



Competition Policy Unit
Treasury
Langton Cres
Parkes ACT 2600

Dear Sir/Madam,

RE: Mandatory Food and Grocery Code: exposure draft regulations

Thank you for the opportunity to respond to the exposure draft of the proposed Food and Grocery Code.

The Australian Chicken Growers' Council

The Australian Chicken Growers' Council represents the interests of all contracted meat chicken and turkey farmers/growers (the two words are used interchangeably) in Australia. It is a federation of State Farming Organisations or equivalents and was formed in the late 1970s. The current CEO, and many of the current Board have been in the industry for more than 25 years and can readily draw on the expertise of some farming families going back to the formation of the industry in the late 1950's. (Note that duck, spatchcock, quail and other speciality poultry are not considered in this response.)

Meat Poultry Farming in Australia

Almost without exception, meat poultry farmers are substantial contracted asset and service providers. Farmers provide land, power, fuels, labour, bedding (*aka* "litter"), insurance, labour/stockmanship and the processors provide hatchling (1-day old) birds, feed, veterinary services and harvest. Farmers control around 45% of the total industry assets, yet contracts may last as little as 5 years, and all contracts include "instant termination" clauses.

Birds are grown from day-old hatchlings to harvest weight/age in "sheds" – actually highly sophisticated and specialised housing with climate control, automated feeding, lighting, watering, deep bedding as is needed to support the amazingly tuned genetics of these birds that grow naturally to market weight in only around 60 days. Each "shed" can cost up to \$2M to construct new and most farms are valued at or in excess of \$10M each.

Only around 700 farmers produce the entire meat poultry production for Australia – around 360,000,000 birds per year – in order to supply Australian consumers with their current domestic consumption of 50kg/head/year. There is no realistic export market, with only about 3% exported and most of that as cuts not used domestically.

An Agricultural Product Uniquely Placed for Unconscionable Behaviour

More than 70% of meat poultry production is sold fresh or frozen through supermarkets, with smaller percentages going to the restaurant/catering and takeaway sectors. With no export market, meat poultry is uniquely susceptible to bad behaviour by supermarkets, as there is not even an export market "buyer" to take excess stock (as there is, for example in the red meat and some seafood industries).

Moreover, the product is exquisitely perishable, with a fresh chicken meat shelf life of only around a week. Production is continuous because donor flocks lay eggs daily, and production meets

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enormously high specifications – there is no ability to “hold the animals for an extra month” as there is in the red meat sectors. Even a “holdover” of a single day can cause chaos in the poultry supply chain.

Processors are acutely aware of this and even though numerically equal to the supermarkets, are unwilling to negotiate too hard because the potential for commercial loss is so great. As a result, they have become proxies for the supermarkets in negotiations with farmers.

These high specifications also mean that Australia’s meat poultry animal welfare is worlds’ best practice, the quality of the meat is incredibly high and consistent, major food-borne diseases are rigidly controlled and biosecurity requirements are met. However, market thuggery at supermarket level has been passed through the processors down to farmers, many of whom are now trading at or below the cost of production.

Moreover, and perhaps paradoxically to current economic theory, those “modern” farms who have embraced change are in more significant financial stress than the “old” farms with limited to no reinvestment. That is as a result of the operation of the farming contracts and thuggish business behaviour right “down” the supply chain to the farmer.

Market Failure in the Meat Poultry Supply Chain

The proposed mandatory Food and Grocery Code of Conduct has been developed to overcome significant market failure that occurs between Supermarkets and their immediate suppliers.

In the meat poultry industry this is almost invariably the “big 2” processors – Inghams (publicly listed) and Baiada (privately owned). These two processors control more than 75% of supermarket chicken sales including fresh and frozen chicken and secondary processed chicken (eg Nuggets etc) and more than 95% of turkey (fresh, and a minute amount of secondary processed product).

Moreover, these two large processors control more than 90% of all chicken genetics in Australia through restrictive licenses with the major genetics suppliers. Thus they are able to exert effective market control over all minor processors in Australia. In recent times major processors have also taken control of key feedmills and some feed ingredients - and as a result are now reported to be putting commercial pressure on some of the egg production companies who processors believe have tried to “steal” “their” farmers.

The proposed mandatory Food and Grocery Mandatory Code does NOT extend down the supply chain to the farmers, except in the relatively rare situation where a large (usually corporate) farm is supplying to supermarkets directly.

While we expect that the proposed mandatory Code of Conduct will provide some critical countervailing power for the supermarket suppliers, importantly it WILL NOT extend down the supply chain to farmer level. The current unconscionable behaviour between meat poultry processors and farmers will not only continue, but may effectively become hidden as a result.

