above section focussed on the scope of application of authorisation proposed in the Draft Determination. This section focusses on the content of authorisation, specifically in relation to the inclusion of sugar marketing contracts and sugar by-products in the list of items which may be collectively bargained for.

2.2 The Draft Determination in paragraph 218 proposes to authorise collective bargaining by the Applicant and its members who supply cane to the same mill in relation to:[7]

(a) essential terms governing the supply of Grower Economic Interest ('**GEI**') sugar to GEI sugar marketers; and

(b) capturing the value of the by-products and related products from sugar cane.

[5] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 83.
[6] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 199.
[7] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 218.

2.3 MSF Sugar wishes to outline the facts of GEI sugar which may not have been made clear to the Commission by the Applicant. As the Commission notes in the Draft Determination, sugar cane is transferred from a grower to a miller at an agreed pick up point.[8] At this point, title in the cane passes in full to the miller, and the grower has no legal or equitable interest in the cane itself, or in any raw sugar or any other product the miller may produce from the cane they now own, from that point onward.

2.4 The arguments advanced by the Applicant to promote collective bargaining in relation to GEI sugar and the value of by-products appear to stem from a misapprehension that growers have an actual (contractual) interest in the cane following its sale to millers. These arguments include:

(a) the complaint that growers currently are "restricted to choose those GEI marketers with which the miller has an On-Supply Agreement";[9]

(b) the complaint that growers have a limited ability to ensure consistency between Cane Supply Agreements and On-Supply Agreements for raw sugar;[10]

(c) in the Applicant's submission, "growers bear the full financial consequences (revenues and cost) arising from the sale of GEI sugar";[11]

(d) that authorising collective bargaining for On-Supply Agreements will increase the competition for the "provision of GEI marketing services to those growers" bargaining;[12] and

(e) that millers' interpretation of the statutory authorisation to collectively bargain, in which revenue from by-products is excluded, is "very narrow".[13]

2.5 The term 'GEI sugar' is a term of convenience to describe portions of revenue. It does not encapsulate any actual legal interest held by a grower in any cane once sold to a miller, or the products a miller may produce from the cane, including raw sugar and by-products such as molasses. As the Commission notes in the Draft Determination, pricing for cane is established pursuant to a formula which ensures the price growers receive for their cane is reflective of the global commodity price for raw sugar.[14] This is a commercial dynamic and, like the term 'GEI', also does not impute or encapsulate any actual interest the grower has in the raw sugar a mill produces or a marketer sells on the global commodities market.

2.6 Additionally, in respect of the value of by-products, MSF Sugar draws the Commission's attention to the fact that by-products from the processing of cane, including molasses, were historically a cost to millers. Molasses was regarded as a waste product and required disposal at the mill's cost. Growers did not claim an interest in the by-products when this was the case. That millers have since been able to monetise this cost does not alter the fact that it is a by-product of the miller's processes, performed on cane owned by the miller.

[8] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 35.
[9] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 78.
[10] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 145.
[11] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 171.
[12] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 185.
[13] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 145.
[14] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 43.

2.7 Current industry developments highlight the significant impact that collective bargaining for by-product value in Cane Supply Agreements could have on millers. In a recent press interview, the Chairman of Mackay Sugar Limited (**Mackay Sugar**), Mr Andrew Cappello, discussed how Mackay Sugar's revenues have been insufficient to do the maintenance work necessary to keep the company's mills operating at full capacity, resulting in a fall in Mackay Sugar's mill crushing availability from 91.1% of maximum to 79% from 2010 to 2016.[15] Mr Cappello stated that Mackay Sugar's inclusion of molasses and fibre sales in its cane payment formula in around 2006 "has taken in excess of $65 million off the available funds that the mill could put back into the factory".

2.8 MSF Sugar submits that the arguments listed in 2.4 above, and much of the narrative accompanying those arguments, rest on an assumption that growers 'should' have these interests and rights, both in cane once title is passed to the miller, and in raw sugar or other products a miller chooses to produce with the cane that the miller owns. There is no legal or policy basis for this assumption, and authorisation should not be granted to realise or give effect to it.

