



# Codifying Supermarket-Supplier Relations

## A Report on Australia's Food and Grocery Code of Conduct

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## Abbreviations

ABR	The Australian Business Review
AC	Companion of the Order of Australia
Agricultural Competitiveness White Paper	Commonwealth of Australia 2015, <i>Agricultural Competitiveness White Paper: Stronger farmers stronger economy</i>
ACCC	Australian Competition and Consumer Commission
ACCC 2008 Grocery Inquiry	ACCC (2008) <i>Report of the ACCC Inquiry into the Competitiveness of Retail Prices for Standard Groceries</i>
ACCI	Australian Chamber of Commerce and Industry
ACL	Australian Consumer Law
ACT	Australian Capital Territory
ADF	Australian Dairy Farmers
AFGC	Australian Food and Grocery Council
AFR	Australian Financial Review
AIDC	Australian Industry Dairy Corporation
ADR	Alternative dispute resolution
Agriculture White Paper, 2015	Commonwealth of Australia 2015, <i>Agricultural Competitiveness White Paper: Stronger farmers stronger economy</i>
AMWU	Australian Manufacturing Workers Union
ARC	Active Retail Collaboration
AO	Officer of the Order of Australia
BCA	Business Council of Australia
CAANZ-ACL review interim report, 2016	Consumer Affairs Australia New Zealand, Australian Consumer Law Review Interim Report, October 2016
CEO	Chief Executive Officer
CC	Competition Commission (UK)
CC 2008 Report	Competition Commission Report (30 April 2008), <i>The supply of groceries in the UK market investigation</i> (UK)
CCA	<i>Competition and Consumer Act 2010</i> (Cth)
CCO	Code Compliance Officer (UK)
CMA	Competition & Markets Authority (UK)
CCM	Code Compliance Manager
COSBOA	Council of Small Business Australia
DSAP	Dairy Structural Adjustment Program
Explanatory Statement, FGC Regulation, 2015	Explanatory Statement, <i>Competition and Consumer Act 2010 Competition and Consumer (Industry Codes—Food and Grocery) Regulation 2015</i>
FGCC	Food and Grocery Code of Conduct
FMCG	Fast moving consumer goods
GCA	Grocery Code Adjudicator (UK)
GFC	Global Financial Crisis
Groceries Market Investigation Order 2009	The Groceries(Supply Chain Practices) Market Investigation Order 2009, UK
GSA	Grocery Supply Agreement
GSCOP	Groceries Supply Code of Practice (UK)
Harper Review	Ian Harper et al (2015) <i>Competition Policy Review</i> (Commonwealth of Australia)
HCC	Horticulture Code of Conduct
HMA	Horticulture Mediation Adviser
HOR, <i>Farm Gate to Plate and Horticultural Code Bills</i> , 2011.	The Parliament of the Commonwealth of Australia <i>Advisory Report on the Constitutional Corporations (Farm Gate to Plate) Bill 2011 and Competition and Consumer Amendment (Horticultural Code of Conduct) Bill 2011</i> , House of Representatives Standing Committee on Agriculture, Resources, Fisheries and Forestry, March 2012
IGA	Independent Grocers of Australia
SERC, <i>Impacts of supermarket pricing on the dairy industry</i> , 2011.	Senate Economics References Committee, <i>The impacts of supermarket pricing decisions on the dairy industry</i> , 2011
IP	Intellectual property
ITV	Independent Television
MGA	Master Grocers Australia Independent Retailers
SERC, <i>Milking it for all its worth</i> , 2010	Senate Economics References Committee Report, <i>Milking it for all it's worth — competition and pricing in the Australian dairy industry</i> , May 2010
MP	Member of Parliament
MSC	Major supermarket chain (in this Report, MSCs refers to Coles and Woolworths)

NCC Dairy – Now and Then, 2004	National Competition Council 2004, <i>NCC Occasional Series: Dairy - Now and Then: The Australian Dairy Industry Since Deregulation</i> , AusInfo, Canberra
NCP	National Competition Policy
NFF	National Farmers' Federation
NFP	National Food Plan
NFP issues paper, 2011	DAFF 2011, <i>Issues paper to inform development of a national food plan</i> , Department of Agriculture, Fisheries and Forestry, Canberra
OASBC	The Office of the Australian Small Business Commissioner
OBPR	Office of Best Practice Regulation
OFT	Office of Fair Trading (UK)
Osegowitsch and Goelz	Tom Osegowitsch and Markus Goelz, University of Melbourne case study, <i>Aldi in Australia</i> , October 2011
PC	Productivity Commission
PC, <i>Consumer Law</i> , Final Report 2017	Productivity Commission, Consumer Law Enforcement and Administration, Final Report, March 2017
PGCC	Produce and Grocery Industry Code of Conduct
RIS	Regulatory Impact Statement
RSR	Retail-Supplier Roundtable
SBDC	Small Business Development Corporation of WA
SBFE	Small Business and Family Enterprise (Ombudsman)
SCOP	Supermarkets Code of Practice (UK)
SDATA	Shop, Distributive and Allied Employees Association
SELC, <i>FGC Regulation</i> , 2015	Senate Economics Legislation Committee, <i>Competition and Consumer Act 2010 - Competition and Consumer (Industry Codes – Food and Grocery) Regulation</i> , Report, 2015
SME	Small and medium-sized enterprise
SSC, <i>Australia's Food Processing Sector</i> , 2012	Senate Select Committee, <i>Inquiry into Australia's food processing sector</i> , August 2012
SMH	Sydney Morning Herald
TFGA	Tasmanian Farmers & Graziers Association
TPA	<i>Trade Practices Act 1974</i> (Cth)
Treasury, FGCC consultation paper, 2014	Treasury, <i>Improving Commercial Relationships in the Food and Grocery Sector</i> consultation paper, August 2014
Treasury, FGCC Final Assessment RIS, 2014	Treasury, <i>Improving Commercial Relationships in the Food and Grocery Sector</i> Final Assessment RIS, November 2014
UK	United Kingdom
VFF	Victorian Farmers Federation

## Executive summary

This report documents the analysis and findings of research relating to the Food and Grocery Code of Conduct (FGCC), introduced by way of regulation in 2015 with the general aim of improving relations between retailers and wholesalers and their suppliers in the Australian grocery sector. The report is accurate and reflects developments as at 1 September 2017.

Funded by an Australian Research Council grant, the research was conducted over a period of two years and involved review of an extensive documentary record and more than 70 in-depth interviews with a wide range of stakeholders across industry, government and civic society.

Two of the key questions guiding the research were as follows:

- What were the problems to which the FGCC was responding and why and how was the FGCC responsive to or seen as likely to address them?
- To what extent has the FGCC been effective to date or is it likely to be effective in the future in addressing such problems?

A summary of the research analysis and findings in relation to each of these questions is set out below.

### Problems

1. The problems to which the FGCC was responsive fall into four broad categories:
  - an economic problem of market structure and conduct;
  - a socio-cultural problem of business culture and behaviour;
  - a political problem of farmer struggles and public sympathies;
  - a systems problem of legal rules and litigious avenues.
2. These problems are not mutually exclusive and in some respects are inter-related. In some cases the problem was clearly and publicly articulated and the FGCC was presented as directly responsive to it. In others, the articulation was not as clear, was often not publicly articulated and nor was it necessarily seen as a problem that the FGCC may be able to address fully if at all, even it was influential as an impetus for the action taken to introduce the Code.
3. Views on whether the issues as set out here were or are problems as such, the degree to which they were or are likely to continue to be problematic and the appropriateness or likely effectiveness of the FGCC to address them vary considerably between stakeholders. This research has sought to capture this diversity of perspectives as well as bring an independent and objective frame of reference to the issues at hand.

4. The analysis in this report does not purport to uncover or canvas the forces or factors that gave rise to the problems in question. A causal analysis of this kind would necessitate a much broader inquiry that would involve a historical as well as more of a sociological perspective, neither of which are within the scope of this report, but are reflected in other aspects of the [Supermarket Power project](#) of which this research relating to the FGCC is part.
5. The report includes comparisons with the experience in the United Kingdom (UK) based on review of the documentary record as well as interviews with stakeholders in that jurisdiction. While similar issues and debates relating to supermarkets exist around the world, the UK is particularly relevant in the Australian context as it has had a mandatory code of conduct in place since 2010 (the Groceries Supply Code of Practice (GSCOP)), which replaced a voluntary code introduced in 2002, and a dedicated statutory officer (the Grocery Code Adjudicator (GCA)) to enforce it since 2013. The design and experience in implementation of the UK regime was influential in Australian developments.

### **An economic problem of market structure and conduct**

6. At its root, the economic problem to which the FGCC was seen to respond arises in the structure of retail grocery markets in Australia, specifically the high level of concentration and the combined market share across a substantial number of product categories of the major supermarket chains (MSCs), Coles and Woolworths.
7. In the lead up to an inquiry into grocery prices by the Australian Competition and Consumer Commission (ACCC) in 2008 (ACCC Grocery Inquiry), this was viewed as a problem principally for horizontal competition and associated detriment for consumers, predominantly by way of high prices. However, in the ACCC's judgement, notwithstanding the concentration, competition was still 'workable'. That view was echoed in the findings of an independent review (Harper Review) in 2015 consistent with the fact that, in the intervening years between the two inquiries, competition intensified and indeed has continued in that vein following the Review and is likely to continue to do so in the future.
8. In the years immediately following the ACCC Grocery Inquiry, the increase in competition was driven principally by two factors: (1) the turnaround in Coles' performance as a result of its acquisition by the conglomerate business, Wesfarmers; and (2) the expansion of the discounter Aldi, with its lean business model and aggressive positioning on prices.
9. Intensified retail competition meant that the MSCs strove harder to achieve efficiencies in their supply chains and this included squeezing suppliers on margins as well as reducing supplier numbers and promoting private labels. These developments, combined with factors in the macro-economic environment both domestically (including regulatory burdens and the carbon tax) and internationally (specifically, the spike in the Australian dollar), placed substantial pressure on suppliers.

10. This shifted the focus and perceptions of the economic problem to vertical dimensions of the grocery sector. The prevailing view was that the buyer power of the MSCs created an imbalance of bargaining power between these retailers and their suppliers at least in many if not all grocery supply chains. The imbalance in turn enabled the MSCs to extract terms and conditions from suppliers which were said to involve a transfer of excessive risk onto these parties. Particularly where such terms and conditions were imposed unexpectedly and even more so when accompanied with threats of adverse commercial consequences for failure to agree, the result was seen as suppliers bearing substantial costs, facing increased variability of cash flow and being inhibited in their capacity to plan ahead for their businesses.
11. In the longer term, this was regarded as likely to diminish incentives for supplier investment, expansion and innovation. In competition terms, these effects on suppliers were of concern because of potential long term detriment for consumers. Erosion in or increased concentration of the supplier base and reduced investment, expansion and innovation by suppliers could result in lower competition between suppliers and higher prices, more limited choice and poorer quality in product range.
12. It was recognised that the FGCC could not and would not alter the structure of retail grocery markets. Structurally, the competitiveness of these markets and high combined share of the MSCs would ultimately be a matter determined by contestability, specifically the degree to which recent entrants could continue to expand and new players viably enter and compete. The condition of entry was thus the focus of the Harper Review in the context of its discussion regarding the grocery sector and underpinned its recommendations regarding changes to the process for planning approvals and the regulation of trading hours. However, even without such changes, there are strong signs of continued expansion by Aldi and entry of at least one further foreign discounter as well as a possible second wholesaler have been foreshadowed. Moreover, the MSCs and others point to the increasing emergence of niche online retailers, the real prospect of AmazonFresh entering the Australian market, and the growing use of technology by grocery consumers generally amongst the factors likely to continue to drive competition in the sector.
13. Despite not altering market structure, the FGCC was seen as necessary and justified on the basis of its perceived capacity to address the conduct of concern that arose from the asymmetry in bargaining power between major retailers and suppliers and in particular, between these retailers and smaller suppliers. Specifically, it was conceived as a mechanism that would ensure that its retailer signatories conduct their trading relationships in such a way as to allow greater transparency and certainty for suppliers in contractual arrangements.
14. Provisions in the FGCC directed at these ends relate to the requirement that grocery supply agreements (GSAs) be in writing and that they not be unilaterally or retrospectively varied by retailers except in limited circumstances and with reasonable notice, and to a range of obligations or prohibitions pertaining to payments, delisting, promotions, standards and specifications, supply chain procedures, shelf space, intellectual property and confidential information. The reasoning

was that such measures would engender greater trust and cooperation in grocery supply chains and provide suppliers with the confidence to invest, expand and innovate, which ultimately would engender efficiencies that would benefit consumers in the long run.

*Assessment of effectiveness*

15. Whether or not the FGCC has delivered improved trust and cooperation in grocery supply chains and greater transparency and certainty for suppliers is a question that is difficult to answer definitively only two and a half years (at the time of writing) since its coming into effect. This is particularly as, for some suppliers, the transitional provisions of the Code would have meant that they would have remained under their former contractual arrangements for 12-18 months following the Code's promulgation. While the passage of more time will assist, making such an assessment at any stage will be complicated by the fact that there is likely to be a wide range of factors that affect supermarket-supplier relations, not least changes in a highly fluid competitive environment (referred to further below).
16. Even more challenging would be any attempt to determine empirically whether, in the long run, the FGCC alone has affected the level of dynamic efficiency in the market; that is the extent to which consumers are benefitting from an increased readiness of suppliers to invest, expand and innovate. This is all the more so given that efficiency of this kind is premised to a substantial degree on suppliers achieving the margins over time that will facilitate the necessary investment for innovation. The FGCC does not regulate prices or price increases and hence will not directly affect these significant determinants of dynamic efficiency over time.
17. Those caveats aside, the FGCC can only be effective in fulfilling its more limited objectives of increasing transparency, certainty, trust and cooperation in grocery supply chains insofar as the relevant retailers comply with it and key representatives in both retailer and supplier organisations are aware of and understand its provisions. Further and importantly, such representatives need to feel able and be willing to use that understanding in supply negotiations.
18. It is evident that the MSCs have gone to considerable lengths to put GSAs in place, bring the FGCC to the attention of and train their buying and other affected personnel in its provisions and processes, appoint prescribed personnel for dispute resolution purposes and make the necessary investments in systems to monitor and record transactions in accordance with Code requirements.
19. Amongst suppliers, however, and despite the considerable efforts of the Australian Food and Grocery Council (AFGC), the ACCC and the MSCs themselves, it appears that awareness is not only low overall but uneven in that it is large rather small suppliers that are more likely to have undergone training. This is consistent with the early experience with the code regime in the UK; however, there is evidence that awareness and use of the GSCOP increased substantially following the establishment of the GCA (the role of which is referred to further below). There are

also criticisms made of the FGCC's legislative-style text, seen as user-unfriendly to small business people in particular, and suggestions are made of confusion amongst members of this sector as a result of the plethora of rules and procedures that now govern or affect transactions with their buyers.

20. That said, there are some signs that informed (and even some uninformed) supplier representatives are showing a willingness to use the FGCC, at least in the sense of being prepared to raise and test issues that previously may have been more difficult to air. Moreover, there are reported instances of suppliers being prepared at least to threaten escalation to the Code Compliance Manager (CCM), the person that the FGCC requires be appointed in-house by retailer signatories to deal at first instance with Code-related grievances independently of buying personnel, as a means of obtaining greater leverage in negotiations.
21. It is reported further that these interactions are generating robust but on the whole constructive discussion about the 'correct' interpretation of the FGCC provisions (for example, as to what constitutes 'genuine commercial reasons' for delisting). In this way it is providing a platform and framework for an exchange of views on matters which suppliers might formerly have been reticent to raise or in respect of which they may have been more readily accepting of outcomes against their interest on the basis that they had no choice but to so accept. It is also evident that supplier confidence in these respects is being shored up by the sense that the ACCC is 'on watch', monitoring compliance with the Code through its audits, and remaining open to receiving complaints and taking enforcement action where deemed necessary.
22. At the same time it needs to be acknowledged that these positive early trends may not just be slow to take hold more broadly across the sector but also may prove only short-term in effect. This is because conduct in accordance with both the intent and the specific provisions of the FGCC necessitates a degree of cultural change, transformation even, on the part of the MSCs and to some extent on the part of suppliers also.
23. Amongst suppliers it is reported that there is a deeply ingrained cynicism about whether the MSCs will in fact 'change their ways' and an ongoing reluctance to 'push back' too strongly for fear of jeopardising important (in some cases critical) business relationships. There is good reason to conclude that the leverage of suppliers in bargaining with their MSC buyers is a matter that ultimately can and will only be improved by increased competition (that is by way of structural change in the market), if or when they have a sufficient range of options by way of retail channels, both domestically and through exports, so as to lessen dependence on Coles and Woolworths. The viability of export growth will continue to be affected by factors extraneous to the domestic market, not least by international commodity prices and currency fluctuations.
24. Within the MSCs, competitive pressures are playing a role in an increased recognition by the corporate leadership that a supplier-friendly culture is in the long-term strategic interests of their supermarket business. Observation of this trend could lend support to the view that in the long

run, issues of the kind that gave rise to the FGCC will be resolved as a function of the normal ebb and flow of competition and strategic responses in a sector in which such dynamics are constantly changing. But at the same time there are some who consider that those pressures are only going to become more acute. They argue that with the continued emphasis on low prices particularly, there is every prospect that the MSCs, or at least individual buying personnel, will revert to former practices of the kind that prompted the regulation, in the ongoing battle for share and an effort to deliver on ambitious profit targets.

25. If there is such a risk, then the FGCC will continue to be necessary and important in reducing its potential materialisation. Equally, however, consideration may need to be given to strengthening or refining the Code at some stage so as to reduce the degree to which it currently allows considerable leeway for contracting out of its provisions. If the MSCs oppose such changes, the FGCC would need to be made mandatory. In addition, in order to counteract the effects on behaviour of intense competitive pressures, consideration should be given to introducing pecuniary sanctions for breaches of the Code and possibly to appointing a dedicated ombudsman or other statutory officer to more actively monitor and facilitate compliance with its provisions.
26. On the assumption that the FGCC will retain some relevance in affecting or responding to competitive dynamics in the sector, it is incumbent on policymakers to consider whether it is having or may have any unintended or unanticipated adverse consequences. At least two possibilities are worth consideration in this regard.
  - a. The first is that the FGCC is not mandatory and so only applies to those retailers that have signed up voluntarily to its obligations. This unevenness in application could be seen to give those retailers (and wholesalers, the conduct of which the Code is also intended to regulate) that have not signed up an advantage over rivals. Parties outside of the Code are not encumbered by the same obligations and compliance burdens as apply to those that have opted in and thus may be able to derive cost savings in ways that are no longer available to the same extent to their competitors. This is a live issue in the UK where there is a much larger number and range of retailers and the GSCOP only applies to those with turnover exceeding what is regarded by some as an arbitrary threshold (£1 billion per year). In Australia currently, given the concentration in the market, it is less of an issue, even if some are troubled by the fact that the wholesaler/retailer, Metcash, has chosen not to be bound by the FGCC. However, at some stage it may be a matter that demands attention, particularly if another global discounting chain was to enter the market and, unlike Aldi but like CostCo, decline to sign up to the Code.
  - b. The second consideration is the prospect of the FGCC unduly inhibiting retailer signatories from continuing to strive for efficiencies in their supply chains. There is no question that the drive for such efficiencies in recent years, led by Coles following the Wesfarmers' acquisition, yielded significant benefits for consumers, largely by way of lower prices. Leaders in these organisations would argue that there has been and will be no dampening of their commitment

to efficiency (and low prices) but rather that they are developing new more strategically smart ways of being efficient. This includes an increasing trend of long-term supply contracts that give key suppliers the certainty and confidence necessary to make investments and innovate in the interests of the supplier, their retail 'partner' and consumers.

However, whatever the high level strategy of the MSCs, it is not possible to exclude entirely the prospect that, lower down in the corporate hierarchy, the behaviour of buyer personnel will be affected by the FGCC's prescriptions in ways that may result ultimately in a poorer deal for consumers. There may be an understandable tentativeness by buyers to bargain as hard as previously for fear of crossing the blurry line from legitimate and permissible commercial negotiation into the treacherous terrain of potential FGCC breaches and even unconscionability. Certainly, on some accounts, there is evidence already of buyer wariness in this respect, both as a result of the introduction of the Code, as well as if not even more so in response to the ACCC's investigations and proceedings against the MSCs for unconscionable conduct. Some argue that this can only be seen as a positive development given the nature of the conduct that gave rise to those interventions. Others identify risks for efficiencies, competition and consumer welfare should such wariness take the form of, in effect, over-compliance. However, it is also emphasised that, to reduce such risks, it is critical that the ACCC take and be seen to take a measured and restrained approach in responding to complaints and determining whether formal enforcement action is warranted.

27. Finally, it is important to record that the FGCC was not seen as a complete solution to the problem of asymmetric bargaining power and the conduct to which it gives rise or that is, as a response to the exclusion of other possible responses and remedies. The FGCC was to supplement and possibly bolster other relevant avenues under the *Competition and Consumer Act 2010* (CCA), specifically the provisions relating to misuse of market power, unconscionability and unfair contract terms.
28. At the time of the drafting of the Code, the potency of these avenues was being borne out by increased enforcement activity by the ACCC in relation to unconscionability (in investigations and suits brought against each of the MSCs, referred to above) and by proposed reform to the prohibition against misuse of market power (a proposal influenced in no small part by concerns surrounding MSC market power and conduct). In addition, at least as far as the MSCs were concerned, the FGCC was seen as complementing and reinforcing a range of internal initiatives, including their own corporate charters or codes of conduct, being taken to heal and strengthen their supplier relationships.

#### **A socio-cultural problem of business culture and behaviour**

29. Albeit less explicitly, it is evident that the FGCC was responsive to what was perceived as not just an economic problem but a separate although possibly related socio-cultural problem in the way in which the MSCs were behaving towards their suppliers. While this element of the concerns that

gave rise to the FGCC is harder to crystallise in clear objective terms, it was most often expressed in the proposition that the MSCs were behaving unfairly.

30. The unfairness was seen as made possible or at least aggravated by the imbalance in bargaining power between these retailers and their suppliers. But it was also ascribed in part to the then culture of the MSCs, both at the corporate level and at the level of individual buyer personnel within these organisations at the time of and in the years immediately following the ACCC Grocery Inquiry. Some attributed the cultural dimension of the problem to the influence of an influx of executives from the UK, importing a tougher management style and practices from a jurisdiction where there had been similar controversy surrounding supermarket-supplier relations leading to the introduction of the GSCOP and establishment of the GCA. Distinctions in this regard were often drawn between the MSCs, on the one hand, and Aldi and Costco, on the other. The distinction was not directly ascribed to the German and US origins of these other companies; however, there was a discernible theme to the effect that they had a very different 'way' to that of the MSCs, one that promoted trust by those who dealt with them. Accounts were that, in these organisations, business continued to be done based on the proverbial handshake and when a buyer gave his/her word, it was honoured.
31. Others explained the MSCs' more hard-nosed way of doing business as referable to the fact that the competitive environment and market realities were becoming harsher. However, as previously noted and not without some irony, one consequence of heightened competition appears to be that, more recently, the MSCs themselves are increasingly emphasising cooperation if not partnership with suppliers and taking steps to inculcate this way of thinking into their business culture so as to strategically shore up security of supply. Whether that emphasis is ongoing or at some point is corroded again by competitive pressures is of course hazardous to predict. Strategies relating to supply relationships, and associated aspects of business culture, will also continue to be shaped also by changes in corporate leadership and the experience, styles and preferences of the executives who determine the future direction of these organisations.
32. There was a strong tendency to view the problem of unfair trading as linked to the problem of competition and consumer welfare. This tendency was most pronounced amongst those who advocate for so-called 'fair competition', such advocates being those closely associated with supporting the cause of small business in the economy – which, in the context of this sector, included those representing not just small suppliers, but small 'independent' retailers also. While accepting the general premise that competition rules should protect the competitive process rather than individual competitors (or at least inefficient ones), proponents of the 'fair competition' thesis argue that competition works best when all efficient businesses have an opportunity to thrive and prosper, regardless of size; in other words, where the market presents a 'level playing field' and it is possible to succeed based on 'merit not muscle.' Consumers are said to be better off in this environment given that diversity, both in price and product choice, is preserved and facilitated.

33. At the same time, there are those who refute the suggestion that problems of fairness and competition are interconnected. Competition by its nature is not supposed to be fair, it is argued, and if unfairness results, that is a matter to be managed through distributive policies (through the tax system, for example) and not through competition policy. If competition is working there will be casualties and in a relatively small, isolated and hence unavoidably concentrated economy such as Australia, those casualties inevitably will largely be small businesses. That may be regarded as 'unfair' but, so it is argued, it is nevertheless competition at work. The destructive dimension of the competitive process is defensible, according to these proponents, on the grounds that the ultimate objective is to engender efficiencies that will promote consumer welfare and in turn, economic growth for the benefit of all. If smaller businesses are disadvantaged or eliminated in the process then so be it: there is a higher or at least wider good at stake.
34. The problem of business culture and associated behaviour that is unfair, particularly vis-à-vis small suppliers, was seen as having undesirable consequences of a socio-cultural nature, quite apart from and in addition to any adverse effects on competition and consumer welfare. In particular, the harm to and possible elimination of small businesses was seen as damaging to the social fabric, amenity and cohesion of the local communities of which they are part. Unfairness by big business of the MSC ilk was seen as accentuating public mistrust in large institutions - not only in the corporate world but also in government and the legal system insofar as those institutions are seen as incapable of or unwilling to hold big business to account for what may be regarded as socially unacceptable behaviour. More generally, unfair trading that threatened the livelihoods of small business people was regarded as contrary to entrenched cultural norms of egalitarianism (a 'fair go') in Australian society.

*Assessment of effectiveness*

35. The FGCC was seen as responsive to the socio-cultural problem because it was specifically aimed at preventing the MSCs from acting unfairly or at least reducing the likelihood that they would do so. This was reflected not just in the specific provisions of the Code directed at unfair behaviours but, importantly, in its imposition of a general obligation of good faith in dealings with suppliers. Not insignificantly, this was not imposed as a reciprocal obligation.
36. The FGCC was not seen as directly addressing problems of public mistrust in or cynicism about business and government elites, albeit there may have been a hope amongst some that it could be pointed to as a concerted effort by the industry and the government to allay public consternation about the behaviour by the MSCs. It also was seen as consistent with the societal value of a 'fair go' by tempering some of the harshness of competition and its effects. That is, the FGCC was seen as conducive with so-called 'fair competition' as a social and not just an economic value.
37. It is unclear to what extent the FGCC has or is likely ever to solve the problem of unfair trading behaviour. As previously mentioned, in the short term there is evidence of genuine commitment

by MSC leadership to the letter and spirit of the code project, in putting the necessary organisational and documentary changes in place, and more broadly taking steps to improve supplier relations through a range of initiatives as part of a broader reformulation or adjustment of strategy. However, in large part, such changes can also if not more be attributed to political and consumer pressures, as well as to the ACCC's scrutiny and enforcement action under the unconscionability provisions, referred to above.

38. Moreover, in the long term, doubters point to the overriding profit maximisation objective, responsibilities to and expectations from shareholders in the context of intensifying competition, and hence associated performance targets and incentives as likely to undermine the effectiveness of the FGCC, at least in terms of stamping out behaviour that could be seen as socially (as well as economically) unacceptable. These sceptics view so-called corporate social responsibility, under which umbrella the fair treatment of suppliers might shelter, as inherently fragile and always prone to the vicissitudes of the market in which private companies, particularly listed ones, are compelled if not obligated to act in their commercial self-interest.
39. In any event, public mistrust in large institutions and cynicism about business motives as well as the perception of an unhealthy close relationship between government and big business are much broader and deep seated issues that, at least in the grocery sector, the FGCC is incapable, on its own, of addressing. They are issues that almost certainly will continue to flare up as a consequence of 'bad' behaviour across the economy, including reports of excessive C-suite salaries, swindles and scams, and from time to time large scale malfeasance and GFC-style collapses. The current controversy and debate surrounding the big banks is a case in point.

#### **A political problem of farmer struggles and public sympathies**

40. The low level of farmgate prices threatening farmer livelihoods, undermining rural and regional economic and social welfare, and putting at risk the future viability of the Australian agriculture sector and possibly our long term food security were and continue to be marked features of the debate concerning the high level of concentration in the retail grocery sector. These concerns were acknowledged but their attribution to the market power of the MSCs was largely dismissed in the ACCC Grocery Inquiry in 2008 and again in the Harper Review in 2015.
41. It was emphasised in both of these inquiries and is recognised more broadly that the struggles facing Australian farmers are a product of a host of factors, amongst which grocery retail concentration is only one and arguably a marginal one relative to others. Such factors include:
- the effects of industry deregulation pursuant to National Competition Policy introduced in the 1990s, ending governmental price support and ushering in a period of significant rationalisation, consolidation and adjustment in primary production sectors;

- concentration at intermediate and particularly processing levels of supply chains (in the dairy, chicken and beef sectors especially);
  - the dysfunctionality of wholesale markets in which agents or merchants are seen as particularly culpable in their dealings with growers and the failure of the Horticulture Code of Conduct to eradicate behaviour which might, at best, be said to be non-transparent and, at worst, criminal;
  - seasonal fluctuations (drought and flood) and the impact of climate change in this regard;
  - under-investment by government in necessary infrastructure for rural and regional communities;
  - high costs (for labour and energy particularly);
  - regulatory burdens (for example as to labelling and technical specifications); and
  - international commodity prices (affecting prices for commodities such as sugar and wheat).
42. Strong concerns in connection with the dairy industry prompted a spate of Parliamentary inquiries between 2009 and 2011 in which the full range of forces at work were canvassed but in which the role of the MSCs still loomed large, amplified by the calls from some Parliamentarians for drastic action to 'break up the duopoly'. This focus of attention was accentuated by the Coles-led initiative to introduce \$1/L milk and the ensuing so-called 'milk wars', a matter which was seen to justify an inquiry all of its own. However government responses failed to exclusively or even directly ascribe the economic and social challenges besetting the dairy sector to the conduct of the MSCs. Rather, the challenges were to be dealt with through other lenses, including an Agricultural Competitiveness package and a National Food Plan, neither of which had the MSCs squarely in their sights.
43. Nevertheless media coverage and popular public discourse relating to these developments perpetuated a focus on the MSCs as 'villains' in the dairy drama and this ensured, if nothing else, a substantial degree of political pressure. Such pressure reflects a general risk confronting governments in mediating the competing demands of, on the one hand, effective management of the economy (including through the promotion of competition, as a policy measure important to productivity and growth) and, on the other hand, effective responses to social needs and values – in particular the need for a stable social order based on shared norms, social values and cultural identity, one inevitably threatened by economic change and uncertainty.
44. In the present context, this risk was reflected in the dilemma facing politicians by virtue of the fact that, while their constituents benefitted from low milk prices, there was also apparent public sympathy for farmers. Even if this sympathy did not necessarily translate into widespread changes in consumer purchasing behaviour, its strength as a public sentiment was undeniable. While

complex to define and explain, some argue that it is a sentiment underpinned by a nostalgia for and allegiance to the primary industries and pastoral communities - the 'sheep's back' - on which the country's economic success was built, and that it is fuelled by cultural syndromes of support for the 'underdog' and denigration of the 'tall poppy'. Marketing initiatives by the MSCs and other retailers, directed at a show of dairy farmer support, reflected supermarket sensitivity to this sentiment as well as sensitivity to the risks that political reactivity would result in unwanted and unproductive regulation in response.

45. It is thus in no way coincidental that in 2012 the industry heavyweights – the MSCs and the AFGC together initially with the National Farmers Federation – decided to act. The Retail-Supplier Roundtable (RSR) was formed to nut out a code that, three years later, would become the FGCC. The FGCC does not apply to indirect supply relationships and so does not benefit farmers directly. Nor does it touch on prices paid to direct suppliers so as to affect prices that may be paid to farmers indirectly. It is evident nevertheless that, to some degree, the FGCC arose out of a course of events in which the MSCs, and the government, considered it necessary to respond to significant public pressure to take action in response to farmer concerns. It is in this sense that the FGCC may be characterised as at least in part responsive to a political problem. That sense is reinforced by MSC insistence that the FGCC only formalised an approach to supply chain relations that reflected commitments and practices they had already started to establish or in fact had always had in place.

*Assessment of effectiveness*

46. The FGCC is seen to have been effective in addressing the political problem, at least in the short to medium term. The consensus amongst both supporters and detractors is that the promulgation of the Code gave both government and 'the industry' (at least the MSCs and the AFGC) the ability to publicly point to it as a targeted and proportionate regulatory response to the concerns of suppliers, consumers and the broader public about the power and conduct of the major grocery retailers.
47. This is not to say that there was not then and indeed continues to be significant dissent regarding the strength of the FGCC and whether it 'goes far enough' in addressing relevant issues. There was no shortage of critics, from a range of organisations representing small business and farmers particularly, who called for the Code to be mandatory, to be less flexible / more prescriptive, and to have a dedicated Ombudsman or other enforcement architecture supplementing the role of the ACCC, as well as for there to be meaningful penalties for Code breaches. However, by and large, and in accordance with a general deregulatory agenda and ethos, the liberal arm of the government was persuaded (and evidently of the view that its most politically important constituencies would be persuaded) that the FGCC was a sufficient response to the concerns at hand. At the same time it promised a review in three years time, reassuring detractors that their views were not being dismissed, rather just deferred.

48. Whether or not the Code continues to be viewed in this way will depend to a substantial degree on assessments made of its operation and impact in its first three years, at the time of the review in 2018. Those assessments in turn will be influenced substantially by the stance taken by key independent stakeholders, the AFGC and the ACCC particularly, in relation to the review. The submissions of the MSCs which are likely to point, amongst other things, to the actions they have taken both in compliance with the FGCC and, indeed, in excess of its requirements to assuage supplier concerns will be given weight also. The criticisms made of the code proposal, at the time of Treasury's consultation and the Senate inquiry in 2013-14, can be expected to be repeated. However, at this stage there are no strong signs that the politics surrounding the sector will favour major change. This is particularly as the government has taken already significant steps separately to address broader small business and farming-related issues.

### **A systems problem of legal rules and litigious avenues**

49. There are laws available to deal with most if not all of the conduct issues at which the FGCC is directed, and a well-resourced and capable independent agency in the ACCC to enforce them, including through legal proceedings with the potential for (soon-to-be) significant financial sanctions imposed, in addition to the reputational fall-out associated with allegations, investigations and litigation of this nature. Nevertheless, these systems were seen as inappropriate or inaccessible avenues for dispute resolution by suppliers in their dealings with the MSCs. This was particularly believed to be the case for small suppliers although there was a view held by some that legal routes were unlikely also to be pursued by large suppliers also. While some argued this was because large suppliers have sufficient leverage to be able to sort out grievances in the context of commercial negotiations, others were of the view that large suppliers too, perhaps even more so than small ones, are reluctant to 'rock the boat', given their degree of dependence on the MSCs as a channel to market.
50. As a systems problem related broadly to 'access to justice', this was an issue seen as having at least the following dimensions:
- the laws intended to protect suppliers from anti-competitive and/or unconscionable conduct are not well understood by suppliers other than the largest businesses with the benefit of in-house and external legal advice;
  - legal proceedings are too slow (especially where the dispute involves perishables), too complex and too expensive;
  - the ACCC has limited resources and has to focus on issues that have economy-wide effect and even where it can and does take action, the penalties applicable to breaches are inadequate to punish and deter; while reputational damage is significant, it is arguably only short term in effect; and

- suppliers are reluctant to complain to the ACCC out of fear of commercial retribution, an issue again predominantly associated with but not limited to small suppliers.

51. The FGCC was seen to address this problem by providing a multi-tiered system of dispute resolution. It would start with avenues internal to the retailer, enabling suppliers to raise issues with or make a complaint to the CCM and to escalate internally to more senior management, if necessary. A supplier would also be entitled to engage an external process of mediation or arbitration, once internal mechanisms were exhausted. At any time, recourse to the ACCC would be preserved. The ACCC would play an important role in monitoring and auditing compliance with the FGCC and could decide to take action to enforce the Code in accordance with its normal enforcement powers and procedures. In addition or alternatively the Commission could take action where the conduct in question was regarded as in potential breach of the general competition and fair trading rules in the CCA.

*Assessment of effectiveness*

52. To date there has been scant use of FGCC's dispute resolution provisions and processes. This appears to be due to several factors that are also material in assessing the degree to which the FGCC is ever likely to be effective in tackling the systems problem outlined above:
- suppliers are either unaware of or reluctant to use the internal dispute resolution process provided for by the Code because it imposes onerous, unrealistic and impractical burdens to make their case, vests power in the retailer to dismiss the complaint on grounds of being vexatious, trivial, misconceived or lacking in substance, and, culturally, is also just not seen as the 'way to do business';
  - suppliers are either unaware of or reluctant to use the external process of mediation/arbitration for the same reasons and also because of the perception that it would be of limited if any value to involve a third party mediator/arbitrator who lacks industry knowledge; there are also concerns about the potential cost of this process;
  - suppliers remain reticent to approach the ACCC for the reasons stated previously, particularly because ultimately neither this nor the other avenues referred to above provide or provide sufficiently for anonymity in relation to complaints.
53. There are mixed views on and accounts as to whether the weaknesses in the dispute resolution framework established by the FGCC are matters about which to be substantially concerned at this stage. On the one hand, there are those who take the positive view that, at least on early indications, the FGCC has 'changed the rules of the game' sufficiently (particularly, through its requirements of written agreements and restrictions on variations and extra-contractual payments) so as to have minimised the extent to which suppliers have grievances that need to be addressed through a formal dispute resolution process. On the other hand, there are those who regard the code enforcement architecture to have been misconceived from the outset and

point, by comparison, to the very different approach taken in the UK and the positive experience of its impact in that jurisdiction to date.

54. In the UK, the GCA is playing a significant and, according to widespread opinion it seems, highly effective role both in heading off and, when they arise, managing disputes between retailers and suppliers. Much more in the style of an ombudsman than an enforcement agency, albeit with coercive investigative and substantial fining powers, the GCA's approach has the following key ingredients:
- a significant commitment to education and training of both supplier and retailer personnel in the purposes and provisions of the GSCOP, through workshops, conferences, web communications, published newsletters, case studies and surveys and the media generally (particularly the trade press);
  - relationship building and collaboration with the retailers' Code Compliance Officers (the equivalent to CCMs), including close regular consultation with these individuals to identify issues early on, assist with interpretation of the relevant GSCOP provisions, develop effective responses to them and feed back concerns raised with the GCA by suppliers;
  - systematic and detailed data collection on GSCOP awareness and compliance generally and on specific issues that have arisen in the course of consultations, published at an annual conference and through the media, both as a way of furthering understanding and education but also to incentivise positive competition by retailers wanting to be seen as committed to the Code;
  - board level contacts by the GCA within the retailers to ensure that there is ongoing vigilance at the most senior level of these organisations in managing the regulatory and strategic risks associated with any slackening in code adherence, and in continuing to engender a business culture conducive to compliance; and
  - the GCA's deep personal experience in and knowledge of the industry and supply chains generally, and her non-legalistic, practical and balanced style and approach to fulfilling her role.
55. The creation of a similar role in Australia was strongly resisted by the MSCs in the negotiations that culminated in the FGCC, and ultimately was not pressed for by the AFGC despite its initial support for such a model. It was also a model advocated for by a range of other stakeholders. The GCA is funded by a levy paid by the retailers designated as subject to the GSCOP in the UK. MSC resistance was not necessarily based on concern about replication of the UK funding arrangements, as there is no obvious precedent for an industry-funded statutory scheme in Australia. However, there was significant concern about the degree of oversight and potential

‘interference’ that an ombudsman-style scheme was likely to involve, and its associated compliance cost.

56. The debate regarding the practical effectiveness of the FGCC dispute resolution framework is likely to be revisited in the 2018 review. The contrasting experience in the UK should be considered in this context. It can be anticipated, however, that the MSCs at least will maintain their opposition to the establishment of a similar scheme for the Australian sector and again, on such matters, the views of the AFGC and the ACCC will be highly influential. Certainly, the introduction of any such scheme would be likely to require that the FGCC be made mandatory, as the MSCs are unlikely to subscribe voluntarily to a code with a UK-style enforcement architecture. This may be reason enough for the government to resist any pressure for change on this score. However, the government is also able to point to the establishment of the Small Business and Family Enterprise Ombudsman’s office that followed the promulgation of the Code as at least providing some of same functions, even if some way short of the dedicated services of the GCA.

**In short...**

57. Economic concerns regarding the conduct of the MSCs and its long term effects on dynamic efficiency and consumer welfare are a product of the structure of the market and specifically the degree of concentration at the retail level owing to the high combined share of Coles and Woolworths across a substantial number of product categories. The FGCC was not intended to and will not address this structural issue.
58. While awareness, understanding and willingness to invoke the FGCC is sub-optimal and varies considerably across the supply sector at present, there are indications that the FGCC has improved transparency and certainty for some suppliers in their contractual arrangements with MSC buyers and may have engendered a greater degree of trust and cooperation in supply chains generally. Even if the MSCs regard the FGCC as only formalising approaches that they had either already adopted or were beginning to adopt anyway, it is evident that the FGCC is playing a useful reinforcement role in this regard.
59. That said, in the medium to long term, the prospect of the MSCs engaging in or reverting to conduct of the kind that prompted the introduction of the FGCC will be determined largely by the level of competition which in turn will remain predominantly a function of market structure. Intensified competition may incentivise retailers to adjust strategically in ways that are beneficial to suppliers; there are signs of this occurring already and with the likely continued expansion of recent entrants as well as new entry, there are grounds for confidence that such adjustments will be retained if not strengthened.
60. However, competitive pressures equally might cause some buyers to revert to former practices or develop new ones inconsistent with the spirit if not the letter of the FGCC. Should this risk

materialise, the FGCC will continue to be an important safeguard in minimising the perpetuation or spread of such practices but only insofar as the Code is regularly reviewed, adapted and refined to reflect developments in the market place and is subject to ongoing close monitoring of compliance by the ACCC, and a willingness and capacity by this agency to take enforcement action as necessary. Review and refinement of the FGCC for this purpose could entail:

- a. making some of its provisions less flexible (more prescriptive);
- b. adding new provisions to address emerging practices; and
- c. providing a more potent consequence for breaches by way of meaningful financial penalties.

61. Social concerns about unfair behaviour on the part of the MSCs are likely to have been ameliorated by the FGCC to the extent that it has resulted in or reinforced changes in the way in which these retailers go about dealing with suppliers. However, just as in relation to economic concerns, the ongoing effectiveness of the FGCC in this regard will be substantially determined by the MSC responses to dynamics in the competitive environment. These responses in turn will be shaped largely by the prevailing culture within these organisations at any given time and these cultures in turn will be influenced by the profile of the corporate leadership. It is corporate culture that will determine ultimately whether targets set for performance and associated remuneration structures, at the corporate level and for individual buyers, and the strategies adopted to achieve them create an environment that prompts and possibly even facilitates a reversion to socially unacceptable conduct.
62. Broader social concerns relating to a general public mistrust of large and powerful institutions will not be addressed by the FGCC, although for some the Code may provide an assurance that government is prepared to step in and regulate where necessary to ensure that big businesses act in accordance with social norms and values. There may also be support for the FGCC on the grounds that it is consistent with a notion of 'fair competition' and, more generally, with the strongly held cultural attachment to egalitarianism in Australian society.
63. Political pressures to take action in relation to the challenges facing farmers and respond to public sympathies in that regard are likely to have been alleviated to some degree by the FGCC. Self-evidently, the FGCC does not apply to MSC relationships with farmers as indirect suppliers and, as it does not affect prices negotiated with direct suppliers, it also cannot be said to be likely to have a positive flow-on effect on farm-gate prices. Despite this, from the perspective of the MSCs at least, the FGCC ameliorated the prospect of the government adopting a more heavy-handed and costly stance given that, in the public arena, the government was able to point to the Code as a welcome industry-led solution to concerns about the power and conduct of the major retailers. It is less clear that consumers, with their deeply engrained suspicion of big business, will be so easily won over.

64. The inappropriateness and inaccessibility of relevant laws and legal proceedings to resolve supermarket-supplier disputes, particularly but not limited to those involving smaller suppliers, is a systems problem that the FGCC, in its current form, is unlikely to address. Even if suppliers are aware of the availability of the internal and external process for dispute resolution provided for by the FGCC, there are reasons to conclude that there is unlikely to be substantial uptake of these processes. Suppliers are and are likely to remain sceptical of the value of such processes and fearful of the consequences of invoking them.
65. Low take up of the FGCC dispute resolution framework may not be of major concern to the extent that the Code's provisions are able to change the behaviour of buyers in a way that minimises disputes arising and certainly there are signs of such change afoot. It may also be said that suppliers now have a considerable range of avenues for raising grievances and making complaints, beyond those available under the Code. They include processes put in place by the MSCs under internal charters and policies, the services provided by the Small Business and Family Enterprise Ombudsman's office and ultimately by way of complaint to the ACCC. At some stage in the future, however, there should be assessment as to whether the combination of these avenues is being effective in addressing supplier access to justice. At that point, depending on the outcome of the assessment, consideration may be given to possible adoption of a UK-style ombudsman scheme given the positive experience with the GCA model in that jurisdiction to date.

## 1. Introduction

The size and power of Australia's major supermarket chains (MSCs), Coles and Woolworths, have been the subject of sustained public debate and controversy for over a decade in Australia. Initially much of the concern was with harm to horizontal competition in grocery markets, that is competition as between retailers, and attendant consumer detriment, mostly by way of the prices paid at the check-out counter and, albeit to a lesser extent, the range of choice on the supermarket shelves. Standard micro-economics would suggest that a largely duopolistic market in which two firms enjoy a combined 60-70% share of sales in a substantial proportion of product categories, barriers to entry are relatively high and customers and suppliers have minimal countervailing or bargaining power, the result will be anti-competitive one – the market will not function effectively and consumer welfare will be diminished accordingly.

Yet at least two major independent inquiries into the sector, in 2008 and 2015, concluded that notwithstanding the high level of concentration, competition is generally working as it should and consumers are benefitting, at least in the short run. Correspondingly, while enforcement scrutiny has intensified in the last five years particularly, regulatory intervention in relation to competition has been fairly light touch, and largely directed at ways in which to reduce barriers to new entry and expansion of recent entrants. The prevailing view in policymaking and enforcement circles has been that, left mostly to its own devices, the 'invisible hand' of the market will be effective in delivering desired outcomes for consumers.

Despite this apparently high level of official comfort with allowing market forces to take their course, there has been no abatement in public and stakeholder agitation regarding the power of the MSCs – if anything, since 2008 industry concerns have escalated. To a large degree the more recent focus has been on vertical issues and specifically on the way in which the MSCs transact with and treat their direct suppliers. In particular, there has been a focus on MSC extraction of terms and conditions seen as involving an unreasonable transfer of risk and a squeeze on margins that dampens incentives for innovation and investment and prompts consolidation (and thus concentration) in some parts of the supplier base. In addition to the adverse implications for direct suppliers and, in the long run potentially for consumers, the flow on effects for indirect suppliers – primary producers especially – has garnered substantial attention. In the process, much of the blame for the struggles of Australian farmers has been levelled at the MSCs.

These concerns culminated in the introduction of a statutory code of conduct regulating supermarket-supplier relations in 2015 – the Food and Grocery Code of Conduct (FGCC). The Code is voluntary but only insofar as it does not apply compulsorily – retailers (and wholesalers, to which the provisions extend) can choose whether or not to agree to be bound. However, once signed up, the obligations are legally enforceable. Thus far, the MSCs, together with Aldi and a small retailer (About Life), have volunteered to be bound by the FGCC.