These behaviours by processors to farmers include but are not limited to :

- “instant” contract termination, reasons sometimes not stated, but often associated with the farmer acting as a negotiator for other farmers, or standing as an office bearer for a farming group, for example,
- inclusion of hidden clauses in contracts by requiring adherence to “manuals” which are not provided until after contract signing for “confidentiality” reasons.

- deliberate or accidental provision of substandard birds, feed, or other inputs which are not the responsibility of the farmer,
 - misrepresentation of what other farmers, or other groups of farmers, have said or done in relation to contracts,
 - threats based around ability to renew contract at the end of the contract period, or not,
 - allegations of “excess mortality”, usually not caused by the farmer’s activity but by age of donor flock, or vaccination changes, or feed changes (all in the sole control of the processor) resulting in thousands of dollars simply being removed from a farmer’s payment,
 - forcing farmers to “compete” in a pool arrangement which takes payments from one farmer and gives them to another based on “efficiency” when the processor has control over the inputs and they vary weekly,
 - requiring farmers to invest in “upgrades” at the will of the processor, some costing \$100,000’s, without scientific evidence and on threat of loss of contract (or loss of renewal of contract),
 - blocking farm sales,
 - dictating a maximum percentage that any one farmer can provide to the total growing group for that processor,
- and so on....

ACCC has been valuable in the provision of class exemptions, but retribution and vilification are a daily reality for meat poultry farmers. Any farmer making a complaint under the ACL is likely to have their contract terminated. Significantly, the value of a meat poultry farm and their ability to get financing is generally contingent on a contract. “No contract” results in bank skittishness; the result is usually a loss of farm business, slashing of farm value, loss of farm and loss of home all at once.

The proposed mandatory Code WILL NOT provide benefit to any farmers or farming groups who are not currently covered by a separate Code of Conduct. Meat poultry farmers will be particularly affected because they do not currently have a Code of Conduct between themselves and the processors as per the Dairy and Horticulture industries. A mandatory Food and Grocery Code will provide some countervailing power to the processors, but will NOT assist those further down the chain. Moreover, if the pressure is “off” the processors because they have a better negotiation position with the supermarkets, they may use that as an excuse to further harass farmers.

Response to Recommendations

Recommendation 1: The Food and Grocery Code of Conduct should be mandatory.

ACGC agrees with this on the basis that an orderly, efficient and competitive market is only as strong as the regulation that underpins it. Relieving the pressure on supermarkets to coerce suppliers in order to feed hungry shareholders might just provide a platform for price transparency and more rational relationships between suppliers and processors.

BUT – unless this strong regulatory activity includes the whole supply chain, there is a real risk that benefits are simply captured at processor level rather than reflecting changed behaviours down the supply chain. To this end the government has enacted mandatory Codes of Conduct in the Dairy and Horticultural sectors – the two other highly perishable produce sectors – but so far refuses to do so for meat poultry even though the concentration in this sector is higher, coercive behaviours far worse and these sectors have more ability to switch to other enterprises.

Meat poultry farmers have requested a mandatory Code of Conduct between farmers and processors ever since the Perishable Agricultural Foods Inquiry recommendations nearly 5 years ago, and in spite of repeated reports and communications supporting a Code, government has not acted.

The meat poultry industry NEEDS a mandatory Code of Conduct to ensure that business behaviour is appropriate through the entire meat poultry supply chain by giving farmers equal countervailing power with processors that this Code is offering processors to supermarkets.

Recommendation 2: All supermarkets, including online supermarkets, that meet an annual Australian revenue threshold of \$5 billion should be subject to the mandatory Code.All suppliers should be protected by the Code.

ACGC would prefer that the threshold was lower than \$2BN, because of the possibility that supermarkets could break up into smaller, related units to avoid a mandatory Code. IF the proposed mandatory Code is only fairly providing a set of rules to govern business behaviour as stated, then there should be no reason why any retailer selling groceries should not follow these rules.

Recommendation 3: The Code should place greater emphasis on addressing the fear of retribution.....

ACGC has read the proposed wording in the exposure draft defining retribution, and on paper it looks to be an excellent rendition. However, those “high up” in the supply chain tend to invent new and clever ways to harass suppliers, and this whole clause should be specifically reviewed at the end of each year’s operation for at least the first 3 years.

Recommendation 4: An anonymous complaints mechanism should be established to enable suppliers and any other market participants to raise issues directly with the ACCC

While the intent of this recommendation is good, it is almost impossible to avoid being identified if there are only one or two suppliers in any category. However, if the ACCC used this anonymous reporting as a mechanism to reschedule “regular reviews” and acted on that basis, it might work.

Recommendation 5: The Code should provide parties with avenues for mediation and arbitration to resolve disputes:

This is a laudable objective, but meat poultry industry farmers have extensive experience in this area because the suggestions for mediation/arbitration as writ in the recommendations are already present in their farming contracts.