3 Other items in Draft Determination

3.1 To take the full opportunity available to MSF Sugar in responding to the Draft Determination, we wish to draw the Commission's attention to a small number of factual inaccuracies which may affect the Commission's appreciation of the Queensland sugar industry and the effect of the proposed authorisation, as well as to clarify some aspects of the Draft Determination.

3.2 The description of the Applicant in paragraphs 14 to 17 of the Draft Determination, particularly that it is "the overarching state body representing the interests of sugarcane growers in Queensland", appears to be an acceptance of the Applicant's own characterisation.[16] While MSF Sugar does not dispute that the 80% of Queensland growers are members of the Applicant's organisation, we submit that the pertinent metric in determining the question of public benefits and detriments arising from the proposed authorisation is the percentage of total cane tonnage that the Applicant's members account for, rather than the headcount of growers.

3.3 The statement in paragraph 118 of the Draft Determination that sugar cane "needs to be crushed within 16 hours of harvest" is, in our opinion, incorrect.[17] It is true that best practice suggests minimise the cut-to-crush timing, however, in reality the cut-to-crush timing varies by mill and is dictated by cane supply logistics issues. It should also be recognised that this issue can be addressed by grower practice changes, such as the implementation of 24 hour harvesting. This is pertinent to the supposed monopolisation by millers as suggested in the Draft Determination.[18]

3.4 The characterisation in paragraph 145 of the Draft Determination, regarding the development of one of MSF Sugar's On-Supply Agreements, is inaccurate. We wish to clarify that the role of the Canegrowers members was limited to an observational capacity, and that they were not party to the negotiations between MSF Sugar and QSL on the terms of the On-Supply Agreement. The conclusion drawn by the Applicant, including that having growers "actively involved" resulted in a "smoothed" development of the On-Supply Agreement, is therefore misplaced.[19]

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[15] 'Mackay Sugar faces challenging 2017', *Daily Mercury*, 7 January 2017, available at http://www.dailymercury.com.au/news/big-read-mackay-sugar-faces-challenging-2017/3129443/.

[16] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraphs 14 - 17.

[17] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 118.

[18] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraphs 28, 118.

[19] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 145.

3.5 The statement made in paragraph 171 of the Draft Determination summarising the Applicant's view that "growers bear the full financial consequences (revenues and costs) arising from the sale of GEI sugar", is incorrect.[20] Millers, who are the contracting party with marketers, bear the commercial risk of the On-Supply Agreements, as detailed in our paragraphs 2.2 and 2.3 of our submission to the Commission dated 28 October 2016.

3.6 MSF Sugar disagrees with the characterisation of On-Supply Agreement negotiations described in paragraph 187 of the Draft Determination. Rather than being a party to the negotiations in a "tripartite" manner, the Canegrowers member was present in the early stages of discussion in which general ground rules were set, not the details of the commercial terms.[21]

3.7 Finally, and while not a factual inaccuracy, we note the Commission's view that the proposed authorisation is likely to result in public benefits through transaction cost savings and facilitating grower inputs into negotiations with millers and marketers.[22]

3.8 We also request the Commission consider the likely effect that the Draft Determination, in authorising information sharing and contract negotiation services by Canegrowers across regions and across different mill owners, would have in importing some contractual terms that are present in isolated Cane Supply Agreements and that are detrimental for efficiency and productivity, into Cane Supply Agreements more broadly. In particular, the authorisation proposed in the Draft Determination may lead to the Applicant being able to negotiate the by-product value inclusion terms that have been detrimental to Mackay Sugar's productivity (as discussed in 2.7 above) into growers' contracts with millers who have been able to fund mill maintenance and keep milling capacity optimised.

Yours sincerely

Mike Barry
Chief Executive Officer

[20] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 171.
[21] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 187.
[22] Application for authorisation (A91558): Draft Determination, Australian Competition and Consumer Commission, 15 December 2016, paragraph 197.