




# NSW Farmers' submission to the Review of the Food and Grocery Code of Conduct

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## About NSW Farmers

NSW Farmers is Australia's largest state farming organisation, representing the interests of its farmer members in the state and across all agricultural commodities. We speak up on issues that matter to farmers, whether it's the environment, biosecurity, water, animal welfare, economics, trade, workforce, or rural and regional affairs.

Agriculture is an economic 'engine' industry in New South Wales. Despite having faced extreme weather conditions, pandemic and natural disasters in the past three years, farmers contributed more than \$23 billion in 2021-22, or around 25 per cent of total national production, and positively contributed to the state's total exports. Agriculture is the heartbeat of regional communities, directly employing almost two per cent of the state's workers and supporting roles in processing, manufacturing, retail, and hospitality across regional and metropolitan areas. The sector aims to grow this contribution even further by working toward the target of \$30 billion in economic output by 2030.

Our state's diverse geography and climatic conditions mean a wide variety of crops and livestock can be cultivated here. We represent the interests of farmers from a broad range of commodities – from avocados and tomatoes, apples, bananas and berries, through grains, pulses and lentils to oysters, cattle, dairy, goats, sheep, pigs and chickens.

We have teams working across regional New South Wales and in Sydney to ensure key policies and messages travel from paddock to Parliament. Our regional branch network ensures local voices guide and shape our positions on issues affecting real people in real communities. Our Branch members bring policy ideas, our member Advisory Committees provide specialist, practical advice to decision makers on issues affecting the sector, and our 60-member Executive Council makes the final decision on the policies we advocate on.

As well as advocating for farmers on issues that shape agriculture and regional areas, we provide direct business support and advice to our members. Our workplace relations team has a history of providing tailored, affordable business advice that can save our members thousands of dollars. Meanwhile, we maintain partnerships and alliances with like-minded organisations, universities, government agencies and commercial businesses across Australia. We are also a proud founding member of the National Farmers' Federation.

## Executive Summary

NSW Farmers welcomes the opportunity to provide a submission to the Independent Review of the Food and Grocery Code of Conduct 2023–24, led by the Hon Dr Craig Emerson.

NSW Farmers has serious concerns for the implications of high market concentration in the food and grocery sector. Markets with many producers but few major retailers can lead to market failure in the form of market power. The harm that arises from this can take many forms including producers receiving prices below their marginal cost of production. As such, NSW Farmers has continued to call for reforms to address concentration in the supermarket sector.

NSW Farmers has major concerns about the effectiveness of the current voluntary Food and Grocery Code of Conduct (hereafter, code). The intention of the code is not to address the market concentration of supermarkets but improve the conduct of retailer toward their suppliers in this context. A mandatory code, with the ability for the regulator to seek meaningful and proportionate civil penalties for non-compliance, would drive better behaviour across the sector. The current code does not provide the ACCC with the necessary enforcement tools to protect suppliers against signatories that fail to comply with its requirements and is essential that this is urgently addressed.

To address the harmful impacts of market power imbalances for producers in the food and grocery supply chain, NSW Farmers makes the following recommendations to this review. These recommendations are explored in more detail throughout the submission.

- **Recommendation 1:** That the code recognises and addresses the specific vulnerabilities faced by suppliers who supply perishable goods including agricultural produce.
- **Recommendation 2:** That the code must be made mandatory for all retailers and wholesalers.
- **Recommendation 3:** That the code has the ability to apply significant civil pecuniary penalties when it is breached including necessary enforcement tools for the ACCC to protect suppliers against signatories that fail to comply with its requirements.
- **Recommendation 4:** That the code is amended to ensure a genuinely independent dispute process to resolve supplier complaints.
- **Recommendation 5:** That appropriate enforcement tools must be available to the ACCC to enable issues identified independently to be acted upon.
- **Recommendation 6:** That public reporting of the code provides important accountability and intelligence on supplier relations with code signatories.