These clauses rarely work because:

- the company “up” the supply chain has enough power, and staff lawyers, to delay and obfuscate to such an extent that the complainant is effectively “starved” out and must withdraw the complaint, or
- any party that complains is very unlikely to be offered a new contract at the normal renewal time, or
- it is relatively easy for the part “up” the chain to whisper to the banks that there is a dispute and that contracts might not be renewed.

The current exposure draft refers to valid “commercial reasons” being a reason to be able to terminate a supplier contract without breaching the proposed Code.

ANYTHING can be determined to be a “valid commercial reason” if a company tries hard enough, and “commercial reasons” can change suddenly - resulting in return to *status quo* but with another supplier. That section needs to be removed from the exposure draft.

Recommendation 6: A Code Supervisor (previously the Independent Reviewer) should produce annual reports on disputes and on the results of the confidential supplier surveys, be able to identify systemic issues with the Code and be available to suppliers to provide information on options to resolve disputes and review the processes of Code Mediators.

ACGC agrees.

Recommendation 7: To ensure exceptions are reasonable and transparent:

- ***All exceptions should be subject to a reasonableness requirement that considers the benefits, costs and risks to the supplier and the supermarket, and protects against exceptions that are not in a supplier's interest, with the supermarket bearing the onus of proof that any exception is reasonable; and***
- ***For all new grocery supply agreements, supermarkets should be required to provide suppliers a simple guide to any exceptions that are included in the agreement.***

ACGC agrees in broad terms, but wonders if this has been achieved anywhere in the economy at present; so would like to follow the development of this proposed test with interest as such a reasonableness requirement could have significant potential for other sectors of the supply chain.

Recommendation 8: To address issues relating to fresh produce, the Code should require that:

- ***Grocery supply agreements must include the basis for determining prices;***
- ***All forecasts of required volumes are conducted with due care; and***
- ***Fresh produce standards and specifications must be reasonable.***

ACGC agrees, but suggests that the terms “due care” and “reasonable” be better defined in both activity and time horizon.

Recommendation 9: Maximum penalties for more harmful breaches of the Code should be the greatest of \$10 million, 3 times the benefit gained from the contravening conduct or, where the benefit cannot be determined, 10 per cent of turnover in the preceding 12 months. Maximum penalties for other breaches should be 3,200 penalty units (currently \$1,001,600).

ACGC agrees.

Recommendation 10: The penalty amount for infringement notices for contraventions of the Code should be 600 penalty units (currently \$187,800), an increase from 50 penalty units (currently \$15,650) that otherwise applies for industry codes

This is patently insufficient for supermarket conglomerates with turnover in the \$Tens of Billions. We suggest a higher figure AND notification to the ASX and media including the name of the person



responsible for the infringement, AND a compensatory payment to the supplier so affected (where this is the case).

There must be sufficient incentive for supermarkets not to infringe, given that a single “infringement” can put a supplier out of business.

Recommendation 11: The ACCC, Code Mediators and the Code Supervisor should engage in education and outreach activities to ensure that suppliers are empowered to take advantage of their rights under the Code

ACGC agrees

General Comments on the Exposure Draft

The proposed mandatory Code of Conduct exposure draft in, in general terms, similar to other mandatory Codes of Conduct. However, there is, for the first time, a clear definition of retribution which is warmly welcomed as a first step towards better and more measurable business behaviour.

The issues in practice are likely to be:

- The ability and resourcing of the ACCC to be able to investigate, prosecute and audit. This is an ongoing issue and by no means impugns the ability or willingness of the ACCC, only capacity,
- A need to prosecute relatively quickly and publish these prosecutions widely as a visible disincentive to coercive behaviours,
- Whether suppliers will have the time and cash resources to be able to take their cases to ACCC or the civil courts (retribution or not, strategic legal delays are very damaging commercially),
- Whether suppliers believe that the Code is strong enough to actually provide countervailing power. This is a culture change that will take some little time and a few published cases to shift, potentially.

We strongly suggest at least short-term additional resourcing for the ACCC to engage in both educational and enforcement activity, particularly until the end of the first review period.

Conclusion

ACGC believes that the meat poultry industry must be robust, efficient and productive, and to that end supports a mandatory Food and Grocery Code of Conduct as a way to provide the processors with greater certainty, fairer countervailing power and a reduction in commercially damaging game-playing in the relationship between the processors and the supermarkets.

However, we also believe that same degree of oversight should be present between the processors and the farmers, and to that end we need a mandatory Code of Conduct between processors and farmers to make consistent the rules for the entire meat poultry supply chain. We remain happy to continue to participate in the process and to provide additional information as needed.

Yours Faithfully

(by electronic transmission)

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