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Response to

Review of the Food and Grocery Code of Conduct

Interim Report

3 May 2024

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Contents

Introduction

1. eastAUSmilk is the voice of dairy farmers in New South Wales and Queensland. It was formed from the amalgamation of Dairy Connect in New South Wales, and Queensland Dairyfarmers' Organisation.
2. We thank you for the opportunity to provide a response to the Interim Report of the 2023-24 Review of the Food and Grocery Code of Conduct, and apologise that our response is slightly late.
3. Generally, we don't propose to repeat any of the content of our initial submission to the Review.

In Summary

4. eastAUSmilk urges that the Review support incorporation of the proposals set out in this submission, in the final report.

Things Which Don't Fit

5. We have chosen to address our response to the interim report chapter by chapter, but have found no comments we need to make in relation to several of the chapters.
6. Where we are not making a comment on any particular chapter, it can be presumed we are comfortable with the discussion, findings, and recommendations, arising in that chapter.
7. We want to raise several issues which don't fit well under the Interim's Report Chapter headings.
8. Later in the submission we address those items which we think will do not fit we ll under the chapter headings.

Interim Report Recommendations

9. Congratulations on the Interim Report.
10. We are very pleased to see your powerful focus on a mandatory code, and addressing the issue of retribution.
11. We believe that adoption of the points we make below will significantly improve the outcomes for the industry beyond the improvements proposed by the review in the initial set of recommendations in the Interim Report.

Chapter 3: Why the Code should be made mandatory

12. We reject the proposition that a voluntary code is more likely to create a positive culture of compliance and collaboration. Such a proposition is completely at odds with the evidence and the facts. The current code is voluntary, and no such culture is evidenced.

13. We reject the proposition that making the code mandatory will increase administrative and compliance costs, and risk unintended consequences. Replacing the current toxic culture with improved relations between supermarkets and suppliers will be so overwhelmingly beneficial to the industry that any additional administrative and compliance costs will be overtaken. In addition, many of the terms of a mandatory Food and Grocery Code will be in exactly the same terms as they operate in the dairy industry code, and we have had sufficient experience with the dairy industry code to be able to identify where there are or are not unintended consequences.

14. The Code must not be weakened as it is made mandatory.

15. There is a great deal of similarity between the Food and Grocery Code and the Dairy Industry Code.

16. While eastAUSmilk are seeking changes to improve the operation of the Dairy Industry Code, the contents of the code are demonstrably workable.

17. Indeed, Coles at least is already bound by the terms of the Dairy Industry Code.

18. The large supermarkets have signed up to the provisions of the Food and Grocery Code as a voluntary Code – how can this provisions not work when mandatory? It all would be simply ridiculous to assert will that provisions which work in a voluntary code will not work if mandatory.

Chapter 4: To whom should the mandatory Code apply?

19. The existence of the Dairy Industry Code is not a reason to not extend the Food and Grocery Code further down the supply chain, as we understand has been proposed by others.
20. A line by line comparison of the two codes will make clear that there are many elements of the two codes which are congruent and not in conflict.
21. We assert and know that it would be simple to draft a revised Food and Grocery Code which is not in conflict with the dairy code.

Chapter 5: Fear of retribution

22. We and many others in the community have been appalled at the statements by the big supermarkets rejecting the proposition that there is a problem with retaliation and retribution, which derives from the behaviour of big supermarkets and their staff.
23. As we predicted in our initial submission the major supermarkets have said they have code of conduct and ethical principles which rule out such behaviour. They have been prepared to assert this in absolute defiance of the findings in the interim report.
24. We believe this bodes very badly for their fulsome and wholehearted implementation of whatever are the final recommendations of this review, in relation to addressing the retribution issue.
25. There can be no doubt that retribution behaviour is driven not only by inappropriate incentives and policies within the supermarkets, but also by a culture which denies there is anything wrong with what is being done.
26. This is not simply a problem at the top nor simply a problem at the bottom – it is a problem which needs to be addressed throughout each of the major supermarkets. The bullying and retaliation which is set out in the interim report, and in the media, is clearly not being done on the ground in our towns and cities by the senior most management of each supermarket. Whatever the solution, it must reach down far enough to change the way supermarket staff do their jobs – the buyers and category managers.
27. The denial by senior management that there is such a problem indicates that whatever the solution must reach up far enough to ensure there is no expectation by anyone management levels behaviour will be tolerated, implicitly or explicitly.
28. That culture will not change unless the supermarkets make a commitment to change it, throughout each organisation. Cultural change of that nature will not happen without a commitment and a plan and a program, and responsibility for change and outcomes on the senior most management.
29. Any expert in change management or culture change will confirm that it normally requires an enormous effort, led with commitment from the top and implemented below, to see a significant change in the culture of a large organisation, particularly where the culture requiring change has previously been thoroughly embedded and has longevity.
30. In our original submission we proposed a package of measures which could be considered a best practice approach to the elimination of retaliation and bullying behaviour, across the whole organisation.
31. While that package we proposed might not be suitable for every supermarket bound by the code (though we think, self-evidently, it is) we believe the review and code must provide concrete guidance to the big supermarkets about the nature of the change they are expected to deploy.
    a. We note that in the interim report, chapter 9 identifies the need for systems and processes to ensure compliance, staff training and appropriate reporting. This is