On any measure, the FGCC is a highly prescriptive regulatory instrument, influencing at least and in some instances dictating the approach taken to almost every aspect of the commercial relationship between the signatories and their suppliers. It imposes a not insignificant compliance burden and, some would argue or hope, cultural change on the MSCs and it also introduces a formalistic multi-tiered process for dispute resolution. The Code is enforceable by the Australian Competition and Consumer Commission (ACCC) in proceedings that would entail intrusive investigation, unwelcome publicity and substantial reputational fall-out for the accused code-breaker, and a range of formal orders even if (currently) the formal sanctions do not involve financial penalties.

If the market is working and consumer welfare is secure (at least in the short run), the advent of such regulatory intervention demands interrogation. This is particularly so given that there may be some support for the view that the code could in fact undermine competition by its uneven application across retailers and wholesalers, by weakening the drive for greater efficiencies in grocery supply chains, thereby undercutting achievement of the very policy objective at which the official attention has been mostly directed in the context of this sector. It warrants investigation even more so given that regulation of business conduct, at least to this degree, may be difficult to reconcile with the free market philosophy that underpins competition policy.

What is more, for some time now business, both big and small, has been pressing for and the government has promised to deliver further deregulation and the reduction of 'red tape' in the interests of increased productivity and economic growth. In this particular instance it was in fact the MSCs that took the regulatory initiative in proposing an enforceable code and drafting much of its content. In effect, the regulated turned regulators and in what could be seen as an astonishing and unprecedented exercise in collaboration and cooperation between two otherwise fiercely competitive and culturally different businesses.

Moreover, the MSCs were effective in co-opting government into the project, producing a co-regulatory instrument with objectives, terms and procedures defined largely by its industry authors but with legislative status and public oversight of its enforcement. The regulatory process thus exhibited an alignment of interests and convergence on norms between powerful private and public actors. Furthermore, the process was not just validated but arguably facilitated by the peak supplier body, the Australian Food and Grocery Council (AFGC), that organisation having convened a Retail-Supplier Roundtable (RSR) with the MSCs to offer up with a solution to the problems besetting the sector. Thus, from a regulatory studies perspective, the FGCC provides a fertile case study not only of the reasons for and outcomes of regulation but also of the processes by which regulation is formulated and the impact in turn of those processes on its legitimacy and effectiveness.

This report is based on research that has probed systematically the background to and developments leading up to the FGCC's introduction and, although it has been in effect for only a relatively short time (just over two years as at the date of this report), the way in which the code is perceived to be and is working in practice. The report draws on a broad range of primary and secondary sources from an extensive public documentary record. It is also informed by in-depth interviews with a large number

of stakeholders from across the grocery sector, related private and government organisations, and civic society.

## 2. About this report

### I. Research aim, questions and time frame

The broad aim of this report is to set out the key findings from two years of research into the FGCC, its background and operation to date, and the analysis on which those findings are based.

The approach to the research has been framed with a view to addressing the following questions:

1. What were the problems to which the FGCC was responding and why and how was the FGCC seen as responsive to or likely to address them?
2. To what extent has the FGCC been effective to date or is it likely to be effective in the future in addressing such problems?
3. What are the insights and lessons from the FGCC experience for regulation of the grocery sector in relation to competition and fair trading, if not regulation of the grocery sector and potentially business more generally?

This report is largely concerned with addressing the first two of these questions.

Its analysis ostensibly commences on 22 January 2008, when the then Assistant Treasurer directed the ACCC to conduct an inquiry into the price of groceries (the ACCC Grocery Inquiry).<sup>1</sup> However, in exploring important context relevant to impetuses for the FGCC's introduction, the report also canvasses earlier developments, including the impact of deregulation on the grocery sector brought about in part by the National Competition Policy (NCP), introduced in the 1990s under the Hawke-Keating Labor Governments as part of a package of microeconomic reforms.

Further, insofar as relevant, the report draws on public inquiries and industry reports that predate the ACCC Grocery Inquiry. The analysis also takes into consideration precursors to the FGCC, including the now defunct voluntary Retail Grocery Industry Code of Conduct in 2003 (renamed the Produce and Grocery Industry Code (the PGCC) in 2005), and the mandatory Horticulture Code of Conduct (HCC), prescribed under the *Competition and Consumer Act 2010* (Cth) (CCA) in late 2006.

The analysis relating to the FGCC's operation is current as at June 2017.

### II. Research method

The research underpinning the report has involved review and analysis of the extensive documentary record bearing on the subject of supermarket-supplier relations in Australia, predominantly from 2008 onwards, including official policy, regulatory and legal documents such as draft and final reports from public inquiries and related submissions; industry/market and consumer research reports and court

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<sup>1</sup> ACCC (2008) *Report of the ACCC Inquiry into the Competitiveness of Retail Prices for Standard Groceries* (ACCC 2008 Grocery Inquiry).

judgments. The report also draws on media releases, speeches, press articles and other sources of commentary relevant to its subject-matter.

The report is informed further by 71 stakeholder interviews conducted over approximately eighteen months between early 2016 and mid-2017. These interviews assisted substantially in supplementing, interpreting and testing the documentary record. They enabled the researchers to explore how a wide range of actors perceive the regulatory goals and processes and hear their views directly on issues relating to competition and fair trading in the grocery sector, including their perspectives on the relative effectiveness of existing and proposed regulatory instruments.

Interviewees were selected according to their knowledge and experience in or of the grocery sector and/or regulation in this space, with the aim of obtaining a diverse range of perspectives from a broad cross-section of the industry, government and civic society. Interviewees included representatives from:

- the MSCs and other grocery retailers;
- individual suppliers and advisers/consultants to suppliers;
- industry associations for retailers and suppliers;
- farmers' federations and fruit and vegetable growers associations;
- business lobby groups;
- consumer groups;
- social researchers;
- journalists;
- the ACCC;
- the federal Treasury;
- parliamentarians; and
- federal, State and local government agencies.

The interviews were structured in accordance with a series of open-ended questions, of which interviewees generally had notice in advance. Based on a general template, each questionnaire was tailored to the individual interviewee. Preference was given to face to face interviews; however where not practical interviews were conducted by phone. The interviews ranged in length from one to two hours and where possible were conducted by two and sometimes more members of the research team.

In compliance with University ethics safeguards, interviewees were guaranteed anonymity and confidentiality, undertakings as to which were set out in a Plain Language Statement provided to interviewees. Interviewees were required to sign a consent form, consenting to the interview and its recording, as well as any individual, mutually agreed naming and quotation arrangements, before the interview commenced.

The professional service used to transcribe the interview recordings was under contractual obligations of confidence and steps have been to ensure secure custody of the interview data. The audio recordings, transcripts and coded data are kept in locked facilities on University premises and can only be accessed on computer by the project team. The interview material will be kept for at least 5 years, after which it will be disposed of using a University approved confidential disposal service.

A largely anonymised list of interviewees is **Appendix A** to this report and the template questionnaire used in the interviews is **Appendix B**. Given the number and range of stakeholders, the interviews do not purport to be representative of all possible views on the issues that are the subject of this report.

The researchers are indebted to the interviewees for the generosity of their time and candour of their views, including on subjects that in some contexts are commercially sensitive or controversial for various reasons. The views of respondents and direct quotes from interviews populate this report, providing at times unique insight into the opinions, issues and concerns that permeate the grocery sector. Attribution for these views is in accordance with the special naming arrangements agreed between the researchers and each interviewee. This varies across interviews. Some have given full consent to be named, others are identified according to the institution they represent, while others still are afforded full anonymity by way of a generic identifier.

### III. UK comparisons

The research also involved analysis of the experience in the United Kingdom (UK). While similar issues and debates relating to supermarkets exist around the world, the UK is particularly relevant in the Australian context.

A Supermarket Code of Practice (SCOP) was introduced in the UK in March 2002 following an inquiry by the Competition Commission (CC),<sup>2</sup> upon referral from the then competition authority, the Office of Fair Trading (OFT). The SCOP was voluntary insofar as it applied only to those retailers that gave undertakings to the OFT, and was overseen by that Office. Its purpose, as with the FGCC, was to redress the power imbalance between big supermarkets and their suppliers by placing relations between these parties on a more transparent and certain footing.

In 2003 OFT undertook a review of the Code and in 2004 reported that it had anecdotal evidence of breaches but no evidence that relations between retailers and suppliers had changed significantly since the Code's inception.<sup>3</sup> The OFT promised to undertake further follow up work and in 2005 completed a 'compliance audit' which in essence concluded that by and large supermarkets were compliant even if the Code was not being used to settle disputes (predominantly, it appeared, because a fear by suppliers of retribution in response to complaints).<sup>4</sup> Despite ongoing pressure to take further action, in late 2005 the OFT concluded that there were no grounds to make a referral back to the CC for a further market study<sup>5</sup>. However, in response to legal action by various industry

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<sup>2</sup> CC, *Supermarkets: a report on the supply of groceries from multiple stores in the United Kingdom*, October 2000.

<sup>3</sup> The Supermarket Code of Practice, Review OFT697, February 2004.

<sup>4</sup> OFT, *Supermarkets: The Code of Practice and Other Competition Issues*, March 2005.

<sup>5</sup> 'OFT rejects supermarket suppliers inquiry', *Financial Times*, 4 August 2005.

associations to compel the reference, the OFT announced it would review its decision and by mid-2006 it had made the referral, announcing that the CC would undertake a full investigation into the sector.

In a substantial report published in 2008 (CC Report) the CC recommended, amongst other things, that there be a new strengthened and extended Code and an independent ombudsman to oversee and enforce it.<sup>6</sup> The Groceries Supply Code of Practice (GSCOP) came into effect on 4 February 2010 by way of an administrative order made by the CC, replacing the SCOP. Unlike the FGCC, the GSCOP is mandatory in its application. However, it only covers the eight major supermarket chains operating in the UK and all other retailers with groceries turnover in excess of £1 billion per year. Like the FGCC, it relates only to direct supply relationships. It includes provisions about fair dealing (including an obligation on retailers to deal with suppliers in good faith), prohibitions on retrospective changes to terms of supply, procedures for customer complaints and de-listing, the burden of proof on retailers for 'requests', and compliance and enforcement, including dispute resolution and binding arbitration procedures and the requirement that retailers have in-house compliance officers. The GSCOP also imposes obligations on retailers to appoint a Code Compliance Officer (CCO), maintain written records of all agreements with suppliers, and supply information to the Competition and Markets Authority (CMA, formerly the OFT) as required.

In June 2013, the office of the Groceries Code Adjudicator (GCA) was established by the *Groceries Code Adjudicator Act 2013* (UK), to enforce compliance with the GSCOP. The GCA's statutory functions are to: investigate confidential complaints from any source about how supermarkets treat their suppliers; make recommendations to retailers if a complaint is upheld; require retailers to publish details of a breach of the code; in the most serious cases, impose a fine on the retailer; and arbitrate disputes between retailers and suppliers. Christine Tacon CBE became the first Adjudicator and was appointed for a four year term. The Adjudicator is wholly funded by a levy on the retailers which for 2016/17 was £2 million. The performance of the GCA, and the scope of her remit, were the subject of a statutory review in 2016. The results released in 2017 resoundingly endorsed Tacon's performance and the effectiveness of the GCA as a regulatory approach to improving supply chain relations.<sup>7</sup> As at the date of writing, there is an ongoing review of whether the GCA's remit should be extended to cover primary producers.

The design and experience in implementation of the UK regime was influential in Australian developments. The research undertaken to facilitate comparisons with and insights for the Australian experience involved review of relevant official reports and submissions and interviews with UK policymakers, regulators, industry association representatives, retailers and leading commentators. The approach taken to these interviews was the same as described above in relation to the Australian interviews and the UK interviewees are included in Appendix A.

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<sup>6</sup> CC, *The supply of groceries in the UK market investigation*, 30 April 2008 (CC 2008 Report).

<sup>7</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017.

## IV. Structure of this report

Following this introduction, the report is structured as follows:

**Part 3**, 'Warning signs', canvasses key regulatory and industry developments, as well as broader shifts in the macro-economic environment, from 2008 onwards and analyses how such developments served as signposts to the likelihood that action would be taken to regulate supermarket-supplier relations.

**Part 4**, 'Immediate catalysts', identifies and explores how critical events in the dairy sector created the political conditions and momentum for regulatory action. It analyses how and why these events had salience amongst the general community and in turn how this, combined with political pressures, placed sufficient pressure on the MSCs and in turn on government to act.

**Part 5**, 'Significant actors', identifies and examines how key actors, both individuals and organisations, in the private and public sectors influenced developments. Without purporting to be exhaustive, and for reasons that should be evident from the analysis, the report singles out for this purpose: the ACCC (and in particular, its two Chairmen over the relevant period, Graeme Samuel AC and Rod Sims), the former Minister for Small Business, Bruce Billson, and the AFGC and its two Chief Executive Officers (CEOs) within the relevant time frame, Kate Carnell and Gary Dawson.

**Part 6**, 'At the negotiating table', explains the process of and critical voices in, as well as those absent from or at the margins of, the negotiations that led to the enactment of the FGCC. It highlights the issues that occupied most attention and explains how they were resolved.

**Part 7**, 'In practice to date', charts the experience with the FGCC in practice since its introduction up until the time of writing and starts to identify aspects of the Code that are seen as working as well as areas in which the Code is proving less effective and the reasons for this.

**Part 8**, 'Up for review and looking ahead', reflects on the analysis and findings in the report with a view to providing insights that may be valuable in the context of the review of the FGCC to be held in 2018.

### 3. About the Supermarket Power project

The research underpinning this report has been undertaken as part of a broader research project – the [Supermarket Power project](#) - funded by the Australian Research Council over four years, 2015-2018.

The project is an interdisciplinary undertaking drawing on empirical and theoretical research that aims to fill key gaps in the regulatory debate when it comes to understanding why and how the MSCs have developed as they have, the strategies that have contributed to their growth, the impact that changes over time have had in the industry and the role of regulatory schemes relating to competition and fair trading in the grocery sector. An important case study for the project centres on relations between the MSCs and their suppliers, and the ways in which those relations have been and are currently regulated. It is this case study that forms the basis of the report.

The project is based at the University of Melbourne's Law School. Led by Professor [Caron Beaton-Wells](#), a specialist in competition law, the other members of the team are regulatory studies expert Professor [Chris Arup](#), economic historian Emeritus Professor [David Merrett](#) and sociologist Associate Professor [Jane Dixon](#). The team is supported by Research Fellow, [Jo Paul-Taylor](#).

## 4. Warning signs

In this Part of the report we canvas key regulatory and industry developments, as well as broader shifts in the macro-economic environment, from 2008 onwards and analyse how such developments served as early signposts to the likelihood that ultimately some action would be taken to regulate supermarket-supplier relations.

The ACCC Grocery Inquiry provides a useful starting point in examining the context in which the FGCC emerged. This is not to suggest that many of the issues grappled with in the inquiry were new. In particular, implications of MSC dominance for small to medium size grocery businesses (both retailers and suppliers) had been the subject of inquiries dating back to the early 1990s. However, the extent to which the inquiry's characterisation of competition in the grocery sector in 2008 remains true today, and for whom, or failed to foretell what was to come, are relevant considerations when tracing the development of the FGCC, and the form that that instrument took.

The inquiry's focus was on retail concentration and its consequences for competition and consumers in the grocery sector in both horizontal (as between retailers) and vertical (as between retailers and suppliers) dimensions. It is contextually significant because of its ultimate findings, namely that the sector at that time was 'workably competitive'<sup>8</sup> and there was nothing 'fundamentally wrong' in the supply chain.<sup>9</sup> However, despite the scope of consultation undertaken for and the detail provided in its 500-plus pages, the ACCC's report provided only a hint of future developments. The period immediately following the inquiry was punctuated by a series of forces and factors that would inflame MSC-supplier relations, drawing these issues further into the public and political spotlight.

In this Part of the report we begin by considering the impetus for and the main findings of the inquiry, together with the divergent responses to these findings of different stakeholders. While the MSCs were supportive of the generally favourable (for them) conclusions, some suppliers believed that the ACCC had missed the mark. Regardless of whether this criticism was valid at that time, it was not long before competition between the MSCs increased significantly, bringing with it direct consequences for vertical relations. We identify and examine the two key reasons for this: the Wesfarmers' takeover of Coles, which saw the previously languishing supermarket chain quickly and aggressively bring the challenge up to Woolworths, and the emergence of Aldi, the German discounting chain, as a major price competitor to the two dominant MSCs.

The amplification of horizontal competition brought with it cheaper prices for consumers but at the same time extra pressure on suppliers as the MSCs fought hard on market share and sought to temper the Aldi effect. We highlight these reverberations of retail competition in the vertical supply chain. At the same time we point to the significance of contemporaneous developments in the macro-economic environment and their effects. Almost immediately after 2008 the Australian dollar began to strengthen. By 2009 it had achieved parity with the US dollar, creating conditions where imports were

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<sup>8</sup> ACCC 2008 Grocery Inquiry, p. 210.

<sup>9</sup> ACCC 2008 Grocery Inquiry overview, p. xiv.

increasingly attractive to the MSCs seeking cheaper stock while export markets for Australian manufacturers became increasingly challenging. The analysis further demonstrates that during this period the MSCs, Coles especially, was undergoing something of a cultural transformation. In an attempt to turn the company around Wesfarmers looked to the UK to fill key senior management positions. The UK grocery retail sector had long been a hotly contested market, and these new leaders brought with them aggressive negotiating and other supply chain strategies that had been employed successfully to squeeze the best deal out of UK suppliers.

As pressure on Australian suppliers mounted they found their political voice, not only behind doors in the Canberra corridors of power but also in mainstream media. We document these political rumblings and point out that, as a consequence, it was no longer sufficient for government to focus on ensuring the sector provided competitive grocery prices. The viability of Australian suppliers was under threat and 90% of these were small to medium size businesses. As the sector heated up the political implications of having two major supermarkets dominating the retail grocery landscape, and an increasingly unhappy supply chain, became far more complex.

## I. The ACCC Grocery Inquiry

While tensions regarding the market size and power of the MSCs have been simmering for many years in Australia,<sup>10</sup> a crucial milestone in tracing key events and actors in the regulatory discourse that led to the FGCC is the inquiry of the ACCC into retail grocery prices which reported in 2008. The impetus was government concerns about inflationary pressures and political debate about costs of living. Thus the focus was squarely on the level of concentration and associated degree of competition between grocery retailers and, in particular, the question whether the largely duopolistic market structure was responsible for rising consumer prices.

After a substantial investigation, the ACCC produced a voluminous report in which it concluded that competition was ‘workably competitive’ and structural problems in the sector were overstated.<sup>11</sup> There was strong price competition on key value items, accentuated by competitive responses by the MSCs to the expansion of the global discounter, Aldi.<sup>12</sup>

The increase in grocery prices above headline inflation was found to be referable to factors other than the size and operations of the MSCs – supply and demand changes in international and domestic markets, increases in production costs and domestic weather conditions.<sup>13</sup> Independent retailers were said to be competing on convenience and service and, to the extent they were struggling to compete on prices, this was attributed to the pricing practices of the monopolistic wholesaler Metcash.<sup>14</sup>

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<sup>10</sup> Such tensions can be traced back at least to parliamentary inquiries in the late 1990s. See, e.g., House of Representatives Standing Committee on Industry, Science and Technology (1997) *Finding a Balance: Towards Fair Trading in Australia*; Joint Select Committee on the Retailing Sector (1999) *Fair Market or Market Failure: A Review of Australia's Retailing Sector*.

<sup>11</sup> ACCC 2008 Grocery Inquiry, p. 212.

<sup>12</sup> ACCC 2008 Grocery Inquiry, p. 97.

<sup>13</sup> ACCC 2008 Grocery Inquiry, pp. 29-40.

<sup>14</sup> ACCC 2008 Grocery Inquiry, p. 144-45.

Moreover, the report concluded that there was nothing 'fundamentally wrong' with the grocery supply chain.<sup>15</sup> While the MSCs had significant buyer power, the competition between them prevented retention of a large part of the benefits from the wholesale prices they extracted; at least some of these benefits were flowing to consumers by way of lower prices.<sup>16</sup>

In relation to farm-gate prices for fresh produce the ACCC did not find any evidence to suggest that the MSCs were acting in an anti-competitive way when dealing directly with suppliers. While the bargaining power of the MSCs was strong in these instances, for a good proportion of fresh products, farmers were said to have the option of selling to export markets or wholesale markets (which in turn supply independent supermarkets, butchers and greengrocers). This was seen to lower the bargaining power of the MSCs.<sup>17</sup> The ACCC accepted that 'many Australian farmers are suffering and low prices for their product may be a significant contributing factor'.<sup>18</sup> However, it was of the view that 'the extent to which the market power of retailers contributes to this problem is limited'.<sup>19</sup>

For packaged groceries, the ACCC conceded that farmers receive a small percentage of the final price charged to consumers; however, it saw this as typically reflecting the other costs that arise in the supply chain, including capital-intensive processing, packaging, advertising, delivery and retailing.<sup>20</sup> The price that farmers receive for many agricultural commodities, particularly products such as sugar and wheat, is set by international supply and demand conditions. Further, while the buyer power of the MSCs may affect individual competitors adversely, the ACCC emphasised that its concern was to protect competition, not individual competitors, and there was no significant evidence to suggest that innovation or competition at the supplier level had been damaged.<sup>21</sup>

The ACCC also pointed out that consumers can benefit from buyer power in the form of lower prices and what is more, consumers constrain the choices that the MSCs make. Consumers do not readily accept all private label products, which therefore limits options and lowers the MSCs' bargaining power in those areas.<sup>22</sup> For those producers that have strong brands with consumer loyalty, the ACCC concluded that there are unlikely to be any concerns about the bargaining power of the MSCs, as these producers hold 'must have' products for retail stores.<sup>23</sup>

In conclusion, the ACCC made a series of recommendations. However, owing to the Commission's findings, giving the sector an almost clean bill of competitive health, the recommendations were not extensive and in some respects could have been characterised as no more than tinkering around the edges. Planning and zoning issues had been identified as a significant barrier to entry in grocery sector. The ACCC therefore recommended that all appropriate levels of government consider ways that decisions regarding the allocation of retail space for supermarkets, with a particular focus on their

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<sup>15</sup> ACCC 2008 Grocery Inquiry p. xiv.

<sup>16</sup> ACCC 2008 Grocery Inquiry, p. 92.

<sup>17</sup> ACCC 2008 Grocery Inquiry, p. 308.

<sup>18</sup> ACCC 2008 Grocery Inquiry p. xx.

<sup>19</sup> ACCC 2008 Grocery Inquiry p. xx.

<sup>20</sup> ACCC 2008 Grocery Inquiry, p. xx.

<sup>21</sup> ACCC 2008 Grocery Inquiry p. xx.

<sup>22</sup> ACCC 2008 Grocery Inquiry, p. xxi.

<sup>23</sup> ACCC 2008 Grocery Inquiry, p. xxi.

impact on competition between supermarkets in a given area, may or may not be facilitating the entry of new supermarkets in to that area.<sup>24</sup> The ACCC also recommended the introduction of a mandatory, nationally-consistent pricing regime for standard groceries be introduced for 'significant supermarket stores'.<sup>25</sup>

The majority of the ACCC's recommendations were directed at the HCC. These included:

- a review of the CCA so as to provide for civil pecuniary penalties and infringement notices in relation to Part IVB provisions, thereby allowing for stronger enforcement mechanisms in relation to the HCC;
- amendments that would increase transparency, clarity and certainty around transactions in the supply chain;
- amendments that would allow for pooling and price averaging;
- the subsidising of costs by Government for parties involved in dispute resolution under the HCC; and
- the implementation of further education initiatives.<sup>26</sup>

Consistent with the wide divergence of views on most aspects of the supermarket debate, stakeholder views on whether or the degree to which the ACCC 'got it right' in the 2008 inquiry are sharply divided.

Some representatives from the independent retailer sector interviewed for this research are of the view that the ACCC got it 'totally wrong'.<sup>27</sup> However, there are also concessions by some that the terms of reference were narrow (with an arguably undue focus on pricing, and thus not directly concerned with considerations such as diversity and choice)<sup>28</sup> and that the Commission struggled to elicit sufficient evidence from suppliers. The impact of the latter is attested to in the account given by Graeme Samuel AC, Chairman of the ACCC at the time of the inquiry:

*The problem was that individually, no one was telling us. So what we did was, we went out with a media release. We went out with private correspondence and we went out with me going on radio, saying, "We guarantee you, absolute confidentiality. "Just come and tell us..." No one told us...<sup>29</sup>*

Lack of information as the reason for lack of findings on certain matters in the inquiry is clearly

<sup>24</sup> ACCC 2008 Grocery Inquiry, p. 9.

<sup>25</sup> ACCC 2008 Grocery Inquiry, p. 14.

<sup>26</sup> ACCC 2008 Grocery Inquiry, p. 13.

<sup>27</sup> Transcript of interview, CEO of MGA, p. 15; Transcript of interview, CEO of an independent supermarket, p. 19.

<sup>28</sup> Transcript of interview, CEO of MGA, p. 15.

<sup>29</sup> Transcript of interview, Graeme Samuel, p. 11.

reflected in the conclusions of the ACCC's report:

*Given the lack of detail in the allegations made and specific denials by well-informed growers, the ACCC considers it unlikely that this kind of conduct [referring to unfair trading practices] occurs otherwise than in exceptionally rare circumstances. If specific complaints are made, the ACCC would investigate the matter under the unconscionability provisions of Part IV of the Trade Practices Act. What is clear, however, is that some growers have concerns, legitimate or otherwise, in their relationships with the MSCs. In the absence of specific complaints, the ACCC will not be able to address these issues.<sup>30</sup>*

The most commonly cited reason for apparent supplier reticence to speak out against the MSCs, both then and since, was and remains fear of commercial retribution by their major buyers.<sup>31</sup> This, according to an ACCC official, could include a so-called 'supply holiday', that is, 'if you complain, if you make a nuisance of yourself, then your supply is cut off'.<sup>32</sup>

While such hesitance is mostly associated with small suppliers, others do not see it as so confined – as implicit in the remarks of a senior representative of AMWU: 'when you've got the likes of Coca Cola and Heinz and Mondelez and companies of that size that aren't keen to come out and speak against the supermarkets, to me that's got to ring alarm bells.'<sup>33</sup> That large suppliers would be just as, if not, more reticent than small suppliers to 'rock the boat' is borne out by the observations of John Noble, Director of British Brands Group, a representative association for large suppliers in the UK (where similar issues have plagued supermarket supply chains):

*...talking about unfair trading practices – very, very few, even the largest suppliers would go to officials or MPs talking about unfair trading practices by their retail customers because that would be death to them. Everything with their retail customers is commercial, it's between us and them, it's confidential: "That's our business not your business, policy maker, keep your nose out."<sup>34</sup>*

In explaining further why large suppliers take this stance, Noble told us:

*The UK market is a huge market; the bigger you are the more you have to lose. It doesn't matter whether you have must-stock brands or not - I think there are relatively few must-stock brands anyway, and companies with them will have other products in their portfolio including small up and coming brands as well. The retailer has the power to target the*

<sup>30</sup> ACCC 2008 Grocery Inquiry, p. 252. Notably in its 2004 report on how the SCOP was working in the UK, the OFT appeared to have been plagued by similar difficulties in eliciting detailed information from suppliers about their grievances and concluded that '[t]his made it impossible to draw any firm conclusions as to how individual supermarkets are operating under the Code.' See OFT press notice 28/04, *OFT publishes supermarkets code review*, 20 February 2004. See also the CC's press notice in relation to progress in its 2006-2007 inquiry noting that while 'many general assertions [had been] made about the activities of and the power held by supermarkets' had been made, 'we have not received as much specific evidence about unfair treatment of suppliers as we might have expected.' Cited in Antony Seely, 'Supermarkets: competition inquiries into the groceries market' SN03653, 2 August 2012, p. 23.

<sup>31</sup> Transcript of interview, Gary Dawson, p. 15.

<sup>32</sup> Transcript of interview, senior representative of the ACCC, p. 13.

<sup>33</sup> Transcript of interview, senior representative of AMWU, p. 32.

<sup>34</sup> Transcript of interview, John Noble, British Brands Group, p. 17.

*weaker brands saying, "Well I'm very sorry, I'm not going to take your promotion, I'm not going to take your new product," or "Yeah, well that's going down on the bottom shelf." ... So even [these suppliers are] extremely vulnerable. And public companies are obviously more vulnerable than private ones, I would say. ... You suddenly get de-listed – one of your big brands gets de-listed, your shareholders will know all about that. (An ACCC official makes a similar point, citing an example of 'one enormously large supplier [who] came to us and basically said "our margins are such that if there is a decrease in our exposure in any one of these majors then we'll go backwards very quickly" ... so they're just as vulnerable.')*<sup>35</sup>

However, as indicated by his comments cited above, Samuel AC has a somewhat different perspective on the 'real' reason for supplier reluctance to speak out, at least at the time of the ACCC inquiry. On his account, representative associations – particularly those representing primary producers – openly made assertions about harsh or oppressive tactics employed by the MSCs against their members. But when the ACCC sought corroborating information from individual suppliers, they encountered considerable stone walling or silence. The reason for this, according to the former Chairman, was that:

*In fact, what they did do, was in Canberra, they said exactly the opposite. They said there is not an issue. And they said if we had a preference to dealing with anyone, it would be to deal with Coles and Woolworths, not to be dealing with Metcash and not to be dealing directly with the markets... none of them, in Canberra, in confidence, would – had a word, a negative word to say about Coles and Woollies...they [referring to individual suppliers] didn't want to say publicly, we actually like dealing with Coles and Woollies, we don't have a problem with them. Yeah, "they're tough but fair" was the constant explanation given, "because if we do that, other suppliers are going to be irritable, because they're saying you are lessening our negotiating capacity, right?" Particularly in the political scene...the groups representing the growers, were out there arguing how bad and nasty Coles and Woolworths, as the major buyers, were. And so you [referring to an individual supplier] would be making statements, basically out of school, from the point of view of your colleagues.*<sup>36</sup>

While some retailer and supplier representatives are critical of the accuracy or completeness of the conclusions reached in the ACCC Grocery Inquiry, it is worth noting that the ACCC's findings were largely consistent not just with the submissions of the MSCs themselves but with the submissions from the peak supplier body, the AFGC. The AFGC acknowledged in its submission that, 'undoubtedly the market power of the retailers and wholesalers has increased'; however it viewed

<sup>35</sup> Transcript of interview, senior representative of the ACCC, p. 14.

<sup>36</sup> Transcript of interview, Samuel, p. 15. See also the statement in the ACCC 2008 Grocery Inquiry report '... there was very little in the way of specific evidence of harsh or unconscionable conduct by the MSCs, or specific incidents of apparent abuse of their market position by the MSCs. In fact, many growers and suppliers summonsed to attend the hearings by the ACCC provided positive reports about the conduct of the MSCs, which would not normally be brought to the public's attention' (pp. 326-7).

this as only underscoring the importance of suppliers having a healthy business relationship with 'all major retailers and wholesalers'.<sup>37</sup> While the AFGC conceded the disparity in market power, it stated that it was 'unaware of behaviour between trading partners which contravenes the provisions of the Trade Practices Act or for which amendments to the Act would improve the competitiveness of the system.' It concluded that 'a competitive food and grocery retail sector exists in Australia and operates to deliver competitive prices for the consumer'.<sup>38</sup> Consistent in many respects with the subsequent findings of the ACCC, the AFGC attributed the challenges in the market to external factors such as drought and high international commodity prices,<sup>39</sup> the arrival of new players in the form principally of Aldi, and the increased vertical integration of the MSC supply chains.<sup>40</sup> It made no complaint relating to or even mention of fair trading or unconscionability-related issues or concerns in its account.

As discussed below, in the years following 2008 many of the ACCC's findings pertaining to competition at the horizontal level of the grocery market were borne out. In contrast, its assurances about supply chain relations appear, in hindsight, to have misplaced or, as some would argue, under-informed. In ensuing years, these concerns began to crystallise and the focus of official and public attention shifted firmly from the horizontal to the vertical dimension of the sector.

Developments post-2008 are traced in the sections that follow. While hindsight's benefit is to be acknowledged, those developments do suggest that the conclusions reached in the milestone inquiry warrant a mixed scorecard. As ruefully observed by one observer:

*I think that the ACCC got it broadly right in 2008 because events have shown that left for itself, there was enough competition in the market ... and it was probably less correct on the – not that it was less correct but there clearly was – there were issues in the supply chain..<sup>41</sup>*

## II. Intensifying competition and external influences

Almost immediately after the ACCC Grocery Inquiry there were developments at the retail level of the grocery sector that saw a substantial increase in competition amongst retailers. The competition manifested in a significant fall in real food prices<sup>42</sup> (including outbreaks of price wars on staples such as milk, bread and eggs) and strong pressure on MSC earnings before interest and tax margins, as well as reports of financial difficulties for Metcash and its banner retailers, the Independent Grocers of Australia (IGAs).<sup>43</sup>

While there is likely to be a myriad of factors that contributed to this uptick in competition, one of the

<sup>37</sup> AFGC public submission to ACCC 2008 Grocery Inquiry, 11 March 2008, p. 6.

<sup>38</sup> AFGC public submission to ACCC 2008 Grocery Inquiry, 11 March 2008, p. 3.

<sup>39</sup> AFGC public submission to ACCC 2008 Grocery Inquiry, 11 March 2008, p. 2.

<sup>40</sup> AFGC public submission to ACCC 2008 Grocery Inquiry, 11 March 2008, p. 11.

<sup>41</sup> Former senior representative of the UK OFT, p. 14.

<sup>42</sup> Just over five years on from the ACCC Grocery Inquiry, food and non-alcoholic beverage prices were tracking at 1.3% compared to inflation at 2.6%. See Woolworths Limited, 'Response to Competition Policy Review' (June 2014), p 15, citing Australian Bureau of Statistics (2014), table 7.

<sup>43</sup> Carrie LaFrenz, 'Watchdog urged to examine grocery market', *SMH*, 14 April 2008.

few matters on which all stakeholders in the sector agree is that two factors were particularly instrumental. The first was the turnaround in Coles's performance following its acquisition by Wesfarmers, and the second was Aldi's consolidation of its status as a serious player in the sector.

### (a) The Wesfarmers turnaround

When Wesfarmers made the acquisition, in late 2007, the Coles business was in a parlous state. In September of that year, despite Coles' management suggesting that the ongoing sales decline had been stemmed, the general response from market analysts was far from optimistic. Credit Suisse announced that it had 'our FY08 down by 8.4 per cent in light of the lack of sales momentum and robust competitive environment'.<sup>44</sup> UBS went further, revising down its 2007-08 forecast by 16%.<sup>45</sup>

In the company's 2007 Annual Report CEO John Fletcher attributed the problems in Coles' supermarket division to the decision to rebrand Bi-Lo stores to Coles stores, saying that the execution of the initiative had been poor and did not deliver 'the planned customer value proposition'.<sup>46</sup> However news reports at the time indicate the division had been in 'state of upheaval' for at least the previous three years.<sup>47</sup> After the retirement of the company's long-serving supermarket CEO Alan Williams, in 2003 British executive Steven Cain was brought in, but stayed in the role just 14 months before being replaced by former Senior Vice President of Merchandising and Marketing at Wal-Mart in Canada, Hani Zayadi, who in turn soon was replaced by Peter Scott in March 2006. Scott was dismissed later that same year, allegedly for having unacceptable dealings with suppliers, including accepting gifts in return for favourable treatment.<sup>48</sup>

Coles' decline has also been attributed to a loss of customer focus as external pressures mounted. By 2007 Coles was not only struggling to achieve the profit targets Fletcher had announced to the market, but to match the big supply chain investments that Woolworths had already made. Having modernised its supply chain, Woolworths was sharing the resultant savings between its bottom line and lower supermarket prices. The effort that Coles was putting into restructuring its supply chain was said to have distracted from the need to maintain and increase investment in day-to-day operations so as to retain and increase its customer base. Macquarie Bank's Greg Dring was reported as suggesting that any profits Coles made at this time came at an unsustainable cost to service and quality.<sup>49</sup>

Archie Norman, the former chairman of Independent Television (ITV) and advisor to Wesfarmers on the acquisition and transformation of Coles by Wesfarmers, reportedly believed the acquisition succeeded in part because of the poor state of the business at the time:

*... the stores were dirty, the shelves were cluttered, queues were long and the head office*

<sup>44</sup> Elizabeth Knight, 'Few believe Coles story', *Brisbane Times*, 21 September 2007.

<sup>45</sup> Elizabeth Knight, 'Few believe Coles story', *Brisbane Times*, 21 September 2007.

<sup>46</sup> Coles Group Limited, *Annual Report (2007)*, p. 3.

<sup>47</sup> Rebecca Urban, 'Coles sacks supermarkets executive over supplier deals', *The Age*, 18 November 2006.

<sup>48</sup> Rebecca Urban, 'Coles sacks supermarkets executive over supplier deals', *The Age*, 18 November 2006.

<sup>49</sup> Malcolm Maiden, 'Coles' slump teaches the lesson that long-distance relationships can be costly', *The Age*, 22 September 2007.

*bureaucratic. Typically, fresh produce was seven-to-eight-days old by the time it arrived in the store and shops held more than five days' worth of stock.<sup>50</sup>*

Others reflecting back recall too that there were 'egregious' inefficiencies in the supply chain, issues that just had to be tackled if Coles was to resurrect itself:

*My perception is that in the period 2008 to 2012, there were just such egregious problems in the supply chain, with waste and other issues. If you talk to the people in Coles about what problems they were trying to solve, most of [these] problems were things that it was in everybody's interest to solve. For example, instead of somebody producing a pallet of goods, they produced a single box and send a whole pallet with one box on it, which is hugely inefficient. The retailer then wouldn't have the supplies in on the days they were supposed to have them in. This had a negative impact on consumers. So I think at that stage there was probably a need to get regularity and order into the system, so that when you said we're going to have Doritos on the shelf in 700 supermarkets ... that you actually have a system in place to deliver that, and not have it in 500 of them and 200 of them missing.<sup>51</sup>*

Following the acquisition, such was the turnaround under new leadership that, by 2013 Coles had outperformed Woolworths for 18 consecutive quarters, with revenue for the food and liquor business growing at a compound annual growth rate of 5.6% from \$28.8bn in 2009 to \$35.8bn in 2013.<sup>52</sup>

## (b) The Aldi incursion

The German grocery chain Aldi, having begun as a collaboration between two brothers in the Ruhr region in the 1940s, had grown into a 'global retailing powerhouse' by 2011 with over 8000 stores operating in 20 countries across three continents, and ranking as the 8<sup>th</sup> largest retailer in the world.<sup>53</sup> However despite its size and success, relatively little is known about this very private company - a fact attributable to the extreme disdain the company's founders had to any form of publicity. According to a close confidante of the family, they believed Aldi was successful because its management did not allow themselves to be distracted by the need to engage with the business press or the public.<sup>54</sup>

Former Managing Director of the company's Australian operations, Michael Kloeters denied the company was intentionally secretive. Instead Kloeters' is said to have attributed the company's repeated turning down of invitations for interviews or to attend industry events to nothing more than

<sup>50</sup> Archie Norman, 'Against the odds Wesfarmers has taken Coles to the top of the supermarket tree', *SMH*, 29 January 2013.

<sup>51</sup> Transcript of interview, former senior representative of the UK OFT, p. 16.

<sup>52</sup> Richard Gluyas, 'How Ian McLeod turned Coles around', *The Australian*, 20 February 2014.

<sup>53</sup> Tom Osegowitsch and Markus Goelz, University of Melbourne case study, *Aldi in Australia*, October 2011 (Osegowitsch and Goelz, 2011), p. 4.

<sup>54</sup> S. Amann and j. Tietz, 'A secretive family's success. What makes Aldi discount empire tick', *Der Spiegel*, 3 March 2000, cited in Osegowitsch and Goelz, 2011, p. 4.

a lack of time on the part of Aldi executives.<sup>55</sup>

As an interviewee who consults to grocery businesses notes, Aldi is culturally different to the MSCs:

*It just wants to run a supermarket and it is actually law-abiding and tries to assist where it can and do the right thing, and sends a very strong cultural message that, “we’re just here to do our job and do the right thing,” and really doesn’t like the Australian environment in terms of ... back and forth in the media, playing media games which its competitors do. It doesn’t give political donations at all, it doesn’t have lobbyists working for it. It doesn’t have anything to do with any of that, it wants to just go about its role.<sup>56</sup>*

In 2001 Aldi entered the Australian market. Starting with two stores in Sydney, in its first five years it was able to secure only a small foothold in the market. However, from the late 2000s its investment and staying power began to show signs of paying off, such that by 2016, in the space of 10 years since 2006, its market share had almost tripled, from 3.1% to 12.5%,<sup>57</sup> with approximately 450 stores nationwide.<sup>58</sup> This was an outcome that may not have surprised Kloeters who reportedly said after studying Australia’s markets and before agreeing to launch the company in Australia, supermarket operators ‘had so much fat here in Australia. It was unbelievable’.<sup>59</sup> Aldi’s strategy is almost entirely price-based. A lean and focused organisation that offers high quality but limited range, most of which are private label products,<sup>60</sup> Aldi is an aggressive discounter. At the time of the ACCC Grocery Inquiry, the competitive price pressure that Aldi was exerting on MSC pricing was more than evident.<sup>61</sup> By 2015, that pressure had intensified considerably – industry reports recording Aldi’s prices on comparable products as 15% cheaper than its major rivals.<sup>62</sup> In late 2016 a Fairfax Media study of Aldi, Woolworths and Coles supermarkets in one suburb found that even on branded products such as Coke, Tim Tams and Weet-Bix, Woolworths shoppers were paying 12% more and Coles shoppers an extra 14%, when compared to those shopping at Aldi.<sup>63</sup>

However it is arguably in private label goods that Aldi has had the biggest impact on consumer spending habits, and with it the grocery supply market. Both Coles and Woolworths acknowledge that Aldi was the catalyst for change in this segment. While Australia, a country that had traditionally shunned private label products as unappealing and sub-standard, is still behind European and North American consumers in this area, Aldi has managed to convince consumers that private label does not necessarily mean lower quality. By 2011 private label sales made up 23% of all

<sup>55</sup> Osegowitsch and Goelz, 2011, p. 4.

<sup>56</sup> Transcript of interview, interviewee that consults to / advises grocery businesses, p. 13.

<sup>57</sup> J. Walker, ‘Inside ALDI’, *Business Review Weekly*, 17 July 2003, cited in Osegowitsch and Goelz, 2011, p. 5.

<sup>58</sup> Osegowitsch and Goelz, 2011, p. 14.

<sup>59</sup> J. Walker, ‘Inside ALDI’, *Business Review Weekly*, 17 July 2003, cited in Osegowitsch and Goelz, 2011, p. 5.

<sup>60</sup> Osegowitsch and Goelz, 2011, pp. 7-8.

<sup>61</sup> An extensive study of MSC local store pricing conducted by the ACCC found that consumers shopping at a Woolworths store with an Aldi within 1 km paid prices that were on average around 0.7 per cent lower than the prices paid by consumers at a Woolworths store without an Aldi within 5 km. And that consumers shopping at a Coles store with an Aldi within 1 km paid prices that were on average around 0.8 per cent lower than the prices paid by consumers at a Coles store without an Aldi within 5 km. The report concluded that Aldi appears to have a far more significant effect on MSC local store pricing across the products it stocks than a competing MSC. See ACCC 2008 Grocery Inquiry, p. 97.

<sup>62</sup> David Potts, ‘Winners and losers in the trolley wars’, *SMH*, 28 July 2015.

<sup>63</sup> Madeleine Heffernan, ‘Woolworths, Coles, Aldi: which is cheapest for branded products?’, *SMH*, 7 November 2016.

supermarket revenue in Australia, up 13% from 2000.<sup>64</sup> As the General Manager of Woolworths' private label division is reported to have observed, 'Aldi actually improved the quality stakes and kept the prices down'.<sup>65</sup> In response Woolworths upgraded 75% of its private label products, while Coles completely redesigned its entire range.<sup>66</sup> The two continue to rework and revamp these lines in an attempt to capture a share of the market that Aldi has invigorated.<sup>67</sup>

Aldi has a relatively simple, flat management structure. It has no marketing, public relations, human resources or legal departments, and instead relies on limited outsourcing.<sup>68</sup> According to Kloeters:

*To save costs we don't have a public relations department. You can't be half pregnant; if you do a decent PR then it is going to cost you a lot of money – or you don't do it at all. It's very difficult to be in-between.*<sup>69</sup>

With regard to promotions, Aldi is said to shun 'marketing gimmicks', relying primarily on its website, hard copy catalogues and word of mouth.<sup>70</sup> In 2008 Aldi's Australian advertising expenditure was estimated at less than 0.5% of annual turnover.<sup>71</sup> The company does not offer loyalty programs or fuel discounts, with management reportedly stating that Aldi, 'prefers to focus on offering customers the best-quality products at the lowest possible price'.<sup>72</sup>

As a privately owned company, Aldi has the advantage of being able to make business decisions that may seem counter-intuitive or that will have a negative short term impact but positive long term benefits outside of the public spotlight and without having to answer to shareholders.<sup>73</sup>

As should be evident from just this brief description, Aldi introduced a whole new dynamic into the Australian grocery sector and its aggressive expansion heralded a shake up of the likes not previously seen since the MSCs had settled into their joint domination of much of the sector. The combined import of this development, together with Coles' turnaround, is neatly captured in this reflection on the period by a former AFGC CEO:

*...very big changes occurred, well, really effectively just after that enquiry handed down its findings [referring to the ACCC Grocery Inquiry], so you had the takeover of Coles by*

<sup>64</sup> Private label growth was also affected by the global financial crisis, with Woolworths reporting a growth in sales at nearly double the rate of branded goods at this time, Eli Greenblat, 'Private labels set to fill more of every trolley', *Sydney Morning Herald*, 6 August 2010, cited in Osegowitsch and Goelz, 2011, p. 19.

<sup>65</sup> B Speedy, 'In-house labels a big hit for Coles', *The Australian*, 18 September 2010, cited in Osegowitsch and Goelz, 2011, p. 19.

<sup>66</sup> B Speedy, 'In-house labels a big hit for Coles', *The Australian*, 18 September 2010, cited in Osegowitsch and Goelz, 2011, p. 19.

<sup>67</sup> Osegowitsch and Goelz, 2011, p. 19.

<sup>68</sup> Richard Dunford, Ian Palmer and Jodie Benveniste, 'Strategy for successful entry into a concentrated and highly competitive market', in *Australian and New Zealand Academy of Management Annual Conference*, Australia, 7-10 December 2005, p. 8.

<sup>69</sup> J. Walker, 'Inside ALDI', *Business Review Weekly*, 17 July 2003, cited in Osegowitsch and Goelz, 2011, p. 5.

<sup>70</sup> Aldi website 2011, cited in Osegowitsch and Goelz, 2011, p. 11.

<sup>71</sup> S. Maseeha, P. Indu, D. Purkayastha, 'Aldi: The European hard discounter's strategy in Australia', ICMR Centre for Management Research, ECCH case 308-375-1, 2008, in Osegowitsch and Goelz, 2011, p. 11.

<sup>72</sup> . Maseeha, P. Indu, D. Purkayastha, 'Aldi: The European hard discounter's strategy in Australia', ICMR Centre for Management Research, ECCH case 308-375-1, 2008, in Osegowitsch and Goelz, 2011, p. 11.

<sup>73</sup> Richard Dunford, Ian Palmer and Jodie Benveniste, 'Strategy for successful entry into a concentrated and highly competitive market', in *Australian and New Zealand Academy of Management Annual Conference*, Australia, 7-10 December 2005, p. 6.