## Market Power and Concentration

Australia has a concentrated economy, which is not unusual for developed countries. Most large, concentrated sectors are not any more concentrated in Australia than in other high-income countries. The exception, however, is in supermarkets. As shown in Figure 1 below, concentration in supermarket retailing is higher in Australia than in other high-income countries. The four largest supermarket chains have around 90 per cent of the market in Australia, and nearly 70 per cent is concentrated in just two firms, Coles, and Woolworths.<sup>1</sup> This is much higher than in large, high-income countries such as the US, the UK, France, and Germany, where the four-firm market share is 70 per cent or less. Italy and Spain are even less concentrated.

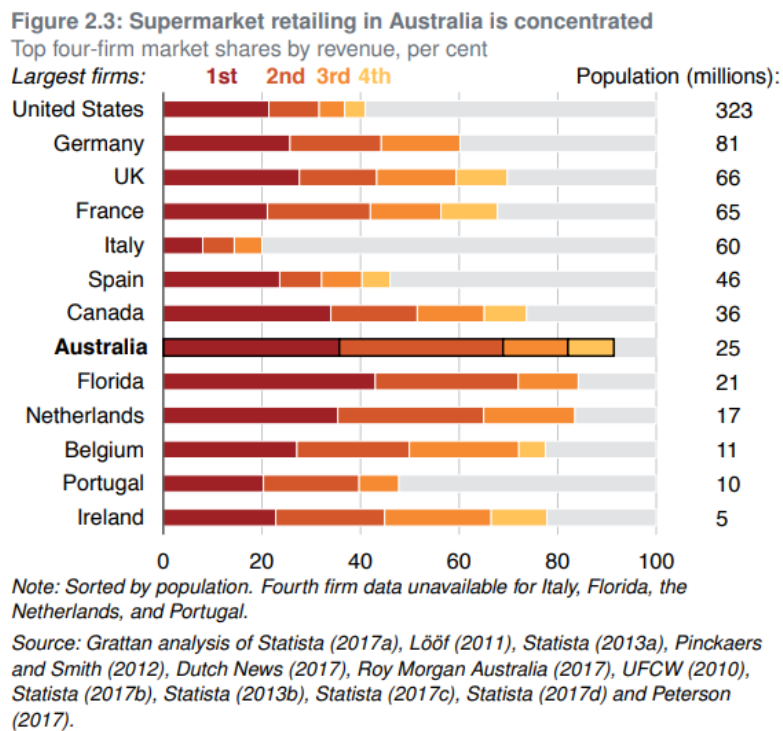


Figure 1: Supermarket retailing in Australia is concentrated.<sup>2</sup>

The current level of market concentration has led to market power, which in turn has led to excessive profits. Market power is a large incentive for firms to invest and innovate, so is not necessarily negative, and can even lead to higher quality goods and services for consumers. However, excessive market power can lead to firms charging higher prices than in a competitive market thus distorting the market, underinvestment, anticompetitive behaviour and barriers to new potentially more innovative firms.

There is evidence of excessive market power in the supermarket sector in the form of supernormal profits. A firm typically seeks to earn profits that exceed the cost of the equity shareholders have invested in it.

<sup>1</sup> Minfie J, 2017. Competition in Australia: Too little of a good thing? The Grattan Institute.

<sup>2</sup> Minfie J, 2017. Competition in Australia: Too little of a good thing? The Grattan Institute.

Supernormal profits are those that exceed the estimated cost of equity and are more than that estimated return required by shareholders.

About 50 per cent of total profits in scale-economy sectors, which includes supermarkets, are above the cost of equity. As shown in the figure below, supermarkets are even at the high end of this group. Supernormal profits account for more than half of total profits in supermarkets, liquor retailing, and wireless telecommunications. This is compared to under 20 per cent of total profits earned in the low-barriers sectors (such as construction, agriculture, and road freight transport) exceed the cost of equity.

On a more granular level, there is also evidence of markups above the cost of production. Over a five-year period, Coles and Woolworths financial accounts show they were able to profit due to increased prices and increased quantities being sold. Gross margins at Coles increased from 24.7% shortly before the pandemic to 26.5% at its most recent disclosure. Margins at Woolworths increased from 29.1% to 30.7%<sup>3</sup>.