a strong endorsement of the proposition that supermarkets must have a proper process in place in order to change the retaliation culture.

32. We propose that the review should recommend an advisory appendix to the code, if it is premature to make it mandatory, and that appendix would address the range of measures we proposed in our initial submission.

33. Noting the comments in chapter 3 of the interim report, calling for the revised code to capture as much adverse conduct as possible, we believe it would be of enormous assistance to the participants in the industry for the code to also include as comprehensive as possible a list of examples of retaliatory behaviour which are prohibited, perhaps as an appendix to the code.

34. We also believe it will be important to make clear to the parties bound by the code that vicarious liability applies to companies, where employees are found to have breached this component of the code.

35. We see the elimination of retaliatory behaviour as a necessary precondition to the effective improvement of the market and competition in the food and grocery sector. If the approach is too light handed, or presumes too much competence for good faith, it risks not making the kind of change necessary, and not improving the industry to the point where it should be. The changes to this behaviour are a gateway to a better industry – don't leave that gateway half closed.

Chapter 6: Dispute resolution under a mandatory Code

36. The dispute resolution processes under the Dairy Industry Code are not well tested, and caution needs to be exercised in asserting that it is entirely appropriate to import those processes elsewhere.
37. It must also be noted that the dispute resolution processes in the Dairy Industry Code are designed to operate between farmers and milk processors, and that is a very significantly different dynamic than what lies between suppliers and supermarkets.
38. We are also concerned at the continuation of the proposition that there should only be external scrutiny and monitoring of dispute resolution processes in the food and grocery sector, where requested. We believe the prospect of better relations between suppliers and supermarkets are sufficiently untested, that such a hands-off approach is not appropriate until after revised dispute resolution processes have been in place and properly tested over several years.
39. Rather, all use of dispute resolution processes, at least for a period of time should be reported and monitored externally and independently.

Chapter 8: Issues specific to fresh produce

40. One issue which might have been identified in this chapter, but which was not, is that the perishable nature of fresh produce, and the short timeframe before the produce becomes unsaleable, makes it essential that dispute resolution processes are exceptionally quick; otherwise produce is sitting on a dock somewhere, possibly air-conditioned or possibly not, and perishing.
41. The short shelf-life of fresh produce means the bargaining power of the supermarket is significantly stronger than for those products which can be stored by the supplier when unsold.
42. We believe this makes it important in relation to perishable goods is not resolved quickly it is automatically deemed resolved in favour of the supplier.

Chapter 9: Enforcement and penalties

43. We absolutely endorse the extension of penalties to non-compliance with dispute resolution provisions.
44. Just as has been the case with the whole of the code, failing to make individual components of a revised code subject to enforcement, will guarantee they fall by the wayside, and the same logic to making the whole code mandatory and imposing bounties applies just as much to dispute resolution processes as to other parts.

Supply Chain Prices and Margins

45. While we are concerned about the lack of focus on monitoring of prices and margins in the Interim Report, we aren't about to repeat what we said our initial submission about the monitoring of supply chain margins.
46. We note your references interim report to the purchase of monitoring services by the Commonwealth from CHOICE.
47. It may be that the monitoring services provided by CHOICE are sufficient to allow the kind of transparency necessary for the community and industry to have confidence that margins are not being inflated, but we are not this point confident of that.
48. Our principal reason for lacking confidence in this monitoring system is the absence of reporting of farm gate prices.
49. All large suppliers to the major supermarkets are presumed to have reasonably efficient recording and processing systems in place, and would be well-positioned to report farm gate prices, which would allow consumers, the community, and government to assess the difference between and what farmers are paid.
50. We believe an essential component of confidence in the fairness and efficiency of the system is good data about farm gate prices, and we believe this burden can quite reasonably and fairly be imposed on suppliers bound by the Food and Grocery Code.
51. At the very least we request that this issue be placed on a reserve list to be revisited when the Code is next reviewed.
52. A further issue arises from the practice of major supermarkets of manipulating the margins of their plain label products, so they can compete unfairly with the branded products they stock. They impose a much lower margin on their plain-label products and a much higher margin on branded products, resulting in much higher sales of plain label retail brands vs. branded processor brands.
53. If the supermarket shelf prices of all milk carried the same retail margin, the price of plain label milk would be higher and the price of branded milk would be much lower. This would lead to higher sales for branded milk and lower sales of the supermarkets' plain label milk.
54. Milk processor margins on plain-label products are forced very low by supermarkets before they will award processing contracts, and on branded products are higher, being more reflective of production costs and a margin.
55. Making the margins of branded and plain label milk products more similar to one another would make milk processing more profitable, which should improve farmgate prices and farm incomes.
56. On average, we believe retail milk prices would not change, or more likely would come down, once supermarkets reduce the exorbitant margins they impose on branded milk products.