*Wesfarmers, a very significant shift, coinciding with Aldi building a real presence, so they started here in 01 but was really only by 09, 10, that they were building influential presence. Both of those, I think, created quite a shift in the competitive reality at the retail level.<sup>74</sup>*

A MSC representative described the 'Aldi effect' on the Australian retail grocery market in the following terms:

*Aldi has reset expectations of value in the Australian market because up until then Homebrand was seen as kind of cheap and nasty quality and Aldi basically provided customers with a low priced alternative that was good quality, and so they have effectively reset how customers see value in the Australian context, so we have to be able to compete with that. We can't be seen as being really expensive relative to Aldi.<sup>75</sup>*

It is notable that the incursion of Aldi and other discount chains such as Lidl have had a similar transformative effect in the UK, shaking up the traditional incumbents and changing consumer perceptions on value. Overall the impact has been to concentrate the minds of all retailers increasingly on price. As the head of the supplier organisation, the British Brands Group, recounted in his interview with us:

*.. I think price has always been at the fundamental level of supermarket competition with the exception of Waitrose and Marks & Spencer's. Everybody else, price – you've got to win on price. And that was all going swimmingly I think for the big companies until the Aldis and Lidl came in with their much simpler business models and suddenly their low prices were looking positively high, and I think that penny dropped after the 2008, 2009 crash and I think here we were talking earlier about reputation, when you get that kind of a disparity in consumer pricing then people begin to think, "I always thought you were the cheapest but actually where's my money going?" I think there's been a big shift there, and I think once that shift takes place and certainly while Aldi and Lidl are always promoting their quality, so making the proposition that you're getting the same quality you had before but it is 20-30% cheaper, then people will stick with that proposition.<sup>76</sup>*

### (c) Vertical reverberations

The intensification of retail competition undoubtedly had ramifications up the supply chain, as the MSCs strove to make cost savings that would allow for lower prices and corresponding competitive advantage over rivals, but especially over Aldi and each other. Some of those savings were derived internally (through staff reductions, for example) but a large proportion of them involved being tougher in supplier negotiations on price, as well as demanding supplier support or compensation in various forms (for promotions, marketing, shrinkage or wastage, for example, or just to cover profit

<sup>74</sup> Transcript of interview, Gary Dawson, p. 18.

<sup>75</sup> Transcript of interview, MSC representative, p. 6.

<sup>76</sup> Transcript of interview, John Noble, British Brands Group, p. 10.

gaps), in some instances with threats of adverse consequences if demands were not met.<sup>77</sup> As one experienced grocery competition commentator observes, 'if you're in a very competitive industry and you want to be more cost competitive, you have to look at your upstream inputs, and the biggest input for the supermarkets is the cost of the food supplies that they buy'.<sup>78</sup>

It was noted by commentators around this time that the MSCs were requiring suppliers to make 'payments above and beyond that negotiated in order to stock their products', that they were imposing 'penalties that do not form part of any negotiated terms of trade'; the MSCs were not paying agreed prices and they were discriminating in favour of their own home-brand products.<sup>79</sup> Along similar lines, in its submission to the Harper Review, the Australian Industry Group reported:

*... very fierce bargaining over terms and conditions of supply and many [suppliers] feel they have little opportunity to push back on the dominant bargaining power of the larger supermarkets. For example, suppliers feel they have been coerced over time by the major supermarkets into supplying their branded product for supermarket private label product or not at all. This has the effect of negatively impacting suppliers' capacity to innovate in the market, erosion of brand value and intellectual property.*<sup>80</sup>

This is not to suggest that MSC practices complained of during this period were in some way novel or new. Indeed, industry insiders point out that they had been part of the supermarket-supplier relational landscape for years.<sup>81</sup> A survey of growers conducted by the NSW Farmers Association in mid-2003 found that 60% of respondents feared raising a concern with the MSCs would invite commercial retaliation.<sup>82</sup> According to the MGA CEO, the MSCs have used their 'market power, behaved unconscionably; knowing that what [they were doing] is damaging another person's business ...for 25 years'<sup>83</sup> - a claim underscored by a consultant to suppliers' plea that, 'we don't want expensive court cases, we just want the retailers to stop doing some of the things that for years have been deemed to be normalised behavior.'<sup>84</sup> However, there is also no doubt that as the going got tough amongst retailers in the late 2000s, it got even tougher for suppliers as a result. At the same time there were other factors at play, both in the broader economic environment and, internally, within the MSCs themselves.

#### (d) Macro aggravations

Former AFGC CEO, Gary Dawson, points out that what many official accounts overlook is that following the ACCC Grocery Inquiry there was a rise in the value in the Australian dollar in 2009 and

<sup>77</sup> Transcript of interview, Robert Hadler, p. 16.

<sup>78</sup> Transcript of interview, former senior representative of the UK OFT, p. 15.

<sup>79</sup> See, e.g., Christine Parker, 'ACCC's inquiry into supermarket bullying misses the real issue of duopoly power', *The Conversation*, 19 February 2013.

<sup>80</sup> Ai (Australian Industry) Group submission to the Harper Review, June 2014, p. 51.

<sup>81</sup> Transcript of interview, CEO of MGA; 'we've known it's been going on for 25 years', p. 3.

<sup>82</sup> Evan Jones, 'The Australian retail duopoly as contrary to the public interest', Report for the Fair Trading Coalition, Department of Political Economy, University of Sydney, April 2006, p. 23.

<sup>83</sup> Transcript of interview, CEO of MGA, p. 59.

<sup>84</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 50.

2010, 'spiking to an over parity with the US dollar', and this had two effects.<sup>85</sup> First, 'it dramatically increased import competition at the same time as the retailers, led by Coles, were looking to source greater private label suppliers to compete with branded domestically produced goods.' Second, it 'choked off export markets dramatically for Australian FMCG manufacturers.'<sup>86</sup> So, Dawson concludes, 'you had a combination of intensifying price competition at the retail level at the same time as other structural factors [that meant] greater reliance on the major domestic retailers to shift product' and 'the intensity of that financial vice ... was very very significant.'<sup>87</sup>

Some of the 'other factors' referred to by Dawson had been picked up in the AFGC's 2011-12 Annual Report, noting that the industry was facing a 'perfect storm' of pressures along the length of the supply chain. Such pressures not only included the high Australian dollar making imports significantly cheaper, but also near record high global commodity prices – sugar, dairy, cocoa, coffee, wheat; aggressive supermarket discounting; the increasing regulatory burden that was adding to compliance costs; complex and uncertain labelling requirements; and the introduction of the carbon tax.<sup>88</sup>

### (e) Cultural shifts and UK influences

Some see the toughening in supplier negotiations in the post 2008 period as attributable to a cultural shift occurring within the MSCs during this time. This in turn is attributed by some to the increasing import and influence of senior executives from the UK where the retail grocery environment had been highly competitive for many years.<sup>89</sup> As explained by one senior industry insider:

*...it had been coming for a while but it's almost like it was a tipping point around then [referring to the late 2000s] when it was no longer all about the handshake deal and no longer all about the: "I'm mates with my buyer, we'll go out drinking and we'll have a good time, we'll have this personal relationship". It became much more solidly commercial where it became like a battle of documents: "here's our documents which prove our side of the story, where's your captivating documents?" "Oh, come on, but we shook hands on it." "No, where's your documents?" So it became a much more profit driven, much more hard business, much less good old boys' handshake type industry than it was. ... And, look, some of that of course was*

<sup>85</sup> By July 2011 the Australian Dollar had reached a high of US\$1.10 (see Ausveg.com.au <http://www.tradingeconomics.com/australia/currency>). This was in part due to the on-going weakness of the US dollar, but it was also the result of elevated commodity prices, Australia's relatively high interest rates, and the preparedness of global investors to take on 'risk' in order to enhance returns in the very low-interest rate environment outside Australia. For trade-exposed sectors of the Australian economy, i.e. those competing in the export markets or at home against imports, this created obvious challenges (see Saul Eslake, 'Explainer: What a strong Australian dollar actually means', *The Conversation*, 11 April 2011).

<sup>86</sup> This point was made also in Senate Select Committee, *Australia's Food Processing Sector: Inquiry into Australia's food processing sector*, August 2012, [3.36].

<sup>87</sup> Transcript of interview, Gary Dawson, pp. 18-19.

<sup>88</sup> AFGC, *Annual Report 2011-12*, p. 3.

<sup>89</sup> Eli Greenblat, 'Metcash chief hits out at Coles executives', *SMH*, 3 March 2011; Blair Speedy, 'Coles raids UK retail talent pool for another chief', *The Australian*, 21 May 2009.

*driven simply by the nature of the people who had been brought in to lead the organisations...*<sup>90</sup>

The UK influence was especially notable in Coles' transformation.<sup>91</sup> The 'team of gun retailers'<sup>92</sup> (as they were referred to), assembled by Wesfarmers to rebuild the business, was headed up by Scottish-born Ian McLeod, who Wesfarmers' Chief Executive Richard Goyder had recruited from Halfords, a British car parts and bicycle retailer in May 2008.<sup>93</sup> Prior to his time at Halfords McLeod served as a Director of Asda and as a member of the WalMart Germany Executive Board.<sup>94</sup> The turnaround of Asda was credited to Archie Norman, the Chairman of ITV that advised Wesfarmers on the acquisition, and who remained in an advisory role to Coles for some time after.<sup>95</sup>

The turnaround strategy adopted by then Australia's reportedly highest paid CEO,<sup>96</sup> was very much based on the UK formula for retailer success, a formula of: 'slashing prices and shrinking shelf space to make way for their own home brands.'<sup>97</sup>

As former head of Kellogg Australia Jean-Yves Heude is said to have observed, the relationship between the MSCs and suppliers changed when Wesfarmers took control of Coles in 2008:

*Before that, the way the industry was working was based on what I call the win-win model, where good relationships with people, long term relationships, not aggressive negotiation, was really the golden rule...*<sup>98</sup>

However, according to Heude, once the executives from Britain were brought in to run things, aggression towards suppliers became the rule, leading to tougher negotiations on industry staples and discounting.<sup>99</sup>

McLeod said in an interview that the new strategy at Coles was directly responsive to both political and consumer pressures. On his arrival at the troubled business, he has reported, the feedback from both consumers and 'the government' (possibly a reference to the ACCC Grocery Inquiry) was that

<sup>90</sup> Transcript of interview, Legal Director at the AFGC, pp. 19-20

<sup>91</sup> Although this was not the first time Coles had sought assistance from the UK. In early 2000 Steven Cain, who had been paramount in turning Asda Stores Limited around in the late 1990s, was brought in to aid the ailing retailer. Cain quickly implemented sweeping changes; merging back office operations, centralising business operations and reducing duplication – and with it staff numbers. Despite these achievements however it has been suggested that the pre-Wesfarmers bureaucracy and resistance to change within Coles at that time was the reason he left after just 14 months. See Gary Mortimer, 'Why Australian supermarkets continue to look to the UK for leadership', *The Conversation*, 20 January 2015. In discussing the recent addition of 'Tesco veteran Claire Peters' to the Woolworths team, Mortimer attributed the continued influx of British trained retail executives to our shores to 'the short sightedness of Australian retail management' and 'years of complacency.' He also noted Margarethe Wiersema's research of Fortune 1000 firms in the 1990s, which found that in periods of significant change, bringing in 'new blood' can help where an organisation is struggling with innovation and the need for strategic change. The challenge for Australian MSCs, according to Mortimer, is whether they are willing and able to embrace those changes.

<sup>92</sup> Miranda Devine, 'The big squeeze on small business', *Herald Sun*, 27 November 2011.

<sup>93</sup> Tony Boyd, 'How McLeod turned Coles around', *AFR*, 25 September 2010.

<sup>94</sup> Ian McCleod, executive profile, Bloomberg

<https://www.bloomberg.com/research/stocks/private/person.asp?personId=24928098&privcapId=32606641>

<sup>95</sup> Gary Mortimer, 'Why Australian supermarkets continue to look to the UK for leadership', *The Conversation*, 20 January 2017.

<sup>96</sup> Miranda Devine, 'The big squeeze on small business', *Herald Sun*, 27 November 2011.

<sup>97</sup> Miranda Devine, 'The big squeeze on small business', *Herald Sun*, 27 November 2011.

<sup>98</sup> Andrew Robertson, 'Woolworths under fire from suppliers as ACCC court action proceeds', *ABC News*, 12 February 2016.

<sup>99</sup> Andrew Robertson, 'Woolworths under fire from suppliers as ACCC court action proceeds', *ABC News*, 12 February 2016.

prices were too high.<sup>100</sup> Hence, ‘the first move’ in the turnaround plan was ‘to increase operational efficiency in order to invest in lower prices’.<sup>101</sup> Referring to the ACCC’s findings, he explained:

*... the investigation concluded that the sector was workably competitive. Three or four years later when we started to change our price position, it was described as “intensely competitive”. That is because part of our underlying strategy to turn Coles around was to lower prices.*

*Australia had endured annual food inflation of between 4 and 6 per cent for the best part of 30 years prior to the change of ownership in Coles in 2007. And because we sharpened our prices and pushed harder for the benefit of the consumer, we turned food inflation into food deflation, saving the consumer about 1bn Australian dollars a year.<sup>102</sup>*

## (f) Political rumblings

As a result of the confluence of these developments, one of the key features of the years following the ACCC Grocery Inquiry was that, whereas previously there had been reticence by suppliers (for whatever reason) to speak openly against the MSCs, supplier discontent began to be heard increasingly in Canberra. In political terms, the problem was no longer about high grocery prices and the costs of living for consumers, but about the harsh commercial reality facing, and in some respects the very survival of a large proportion of Australian small business operators in the grocery sector. The proportion of small businesses in this sector is higher than in any other sector of the economy – almost 99% of Australia’s food processors and wholesalers are small to medium sized enterprises.<sup>103</sup>

According to one former senior Coles executive, during that period:

*.. it wasn’t consumers per se that were complaining about supermarkets, it was the small business supplier. You know, in the environment of a higher dollar and sluggish demand, that really saw their margin squeezed, that led to a lot of the complaints. So it was the macro-economic factors, which they couldn’t influence, which were driving them to the wall. But they sought protection from that, the only lever they had, which was to go to the government, say “you’ve got to do something about the supermarkets”.<sup>104</sup>*

These voices were heard loud and clear in the public and political arena. One explanation given for this by a MSC representative is that when small businesses are affected by market dynamics, there is ‘a lot of emotion’ involved. It is not as if large suppliers are ‘any less passionate about their businesses’ but, he ruefully remarked, ‘to a small supplier, take their product out of the range, it’s like

<sup>100</sup> Mike Dawson, ‘Talk with Coles legend Ian McLeod’, *German Retail Blog*, 4 December 2014.

<sup>101</sup> Mike Dawson, ‘Talk with Coles legend Ian McLeod’, *German Retail Blog*, 4 December 2014.

<sup>102</sup> Mike Dawson, ‘Talk with Coles legend Ian McLeod’, *German Retail Blog*, 4 December 2014.

<sup>103</sup> Bruce Billson, ‘Speech to Committee for Economic Development of Australia Lunch’ (Speech, Melbourne, 9 May 2014).

<sup>104</sup> Transcript of interview, Robert Hadler, pp. 9-10

killing their babies ... and that's why you get much more public awareness and noise'.<sup>105</sup> Another MSC representative pointed out that the media plays a crucial role in this dynamic:

*...the media's very powerful in the retail sector and ... [in] bringing select issues to the fore and, of course, interest groups are very well aware of that ... [I]n a smaller market the media people that cover this area, the politicians that cover it and the interest groups are a lot smaller and so it's easier, I think, to synthesise things into key messages and pick an interest group or a voice that can really get that, I suppose, amplification quite quickly in this sector and the general population is very, very interested in it.<sup>106</sup>*

By contrast, she pointed out, it is difficult for the MSCs to get their own 'voice' heard in the media in the same way, and in particular, a voice that enables them to bring to public attention their initiatives in supporting small suppliers, including farmers:

*...often our media people say it's not in our interest to put across our view as our own view, we can speak as a collective through other industry bodies ... and I find that a shame but because a supermarket is perceived straight away as a powerful, I suppose, corporation that is probably simply profiteering that – although people love Coles and Woolies as supermarkets, they love shopping there, they don't want to hear their voice in the media in that way ... the advice we get is that it will be viewed cynically no matter what we say.<sup>107</sup>*

However, it wasn't just 'macro-economic factors' responsible for the growing chorus of supplier discontent. It is undeniably also the case that in the five years after the ACCC reported on the sector, the intensification of competition led the MSCs not only to get tough in their negotiations but also to rationalise their number of suppliers. Suppliers were not only being hurt, they were being eliminated. As McLeod rather understatedly recounted in 2014:

*We have had to rationalise our supplier base by around 20 per cent over the last five years because we carried several thousand too many products on our shelves. Obviously some will have benefited from this decision, and others will have lost out.<sup>108</sup>*

Adding, in response to a question about supplier bitterness towards Coles:

*Also, I guess that, if you are a big player in a market place, then you are inevitably going to be subject to a degree of criticism.<sup>109</sup>*

The difficulty for policymakers and the political challenge in this environment was and will remain that while intensified retail competition meant a harder life for some suppliers, there were others that were benefitting and, inevitably, it was only the voices in the former camp that were being heard in the call for action:

<sup>105</sup> Transcript of interview, MSC representative, p. 24.

<sup>106</sup> Transcript of interview, MSC representative, p. 7.

<sup>107</sup> Transcript of interview, MSC representative, p. 18.

<sup>108</sup> Mike Dawson, 'Talk with Coles legend Ian McLeod', *German Retail Blog*, 4 December 2014.

<sup>109</sup> Mike Dawson, 'Talk with Coles legend Ian McLeod', *German Retail Blog*, 4 December 2014.

*...for every supplier who complains about losing a contract, there's at least one more supplier that's so busy hiring people, building plans and doing other stuff that they don't have time to talk to anybody let alone complain, whereas the people who do not win the contracts are less busy and very disgruntled. So you get this asymmetry, because supermarket prices have been falling, sales have been going up. My understanding is that the percentage of Australian produced food and groceries has gone up... as a result of this increased competition. And they may be busier at lower prices, but they're still busier, and therefore there's a good news story about that competition that's often missing from public comment on the sector...<sup>110</sup>*

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<sup>110</sup> Transcript of interview, former senior representative of the UK OFT, p. 15.

## 5. Immediate catalysts

In this Part of the report we explore how critical events in the dairy sector between 2010 and 2012 created the political conditions and momentum for regulatory action. We analyse how and why these events had salience amongst the general community and in turn how this, together with political pressures, catalysed industry and in turn government to act.

However, in order to understand how and why the dairy sector loomed large in these developments, it is necessary first to go back in time. The development and implementation of NCP as an element of wide ranging micro-economic reforms by the Hawke-Keating Labor Governments in the 1990s, particularly with regard to deregulation, had far ranging implications for Australian business and industry. The implications of deregulation for primary producers and for our purposes, for the dairy industry in particular, are an important backdrop in understanding the series of events that jump-started negotiations that culminated in the FGCC.

Up until the start of this century the Australian dairy industry consisted primarily of small, privately owned dairy farms dispersed across the country and represented by their own industry body, which set farmgate prices for the selling of milk to processing collectives. We first consider how deregulation, the decline of industry-specific bodies and advances in technology put an end to pricing support for liquid milk, leading to the rationalisation and consolidation of dairy farms and processors. We then consider the political implications of the resultant shift in power from the processors to the MSCs.

In 2008, at a time when concerns that prices were too high had led to the ACCC Grocery Inquiry, high international milk prices had disguised the full impact of deregulation on the dairy sector. We consider the political response once this mask was removed in 2010 by a rapidly declining international milk price and the Global Financial Crisis (GFC), with not one but two public inquiries into the dairy sector within two years (one in 2010 and another in 2011). Crucially, between the two, came the 'milk wars', with the MSCs competing aggressively for consumer share by selling milk for as little as one dollar a litre.

We examine the findings of the two inquiries and the government's response, how both were shaped by the growing public and political visibility of the challenges being faced by the dairy industry, and how the conduct of the MSCs came to be seen as relevant in these developments. At a political level it is important to take into consideration the change of government that brought with it a new Agriculture Minister with a passion for regional Australia in Barnaby Joyce. Joyce's advocacy and policy initiatives, in particular the Agricultural Competitiveness White Paper advocating 'a fairer go for farmers',<sup>111</sup> provides an effective lens through which to consider a central political tension in the Coalition government, and Australian politics more generally. The tension arises in the desire to minimise government interference and maximise competition in the interests of consumer welfare on

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<sup>111</sup> Commonwealth of Australia 2015, *Agricultural Competitiveness White Paper: Stronger farmers stronger economy* (Agricultural Competitiveness White Paper, 2015), p. 1.

the one hand, while retaining the support of the rural and small business sector, so often the casualties of competition, on the other. This political dilemma loomed large in the intervening years, between the ACCC Grocery Inquiry and the government's decision to regulate by way of the FGCC.

In identifying this tension, however, it is important also to appreciate the socio-cultural dynamics at work, insofar as consumers or the general public are concerned. In examining these dynamics, we highlight how the distinctively Australian ethos of egalitarianism, a deep suspicion of big business and powerful institutions and the desire to support the underdog, generated public sympathy for Australian farmers. At the same time, our love of a bargain, the popularity of one dollar milk particularly and the success of the discounter Aldi, meant that these sentiments failed to be reflected in purchasing behaviour. In the context of the political heat generated by the milk wars, this contradiction serves to highlight the pressures that both the MSCs and government were experiencing by 2012, at the time negotiations over a code of conduct for supermarket-supplier relations kicked off.

## **I. A changing industry – the dairy sector consolidates**

While both industry-specific and macro-economic factors were affecting grocery suppliers generally post-2008, the 'pain' was particularly acute amongst farmers, and dairy farmers especially. This was in part a fall out from the major structural upheaval that had taken place in the dairy industry over the previous decade.

As one industry representative observed of the period prior to the structural transformation, 'the whole issue of supermarkets wasn't really an issue back then because everything was totally and absolutely regulated, including those who supplied milk for fluid milk purposes.'<sup>112</sup> Until 2000, the price paid for manufacturing milk was determined by factors including world prices of manufactured dairy products; however, support was provided through the use of national export pools that ensured farmers received an average pool price for their product regardless of its quality, use and destination. State authorities set the farmgate price for fresh drinking milk to ensure the additional costs of year-round supply were covered. Steps towards market deregulation commenced in the mid 1980s and continued throughout the 1990s. The change was driven largely by the dairy industry itself as participants sought opportunities for growth, albeit with significant government support in line with its micro-economic reform agenda generally and NCP in particular.

In early 1999 the industry's peak policy body, the Australian Industry Dairy Corporation (AIDC) approached the federal Coalition government with a plan for a national approach to the 'orderly' deregulation of the drinking milk sector, and the end of manufacturing milk price support.<sup>113</sup> While driven by industry there was a sense that such deregulation was 'inevitable'.<sup>114</sup> The Coalition Government's much championed NCP focus on efficiency meant plans had been afoot for some time

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<sup>112</sup> Transcript of interview, senior representative of dairy industry association, p. 10.

<sup>113</sup> Dairy Australia, 'History of Australian dairy industry deregulation', <http://www.dairyaustralia.com.au/Industry-information/About-the-industry/Deregulation.aspx>

<sup>114</sup> National Competition Council 2004, *NCC Occasional Series: Dairy - Now and Then: The Australian Dairy Industry Since Deregulation*, AusInfo, Canberra (NCC Dairy – Now and Then, 2004), p. 19.

to remove governmental domestic milk support.<sup>115</sup> Further, the decision by major manufacturers to sell milk to retailers and/or processors at low prices would in effect make the farmgate pricing systems redundant.<sup>116</sup>

The impact of NCP is apparent in the way that deregulation was managed. A state-by-state review had identified the need to increase value and efficiency in both farmgate pricing and supply chain management. A forecast quantum loss of farm incomes was an accepted outcome of such reforms and as such the AIDC relied on these forecast losses to argue for an industry adjustment package.<sup>117</sup> On 28 September 1999 the government announced it would implement the Dairy Structural Adjustment Program (DSAP), a program that would see the dramatic reduction of regulation in the sector.<sup>118</sup>

Following its deregulation in 1999 the industry went through a period of significant rationalisation, consolidation and adjustment. The numerous small, often family-operated, farms started to be replaced by larger commercial farming enterprises. For many, remaining in the industry was simply not sustainable:

*A lot of people have just gone out of dairying and sold their water rights as well [and then] you're not a dairy farmer any more, and buying it back is not a simple process. You can buy it on the market but it's a pretty expensive commodity compared to what they used to be.*<sup>119</sup>

As one industry observer noted, many struggled to adapt:

*I'm not convinced the sector has changed its thinking ... I don't think they understand that the ground they were playing on 15, 20 years ago has now shifted and the epicentre of that now is a lot of the regulatory issues that are dealt with by bodies by the ACCC.*<sup>120</sup>

This may be due in part to nature of farming in Australia, in particular its geographical isolation. As pointed out by a senior ACCC representative:

*Australian farmers, almost without fail, are virtually the only ones who live in isolation on their farms. Virtually, all other substantial farm populations live in villages and travel to their farms.*<sup>121</sup>

This might also explain why Australian farmers, unlike those in so many other countries, do not have a, 'very strong co-operative culture'.<sup>122</sup> One possible ramification of this, according to the same interviewee, is that:

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<sup>115</sup> Dairy Australia, 'History of Australian dairy industry deregulation' <http://www.dairyaustralia.com.au/Industry-information/About-the-industry/Deregulation.aspx>.

<sup>116</sup> NCC Dairy – Now and Then, 2004, p. 19.

<sup>117</sup> NCC Dairy – Now and Then, 2004, p. 19.

<sup>118</sup> Dairy Australia, 'History of Australian dairy industry deregulation' <http://www.dairyaustralia.com.au/Industry-information/About-the-industry/Deregulation.aspx>.

<sup>119</sup> Transcript of interview, senior representative of a dairy industry association, p. 8.

<sup>120</sup> Transcript of interview, senior representative of the ACCC, p. 3.

<sup>121</sup> Transcript of interview, senior representative of the ACCC, p. 5.

<sup>122</sup> Transcript of interview, senior representative of the ACCC, p. 4.

*Australia farmers are very self-sufficient, very independent in terms of their approach to getting things done. And I suspect that bleeds into, you know, their reluctance to agreeing to work collectively.*<sup>123</sup>

Accepting this, once floor prices and the single desk were gone, the decline in the relevance of sector-specific industry bodies may have been exacerbated by technological advances happening at around the same time:

*Look again at the history from perhaps 1990 to now, you move from zero access to the Internet and very limited telecommunications to instantaneous and universal telecommunications, albeit not brilliant in the bush, but most people can get access to the Internet and mobile phones. So, again, the role of those organisations used to be as the information conveyors to and from the policy makers. Well, you can be on the tractor in the middle of a paddock in Dubbo and get Barnaby Joyce on the phone straight away. So, the, you know, that crucial role they had as the conveyors of information and [access to] the representative has broken down.*<sup>124</sup>

The decline of the small family farm brought with it an associated increase in herd sizes and milk yields per cow as farmers sought to benefit from the efficiencies of larger operating systems.<sup>125</sup> In addition, over the same period, there was increasing concentration at the processor level of the industry. In 1999 there were five major milk manufacturers. However, just under a decade later, this had reduced such that, in the drinking milk market, there were only two big players - National Foods (with 81% share) and Parmalat (with 12% share).<sup>126</sup> Moreover, prior to deregulation, many of the processors were cooperatives owned by farmers which would largely price at a level that aimed merely to cover the processing costs.

Reflecting back, a senior representative of a dairy industry association has noted: 'up until the mid-90s the margins of all the players were regulated, 'and then slowly but surely they got rid of the retail margin, got rid of processor margin, and the only margin that was left for the last few years of regulation was the ... farm gate price.'<sup>127</sup> By July 2010, in line with the DSAP, all states had repealed any legislation governing the sourcing and pricing of drinking milk and all the state milk authorities that had administered these controls had been wound up.<sup>128</sup> Only Murray Goulburn remained a cooperative; most of the other processors were foreign-owned companies,<sup>129</sup> the shareholder interests in which were not necessarily aligned with the interests of farmers.

<sup>123</sup> Transcript of interview, senior representative of the ACCC, p. 6.

<sup>124</sup> Transcript of interview, senior representative of the ACCC, p. 6.

<sup>125</sup> The Australian Bureau of Statistics Australia Social Trends 2003 'Living arrangements: Farming Families' <http://www.abs.gov.au/AUSSTATS/abs@.nsf/7d12b0f6763c78caca257061001cc588/cdcd7dca1f3ddb21ca2570eb00835393!OpenDocument>.

<sup>126</sup> Senate Economics References Committee Report, *Milking it for all it's worth — competition and pricing in the Australian dairy industry*, May 2010 (SERC, *Milking it for all its worth*, 2010), p. 16.

<sup>127</sup> Transcript of interview, senior representative of a dairy industry association, p. 25.

<sup>128</sup> Dairy Australia, 'History of Australian dairy industry deregulation' <http://www.dairyaustralia.com.au/Industry-information/About-the-industry/Deregulation.aspx>.

<sup>129</sup> SERC, *Milking it for all its worth*, 2010, p. 32.

Concentration at the retail level of the grocery sector was a significant driver of the concentration amongst processors. The MSCs generally prefer a single supplier and hence there is enormous pressure on the processors to secure a MSC contract (or otherwise be locked out of half the drinking market).<sup>130</sup> This promoted consolidation within the processing market as only large processors could credibly bid for the contracts and without a MSC contract could not realise economies of scale. As one industry representative observed:

*I think it's about 55% of milk is sold to supermarkets now so that's a big market, when supermarket contracts change hands, it has a big impact on the processor who supplies them, Lion, Parmalat, Murray Goulburn. They've got a 10 year contract now and it has an enormous impact on them and you're seeing companies like Lion and others try and get into the export market a bit more, I think, because of that reliance on the domestic market here.*<sup>131</sup>

The growth in generic milk sales also meant that the processors dominating the fresh milk market were increasingly competing with their own branded products as they also supplied the MSCs with their generic milk.<sup>132</sup> Combined with the pressure placed on processors by the high level of retail concentration, this competition was said to be producing conduct that some argued amounted to misuse of market power, including price discrimination (smaller retailers being charged higher wholesale milk prices than the larger retailers),<sup>133</sup> and waterbedding (processors cross-subsidising losses on milk with higher prices on other dairy products).<sup>134</sup> With respect to the latter, when asked why the MSCs press for lower prices on liquid milk but not cheese and other dairy products, a senior representative of a dairy industry association explained:

*...they're doing a deal. Part of the dollar milk is access to better shelf space and larger shelf space for your branded cheese....some processors have lost their contract for sale of their particular branded cheese in a supermarket because of the dollar milk thing.*<sup>135</sup>

## II. Dairy sector concerns become political concerns

In the late 1990s it had been a 'serious concern' that, under deregulation, the control provided by regulation would 'shift to processors and large retailers who would then be able to dictate terms to the industry and marketplace.'<sup>136</sup> In 2010, pointing to the concentration at processing and retail levels of the market and the competitive dynamics between the two, a Senate Economic References Committee conceded that this appeared to be exactly what had happened.<sup>137</sup> As an industry representative noted:

<sup>130</sup> SERC, *Milking it for all its worth*, 2010, p. 53.

<sup>131</sup> Transcript of interview, senior representative of a dairy industry association, p. 17.

<sup>132</sup> By 2010 about half of the drinking milk sold in Australia was generic (private label) milk (see Dairy Australia, *Australian Dairy Industry in Focus* 2009, p. 43.)

<sup>133</sup> SERC, *Milking it for all its worth*, 2010, at p. 56.

<sup>134</sup> SERC, *Milking it for all its worth*, 2010, at p. 32.

<sup>135</sup> Senior representative of a dairy industry association, p. 27.

<sup>136</sup> *Deregulation of the Australian Dairy Industry*, October 1999, p. 170, cited in SERC, *Milking it for all its worth*, 2010, p. 14.

<sup>137</sup> SERC, *Milking it for all its worth*, 2010, p. 17.

*... all of a sudden a supermarket decide[s] that this brand does a better job of sale than this one does, there's no transparency in any of that, but they're the sorts of problems that exist, which have not to do with competition as much as the power that you have.*<sup>138</sup>

The effects of the structural transformation had been masked in the boom years - in 2007-08 Australia's dairy farmers were receiving record farmgate prices for their milk and confidence was high.<sup>139</sup> In 2008, Dairy Australia reported that the Australian dairy industry was 'enjoying the best world market conditions in decades.'<sup>140</sup> International dairy commodity prices rose to record levels through 2007, due to consistent strong demand and tight supplies, as well as the effects of exchange rates and cuts in export subsidies. This led to higher farmgate milk prices for dairy farmers – prices increasing by more than 50% in southern regions during 2007-08.<sup>141</sup> Higher farmgate prices continued into the 2008-09 season until, following the GFC, milk processors reduced the price paid to farmers sharply. The reduction in price per litre paid to farmers was initiated by Murray Goulburn which announced a 'step-down' in response to the weakening international commodity market.<sup>142</sup> Following Murray Goulburn's announcement, the remaining major milk processors also announced reductions in the price they would pay.<sup>143</sup> As reported in the Senate Committee's report, the boom times ended 'more or less overnight'.<sup>144</sup>

The farmgate price plummet led the Senate in September 2009 to refer the matter to the Economic References committee for inquiry, with terms of reference particularly focussed on the impact of consolidation on the dairy supply chain since deregulation of the industry a decade previously and the effectiveness of the *Trade Practices Act 1974* (TPA), as the CCA was then called.<sup>145</sup> The referral reflected the degree of political pressure that the dairy farmers were starting to exert. As the Committee observed:

*The inquiry commenced at a time when dairy farmers were appealing to government that the larger players within the processing and retail sectors were taking advantage of their market power to "milk them for all they were worth" in what was a volatile period in the global marketplace.*<sup>146</sup>

The Committee found that farm gate prices were being determined by the amount of competition – or lack thereof – between processors in different regions, rather than the international commodity market.<sup>147</sup> Consequently, in contrast to the findings of the ACCC Grocery Inquiry, while retail prices

<sup>138</sup> Transcript of interview, senior representative of a dairy industry association, p. 29.

<sup>139</sup> SERC, *Milking it for all its worth*, 2010, p. 10.

<sup>140</sup> SERC, *Milking it for all its worth*, 2010, p. 10.

<sup>141</sup> SERC, *Milking it for all its worth*, 2010, p. 10.

<sup>142</sup> SERC, *Milking it for all its worth*, 2010, p. 11.

<sup>143</sup> SERC, *Milking it for all its worth*, 2010, p. 11.

<sup>144</sup> SERC, *Milking it for all its worth*, 2010, recommendation 5, p.1.

<sup>145</sup> SERC, *Milking it for all its worth*, 2010, p. 7.

<sup>146</sup> SERC, *Milking it for all its worth*, 2010, recommendation 5, p.1.

<sup>147</sup> SERC, *Milking it for all its worth*, 2010, recommendation 5, pp. 1-2.

for milk had increased, farm gate prices had reduced, in some cases to below the cost of production.<sup>148</sup> As one industry observer has said:

*So the bigger picture is that Australia is a high cost country, quite high wages, quite high cost of living. So any notion that agriculture in Australia can remain competitive purely on a cost basis is quite a dangerous one.*<sup>149</sup>

In response, the Committee made a series of recommendations aimed at addressing both structural and conduct concerns at both the processing and retail levels of the grocery sector. The ACCC should conduct a further study of the implications of the growing shares of the generic milk market held by the MSCs, it recommended.<sup>150</sup> There should be a moratorium on further mergers and acquisitions in the milk processing industry and the Productivity Commission (PC) should consider whether there should be separate agencies for the approval of mergers and subsequent assessment of excessive levels of concentration.<sup>151</sup> There should be more transparency and consistency in milk pricing for farmers.<sup>152</sup> The ACCC should gather more information on and monitor closely pricing practices in the dairy supply chain with a view to ascertaining whether or not there were misuses of market power and the government should consider reinstating a prohibition on price discrimination.<sup>153</sup> The government should also look into how new processors owned by farmer cooperatives might be established<sup>154</sup> and in the meantime it should consider measures to facilitate more and more effective collective bargaining by farmers in negotiations with processors.<sup>155</sup> More broadly, there should be multi-government and stakeholder engagement in considering long term trends in the industry and their implications for its sustainability as well as Australia's food security.<sup>156</sup>

The Government provided its response to this, and to a subsequent 2011 inquiry into pricing issues in the sector,<sup>157</sup> separately but concurrently. Given that the subsequent inquiry focussed squarely on the impact of supermarket pricing decisions on the dairy industry, the recommendations with regard to dairy pricing from both inquiries were addressed in the Government's response to the 2011 report (see below).

Concerns around the effectiveness of the provisions that allow for farmers to engage in collective bargaining were raised in both inquiries. However the Government did not accept that there was a need to review these provisions, reasoning that they were 'generally operating effectively for dairy farmers'<sup>158</sup> and that they were in the best interests of Australian businesses, consumers and the

<sup>148</sup> SERC, *Milking it for all its worth*, 2010, p. 7.

<sup>149</sup> Transcript of interview, senior representative of the ACCC, p. 9.

<sup>150</sup> SERC, *Milking it for all its worth*, 2010, recommendation 8, p. 4.

<sup>151</sup> SERC, *Milking it for all its worth*, 2010, recommendation 6, p. 4.

<sup>152</sup> SERC, *Milking it for all its worth*, 2010, recommendation 6, p. 2.

<sup>153</sup> SERC, *Milking it for all its worth*, 2010, recommendation 4, p. 3.

<sup>154</sup> SERC, *Milking it for all its worth*, 2010, recommendation 11, p. 3.

<sup>155</sup> SERC, *Milking it for all its worth*, 2010, recommendation 2, p. 2.

<sup>156</sup> SERC, *Milking it for all its worth*, 2010, recommendation 14, p. 5.

<sup>157</sup> Senate Economics References Committee, Final Report, *The impacts of supermarket pricing decisions on the dairy industry*, 2011 (SERC, *Impacts of supermarket pricing on the dairy industry*, 2011).

<sup>158</sup> Government response to SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. 4.

broader economy. However, the Government did support the increased provision of information so as to facilitate more and more effective collective bargaining arrangements.<sup>159</sup>

With regard to calls for further study into the implications of the growing generic milk market, the Government cited the development of the National Food Plan (NFP), stating that this would provide a 'strategic and integrated approach' to the issue as it pertained to food security and the future sustainability of the dairy industry.<sup>160</sup> In doing so the Government also addressed the call for separate multi-governmental and stakeholder engagement in response to concerns around these issues, stating that these too would be addressed through the NFP. With regard to possible misuses of market power the Government noted that the ACCC had already indicated it would actively monitor generic products, including generic milk, citing ACCC Chairman, Rod Sims' statement that, when it came to private label products:<sup>161</sup>

*This vertical integration in the supply chain needs close scrutiny to ensure the supermarkets do not misuse their market power under Section 46.*<sup>162</sup>

In response to calls for the PC to consider the appropriateness of separating the functions of the ACCC when it came to merger approvals and market concentration, the Government determined that, 'the ACCC, as the expert, independent competition regulator, is the agency best placed to consider all aspects of the competitive effects particular of mergers and acquisitions.'<sup>163</sup> The Government also made clear that it did not consider the establishment of new processors and their corporate structure fell within the scope of Government intervention and that these were matters best left to industry members.<sup>164</sup>

### **III. One dollar milk hits the shelves, heralding yet another government inquiry**

Then, barely before policymakers and politicians had had a chance to draw breath, on Australia Day (26 January) 2011 Coles kicked off what has come to be known as 'the milk wars', reducing the price of its private label plain white milk from \$2.41 for a two-litre container to \$1 per litre.<sup>165</sup> Woolworths, Aldi and others quickly followed suit. This generated a further angry backlash from farmers. Dairy producers and their representatives again beat a path to the doors of Canberra. The government's response was to commission yet another Senate committee inquiry, in February 2011.<sup>166</sup>

<sup>159</sup> Government response to SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. 5.

<sup>160</sup> Government response to SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. 5.

<sup>161</sup> Government response to SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. 5.

<sup>162</sup> Rod Sims, Some perspectives on competition and regulation Melbourne Press Club (10 October 2011), referred to in Government response to SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. 5.

<sup>163</sup> Government response to SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. 6.

<sup>164</sup> Government response to SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. 6.

<sup>165</sup> Jared Lynch and Eli Greenblat, 'Farmers warn on milk war threat', *The Age*, 8 March 2011; 'Woolworths admits milk war will hurt farmers', *ABC News*, 8 March 2011; 'Farmers froth over \$2 milk', *SMH*, 26 January 2011.

<sup>166</sup> In the meantime, the third interim report of the former Senate Select Committee on Agricultural and Related Industries' inquiry into food production, tabled in November 2009, had also focussed on the dairy industry.

This inquiry was focussed squarely on the supermarket price cuts and their impact on the dairy industry supply chain but again inevitably there was reflection on the imbalances in bargaining power between farmers and processors. The Committee traversed much of the same ground as had been covered in the 2010 inquiry little over a year before and many of its findings and recommendations were not dissimilar. The combination of concentration at both processor and retail levels of the sector, and the competitive tensions introduced by the growth in generic milk, were major contributors to the difficulties besetting dairy farmers.<sup>167</sup> However, for those regions reliant on exports to a considerable extent, international prices were also a factor and phenomena such as drought and flooding should not be overlooked.<sup>168</sup>

Taking this all into account, the Committee restated that it would assist farmers if there was more clarity and transparency in processor pricing structures,<sup>169</sup> as well as greater scope for collective bargaining.<sup>170</sup> There should be an independent review of the competition rules, not confined to but particularly focussing on the effectiveness of the misuse of market prohibition in s 46<sup>171</sup> and, looking beyond concerns about competition, there should be a study of the sustainability of the dairy industry.<sup>172</sup> Moreover, the voluntary PGCC should be reviewed and consideration should be given to its replacement with a mandatory prescribed code under the CCA as a means to address issues in supermarket-supplier relationships.<sup>173</sup> What's more, consultation should be undertaken with respect to the possibility of creating a new statutory office to manage and respond to such issues.<sup>174</sup>

In its response to the second milk inquiry the Government, while acknowledging that pricing structures were a commercial matter for industry, encouraged 'all participants in the dairy industry to be transparent in their transactions along the supply chain.'<sup>175</sup> Processors were encouraged to provide more stable pricing to farmers to allow farmers to set a fixed price, albeit at the risk of less profits for farmers.<sup>176</sup> Development of a clear, consistent formula for milk pricing with unambiguous conditions was encouraged.<sup>177</sup>

As previously noted, the Government did not believe there was a need to review existing collective bargaining provisions.<sup>178</sup> The Government was also not convinced of the need for independent review of the competition provisions. Drawing attention to Rod Sims' stated intention for the ACCC to take action 'even where the law is not completely clear', the view was that the watchdog should be given the opportunity to first further test the existing laws in the courts.<sup>179</sup> There was no direct response to calls for changes or the replacement of the PGCC. Instead the Government again highlighted the

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<sup>167</sup> See Chapter 5 in particular, 'Impact of the retail price cuts at the farm gate', in SERC, *Impacts of supermarket pricing on the dairy industry*, 2011.

<sup>168</sup> SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. 16.

<sup>169</sup> SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, recommendation 1, p. xv.

<sup>170</sup> SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, recommendation 6, p. xviii.

<sup>171</sup> SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, recommendation 5, p. xvi.

<sup>172</sup> SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, recommendation 3, p. xv.

<sup>173</sup> SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, recommendation 7, p. xix.

<sup>174</sup> SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, recommendation 7, p. xix.

<sup>175</sup> Government response to *Impacts of supermarket pricing on the dairy industry*, 2011, p. 1.

<sup>176</sup> Government response to SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. 1.

<sup>177</sup> Government response to SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. 2.

<sup>178</sup> Government response to SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. 5.

<sup>179</sup> Government response to SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. 4.

work currently underway to develop the NFP, noting that through the Food Processing Industry Strategy Group and the Senate's Select Committee on Australia's Food Processing Sector, further input for consideration by the Government on these issues may arise.<sup>180</sup>

#### **IV. The political dilemma – deny farmers or consumers?**

Two Senate inquiries reporting in the space of just two years: there was no doubt that pressure on the then Labor government to respond to the grievances of the dairy industry was mounting. The dilemma that politicians faced in fashioning a coherent response that would quell the controversy was acute.

It was this dilemma, among others, that Tony Abbott's Coalition Party inherited when it defeated Labor on 18 September 2013. The change of government brought with it an ally for farmers in Deputy Prime Minister and National Party member Barnaby Joyce. One of six children from a farming family, with a long held passion for the rural sector, Joyce was promptly appointed Agriculture Minister, having already held related shadow portfolios in Regional Development, Infrastructure and Water (2010), and Regional Development, Local Government and Water (2010–13).

Less than two months after the election Joyce announced the terms of reference for a White Paper to examine agricultural competitiveness and the establishment of a taskforce to consult with stakeholders in order to develop the government's plan to 'grow agriculture'.<sup>181</sup> This White Paper would be very much a product of the National Party, and of Joyce's fervour for life on the family farm, as evidenced by this statement he is reported to have made just after the release of the final report in 2015:

*I hear from some quarters, the day of the family farm is over, possibly walking out the door with the family business and the family house. Like journalism without grammar, the land without the family farm is meaningless, soulless, it goes to the core fabric of our nation.*<sup>182</sup>

An Issues Paper released in early 2014 attracted more than 600 submissions, drawing comments and suggestions on a range of topics including food security, improving farmgate returns, enhancing competitiveness, and the reduction of regulatory burdens.<sup>183</sup>

The first priority of the subsequent White Paper, promoted by the Government as a '\$4 billion investment in our farmers', was 'a fairer go for farm businesses' and included a substantial funding boost to the ACCC so that it could engage more with the agricultural sector, including through a new Commissioner dedicated to agriculture. The objective was said to be to support 'a more farm-savvy and proactive ACCC [that] will encourage fair-trading and strengthen competition in agricultural supply chains'.<sup>184</sup>

<sup>180</sup> Government response to SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, pp. 6-7.

<sup>181</sup> 'Joyce announces agriculture white paper', *SBS news*, 9 December 2013.

<sup>182</sup> Gabrielle Chan, 'Dams, droughts, deposits: a guide to Barnaby Joyce's agricultural white paper', *The Guardian*, 7 July 2015.

<sup>183</sup> Media release, 'Big response on the future of agriculture', The Hon. Barnaby Joyce MP, Deputy Prime Minister, Minister for Agriculture and Water Resources, 1 May 2014.