The Perishable Agricultural Goods Inquiry conducted by the ACCC sets out many of the instances of market power imbalances across agricultural supply chains and the impacts of these on the agriculture industry and the broader economy. Agricultural markets are characterised by many producers, but few processors and retailers. As an example, Dairy Cattle Farming was identified as the least concentrated industry by ANZSIC Division in 2019. Many products cannot be stored and must be delivered within a short period, which prevents their ability to hold out for better terms and conditions of sale. Both of these market characteristics limit the bargaining power of producers. Another example of bargaining power impacts that NSW Farmers members have raised concerns about is being requested to provide commercially sensitive information, for example financial statements by major retailers that they supply to.

NSW Farmers has continued to call for important competition reforms to address market power imbalances and concentration.<sup>4</sup> NSW Farmers recommended to the Senate Inquiry on Supermarket Prices that: divestiture powers to use of cases of gross market power imbalances against the national interest, such as the supermarkets; stronger mergers and acquisitions framework; incentives for new entrants into the supermarket sector; increased price transparency across the food supply chain; and more powers and funding for the ACCC to undertake enforcement activities to disincentive harmful behaviour.

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<sup>3</sup> The Guardian, 2023. Australia's big supermarkets increases profit margins through pandemic and cost-of-living crisis, analysis reveals, <https://www.theguardian.com/business/2023/may/22/australias-big-supermarkets-increased-profit-margins-through-pandemicand-cost-of-living-crisis-analysis-reveals>

<sup>4</sup> NSW Farmers submission to the Senate Inquiry on Supermarket Prices – February 2024.

## Supplying perishable agricultural goods

Farmers are ‘price takers’, subject to market and climate forces beyond their direct control and long supply chains leave them vulnerable when something goes wrong ‘beyond the farm gate’, for example improper storage or refrigeration. As identified in the ACCC’s Perishable Agricultural Goods Inquiry<sup>5</sup> in 2020, a supplier’s bargaining power is inherently reduced where goods have a very limited window of time for harvest and producers have no ability to delay harvest or delivery.

The high perishability of the agricultural goods that primary producers supply to retailers (for example, fresh fruit, vegetables and meat) places them at a distinct disadvantage compared to their counterparts supplying non-perishable items as they have limited ability to hold out for better terms and conditions of sale, or find an alternate buyer. Due to the perishability and volume of goods that the supplier needs to sell, bargaining power and willingness to pursue a complaint are impacted by concerns about future commercial dealings and limited flexibility to delay sales or find a more competitive buyer. The risk of a negative commercial outcome by raising a complaint is perceived to outweigh the potential gain from pursuing a complaint with only a small possibility of succeeding where agricultural goods have a limited shelf life for which they can be harvested and/or sold. In most cases the producer will have more produce in the pipeline with limited delivery and/or harvest windows, requiring them to consider the potential financial implications of a dispute versus loss of future deliveries. This is particularly pertinent for suppliers of perishable goods (for example, fruit and vegetables) which have a limited shelf life and require refrigeration.

Data from the Independent Reviewer’s 2022-23 annual supplier survey indicates notable issues for suppliers and in some cases clear differences by product category. These highlight particularly negative experiences for suppliers of agricultural goods. For example, a significantly higher percentage of fruit/vegetable suppliers reported that they were treated unreasonably either frequently or at times (Figure 2). Another example is, that on raising an issue with the wholesale/buying team, 100 per cent of fruit/vegetable suppliers reported that they did not consider their issues satisfactorily assessed. The results from this annual report indicate that there are significant challenges for suppliers of fruit/vegetable, and in some cases meat/meat products.

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<sup>5</sup> ACCC, 2020. Perishable agricultural goods inquiry – November 2020.