57. Better profitability for dairy farms would begin to address the decline in the Australian milk pool and dairy farm numbers, identified by the Report of the House of Representatives Standing Committee on Agriculture Inquiry into Food Security in Australia.
58. At the very least we request that this issue be placed on a reserve list to be revisited when the Code is next reviewed.

National vs. Regional Pricing

59. We believe the policy of major supermarkets bound by this code, of applying a national price to almost all products in store, has a significant and negative impact on competition.
60. We do not believe the impact of this policy is well understood amongst researchers or policymakers.
61. The comments below are informed by our discussions with suppliers to supermarkets, and while it principally reflects our understanding of the dairy industry, in some respects is fully applicable to other product lines supermarkets.
62. Major supermarkets apply a policy of uniform pricing regardless of location.
63. This inevitably means that for some products, the shelf price produces a lower margin for the supermarket than in other locations, because of the additional cost of getting that product onto those particular shelves.
64. In some locations, additional transport costs are so high that the supermarket prefers to not stock particular products, because the margin is too low or below zero.
65. In such high-cost regions, national pricing makes it unprofitable for processors to supply products to retailers. This is the case for milk in some parts of Queensland and especially in north Queensland.
66. Processors are forced to supply milk at a price which enables retailers to make a margin in high-cost regions. This has meant processors supplying at a lower price than is profitable in a high-cost region, or processors accepting a lower price in low-cost regions and cross subsidising between regions. Either way, national pricing forces processors to make less than commercial margins overall for their business.
67. The low price for plain-label milk in high-cost regions also blocks processors from setting the price of their own brands of milk at a profitable level.
68. This national pricing policy forces insufficient milk production in some high-cost regions and availability for consumers is affected, with from time to time no milk on shelves. This shortage of milk is already occurring in north Queensland and will became significantly more widespread in the future unless something is done.
69. It should be noted that transporting milk into north Queensland is more expensive than local supply. Bega currently transports milk from Victoria to Malanda which is around 3000km and the landed cost into Malanda is well above locally sourced milk.
70. It is important to note that this pattern of seasonal or permanent reduction in margin is a policy choice open to supermarkets, one they have clearly been prepared to live with in some locations, and possibly their only option while they adhere to a policy of national pricing.
71. If they can accept lower margins in some locations, they could accept them more broadly.

72. Because of calving and other dairying cycles, February/March is, nationally, a seasonal low production period, and processors seeking milk to make up their volumes create unusually high demand. This forces milk to its highest price, and it is during this time that processors and supermarkets between them determine to import less milk into Queensland than the market wants, and there are shelves empty of milk.

73. Abandoning national pricing for selected commodities such as milk would enable price reductions for milk at some times and in some locations.

    a. It would also mean higher milk prices at times as well, reflecting supply and demand for milk in that region.

74. Where supermarkets insist on a national pricing policy for products with significantly variable price-to-shelf, the margins they are currently setting for such products must, mathematically, provide windfall profit at times of low cost-to-shelf, while providing a lower profit at times of high cost-to-shelf.

    a. That is, if the national price is set so a profit can be made when milk is expensive for processors and supermarkets to buy, the margin they are making when milk prices are low must be high.

    b. Abandoning national pricing for such products could see a significant price cut in regions when the cost of getting to the shelf are lower.

75. We believe that it is the national pricing policy of big supermarkets which keeps their competitors out of high cost regions.

76. We accept that it is possible that the review might be insufficiently moved by our comments above to be sufficiently confident of their factual grounds to address this issue comprehensively in the final report, but would strongly urge that the final report, at least, recommend a comprehensive evaluation by an appropriate research entity into the of the impact on competition and market dynamics of the national pricing policy of the big supermarkets.