<sup>184</sup> Agricultural Competitiveness White Paper, 2015, White paper at a glance, <http://agwhitepaper.agriculture.gov.au/white-paper/white-paper-at-a-glance>

While the Government was anxious to support the rural sector generally, the political sensitivities around farmgate milk prices in particular may explain why the White Paper was released at a dairy farm near Warnambool.<sup>185</sup> At the same time, it was difficult if not impossible to ignore the fact that, in the short term at least, the direct beneficiaries of the milk price wars were consumers. According to one industry lobbyist, in a conversation with the then Shadow Minister for Small Business (now opposition leader), Bill Shorten, he was bluntly told: 'I really have no interest in depriving my constituents of \$1 milk... anything that is going to increase prices, any initiative, I'm not for that at all.'<sup>186</sup> Indeed the irony in the referral to a parliamentary inquiry of the case of prices being too low, just 3 years after an ACCC inquiry into the case of prices being too high, was not lost on the 2011 Senate committee:

*The circumstances which gave rise to this inquiry appear unusual in many respects. In recent years, public debate about the competitiveness of the supermarket sector has been focused on concerns about food price inflation and grocery prices being too high. In conducting this inquiry, the committee has been troubled that the benefits gained by consumers have not received sufficient attention in the debate about milk prices. In general, price discounting is likely to be pro-competitive and of benefit to consumers. Provided it does not constitute predatory pricing, a retail price cut should not be discouraged. The January 2011 price cuts in a staple product is undoubtedly good news for consumers in the short-term. Attempting to predict with any certainty any longer-term impact on overall consumer welfare is difficult, if not impossible.<sup>187</sup>*

On the other hand, there was clearly growing consumer consciousness of and sympathy for farmers, and politicians were anxious not to ignore that tide of sentiment entirely. Looking back, former AFGC CEO Dawson is of the view that, in political terms the climax reached in the MSC debate around 2012 can be explained as follows:

*...the most significant thing that ...lit the fuse or created particular focus on it were things like the \$1 milk, \$1 bread which consumers love but are outraged by at the same time...it was the perception that farmers are being duded, there was a very strong vein of sympathy for farmers across the Australian community and that was the perception that farmers were being duded, 60 – over 60% of milk sales, \$1 private brand label, so it doesn't stop them buying it but there was - in terms of what drives a sense of outrage or a focus. And I think there was then a bit of a snowball of stories about - - - suppliers, truck drivers, all sorts of things that - - - there were factory closures - - and as happens with the media often when a certain perception takes hold then things are seen through the prism of this is further evidence of x and I think those things go in cycles really. And so I think by 2012 there'd been a raft of those*

<sup>185</sup> Brett Worthington, 'Agricultural Competitiveness White Paper launched', *ABC news* 4 July 2015.

<sup>186</sup> Transcript of interview, CEO of MGA, pp. 46-7.

<sup>187</sup> SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. xiii.

*stories and it transmits very quickly through to the legal pressure for action because governments are expected- - - to fix things.*<sup>188</sup>

Searching for explanations for the ‘outrage’ or ‘focus’ to which Dawson referred, one MSC representative reflected on the ‘influence of the rural lobby’, and a sense that farmers ‘punch above their weight in publicity terms’. She went on to say:

*...in Australia we're very proud of our history in farming and I think in the small businesses that have grown up. ... [S]ome businesses have obviously succeeded more than others over time and we do have, although I say this quite colloquially, the tall poppy syndrome, I do think there is something about us Australians that ... we don't like that lack of equilibrium where some really succeed and have worked perhaps from the same starting point but for whatever reason are meeting the demands of consumers at the expense of others. [T]here are real roots in our culture, our farming culture, our working on the land that we don't want to lose as Australians, and if our regulation can help that – that's not dissimilar I think to what you see in France where in Paris there is a periphery, the line around where you could have large supermarkets and they needed to be outside so you could keep that small business, butcher, baker, candlestick maker they're things that people feel emotionally strongly about. And I think with the digitalisation of our world, the demand for instant, everything being instant it's hard to reconcile those things in balance and that, I think, is the tough challenge for regulators to be thinking economically, to be thinking about promoting competition, to be thinking about efficiencies but to be balancing it against what's really important to the people in terms of the sentiment that they feel, how they want their country to function. These are tough areas....*

*... [In] Australia we do prioritise fairness but economically we've also promoted free market economics and competition. And the tension there, I think that's where I was coming from with cake and eating it too, is we want all that competition brings – fierce competition, ruthless competition – but when we see that there are losers we want them protected as well. [T]his is where I see the real tensions that good regulation has to tackle and it's so tough.*<sup>189</sup>

## **V. The conundrum – but what do consumers truly want?**

In many respects this community sentiment is most readily interpreted or understood through a socio-cultural lens. The public reaction to a narrative which depicted the plight of Aussie farmers as the consequence of the ruthless actions of powerful corporates and their white collar executives (no matter how incomplete, simplistic or distorted that story-line may have been) reflected an ingrained Australian attachment to egalitarianism, associated sympathy for the underdog, and suspicion of the tall poppy. To quote one interviewee:

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<sup>188</sup> Transcript of interview, Gary Dawson, pp. 30-2. See also comments by a senior business columnist that: ‘politicians are very much driven by the media... they can see the sort of support it's [concerns about milk prices and impact on dairy farmers] getting in the media and it's really not hard to support it when you're seeing the human faces of people in a lot of pain’ (Transcript of interview, senior business journalist, p. 9).

<sup>189</sup> Transcript of interview, MSC representative, pp. 9-11, 14.

*There's a bit of that – yes, I want my groceries cheap, but not to the extent that you're absolutely smashing these people that are providing it. And if I see examples where you are doing that, I'm not going to be very happy. So that social licence seems to have quite a strong, yes, egalitarianism associated with it.*<sup>190</sup>

He went on to say that the idea of MSCs having a 'social licence to operate' explains in part 'the inordinate amount of promotion that, for example, Coles and Woolworths put around: "we're with farmers" ... they obviously see quite a strong resonance with that identification of helping farmers and farmers being their mates, that help them put the food on the table.'<sup>191</sup> There is a similar dynamic in the UK where farming concerns, and dairy milk prices particularly, have been the focus of much of the public debate concerning supermarkets (see further below).

And there was further evidence of the power of farmer sympathies in shifting organisational behaviour, albeit not always in ways that are positive. In early 2013 at the height of the milk wars, in an apparent attempt to garner consumer support, Coles published a video and cartoon entitled Our Coles Brand Milk Story on social media. The promotion suggested that the price farmers were getting for milk increased from 86 cents per two litre bottle of Coles-brand milk in 2010-11 to around 90 cents in 2011-12. This turned out to be an estimate. Final industry figures showed the 2011-12 farmgate milk price had in fact decreased to 84 cents in that time. In an investigation into the promotion the ACCC found that Coles was aware, or should have been aware, of its error. The promotion also made unsubstantiated claims about the profits that farmers were making on Coles-brand milk, and that the Coles' price cut had increased the consumption of drinking milk and therefore Australian dairy production.<sup>192</sup>

Rather than enhancing Coles' reputation, the retailer found itself giving an enforceable undertaking to the ACCC that, for a period of three years, it would not make misleading or deceptive representations with regard to the impact of reductions in the retail price for Coles brand milk on the farmgate milk price, Coles' or processor margins on Coles brand milk, and/ or Australian milk production generally; that it would review its Australian Consumer Law (ACL) compliance program as it related to advertising and promotional strategies with regard to Coles brand milk; and that it would undertake training of relevant employees to ensure such conduct did not arise again.<sup>193</sup> As one journalist observed, 'Coles spruiked a rosy picture of the dairy industry at the height of the \$1 milk wars last year using data it could not substantiate'.<sup>194</sup>

Woolworths responded to public sympathy for farmers by introducing a milk brand, Farmer's Own, sold at a higher price point and derived from direct long term contracts with dairy farmers.

Independent retailers responded too. In December 2016 family-owned grocer Harris Farm announced

<sup>190</sup> Transcript of interview, senior representative of the ACCC, p. 17.

<sup>191</sup> Transcript of interview, senior representative of the ACCC, p. 15.

<sup>192</sup> ACCC Media Release, Coles gives undertaking to ACCC in relation to representations in YouTube video and cartoon, 7 April 2014.

<sup>193</sup> ACCC Media Release, Coles gives undertaking to ACCC in relation to representations in YouTube video and cartoon, 7 April 2014.

<sup>194</sup> Esther Han, 'Milk Wars: Coles admits to errors in ad campaign', *SMH*, 7 April 2014.

it was removing \$1 a litre milk from the shelves of its 24 NSW stores, in what it claimed was a bid to support the local dairy industry. Harris Farm instead was introducing the Farmer Friendly Milk range, selling at \$2.29 for two litres, which the company said reflects the true cost of production and would see Harris Farm return 95% of the sale price back to the cooperative and from there to the farmers that own it. Harris Farm co-CEO Tristan Harris is reported to have said:

*We understand that people want good value on products they use lots of every day, However, we believe most people don't agree that it should be cheap at all cost, including the costs of lives and livelihoods of Aussie farmers.*<sup>195</sup>

As mentioned above, the social and political influence of dairy farmer woes, and supermarket sensitivity to such issues, is not distinctive to Australia. In the UK, retailers are reported to be paying farmers higher prices for their milk as a way of:

*..trying to get the consumers off their back, because there's been so much interest in milk prices for so many years...trying to get better prices for farmers for milk is the retailers trying to say "we want to be responsible" ... [and to make the point that] it wasn't actually them that was setting the price... [it was] the processors.*<sup>196</sup>

As in Australia, there is a range of factors generating challenges for British dairy farmers and an associated degree of 'political noise' – in the case of price particularly, there are said to be problems of oversupply and competition from overseas including the subsidy regime in Europe, exacerbated by a high pound, and increasing concentration amongst processors. Yet, there is still a sense that at least part of the problem is that it is 'the retailers beating up the farmers'.<sup>197</sup> Farming concerns were a consistent thread in the inquiries conducted by competition authorities into the supermarket sector from 2000 onwards - those inquiries were framed in competition terms but 'that was obviously against a backdrop of concern about sustainability of the farming community'<sup>198</sup> - and today still, there is active consideration of whether it is necessary to regulate relationships between grocery retailers and indirect suppliers (namely, farmers).<sup>199</sup> One UK interviewee, a compliance manager at Waitrose, explained the challenges for supermarkets arising out of concerns for farmer livelihoods in the following terms:

*It is a tension between the end user, the retailers and the farmers. The farmers would love the highest prices; the consumer wants the lowest prices. And the supermarkets are in the middle doing a very clear balancing act between competing with each other, be as competitive as possible, serving the consumer, [while] answering to political pressure at the same time.*<sup>200</sup>

<sup>195</sup> Retail World Editor, 'Harris Farm Markets removes \$1 milk', *Retail World*, 20 January 2017.

<sup>196</sup> Transcript of interview, Christine Tacon, p. 6.

<sup>197</sup> Transcript of interview, John Noble, British Brands Group, p.11; Transcript of interview, former senior representative of the UK OFT, p. 7; Transcript of interview, experienced legal advisor to suppliers in the UK, 3.

<sup>198</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 3.

<sup>199</sup> See reference to the results of the 2016-17 review of the GCA and to the ongoing (at the time of writing) review of whether its remit should be extended to indirect suppliers in Part 7 of this report.

<sup>200</sup> Transcript of interview, compliance manager at a major UK retailer, 6.

## VI. Socio-cultural undertones and contradictions

Coles' apparent attempt to manage public opinion on the issue of cheap milk not only raised the ire of the ACCC but may have been counterproductive given elements of public antipathy towards powerful institutions generally in Australian society, pointed to by several commentators in their account as to why the MSCs attract such derision and hostility amongst parts of the Australian community. A highly experienced former MSC lobbyist, for example, explained the phenomenon as follows: government needs to be seen to be protecting 'the small guy' or 'the battler' because of 'community sentiment' which:

*...is negative towards anything that's big. It doesn't matter whether it's Telstra, whether it's the banks, whether it's big retail, energy companies, whether it's the supermarkets. The same dynamic is at play, big is bad in Australian politics, and small is good.*<sup>201</sup>

Post-2008 and the GFC, he went on to explain, this sentiment was amplified. In the public's eyes, big businesses and their leaders were 'just seen to be for profit and individual aggrandisement'.<sup>202</sup> This offended the 'Australian ethos of a "fair go"' and while they were no 'less cynical' about politicians, the public still looked to government to 'fix the problems'.<sup>203</sup> A representative from another MSC echoed this view:

*...obviously the Australian concern around the prosperity of small suppliers has been an absolute key theme that ... we're always aware of. We need to work with small suppliers for our business to work. We need to work with large suppliers and the relationships that we have with those individual suppliers are often very individual. But I think the narrative, the discourse around making sure small suppliers aren't being hurt somehow at the expense of the prosperity of larger business has definitely been something that everybody's latched onto and wanted to hear more about.*

...

*... there's something about the political culture of Australia as well that really wants – it's the fair go. It's wanting everybody to be able to compete on a level playing field, which underpins competition policy in itself.*<sup>204</sup>

A survey of 1000 adult Australians applying age, gender and regional quotas conducted by the Master Grocers Association (MGA) in 2015 lends weight to these sentiments. The survey carried a margin of error of +/-3.1%.<sup>205</sup> 75% of respondents believed that the strengthening competition laws (by adding an effects test) would lead to greater choice and better quality goods and services and lower prices, and that it would help small business suppliers in their dealings with big corporations. Furthermore

<sup>201</sup> Transcript of interview, Robert Hadler, p. 4.

<sup>202</sup> Transcript of interview, Robert Hadler, p. 7.

<sup>203</sup> Transcript of interview, Robert Hadler, p. 8.

<sup>204</sup> Transcript of interview, MSC representative, pp. 7-8.

<sup>205</sup> MGA national survey of attitudes to supermarket concentration 2015, pp. 3-4.

80% believed healthy competition makes for a generally fairer society.<sup>206</sup> With regard to the MSCs, 72% of those surveyed said that the grocery market was too dominated by Coles and Woolworths and that this led to 'unhealthy competition'. 90% believed it important that local independent supermarkets survive.<sup>207</sup> While the survey questions were worded in such a way as to arguably colour responses, the views expressed by interviewees for this research suggest that, in broad-brush terms, the survey findings captured the feelings of many Australians.

Independent observers echoed the view that there is an almost instinctive scepticism harboured by Australians in relation to the MSCs by virtue of the perception that these companies wield enormous control over many aspects of economic and social life:

*... looking at it from a consumer point of view I think there is a huge lack of trust and I think that's a big problem. ... it's about the power that these two supermarkets hold and they control what we do or don't eat or can or don't have access to.. (Senior representative, Choice)<sup>208</sup>*

*There's almost no national pride in the fact that these are two highly successful businesses that are employing a whole lot of people, that is not an argument that the supermarkets are going to win ... the fact that they are Australian companies does not give them any credit whatsoever, none.... So people would say, "it's so awful, the supermarkets, they just – they don't support Australian made and they don't support Australian farmers and they're un-Australian and therefore I'm going to go and shop at Aldi...".. if you gave them a questionnaire saying, is Aldi an Australian company, a German company ... it doesn't really matter, emotionally they felt that these two supermarkets had control of the environment for so long, that there needed to be a third player... We feel like we're tied to the two big supermarkets to some extent, maybe we can shave off some of their competition by not buying private label in there, by sometimes going to Aldi, by sometimes growing our own herbs, by sometimes directly getting a fruit box or whatever, doing those kinds of things, maybe we can do that.<sup>209</sup> (Social researcher, Rebecca Huntley)*

*I think there is a genuine reader interest in how the supermarkets are dealing with suppliers, particularly in Australia which has such a high concentration of a supermarket ownership...I think there is probably a natural scepticism about how these big businesses are operating behind closed doors to get the prices that they get.<sup>210</sup> (Experienced retail journalist)*

Public 'outrage' in response to what was seen as MSC responsibility for the struggles of farmers also reflected a somewhat nostalgic albeit no less strong attachment to 'the bush', a throwback to our agricultural roots and lingering national identity-imagery as a sunburnt country riding on a sheep's

<sup>206</sup> MGA national survey of attitudes to supermarket concentration 2015, p. 4.

<sup>207</sup> MGA national survey of attitudes to supermarket concentration 2015, p. 4.

<sup>208</sup> Transcript of interview, senior representative of Choice, pp.19, 46.

<sup>209</sup> Transcript of interview, Rebecca Huntley, pp. 10, 12.

<sup>210</sup> Transcript of interview, experienced retail journalist, p. 2.

back.<sup>211</sup> Again, several stakeholders saw these cultural nuances as important in fully understanding the public and hence political heat that surrounded the MSCs over this period:

*... it's [referring to and explaining public support for farmers] empathy, there's a splash of nostalgia to it ... I think it frames our life and our story of who we think we are.*<sup>212</sup> (Bruce Billson)

*... there is that feeling there that people want to see farmers survive and it is part of the Australia's culture and we're an agricultural nation.*<sup>213</sup> (CEO of a state farmers' organisation)

*... a lot of Australians still think they're bound to the earth and maybe cultural society in a way that actually they're not anymore. ... I think it's an incredibly emotive topic, which ignores also a lot of economic reality about productivity, under investment and so on.*<sup>214</sup> (MSC representative)

At the same time, public cynicism or hostility towards big businesses such as the MSCs appears to involve a disconnect between 'the company', as in the headquarters and the C-suite executives housed in them, and the local store and the people behind the check-out counter or stacking the shelves. When asked about whether consumers respond to bad press about a large retailer – for example, in connection with an ACCC proceeding – we were told by a MSC representative that in their 'customer feedback ... that doesn't tend to come through.'<sup>215</sup> As another ruefully remarked that in:

*...some of the commentary around customers and how they perceive Woolworths and how they perceive Coles ... there's a real dichotomy there. Customers are happy to shop with [MSCs], and their children may work with us ... yet they're quite happy to see something on TV and say, "Oh, bloody supermarkets again." They don't feel like there's any conflict between the two things.*<sup>216</sup>

Moreover, there is widespread agreement that the anti-MSC sentiments just described do not generally translate into anti-MSC shopping choices. One IGA owner put it bluntly: 'with all respect to our customers ... what the consumers will say and how the consumers behave are poles apart.'<sup>217</sup> Similarly, a senior policy analyst with a dairy industry association, reflecting on a more recent outbreak of savage milk price cuts in 2016, pointed out:

<sup>211</sup> See Jane Dixon and Bronwyn Isaacs, 'There's certainly a lot of hurting out there: navigating the trolley of progress down the supermarket', *Agric Hum Values* 30 (2013), pp. 238-297.

<sup>212</sup> Transcript of interview, Billson, p. 20.

<sup>213</sup> Transcript of interview, CEO of a state farmers' organisation, p. 26.

<sup>214</sup> Transcript of interview, MSC representative, p. 8.

<sup>215</sup> Transcript of interview, MSC representative, p. 30.

<sup>216</sup> Transcript of interview, MSC representative, p. 24.

<sup>217</sup> Transcript of interview, CEO of an independent supermarket, p.11.

*...we went through the same in 2011 when they dropped the price to a dollar a litre – very large amount of publicity, good consumer support for a while, they go back to their old buying habits.*<sup>218</sup>

And from a MSC representative:

*People want to do the right thing but in the end if I'm on a tight budget I'm not going to pay 50% more for this product ... That's why I think it's our role to try and make it affordable.*<sup>219</sup>

This observation was borne out by the experience in introducing higher priced milk, branded as product sourced directly from and benefitting farmers. A MSC representative also reported to us that while there has been some switching away from the lower priced alternatives in response to recent publicity of the difficulties facing dairy farmers, 'there's still a big segment of the market that didn't move.'<sup>220</sup>

A dilemma facing retailers is that the simplified portrayal of farmer woes in the media does not reflect the complexity of the supply chain in relation to own brand milk. As stated by a MSC representative:

*...in the end we as a retailer don't have power over the milk price... [T]he milk price is effectively set given where the export milk price is at, and our contracts are with the processors that effectively then pay the farmers, so we don't really even have transparency over that process. It's something that ... we have tried to provide choice to our customers around but we try and do the best we can on that issue. It's a difficult one for us because it's difficult to explain to a customer that we don't actually pay the farmer direct, we pay the processor...*<sup>221</sup>

The MSCs grapple with a tension between being competitive on the one hand (particularly on price), while at the same time attempting to persuade consumers that they are socially responsible on the other:

*...if we don't respond competitively we will just lose our budget customer base, but if customers, as they did do, say actually we're prepared to pay a bit more and the ... branded products sell well, if that's what the market is demanding, that's what we can provide. But in such a competitive market, not responding to somebody who is competitive on price is a killer. And it is an example of an area where there is a disconnect between what some customers are vocal about and then what a large percentage of customers are actually doing. Because people are still buying \$2 per 2 litre milk in droves, but we've got [premium milk] as well, but people want the nutritious staple at a low price and if we [will be at] a higher price which is an issue.*<sup>222</sup>

<sup>218</sup> Transcript of interview, senior representative of a dairy industry association, p. 23.

<sup>219</sup> Transcript of interview, MSC representative, p. 22.

<sup>220</sup> Transcript of interview, MSC representative, p. 24.

<sup>221</sup> Transcript of interview, MSC representative, p. 24.

<sup>222</sup> Transcript of interview, MSC representative, p. 27.

Similar observations have been made of consumer fickleness in the UK:

*... consumers can be somewhat schizophrenic about this, because while they say they want local butchers and smaller corner shops, they often walk past them and go into supermarkets to do their shopping. So people have this idealised image of what they want on the High Street, but it's not where they shop. So I think that one problem is that ... people have a romantic idea of what they want the High Street to be like. But actually, the shopping habits are that they drive to a shopping centre on a Saturday and shop there and do everything there, because they want the convenience and price associated with that, but then complain when a smaller shop on the High Street closes down.<sup>223</sup>*

Of course, therein lay the political dilemma back in 2011 (and arguably still today) – consumers want low prices but at least some (and possibly a considerable proportion) don't want supermarkets that have the buyer power to deliver them or at least do not want to see such power exercised in a way that is perceived as unfair to small suppliers, and farmers particularly.

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<sup>223</sup> Transcript of interview, former senior representative of the UK OFT, p. 5.

## 6. Significant actors

In this Part we identify and examine how key actors, both individuals and organisations in the private and public sectors, influenced developments between 2010 and 2015, leading up to the introduction of the FGCC. Without purporting to be exhaustive, and for reasons that should be evident from the analysis, we single out for this purpose:

- the ACCC and in particular, its two Chairmen over the relevant period, Graeme Samuel AC and Rod Sims;
- the former Minister for Small Business, Bruce Billson MP; and
- the AFGC and its two CEOs within the relevant time frame, Kate Carnell and Gary Dawson.

During the course of 2010-2011 and in the particular context of attention focussed on the dairy industry, the ACCC came under substantial pressure regarding its oversight and interventions in the grocery sector, both as to correctness of decisions it had made (in particular with respect to merger approvals) and as to the processes it had adopted with respect to investigations (in particular, in relation to the milk price cuts). We document the ensuing enforcement activity of the watchdog agency over the years that followed, from 2012 onwards particularly, reflecting a galvanisation in action. In part it is hard to avoid the conclusion that the Commission was responding, at least in part, to the criticism levelled at it in the spate of parliamentary inquiries over this period. However, our research indicates that the apparent change in approach was also attributable to a degree to the appointment of Rod Sims as Chairman and his quite different personal style to that of his predecessor, Graeme Samuel AC. A particular feature of Sims's leadership over this period was the litigation brought against Coles and then Woolworths for unconscionability in their treatment of suppliers. The significance of these actions and their outcomes, a win in the former and a loss in the latter, is examined in Part 6 of this report in the context of considering the relative effectiveness of the FGCC in changing behaviour.

In addition to the ACCC, the role and influence of the Small Business Minister at the time, Bruce Billson MP, is hard to understate. His personal passion for all things 'small business' and his particular commitment to a wide ranging review of competition laws (with a strong undercurrent of levelling the playing field for small to medium sized enterprises (SMEs)) and to the FGCC drove a considerable proportion of the developments affecting the grocery sector during the 2012-2015 period. While Billson was to retire in late 2015, having been ousted from Cabinet courtesy of a Turnbull reshuffle which returned competition policy to the Treasury portfolio (a relief for some), it was not before many of his causes came to fruition. In particular, the lead up to his exit saw the introduction of unfair contract laws for small business, the government's final endorsement of an effects test for s 46, and last by no means least in the present context – the enactment of the FGCC.

A more nuanced but arguably no less important role was played by the AFGC over this period. The strong voice of its CEO, Kate Carnell, in the 2010-2011 inquiries, calling for a replication of the UK grocery reforms in Australia, is documented below. Fittingly perhaps, upon leaving the supplier body,

Carnell went on to become the country's first federal Small Business and Family Enterprise (SBFE) Ombudsman. Her successor, Gary Dawson, had a somewhat different, arguably more muted, style and this was evidently an important factor in bringing the AFGC and the MSCs together in what some might regard as an unexpected and possibly unparalleled episode of collaboration to negotiate a code that would become the FGCC. Dawson showed himself to be adept at working across the industry and government, finding common ground and where necessary making the compromises that he regarded as justifiable in taking action that would substantively improve retailer-supplier relations. This he saw as genuinely in the interests not just of AFGC members but suppliers generally, the retailers too and ultimately consumers. Like Billson, Dawson leaves a particular legacy in this regard. However, his decision to resign from the organisation at the end of March 2017 also leaves a question mark over the role that the AFGC will play in the future, most immediately the stance it will take in preparing for and participating in the FGCC's 2018 review (see further Part 7).

## I. The watchdog, watching and being watched: the ACCC

As should be evident from the account in Part 3 above, farmers, suppliers and politicians were not the only ones under pressure as the calendar ticked over to 2010. The competition / consumer watchdog too may have been feeling the heat. In both milk inquiries, the ACCC had been in the firing line. In the 2010 parliamentary inquiry, submitters were scathing of the Commission's approval of National Foods' acquisition of Dairy Farmers having regard, in particular, to its impact on competitive dynamics in the Tasmanian dairy market:

*Who in their right mind would approve National Foods taking over Dairy Farmers? ...That would have to be the biggest blunder that has ever happened to the Australian dairy industry (Grant Rogers, Tasmanian farmer).<sup>224</sup>*

*...it seems extraordinary to us as ordinary dairy farmers that the ACCC allowed the takeover of Dairy Farmers by National Foods, which in a sense is almost creating a monopoly (Phil Beattie, Tasmanian Suppliers Collective Bargaining Group).<sup>225</sup>*

*...quite frankly I think the ACCC, through Mr Graeme Samuel, was really asleep at the wheel in allowing National Foods to buy Dairy Farmers in the first place, as it was a direct competitor to them in the marketplace... (John Oldaker, Chairman, Cadbury Suppliers).<sup>226</sup>*

In addition to being portrayed as at least in part responsible for the increased level of concentration amongst processors (criticism that may have been ringing in the ACCC's ears when it expressed concerns in the same year about a proposed acquisition by Murray Goulburn of Warrnambool

<sup>224</sup> Grant Rogers, Tasmanian farmer, *Committee Hansard*, 5 November 2009, p. 11, cited in SERC, *Milking it for all its worth* 2010, p. 63.

<sup>225</sup> Phil Beattie, Tasmanian Suppliers Collective Bargaining Group, *Committee Hansard*, 5 November 2009, p. 24, cited in SERC, *Milking it for all its worth*, 2010, p. 63.

<sup>226</sup> John Oldaker, Chairman, Cadbury Suppliers, *Committee Hansard*, 6 November 2009, p.7, cited in SERC, *Milking it for all its worth*, 2010, p. 63.

Cheese, leading to the withdrawal of the bid),<sup>227</sup> there were questions raised about the agency's capacity to impartially investigate market power abuses by the behemoth businesses created post merger approvals. On this issue, the Senate Committee concluded in its 2010 report that:

*There is inadequate assessment of whether markets have become excessively concentrated because the agency assessing this (the ACCC) is the same agency that approved the mergers leading to the high degree of concentration. The Committee is also concerned that the 'public interest' which the ACCC seeks to protect appears to be restricted to consumers and it does not pay sufficient attention to ensuring that farmers get a fair deal...<sup>228</sup>*

It recommended that the PC look into the matter and consider whether separate agencies were required.<sup>229</sup>

In 2011, the spotlight was on the ACCC again, this time in relation to its response to Coles' milk price cuts and its investigation into whether the conduct constituted so-called predatory pricing, in breach of the misuse of market power provisions of the CCA. The inquiry that year heard submissions questioning whether the ACCC had been sufficiently proactive or prompt in its response, a strong element in which was that, if indeed the Commission had been investigating, it had not announced as much – hence stakeholders were left in the dark as to whether their concerns were being taken seriously:

*We wonder if the ACCC is providing leadership in the area of supermarkets. They might be doing a lot of things behind the scenes... I suppose I got the impression—and this is a broad impression I got—that the ACCC does not always signal what they are doing in terms of investigation. I do not know if that applies to supermarkets. I think it was argued that perhaps there needed to be more prominent smoke signals, as it were, to the ACCC. Basically, they have been very quiet on this whole issue. I think many people would have looked to them to have real guidance in terms of what was and was not predatory pricing and what was and was not in the consumer interest (Christopher Zinn, Director, Campaigns and Communications, CHOICE).<sup>230</sup>*

*From what we have seen, the ACCC likes to watch. They take a long time to investigate. They could not even answer the question on whether they could give an answer about their investigation before the end of the year. If we have to wait beyond the year then there is*

<sup>227</sup> In 2013 Murray Goulburn attempted the acquisition again however lost out to a successful competing bid by Canadian dairy giant, Saputo Inc. The ACCC again registered concerns about the cooperative's proposal and was criticised for failing to recognise or give sufficient weight to the benefits that the acquisition would have had for the Australian dairy industry, in export market growth in particular. See, 'Murray Goulburn waits as Hockey approves Saputo bid', *Dairy News Australia*, 12 November 2013; ACCC's Issues Paper – ACT No. 4 of 2013 *Re Proposed acquisition of Warrambool Cheese and Butter Factory Company Holdings by Murray Goulburn Co-Op Co Ltd.*

<sup>228</sup> SERC, *Milking it for all its worth*, 2010, p. 65.

<sup>229</sup> SERC, *Milking it for all its worth*, 2010, recommendation 9, p. 66

<sup>230</sup> Christopher Zinn, Director, Campaigns and Communications, CHOICE, *Committee Hansard*, 29 March 2011, cited in SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. 81.

*something seriously wrong with someone's investigative processes (Associate Professor Frank Zumbo).<sup>231</sup>*

*I suppose I got the impression—and this is a broad impression I got—that the ACCC does not always signal what they are doing in terms of investigation. I do not know if that applies to supermarkets. I think it was argued that perhaps there needed to be more prominent smoke signals, as it were, to the ACCC. Basically, they have been very quiet on this whole issue. I think many people would have looked to them to have real guidance in terms of what was and was not predatory pricing and what was and was not in the consumer interest (Christopher Zinn, Director, Campaigns and Communications, CHOICE).<sup>232</sup>*

As became obvious in the course of the inquiry, the ACCC had indeed been investigating, and actively so. Its 'behind the scenes' approach in this regard was consistent with its longstanding policy not to comment on investigations out of sensitivity to procedural fairness. However, owing to the substantial public interest in the milk pricing issue, in this instance the ACCC had in fact issued a media release, albeit only upon conclusion of its investigation, declaring there to be no evidence of unlawful conduct. Coles had not acted with an anti-competitive purpose, which was an element required for liability under s 46 of the Act.<sup>233</sup>

It was evident that the Committee had wrestled with whether the ACCC's handling of the matter warranted criticism. Ultimately, taking a middle ground position, it acknowledged the independence of the agency, the need to protect the integrity of its investigative processes and the importance of not unfairly damaging reputations of those subject to such processes, but at the same time called for additional transparency in the Commission's enforcement activities. In relation to the latter the Committee noted that 'at times, there can be significant concern within certain sectors and the wider community regarding the effectiveness of the ACCC in enforcing the CCA'<sup>234</sup> - hence more information about what the agency is actually doing 'could help ensure that the public is confident that matters are being taken seriously, and increase the accountability of the ACCC'.<sup>235</sup>

### (a) Yet more public inquiries, yet more pressure on the ACCC

Given the public and political focus, it is not perhaps not surprising that from 2011 onwards the grocery sector became more of a focus for the ACCC, at least as manifest in enforcement action. Following the conclusion of the ACCC Grocery Inquiry, the agency had only a few loose ends to tie up. In late 2009 it dealt with the issue identified in the inquiry regarding the use of restrictive covenants in lease agreements for supermarket space that were hampering independent supermarket

<sup>231</sup> Associate Professor Frank Zumbo, *Committee Hansard*, 9 March 2011, p. 50, cited in SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. 81.

<sup>232</sup> Christopher Zinn, Director, Campaigns and Communications, CHOICE, *Committee Hansard*, 29 March 2011, p. 92 cited in SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. 81.

<sup>233</sup> ACCC Media Release, 'ACCC: Coles discounting of house brand milk is not predatory pricing', 22 July 2011.

<sup>234</sup> SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, recommendation 5, p. xvii.

<sup>235</sup> SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, p. xvii.

operators from setting up shop in large retail centres.<sup>236</sup> Consistent with what had come to be known as Chairman Samuel's trademark backroom dealing style, the approach taken with respect to this issue was to negotiate first with Coles and Woolworths and then with other retailers to obtain enforceable undertakings by which there was agreement not to include such provisions in any new supermarket leases and not enforce any existing provisions.<sup>237</sup> In 2009 and 2010 the Commission examined the competitive implications in petrol markets of cross-promotions between fuel and grocery sales but decided no action was warranted (a stance that would change under Samuel's successor).<sup>238</sup> It also undertook a range of activities aimed at securing greater compliance with both the Unit Pricing Code and the HCC,<sup>239</sup> again areas identified in its 2008 report where there could be further work done in the sector.<sup>240</sup>

In late 2010 the ACCC announced its decision to oppose the acquisition by Metcash of the Franklin supermarket business from the cash-strapped South African Pick n Pay business.<sup>241</sup> This decision was consistent with the finding in its 2008 report that Metcash's wholesale pricing policies were a significant factor inhibiting independent retailers from competing aggressively on price with the MSCs.<sup>242</sup> Based on a much criticised approach to defining the relevant market, the ACCC's opposition was on the grounds that the acquisition would reduce the number of players competing to provide wholesaling services to medium to larger sized supermarkets from two to one, effectively giving Metcash a wholesaling monopoly in New South Wales. Metcash's aim was to re-sell Franklins' 77 company-owned stores to independent operators, making its profit from the deal by becoming the wholesale supplier to the expanded network of supermarkets. A handy side effect of the deal was that Franklins agreed to end a long-running legal action against Metcash relating to a claim that Metcash owed it millions of dollars in rebates when it was Franklins' wholesale supplier of groceries.<sup>243</sup> Given the ACCC's stance, instead of its IGA stores increasing their share of NSW supermarket sales from 11 to 18%, it was reported that 'the likelihood was that the Franklins chain

<sup>236</sup> ACCC 2008 Grocery Inquiry, [9.4.2] at pp. 184-189; ACCC Media Release, 'ACCC focuses on lasting change in the supermarket sector', 11 August 2009.

<sup>237</sup> ACCC Annual Report 2009-10, p. 41; ACCC Media Release, 'Supermarket agreement opens way for more competition', 18 September 2009.

<sup>238</sup> Ashley Hall, 'ACCC tells independent grocery to match supermarket petrol discounts', *ABC PM*, 15 July 2009.

<sup>239</sup> ACCC, *Annual Report 2008-09*, p. 8; ACCC, *Annual Report 2010-11*, p. 66.

<sup>240</sup> Unit pricing is the practice of displaying the price by unit of measure along with the total sale price of each item. In its Grocery Inquiry report, the ACCC found that while the introduction of unit pricing would impose costs on retailers, these would reduce over time (p. 451), and that there was broad support for unit pricing from consumers (p. 450). Both Coles and Woolworths supported the introduction of a mandatory unit pricing scheme (p. 452) and the ACCC recommended, 'a mandatory, nationally-consistent unit pricing regime be introduced for standard grocery items both on in-store price labels and in print advertising' and that this regime apply to 'significant supermarkets' (20.8. p. 456). An assessment of the effectiveness of the HCC was one of the terms of reference of the Grocery Inquiry (p. 388). The ACCC undertook a detailed review of the Code, finding ultimately it was not operating as effectively as anticipated and recommending a range of amendments, including that: the CCA, 'be amended to introduce civil pecuniary penalties and infringement notices for a breach of a mandatory code made under Part IVB such as the Horticulture Code and that the ACCC be given powers to facilitate the conduct of random record audits as an enforcement mechanism under the code.' (18.5.5. p. 400); and 'that the Horticulture Code be extended to regulate first point of sale transactions of horticulture produce between a grower and a retailer, exporter or processor.' (18.5.6. p. 406). The ACCC also recommended several amendments be made to the way that contracts and transactions were conducted under the Code (18.5.8. p. 410) and found that further education was needed in relation to dispute resolution procedures available under the Code. It was recommended that these be subsidised by the Government (8.5.13. p.420).

<sup>241</sup> ACCC Media Release, 'ACCC to oppose Metcash proposed acquisition of Franklins supermarket', 17 November 2010.

<sup>242</sup> ACCC 2008 Grocery Inquiry, p. 145.

<sup>243</sup> Elizabeth Knight, 'Metcash defies competition ruling on supermarkets', *InvestSMART*, 24 November 2010.

would be broken up, and buyers of the stores were likely to include the industry gorillas, Woolworths and Coles'.<sup>244</sup>

Again, the Commission resisted litigation as a way to resolve the issue – an application to the court to prevent the acquisition would have seen its economic analysis judicially tested. No such application was made and Metcash called the agency's bluff, indicating in response to the ACCC's decision that it would complete the transaction in five business days unless the Commission applied for an injunction to restrain it. The ACCC folded, filing an action in the Federal Court, which it eventually lost on appeal.<sup>245</sup> In the meantime, Metcash CEO, Andrew Reitzer, had been ratcheting up the political heat on the Commission – reportedly having lobbied for a Senate Economics References Committee inquiry into the ACCC's opposition. This was portrayed by some as having a distinctly acrimonious personal flavour – the move as tantamount to a declaration of war on the competition chief, Graeme Samuel AC, as it would force the agency boss to face questioning from the Committee. As one interviewee put it:

*I believe that Graeme Samuel had a personal issue with Metcash. Not Metcash, but with the former CEO, Andrew Reitzer. My understanding is that they very much had a conflict. A public conflict and I don't think that Graeme Samuel ever forgot about it.*<sup>246</sup>

It is not only highly unusual that the Committee would be convened to scrutinise an individual regulatory decision, but the sequence of events and timetable for the inquiry was so astonishingly fast as to suggest that this was far from run of the mill parliamentary business. The ACCC announced its decision on 17 November 2010,<sup>247</sup> the Senate referral took place on 23 November<sup>248</sup> and Nationals Senator Ron Boswell, who had led the Senate motion for the reference,<sup>249</sup> was reported as saying that the Committee would report back by 17 December, 'after it has asked Mr Samuel to explain why the commission made a decision that seemed to give independent supermarket operators less market clout than before.'<sup>250</sup> The Committee handed down an interim report on 6 December and 2 days later the ACCC filed its Federal Court application, one result of which was that the Committee's proceeding became largely redundant.

Not only was this the third parliamentary inquiry with a grocery sector focus in the space of just three years, it was the third in which an individual regulatory decision of the ACCC was the subject of Senate committee scrutiny - the National Foods-Dairy Farmers acquisition having been examined in the first milk inquiry which was convened in September 2009 and reported in May 2010 and the investigation into Coles milk price cuts having been a focus in the second milk inquiry which was convened in January 2011 and reported in November 2011.

<sup>244</sup> Elizabeth Knight, 'Metcash defies competition ruling on supermarkets', *InvestSMART*, 24 November 2010.

<sup>245</sup> ACCC Media Release, 'ACCC responds to Metcash decision', 5 December 2011.

<sup>246</sup> Transcript of interview, CEO of MGA, p. 30. See also Association of Sales and Marketing Companies Australia Update, vol. 8/35 2 December 2010.

<sup>247</sup> ACCC media release, 'ACCC to oppose Metcash proposed acquisition of Franklins supermarkets', 17 November 2010.

<sup>248</sup> ACCC 2010-11 Annual Report, p. 128.

<sup>249</sup> Journals of the Senate, No. 13 – 23 November 2010, Parliament of the Commonwealth of Australia, p. 398.

<sup>250</sup> Elizabeth Knight, 'Metcash defies competition ruling on supermarkets', *InvestSMART*, 24 November 2010.

Around the same time the ACCC contributed comments to yet a further two other parliamentary inquiries that had a substantial grocery sector and MSC-related focus: the House of Representatives Standing Committee on Economics inquiry into the Constitutional Corporations (Farmgate to Plate) Bill 2011 and Competition and Consumer Amendment (Horticulture Code of Conduct) Bill 2011,<sup>251</sup> and the Senate Select Committee inquiry into Australia's Food Processing Sector.<sup>252</sup> In the House of Representatives Committee's report, although the Committee recommended neither bill be passed, it did note that the ACCC's 2008 rejection of a widening gap between farmgate and retail prices was under question.<sup>253</sup>

In the Senate Select Committee report, an entire chapter was devoted to competition issues afflicting the food processing sector. As is evident from the chapter, echoing the questions raised in the first milk inquiry and looking for explanations of the level of concentration in the sector, the inquiry involved questioning of the ACCC's effectiveness in performing its merger review function.<sup>254</sup> Concerns about the growing penetration of private label products were also revisited, highlighting again the implications of the MSCs competing with their suppliers, and also the prospect of a reduction in consumer choice over the long run.<sup>255</sup>

Furthermore, contrary to the ACCC's 2008 finding regarding an absence of serious issues in supply chain relationships, the Committee expressed concern about the imbalance of bargaining power between retailers and suppliers. Contrary to Samuel AC's account of why suppliers were reluctant to speak out in the ACCC Grocery Inquiry (see Part 1 of this report), the Committee heard enough from grower associations and other representative groups to accept that such reluctance was on account of fear of commercial retribution. It made a strong appeal to suppliers to approach the ACCC with evidence of 'specific instances of abuses of market power' by the MSCs in contract negotiations and, like the Committees before it, called for review of the misuse of market power provisions of the CCA.<sup>256</sup> It further proposed that consideration be given to including the functions of a food supply chain ombudsman within the ongoing role of the ACCC,<sup>257</sup> resisting calls for a mandatory code to regulate supplier-retailer relations with a separate ombudsman, at least until there had been a proper investigation as to why the existing office (referring to the PGCC Ombudsman) was not effective.<sup>258</sup>

Just as in the milk inquiries, both parliamentary reports had implicit if not explicit strains of concern that while competition in the retail grocery sector might be benefitting consumers, the benefit may only be short term. Thus, while the Senate Select Committee acknowledged 'the need for the CCA to

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<sup>251</sup> House of Representatives Standing Committee on Agriculture, Resources, Fisheries and Forestry, *Advisory Report on the Constitutional Corporations (Farm Gate to Plate) Bill 2011 and Competition and Consumer Amendment (Horticultural Code of Conduct) Bill 2011*, March 2012 (HOR, *Farm Gate to Plate and Horticultural Code Bills*, 2011).

<sup>252</sup> Senate Select Committee on Australia's Food Processing Sector, *Inquiry into Australia's food processing sector*, August 2012 (SSC, *Australia's Food Processing Sector*, 2012).

<sup>253</sup> HOR, *Farm Gate to Plate and Horticultural Code Bills*, 2011, [2.10]-[2.11].

<sup>254</sup> SSC, *Australia's Food Processing Sector*, 2012, [3.22]. Treasury too was questioned about this, from a policy perspective, the Committee concluding that it found the assertions of Treasury officials on the matter 'less than reassuring' [3.30]. It called for the effectiveness of s 50 of the CCA in addressing creeping acquisitions to be reviewed yet again (despite that section having been amended in December 2011) [3.31].

<sup>255</sup> SSC, *Australia's Food Processing Sector*, 2012, [3.14-3.69].

<sup>256</sup> SSC, *Australia's Food Processing Sector*, 2012, [3.68], [3.91], [3.108], [3.118].

<sup>257</sup> SSC, *Australia's Food Processing Sector*, 2012, [3.109].

<sup>258</sup> SSC, *Australia's Food Processing Sector*, 2012, [3.115].

protect and promote the interests of consumers and ensure food remains affordable', it also expressed concern 'that soon the "pendulum" might swing so far in favour of the short-term interests of consumers that research and development, innovation and diversity will be lost in the market place and consumers begin to lack choice and may face increased prices.'<sup>259</sup> Further both reports suggested that up to that point insufficient consideration had been given to the adverse impacts of such competition on other groups in society – farmers and food manufacturers specifically – such that there was seen to be a not insignificant threat to the future viability of these sectors, with wide ranging social and economic repercussions.

Further, in its Issues Paper in relation to the NFP, released in June 2011, the government identified competition in the food sector as being 'essential to ensuring efficient use of resources and encouraging rapid uptake of new technologies in food production and services'<sup>260</sup> and highlighted the current level of competition in the grocery sector as a matter causing concern to some stakeholders.<sup>261</sup> In particular, it was noted that 'recent strong price competition between major supermarkets, which is placing downward pressure on grocery prices, is raising some stakeholder concerns about the impact on prices received by food processors'.<sup>262</sup> However the Issues Paper stated that the Australian Government believed, 'competition is by far the most effective means of exerting downward pressure on grocery prices'.<sup>263</sup> Relying on the ACCC Grocery Inquiry finding, it was determined that the best way to address price competition issues was, 'to lower barriers to entry and expansion'.<sup>264</sup> The paper fell back on the ACCC inquiry finding that there was no evidence that MSCs were acting in an anti-competitive manner when dealing with fresh produce suppliers.<sup>265</sup>

In line with this, the NFP White Paper, while acknowledging the concerns of 'many stakeholders' that the dominance of the two MSCs was negatively impacting competition in the sector, concluded that the sector was continuing to evolve and that the expansion of Aldi and Costco, along with the increased popularity of alternative shopping options such as farmers' markets, meant that the sector was competitive. The NFP cited the work that was currently underway to create an industry-driven voluntary code of conduct (a reference to the RSR described in Part 5 below), and the increased activity of the ACCC in monitoring supplier relationships in the sector as evidence that the concerns raised by stakeholders were being addressed. Further, the NFP cautioned against allowing regulation to, 'stifle competition or impose unnecessary red tape and costs' that may lead to higher food prices.<sup>266</sup>

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<sup>259</sup> SSC, *Australia's Food Processing Sector*, 2012, [3.68].

<sup>260</sup> DAFF 2011, *Issues paper to inform development of a national food plan*, Department of Agriculture, Fisheries and Forestry, Canberra, (NFP issues paper, 2011), p. 31.

<sup>261</sup> NFP issues paper, 2011, p. 31.

<sup>262</sup> NFP issues paper, 2011, p. 31.

<sup>263</sup> NFP issues paper, 2011, p. 31.

<sup>264</sup> NFP issues paper, 2011, p. 31.

<sup>265</sup> NFP issues paper, 2011, p. 32.

<sup>266</sup> NFP issues paper, 2011, p. 50.

## (b) A new leader at the helm

Given the level of political attention on the sector, and the fact that it was not only the powerful industry players but the (some might say) equally powerful enforcement agency in the firing line, it is hardly surprising that in 2011 the grocery sector was elevated officially to a corporate priority for the ACCC. It was also the year when there was a change-over at the helm, Rod Sims taking over from Graeme Samuel AC as Chairman. Both had completed their undergraduate studies at the University of Melbourne. However while Samuel's education had had a legal focus (he completed a Bachelor of Laws before undertaking a Master of Laws from Monash University), Sims is an economist through-and-through, with a first class honours degree in Commerce from the University of Melbourne and a Master of Economics from the Australian National University. Both men had had experience in the private sector - Samuel, in particular, as a past president of the Australian Chamber of Commerce and Industry, having worked in law and investment banking, and in 2000 having been appointed an honorary fellow of the Australian Institute of Company Directors.<sup>267</sup> Sims in turn had more of a public policy background. His previous roles included Chair of the Independent Pricing and Regulatory Tribunal of NSW and Deputy Secretary in the Commonwealth Department of Prime Minister and Cabinet responsible for economic, infrastructure and social policy.<sup>268</sup>

It is notable perhaps that when Samuel was nominated for the role of ACCC Chairman by the then Liberal Federal Treasurer Peter Costello, the Labor States, in a rare split with the federal government, rejected his nomination. In part this was seen to be because they feared he would be soft on big business.<sup>269</sup> Sims, Bob Hawke's former Chief Economic Adviser, was nominated by the Labor Gillard Government.<sup>270</sup> While some believe Samuel was too close to big business – Council of Small Business Australia (COSBOA) CEO Peter Strong has been reported as referring to Samuel as 'an apologist for big business',<sup>271</sup> Sims' chairmanship too has been coloured at times by a tendency to draw ire from the big end of town. Reflecting on his at times fraught relations with the MSCs, one interviewee said, 'Rod Sims in particular had a view that Coles had become cavalier about its responsibilities, particularly driven by [a] view of the then MD Ian McLeod, and they didn't have a very great relationship...'<sup>272</sup>

The stylistic if not ideological differences between the two were evident in the recent and very public opinion war waged between Sims (supported in his views by former ACCC Chair Allan Fels AO and the architect of the 2015 Competition Policy Review, Ian Harper) on the one hand, and Wesfarmers CEO Richard Goyder (supported in his views by Samuel AC), on the other in early 2016. At times the

<sup>267</sup> Professor Graeme Samuel AC, CEDA Council on Economic Policy, <http://www.ceda.com.au/about/governance/ceda-council-on-economic-policy/samuelgraeme>.