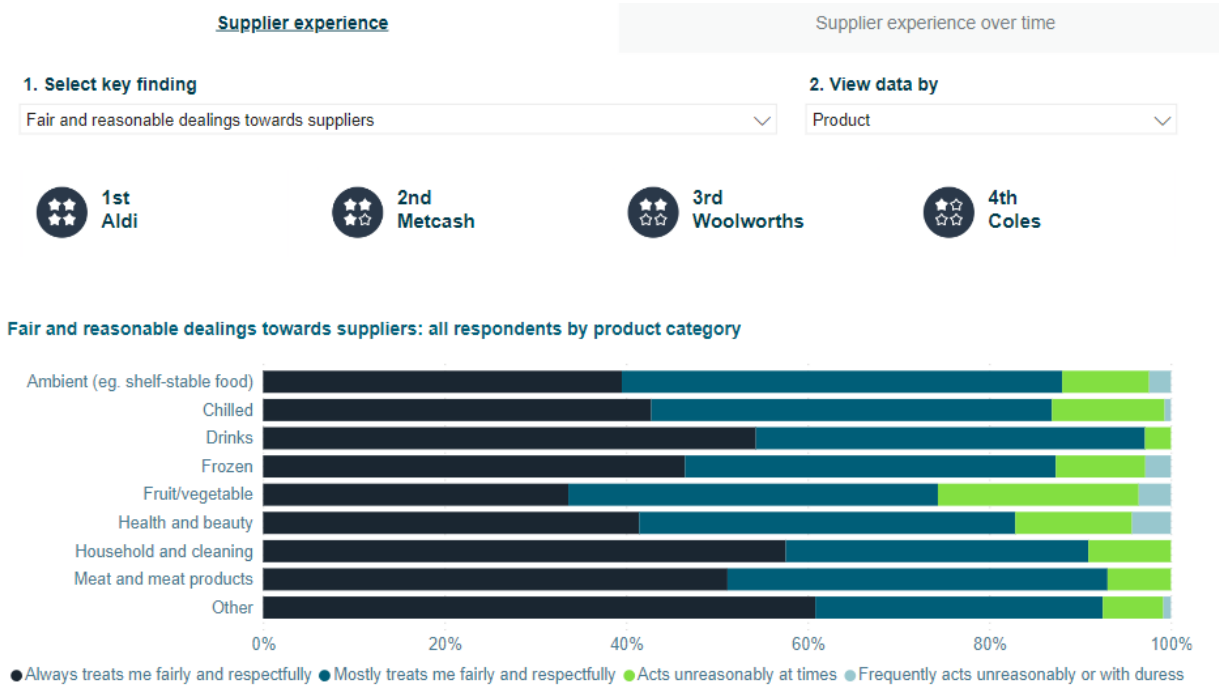


Figure 2: 2022-23 Annual Report – Fair and reasonable dealings towards suppliers all respondents by product category.<sup>6</sup>

**Recommendation:** That the code recognises and addresses the specific vulnerabilities faced by suppliers who supply perishable goods including agricultural produce.

<sup>6</sup> Food and Grocery Code Independent Reviewer, 2023. 2022-23 Annual Report – Fair and reasonable dealings towards suppliers: all respondents by product category.



## Mandatory Code

### Penalties and enforcement

The current voluntary code without penalties for non-compliance inhibits compliance and effective dispute resolutions. Pecuniary penalties, such as those within the Horticulture and Dairy Codes, should be introduced to provide more confidence to suppliers in the objectives of the Code. As it currently stands, the code does not provide the ACCC with the necessary enforcement tools to protect suppliers against signatories that fail to comply with its requirements.

It is well understood penalties that are insignificant in terms of the benefit accrued from the prohibited behaviour or relative to the turnover of the business do not act as a deterrent and are instead viewed as a cost of doing business. For this reason, in 2022 maximum penalties for breaches of certain provisions of the Competition and Consumer Act including the Australian Consumer Law increased five-fold, to the greater of \$50 million or three times the value derived from the relevant breach, or, if the value derived from the breach cannot be determined, 30 per cent of the company's turnover during the period it engaged in the conduct.

The Food and Grocery Code of Conduct is intended to be a primary safeguard to protect supermarket suppliers from unscrupulous practices, however it contains no provision for imposing penalties where the code is breached. This is dissimilar to other industry codes where the ACCC has enforcement powers including the ability to seek penalties to address breaches. NSW Farmers recommends that the Food and Grocery Code should be updated to include significant civil pecuniary penalties and infringement notices for contraventions such as those within the Horticulture and Dairy Codes.

#### Comparison to other industry codes:

- The Horticulture Code of Conduct is a mandatory industry code that applies to the relationship between a grower and a trader (agent or merchant) of horticulture produce which aims to improve clarity and transparency of trade between growers and traders. The code requires all trade in horticultural produce to have a horticulture produce agreement, and failure of growers and traders to deal in good faith can lead to penalties. Breaching the Horticulture Code of Conduct can have serious consequences, including penalties and other enforcement action. Horticulture growers who sell to a trader are governed by the mandatory Horticulture Code, in contrast to those who sell directly to a supermarket which are governed by the voluntary Food and Grocery Code. In practice this means that growers who sell fruit and vegetables directly to a supermarket have less protections and price information than when supplying traders (i.e. wholesalers). The requirements and minimum standards for trade between horticultural growers and supermarkets must be equivalent to those standards set for growers and traders under the Horticulture Code.
- The Dairy Code of Conduct aims to promote fair trading in the dairy industry by imposing minimum standards of conduct on farmers and processors. Under the code all raw milk must be bought from dairy farmers under a milk supply agreement that complies with the code. This code (not the Food and Grocery Code) applies to retailers, such as supermarkets, to the extent that they buy milk

directly from farmers. The ACCC is responsible for enforcing the code and may seek civil penalties to address a breach of the code.

**Recommendation:** That the code has the ability to apply significant civil pecuniary penalties when it is breached including necessary enforcement tools for the ACCC to protect suppliers against signatories that fail to comply with its requirements.

## Code Arbiters

NSW Farmers considers that the current process under the code does not provide an effective, fair or equitable means for resolving supplier complaints. The small number of complaints escalated through the code arbiters is concerning and consistent with the perception that producers lack confidence in the process resulting in a beneficial outcome to warrant escalating a complaint. The perishability of a supplier's goods such as agricultural produce further impacts their willingness to pursue a complaint with concerns about damaging future commercial dealings cited as a common barrier to pursuing. A genuinely independent process is needed that is underpinned by a level playing field, trust and stronger supplier awareness.

NSW Farmers is supportive in-principle of a genuinely independent dispute process to assist in resolving individual complaints, as outlined previous submissions<sup>8</sup>. However, the current functions of the Code Arbiters do not in practice support genuinely independent consideration of complaints from suppliers. The two main reasons for this are that they create confusion and they do not remove suppliers' concerns of retribution.

NSW Farmers has major concerns about the true independence in the existing dispute resolution process due to code arbiter's alignment with each retailer, which means market power imbalances persist in the dispute process. The perceived independence of the code arbiters is problematic given they are appointed by individual code signatories. This results in a reluctance to raise disputes due to fear of retribution by retailers. The Food and Grocery Code needs to provide a genuinely independent dispute resolution process, so that suppliers are not deterred from using it because of concerns over confidentiality, bias, or commercial retaliation by retailers or wholesalers.<sup>9</sup>

The number of complaints reported to the code arbiters is unusually low with only three reported in 2020-21 FY, two in 2021-22 FY, zero in 2022-23 and complaints only received for one code signatory. Consultation with NSW Farmers members has highlighted that the low number of complaints is not indicative of positive behavioural changes nor generally low numbers of disputes between suppliers and Code signatories. Issues raised include the fear of retribution, complexity of the code and low awareness of dispute resolution avenues available as the major reasons why there have been so few disputes go through Code Arbiters.

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<sup>8</sup> NSW Farmers, 2018. Response to Draft Report Independent Review of the Food and Grocery Code of Conduct.

<sup>9</sup> NSW Farmers submission to Review of the Dispute Resolution Provisions in the Food and Grocery Code – February 2023.

The specific vulnerabilities of supplying perishable agricultural goods also need to be considered (as compared to non-perishable goods) for example an appropriate timeline. Where a complaint is raised, the code arbiter has up to 20 business days to close an investigation and a further 5 business days to provide written notice to the supplier of their decision. In perishable agricultural good supply chains, there is limited flexibility to hold or stockpile goods for up to 25 business days. Complaints handling needs to be agile to reflect the pressures of suppliers in selling their agricultural goods which often have high perishability.