<sup>268</sup> ACCC Chairs & Commissioners, Chairman Rod Sims, <https://www.accc.gov.au/about-us/australian-competition-consumer-commission/accc-chair-commissioners>.

<sup>269</sup> Stephen Long, 'States reject Graeme Samuel as ACCC head', *AM transcript*, Wednesday 13 November 2002.

<sup>270</sup> Media release, 'Government nominates Rod Sims and ACCC Chairman', 3 May 2011.

<sup>271</sup> Peter Strong, 'Why an effects test could help fix our failed competition policy', *Smart Company*, 3 September 2014. In our interview with him, Strong repeated the observation: 'He [referring to Samuel] was a big business apologist ... I've had a lot of blues with him, he doesn't talk to me anymore ... he would just blame the small business ... [and] I'd say, "you're blaming the victim here."' See Transcript of interview, CEO of COSBOA, p. 25.

<sup>272</sup> Transcript of interview, MSC representative, p. 26.

two sides appeared trapped in 'a bitter deadlock' over the proposed strengthening of misuse of market power laws. While Goyder warned that the so-called 'effects test' for s 46 of the CCA would 'chill competition'<sup>273</sup> Sims is reported to have countered with a veiled threat that, 'companies that want to compete on their merits have nothing to fear. Only those who wish to exclude their competitors and damage the competitive process will need to re-examine their conduct.'<sup>274</sup> If the way in which Samuel handled the issue of restrictive covenants after the ACCC Grocery Inquiry is any guide, it might be surmised that he would have dealt with the difference of opinion quite differently – picking up the phone to Goyder perhaps, rather than going head to head in the mainstream media.

In its 2011-12 Annual Report the Commission recorded having undertaken a 'strategic enforcement review' with a particular focus on concentrated markets, as exemplified by 'supermarkets and fuel'<sup>275</sup> and looking ahead, it indicated that its enforcement and compliance priorities would continue to include 'acting on competition and consumer issues in highly concentrated sectors, in particular supermarkets and fuel.'<sup>276</sup> Notably also, close attention was to be paid to alleged unconscionable conduct, in both business-to-business and business-to-consumer markets; and to instances of alleged misuse of market power by firms that have a substantial degree of power in any market.<sup>277</sup> If not already obvious, the relevance of this to the MSCs specifically became evident in late 2012-early 2013.

In its review of the year in its 2012-13 Annual Report, the ACCC identified maintenance and enhancement of competition in 'concentrated markets' as having been one of five key objectives. To that end the report recorded that the Commission had commenced investigations into potential unconscionable conduct by the MSCs relating to their dealings with suppliers and into shopper dockets, as well as into potential misuse of market power in connection with their supply of house brand products.<sup>278</sup> That year it also announced a particular focus on incremental (creeping) small retail acquisitions by the MSCs.<sup>279</sup> It was also in 2012 that discussions at a government-industry forum initiated the process of development of what became the FGCC and the ACCC reported on its engagement with this process during the course of that year.<sup>280</sup>

To some extent, for those inclined to regard the ACCC as influenced by populist or political pressures, this surge in focus and activity post-2010 could be interpreted as the Commission responding to the degree of public noise and heat surrounding the MSCs over this period. As one interviewee commented (albeit more by way of observation of objective reality than by way of criticism):

*They're [referring to the ACCC leadership] have to be very politically savvy, because they depend on government money. And they go before Senate estimates every year, twice a year, to explain their performance to the Senate. ... They're appointed by federal and state*

<sup>273</sup> Patrick Durkin, 'Goyder joins Samuel in war over ACCC powers', *AFR*, 12 January 2016.

<sup>274</sup> Patrick Durkin, 'ACCC chairman Rod Sims: 'Nothing to fear' from effects test', *AFR*, 17 March 2016.

<sup>275</sup> ACCC, *Annual Report 2011-12*, p. 5.

<sup>276</sup> ACCC, *Annual Report 2011-12*, p. 8.

<sup>277</sup> ACCC, *Annual Report 2011-12*, p. 8.

<sup>278</sup> ACCC, *Annual Report 2011-12*, p. 8.

<sup>279</sup> ACCC, *Annual Report 2012-13*, p. 45.

<sup>280</sup> ACCC, *Annual Report 2012-13*, p. 185.

*governments as well. So they're very politically savvy. And they do play – and they're very attentive and play to political perceptions about big business...it was the political and media focus on the issue that drove the regulators.*<sup>281</sup>

A not dissimilar view is taken by a former member of a MSC board of directors who expressed sympathy for the ACCC with regard to its limited resources when he said, 'I think they are forced to take on the cases that might have more political connotations and I can understand that.'<sup>282</sup> A further perspective, offered by a current MSC representative and reflecting specifically on the ACCC's unconscionability cases against the MSCs, was that 'when you get a new law you've got to show that you're going to use it especially if you've lobbied for it hard so the ACCC will, like, they will be under some, not pressure, but people will want to see when the new law comes in that there's activity in the area.'<sup>283</sup>

For others, the ratcheting up of enforcement activity against the MSCs was more or perhaps also a function of the particular views or style of the then new Chairman. For one critic, there was evident frustration with the approach of the former Chairman:

*...we've known it's [referring to the type of conduct that was the subject of the ACCC's unconscionability cases] been going on for 25 years, so why has it taken this incredible determination from one particular ACCC chairman? Surely the previous chairman saw that, but no, the previous chairman did not see that. Or maybe saw it, but wasn't at all perturbed. The fact is, it's been happening for a long, long time and suppliers have been held to ransom....*

*I think the ACCC, under the auspices of Graeme Samuel, was very aware of our concerns, but was never willing to do anything. And I don't think that Graeme Samuel left much of a legacy in that area at all. And the current chairman, I think realised that there is an issue and that there is a threat to the Australian public of large organisations actually behaving - misbehaving. Their conduct being exclusionary and that kind of thing...*

*What's happened is that you've had - you've got a regulator that has an appetite now to investigate, as it should do, misdemeanours. Investigate accusations of breaches in the law. And that's what a regulator should do.*<sup>284</sup>

Others saw the shift in ACCC approach as reflecting both the change in political environment (as the government moved from a majority (under Kevin Rudd, from 2007 to 2010) to a minority (under Julia Gillard and then Kevin Rudd, from 2010 to September 2013), as well as a change in the personal style of the ACCC leader:

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<sup>281</sup> Transcript of interview, Robert Hadler, pp.13-14.

<sup>282</sup> Transcript of interview, former member of a MSC board of directors, p. 30.

<sup>283</sup> Transcript of interview, MSC representative, p. 33.

<sup>284</sup> Transcript of interview, CEO of MGA, pp. 3, 8, 16.

*...when Graham Samuel was head of the ACCC and he did the 2008 review, he's very bright, very analytical and he was dealing with a government that didn't see it, didn't want to do anything about it, really. Because they saw supermarkets providing value to consumers. They were big employers, it was a Labor government, it was the SDA; it was close to the ALP. So they referred it to Graham. There was a report done. Said that there was nothing fundamentally wrong in the competitive environment. Clearly, there were things wrong in the macro-economic environment. But not in the competitive environment. And was confident that he had the tools to manage it. Now Graham's modus operandi was to say - was if an issue arose, he would ring the CEOs of the major supermarkets and say, "Look, there's an issue. Whether it's perception or not, we don't need to have a fight over it. If we do this deal, it goes off the radar screen." And the deal would be done. So supermarket leases in big retail centres was a major issue. Graham brokered a deal for that. So that was a phase and a cycle and a personality issue. Change of the phase and the cycle, where government changed. The economic environment changed, became a lot tougher for suppliers. The small business supplier started complaining. And Rod Sims came in. And I felt sorry for Rod, because he was probably the first chairman of the ACCC, who had to work to a minority government. And a Senate dominated by independents. Therefore, he had to be very cognisant of the issues they were raising. You know, I know Rod. I used to work with him in Prime Minister in Cabinet in the 80s. Very smart, former Labor policy advisor. But he – unlike Graham, he would not ring and head off a problem. He would say, "We're going to take action over a problem." And he would go through and he would aggressively pursue the law. So I think different styles, different people at different phases, had a big impact on regulation.<sup>285</sup>*

### (c) The enforcer takes aim

Almost immediately upon his appointment, Sims signalled that his approach would be a more litigious one. In 2011, in his first speech to the Law Council of Australia's Competition and Consumer Committee annual workshop after becoming Chairman, Sims made it clear that, under his watch, the Commission would be taking more litigation risks, in particular when it came to matters of predatory pricing and possible breaches of s 46 for taking advantage of substantial market power.<sup>286</sup> In Sims' view the ACCC's close to 100% success rate in first instance litigation was, 'frankly too high', as it suggested the Commission had become too 'risk averse'.<sup>287</sup> By taking a more aggressive approach to litigation Sims believed it was important both that action would be seen to be taken (presumably by the general public, as well as by those operating under these laws), and that the existing laws would thereby be tested in the courts.<sup>288</sup> Sims also let it be known that the ACCC would, 'be increasingly

<sup>285</sup> Transcript of interview, Robert Hadler, p. 10.

<sup>286</sup> Rod Sims, *Future Directions*, speech to the Law Council Workshop, 2011, p. 4.

<sup>287</sup> Rod Sims, *Future Directions*, speech to the Law Council Workshop, 2011, p. 5.

<sup>288</sup> Rod Sims, *Future Directions*, speech to the Law Council Workshop, 2011, p. 5.

assessing whether quick action in applying for interlocutory orders is necessary to stop conduct that is detrimental to consumers or the market.’<sup>289</sup>

Sims kept his word. As a compliance consultant observed of the ACCC under Sims, ‘its enforcement / litigation-focused, it’s not compliance focused.’<sup>290</sup> This view is supported by another industry commentator who observed, ‘my impression of the ACCC is it’s an organisation that measures its performance by how many cases it brings, not by what its impact is on consumers.’<sup>291</sup> Regardless of whether such observations have merit (a matter on which minds would differ), there is no doubt that, from 2012 onwards, ACCC scrutiny and enforcement activity against the MSCs picked up considerably.

In 2012 and 2013 the ACCC instituted a number of cases concerning credence claims in the food industry, which the ACCC viewed as having the potential to significantly impact consumers and the competitive process. Examples included an action against Coles for false, misleading and deceptive conduct in the supply of bread that was partially baked and frozen off site, transported to Coles stores and ‘finished’ in-store, and then promoted as ‘Baked Today, Sold Today’ and/or ‘Freshly Baked In-Store’ at Coles’ in-house bakeries.<sup>292</sup> A similar investigation triggered by a complaint that Coles was displaying imported navel oranges and kiwi fruit underneath signs that read ‘Helping Australia Grow’ and featuring the ‘Australian Grown’ symbol saw Coles receive six infringement notices totalling \$61,200 for alleged misleading representations about the country of origin of fresh produce made in five of its stores.<sup>293</sup>

In February 2013, the ACCC made clear that in addition to ongoing areas of priority across the economy, one of its particular focuses for the year ahead would be yet again, ‘competition and consumer issues arising in highly concentrated sectors, especially the supermarket and fuel sectors.’<sup>294</sup> In a statement tabled at a hearing of the Senate Economics Committee to update the Committee on the ACCC’s investigation into supermarket-supplier issues that same month,<sup>295</sup> Sims outlined allegations raised with the ACCC, including that some supermarket conduct did not conform with, ‘acceptable business practice and may be unconscionable or a misuse of market power, including in their supply of house brand products.’<sup>296</sup> The ACCC had been actively seeking information from suppliers from early 2012 about their dealings with the MSCs. As one supplier said, ‘the ACCC came to us and said, “we understand that you transact with Coles and that you’ve been involved in the ARC Scheme [a reference to a scheme that was to become the subject of the ACCC’s subsequent unconscionability suit against the retailer] and we want to see all the correspondence

<sup>289</sup> Rod Sims, *Future Directions*, speech to the Law Council Workshop, 2011, p. 4.

<sup>290</sup> Transcript of interview, interviewee that consults to / advises grocery businesses, p. 37.

<sup>291</sup> Transcript of interview, former senior representative of the UK OFT, p. 10.

<sup>292</sup> ACCC *Annual Report* 2012-13, p. 72.

<sup>293</sup> ACCC *Annual Report* 2012-13, p. 74.

<sup>294</sup> ACCC *Annual Report* 2012-13, p. 34.

<sup>295</sup> See the Chairman’s statement dated 13 February 2013, tabled at an Additional Budget Estimates hearing of the Senate Economics Committee at

[http://www.aph.gov.au/Parliamentary\\_Business/Committees/Senate\\_Committees?url=economics\\_cte/estimates/add\\_1213/index.htm](http://www.aph.gov.au/Parliamentary_Business/Committees/Senate_Committees?url=economics_cte/estimates/add_1213/index.htm)

<sup>296</sup> ACCC *Annual Report* 2012-13, p. 38.

associated with it.”<sup>297</sup> According to a spokesperson from one of the MSCs, ‘[around this period] the ACCC were relentless in their pursuit to find things that were wrong.’<sup>298</sup>

In December 2013 the ACCC instituted proceedings in the Federal Court against Colgate-Palmolive Pty Ltd, PZ Cussons Australia Pty Ltd, a former sales director of Colgate, and Woolworths regarding alleged cartel conduct and anti-competitive arrangements in supplying laundry detergents. It was alleged that Woolworths were knowingly concerned in the arrangements. The ACCC won the case to the tune of \$18m in penalties against the detergent manufacturer, landing \$9m against its MSC accessory.

In its 2014 Compliance and Enforcement Policy, for the fourth consecutive year, the ACCC identified competition and consumer issues arising in highly concentrated sectors, in particular the supermarket and fuel sectors, as priorities.<sup>299</sup> In line with this, the agency began separate actions in the Federal Court against Coles and Woolworths for allegedly breaching court enforceable undertakings made to the ACCC regarding fuel shopper dockets. In 2012 the ACCC had begun investigating fuel savings offers made by the MSCs to determine whether they substantially lessened competition for the retail sale of fuel. As previously mentioned, in December 2013 the ACCC accepted voluntary court undertakings from Coles and Woolworths that they would stop offering fuel discounts that were wholly or partially funded outside their fuel retailing business. Both MSCs agreed that from 1 January 2014 they would limit discounts offered in concert with supermarket purchases to four cents per litre.<sup>300</sup> However Woolworths continued to offer its 4+4 discount until 9 April and in February 2014 Coles began offering bundled fuel savings of 14 (10+4) cents per litre. In April 2014 the Federal Court found that Woolworth’s 4 + 4 cent offer to 9 March 2014 had breached their voluntary undertaking, as the discount depended on a supermarket purchase. However the Court dismissed the ACCC’s proceedings against Coles, determining that only 4 cents of the total bundled discount of 14 cents per litre was contingent on a qualifying supermarket purchase.<sup>301</sup>

In May 2014 its two year investigation came to a head with proceedings launched in the Federal Court against Coles, alleging it had engaged in unconscionable conduct regarding its Active Retail Collaboration (ARC) program. The ACCC alleged that in 2011 Coles had developed a strategy to improve its earnings by gaining better trading terms from suppliers, including through the introduction of ongoing rebates to be paid by suppliers for the ARC program. It alleged that Coles had engaged in unconscionable conduct towards 200 of its smaller suppliers, in breach of the ACL by, among other things: misleading suppliers about the savings from and value of the changes Coles had made; using undue influence and unfair tactics against suppliers to make them pay the rebate; taking advantage of their superior bargaining position by seeking payments without a legitimate basis for seeking them;

<sup>297</sup> Transcript of interview, CEO of major packaged goods supplier to the MSCs, p. 27.

<sup>298</sup> Transcript of interview, MSC representative, p. 24.

<sup>299</sup> ACCC *Annual Report* 2013-14, p. 30.

<sup>300</sup> ACCC *Annual Report* 2013-14, p. 34.

<sup>301</sup> ACCC Media Release, ‘Court finds Woolworths breached fuel shopper docket undertaking but later offers by Coles and Woolworths did not’, 14 April 2014.

and requiring suppliers to agree to the ongoing ARC rebate without giving them sufficient time to assess the value, if any, of the purported benefits of the ARC program to their business.<sup>302</sup>

In October 2014 the ACCC instituted further proceedings against Coles arising out of the same investigation, alleging that in 2011 Coles, outside of its trading terms with the suppliers concerned, pursued agreements from suppliers to pay Coles for 'profit gaps' on a supplier's goods, and imposed fines or penalties on suppliers for short or late deliveries.<sup>303</sup> In the face of continued adverse publicity it did not take long for Coles to settle. As senior counsel for the ACCC is quoted to have said when urging Federal Court (now High Court) Judge, Michelle Gordon, to accept the high penalties proposed by the Commission:

*This is not only a test case but a headline test case. It is one of the largest companies involved in trade and commerce in the country dealing with some of the smallest suppliers.*<sup>304</sup>

In December 2014 Coles was ordered to pay pecuniary penalties of \$10 million and the ACCC's costs. The retailer subsequently engaged the former Victorian Premier, Jeff Kennett AC, as an independent arbiter to administer a compensation scheme, a scheme that led to a refund of over \$12 million to suppliers.<sup>305</sup> In addition to taking the court-ordered penalties and compensation on the chin, Coles moved quickly in an attempt to mitigate reputational damage, with CEO John Durkan offering a full and unconditional public apology:

*I believe that in these dealings with suppliers, Coles crossed the line and regrettably treated these suppliers in a manner inconsistent with acceptable business practice. These suppliers were not treated with the transparency and respect they should be able to expect, Coles sincerely regrets and apologises for its conduct in these dealings.*<sup>306</sup>

It is beyond doubt that the action against Coles focussed the corporate mind of the organisation. As one Coles' representative put it, the unconscionability action 'had a significant impact. From the Wesfarmers board right down, I mean, that is a terrible thing for the ACCC to be calling out against the company.'<sup>307</sup> It also brought about behavioural change, at least in the short term.<sup>308</sup> As one interviewee told us, 'in all fairness Coles have gone out of their way considerably since the findings of the case to have better relationship with suppliers.'<sup>309</sup> He went on to stress that, from a supplier point of view, 'the money wasn't the driver ... at the time I think it served its purpose in terms of building a better relationship with Coles.'<sup>310</sup>

<sup>302</sup> ACCC Annual Report 2014-15, p. 68.

<sup>303</sup> ACCC Annual Report 2014-15, p. 68.

<sup>304</sup> Sue Mitchell and Madeleine Heffernan, 'Coles to settle unconscionable conduct cases with ACCC', *AFR*, 15 December, 2014.

<sup>305</sup> ACCC Annual Report 2014-15, p. 68.

<sup>306</sup> Sue Mitchell and Madeleine Heffernan, 'Coles to refund suppliers as it settles cases with ACCC', *SMH*, 15 December 2014.

<sup>307</sup> Transcript of interview, MSC representative, p. 22.

<sup>308</sup> Transcript of interview, CEO of major packaged goods supplier to the MSCs, p. 20.

<sup>309</sup> Transcript of interview, CEO of major packaged goods supplier to the MSCs, p. 33.

<sup>310</sup> Transcript of interview, CEO of major packaged goods supplier to the MSCs, p. 38.

Coles certainly does appear to have made some substantive changes in its approach to supplier relations in recent years. In response to the unconscionable conduct investigation, in an effort to curb the temptation on the part of some buyers to drive a hard bargain regardless of cost, the company changed its buyer remuneration strategy.<sup>311</sup> Then in April 2015, Coles established the Coles Nurture Fund, allocating \$50 million over five years for 'no strings attached'<sup>312</sup> grants and interest-free loans aimed at developing new products, technologies, systems and processes.<sup>313</sup> Any farmer in a food business with less than 50 employees that generates less than \$25 million in annual business revenue can apply for a grant under the scheme, and does not have to be currently supplying Coles. CEO John Durkan is reported to have denied suggestions that this was a 'public relations stunt':

*We know small entrepreneurs, be they farmers or food processors, are a great launch pad for innovation and clever ideas. With modest financial support, we can help get those ideas out to consumers.*<sup>314</sup>

In September that same year Coles held its inaugural Supplier Awards Gala Dinner, publicly and lavishly celebrating its suppliers.<sup>315</sup> In its 2015 Annual Report the company stated that:

*We have fundamentally changed the way we source food for our customers by fostering longer-term and deeper relationships with our suppliers.*<sup>316</sup>

A year later Woolworths would face similar allegations to those by which Coles had been burnt. In December 2015 the ACCC instituted proceedings in the Federal Court alleging Woolworths had engaged in unconscionable conduct through the development and implementation of the 'Mind the Gap' scheme (a name strangely redolent of the London subway and hence possibly the inspiration of UK imports amongst Woolworths' staff), which was designed to obtain payments from a group of 'Tier B' suppliers in order to urgently reduce a significant half year gross profit shortfall. The ACCC further alleged that, 'these requests were made in circumstances where Woolworths was in a substantially stronger bargaining position than the suppliers, did not have a pre-existing contractual entitlement to seek the payments, and either knew it did not have or was indifferent to whether it had a legitimate basis for requesting a Mind the Gap payment from every targeted Tier B supplier.'<sup>317</sup>

However in this one, the ACCC chalked up a loss. The Court held that the Mind the Gap requests were not unconscionable within the meaning of the ACL.<sup>318</sup> The retailer's scheme was held to be within the law because, in effect, it involved conduct that was not qualitatively different to conduct that occurs in the normal course of Woolworths' and indeed any supermarket's dealings with its suppliers. Yates J accepted Woolworths' primary contention that:

<sup>311</sup> Transcript of interview, MSC representative, p. 23.

<sup>312</sup> Sue Neales, 'Coles unveils \$50m fund to help farms expand', *The Australian*, 24 April 2015.

<sup>313</sup> Coles Supplier Portal, Coles Nurture Fund, <https://www.supplierportal.coles.com.au/csp/wps/portal/web/ColesNurtureFund>

<sup>314</sup> Sue Neales, 'Coles unveils \$50m fund to help farms expand', *The Australian*, 24 April 2015.

<sup>315</sup> 'Coles honours top suppliers', *Retail World*, 18 September 2015.

<sup>316</sup> Coles, *Annual Report 2015*, p. 6.

<sup>317</sup> ACCC media release, 'ACCC takes action against Woolworths for alleged unconscionable conduct towards supermarket suppliers', 10 December 2015.

<sup>318</sup> *Australian Competition and Consumer Commission v Woolworths Limited* [2016] FCA 1472 at 1.

*...from the perspective of any individual supplier who was contacted as part of the Mind the Gap scheme', the experience would have been no different to any ordinary negotiation that the supplier might have had with Woolworths.<sup>319</sup>*

Not surprisingly, the outcome provoked some strong reactions. From a defiant ACCC Chairman, despite the finding of legality: a description of the conduct as an 'unfortunate' way to do business and 'not the sort of business behaviour I am used to, having spent 20 years in the private sector'.<sup>320</sup> And, in the media release announcing the judgment, a promise 'to continue to take enforcement action where appropriate, particularly in relation to supply chain issues'.<sup>321</sup> Notwithstanding the loss, the ACCC's reaction suggests it is possible that a supplier representative was correct in his suspicion, voiced prior to the decision being handed down, that, as with Coles, 'the ACCC are trying to bang the drum as loudly as they can to force Woolworths into behaviour change'.<sup>322</sup>

From the then head of the AFGC there was a strongly worded observation that 'it would be pretty appalling if it [the judgment] were seen as a green light to do the same thing again' and an associated warning that it too would be continuing to keep 'a close eye' on supplier relationships.<sup>323</sup> In a follow up interview for this research, on eve of his departure from the supplier association, Dawson reflected further on the decision, observing:

*We think it sent a terrible signal and that's our view. We're particularly concerned at the element in the judgement that questioned whether Woolworths has any market power. ... I think there's widespread concern at the judgement and the signal that it potentially sent. So the concern was if the lesson that is drawn from this by both Coles and Woolworths is, hey, its open slather again, then obviously it's hugely concerning. So that was the initial reaction...<sup>324</sup>*

Despite its victory in court, and having successfully defended the action on the grounds that the Mind the Gap scheme was an acceptable norm in dealings with suppliers (at least for Woolworths if not the industry), at the Woolworths Annual General Meeting in November 2016 the Chairman Gordon Cairns stood behind the decision to test challenge the ACCC's allegations. But he also announced that Woolworths would 'hold ourselves going forward to higher standards'.<sup>325</sup> The irony of this was not lost on Dawson:

*Now, of course, interestingly, Woolworths then and still today were at pains to say, "But we hold ourselves to a high standard." Well ... from a supplier's point of view you're left ... with the question of what is "the Woolworth's way"? "Is it the one they stand up in court under*

<sup>319</sup> *Australian Competition and Consumer Commission v Woolworths Limited* [2016] FCA 1472 at 199.

<sup>320</sup> Eli Greenblat and John Durie, 'Woolworths beats ACCC supplier mistreatment case', *ABR*, 8 December 2016.

<sup>321</sup> ACCC media release, 'ACCC won't appeal Woolworths unconscionable conduct decision', 10 December 2015.

<sup>322</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 64.

<sup>323</sup> Madeleine Heffernan, 'Suppliers on edge after Woolworths wins cash-demand case', *SMH*, 12 December 2016.

<sup>324</sup> Transcript of interview, Gary Dawson 2, pp. 18-19.

<sup>325</sup> Sue Mitchell, 'ACCC Woolworths' unconscionable conduct case dismissed', *AFR*, 8 December 2016.

*oath and say or is it the one they say in supplier [discussions]? Well, you can work that out. That's still the concern I think ...*<sup>326</sup>

There are also possible broader, potentially legislative implications of the case. According to one media outlet, 'victory may prove pyrrhic if the case leads to renewed calls for tougher competition laws.'<sup>327</sup> The CEO of COSBOA expressed strong views too on any suggestion that the ACCC proceedings against the MSCs in these cases should be taken as evidence that 'the system works'. Reflecting specifically on the Coles' admission, he observed:

*... that's like saying that if a truck hits a bus, 20 kids are killed, as long as that truck driver goes to jail the system works.. We're all happy?*<sup>328</sup>

Senator Xenophon, a long time advocate of drastic measures to break up the grocery retail 'duopoly', suggested that the outcome in the case against Woolworths strengthens the case for the amendment of the misuse of market power prohibition to create an anti-competitive effects test.<sup>329</sup> As noted below, that amendment has now been approved by the government, albeit the approval preceded the Federal Court judgment, and on 28 March 2017 the amending Bill passed the House of Representatives. As of 29 March the Bill had been introduced into the Senate and a second reading moved.<sup>330</sup>

The judgment may also pave the way for consideration of whether the unconscionability provisions require further elucidation refinement, or even extension. The test for unconscionability is based on the norms of society, not the norms of the business in question or even the industry at large. It would make a mockery of the law if an accepted defence to a charge of unconscionability was, in effect: 'but this is how things have always been done.' Moreover, norms are fluid and change over time. Even if conduct has been seen as socially acceptable in the past, that is not to say it will always remain so. An Interim report by Consumer Affairs Australia and New Zealand (CAANZ) in its review of the ACL (CAANZ-ACL Review) released in October 2016, just prior to the Woolworths judgement, did not support the calls by some commentators for lowering the standard and introducing a general prohibition on unfair trading into the law. It instead favoured allowing the case law on unconscionability to develop.<sup>331</sup> Perhaps the outcome in the Woolworths case will prompt a rethink of this assessment.

Moreover, the former AFGC CEO has reflected that Woolworths' decision to defend the case, the basis for its defence and the courts' acceptance of that defence, only serve to open the door for considering whether the FGCC needs to be toughened up, in the context of the 2018 review. After all,

<sup>326</sup> Transcript of interview, Gary Dawson 2, pp. 18-19.

<sup>327</sup> Sue Mitchell, 'ACCC Woolworths' unconscionable conduct case dismissed', *AFR*, 8 December 2016.

<sup>328</sup> Transcript of interview, CEO of COSBOA, 14.

<sup>329</sup> Caron Beaton-Wells, 'Supermarket unconscionability – the difference two years can make', <http://law.unimelb.edu.au/news/cen/supermarket-unconscionability-the-difference-two-years-can-make>.

<sup>330</sup> *Competition and Consumer Amendment (Misuse of Market Power) Bill 2017* (Cth).

<sup>331</sup> Consumer Affairs Australia New Zealand, *Australian Consumer Law Review Interim Report*, October 2016 (CAANZ-ACL review interim report 2016), [2.3] at pp. 105-106

the conduct that was the subject of the case – in essence, retrospective claims under threat of retribution – is the very type of conduct that the Code is intended to eradicate.

The decision may also have ramifications for the strengthening of deterrence and Rod Sims' support for this is evident in the ACCC's submission to the CAANZ-ACL review that:

*...the current maximum penalties available under the ACL are too low and need to be increased if they are to act as an effective deterrent. Court ordered penalties are an important part of our enforcement toolkit and, like all enforcement tools, need to be set at an appropriate level if they are to form part of a proportionate response to consumer harm.*<sup>332</sup>

Sims and other ACCC representatives subsequently took to the media, reinforcing the call for higher penalties in the media with a particular emphasis on stronger deterrence for 'the big end of town'.<sup>333</sup> It was a call that received wide support including from Choice<sup>334</sup> and the ALP,<sup>335</sup> amongst others, while opposed not unexpectedly by big business groups, including the National Retail Association.<sup>336</sup> In a separate review of Consumer Law Enforcement and Administration conducted by the PC at about the same time as the CAANZ-ACL Review, and concluded in April 2017, the PC agreed with the CAANZ-ACL Review's view on this, supporting an increase in the maximum financial penalties for breaches of the ACL.<sup>337</sup> It made particular note of the submissions in support of higher penalties that would see the maxima recalibrated to match the maximum penalties for breaches of the competition rules under the CCA.<sup>338</sup> In the recently handed down Budget, the government announced that it would support this change.<sup>339</sup>

Having decided not to appeal the decision in the Woolworths' unconscionability case, it is unclear to what extent the ACCC is likely to continue to seek out or take opportunities to test further this particular aspect of the law.<sup>340</sup> Moreover, as both its 2016 and 2017 Compliance and Enforcement policies suggest,<sup>341</sup> as far as supplier relationships in the grocery sector are concerned, its focus now is very much on monitoring compliance with the FGCC and this is likely to be accentuated by the approach of the 2018 review (see further Part 7 below).

<sup>332</sup> ACCC submission to Productivity Commission Inquiry into Consumer Law Enforcement and Administration, p. 9.

<sup>333</sup> Patrick Durkin, 'Rod Sims says ACCC 'too cautious' on penalties in the past', *AFR*, 5 February 2017.

<sup>334</sup> Choice Submission to CAANZ-ACL Issues Paper, pp. 40-42.

<sup>335</sup> Andrew Leigh, 'Australian Labor Party submission to the Productivity Commission Inquiry into the enforcement and administration of Australian Consumer Law', p. 1.

<sup>336</sup> National Retail Association submission to Productivity Commission's Inquiry into Consumer Law Enforcement and Administration, p. 5.

<sup>337</sup> PC, *Consumer Law Enforcement and Administration*, March 2017 (PC, *Consumer Law*, Final Report 2017), Finding 4.5 at p. 19.

<sup>338</sup> This would mean that companies incur the greater of: a maximum penalty of \$10 million, three times the value of the benefit the company received from the breach or 10 per cent of annual turnover in the preceding 12 months if the benefit cannot be determined.

<sup>339</sup> Budget Measures: Budget Paper No. 2. 2017-18, Part 1: Revenue measures, 9 May 2017, The Commonwealth of Australia, p. 35.

<sup>340</sup> Cf comments made by the ACCC Deputy Chair (Small Business) at the AFGC Conference in 2017 to the effect that the decision not to appeal was based entirely on advice regarding the approach that the judge in the case had taken to the evidence, implying there was no dampening of the ACCC's appetite for litigation in this area. See Michael Schaper, 'Current Food & Grocery Issues: An ACCC Perspective', Presentation at AFGC Conference, 24 May 2017.

<sup>341</sup> ACCC *Compliance and Enforcement Policy* 2016, p. 3; ACCC, *Compliance and Enforcement Policy* 2017, p. 4.

## (d) Harper gives grocery a free pass but goes not so easy on the ACCC

The Harper Review included a focus on the grocery sector and the MSCs particularly. This was hardly surprising given the calls for review of competition laws in relation to various aspects of the workings of the sector in the parliamentary inquiries in 2010 and 2011, as well the heightened controversy surrounding the MSCs generally during that period. However, in many respects, the findings of the review on this subject echoed those of the ACCC in 2008. The review panel acknowledged the receipt of a number of submissions tabling concerns about the MSCs, including a statement from the MGA that:

*... the market dominance of two major retailers is seriously affecting the ability of smaller independent retailers to compete effectively in Australia.*<sup>342</sup>

However the panel also noted that other stakeholders, including Coles and Woolworths, had submitted that ‘that the grocery industry is highly competitive and has become more so in recent years’.<sup>343</sup> The findings of the review supported this position (as does the analysis in Part 2 of this report). It was confirmed that competition had intensified as a consequence of Wesfarmers’ acquisition of Coles and the growing presence of Aldi and Costco in the market in the years leading up to the review, and reported that, as a consequence, ‘few concerns have been raised about prices charged to consumers by supermarkets’.<sup>344</sup>

While issues of horizontal competition were not considered significant, the panel did acknowledge strains in the supply chain. In response to concerns raised by suppliers about unconscionable conduct and misuse of market power by the MSCs (possibly evidencing less reluctance by suppliers to speak up than at the time of the ACCC Grocery Inquiry), the panel repeated the mantra that, ‘the CCA prohibits conduct that harms the competitive process, not individual competitors.’<sup>345</sup>

With regard to unconscionable conduct, the review panel largely took a watch-and-see approach. The panel did call for continued ‘active and ongoing review’ of the relevant provisions; however, it also cited the settlement by Coles of the action that the ACCC had brought against it, and its admission of unconscionable conduct, as evidence that the current provisions were, ‘working as intended to meet their policy goals’.<sup>346</sup> One can only speculate as to whether the same conclusion might have been reached had the panel been considering the matter after the Woolworths’ decision was handed down. Further, the panel determined that the recently announced FGCC should also assist suppliers to contract ‘fairly and efficiently’ with the MSCs’.<sup>347</sup>

<sup>342</sup> MGA submission, p. 6, cited in Harper Review 2015, p. 433

<sup>343</sup> Harper Review 2015, p. 433.

<sup>344</sup> Harper Review 2015, p. 433.

<sup>345</sup> Harper Review 2015, p. 88.

<sup>346</sup> Harper Review 2015, p. 88.

<sup>347</sup> Billson, B (Minister for Small Business) 2015, Grocery Code to improve relationships between retailers, wholesalers and suppliers, media release 2 March, Canberra, cited in Harper Review 2015, p. 88.

When it came to misuse of market power however the panel made the controversial call for a strengthening of s 46 of the CCA, recommending the provision be reframed so as to:

*..prohibit a corporation that has a substantial degree of power in a market from engaging in conduct if the proposed conduct has the purpose, or would have or be likely to have the effect, of substantially lessening competition in that or any other market.*<sup>348</sup>

As discussed below, this amendment so as to create an ‘effects test’ for the misuse of market power was one of the most contentious recommendations of the Harper Review, and resulted in a passionate and highly public debate between its supporters, including the then Small Business Minister Bruce Billson, ACCC Chairman Rod Sims and former Chairman Allan Fels AO; and its very vocal detractors, which included the BCA,<sup>349</sup> Wesfarmers boss Richard Goyder,<sup>350</sup> former ACCC commissioner Stephen King and former ACCC Chairman Graeme Samuel AC.<sup>351</sup>

The review’s terms of reference included the institutional framework for competition policy-making and legal enforcement and hence, yet again, the ACCC found itself the subject of scrutiny. While the panel was largely supportive of the agency, the changes that were recommended aligned closely with concerns raised in earlier inquiries (referred to in Part 3 above). With regard to transparency, the government supported the recommendation that the ACCC should ‘establish, publish and report against a Code of Conduct for its dealings with the media with the aim of strengthening the perception of its impartiality in enforcing the law.’<sup>352</sup> Further, the government said it would continue ‘to liaise with the ACCC with a view to enhancing public disclosure of operational procedures and decision-making processes where it is appropriate and feasible to do so.’<sup>353</sup> It appears this has had some substantive impact, and a positive one in the view of at least one commentator:

*I would say that two years later, the relationship [between the ACCC and MSCs] is now much better. I think the ACCC – the ACCC got criticised by Harper on the way it uses the media, and I think it’s become a little better on that. I think the ACCC has got to understand the grocery sector better.*<sup>354</sup>

When it came to the governance of the agency, the Government supported the panel’s recommendation that the ACCC report regularly to a ‘broad based committee of the Parliament, such as the House of Representatives Standing Committee on Economics.’<sup>355</sup> The government also accepted the recommendation that a specialist small business commissioner be retained, as well as

<sup>348</sup> Harper Review 2015, recommendation 30, p. 348.

<sup>349</sup> Eloise Keating, ‘Allan Fels slams big business lobbying over effects test and government’s “disastrous incapacity” to deliver reform’, *Smart Company*, 4 September 2015.

<sup>350</sup> Eli Greenblat and Annabel Hepworth, ‘Goyder blasts PM’s effects test’, *ABR*, 17 March 2016.

<sup>351</sup> Graeme Samuel and Stephen King, ‘Competition law: Effects test would have shackled competition’, *AFR*, 9 September 2015.

<sup>352</sup> Government response to the Harper Review 2015, recommendation 52: Media Code of Conduct, pp. 39-40.

<sup>353</sup> Government response to the Harper Review 2015, recommendation 53: Small business access to remedies, p. 40.

<sup>354</sup> Transcript of interview, former senior representative of the UK OFT, p. 10.

<sup>355</sup> Government response to the Harper Review 2015, recommendation 51: ACCC Governance, p. 39.

committing to the creation of a specialist agriculture commissioner, as announced in the Agricultural Competitiveness White Paper.<sup>356</sup>

In February 2016 Mick Keogh was appointed to this role. Keogh is a leading agricultural analyst, with a strong background in this area, having grown up on a farm and obtained degrees in Wool and Pastoral Sciences from the University of New South Wales before working as an agricultural management consultant across the private and public sectors. He has also served as the General Manager Policy for the NSW Farmers' Association and the Executive Director of the Australian Farm Institute, as well as Chairman of the National Rural Advisory Council, and a Member of the CSIRO Sustainable Agriculture Flagship Advisory Committee.<sup>357</sup> Keogh's appointment was well received by the rural sector. The National Farmers' Federation (NFF), while complaining that the position was well overdue, welcomed his appointment;<sup>358</sup> and NSW Farmers Association President Derek Schoen was quoted as saying:

*He brings a depth of understanding about the complexity and sensitivity of our agricultural supply chains and he will be a valuable source of practical knowledge for the competition regulator,*

*For the first time ever, farmers will have a voice at the decision making table when the commission makes important decisions about both competition and consumer protection issues.*<sup>359</sup>

Further support for the small business sector was evident in the government's 'in principle' acceptance of the recommendation that the ACCC improve its communication with small business, and complainants more generally, noting that the Government had requested that the ACCC 'improve transparency and clarity for small businesses on why it is unable to pursue certain complaints'.<sup>360</sup>

Yet again the need for the ACCC to take further steps to facilitate greater awareness on the part of small business about collective bargaining, the exemption process and how this might be used to improve their bargaining position featured in the recommendations.<sup>361</sup>

## **II. A small business man: the Small Business Minister**

During this time the smaller players in the sector – farmers, manufacturers, distributors and independent retailers – had an energetic and vocal champion in government. In 1996 Bruce Billson, a working class boy from Frankston who had himself worked in several small businesses before running his own, was elected to represent the outer Melbourne constituency of Dunkley. After holding a

<sup>356</sup> Government response to the Harper Review 2015, recommendation 51: ACCC Governance, p. 39.

<sup>357</sup> Australian Farm Institute, Key Staff, Mick Keogh, Executive Director, <http://www.farminstitute.org.au/about-us/institute-structure/key-staff.html>

<sup>358</sup> Anna Vidot, 'Mick Keogh appointed as competition watchdog's first ever agricultural commissioner', *ABC Rural*, 24 February 2016.

<sup>359</sup> 'New ACCC agriculture commissioner appointed', *The Rural*, 24 February 2016.

<sup>360</sup> Government response to the Harper Review 2015, recommendation 53: Small business access to remedies, p. 40.

<sup>361</sup> Government response to the Harper Review 2015, recommendation 54: Collective bargaining, p. 41.

variety of portfolios for the Liberal party Billson became the Shadow Minister for Small Business in 2009, and in 2013 was sworn in as the Minister for Small Business in the Abbott-led Coalition government.<sup>362</sup> As Billson himself reportedly said, he spent this time ‘...fearlessly advocating the case for the small business, family enterprise, start-up and self-employed community.’<sup>363</sup> To quote journalist Matthew Knott, ‘Bruce Billson talks about small business the way other people talk about God or football or their favourite band.’<sup>364</sup>

Billson was Australia’s 15th Minister for Small Business. But he was one of the first to hold the portfolio within the cabinet. In 2012, the then Labor Prime Minister Julia Gillard, possibly in response to the increasing political pressure from the sector, determined it necessary to elevate the small business portfolio from the outer ministry. However, the turbulent years of the Gillard government meant there was a succession of Ministers in the role.<sup>365</sup>

While all previous Small Business Ministers held shared portfolios Billson was the first, as Shadow Minister, to combine the Small Business, Competition Policy and Consumer Affairs portfolios. For some, the combination of small business and competition policy in the one portfolio was incongruous and potentially problematic:

*The change cements some of the fears over a small business focus for competition policy that have arisen in recent months ... [it] suggests a move away from the protection of the competitive process to the protection of the competitors.*<sup>366</sup>

### (a) Competition reform for small business – roots, branches and all

A ‘root and branch’ review of Australia’s competition laws, as the Harper Review was known initially, had been a key campaign promise of the Coalition party in the lead up to 2013 Federal election, an election where the small business vote had been viewed as ‘critical’.<sup>367</sup> In an open letter to small business published in the Sydney Morning Herald in April 2013, Billson bemoaned the declining number of people working in the small business sector, attributing this in no small part to the ‘22,000 new regulations’ that Labor had introduced, and the recent churn of small business ministers.<sup>368</sup> Billson stated in the letter that he, Prime Minister Abbott and Treasurer Hockey had been listening to small business and announced that the Coalition have, ‘developed a plan that will double the rate of small business formations and create one million new jobs within five years.’ The plan included a commitment to instigate ‘a root and branch review of competition laws and policy and deliver more competitive markets.’<sup>369</sup>

<sup>362</sup> The Hon. Bruce Billson, <http://www.brucebillson.com.au/about-bruce-billson/>.

<sup>363</sup> Tim Mazzarol, ‘Farewell Bruce Billson your passion for small business will be sorely missed’, *The Conversation*, 29 November 2015.

<sup>364</sup> Matthew Knott, ‘Meet Bruce Billson, the evangelical minister for small business’, *SMH*, 26 May 2015.

<sup>365</sup> Mark Arbib (December 2011 to March 2012), Brendan O’Connor (March 2012 to February 2013), Chris Bowen (February to March 2013), and Gary Gray (March to September 2013).

<sup>366</sup> Julie Clarke, ‘No competition minister in new cabinet’, 16 September 2013, *Competition Law, Australian competition law and policy discussion*, <https://competitionlaw.wordpress.com/2013/09/16/no-competition-minister/>

<sup>367</sup> The Hon Bruce Billson MP, ‘Revealed: Coalitions small business policy’, *SMH*, 9 April 2013.

<sup>368</sup> The Hon Bruce Billson MP, ‘Revealed: Coalitions small business policy’, *SMH*, 9 April 2013.

<sup>369</sup> The Hon Bruce Billson MP, ‘Revealed: Coalitions small business policy’. *The SMH*, 9 April 2013.

This commitment echoed the recommendations of the Senate inquiry into the impacts of supermarket price decisions on the dairy industry in 2011, that had called on the Government to initiate an independent review of the competition provisions of the CCA, stating:

*It is clear that Coles and Woolworths have a very strong position in Australia's grocery market. While the recent signs of Coles and Woolworths more fervently seeking to attract consumers to their respective stores are encouraging for competition, the effects need to be closely monitored. Other possible developments, such as implications for the major supermarkets' dealings with their suppliers due to the growth in private label products generally, need to be monitored for any signs of anticompetitive conduct. The committee expects the Government and the ACCC to keep a watching brief on these issues and the grocery sector in general.<sup>370</sup>*

This was a recommendation that had been mirrored less than a year later, in the report of the Senate Committee on Australia's food processing sector:

*The committee recommends that the government initiate an independent review of the competition provisions of the Competition and Consumer Act 2010. The committee recommends that the review should include consideration of: the misuse of market power; creeping acquisitions; predatory pricing; and unconscionable conduct.<sup>371</sup>*

The Coalition made good on its pledge. The terms of reference for a Competition Policy Review were released in December 2013, just three months after it had won the Federal election. While some, particularly within Coles and Woolworths, may have viewed the review as a pointed attack, the terms of reference were seen as 'extraordinarily wide'.<sup>372</sup> However, as the Prime Minister said, this was to be the first review of competition laws and policies in over 20 years and it would, 'examine not only the current laws but the broader competition framework, to increase productivity and efficiency in the markets, drive benefits to ease cost of living pressures and raise living standards for all Australians'.<sup>373</sup>

Both the focus of the review and composition of the review panel reflected Billson's sympathy for small business. The review panel included individuals with previous experience and profile in relation to small business, as well as regional issues, and was instructed to focus on identifying, 'regulations and other impediments' that restricted competition and reduced productivity without serving any broader public interest; and to examine the competition provisions and special protections for small business in the CCA 'to ensure that efficient businesses, both big and small,' could 'compete effectively and have the necessary incentives to invest and innovate for the future'. The panel was also expected to ensure that the competition provisions in the CCA were driving 'efficient, competitive and durable outcomes, particularly in light of changes to the Australian economy' both locally and

<sup>370</sup> SERC, *Impacts of supermarket pricing on the dairy industry*, 2011, recommendation 5 p. xvi.

<sup>371</sup> SSC, *Australia's Food Processing Sector*, 2012, recommendation 4, p. vi.

<sup>372</sup> John Durie, 'Billson packs licence to kill of any impediments to small business', *AFR*, 9 January 2014.