One advantage of the code which should be maintained is the confidentiality protections which were enhanced in 2020. Initiatives such as this which protect suppliers should be the main focus of any chosen dispute resolution mechanism, recognising that they are already at a disadvantage in dealings with retailers and this situation should be avoided in dispute resolution.

NSW Farmers favours the more flexible, impartial, and independent dispute resolution processes in mandatory codes such as the Horticulture Code. The Horticulture Code allows growers and traders to prescribe and agree on a dispute resolution process in their horticulture produce agreement, or choose the procedure described in the code. The procedure prescribed in the code must be resolved in three weeks, otherwise mediation is then used. The mediation process in the Horticulture Code provides a better avenue than the code arbiters, as it includes an independent mediator who is unaligned to either party. Genuine attempts to resolve the dispute must be made, otherwise penalties apply and a time limit of 30 days applies. These conditions make it more likely that complaints are considered in an independent manner and reaches consistent outcomes.

**Recommendation:** That the code is amended to ensure a genuinely independent dispute process to resolve supplier complaints.

## Independent Reviewer

Under the current code, a lack of powers is available to the ACCC and Independent Reviewer to enforce the code and handle disputes. In the absence of a truly independent dispute resolution process, the role of the Independent Review is essential to provide a level of oversight to how the arbiters and signatories deal with complaints. Code arbiters currently have too much power with the result being that power imbalances that already exist in the market are carried through to the dispute resolution process. This power should be shifted to the Independent Reviewer and ACCC.

Independent Reviewer is constrained by a number of restrictions to their role regarding dispute resolutions. Firstly, they should be able to make recommendations directly to retailers, rather than only to code arbiters. Secondly, the ACCC needs to have the appropriate enforcement abilities including penalties and infringement notices to act on issues when identified by the Independent Reviewer. This would better realise the Independent Reviewer's existing powers to refer potential contraventions of the code to the ACCC where it becomes aware through its own processes.

Another example is that the process of the Independent Reviewer is too long which hinders and effective role in dispute resolution. For example, the Independent Reviewer received a request from a supplier to review a decision by the Coles Arbiter which followed the following timeline:

- Commenced on 21 September with the Independent Reviewer notifying Coles that they were conducting a review,
- Coles provided documents on 7 October,
- The Independent Reviewer provided their final decision on 27 October,
- And then on the 9 November, the Code Arbiter responded that they rejected all recommendations.

In total, this process took 49 days, post the time already taken for the Code Arbiter to reach their initial decision. Further, the Independent Reviewer’s decision was disregarded. This creates significant uncertainty for suppliers, eroding their confidence and trust in the process.

The Independent Reviewer’s annual supplier survey and report has provided valuable intelligence regarding the effectiveness of the code. This can also support greater competition in a relatively non-competitive environment by allowing suppliers to compare the performance of retailers. Public reporting of retailer’s performance and suppliers’ sentiment through this survey and report is a useful and important exercise. These reports have provided useful information that reflects dissatisfactory experiences of suppliers and harmful behaviour by the code signatories, particularly in regard to agricultural supplier. The addition of reporting of results by product category in the 2022-23 has allowed for greater visibility of varied supplier experiences between sectors and areas to target improvements. For example, fruit/vegetable suppliers were significantly overrepresented in reports of being treated unreasonably through dealings.<sup>10</sup> However, consultation with NSW Farmers members has identified that suppliers are often unaware of the survey and associated public reporting. This suggests that barriers to overcome limitations the consistently low response rates to the survey need to be considered, for example timing, promotion and perceptions of confidentiality.

Despite this limitation, in the context of accountability and effectiveness of the code, the annual supplier survey and report undertaken by the Independent Reviewer has provided valuable public reporting and intelligence on supplier relations with code signatories.

**Recommendation:** That appropriate enforcement tools must be available to the ACCC to enable issues identified independently to be acted upon.

**Recommendation:** That public reporting of the code provides important accountability and intelligence on supplier relations with code signatories.

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<sup>10</sup> Food and Grocery Code Independent Reviewer, 2023. 2022-23 Annual Report – Interactive Dashboard.