<sup>373</sup> Media release, Tony Abbott, PM, 'Review of Competition Policy' Wednesday 4 December 2013.

globally; to consider the existing ‘structure and powers of the competition institutions’ to ensure they were still appropriate, ‘given changes to the economy and the desire to reduce the regulatory impost on business’; and ‘to review government involvement in markets’ with a view to reducing this involvement where it was no longer in the public interest.<sup>374</sup>

It was clear nevertheless that the grocery sector was of particular interest. The panel was to consider ‘whether the misuse of market power provisions effectively prohibit anti-competitive conduct’<sup>375</sup> and, more pointedly in the present context, to:

*...examine whether key markets – including, but not limited to, groceries, utilities and automotive fuel – are competitive and whether changes to the scope of the CCA and related laws are necessary to enhance consumer, producer, supplier and retailer opportunities in those markets and their broader value chains.*<sup>376</sup>

### (b) Small business budget measures

Billson’s influence and passion for his portfolio, and its increasing political significance, were further evident in the 2014 federal budget. Indeed, the few policy initiatives that the federal opposition did not seek to obstruct included: cuts to the corporate tax rate for small businesses, and significant investment in an Industry Skills Fund to provide training support for SMEs together with an Entrepreneurs Infrastructure Program to help boost innovation and commercialisation in the sector. Funding was made available to improve access by SMEs to government contracts and for the ACCC to investigate a possible extension of the unfair contract provisions to small businesses. The budget also provided for the creation of a SBFE Ombudsman’s office so as to provide a single entry point for SMEs seeking access to government assistance and dispute resolution.<sup>377</sup>

The 2015 budget in turn was declared a ‘small business budget’.<sup>378</sup> All small businesses were to get an immediate tax deduction for any individual assets purchased for less than \$20,000 (the previous threshold having been \$1,000); the company tax rate for incorporated businesses with an annual turnover of less than \$2 million was to reduce to 28.5%; and fringe benefits tax exemptions were expanded to include work-related portable electronic devices, a move aimed at reducing red tape for small business while helping ‘small business employees stay connected in the digital economy’.<sup>379</sup>

Later that same year, on 24 November 2015, Billson announced that he would leave politics after the next election, a decision that came in the wake of Malcolm Turnbull replacing Tony Abbott as Prime Minister after a leadership spill in September 2015. In the subsequent cabinet reshuffle Turnbull demoted Billson in favour of Kelly O’Dwyer, who became both Minister for Small Business and

<sup>374</sup> Harper Review 2015 terms of reference, overview.

<sup>375</sup> Harper Review 2015 terms of reference, 3.3.2.

<sup>376</sup> Harper Review 2015 terms of reference, 4.2.

<sup>377</sup> Expense Measures: Budget Paper No. 2. 2014-15, Part 2: Expense measures, Treasury, 13 May 2014, The Commonwealth of Australia, p. 217.

<sup>378</sup> Tim Mazzarol, ‘Farewell Bruce Billson your passion for small business will be sorely missed’, *The Conversation*, 29 November 2015.

<sup>379</sup> Budget 2015, Jobs and Small Business: the right time to invest, Australian Government <http://www.budget.gov.au/2015-16/content/highlights/jobsandsmallbusiness.html>

Assistant Treasurer.<sup>380</sup> In announcing his decision to retire from parliament Billson reportedly said, 'it has become clear to us that while I love what I do, it is not possible for me to fully do what I love'.<sup>381</sup>

### (c) Effecting an effects test

A key area of unfinished business for Billson was the introduction of an effects test for s 46 of the CCA, as recommended by the Harper Review released in March 2015. Billson firmly believed that while nothing could guarantee success when it came to small business operators, 'success or otherwise will be determined on merit, not on muscle'.<sup>382</sup> This meant getting the incentives right, minimising regulatory burdens, and giving businesses, regardless of size, the chance to prosper (which, in turn, meant ensuring big business did not misuse its market power).<sup>383</sup>

Billson had been one of the few government ministers willing to defend (publicly at least) the introduction of such a reform.<sup>384</sup> In an opinion piece penned in August 2015 he argued that the proposed change, 'strikes the right balance and has the potential to better foster innovation and efficiency, improve productivity and ultimately deliver economic, employment and consumer benefits'.<sup>385</sup> Large corporates represented by the BCA vehemently opposed the mooted amendment.<sup>386</sup> BCA President Catherine Livingstone warned in a public statement released in August 2015 that:

*Changing the 'misuse of market power' provision by introducing an effects test and removing the 'take advantage' clause will create major regulatory uncertainty for business. It will expose our business to the risk of investigation and prosecution due to effects on competition that we cannot foresee. It will deter legitimate innovative pricing, product development or business expansion that would be good for consumers.*<sup>387</sup>

Livingston also foreshadowed that small business would not be immune:

*Small business needs to understand they will not be quarantined from the impact of this change which will apply equally to all business, for example, in regional towns or markets where a small business' product or service is dominant. In these circumstances, small businesses could be the instigator of actions against other small businesses, who would bear the unintended consequences of additional cost and uncertainty.*<sup>388</sup>

<sup>380</sup> Tim Mazzarol, 'Farewell Bruce Billson your passion for small business will be sorely missed', *The Conversation*, 29 November 2015.

<sup>381</sup> Tim Mazzarol, 'Farewell Bruce Billson your passion for small business will be sorely missed', *The Conversation*, 29 November 2015.

<sup>382</sup> Transcript of interview, Bruce Billson, p. 8.

<sup>383</sup> Transcript of interview, Bruce Billson, p. 9.

<sup>384</sup> Tim Mazzarol, 'Farewell Bruce Billson your passion for small business will be sorely missed', *The Conversation*, 29 November 2015.

<sup>385</sup> Bruce Billson, 'Harper review misuse of market power clause would energise enterprise', *AFR* 31 August 2015.

<sup>386</sup> Bruce Billson, 'Harper review misuse of market power clause would energise enterprise', *AFR* 31 August 2015.

<sup>387</sup> BCA Statement on the Introduction of an Effects Test, 3 August 2015 at <http://www.bca.com.au/media/statement-on-the-introduction-of-an-effects-test/view-all-related-publications>.

<sup>388</sup> BCA Statement on the Introduction of an Effects Test, 3 August 2015, at <http://www.bca.com.au/media/statement-on-the-introduction-of-an-effects-test/view-all-related-publications>

The BCA has considerable political influence in Australia, but also is said to have a track record of opposing the strengthening of competition regulation. It opposed the introduction of the TPA (now the CCA) in 1974, the strengthening of the merger law in 1993, the broadening of laws that capture unconscionable conduct, and initially at least, the criminalisation of cartel laws.<sup>389</sup> As Allan Fels AO has observed, the core approach of the BCA is to oppose stronger competition law to the extent that it affects large businesses. And while not all BCA members were concerned with changes to s 46 it is perhaps not surprising that the MSCs were highly opposed to, and had the support of the BCA in their opposition to the proposed amendment:<sup>390</sup>

*The people who don't want the effects test are half a dozen retailers from the top end of town, the big end of town have the money for a major advertising campaign.*<sup>391</sup>

In the opposite corner, one of the strongest advocates for the SME sector and the introduction of an effects test was the COSBOA. While nowhere near as well-resourced as advocates for big business,<sup>392</sup> CEO Peter Strong appears to have been effective in having the views of his members heard,<sup>393</sup> particularly by the media and by governments that increasingly have become very sensitive to the political implications of not being seen to listen to small business.<sup>394</sup> Strong, a small bookshop owner, appears to have captured the attention (if not the imagination) of many in the political sphere, with his emphasis on 'people' as opposed to economics in debates relating to small business, his avid use of the media, including social media ('COSBOA has been noisy'),<sup>395</sup> and his willingness to work with but also to challenge the arguments put by senior representatives across industry and government. The bluntness of his approach was borne out by an anecdote he shared with us regarding a conversation he had had with a senior retailer representative:

*I said, "You know [name], do you keep a record of the number of suicides in the supply chain?" which really threw him. "What do you mean?" he said. I said, "well, there's been suicides in the malls ... there's certainly suicides in the Coles or Woollies supply chain; we know that." They didn't know what to say to that.*<sup>396</sup>

Strong is an unconditional fan of Billson. As he told us, 'I just supported Bruce to the hilt. I gave him ten out of ten, you never give that to a pollie ... he was relentless.'<sup>397</sup> He is highly complementary too of Kate Carnell. Referring to Carnell and the establishment of the SBF E Ombudsman's office, he told

<sup>389</sup> Allan Fels AO, 'The Australian controversy over abuse of market power law, a study in political economy', Competition Policy at the Intersection of Equity and Efficiency Honouring the Scholarship of Eleanor M. Fox, Brussels, 8 June 2016, p. 5.

<sup>390</sup> Allan Fels AO, 'The Australian controversy over abuse of market power law, a study in political economy', Competition Policy at the Intersection of Equity and Efficiency Honouring the Scholarship of Eleanor M. Fox, Brussels, 8 June 2016, pp. 6.

<sup>391</sup> Catie Low, 'Big business 'called on' to pull down effects test', *SMH*, 17 September 2015.

<sup>392</sup> Allan Fels AO, 'The Australian controversy over abuse of market power law, a study in political economy', Competition Policy at the Intersection of Equity and Efficiency Honouring the Scholarship of Eleanor M. Fox, Brussels, 8 June 2016, p. 7.

<sup>393</sup> Patrick Durkin, 'The Wesfarmer's Affect: BCA accused of driving supermarket's agenda', *AFR*, 23 September, 2015.

<sup>394</sup> Michelle Grattan, 'Big win for small business in government embrace of competition 'effects test'', *The Conversation*, 16 March 2016.

<sup>395</sup> Transcript of interview, CEO of COSBOA, p. 26.

<sup>396</sup> Transcript of interview, CEO of COSBOA, p. 26.

<sup>397</sup> Transcript of interview, CEO of COSBOA, pp. 24-5.

us: 'she's fantastic. You know what, I'll say, we got that position in and I thought of resigning; we thought she was doing a great job but I can still say stuff she can't say...'.<sup>398</sup>

Section 46 reform had Carnell's support also. Still the head of the Australian Chamber and Commerce in 2015, Carnell is reported to have expressed surprise at the ferocity of the BCA's stance, stating that it was a 'moderate' reform and pointing out, in contradiction of claims by others, that, 'it doesn't stop a company with significant market power from pushing down prices with a particular supplier. It would only be if the effect of that activity impacted on the competitiveness of the whole market.'<sup>399</sup>

Six months later, as the newly appointed SBFE Ombudsman, Carnell commended the Minister for Small Business in a media release for supporting the 'effects test':

*Focussing on the effect of conduct, rather than just the purpose of conduct, will provide better protection for all small businesses and family enterprises. The Minister's decision to support the effects test sends a positive message to the small business sector that the Government supports them and understands the need for an appropriate balance in business relationships.*<sup>400</sup>

This was a view echoed by the MGA, with its CEO having been reported to have said that the effects test was important because it would give the ACCC the clout to 'crack down' on anti-competitive practices.<sup>401</sup>

As mentioned above, there was dissent amongst the current and former chairs of the ACCC when it came to the need for the reform. As former chairman Allan Fels AO acknowledged:

*Whilst generally supporting a strengthening of the competition law, its [the ACCC's] approach to abuse of dominance has varied from one Chair of the Commission to the next. It has never been neutral, nor, some would say, disinterested.*<sup>402</sup>

Fels, as Chairman, had in fact advocated for the addition of an effects test since as far back as the 1990s without success. Then, when Samuel took the helm, there had been opposition to any substantial reform of the abuse of dominance laws. Rod Sims, however, as a former government official and a strong advocate for change, seemed the right person to support a further push for such reform.<sup>403</sup> As mentioned above, the result was a very public and at times pointedly personal exchange between parties with opposing views.

At a political level the Labor Party traditionally has been a strong supporter of the strengthening of competition laws. However, it opposed the proposed reform. While an examination of the reasons for

<sup>398</sup> Transcript of interview, CEO of COSBOA, p. 20.

<sup>399</sup> Catie Low, 'Big business 'called on' to pull down effects test', *SMH*, 17 September 2015.

<sup>400</sup> The Australian Small Business and Family Enterprise Ombudsman applauds Minister's support for 'effects test', 16 March 2016.

<sup>401</sup> Catie Low, 'Big business 'called on' to pull down effects test', *SMH*, 17 September 2015.

<sup>402</sup> Allan Fels AO, 'The Australian controversy over abuse of market power law, a study in political economy', Competition Policy at the Intersection of Equity and Efficiency Honouring the Scholarship of Eleanor M. Fox, Brussels, 8 June 2016, p. 7.

<sup>403</sup> Allan Fels AO, 'The Australian controversy over abuse of market power law, a study in political economy', Competition Policy at the Intersection of Equity and Efficiency Honouring the Scholarship of Eleanor M. Fox, Brussels, 8 June 2016, p. 8.

this policy stance is beyond the scope of the current discussion, it has been said by some that it was due in part to the close ties between the Labor Party and the Shop Distributive and Allied Trades Association (SDATA), the union that covers retail employees and is in turn closely associated with the MSCs.<sup>404</sup>

The Coalition Government itself had to manage tensions within its own ranks, tensions that are a product of it being made up of a Liberal Party that is pro-business and traditionally cautious when it comes to strengthening competition law and/or regulation; and the National Party, which at that time had a considerable number of members in the Cabinet and was both pro-small business and pro-farmer. As is made clear above, a key player in all of this was Bruce Billson.<sup>405</sup>

Upon leaving his Ministerial role Billson is reported to have warned Prime Minister Turnbull that giving in to the big business lobby would, 'essentially see the government capitulate to powerful vested interests, and encourage business behaviour that would have the "effect of substantially lessening competition"'.<sup>406</sup>

On 24 November 2015, a day after Billson announced his retirement, the Government released its response to the Harper Review. Despite stating its intention to implement 'the majority of the Review's recommendations',<sup>407</sup> when it came to an effects test, it was not yet able to commit:

*The Government acknowledges concerns raised in submissions to the Harper Review about the operation of the misuse of market power provision (section 46 of the CCA) and the Harper Review's recommendation for reform. In light of the importance of this issue for business and consumers, the Government will consult further on options to reform the provision and release a discussion paper on this topic.*<sup>408</sup>

Ultimately, however, Billson's view prevailed. A further consultation completed, including consideration of 'part-Harper' options,<sup>409</sup> the Government came through the test of its mettle, supporting the 'full Harper' in amendment of s 46. A key reason for the success of the s 46 reform has been said to have been the strong support of the National Party. Turnbull had needed the support of the Nationals to wrest the Prime Ministership from Abbott. According to Fels, the Nationals are said to have made support of the effects test a condition of that support. Fels argues Turnbull may have agreed to this on the condition that there could be discussion at some later stage about the exact

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<sup>404</sup> Allan Fels AO, 'The Australian controversy over abuse of market power law, a study in political economy', Competition Policy at the Intersection of Equity and Efficiency Honouring the Scholarship of Eleanor M. Fox, Brussels, 8 June 2016, p. 8. The influence of the union in this debate was also emphasised by Peter Strong in our interview with him. When asked about Labor's platform and its opposition to the effects test and the reason for it, he responded: '... they've walked away from small business ... [In relation to the effects test], they've gone back to their root, which is the worker ... because the SDA are in bed with Coles and Woollies...' (Transcript of interview, CEO of COSBOA, p. 12).

<sup>405</sup> Allan Fels AO, 'The Australian controversy over abuse of market power law, a study in political economy', Competition Policy at the Intersection of Equity and Efficiency Honouring the Scholarship of Eleanor M. Fox, Brussels, 8 June 2016, p. 8.

<sup>406</sup> Tim Mazzarol, 'Farewell Bruce Billson your passion for small business will be sorely missed', *The Conversation*, 29 November 2015.

<sup>407</sup> Government response to Harper Review 2015, p. 1.

<sup>408</sup> Government response to Harper Review 2015, p. 2.

<sup>409</sup> Fleur Anderson, 'Scott Morrison to consider 'part-Harper' option for the effects test', *AFR*, 24 November, 2015.

wording of any changes to the relevant provisions.<sup>410</sup> In the end however, the form recommended by the Harper Review remained intact.

On 16 March 2016 the Turnbull Government announced it would 'legislate to fix competition policy in Australia', by implementing the recommended amendment to s 46.<sup>411</sup> On 5 September 2016 the Government released Exposure Draft legislation incorporating the 'effects test' and on 1 December 2016 the *Competition and Consumer Amendment (Misuse of Market Power) Bill 2016* was introduced into the House of Representatives. A Senate Economics Committee inquiry recommended that the Bill be passed, but it also recommended changes to some of the drafting of the provisions and that the Government review the reform five years from commencement.<sup>412</sup>

In March 2017 the PC was critical of the changes to section 46 in its final report into the Regulation of Agriculture, reportedly saying that that they would neither benefit consumers nor protect small farm businesses from the MSCs. Advocating a position that aligns with that of the Labor party, the PC said:

*The perception in the agricultural sector that introducing an effects test to section 46 of the Competition and Consumer Act 2010 is likely to shield farm businesses from intense competition in retail grocery markets is ill-founded. ... In any event, doing so would not be in the interest of consumers. ...In agricultural markets, consumer interests are served by competitive forces that lower the cost of food and improve its quality.*<sup>413</sup>

As at the date of writing, while the Bill was introduced and read in the Senate at the end of March 2017, the Government is yet to respond either to the PC's report or to the Committee's report.

### **III. A monitor and mediator: the AFGC**

Beyond Billson and Joyce, suppliers to the MSCs had another champion – this one outside government, in the AFGC. First under Kate Carnell, the CEO from 2008 and until 2012, and then under her successor, Gary Dawson, the peak association representing suppliers played a pivotal role not just as advocate for a substantial proportion of the businesses supplying the MSCs, but as a trusted intermediary in negotiations between stakeholders within the industry and between industry and government. How did a lobbyist organisation come to play such a pivotal role and play it so effectively?

Founded in 1995, the AFGC is an influential voice for the Australian fast moving consumer goods (FMCG) industry, a sector populated by a significant numbers of SMEs not readily capable of advocating collectively on their own behalf. As the AFGC sees it:

<sup>410</sup> Allan Fels AO, 'The Australian controversy over abuse of market power law, a study in political economy', Competition Policy at the Intersection of Equity and Efficiency Honouring the Scholarship of Eleanor M. Fox, Brussels, 8 June 2016, p. 21.

<sup>411</sup> Joint Media Statement: Fixing Competition Policy to Drive Economic Growth and Job, Prime Minister, Treasurer, Assistant Treasurer, 16 March 2016.

<sup>412</sup> *Australian Competition Law, Competition and Consumer Amendment (Misuse of Market Power) Bill 2016* (Cth).

<sup>413</sup> Phillip Coorey, 'Effects test won't help farmers or consumers: Productivity Commission', *AFR*, 28 March 2017.

*...there is a real reluctance from a lot of companies to speak to a regulator or anyone else about difficulties they face whereas they'll speak to us quite openly. So for the ACCC, if you think if they're – or for government to engage in detail on this – in the regulation of this space, they need to understand it. How do they understand it if the players won't talk to them? Well, I think it's a critical role, really, that we play in that.*<sup>414</sup>

The AFGC is both a vocal and an effective advocate for its members on a broad range of issues and concerns. As well as engaging with issues spanning the supply chain, including on competition and fair trading issues, the AFGC plays an important role in providing specialist technical expertise. This includes liaising with the Food Standards Agency and non-food related regulators such as the Therapeutic Goods Association, and providing relevant advice to members on food labelling, health/nutritional and environmental regulation.<sup>415</sup>

The AFGC has a strong public profile and lobbies government, industry and stakeholder groups, makes submissions and actively engages with the media to achieve its ends. It also works strategically. As Dawson says, 'outrage in newspaper columns will get you so far, it will get you an awareness, doesn't actually get you a result'.<sup>416</sup>

The overall aim of the AFGC is to promote the role that the \$125.9 billion food and grocery processing sector plays in sustaining Australia's economic, community and environmental health, and to champion initiatives in its sector that increase productivity and profitable growth.<sup>417</sup> A key sector in the Australian economy, it is made up of over 27,745 businesses, directly employing more than 307,170 people.<sup>418</sup>

As at June 2016 the AFGC had 135 full members, 59 associate members and 13 affiliate members. These 207 member organisations include Australian operations of the world's biggest FMCG companies (of the Nestle, Mondelez, Procter & Gamble ilk) through to small, family owned Australian businesses and many mid-tier companies.<sup>419</sup>

The food, and in particular the horticulture, sector is awash with trade and industry associations. AusVeg cites 43 peak vegetable industry bodies<sup>420</sup> the Australian Agricultural Directory lists 4 associations for sugar cane growers alone, 20 associations for crop growers, and 27 grower and professional associations for the horticultural sector, topped only by the 38 for breeders and producers of livestock.<sup>421</sup>

Horticulture is a particularly disparate sector. Still predominately small-scale family farms (although, as noted in Part 2, this is starting to change), these primary producers often work in isolation and

<sup>414</sup> Transcript of interview, Gary Dawson, pp.14-5

<sup>415</sup> AFGC website, our business <http://www.afgc.org.au/about-afgc/our-business/>

<sup>416</sup> Transcript of interview, Gary Dawson, p. 31.

<sup>417</sup> AFGC website, our business <http://www.afgc.org.au/about-afgc/our-business/>

<sup>418</sup> AFGC website, our business <http://www.afgc.org.au/about-afgc/our-business/>

<sup>419</sup> AFGC, *Annual Report* 2016, p. 3. For a full list of members see pp. 38-39. <http://www.afgc.org.au/wp-content/uploads/AFGC-Annual-Report-2016.pdf>

<sup>420</sup> Ausveg website <https://ausveg.com.au/>

<sup>421</sup> AgLinks, The Australian Agriculture Directory website <http://www.aglinks.com.au/>

must continually adjust operations in line with competition from imported and processed produce, changing market demands and pricing, and seasonal conditions. Further, the range of produce being farmed, from potatoes to macadamia nuts, berries to bananas, and rare and exotic fruits such as abiu and durian means that the needs and concerns across the sector vary greatly.<sup>422</sup> And as one industry representative observed:

*As always with any industry, people always think their patch is the most important and that's why you get the separation. I mean, I believe that you'd probably get better value by bringing different groups together and working on the common issues ... which would make it work better but our horticultural people probably think a little bit differently.<sup>423</sup>*

A possible consequence of this disparity is the lack of a cohesive voice and, at a more practical level, a lack of sufficient resources on the part of smaller produce-specific associations to have their specific concerns heard. By contrast, as noted by Gary Dawson, the AFGC does, 'recognise within our membership that it's not homogeneous and we do have strategies ourselves based on a fairly thorough piece of member research to target out offerings to various levels.'<sup>424</sup>

Kate Carnell took over from Dick Wells as CEO of the AFGC in 2008. Like Billson, she had started out in small business before entering public life. Carnell bought her first pharmacy at the age of 25, purchasing three more before being elected as a member of the Liberal Party to the Australian Capital Territory (ACT) Legislative Assembly in 1992.<sup>425</sup> By 1993 she was the ACT opposition leader and in 1995 Chief Minister. In October 2000 Carnell resigned, apparently pre-empting a no-confidence motion in relation to cost over-runs in a sports stadium redevelopment project.<sup>426</sup> Carnell went on to be the CEO of the National Association of Forest Industries until 2004, before serving as the CEO of the Australian General Practice Network for the following four years.

In 2008 the AFGC board of directors appointed Carnell as CEO. Taking to the role with gusto, she was a vocal advocate for her members, in particular those operating SMEs. During the 'milk wars' in 2011 Carnell spoke out forcefully on behalf of dairy farmers, and is reported to have observed that, '[t]his [the heavy discounting of generic milk] has caused real problems for Australian farmers and producers in terms of their profitability', noting that some companies were considering moving off-shore or modifying local operations as a result. Carnell also raised concerns about the spread of private-label goods on supermarket shelves, warning that the introduction of cheap private-label milk had set a dangerous precedent.<sup>427</sup>

This concern was also a theme in Carnell's evidence to the Senate Select Committee Inquiry into Australia's Food Processing Sector that same year, in which she elaborated on the difficulties faced

<sup>422</sup> Horticulture fact sheet, [http://www.agriculture.gov.au/ag-farm-food/hort-policy/horticulture\\_fact\\_sheet](http://www.agriculture.gov.au/ag-farm-food/hort-policy/horticulture_fact_sheet)

<sup>423</sup> Transcript of interview, CEO of a state farmers' organisation, p. 19.

<sup>424</sup> Transcript of interview, Gary Dawson, p. 7.

<sup>425</sup> Ross Peake, 'ACT's controversial former chief minister Kate Carnell has returned to the main game selling a forceful message', *The Canberra Times*, 15 March 2014.

<sup>426</sup> Ross Peake, 'ACT's controversial former chief minister Kate Carnell has returned to the main game selling a forceful message', *The Canberra Times*, 15 March 2014.

<sup>427</sup> Henrietta Cook, 'Milk wars leave sour taste in farmers', *SMH*, 21 January 2012.

by branded products when competing with private label products, sheeting home the blame to the high level of retail concentration:

*So what you see is a scenario where Coles and Woolworths own 80 per cent of the supermarket shelf space in this country. You can look at it almost like real estate. ... You need to be able to get onto that shelf to grow your product and to have the economies of scale that you need to be able to compete with those cheap imports. The dilemma is that, of that 80 per cent, more of that 'real estate' is being taken up by private label products, which means that the real estate that is left for Australian branded products is decreasing quite significantly. That means that access to customer is becoming significantly harder. Also, the other issue is that, unless you deal with Coles and Woolworths—that 80 per cent of the shelf space—your capacity to get your product in front of enough consumers to achieve the economies of scale you need to achieve to compete in this market goes down significantly.<sup>428</sup>*

During the same inquiry, in response to Treasury's view that concentration does not 'necessarily indicate that incumbent firms have market power',<sup>429</sup> Carnell drew attention to the fact that even if the market is competitive, the MSCs' power could still be used unconscionably:

*...there is market failure in this space at the moment. One of the things about market failure is that, where you have such an imbalance in power, the people with no power are not game to say anything. ... At the moment, with the ACCC legislation, unconscionable conduct is almost impossible to prove unless you can prove they actually set out to send you broke. Coles and Woolies are [not] setting out to send our members broke, [so] it is almost impossible for our members to win.<sup>430</sup>*

As previously noted, Carnell was supportive of the changes to s 46 recommended by the Harper Review and in advocating for these and other reforms, she did not mince words about what she saw as the likely consequences of a failure to act:

*In five years' time, we will be talking about when we used to have a food manufacturing industry in Australia and how unfortunate it was that it closed. ... We have got a good example of what happens if you take your eye off the ball.<sup>431</sup>*

However, while Carnell has been recognised as raising the profile of her members' concerns on both sides of the political aisle, some believe she also 'polarised her membership', with the multinationals in particular not sharing the desire of some of the smaller members to take the fight to the MSCs.<sup>432</sup>

<sup>428</sup> Kate Carnell, *Committee Hansard*, 13 December 2011, p. 20, cited in SSC, *Australia's Food Processing Sector*, 2012, p. 43.

<sup>429</sup> Treasury submission to SSC, *Australia's Food Processing Sector*, 2012, p. 5

<sup>430</sup> Kate Carnell, *Committee Hansard*, 13 December 2012, p. 28, cited in SSC, *Australia's Food Processing Sector*, 2012, p. 56.

<sup>431</sup> Kate Carnell, *Committee Hansard*, 13 December 2012, p. 28, cited in SSC, *Australia's Food Processing Sector*, 2012, p. 56.

<sup>432</sup> Transcript of interview, Robert Hadler, p. 13.

Carnell's focus was reflected in the establishment of the AFGC's SME Forum in early 2012, the impetus for which was a change in membership as more SMEs sought representation. As Carnell said in a press release:

*AFGC has an increasing number of SMEs joining our industry organisation ... Manufacturers are feeling pressure right across the supply chain, so it is important for AFGC to offer a wider range of services. ... Industry is currently weathering a 'perfect storm' from an extraordinary number of pressures including rising costs of wages, water and energy, a carbon tax, global commodity prices: sugar, dairy, cocoa, oilseeds and wheat and the near record Australian dollar making imported products significantly cheaper. ... Intense supermarket discounting in and private label growth is also forcing down retail prices and seriously impacting manufacturers' margins.*<sup>433</sup>

The AFGC's structure allows member companies within particular industry sectors to establish sector-specific forums, providing them with the opportunity to address specific issues affecting their sector, promote sector interests, and network amongst each other. These fora are seen as a way for members to advance interests and have greater leverage in influencing policy.<sup>434</sup> The SME Forum was established to serve the needs of smaller food and grocery manufacturers and to explore emerging issues impacting this group.

In May 2014 Carnell left the AFGC to become the CEO of the Australian Chamber of Commerce and Industry (ACCI). The ACCI slogan is, 'small business – too big to ignore' and the organisation represents over 30,000 business operators and industry associations.<sup>435</sup> Noting that she has run small businesses herself, Carnell made it clear that she is prepared to argue forcefully on behalf of this broad constituency and that she had the political experience to do so.<sup>436</sup>

Carnell did not stay at ACCI long however. In early 2016 she was selected by Small Business Minister Kelly O'Dwyer to be Australia's first SBFE Ombudsman. Carnell is reported to have said that she sees the position as having two key roles: to act as an advocate for SMEs, serving as a conduit between them and government and providing a single point of entry; and to focus on alternative dispute resolution (ADR) mechanisms to prevent small operators getting caught up in lengthy and expensive legal proceedings. Carnell is said to have described the role as similar to what she had been doing previously, acting as 'an advocate for small to medium business, but inside the tent.'<sup>437</sup>

As pointed out below, Billson's initial intention was that the SBFE Ombudsman have jurisdiction for dispute resolution under the FGCC but the office was not set up in time for this to come to fruition. Whether or not the Ombudsman could play such a role may be a question revisited at some stage in

<sup>433</sup> 'AFGC establishes SME Forum', *What's new in food technology and manufacturing*, 24 February 2012.

<sup>434</sup> <http://www.foodprocessing.com.au/content/training-education/news/afgc-establishes-sme-forum-1111858545>

<sup>435</sup> <http://www.afgc.org.au/our-expertise/afgc-supported-forums/>

<sup>436</sup> Australian Chamber of Commerce and Industry website; home page and 'About the Australian Chamber', <https://www.acci.asn.au/program/small-business-too-big-ignore>

<sup>437</sup> Ross Peake, 'ACT's controversial former chief minister Kate Carnell has returned to the main game selling a forceful message', *The Canberra Times*, 15 March 2014.

<sup>438</sup> James Massola, 'Kate Carnell quits business lobby to become first small business ombudsman', *SMH*, 1 February 2016.

the future. In the meantime, however, the Labor Party would like to see the capacity of the office extended, proposing that an additional \$1 million in funding be made available over two years so that the Ombudsman can help small businesses assess the likelihood of success before engaging a lawyer to commence legal action for anti-competitive behaviour.<sup>438</sup>

The Harper Review appeared to echo these views in considering ways to increase access to justice for small business. The panel did suggest that the ACCC could play a more active role in connecting small businesses to ADR schemes and noted the role of the extension of unfair contract terms for small businesses in this regard;<sup>439</sup> however it also recognised that this would not always be the best use of ACCC resources. The Panel noted the newly created SBFEE Ombudsman position, along with the role to be played by existing ombudsman offices, small business commissioners and small business offices,<sup>440</sup> before endorsing several recommendations made in the PC's Access to Justice Arrangements report, including:

*...that future reviews of industry codes consider whether dispute resolution services provided pursuant to an industry code, often by industry associations or third parties, are provided instead by the Australian Small Business Commissioner under the framework of that industry code.*<sup>441</sup>

The new CEO of the AFGC had a very different background from that of Billson or Carnell. Gary Dawson was a journalist, having worked in print, radio and television before completing a Bachelor of Economics and moving into strategy and communications roles, including that of a senior advisor to former Prime Minister John Howard and as an advisor to his AFGC predecessor when Carnell was still the ACT Chief Minister.<sup>442</sup> Dawson sported a somewhat different style to Carnell. As one industry observer noted, he 'is an effective advocate for the AFGC but in a quieter way [than Carnell]'.<sup>443</sup>

The most significant initiative – and as he says himself 'far and away the hottest issue'<sup>444</sup> – during Dawson's time with the AFGC was the development of the FGCC. On his first day in the job Dawson found himself not in his office but at Woolworths, meeting with senior executives to discuss the issues that had arisen out of the development of the NFP. In Dawson's words:

*... the relevant ministers ..., Joe Ludwig, the Agriculture Minister, and David Bradbury who was the Assistant Treasurer with responsibility of competition law, convened a stakeholder forum in Sydney that involved us and the retailers and farmers and various produce groups and they made it very clear at that meeting that they were not willing to amend the law to take – in order to take particular action over this perceived problem of retailers market power, that there'd just been a range of amendments to the Competition Consumer Act, they were simply not interested in taking further amendments forward and that they wanted the players – the*

<sup>438</sup> Broede Carmody, 'Labor plans to make it easier for small business to sue big companies', *Smart Company*, 15 March 2016.

<sup>439</sup> Harper Review 2015, recommendation 53 – small business access to remedies, p. 85.

<sup>440</sup> Harper Review 2015, p. 84.

<sup>441</sup> Harper Review 2015, recommendation 53, p. 85.

<sup>442</sup> AFGC website, <http://www.afgc.org.au/about-afgc/key-contacts/mr-gary-dawson-chief-executive/>.

<sup>443</sup> Transcript of interview, Robert Hadler, p. 19.

<sup>444</sup> Transcript of interview, Gary Dawson, p. 29.

*stakeholders, the market players – to see what they could do to address perceived problems.*<sup>445</sup>

*..the AFGC certainly put proposals, that was under my predecessor, for a mandatory code similar to what's been done in the UK with its own statutory watchdog, code ombudsman or code of UK ... so that had been put forward as a proposal. I come into this role, the then government made it clear they weren't willing to amend the Act to do that and so, I suppose, from my point of view and my board's point of view it was a matter of, well, what can we usefully do that will make it – that will improve the environment for our members and that's where we decided to sit down with Coles and Woolworths and the NFF and that was the initial discussion that – around what might be possible.*<sup>446</sup>

Dawson soon realised that 'anecdotes will get you so far but eventually you need evidence and data' and so engaged accounting giant, KPMG to undertake a detailed investigation into what was actually happening in the market.<sup>447</sup> In releasing the resultant Competitiveness and Sustainable Growth Report covering 2010-13, Dawson said that the report:

*... demonstrates how tough the market conditions have become for food and grocery suppliers, squeezed between the unstoppable force of dominant retailers and the immovable object of high labour, utility and regulatory costs.*<sup>448</sup>

Dawson believed strongly in the potential of an industry code to level the playing field between retailers and suppliers.<sup>449</sup> Under his leadership some have argued it was in fact the AFGC that 'led the charge' for the first draft of what would become the FGCC.<sup>450</sup> Dawson was later to characterise the FGCC as, 'an industry led solution to put some rules of engagement in place and remove some of the bad behaviour we've seen in the past,' going on to say, 'it will improve the trading environment, give suppliers a fair go.'<sup>451</sup>

In early 2017 Dawson announced his decision to step down as CEO of the AFGC. With the first review of the FGCC slated for early 2018, an element in his decision to leave may well have been that at this critical juncture in the code experiment, it is important that the AFGC and its members be represented by a CEO unencumbered by the style and approach taken in the previous negotiations.<sup>452</sup> He would leave in March,<sup>453</sup> and regardless of the outcome of the review or any assessment that may be made of the FGCC in the longer term, it would be fair to say that the Code is an important and, as far as the AFGC is concerned, a positive legacy of his leadership.

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<sup>445</sup> Transcript of interview, Gary Dawson, p. 27-28.

<sup>446</sup> Transcript of interview, Gary Dawson, p. 29.

<sup>447</sup> Transcript of interview, Gary Dawson, pp. 31-32.

<sup>448</sup> 'Financial squeeze getting tougher for food and grocery suppliers', AFGC media release, June 2014.

<sup>449</sup> 'Financial squeeze getting tougher for food and grocery suppliers', AFGC media release, June 2014.

<sup>450</sup> Director of a consultancy that advises suppliers, p. 17.

<sup>451</sup> Sarina Locke, 'Farmers and food suppliers welcome more power under recommended changes to competition policy', *ABC Rural*, 1 April 2015.

<sup>452</sup> Transcript of interview, Gary Dawson 2, p. 22.

<sup>453</sup> 'AFGC CEO resigns', *Retail World*, 3 February 2017.

## 7. At the negotiating table

In this Part of the report we look at how the substance and form of the FGCC was negotiated. We start with identifying who was at, who walked away from, and who apparently was not invited to join the RSR that produced a first draft of what was to become the FGCC. In the end, just three organisations were represented: Coles, Woolworths and the AFGC. Explanations for this vary and we consider the reasons if and why others, particularly the NFF and Metcash, as well as the retailers - Aldi, Costco and the IGAs - particularly did not participate to the same extent if at all. We trace the process of negotiation, highlighting the matters on which agreement was readily reached, and why, and the compromises that this entailed.

Moving from industry to political machinations, we document the role played by Billson, mostly behind the scenes, supporting at times, coaxing at others but also strong-arming where he saw necessary, on issues that he regarded as critical and, in particular, in an attempt to bring around important stakeholders in support of the process. We also explore the impact of other political dynamics afoot - in particular, the ultimately unproductive dialogue between the Labor Party and the NFF as to its role in the negotiation, before turning then to the role of Treasury.

We provide an overview of the process by which Treasury reviews and consults on draft codes, such as the one presented to it by the RSR. It is important in this context and so we provide a brief background on the manner in which such codes are developed from a regulatory perspective, their place in the overall regulatory framework and the benefits that they are seen to deliver. We note that elected Australian governments of both persuasions have long advocated codes of conduct as a method of self- or co-regulation; that industry is often seen as the best driver of tailored and effective codes; and that the prescription of mandatory codes under the CCA is viewed generally as an avenue of last resort.<sup>454</sup> Not insignificantly, in the almost 20 years since provision for codes was legislated, the FGCC is the first prescribed voluntary code to be promulgated, all others being mandatory, and as will become apparent in this section of the report, the question of the FGCC's status in this regard was fiercely debated. It is a matter also likely to be reargued in the 2018 review.

In the context of Treasury's regulatory review of the proposed code, we record the stated purposes of the FGCC and map out its main provisions. We then document the debate overseen by Treasury and continued in the Senate inquiry that was held once the FGCC was laid before Parliament. As is clear from this exercise, this debate coalesced on more than just the issue of the Code's coverage (to be determined by whether it was voluntary or mandatory), encompassing a range of issues concerning whether the proposed provisions were too lax and whether the dispute resolution processes were appropriate and likely to be workable. On each of the issues at stake, the position put by the RSR more or less held sway.

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<sup>454</sup> *Policy guidelines on prescribing industry codes under Part IVB of the Competition and Consumer Act 2010*, May 2011, Australian Government Treasury, p. 6.

## I. The (not so) round Roundtable

The so-called RSR that was established to negotiate and produce a first draft what was to become the FGCC was in fact more triangular than round. Places at the negotiating table were limited. In the end, there were only three seats taken: by the AFGC, Coles and Woolworths. For the AFGC, this became Gary Dawson's chief preoccupation from virtually day one in the job. Clearly his predecessor had already started the conversation from the AFGC's side, taking the strong position that Australia's should emulate the UK example – nothing less than a mandatory code, administered and enforced by a dedicated independent grocery ombudsman would suffice. Dawson's mission and challenge was to translate that position into a proposition that would bring the MSCs on board.

For Coles, the lead negotiator was General Manager of Corporate Affairs, Robert Hadler, a self-described specialist in advocacy, crisis management and reputational strategies, with a long track record and experience in large corporates, including grocery suppliers such as Goodman Fielder, as well as AWB and National Australia Bank.<sup>455</sup> For Woolworths, Hadler's opposite number, Andrew Hall, occupied the other retailer seat at the table, at least initially, and then was replaced by Tjeerd Hegen (Woolworths Manager of Supermarkets and Petrol, and like several of the MSC executives, formerly of the UK grocery giant Tesco).<sup>456</sup> As might be expected given their roles at each of the MSCs, both Hadler and Hall had politics in their education, and Hall had practised in it – as a media adviser to Warren Truss MP (having been a journalist prior to that) and then as Federal Director of the National Party, before taking up the position as Director of Corporate and Public Affairs at Woolworths. Hadler, Hall and Hegen have all since left the MSCs, but Hadler and Hall are still plying their corporate affairs craft, Hadler at a global consulting firm (FTI Consulting) that helps businesses manage change and risk and Hall as Executive General Manager, Corporate Affairs at the Commonwealth Bank, while Hegen now heads up Dutch discount retailer, HEMA. Hadler participated in an interview for this research. Regrettably both Hall and Hegen declined the invitation.

Over the course of just more than a year, from about September 2012, there was a frenzied process of discussion, debate and drafting, involving multiple meetings between the three men as well as follow up and side meetings with others from their own organisations and constituencies. While Hadler and Hall consulted internally, and it is also clear that external legal advice was sought, it is telling perhaps that the MSC representatives leading the negotiations on behalf of their organisations were in public and government relations roles, with no front-line involvement in the actual business of buying and selling groceries.

The AFGC consulted with its members and particularly those involved in its SME forum. But it also consulted with the ACCC and, according to Dawson, with Aldi and Metcash too. At some stage in 2012 it had become known, at least within the industry, that the ACCC was investigating with a possible view to an unconscionability action against one or both of the MSCs. An ACCC

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<sup>455</sup> Robert Hadler, LinkedIn profile, <https://www.linkedin.com/in/robert-hadler-49154215/?ppe=1>

<sup>456</sup> In addition, in 2017, a former Tesco executive (Jeff Adams) was appointed to lead Metcash. See 'Former Tesco exec Jeff Adams to be next Metcash CEO' *Sydney Morning Herald*, 11 July 2017.

representative recalls that around that time there was an approach made to the agency by ‘industry associations’ in the sector. However, he also recalls that unlike in most instances where the ACCC is asked for and provides quite detailed guidance on design and drafting of a code, in this instance the association in question was prepared to and took much of the running itself:

*So we were approached initially by two industry associations together who had some interest in a food and grocery code of conduct, and at the time there was a genuine question mark about whether it would be something they would consider, whether they felt needed to be prescribed... So we had our investigation on foot and we had the industry association saying so is there some other way beyond the investigation that we can help, and so we said well there’s codes of conduct and this is how they work and so forth, so there was interest coming from them on that. I think it would be fair to say at some point in the investigation, one or more of the retailers also expressed a strong interest in a code approach and arguably to find a way forward that was able to show... that they might be able to use to say: here’s our commitment to treating our suppliers well, we submit ourselves to a code of conduct and we’re willing to sign up for that. So that’s really the genesis, and giving that we had long standing guidance as to what we think works as an industry code of conduct, less aspirational, more concrete commitments and so forth, for example, some sort of administration mechanism, it’s more the engineering of a code that we think is more likely to work, transparency, that we are able to say, well look in these circumstances... sit down with them, understand the kind of issues that were of concern to the industry associations on behalf of their members and give some guidance on how some of that might be ultimately captured in a code of conduct, but to be fair, to be quite frank, [in this instance] the industry associations took some very high level suggestions or guidance on how codes might work in this situation and secured their own legal advice and so forth, and worked up a code.<sup>457</sup>*

This account is consistent with the recollection of a MSC representative who recalls that initially there was:

*...an open agreement on how we would conduct ourselves, but it wasn’t a legally structured agreement. A lot of it [was] based on UK wording. But when we approached the market and the ACCC in particular and said, we would like this to be an industry code, they gave us very strong and good advice on how to set up what was known as a voluntary code. And we went down that path, and with their assistance got to the stage of it becoming an instrument that went through a whole range of treasury drafting, and eventually ended up as a regulation.<sup>458</sup>*

As is the way of any negotiation, the parties started some way apart. On Hadler’s account, he ‘did the first draft... a principles draft, based on the [Produce and Grocery Code]’.<sup>459</sup> The AFGC countered with its own draft and a quite different version: ‘basically a straight lift out of the UK legislation’<sup>460</sup> (a

<sup>457</sup> Transcript of interview, senior representative of the ACCC, p. 20.

<sup>458</sup> Transcript of interview, MSC representative, pp. 1-2.

<sup>459</sup> Transcript of interview, Robert Hadler, p. 21.

<sup>460</sup> Transcript of interview, Robert Hadler, pp. 20-21.

draft that had possibly been on Carnell's desk in some form for some time and that may also have reflected the consultations that the AFGC had had with the grocery adjudicator in the UK, Christine Tacon). According to the same ACCC official, this initial divergence in approach is common in code negotiations, and the agency's advice was very much in favour of 'more concrete' provisions so that those subject to and benefiting from the code would 'understand what was intended in a given situation.'<sup>461</sup> Apart from that advice though, the only substantive input that the ACCC had at that stage was to identify 'the degree to which we thought the issues covered in the code aligned with the issues that we had as live issues in the matters we were investigating.'<sup>462</sup>

Predictably perhaps, Coles's response to the AFGC's opening gambit was: 'no'.<sup>463</sup> But it took hardly any time at all it seems, to close the gap and the parties quickly came into alignment on at least two significant points, namely that:

- (1) the proposed code had to be sufficiently detailed in relation to the behaviour with which it was concerned but at the same time sufficiently flexible to allow for legitimate commercial negotiation; and
- (2) it had to be a statutory instrument but should be voluntary rather than mandatory in its application.

On these things, according to Dawson, from early on, 'everyone knew where each other was coming from.'<sup>464</sup>

#### (a) Detailed but still flexible

It was readily agreed that 'in order to be credible' the code 'couldn't simply be an aspirational statement or set of principles'.<sup>465</sup> It had to get to the specifics of the matters about which suppliers were aggrieved – matters such as unilateral and retrospective variations, payments for shrinkage and wastage and even intellectual property protection where a supplier is supplying for MSC private labels as well as their own brands (a matter not covered in the UK counterpart). As Dawson explains, his personal view was: 'let's not talk about generalities', we need the code to deal and deal meaningfully with 'the top 10 things that the industry wants to change in terms of the behavioural relationship'.<sup>466</sup>

At the same time, it is clear that the parties were also in heated agreement that the code could not be overly prescriptive. It had to allow for commercial flexibility. A MSC representative explained this balance, which he saw as having been achieved in the drafting of the code, as follows:

*...the best part of it was that it was prescriptive enough for people to have comfort on both sides of the fence in certain aspects of mutual dealings that we do. Areas of particular*

<sup>461</sup> Transcript of interview, senior representative of the ACCC, p. 22.

<sup>462</sup> Transcript of interview, senior representative of the ACCC, p. 22.

<sup>463</sup> Transcript of interview, Robert Hadler, pp. 20-21.

<sup>464</sup> Transcript of interview, Gary Dawson, p. 32.

<sup>465</sup> Transcript of interview, Gary Dawson, p. 41.

<sup>466</sup> Transcript of interview, Gary Dawson, p. 41.

*sensitivity were covered with some degree of prescription, but it wasn't written in a way that was so absolutely prescriptive that we couldn't operate the business.*<sup>467</sup>

For Dawson, flexibility in the code provisions was not only in the interests of the retailers. He could see the merit in it for suppliers ('our members') and that meant for consumers as well. So strong was his view on this that he was prepared to wear the inevitable criticism from AFGC constituents for not going in hard enough:

*...one of the key features of the code which has been subject to criticism is the fact that the code allows the retailers a significant degree of commercial flexibility, so the code – it's not business as usual for them, but it certainly doesn't impede their own corporate need to respond flexibly to the shifting tides of consumer demand and consumer pull. So I think one of the benefits for them was to end up with a quasi, well, what is a regulatory instrument but which nonetheless does not dictate a rigid structure in which they must operate but one which has that flexibility for them to operate as they need to operate to be successful and in some ways we copped a bit of criticism for allowing those provisions, but in many ways it's of as much interest to our members to have commercial flexibility as it is for the supermarkets. We were, look, frankly we were conscious of the interests of suppliers, many of whom might want the opportunity to go in and negotiate a particular deal and ultimately that's in the consumer's interest as well and the consumers – you don't want the things that are on the shelf now to be there set in stone forever, that's the whole point of a dynamic market - - - you have movement and by definition that means there's going to be winners and losers every day in this market. Now, you want some rules of engagement, some bumper rails - as Bruce Billson used to put it - but you don't want it to be too prescriptive because you choke off that competitive drive...*<sup>468</sup>

As for whether the code drafting strikes the 'right' balance between detailed prescription of behaviours on the one hand, and flexibility so as not to stifle negotiating capacity on the other, commentators are divided. Certainly there can be no quibble that the Code delves into minutiae, touching on both the form and substance of almost every aspect of contractual dealings between grocery retailers and their suppliers. Its formal style of language is consistent with its status as a legislative instrument but is also redolent of many federal statutory texts – torturous in the drafters' evident attempt to be both comprehensive while building in qualifications and creating carve-outs. In many instances, obligations as to retailer conduct are framed in terms of 'reasonableness' and where certain conduct is prohibited, the prohibition is subject to provision otherwise in the grocery supply agreement (GSA).

According to an experienced adviser to suppliers, a person who has conducted extensive training on the Code, the provisions are not prescriptive enough and the reason for that deficiency is that because it has been written by 'lawyers':

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<sup>467</sup> Transcript of interview, MSC representative, p. 2.

<sup>468</sup> Transcript of interview, Gary Dawson, pp. 49-50.

*...I would make some elements of this more explicit, so specifically around things like range reviews so publishing criteria on range reviews, I'd make it less ambiguous what that means... The ability to create a little bit more structure around how some of these things are applied I think is very straightforward, that isn't – law makers would really struggle with that, the reason we've run this program rather than lawyers is because we look at this through – I'm not a lawyer, never could be or would be, I'm nowhere near bright enough – but the ability to apply the commercial intent to this is the crucial piece, but it's been written in large part by lawmakers ... So the way that we train parts of this is through joining the dots because each dot in isolation doesn't do the job, so a good example of that is the retailer must publish their range review criteria for range and space, doesn't say what criteria need to be or anything along those lines...<sup>469</sup>*

Concerns about the legalistic character of the Code were also raised by another interviewee with extensive training and consulting experience in the sector:

*My focus is always on the issue of dispute resolution but the way in which this is framed in terms of the rights of suppliers, well ... it's almost a roadblock to a supplier's success because the language and the manner of drafting creates almost impenetrable barriers.<sup>470</sup>*

A MSC representative in turn complains of the opacity of the FGCC, comparing it to, 'having to hand a copy of legislation to people'.<sup>471</sup> The interviewee went on to say that even after providing training to ensure that employees understand their obligations under the Code there remains some confusion. While being in no way opposed to having clear guidelines for the industry, she added: 'handing out legislation is really unfair and actually quite unhelpful, but I had to do it.'<sup>472</sup>

An insider with knowledge of the negotiations has suggested that this lack of precision may have been intentional on the part the MSCs:

*... typically the retailers would try and negotiate language that was aspirational and less likely to be something that you could actually have enforced in a concrete way ...<sup>473</sup>*

By contrast, according to a grocery business advisor, the provisions fall short because they are too prescriptive and so either duplicate or conflict with general obligations under the CCA, and the reason for this is because the drafting was not done by 'legally trained practitioners':

*...whilst the ACCC is party to the conversations, industry representatives who represent certain players are dominating the drafting. The drafting isn't being done by legal-trained practitioners so the drafting is pretty average in my view and, really, what is it going to result*

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<sup>469</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 52.

<sup>470</sup> Transcript of interview, Robert Gaussen, p. 42.

<sup>471</sup> Transcript of interview, MSC representative, p. 22.

<sup>472</sup> Transcript of interview, MSC representative, p. 22.

<sup>473</sup> Transcript of interview, senior representative of the ACCC, p. 22.

*in? ... I think there's far too many mandatory, voluntary, industry-based, voluntary codes, mandatory codes and I think it's actually detracting from the statute itself.*<sup>474</sup>

Graeme Samuel AC too has suggested, somewhat disparagingly, that the Code is so lacking in flexibility as to read more like a rule book for the industry:

*...40 pages of specific prescription as to how they must conduct their business.*<sup>475</sup>

Reflecting the not uncommon divergence of views on many aspects of regulation of this sector, others however believe a prescribed code such as the FGCC strikes just the right balance:

*[It] provides an avenue for the government to consider a policy response that is not statute, it's not too prescriptive but it provides – with these prescribed codes... you get transparency about the contract you're getting into, you get an ability to resolve disputes while you're within the term of your contract and the termination process for the contract is one that is reasonably fair.*<sup>476</sup>

## (b) Prescribed but voluntary

The AFGC-MSA negotiators also agreed that the Code had to have some 'regulatory force'.<sup>477</sup> What this meant in effect was that it had to be a statutory instrument, prescribed under the provisions of the CCA, and not yet another industry (non-statutory) code. BUT, between the two models provided for by the legislation – a mandatory and a voluntary model – it was also readily (in the end) agreed that this code had to be in the latter category. To the layperson, this would appear to suggest that the code would be optional. However, the only option is in fact whether or not to sign on. Once signed on, compliance with the code is in effect mandatory in the sense that its provisions are legally enforceable - a breach of the Code is a breach of the CCA. While the terminology and difference between the two models may have generated some confusion amongst outside observers and commentators, there was no doubt about its effect amongst those at the negotiating table. For the MSCs, signing up to a so-called voluntary (but prescribed and enforceable) code would represent a serious legal commitment and in turn lend serious credibility to the initiative.

It is possible that the decision to support a statutory code and one that was detailed in its prescription of behaviour was influenced too by the experience with the PGCC – a purely voluntary instrument introduced by the industry in 2000 to deal with many of the same issues that had brought the parties to the table on this occasion. That code had had a wide ranging industry membership and had addressed issues concerning product standards and specifications, contracts, product labelling, packaging and preparation and notification of acquisitions. It provided for an ombudsman who provided dispute resolution and facilitated mediation services. Yet, despite covering much of the same ground as the RSR-proposal, the PGCC was criticised for being too high level in its prescriptions, for

<sup>474</sup> Transcript of interview, interviewee that consults to / advises grocery businesses, pp. 4-5.

<sup>475</sup> Transcript of interview, Graeme Samuel AC, p. 29.

<sup>476</sup> Transcript of interview, senior representative of the ACCC, p. 9.

<sup>477</sup> Transcript of interview, Legal Director at the AFGC, pp. 36-7.

the lack of reporting responsibilities and its failure to offer protection from commercial retaliation.<sup>478</sup> In an independent review in 2004, it was recommended that government step in and mandate the code.<sup>479</sup> But there was no appetite for that recommendation, government being sensitive to imposing additional regulation and associated compliance costs. From 2009, parties began to resign their memberships and by 2011 the PGCC had fallen into desuetude, regarded by many as ‘very aspirational ... [lacking] any real bite, any real expectation in terms of behaviour other than the spirit of goodwill.’<sup>480</sup>

In the context of the RSR, it appears to have been the Coles negotiator who in fact first proposed the idea of a voluntary prescribed code. Hadler told us that he was able to secure agreement to the idea high up in the Coles hierarchy not least because the provisions being negotiated were not seen to go beyond the retailer’s obligations under existing laws anyway.<sup>481</sup> Another interviewee pointed out that agreement to involvement in the Code was very much influenced by the pressure being brought to bear by the ACCC unconscionability investigation was then in full swing (‘it was done at a particular point in time when they had an unconscionable conduct investigation going on....’).<sup>482</sup>

At same time, there was clear recognition that, in practical and political terms, the code would be voluntary in name only. As Hadler points out:

*...despite being voluntary, the statutory version was seen as having regulatory teeth because once you’ve signed it, you’re in. And you won’t opt-out. The reputation damage is too big...it wasn’t actually – it wasn’t voluntary, I mean, to be honest.*<sup>483</sup> (emphasis added)

Hadler’s view on this resonates with the ACCC. There is certainly ‘reputational risk’ as a deterrent to a party opting out of a code and added to this, a senior ACCC representative pointed out, would be the risk that the government would take the action to step in and mandate the code, thereby producing the very situation that had sought to be avoided in the first instance:

*So you can think about walking away but it’s at your cost and it’s at the risk of having a mandate [imposed].*<sup>484</sup>

This risk is evidently a real one in the minds of MSC representatives. One told us that, were his organisation to opt out, ‘it would be an automatic move to a mandatory code’.<sup>485</sup>

In some respects, agreement to a voluntary rather than a mandatory code represented an early back down by the AFGC, given its previous position. But it had also been made clear by government that it

<sup>478</sup> Treasury, *Improving Commercial Relationships in the Food and Grocery Sector* consultation paper, August 2014 (Treasury, FGCC consultation paper, 2014), pp. 39-40.

<sup>479</sup> Neill Buck and Associates, *Report of the review of the retail grocery industry code of conduct*, Dept. of Industry, Tourism and Resources, 2003.

<sup>480</sup> Transcript of interview, senior representative of the ACCC, p. 8.

<sup>481</sup> Transcript of interview, Hadler, p. 22.

<sup>482</sup> Transcript of interview, former senior representative of the UK OFT, p. 7.

<sup>483</sup> Transcript of interview, Hadler, pp. 23, 26.

<sup>484</sup> Transcript of interview, senior representative of the ACCC, p. 23.

<sup>485</sup> Transcript of interview, MSC representative, p. 7.

was looking to the industry to 'solve' the problem and would only step in an industry solution was not forthcoming:

*... they [referring to various government representatives] made it very clear at that meeting [referring to a meeting between government and industry representatives] that they were not willing to amend the law to take – in order to take particular action over this perceived problem of retailers market power, that there'd just been a range of amendments to the Competition and Consumer Act, they were simply not interested in taking further amendments forward and that they wanted the players - the stakeholders, the market players – to see what they could do to address perceived problems before - - - That was the, I think, the catalyst for the first discussions around a code that – so, there'd been proposals put forward for a mandatory supermarket code which would have been an amendment to the Act and that's where the ministers were saying, no, we're not willing to do that.<sup>486</sup>*

The steer from government aside, for Dawson, unlike his predecessor, a voluntary code was a no-brainer. Firstly, it was clear in his mind that Carnell's call for the replication of the UK model in Australia would not be supported by government. Secondly, the MSCs had to be involved in the project and there was no doubt that they were not going to come to the party for a mandatory code. The voluntary model under the CCA enabled the AFGC to lead the charge for an instrument with 'real teeth',<sup>487</sup> but at the same time bring and keep the MSCs on board. As another AFGC representative has explained:

*... it started off with all options but very quickly narrowed to that [a prescribed voluntary code] and there were a number of - - - Yeah, look, I can tell you that Coles put forward the option of a prescribed voluntary code. [The benefits of having it prescribed] were that it had some, well, that it was a legislated instrument and had some regulatory force .. they were sensitive to the perception issue around it being seen as just a bit of paper versus something that had real teeth and from our point of view the AFGC having previously had a position around a mandated legislated approach we couldn't accept anything less than something that had some regulatory rigour behind it, regulatory force, so the fact that the Act provided for that was quite fortunate because it gave us a, if you like, a bit of a bridge to an instrument that has real effect. In the game of chess that is one party trying to read thoughts of the other person about what they're thinking about you and so forth, from our perspective there were obvious attractions to the supermarkets, for it being a voluntary prescribed code, number one, it gave them the appearance of being the good guys, they get to sign on and get the marketing and publicity PR kudos or something like that.<sup>488</sup>*

The cynicism in this perspective as to why the MSCs backed a voluntary code may not be entirely fair. According to Dawson, the MSCs 'genuinely felt they needed to find a way forward because of the

<sup>486</sup> Transcript of interview, Gary Dawson, pp. 27-8.

<sup>487</sup> Transcript of interview, Legal Director at the AFGC, pp. 36-7.

<sup>488</sup> Transcript of interview, Legal Director at the AFGC, pp. 36-7.

pressure that was being brought to bear ... [and they] genuinely they felt that this was only worth doing if it stood up to scrutiny.<sup>489</sup> What's more, Dawson held the view, to which the MSC representatives evidently also subscribed, that going down the voluntary code route meant that the drafting of the code's provisions could be controlled by the 'industry' (which in this context meant the AFGC and the MSCs). The alternative, a mandatory code, meant that that control would be divested to government. Drafting control was seen as critical as it would enable the code to be tailored to 'the realities of the market'<sup>490</sup> and ensure that it addressed the particular issues at hand. Hence, the voluntary model was viewed as essential ultimately to maximise the chances of the Code being effective, as well as legitimate:

*...it was another reason in my mind for us to pursue a prescribed voluntary code rather than expecting governments to legislate and write amendments to the Act to deal specifically with this particular market and, I think, again, I think that's one of the strengths. ... I think if you ask a – if you just ask the Treasury or the ACCC to draft a mandatory code I'm not sure it would have been at all as relevant to the market, the realities of the market as this is and that's in part a function of the fact that it is a voluntary – it's voluntary sign up and therefore required negotiation with the other players...<sup>491</sup>*

Dawson is also of the view that for the MSCs, there were significant commercially strategic benefits in a code that was meaningful in its degree of detail and in its statutory status. Signing up would establish credibility not only in the eyes of government, but in the eyes of suppliers as well and, in the long term, this could be important in maintaining security of supply:

*... there are benefits for them in it as well. I think in terms of their credibility around the way they deal with their suppliers, in terms of, so it won't always be the case that Australian food and grocery manufacturers will have to go to Coles and Woolworths to sell their wares. Markets change, markets are already changing, our export markets are opening up dramatically. So from their point of view when they think about certainty of supply in the future around key categories, key lines, key products, the ability to have a framework in place as provided by the code is going to work in their favour and I think that's going to be more of an issue in the future than has been the case in the last few years..<sup>492</sup>*

## II. Holding out: the NFF

The NFF pulled up a chair at the negotiating table initially but at some stage, relatively early in proceedings it seems, decided to leave the room. Having the NFF at the table made sense. It meant that the issues from the perspective of both packaged and fresh food suppliers could be covered. Indeed, early on, it even appeared to be contemplated that an all-encompassing code, one that

<sup>489</sup> Transcript of interview, Gary Dawson, pp. 36-7.

<sup>490</sup> Transcript of interview, Gary Dawson, p. 43.

<sup>491</sup> Transcript of interview, Gary Dawson, pp. 42-3.

<sup>492</sup> Transcript of interview, Gary Dawson, p. 49.

subsumed all pre-existing codes (the PGCC and the HCC), was on the drawing board and that the new code might cover indirect as well as direct suppliers.<sup>493</sup> But it fairly quickly became evident that that idea was utopian.

In part, the restriction of the draft code to direct suppliers may have been a function of the fact that the process moved so quickly and there was such a strong sense of urgency to get it completed that there was not time to grapple with the much wider set of issues as well as negotiate with the broader range of stakeholders that would have been necessary to produce an all-encompassing instrument.

In part, it may have been because the NFF pulled out of the process thereby removing a strong voice for fresh suppliers from the negotiating table. Both Hadler and Dawson give an account of the reasons for this that involved reference to ‘political factors’.<sup>494</sup> Ultimately though it was clear that the NFF was holding out for a mandatory code:

*So there was a bit ... around how much relevance it [had], and also [whether] it was going to be mandatory. So we were of the view that it should be mandatory.*<sup>495</sup>

It appears that what the NFF was striving for was a fully inclusive, mandatory code of conduct to regulate the entire sector. While acknowledging that this could be ‘tricky’ given the diversity of stakeholders,<sup>496</sup> the NFF’s view was that ‘if it’s [the Code] going to be across the supply chain then it should be mandated, it should be that all players are in.’<sup>497</sup>

It would have become obvious at some early stage that this was not the way in which the majority at the table were headed. As the CEO of the NFF explained:

*So from the farm sector – we actually had the discussion to say, farmer’s supply chain to processors, not necessarily all directed to retailers. So can we be involved in this code of conduct, given it’s a retailer supply chain? And the actual code itself has a lot to do with shelf space and contracts, which really are not directly relevant to farmers.*<sup>498</sup>

Perhaps given the political heat and traction surrounding the dairy industry around the time, the NFF considered that it had more bargaining power in direct negotiations with government. If that was their call, history shows it was the wrong one. In his typically colourful account, Billson points out – ‘the NFF played that card and then were left out in the cold ...’<sup>499</sup>

The NFF stuck to its guns nevertheless, making it clear in its submission to the Senate Economics Legislation Committee review of the proposed code in March 2015 that it continued to support a ‘mandatory, binding code that encompasses all retailers’ and would be ‘monitoring how the initiative

<sup>493</sup> Transcript of interview, Robert Hadler, p. 21.

<sup>494</sup> Transcript of interview, Gary Dawson, p. 34; Transcript of interview, Robert Hadler, p. 23.

<sup>495</sup> Transcript of interview, CEO of NFF, p. 13.

<sup>496</sup> Transcript of interview, CEO of NFF, p. 17.

<sup>497</sup> Transcript of interview, CEO of NFF, p. 13.

<sup>498</sup> Transcript of interview, CEO of NFF, p. 13.

<sup>499</sup> Transcript of interview, Bruce Billson, pp. 30-1.

will work in practice'.<sup>500</sup> However the NFF also acknowledged that while 'not perfect' the FGCC 'does address several key imbalances with regard to major retailer power over suppliers.'<sup>501</sup>

### III. Outside the tent: Aldi and Costco

Neither Aldi nor Costco were seated at the negotiating table. On one view, the absence of Aldi might be regarded as particularly troublesome given its growing competitive significance in the sector. Costco has a much lower retail share but is nevertheless a major wholesale presence in groceries. Aside from their market relevance, an objective observer might have taken the view that as large foreign companies they may well have been able to make a valuable contribution, drawing on their regulatory experience from other jurisdictions. But the fact is they were not were not involved, and reasons for this vary again depending on who is offering them.

According to Hadler, Aldi 'refused to participate'.<sup>502</sup> This appears to suggest that Aldi was invited and declined to pull up a chair. According to Dawson, Aldi was approached (possibly by the AFGC on its own) for feedback on drafts and gave it. Nevertheless, there appears to have been a feeling that Aldi's input was not a priority and could even be a hindrance. Securing agreement, and doing so quickly (as the circumstances were evidently seen to demand), were imperative and the only way to reach this outcome was to confine substantive input to the MSCs. According to Dawson:

*...from a practical point of view we felt that to be effective it had to have Coles and Woolworths signatories and to broaden it beyond that in terms of the negotiation would potentially jeopardise the ability to get an outcome, so that was simply a pragmatic view on what might be achievable.*<sup>503</sup>

A direct account from Aldi as to whether it was or was not invited to participate in the code negotiation and drafting process is not available. However, Aldi did make a submission to the consultation held by Treasury on the AFGC-MSC draft that had been handed to government. As is pellucidly clear from that submission, Aldi did not see much in the initiative that should be material or could even be relevant to it. Indeed, at the time of their submission, Aldi was in two minds as to whether it would sign on – 'ALDI is still considering whether it would be prepared to opt in to the Code'<sup>504</sup> – expressing concern that to do so would only:

*...add complexity to our current effective and transparent procedures and processes with suppliers. This would increase administrative and compliance costs on ALDI and its suppliers*

<sup>500</sup> NFF submission to the Senate Economics Legislation Committee Inquiry, *Competition and Consumer Act 2010 (Competition and Consumer (Industry Codes – Food and Grocery) Regulation 2015*, March 2015, p. 3.

<sup>501</sup> NFF submission to the Senate Economics Legislation Committee Inquiry, *Competition and Consumer Act 2010 (Competition and Consumer (Industry Codes – Food and Grocery) Regulation 2015*, March 2015, p. 3.

<sup>502</sup> Transcript of interview, Robert Hadler, p. 23.

<sup>503</sup> Transcript of interview, Gary Dawson, p. 34.

<sup>504</sup> Aldi submission to Treasury, FGCC consultation paper, 2014, 19 September 2014, p. 1.

*which is in contrast to ALDI's business model to simplify and standardise its operations to keep operating costs low in order to ensure everyday low prices for consumers.*<sup>505</sup>

Aldi also made clear that it did not view the code as having direct application to its behaviour or business model:

*In short, we understand that the Code seeks to respond to concerns in relation to specific behaviours of the two major supermarket chains ('MSCs') who have significant market power...*

*In considering the Code, ALDI notes that it does not have the same market power as the MSCs, and it does not engage in the types of behaviours that have been raised in relation to the MSCs as outlined in the Consultation Paper. ALDI already has clear and fair agreements and good relationships with suppliers, and efficient and simple processes to resolve any issues that emerge from time to time with suppliers.*<sup>506</sup>

Furthermore, Aldi's submission suggests that it had not been involved in the development of the Code. This is so despite the former AFGC head recalling that he had consulted offline with the discounter during the course of negotiations with MSCs. Aldi's submission, however, reads:

*We also observe that the Code is based on the AFGC Code, the drafting of which did not involve ALDI. Accordingly, many of the provisions in the Code suit the business model of the MSCs but are inapplicable or inconsistent with ALDI's business model as a limited line, low cost retailer.*<sup>507</sup>

There also appears to have been a sense that any critique that Aldi constructively offered would not have held much sway given the dominance of the MSCs in the process and also given that there seemed to be rush in getting to an outcome:

*[Aldi] did make comments about it [Treasury's draft] but the comments were so limited because it was rushed through. And also, if you actually look at it from the perspective of definitions it talks about senior buyers. Well, that is not our definition because we have group line directors so the code doesn't even cater for the lines with Aldi. And we wanted liquor in it and it should've been but the others [said], "No, no, no, we don't have time for this, no, no, no, it's not relevant, and push it through."*<sup>508</sup>

Yet despite its strong views on the irrelevance and the attendant disadvantages for it of the Code, Aldi signed up. Why? Again, the answer lies in the politics. Aldi, not unlike the MSCs, appreciated that if 'the industry' did not provide government with a solution to the problems in the sector (and a way to relieve the political pressure), the government would take its own action so as at least to be seen to

<sup>505</sup> Aldi submission to Treasury, FGCC consultation paper 2014, 19 September 2014, p. 1.

<sup>506</sup> Aldi submission to Treasury, FGCC consultation paper 2014, 19 September 2014, p. 1.

<sup>507</sup> Aldi submission to Treasury, FGCC consultation paper 2014, 19 September 2014, p. 1.

<sup>508</sup> Transcript of interview, interviewee that consults to / advises grocery businesses, p. 23.

be addressing the crescendo of grievances, now fully in the public eye and capturing community sympathy. Aldi faced an invidious choice: sign up to what it saw as the Coles-Woolworths code and cop the added compliance cost or refuse to sign up and cop the bad press and potentially a mandatory code. As one interviewee ruefully remarked, for Aldi it was a case of 'damned if you do and damned if you don't'.<sup>509</sup> Given the company's strong cultural preference for staying out of politics and the media spotlight, it is little surprise that it chose the 'damned if you do' option. And from Billson at least, for that, it deserves due credit:

*... they [referring to Aldi] didn't have to [sign up to the Code] but they were excellent, I found dealing with Aldi extremely positive, in fact they were first cab off the rank...<sup>510</sup>*

From a supplier perspective, Aldi really had nothing to lose from signing up to the FGCC. As one experienced supplier consultant told us with more than a touch of wryness:

*..they strive for a good deal, nothing wrong with that, but once you're in they look after you, they're fair, they're honourable ..But when you're expecting to deliver a 3 EBIT and you're delivering – or 3.5 and a half and you're delivering a 5 EBIT as Aldi is, it's roses in the garden... they don't have to be horrible, they can make great margins just by being normal.<sup>511</sup>*

According to a senior representative of the US discounting chain, Costco wasn't asked to participate or consulted by the code negotiators. Exclusion does not appear to have been a matter of any concern to Costco, however. This exercise was, in their view, 'very much a Woolworths/Coles thing'<sup>512</sup> - a reference not only to the fact that the process was being driven by the MSCs but also, echoing Aldi's position, that it was being undertaken as a result of bad behaviour by Coles and Woolworths and that type of behaviour was simply not a part of the Costco culture. As the same representative explained:

*... if we had have been consulted we may have had some input, but I think what we've illustrated to you here today too is that we don't really need that code ... The code basically says you have to obey the law. We will obey the law, and the first thing they will do is break the code... It's not our business, it's their business regulation, not ours.<sup>513</sup>*

Like Aldi, Costco made a submission to the Treasury consultation and like Aldi, it pointed out the ways in which proposed code would conflict with its business model. Costco acknowledged the Government's desire to better regulate supermarket-supplier relations, but stated that, 'it does not

<sup>509</sup> Transcript of interview, interviewee who consults to grocery businesses, pp. 34-5.

<sup>510</sup> Transcript of interview, Bruce Billson, p. 43. In fact the first retailer to sign on to the Code was About Life, a NSW-based wholefoods grocer that has 7 stores in Sydney and 1 in Port Melbourne. About Life signed up on 19 May 2015, Aldi signed on 15 June and both Coles and Woolworths signed up soon after on 1 July 2015 (see ACCC Food and Grocery Code of Conduct website).

<sup>511</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 43.

<sup>512</sup> CC 2008 Report, p. 55.

<sup>513</sup> CC 2008 Report, p. 56.

agree with the proposed regulation in that it attempts to treat very different businesses in the same manner.<sup>514</sup>

Costco made clear that it did not consider itself to be part of the problem when it came to suppliers, ‘primarily because Costco considers that a sustainable relationship with its suppliers is commercially astute’, and attributed the lack of relevance of the Code to its operations to ‘the process by which the draft Code was composed – that is, in close consultation with the two MSCs.’<sup>515</sup>

However, unlike Aldi, Costco stood its ground when it came to the crunch of signing up, stating in its submission that ‘in the Code’s current state, Costco would not volunteer to be bound by it’.<sup>516</sup> Possibly reflecting a greater risk tolerance (in turn possibly reflecting its US origins), the company was not prepared to put its name to an instrument that, in its view, had no relevance to its *modus operandi*.

#### **IV. A bet both ways: Metcash, MGA and the IGAs**

Independent retailers, their representative association (the MGA) and their principal wholesale supplier (Metcash) were also not involved in the roundtable discussions that preceded the Treasury consultation, although again Dawson’s recollection was that he consulted with Metcash representatives separately.

According to Hadler, ‘they were asked to participate and declined.’<sup>517</sup> However the owner of a group of IGA stores believes it was the lack of any such request that in part explains why Metcash have not signed up:

*I know why Metcash didn’t want to sign because Coles and Woolworths set the code up but Metcash actually didn’t have any input into what the design of the code was, so I know that was the biggest issue that they had.*<sup>518</sup>

He went on to say that he thought Metcash’s position was:

*“Don’t come and ask us to sign it after you’ve put it all together because obviously the Code is going to be stacked in the favour of Coles and Woolies for all the mistakes they’ve made ... where Metcash has maybe made three or four mistakes you’ve got these guys have actually made a couple hundred”.*<sup>519</sup>

Whether or not Metcash was invited to provide input to the RSR aside, reasons offered second-hand as to why they apparently remained aloof again vary depending on the source. Hadler says Metcash saw the code initiative as irrelevant to them because they are a wholesaler not a retailer. But he is also somewhat cynical about this position: ‘they play a funny game... the reality is that they source

<sup>514</sup> Costco submission to Treasury, FGCC consultation paper 2014, 11 September 2014, p. 2.

<sup>515</sup> Costco submission to Treasury, FGCC consultation paper 2014, 11 September 2014, p. 2.

<sup>516</sup> Costco submission to Treasury, FGCC consultation paper 2014, 11 September 2014, p. 3.

<sup>517</sup> Transcript of interview, Robert Hadler, p. 24.

<sup>518</sup> Transcript of interview, managing director of an independent supermarket group, p. 46

<sup>519</sup> Transcript of interview, managing director of an independent supermarket group, p. 46.

from suppliers anyway and then they just distribute through the IGA network. And the IGA guys, who are the franchisees, say they don't buy the product. So they try and play both sides.<sup>520</sup>

This view is reinforced by an industry expert who works closely with suppliers and believes that while some of Metcash's activities may not be covered by the Code in its current form, perhaps they should be. In his opinion, the Code should be broad enough that 'if you do business with a retailer in Australia you're protected by the code because the core poor behaviours exist across grocery supermarkets, liquor, DIY, you name it.'<sup>521</sup> The same interviewee expressed disappointment that Metcash and Costco had not signed up, and expressed the view that there was, 'no reason why IGA groups shouldn't be party to this at all'.<sup>522</sup>

Interestingly the owner of one such group, while also attributing Metcash and his own group of IGA stores' decision not to opt in to a lack of business relevance, did entertain the possibility of Metcash and his group signing up to a revised Code:

*Metcash is a different model to Woolies and Coles so it can't be "just sign here" because it's the same Code. But if the Codes are modified to be relevant then I'm not against – in my opinion, if it was good enough – and I'm saying, if that's good enough for [my stores] to work to a code, I think it's perhaps good enough for Metcash to work to a code, whereas I think it would be a more stringent code for the likes of perhaps Coles and Woolies.*<sup>523</sup>

The MGA head is more generous. Metcash did not sign onto the code, in his view, 'because that independent wholesaler model is something very complex' but 'they've committed to acting on a lot of the initiatives within it' in any event.<sup>524</sup> As for independents outside of the Metcash-IGA network, he was even more accommodating as to why these smaller retailers did not sign up and were justified in not doing so: 'it really became kind of an unknown... it could put some real added red tape and cost burden pressure on them.'<sup>525</sup>

Billson's reflections on Metcash's position echo the comments of both Hadler and the MGA's CEO but also paint a picture of an organisation trying to have a bet both ways. The former Minister recollects Metcash's position as being to the effect: ' "oh, we're all really nice and charming and we don't need this [ie to subscribe to the code]" – a position Billson, and many others reject, on account of reports that Metcash was as tough if not even tougher for suppliers to deal with. However, Billson also remembers Metcash's reasons for refusing to sign on as relating to the complexity of their model (the head of MGA's point) and the argument that the regulatory burden, not just on Metcash but and arguably even more so on their retail arm, would put them at a disadvantage to the MSCs. At the same time, Billson distinctly recalls the Metcash MD telling him that the company nevertheless would 'comply with it [the code] in every respect.' The contradiction in this was not lost on Billson:

<sup>520</sup> Transcript of interview, Robert Hadler, p. 24.

<sup>521</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 57.

<sup>522</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 60.

<sup>523</sup> Transcript of interview, CEO of an independent supermarket, p. 23.

<sup>524</sup> Transcript of interview, CEO of Master Grocers' Association (MGA), p. 21.

<sup>525</sup> Transcript of interview, CEO of MGA, p. 23.

*..I said, "So hang on, you just told me it was the cost you were worried about and that's why you weren't going to sign, now you're telling me you're going to mimic full compliance therefore incur those costs that were so traumatising and still not sign." I said, "That's like saying you're playing footy but you're sitting in the third row back. What logic is that?"...*<sup>526</sup>

There may be broader repercussions that flow from Metcash's reticence to sign on. As Dawson recently observed, if Metcash still hasn't signed on by the time the Code is reviewed in 2018 then the option to make the Code mandatory may once more be on the table.<sup>527</sup>

Indeed, it was made clear in response to a recent AFGC survey of suppliers that, 'there is a very strong view that [the] Code should have 'whole of industry' application'. The majority of suppliers surveyed were in favour of Costco, the independents and in particular Metcash, along with on-line grocery retailers, to become signatories.<sup>528</sup>

## **V. Behind the scenes: Billson**

While AFGC and MSC representatives and advisors were busy meeting, consulting and drafting, there was evidently a lot of negotiation taking place behind the scenes and this appeared to escalate when the rubber hit the road and it came time during the Treasury consultation to determine which parties would sign on and which would withstand the pressure to do so. Billson was a key protagonist in these backroom dealings.

With all of the stakeholders, Billson's message was clear: come up with something that works and is politically sale-able, and then I will run with it; but come up short, and I will flick the switch that ignites the cumbersome and heavy-handed regulatory machine. There is no doubt that most of the primary parties involved took the (not so) veiled threat seriously, as reflected in the degree of commitment to and urgency in the process being undertaken by the AFGC and MSC trio. Not content to leave matters to Harper et al in the root and branch competition law review, Billson continued to press the MSCs to come up with a fix for the problems in the supply chain.

However, as Billson readily concedes, there may have been challenges in carrying out the threat to pull the trigger on a mandatory code. Partly that was because it would have flown in the face of the government's red tape cutting agenda and he may have encountered resistance in the party room ('to be absolutely frank with you, and it's probably not a great justification but I'll share it with you as well, we had deregulation targets, now, I've got to tell you.. in this space you could regulate everything up the wazoo and never stop').<sup>529</sup> Partly it was because Billson's personal philosophy and preference favoured a lighter touch:

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<sup>526</sup> Transcript of interview, Bruce Billson, 47.

<sup>527</sup> Transcript of interview, Gary Dawson 2, p. 16.

<sup>528</sup> AFGC, *Annual Food and Grocery Code of Conduct Survey Report*, 2017, p. 20.

<sup>529</sup> Transcript of interview, Bruce Billson, p. 24.

*I'm a gradualist on regulatory interventions, you don't bring a sledge hammer if that's not what's needed. Why? Well, that's intuitively who I am. And secondly there's the bloody red tape accounting process, so I was trying to deliver the best bang for the least amount of regulatory burden bucks knowing that if it didn't work we would then have an evidence base to move to the next level. Now, if you want to check my form on that look what I did with the Franchising Code, we said let's get this – I – my mantra is minimum effective regulation, that's what gets me in a bit – minimum effective regulation. You overreach it's a drag on the economy and we can't afford that, so to live that discipline I had to walk the talk and, so this was about saying to them, "No, no, don't play me on this," they tried it a couple of times, I said, "Don't try me on, I will regulate, I will impose something on you if you can't give something that's adequate so just get that little idea out of your head that is there, call it a threat, whatever you want, but there is going to be something happening and if it's not adequate I will make sure it happens and it might not look like what you want it to look like so you best get yourselves back together."* <sup>530</sup>

Tensions between the appointment of an adjudicator to enforce GSCOP and a deregulatory agenda were felt also in the UK. As one of our interviewees told us, 'introducing [the GCA] at the time it came in, was uncomfortable in some ways for a conservative government that believes in deregulation.'<sup>531</sup> That discomfort is reflected in the fact that the GCA apparatus is reviewable every three years and in the recently completed review, one of the explicit considerations was whether or not it should be replaced by another body, if not removed altogether.<sup>532</sup>

On the disadvantages of regulation, not unexpectedly, Billson and the big business representatives were one. As Hadler explains of the voluntary code approach:

*...this was designed to manage the – close perception gaps and to avoid increased regulation that would result in dead weight cost to industry and unintended consequences for suppliers, without any consumer benefit... I think if it was a heavily prescribed, mandatory code with an industry funded regulator, I think it could result in consumer detriment...It was going to be regulated. It was a question of how it was going to be regulated..<sup>533</sup>*

In getting what needed to be done, Billson evidently saw an ally or a partner in the AFGC and Dawson in particular:

*..I said to a few of the players and particularly with Gary, "Take it as far as you can get it," and I think I said when they handed it to me I think I gave it a six out of 10 or something if I remember correctly ... we'd been closely monitoring it and I was giving a few cues to the players about what I thought would be adequate. They were short on a few of those things. Gary did exceptionally good work there but he took it as far as he could and he – and I'll be*

<sup>530</sup> Transcript of interview, Bruce Billson, p. 26.

<sup>531</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 7.

<sup>532</sup> See further Part 7 below.

<sup>533</sup> Transcript of interview, Robert Hadler, pp. 30-1.

*honest with you, he rang me and he said, "I can't take it any further, I just can't take it any further, we're going to have to pass the parcel." I said, "Okay, well, I'll run with it now." So we exhausted that collegiate collaborative thing and then I got my piece of work which was a little more targeted cajoling with the knowledge that if we couldn't get an adequate outcome I would push and I would count the red tape costs and if I got it wrong, well, too bad, you're going to have to wear it then because you wouldn't work with us on it. So that was how that worked and by acting the way we did the red tape cost counter was a dramatically different piece of work, dramatically, so.<sup>534</sup>*

With the MSCs, Billson may have been a bit more forceful and it is also evident that with these parties, he was dealing over the heads of the corporate affairs negotiators. Referring to the Coles' CEO, Billson recounts:

*You see, John Durkan and I got on pretty well but we had some Bruce and John chats because we'd get to a point where we thought we were there and then it would go back into their machine and it would spit out and I said, "Mate, that's not what we agreed, that's bullshit, that's not what we agreed, you go and have another go." "Oh, but, but," I said, "That is not," sorry, that was a little bit dramatic but that's basically how it went and that was – Woolworths were – they didn't want to be left out but Coles were the ones that were probably most active...<sup>535</sup>*

According to one source, and despite Billson's favourable depiction of Aldi's attitude, he played it no less tough with the discounter. The recollection of this interviewee was that Aldi decided to make a submission to Treasury '...when Billson said, "I'm going to make this mandatory so you'd better sign up"<sup>536</sup>.

As for the NFF, as previously mentioned, politics was very much in play. It was an election year. According to Billson, the NFF had assurances from Labor: 'if you bail ... if you abandon this process and say how unsatisfactory it is ... we will impose a mandatory code' (which was, after all, what the NFF wanted). So the NFF duly jumped ship. But the process had gathered such steam by that stage that the farmer group's withdrawal seems to have constituted little more than a hiccup. And by the time it became apparent that a code would be enacted and it would be voluntary, it would have become obvious to the NFF that its strategy had tanked (and Rudd's failure at the 2013 election meant that Labor's promises could not have been made good in any event). According to Billson, the NFF then came to him saying in effect: "oh, that didn't turn out the way we hoped ...", and from his response it is clear that at that stage Billson was no longer listening:

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<sup>534</sup> Transcript of interview, Bruce Billson, pp. 26-7.

<sup>535</sup> Transcript of interview, Bruce Billson, p. 28.

<sup>536</sup> Transcript of interview, interviewee that consults to / advises grocery businesses, p. 23.

*I said, "Looks like you've cracked a sooky la la and you've got nothing for it, you realise when you throw the toys out of the cot you can't reach them after that so just chuck them to the other end of the cot next time".<sup>537</sup>*

Other primary produce stakeholders were watching from the sidelines and Billson may have been prepared to include them in the process but, amongst some at least, there was a view shared with and perhaps influenced by the NFF that 'they could do better'.<sup>538</sup> They too read the politics wrong. Billson again:

*...there was an awful lot going on there and just to frame it a bit further if I could, the other Codes, the yeah, and the grape growers and the wine makers ... they were pretty convinced that they could do better and so they stayed out as well ... they thought they could do their own thing and then I said, "Oh, okay, good luck with that." And it was ironic because then the horticultural industry, having known of the problems of the Hort Code ... they came very late in the piece and said, "We can't get anything near what you've got, can we have in?" I said, "You just left it too late guys, its five to 12, I've been asking you to get on board." And they said, "Oh, we so want this now, we're never..." so I found that really quite reassuring that the hort industry and the winemakers who were pretty convinced they were on better ground than we were, they saw what I tried to do with this Code, it had far more utility in than people anticipated..<sup>539</sup>*

Billson's strategy of monitor, guide, cajole and where necessary threaten may have worked with most of the major players, but it failed with Metcash. The larger than life small business politician pulled out all the stops to get Metcash over the line. His threats were not confined to heavy regulatory intervention (by way of a mandatory code) should the industry initiative fall short; they extended to bad publicity for Metcash. Billson had been told by suppliers that some of the most 'egregious' treatment was meted out not by the MSCs but by the wholesaler-retailer. When faced with denials from a senior Metcash representative, Billson's response was: "Don't take my word for it, do you want me to get the suppliers talking publicly? I can organise that..."<sup>540</sup> When threats didn't work, he tried reasoning on commercial grounds: "What are you saying, that you don't want to play fair, you want to be able to behave in an unfair way and that's good for your share price? ..."<sup>541</sup> Finally, concessions:

*I gave them longer to transition because they did have a different contractual platform and I thought that was legitimate; and the second thing was I cut them an awful lot of slack with their customer facing businesses, they have a multibillion dollar retail business and I said, "I'm not going to give you a hard time about that, you've got to at least get your wholesale business."<sup>542</sup>*

<sup>537</sup> Transcript of interview, Bruce Billson, pp. 30-1.

<sup>538</sup> Transcript of interview, Bruce Billson, p. 31.

<sup>539</sup> Transcript of interview, Bruce Billson, p. 31.

<sup>540</sup> Transcript of interview, Bruce Billson, pp. 43-47

<sup>541</sup> Transcript of interview, Bruce Billson, pp. 43-47

<sup>542</sup> Transcript of interview, Bruce Billson, pp. 43-47

When both bad cop and good cop failed, Billson was left angry, bewildered even:

*And they still said no and I said, "I just can't believe it," so I did my nana with them and said, "That's just bizarre and if I'm asked I'll say so, so don't expect any polite no comments about your decision, it's a shocker and I'll say it's a shocker and I can't understand the logic to it."*<sup>543</sup>

## VI. Making it official: Treasury

Competition and consumer policy and law-related matters lie within the Treasury portfolio and so it fell to the engine room of government policy-making and administration to take the draft code presented to it by the RSR in November 2013 to the next stage. Treasury has a standard process for dealing with and consulting on these types of regulatory proposals. The process accords with the Treasury's guidelines on code prescription and the requirements of the federal Office of Best Practice Regulation (OBPR) directed at ensuring that 'public policy achieves a desired objective in a cost-effective manner'.<sup>544</sup>

The initial step was to redraft the Roundtable version to ensure it had the requisite degree of formality required for legislative instruments and was consistent not just with the Treasury's but also the ACCC's guidelines for industry codes.<sup>545</sup> It does not appear that, at that stage, any substantive changes were made to the AFGC-MSD draft. The Treasury version then became the basis for consultation. A consultation paper that constituted the government's Early Assessment Regulatory Impact Statement (RIS) was produced, together with a Fact Sheet and Explanatory Statement, and these documents were published with a call for submissions in August 2014.<sup>546</sup> 33 submissions (13 of which were confidential) were received over the five week period that the consultation stayed open and were also published on the Treasury website.<sup>547</sup> Some face to face hearings were held. The submissions were reviewed. Treasury 'took on board all the feedback', liaised with the responsible Minister, Billson, and also negotiated further with the MSCs.<sup>548</sup> A Final RIS was approved by OBPR and published in November 2014.

As the responsible Minister, Billson then sought the approval of the federal Executive Council to have the relevant Regulation made. Approval was forthcoming and the *Competition and Consumer (Industry Codes—Food and Grocery) Regulation 2015* subsequently received the final rubber stamp, that of the Governor-General. The FGCC is contained in Schedule 1 to the Regulation and came into operation on 3 March 2015. It was gazetted on 9 March 2015 and then tabled before both Houses of Parliament. At this stage the Parliament had the option of allowing the prescription of the Code in its

<sup>543</sup> Transcript of interview, Bruce Billson, pp. 43-47.

<sup>544</sup> Australian Government, Department of Prime Minister and Cabinet, Best Practice Regulation, <https://www.dpmc.gov.au/regulation/best-practice-regulation>

<sup>545</sup> Treasury, *Policy guidelines on prescribing industry codes under Part IVB of the Competition and Consumer Act 2010*, 2011; ACCC, *Guidelines for developing effective voluntary industry codes of conduct*, 2011.

<sup>546</sup> Treasury, FGCC consultation paper, 2014.

<sup>547</sup> See <http://www.treasury.gov.au/ConsultationsandReviews/Consultations/2014/Improving-Relationships-Food-Grocery-Sector/Submissions>.

<sup>548</sup> Transcript of interview, Treasury, p. 10.

proposed form, disallowing the prescription of the Code or asking the Minister to make amendments to address any deficiencies identified.

On 21 April 2015 a Senate Economic Legislation Committee, having called for submissions and received 13, met to inquire into the proposed Regulation. Several witnesses were heard, including representatives from Treasury, Queensland Dairyfarmers' Organisation Ltd, Mareeba District Fruit and Vegetable Growers Association Inc and the ACCC. In its report, the Committee acknowledged concerns about the Code in its current form:

*In particular, the committee notes concerns expressed by a number of witnesses regarding the voluntary nature of the Code, the provisions for exceptions to conduct otherwise prohibited under the Code, the potential costs and difficulties raised by the dispute resolution processes provided for by the Code, and the extent of penalties that might be applied in response to breaches of the Code. The committee further notes concerns regarding the coverage of the Code, and in particular concerns that it does not cover alcoholic beverages or issues relating to pricing.<sup>549</sup>*

Notwithstanding these concerns, the Committee found that there was general support for a code of conduct for the industry and concluded that:

*... the Code represents significant progress in improving the standards of business conduct in the food and grocery sector. [It will] achieve its stated purposes, as set out in clause 2 ... [and] the fact that the Code has emerged from an industry-led process [is to be welcomed] ... industry participants are often best placed to develop codes that properly reflect the circumstances of their industry.<sup>550</sup>*

While prescribed codes are typically reviewed every five years in consultation with industry, consumers and business, in this instance an earlier review was determined appropriate. Further consultation had been undertaken prior to the Committee's inquiry and a provision inserted requiring a review be undertaken three years from commencement of the Code.<sup>551</sup> The Committee noted this, stating:

*This review must consider certain matters, including whether the purposes of the Code are being met, levels of compliance with the Code, whether it should be mandatory or voluntary, and whether it should include civil penalty provisions. The committee notes that the review will be able to draw on assessments of the Code's operations and effectiveness. As such, the*

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<sup>549</sup> Senate Economic Legislation Committee Report, Competition and Consumer Act 2010—Competition and Consumer (Industry Codes—Food and Grocery) Regulation 2015, 14 May 2015 [SELC, *FGC Regulation*, 2015], 2.61 at p. 22. With reference to the concerns that the proposed code would not cover alcohol in its definition of groceries it may be noted that in the UK, alcoholic beverages are covered by the CC, GSCOP (The Groceries (Supply Chain Practices) Market Investigation Order 2009, UK, Part 1 s 1.

<sup>550</sup> Explanatory Statement, *Competition and Consumer (Industry Codes—Food and Grocery) Regulation 2015* (Explanatory Statement, FGC Regulation, 2015).

<sup>551</sup> SELC, *FGC Regulation*, 2015, p. 22.

*committee believes that the concerns raised during this inquiry would be best considered as part of the required review.*<sup>552</sup>

The Committee closed with the recommendation that the Regulation stand as promulgated.<sup>553</sup> The FGCC did not come into immediate effect, however. Naturally there were transitional provisions. Any new GSAs entered into after a retailer or wholesaler had agreed to be bound by the Code did have to comply with the requirements of the Code. But for agreements made prior to the retailer or wholesaler agreeing to be bound by the Code, there would be six months for retailers and 18 months for wholesalers (fulfilling Billson's promise to Metcash of a longer transition), to offer to vary existing agreements so as to comply with the Code. If an agreement was not varied, the entire Code would apply to a retailer 12 months, and to a wholesaler 24 months, after they agreed to be bound. The good faith (and freedom of association) obligations however applied immediately upon either party agreeing to be bound.<sup>554</sup>

Before examining further the substance of Treasury's consultation on the proposed code and its outcomes, it is useful to provide some brief background. As this background makes clear, the codification exercise entailed in the FGCC's introduction was by no means some novel or unprecedented experiment from a regulatory perspective, even if this was/is the first voluntary code to be prescribed under the CCA.

### (a) Codification as a way of doing business, both for industry and government

Prescribed codes of conduct were introduced into the CCA framework at the same time as the unconscionability provisions in the Act were extended to small business in 1998.<sup>555</sup> However, non-statutory industry codes had been around for a long time previously, seen by the business sector and often driven by active industry associations as a constructive way of self-regulating in the interests of improving standards, promoting consistency, enhancing reputation and bolstering community confidence, providing for efficient and effective dispute resolution, and warding off more draconian regulatory responses from government.<sup>556</sup> As explained by Treasury:

*... from industry's perspective it's the opportunity to tailor the law to their particular circumstances. And also with the way that codes operate from the purely voluntary ones to the grocery codes, it is potentially less onerous regulation than a full mandatory code, so there's a bit of a benefit there as well. It's just about getting the balance right.*<sup>557</sup>

<sup>552</sup> SELC, *FGC Regulation*, 2015, p. 23.

<sup>553</sup> SELC, *FGC Regulation*, 2015, p. 23.

<sup>554</sup> Explanatory Statement, *FGC Regulation*, 2015.

<sup>555</sup> See s 51AE, *Trade Practices (Industry Codes - Franchising) Regulations 1998* (Cth).

<sup>556</sup> Transcript of interview, Treasury, p.4.

<sup>557</sup> *Policy guidelines on prescribing industry codes under part IVB of the Competition and Consumer Act 2010*, May 2011, Commonwealth of Australia, see in particular pages iv, 1, 2 and 6.

Such code practices had also been part of ACCC business for some time. In the late 1980s the then Trade Practices Commission had conducted a review of self-regulation that was supportive of such schemes as a cost-effective, efficient and unobtrusive alternative to government regulation and providing a set of principles to guide industry in developing their own codes of practice.<sup>558</sup> The initial guide developed by the ACCC in relation to industry codes evolved into a more detailed manual on the appropriate uses, design and implementation of codes of conduct, first published in 1989 and in revised version again in 1996.<sup>559</sup> The ACCC developed a practice of assisting industry, often through their own association, in decision-making about and drafting of such codes, but also encouraged industry bodies to apply for authorisation of such instruments under the CCA where there was potential for anti-competitive effects. According to one interviewee from the ACCC, provision of such assistance is 'standard'; '[it's] an avenue that's available, and it is an avenue that was pursued [with regard to the development of the FGCC].' He went on to say, with regard to any industry seeking the assistance of the ACCC:

*We give them guidance ... on just how or what they should think about in terms of mechanisms to deliver the rigour that they would seek to make the code effective. And it's not uncommon, ... where we'll have some preliminary discussions, we'll explain how the mechanism works in our view and then they will go and consult and work through a process and basically take it offline, develop an industry code of conduct consistent with our best practice guide, and not necessarily come back to us to seek any kind of advice.<sup>560</sup>*

1996 was an important year for codes in two other respects. It was the year in which a major report into the burdens on small business of government regulation was released and a call made for a change in the culture of government so as to reduce compliance requirements and associated paperwork.<sup>561</sup> In the same year a parliamentary inquiry into fair trading was commenced, a substantial theme in which was the imbalance in power between small and large businesses (in the context of franchising and leasing particularly).<sup>562</sup> Small business associations saw the solutions lying both in a strengthening of black letter laws addressing oppressive conduct as well as strengthening codes of conduct - a dual pronged approach. The outcome was the introduction of the *Trade Practices Amendment (Fair Trading) Bill*, a year later, extending protections from unconscionability (previously applicable only to consumers) to small businesses,<sup>563</sup> and establishing a legislative framework for the recognition, governance and enforceability of codes of conduct so as to send the strongest possible message to the Australian business community that:

*... commercial relations between big and small businesses must be treated on a fair and reasonable basis ... [and to] induce behavioural change in commercial practices so that small*

<sup>558</sup> Trade Practices Commission, *Self-Regulation in Australian Industry and the Professions: Report by the Trade Practices Commission*, 1988.

<sup>559</sup> For the most recent guidelines, see ACCC, *Policy guidelines on prescribing industry codes under Part IVB of the Competition and Consumer Act 2010*, July 2011.

<sup>560</sup> Transcript of interview, senior representative of the ACCC, p. 6.

<sup>561</sup> Small Business Deregulation Task Force, *Time for Business*, November 1996.

<sup>562</sup> House of Representatives Standing Committee on Industry, Science and Technology, *Finding the Balance: Towards fair trading in Australia*, May 1997.

<sup>563</sup> See s 51AC, *Trade Practices Amendment (Fair Trading) Bill 1997* (Cth).

*businesses do get a fair go and, where they are treated unfairly, they have available to them a means of redress.*<sup>564</sup>

The introduction of provisions allowing for the creation of statutory industry codes evidently did not signify a desire by the government to see a slew of such codes come into force. Instead, the Coalition government continued to advocate for industry self-regulation which was viewed as providing a more flexible alternative to direct government regulation.<sup>565</sup> Correspondingly the ACCC continued its work in supporting the development and where necessary authorising non-statutory industry codes, although over time such work has become less of a priority and particularly at present given the focus on the new provisions relating to unfair contract terms.<sup>566</sup> The process involved in having a code prescribed, by contrast, was much more formal and in 2010, became the subject of policy guidelines issued by Treasury.<sup>567</sup> The guidelines make it clear that mandating a code of conduct under the CCA is seen by government as a last resort<sup>568</sup> given that, in most instances, the net benefit of effective self-regulation will exceed government intervention. Such intervention will only be used where there is 'a demonstrable problem' that the industry itself or the market cannot overcome.<sup>569</sup>

According to the Treasury guidelines:

*The primary goal of an industry code, from the perspective of the Australian Government, is that it enhances the wellbeing of the Australian people. This might be achieved by reducing complexity that industry participants or consumers are required to deal with, by reducing risks, by ensuring that industry participants are afforded some measure of fairness in their dealing with other industry participants, or by increasing the aggregate output from a particular industry.*

...

*Industry codes are not, as a general proposition, designed to address circumstances in which smaller participants in an industry experience competitive pressures that relate to limited access to economies of scale in purchasing, bargaining or access to markets. If this is the case, there should be compelling evidence to indicate that the problems experienced are so significant that they have effects beyond individual firms or groups of firms within an industry, such that there is a public interest in the prescription of an industry code.*<sup>570</sup>

The formal process for prescribing an industry code is generally started by representations made to government by industry participants in favour of intervention, as indeed was the case with the FGCC. Consideration is then given to the introduction of a prescribed code by way of response and

<sup>564</sup> Australia, House of Representatives, *Hansard*, 30 September 1997: 8546.

<sup>565</sup> Treasury, *Industry Self-Regulation in Consumer Markets, Report prepared by the Taskforce on Industry Self-Regulation*, August 2000.

<sup>566</sup> See <https://www.accc.gov.au/business/business-rights-protections/unfair-contract-terms>.

<sup>567</sup> Treasury, *Policy guidelines on prescribing industry codes under Part IVB of the CCA 2010*, May 2011.

<sup>568</sup> Treasury, *Policy guidelines on prescribing industry codes under Part IVB of the CCA 2010*, May 2011, p. 6.

<sup>569</sup> Treasury, *Policy guidelines on prescribing industry codes under Part IVB of the CCA 2010*, May 2011, p. 2.

<sup>570</sup> Treasury, *Policy guidelines on prescribing industry codes under Part IVB of the CCA 2010*, May, 2011, p. 6.

consultation to that effect undertaken with key stakeholders, including with States and Territories and the ACCC, by the responsible government department. Where the consultation supports this response, a draft RIS is prepared and is to identify the relevant problem or problems giving rise to the need for a code, its objectives, the options for achieving such objectives (including an assessment of each option in terms of costs and benefits for consumers, businesses, government and the community generally – both financial and non-financial), a preliminary conclusion as to which is the preferred option based on that assessment, and a draft implementation strategy. The draft RIS is then released for public comment. Upon completion of the consultation process, a final RIS is issued and presented to the OBPR for approval. The decision as to whether to proceed with a prescribed code then falls to the responsible Minister, having taken the final RIS and the consultation feedback into account. If in favour, the code is submitted to the federal Executive Council for approval. Upon approval, the Governor-General is asked to make regulations to this effect, to which the code itself is a Schedule. The Regulations are laid before both Houses of Parliament, which may request amendments or may disallow the code, albeit that rarely occurs.

Pursuant to this process, there have been five industry codes prescribed as mandatory codes under the CCA to date.<sup>571</sup> The FGCC emerged out of the same process, albeit as the first voluntary code under the legislative framework introduced almost 20 years prior.

### (b) Purposes and provisions

In the broadest terms, the policy objective justifying the FGCC was identified by government as being ‘to improve standards of business conduct in the food and grocery sector, so as to address ‘potential market failures resulting from imbalances between retailers or wholesalers, and suppliers in the allocation of risks in commercial transactions.’<sup>572</sup> It was said to be an initiative ‘in response to concerns raised in the public debate in recent years about the conduct of retailers (in particular, supermarkets) towards their suppliers’ and it was acknowledged that the code’s development had been industry-driven.<sup>573</sup> Government made it clear that the industry’s initiative and response was to be ‘welcomed’ and was ‘considered to represent an important step forward for the industry.’<sup>574</sup>

More specifically, the purposes of the FGCC were said to be:

- *to help to regulate standards of business conduct in the grocery supply chain and to build and sustain trust and cooperation throughout that chain;*
- *to ensure transparency and certainty in commercial transactions in the grocery supply chain and to minimise disputes arising from a lack of certainty in respect of the commercial terms agreed between parties;*

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<sup>571</sup> The Franchising Code of Conduct; Horticulture Code of Conduct; Wheat Port Code of Conduct; Oil Code of Conduct; and the Unit Pricing Code.

<sup>572</sup> Explanatory Statement, FGC Regulation, 2015, p. 4.

<sup>573</sup> Explanatory Statement, FGC Regulation, 2015, introduction.

<sup>574</sup> Explanatory Statement, FGC Regulation, 2015, p. 1.

- *to provide an effective, fair and equitable dispute resolution process for raising and investigating complaints and resolving disputes arising between retailers or wholesalers and suppliers; and*
- *to promote and support good faith in commercial dealings between retailers, wholesalers and suppliers.*<sup>575</sup>

The provisions in the Code directed at fulfilling the stated purposes are summarised and justified in the Explanatory Statement accompanying the code regulations as follows.

Part 1 deals with preliminaries, including a statement of purposes, definitions of terms, explanation of applications and transitional arrangements. In its definitional provisions, the Part makes clear the scope of the code as applying to retailers, being corporations carrying on supermarket business (in turn defined by reference to the business of selling certain grocery products to consumers), wholesalers, being corporations in the business of buying groceries from suppliers for the purpose of selling them to suppliers, and suppliers, being persons in the business of supplying groceries to other persons for retail sale. As is explained in the RIS, the definition of wholesale was added at a relatively late stage in the consultation 'in light of many stakeholders calling for greater coverage of the sector' and possibly still at a stage when Billson and/or the AFGC might have thought that Metcash could still be talked into signing up, or perhaps to leave open the option of it being covered if/when the code was mandated. In its application provisions, Part 1 makes clear that the Code binds a corporation as a retailer or as a wholesaler, if the corporation has agreed by written notice to the ACCC to be so bound, but also that a corporation would be able to withdraw its agreement by the same means – it is in this sense only that the Code is voluntary.

Part 2 sets out minimum obligations for retailers and wholesalers bound by the Code relating to the making of GSAs. The agreements must be in writing and address certain matters, such as requirements for the delivery of groceries and when they may be rejected. The Code does not stipulate minimum terms — it leaves it up to the parties to consider and agree on these matters. The requirement to keep records encompasses documents comprising or forming part of the agreement.

Importantly, this Part also governs unilateral variations and retrospective variations to GSAs. Such variations are not permitted except where the agreement allows them and clearly sets out the circumstances in which they may be made. The Code requires written notice to be given to the supplier of the variation and the basis for it. An additional requirement is that a unilateral or retrospective variation of an agreement must be reasonable in the circumstances. The onus of proof in establishing the matters required for the exception to apply lies with the retailer or wholesaler. As explained further below, suppliers are able to initiate the Part 5 dispute resolution process on the basis of detriment resulting from a unilateral or retrospective variation.

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<sup>575</sup> Explanatory Statement, FGC Regulation, 2015. These purposes are directly reproduced in the FGCC (Clause 2 – Purpose, Competition and Consumer (Industry Codes — Food and Grocery) Regulation 2014, p. 4.

In short, the provisions in Part 2 are said to improve transparency and clarity in commercial transactions within the supply chain by, in effect, encouraging the parties to include upfront provisions in their GSAs about a number of aspects of their relationship.

Part 3 deals with a retailer's conduct towards suppliers and does not apply to wholesalers. It sets minimum standards of conduct in relation to a number of aspects of the relationship between a retailer and a supplier, including payment terms. This is with a view to providing further clarity for businesses and improving standards of conduct in the grocery sector.<sup>576</sup>

Generally speaking, a retailer must pay a supplier in accordance with the terms of the GSA. Certain payments (for example, for wastage or better positioning of groceries) are generally prohibited unless an exception is provided for in the agreement and the payment would be reasonable having regard to certain circumstances. The retailer would have the onus of proving the requirements for the exceptions. Payments for shrinkage would be prohibited under a GSA and a retailer would be prevented from otherwise demanding such payments.

This Part also regulates other aspects of the relationship between a retailer and a supplier, such as delisting products, funding promotions, fresh produce standards and quality specifications, changes to supply chain procedures, business disruption, confidential information, intellectual property rights and allocation of shelf space. By regulating a broad range of circumstances relating to the retailer-supplier relationship, the Code is seen as promoting improved practices in commercial transactions, and improving transparency, whilst allowing sufficient flexibility to the parties.<sup>577</sup>

Part 4 includes a number of more general obligations applicable to corporations bound by the Code. As noted above, these obligations bind retailers and wholesalers in their dealings with suppliers from the time they agree to be bound by the Code. The most important obligation is the overarching duty to act lawfully and in good faith at all times in dealing with suppliers. The meaning of 'good faith' is said to be the same as that at common law and intended to build trust and improve standards of conduct. It does not apply to suppliers as they are not compelled to opt in to the Code, which only provides for retailers and wholesalers to elect to be bound. As the Law Council of Australia's Small to Medium Enterprises (SME) Committee noted in its submission regarding the development of the FGCC:

*The SME understands that the Code is a response to anecdotal evidence of widespread negative commercial behaviours by major grocery retailers towards their suppliers. The SME Committee also understands that there are allegations that such negative commercial behaviours have been made possible by the substantial degree of market power which the major grocery retailers possess. In these circumstances, it seems that the purpose of the Code is to provide protections for suppliers, and not to provide unnecessary protections for the major retailers.*<sup>578</sup>

<sup>576</sup> Part 3 – Conduct generally, *Competition and Consumer (Industry Codes—Food and Grocery) Regulation 2015*.

<sup>577</sup> Clause 2 – Purpose, Explanatory Statement, FGC Regulation, 2015, p. 4.

<sup>578</sup> Law Council of Australia, submission, Treasury, FGCC consultation paper, 2014, 12 September 2014 at [14].

However, the Code provides that when a court is assessing whether a retailer or wholesaler has acted in good faith, it may consider whether or not a supplier has acted in good faith.

Other obligations in this Part protect suppliers' freedom of association and include requirements for the provision of relevant buyers' contact details to suppliers.

Part 5 sets out internal and external dispute resolution processes for suppliers to lodge complaints and seek to have their disputes with retailers and wholesalers resolved. The provisions aim to establish fair and equitable mechanisms for dispute resolution which should promote transparency and accountability.<sup>579</sup>

Under the Code, it is open to suppliers to choose the type of dispute resolution option that best meets their needs. A supplier may make a complaint to a Code Compliance Manager (CCM), a person appointed by the retailer or wholesaler under the Code, and may escalate its concerns to senior management if not satisfied with the outcome. Importantly, the Code sets out a requirement that the CCM is independent of the retailer or wholesaler's buying team. A supplier also has the ability to request that the complaint be elevated directly to senior management for consideration.

A supplier is also able to take a complaint directly to mediation or arbitration (or to the ACCC). The only requirement is that if the complaint has already been raised with the CCM or elevated to senior management, the supplier may not seek mediation or arbitration until such procedures have, or should have, been completed. Importantly, the Code requires a retailer or wholesaler to take part in mediation or arbitration in good faith. According to Treasury:

*It's structured in a way to give the participants maximum choice [as to] what dispute resolution path they'd like to follow. So normally you'd go to internal dispute resolution before you went to external dispute resolution, but I think the grocery code is structured that they can do that, or they can elevate to the senior management through the code compliance manager or they can go straight to mediation and arbitration. So it's maximum flexibility for the participants to make sure that they resolve their dispute as expeditiously as they wish.<sup>580</sup>*

There are some limited exceptions to recourse to this external procedure where the mediator or arbitrator forms the view that the complaint is vexatious, trivial, misconceived or lacking in substance, or the supplier is not acting in good faith.

With respect to disputes relating to unilateral and retrospective variations of a GSA, a supplier's obligation to provide certain details required in order to initiate a dispute will be met by the provision of particulars of detriment to it, even though supplier detriment alone may not be sufficient to constitute a breach of the provisions relating to variations. Further, a complaint of this nature cannot be dismissed

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<sup>579</sup> Explanatory Statement, FGC Regulation, 2015, p. 12.

<sup>580</sup> Transcript of interview, Treasury, p. 15.

as vexatious, trivial, misconceived or lacking substance solely because the only ground raised by a supplier is detriment to it.

The rules of the Institute of Arbitrators and Mediators Australia will apply to mediation and arbitration processes commenced under the Code.

Finally, Part 6 sets out the requirements for retailers and wholesalers to ensure they have appropriate mechanisms in place in order to comply with the Code. It includes obligations for retailers and wholesalers to train their buying team on the requirements of the Code. It requires the retailer or wholesaler's CCM to prepare written reports on complaints twice a year and also sets out obligations about record keeping.

### (c) Getting to 'yes'

In order to understand fully how Treasury and government arrived at the conclusion that the provisions as summarised above were the best way of addressing the stated policy objectives and how they would do so, it is necessary to go back in some detail to Treasury's consultation on the RSR draft of the Code. What emerges from a review of that process and its outcomes is that there was significant concern regarding several key aspects of the approach proposed by the AFGC and MSC alliance from various industry quarters. Yet, on each of these issues of concern, ultimately the views of the alliance prevailed, with the support of Treasury and the Government.

#### *a) What's the problem?*

Adhering to the template for regulatory review of such proposals, Treasury's first task in the regulatory review process was to identify 'the policy problem to be solved'.<sup>581</sup> The logical starting point, albeit more by way of context-setting than anything else, was to note that Australian retail grocery markets are relatively concentrated by international standards and that this gave the large incumbents buyer power.<sup>582</sup> While supermarket size could result in benefits for suppliers, and vigorous competition between supermarkets in benefits for consumers, there was also the prospect of costs in terms of dampened incentives for dynamic efficiencies on the part of suppliers.<sup>583</sup> This, in essence, was identified as the structural issue, explaining rather than justifying the need for a code. It went without saying perhaps that it was not an issue that a code could address. Rather, a code of conduct, as the name suggests, is an instrument concerned with market behaviour as distinct from market structure.

In this connection, the jumping off point was to acknowledge that concerns about supermarket conduct in their negotiations with suppliers had been the subject of public concern and debate for some time, raised as long ago as in submissions to the ACCC Grocery Inquiry.<sup>584</sup> This debate, Treasury recounted, had focussed on differences in bargaining power between suppliers and

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<sup>581</sup> Treasury, FGCC Final Assessment RIS, p. 3.

<sup>582</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 3.

<sup>583</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 4.

<sup>584</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 4-5.

supermarkets (and in some cases between suppliers and wholesalers – a veiled reference to Metcash), and resultant difficulties suppliers may face in negotiating fair (notably, the reference here was to ‘fair’ rather than competitive) terms.<sup>585</sup> There are views, it was noted, that grocery suppliers looking to do business in Australia have relatively limited options besides supermarkets to get their product to market, particularly on a national basis.<sup>586</sup>

Treasury went on to record that there have been ‘anecdotal claims’ that:

*... some suppliers may have little choice but to accept disadvantageous terms for fear of losing contracts, and may similarly be unwilling to complain to the supermarkets, or other bodies to resolve issues or enforce their legal rights during the life of the agreement for fear of retribution.*<sup>587</sup>

Having listed the types of behaviour that had been the subject of such ‘claims’, and noted that some of these had resulted in ACCC litigation (a reference to the unconscionability actions against the MSCs), Treasury neatly summarised the ‘problems’ as having the following three themes:

1. *Poor transparency and clarity in grocery supply agreements – particularly in cases where the agreement is not in writing and does not sufficiently cover basic matters, such as quantity and quality requirements in respect of grocery produce.*
2. *Poor business conduct and behaviour – not engaging in commercial dealing with suppliers in good faith.*
3. *Lack of dispute resolution mechanisms and access to justice – suppliers may be unable to have their complaints heard or addressed.*<sup>588</sup>

The Department concluded that ‘to the extent that these behaviours are present in the grocery sector they may have adverse effects on the efficiency of commercial dealings between retailers and suppliers, which may ultimately result in long term detriment to consumers.’<sup>589</sup> More specifically:

*To the extent that these behaviours are present, they may result in inappropriate levels of risk being shifted on to the suppliers. If these types of retailer behaviours occur unexpectedly or recurringly, they could result in serious detriment to suppliers, particularly smaller ones. This includes: forcing suppliers to bear unnecessary costs; inhibiting the ability of suppliers to plan appropriately for their businesses; increasing variability of cash flow; and imposing additional financing costs. In turn, this would detract from the incentive for suppliers to invest, innovate,*

<sup>585</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 6.

<sup>586</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 4.

<sup>587</sup> ACCC 2008 Grocery Inquiry, p. 326, cited in Treasury, FGCC Final Assessment RIS, 2014, p. 4.

<sup>588</sup> Treasury, FGCC Final Assessment RIS, 2014, pp. 6-7.

<sup>589</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 7.

*expand capacity or develop new product lines. Ultimately, some suppliers may be forced out of business as a consequence.*

*There may also be long term detrimental effects for Australian consumers. Erosion of the supplier base, including deterring suppliers from investing, innovating and expanding, may result in higher long-run prices, limited product range and variety, poorer quality products, less intense competition between suppliers, and potentially fewer new products coming to the market. This outcome would not be in the long term interest of Australian consumers and may reduce the efficiency of the grocery sector.<sup>590</sup>*

Notably, Treasury acknowledged that additional in the public debate had been concerns raised by primary producers that they are offered unsustainably low prices.<sup>591</sup> This framing could be seen as understated given that, as Part 3 of this report makes evident, such concerns had in fact been the preoccupation of many participating in the debate in the years leading up to and continuing throughout the code negotiations. However, such framing was evidently deliberate as Treasury was quick to dispense with any prospect of such matters being the subject of response by way of the FGCC. Rather, these were issues being addressed in the separate policy context of agricultural competitiveness that was then the subject of the Government's Agricultural Competitiveness White Paper. The proposed code, Treasury pointed out, 'does not seek to deal with the issue of the base prices that suppliers receive for their goods'.<sup>592</sup> For reasons that are explained below (see Part 6), for some suppliers, it might have been tempting to stop reading there.

### ***b) Why should government get involved?***

Having identified the problem/s, the second task for Treasury was to explain and justify why government action was needed to address them. A prescribed industry code of conduct may be required to address specific problems and will only be effective if it sets out clear requirements and obligations<sup>593</sup> (as distinct from aims and ideals), Treasury explained. However, and consistently with the policy discourse preceding the introduction of Part IVB into the CCA, it hastened to add:

*The Government is keenly aware that any intervention needs to be beneficial overall, and not impose undue regulatory burden. Retailers should continue to have sufficient flexibility to negotiate good deals with suppliers that ultimately benefit consumers. An outcome that is too prescriptive or restrictive may have the unintended effect of resulting in higher retail prices for consumers. Conversely, allowing too much flexibility may mean that the issues of concern outlined above are not addressed.*

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<sup>590</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 6.

<sup>591</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 6.

<sup>592</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 6.

<sup>593</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 7.

*The intention of any Government action is not to prevent hard bargaining and vigorous competition, but rather to ensure that market distortions do not compound and have a longer-term detrimental impact on consumers or the grocery sector more broadly.*<sup>594</sup>

As the origins of the RSR account in Part 4 of this report reveal, it was in part government compulsion and in part public pressure (the two not being unrelated) that had led ‘the industry’ to develop a response and deliver it to government to formalise as official regulation. Government evidently appreciated the initiative. As Treasury noted in concluding this aspect of the RIS:

*The Government also wishes to encourage industry-led responses to resolving issues in different sectors where this is feasible. Allowing industry to lead the response to problems in a market can have several benefits, as outlined in the guidelines for developing industry codes of conduct. In particular, prescribing an ‘opt-in’ industry code reinforces that the Code has industry buy-in and is not overly prescriptive or burdensome. An effective code would codify good practice, provide greater transparency between affected parties, and provide more dependable commercial relationships moving forward.*<sup>595</sup>

### ***c) So what are the options?***

In the ensuing two sections of the RIS Treasury mapped the costs and benefits of the three options that it had identified as ‘alternative courses of action’ for tackling the problem at hand:

**Option 1:** *Status quo* — *Involves maintaining the ‘status quo’ and relying upon existing laws, regulations and codes. This option would not preclude a code of conduct being implemented by the industry outside of the CCA.*

**Option 2:** *Opt-in, prescribed code* — *Involves prescribing a Grocery Code, whereby a retailer or wholesaler chooses whether or not to be bound by the Code. Retailers and wholesalers that agree to be bound by the Code would then be legally required to comply with it.*

**Option 3:** *Mandatory prescribed code* — *Involves prescribing a mandatory Grocery Code, whereby a retailer or wholesaler (as defined in the Code itself) would be legally bound by the Code.*<sup>596</sup>

#### ***i. Option 1: do nothing***

In the highly charged environment leading up to the FGCC’s promulgation, it is hard to imagine for whom exactly this first, in effect, ‘do nothing’, option might have been acceptable. But in the setting of a liberal government with a vigorous deregulatory-minimal intervention agenda, it was a ‘course of action’ (or inaction, rather) that at least had to be on the table.

<sup>594</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 7.

<sup>595</sup> Treasury, FGCC Final Assessment RIS, 2014, pp. 7-8.

<sup>596</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 9.

Treasury noted that there were other codes and laws that touched on the issues that were the subject of concern. But, as far as the other codes (the PGCC and the HCC) were concerned, the feedback was 'mixed':

*... the Horticulture Code lacks sufficient transparency around contracts and the prices received for goods; and it has failed to deal effectively with disclosure about the method of sales engagement. ... There are also many exemptions to this Code. Importantly, it is obvious that there has been insufficient resourcing provided to the ACCC to police and enforce the Horticulture Code. This has contributed to the lack of successfully prosecuted outcomes. As a result, people are unwilling to bring complaints forward, as they fear that they may lose their contract or be 'punished' in some other way.<sup>597</sup>*

Of the PGCC, Treasury observed (arguably somewhat understatedly given that the PGCC had been disabled for at least 3 years) that it:

*... is not widely recognised or understood in the industry, its terms are unenforceable and its voluntary nature allows participants to opt in and out at will.<sup>598</sup>*

While still live, it is certainly true to say that the HCC has had a chequered history. This code was introduced by the Howard government in 2007 following grower concerns over a number of years about the need to improve commercial transparency in fresh fruit and vegetable wholesale markets. At the time, growers and wholesalers could not agree on a voluntary code, so the government agreed to prescribe a mandatory code of conduct under the CCA. A grower we interviewed expressed doubts that such a Code could be truly effective, given the process through which it was developed:

*So what happened was a team of growers were put together for developing the current code. And they were effectively the people that sat on that management group were CEOs of peak industry bodies in horticulture predominantly. And not to speak ill of them but they don't understand the problem. They didn't understand the problem. They don't have the skin in the game, they don't have an invested interest where I – the growers understand it and have skin in the game.<sup>599</sup>*

The HCC applies to all growers and traders of horticulture produce, but not to parties that purchase horticulture produce for retail, export or processing. In basic terms, it is intended to regulate trade in horticulture produce between growers and traders to ensure transparency and clarity of transactions; and to provide a fair and equitable procedure for dispute resolution.

In the ACCC Grocery Inquiry, a number of recommendations were made with a view to improving the operation and effectiveness of the HCC. Like many other aspects of that inquiry's findings and proposals, the HCC-related recommendations were met with strong and contrasting views within the

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<sup>597</sup> Tasmanian Farmers and Graziers Association submission, Treasury, FGCC consultation paper, 2014, September 2014, p. 6.

<sup>598</sup> AMWU submission, Treasury, FGCC consultation paper, 2014, September 2014.

<sup>599</sup> Transcript of interview, former primary produce supplier to the MSCs, p. 20.

industry. The then Minister for Agriculture subsequently appointed the HCC Committee to consider the implications of implementing the ACCC's recommendations. The committee undertook extensive consultation with industry in the preparation of its report, which the Rudd Government released in November 2009. In its report, the committee noted that business practices of the horticulture industry vary widely and that the implementation of the recommendations was expected to standardise practices throughout the industry. The committee predicted that this could be met with initial resistance, but it believed the industry would benefit from improved efficiencies and transparency in the long run.

In June 2015, Billson and Joyce launched a further independent review of the beleaguered HCC. This review provided a damning assessment of the effectiveness of the Code since its introduction in 2007, an assessment echoed in our interviews: 'I think it's fairly safe to say there's a fair bit of cynicism about the Horticulture Code and its effectiveness'.<sup>600</sup> Most transactions were found to be based on contracts and trading terms that had come into force before the Code was enacted and therefore fell outside the scope of the HCC. As an ACCC member observed when asked his thoughts on the Code's effectiveness, this is not entirely surprising:

*The framework of the code and its application were revealed about a year before the code took effect, which enabled those that it was intended to regulate to seek some good advice on how to avoid the application of the code and by doing so there was a flurry of activity by wholesalers, fresh fruit and vegetable wholesalers at the time, to sign up their suppliers to long-term contracts and thereby avoid the application of the codes, because they're a grandfather provision.*<sup>601</sup>

The review found fear of retaliation meant that few growers were prepared to pursue disputes under the HCC, and that the separation of market traders into agents or merchants had only served to create a hybrid system that continued to pass market risk to growers.<sup>602</sup> One interviewee was sympathetic to the challenges faced in the sector in this regard, noting that poor communication and, in some cases, a low level of education makes this a very complex issue. However he went on to say that the existing dispute resolution process meant 'something will fail' unless the right support is provided, and that 'the code hasn't got that type of support built into it'.<sup>603</sup>

The review also noted that there had been significant changes in the sector since 2007, with larger specialised traders entering the market and an increased concentration of trading in the Sydney and Melbourne produce markets.<sup>604</sup> The current Code sunset on 30 March 2017.

The Government published its response to the recommendations of the independent review in early 2017. While the Government did not deem it necessary to remove the distinction between agent and

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<sup>600</sup> Transcript of interview, senior representative of a dairy industry association, p.36.

<sup>601</sup> Transcript of interview, senior representative of the ACCC, p. 50.

<sup>602</sup> Mark Napper and Alan Wein, *Issues Paper: Review of the Horticulture Code of Conduct*, pp. 24-6, 36-40.

<sup>603</sup> Transcript of interview, Robert Gaussen, p. 46.

<sup>604</sup> Mark Napper and Alan Wein, *Issues Paper: Review of the Horticulture Code of Conduct*, p. 23.

merchant,<sup>605</sup> it did accept the recommendation that the current exemption for contracts entered into prior to 15 December 2006 be removed. Instead a transitional period similar to that of the FGCC was proposed. Where existing arrangements are not brought into line with the Code within 12 months, all transactions between growers and traders will be captured by the HCC.<sup>606</sup>

The Government also recognised that the informal nature of transactions in the industry meant that, at times, these transactions were occurring without the protection of a formal signed agreement. The Government therefore proposed to amend the Code, 'to allow for a greater range of options for acceptance of horticulture produce agreements'.<sup>607</sup> In an attempt to ensure all growers' transactions with retailers are covered by a code, the reviewers recommended that where a retailer was not a signatory to the FGCC their transactions with growers automatically be regulated by the HCC.<sup>608</sup> The Government did not determine this appropriate, in part because of the different ways the two codes had come into being - a position that presumably the MSCs would support. As one interviewee reported when asked about his involvement during the development of the HCC, 'Coles and Woolies said, whoa, that's got nothing to do with us, which in fairness to them it didn't, and so they got severed out and went down their own path.'<sup>609</sup> However the Government has said that the interaction between the two codes could be considered further when the FGCC came up for review in 2018 (and the terms of reference for that review reflect as much).<sup>610</sup>

With regard to dispute resolution the Government reported that the review had found 'that the Code's dispute resolution mechanism is irrelevant, inappropriate and largely not adopted by parties in the horticulture sector.'<sup>611</sup> However it did not support the review's call for the Horticulture Mediation Adviser (HMA) to be phased out, instead stating that the HMA role would be reviewed.<sup>612</sup> Likewise the Government did not support calls for horticultural produce assessors to be registered with the ACCC or the SBF E Ombudsman, who in turn the review proposed would act as 'non-determinative conciliators' between parties in dispute. The Government made clear that this was not the role of these agencies, and that there may also be legislative constraints on such an approach.<sup>613</sup>

The Government also stated in its response that civil penalty provisions will be introduced for breaches of provisions of the HCC, 'to enhance the enforcement tools available to the ACCC by allowing it to take rapid action when breaches of the Code do occur.'<sup>614</sup> Other proposed amendments include the annexing of a standard produce agreement to the HCC<sup>615</sup> and the introduction of an obligation to act in good faith for all parties, consistent with the approach taken in the FGCC.<sup>616</sup>

<sup>605</sup> Australian Government response to the Independent Review of the Horticulture Code of Conduct, p. 2.

<sup>606</sup> Australian Government response to the Independent Review of the Horticulture Code of Conduct, p. 9.

<sup>607</sup> Australian Government response to the Independent Review of the Horticulture Code of Conduct, p. 7.

<sup>608</sup> Mark Napper and Alan Wein, *Independent Review of the Horticulture Code of Conduct: Final Report*, November 2015.

<sup>609</sup> Transcript of interview, Robert Gaussen p. 45.

<sup>610</sup> Australian Government response to the Independent Review of the Horticulture Code of Conduct, p. 10. See further Part 7 of this report.

<sup>611</sup> Australian Government response to the Independent Review of the Horticulture Code of Conduct, p. 14.

<sup>612</sup> Australian Government response to the Independent Review of the Horticulture Code of Conduct, p. 13.

<sup>613</sup> Australian Government response to the Independent Review of the Horticulture Code of Conduct, p. 14.

<sup>614</sup> Australian Government response to the Independent Review of the Horticulture Code of Conduct, p. 15.

<sup>615</sup> Australian Government response to the Independent Review of the Horticulture Code of Conduct, p. 3.

<sup>616</sup> Australian Government response to the Independent Review of the Horticulture Code of Conduct, p. 4.

A new Code was subsequently drafted and came into effect on 1 April 2017.<sup>617</sup> Key changes to the Code, in accordance with the findings of the Review include: after the expiry of a 12-month transition period for parties with existing written agreements, all agreements must comply with the current Code. This includes agreements entered into before 15 December 2006, which had not been covered by the earlier code. There are also new, stiffer penalties for non-compliance and increased auditing powers for the ACCC.<sup>618</sup>

Reflecting perhaps the issues with these existing codes, some submissions in Treasury's consultation on the FGCC called for that code and the HCC to be combined into a single whole of supply chain instrument.<sup>619</sup> Others suggested that the PGCC be revamped:

*... the NFF believes that suppliers may be better served by reviewing, amending and significantly revamping the Produce and Grocery Industry Code to cover retailer supply agreement – terms of trade.*<sup>620</sup>

The ADF sought a broader-ranging code, reasoning that their industry 'must be viewed as an integrated supply chain', and as a consequence it was desirable that there be a code to 'cover the whole of the supply chain in order to facilitate more complete application of [its] provisions.'<sup>621</sup>

Apart than noting that there were some for and some against such propositions, the RIS did not dwell on these proposals. As far as a broader instrument was concerned, and as Billson had explained to the NFF with his customary eloquence after the farmer group pulled out of the RSR, that boat had effectively sailed. It is also unlikely to re-emerge as a serious contention in the 2018 review of the FGCC given that there is now a new HCC.

However, in an interesting parallel to the Australian debate, it is perhaps notable that in the UK there have been calls for the GCA's remit to be extended to encompass indirect suppliers to the designated grocery retailers. This is an apparent reflection of the positive impact of the GCA to date in overseeing the application of the GSCOP to direct supply relationships. As Tacon herself ruefully observed in her interview with us, there has been growing 'frustration' associated with the restricted nature of her remit. Many had believed that she 'would be the fairy godmother to the food chain' and as she has 'only been working in one part of the food chain they're all saying, "could she please come and wave her wand over here."<sup>622</sup> In a statutory review of the GCA launched in 2016 (to be reported on at some stage in 2017), the responsible Minister explained:

*The GCA monitors and enforces the Code. The remit of the GCA – or the extent to which its powers apply in the groceries supply chain – is limited to the carrying out of this purpose. This*

<sup>617</sup> Australian Government Department of Agriculture and Water Resources website, Horticulture Code of Conduct, <http://www.agriculture.gov.au/ag-farm-food/hort-policy/code-of-conduct>

<sup>618</sup> Explanatory Statement, *Competition and Consumer Act 2010 Competition and Consumer (Industry Codes—Horticulture) Regulations 2017*.

<sup>619</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 11.

<sup>620</sup> NFF submission, Treasury, FGCC consultation paper, 2014, p. 8.

<sup>621</sup> ADF submission, Treasury, FGCC consultation paper, 2014, p. 10.

<sup>622</sup> Transcript of interview, Christine Tacon, p. 5.

*means that the GCA's remit applies to the grocery retailers subject to the Code and their direct suppliers only. It does not apply elsewhere in the groceries supply chain: for example, it does not apply to businesses which supply these retailers through a third party (referred to as "indirect suppliers").*

*A number of these indirect suppliers and their representatives have argued that the limitation in the GCA's remit is unfair. They argue that they are at least as vulnerable as direct suppliers to the practices referred to above, if not more so, but have no regulatory protection. These points received particular attention when a global over-supply of milk exposed problems in the dairy industry – and which brought greater attention to current issues across the whole farming and primary production sector.<sup>623</sup>*

In response to these concerns the statutory review has included a 'call for evidence' seeking the views of a range of stakeholders on how the grocery supply chain is functioning and whether there is a need for further government intervention by way of extension of the GCA remit or by other means.<sup>624</sup>

As far as the economy-wide provisions of the CCA, as well as common law and intellectual property (IP) laws were concerned, and with the exception of Aldi's stance on existing IP protections (referred to below), the view was that they were insufficient or ineffective in targeting the specific issues at which the FGCC would be directed.<sup>625</sup> In the case of the unconscionability provisions there was also a preference for further assessing their effectiveness after the resolution of the ACCC's then current litigation against Coles.<sup>626</sup> Reflecting the centrality of private brands to its business model, Aldi contended that IP laws were sufficient and expressed concern that the proposed Code might further burden Aldi in this regard:

*There are already requirements at law, both under statute and at common law, to recognise the intellectual property rights of a party. If a supplier considers that a retailer has breached its intellectual property, then it could take legal action to protect that intellectual property.*

*ALDI is concerned that the obligation to "respect" the intellectual property rights of suppliers in clause 21(1) of the Code is vague and may require ALDI to go above and beyond the requirements of the law in recognising the intellectual property rights of suppliers, particularly when combined with the effect of the proposed dispute resolution procedures which would easily allow suppliers to make such allegations.<sup>627</sup>*

<sup>623</sup> Department of Business, Energy and Industrial Strategy, *Groceries Code Adjudicator Review: Part 2, Call for evidence on the case for extending the Groceries Code Adjudicator's remit in the UK groceries supply chain*, October 2016.

<sup>624</sup> Department of Business, Energy and Industrial Strategy, *Grocery Code Adjudicator Review Part 1: Statutory review of the Grocery Code Adjudicator*, October 2016, p. 13.

<sup>625</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 10.

<sup>626</sup> Law Council of Australia SME Committee submission, Treasury, FGCC consultation paper, 2014, September 2014, p. 8.

<sup>627</sup> Aldi submission, Treasury, FGCC consultation paper, 2014, September 2014, pp. 5-6.

Notably, the question as to whether IP protection in respect of private labels was an issue considered, in the UK, by the CC in its 2008 report.<sup>628</sup> The CC did not accept that there was sufficient evidence to suggest this was an issue that warranted inclusion in the proposed new Code, and in any event, was satisfied that it was a matter that would be dealt with by laws on passing off.<sup>629</sup>

It was also acknowledged by Treasury that some retailers had already taken their own action in response to the concerns with which the FGCC was to deal. The Coles Supplier Charter, presided over by Jeff Kennett (referred to in Part 4 above), was cited as an example.<sup>630</sup> But self-evidently perhaps, such measures were not regarded as likely to be adequate and given the degree of angst about 'industry practice', some 'regulatory intervention' was seen as required.<sup>631</sup> Indeed as one MSC representative conceded in his interview with us, the company had an internal code of conduct but 'the genesis of the need for a [statutory] code [was] a public concern about whether or not suppliers were being treated fairly and appropriately' and it was in response to this that 'the role of government kicks in'; for this purpose industry codes [would prove to be ineffective in placating the public's expectations].<sup>632</sup>

## ii. Option 2: do what the Roundtable proposes

The second, RSR-proposed and government-recommended, option was a voluntary prescribed code. As is apparent from pros and cons discussion in relation to this option in the RIS, the benefits were seen as far outweighing the costs and in certain respects this section of the document reads as essentially the case for the Roundtable's proposal. The following benefits were identified and then each elucidated upon:

- creating a spirit of compliance with the code;
- creating transparency and certainty in commercial transactions;
- creating trust and cooperation during commercial dealings;
- higher likelihood of compliance because of the audit and enforcement powers of the ACCC.<sup>633</sup>

Notably, with the exception of the first cited, the other benefits would flow equally from a mandatory code, assuming the provisions would be largely the same (albeit possibly less flexible) and the only key difference would be that application was comprehensive and compulsory. If this analysis is correct, then it would appear that the most significant benefit of this option over the mandatory option was that there would be 'buy in' from the signatories.

<sup>628</sup> See Section 9.71-9.81, Competition issues in the groceries supply chain in 'Competition Commission, 'The supply of groceries in the UK market investigation', 30 April 2008, p. 171.

<sup>629</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, pp. 43-44; CC, 'The supply of groceries in the UK market investigation', 30 April 2008, p. 171.

<sup>630</sup> Coles supplier portal <https://www.supplierportal.coles.com.au/csp/wps/portal/web/ColesSupplierCharter>

<sup>631</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 11.

<sup>632</sup> Transcript of interview, MSC representative, p. 13.

<sup>633</sup> Treasury, FGCC Final Assessment RIS, 2014, pp. 21-23.

Another, more blunt, way of putting this is that the MSCs (if not the AFGC also) would support the voluntary ‘course of action’; they would oppose, and vehemently, the mandatory one. This position was not expressed in quite this way in the submission put by the RSR to the consultation. The softer but still direct and unambiguous position was there stated in essentially the following terms: because we are committed to a voluntary code, we do not support a mandatory code and if the government wants to see others bound by a code, then it is for government to persuade them to sign up voluntarily. As highlighted already, Billson certainly exercised his ardent powers of persuasion in this regard, but was only partly successful (with Aldi, not so Costco and Metcash). Coles and Woolworths may have gone further on the point in their own submissions but regrettably, such submissions were marked and kept confidential. It is hard to imagine what might have justified confidentiality in this context – political / public relations sensitivity possibly, as distinct from commercial necessity? The AFGC SME Forum made a public submission but it was brief – a page and a half – and mostly by way of affirmation of the approach it had negotiated through the RSR, although it did add that ‘*eventually* [it] would be keen for [the code] to be extended to the broader industry by additional retailers choosing to do business within the framework of the Code as signatories’<sup>634</sup> (emphasis added).

Treasury also remarked on ‘other benefits’ associated with the voluntary option, at least for the signatories, pointing out that for these retailers there would be a substantial public relations boost in submitting themselves to the regulation:

*The Grocery Code may also have commercial benefits for retailers and wholesalers that opt-in with respect to their corporate goodwill, and public relations, with positive coverage in media enhancing their public image. Retailers and wholesalers may be able to leverage their participation in the Code to better promote themselves as good corporate citizens and derive a competitive advantage over others that are not signatories to the Grocery Code.*<sup>635</sup>

In summarising the submissions that supported the voluntary option, Treasury gave prominence to the RSR submission. Other stakeholder submissions, said to include submissions from ‘supplier groups’, were noted as having recognised the voluntary code as a ‘worthwhile step’, despite otherwise supporting a mandatory code. This quote may have been drawn from a confidential submission. The only public submission that contains these words was from the NFF and, read in context, it is evident that the national farmers group strongly retained the view that a voluntary code was inadequate:

*The NFF does not believe the proposed Code is a sufficient solution to the problems identified in Part A, although it recognises the added formality and transparency in negotiating trading terms and documenting these in Supply Agreements as a worthwhile step forward and should go some way towards assisting in compliance.*<sup>636</sup>

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<sup>634</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 1.

<sup>635</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 23.

<sup>636</sup> NFF submission, Treasury, FGCC consultation paper, 2014, September 2014, p. 7.

Yet others were recorded as having pointed out that whatever its status, the drafting of the code had not been in consultation with them, its concern was not with their behaviour, and was so irrelevant to their business models that it really should not apply to them – essentially the Aldi/CostCo position.<sup>637</sup> But there were others who too were critical of what they saw as their exclusion from the process. According to the Australian Chamber of Fruit and Vegetables Industries:

*There was a lack of consultation regarding the introduction of the Code and The Australian Chamber of Fruit and Vegetable Industries Limited, as the peak industry body representing the Market wholesalers had no opportunity to propose a voluntary code (as is currently the situation with the major retail chains); and no final say as to whether the code was workable or acceptable to those who were to be regulated by it.*<sup>638</sup>

In response to the latter, Treasury observed that as the proposed code was an opt-in instrument, 'it is currently best suited to those that have currently indicated an intention to be bound by the code.'<sup>639</sup> In other words, this is a code by and for the MSCs. Accepting this position, the views of others were perhaps less relevant.

In relation to costs associated with option 2, the RIS identified a range of largely financial compliance-related 'burdens' associated with extra paperwork, training, monitoring and dispute resolution. There was an effort to quantify estimates of these in an attachment to the document. According to Treasury the 'best practice requirements' for creating an RIS include estimating compliance costs and it acknowledges that the making of such estimates involves making considerable assumptions:

*So a lot of assumptions [had to be made] about how much time would it take, how many staff members to do something required under the code and that incorporated information that we had about the major retailers and so adjusting that for what it might be for a smaller retailer.*<sup>640</sup>

Such assumptions were:

*... informed by consultations that we'd had with the major retailers. ... about how much time it might take to do certain things under the code and then some assumptions to allow for different types of business models and then we just put that out for public consultation to see if other people wanted to challenge those assumptions and say, no it won't take four hours, it will take six hours or and then revise the estimates for the final decision.*<sup>641</sup>

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<sup>637</sup> Note the similar stance taken by Aldi and Lidl in the UK. As recounted by Noble of the British Brands Group, '...some retailers are saying "why am I being hit with this cost of regulation – the Icelands of this world – when actually it's Tesco and ASDA that are causing the problem". I think it's the same with Aldi and Lidl; our relationships with our suppliers is very straightforward, yes, we negotiate, we get the best deal we have, but then the deal is the deal and we don't go back on it, so why are we getting all of this grief just because the big guys have been misbehaving? So that, I think, has been quite prevalent in the dialogue for the last three, four years.'" Transcript of interview, John Noble, British Brands Group, p. 36.

<sup>638</sup> Australian Chamber of Fruit and Vegetable Industries submission, Treasury, FGCC consultation paper 2014, September 2014, p. 2.

<sup>639</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 24.

<sup>640</sup> Transcript of interview, Treasury, p. 11.

<sup>641</sup> Transcript of interview, Treasury, p. 12.

It would seem, however, that despite reflecting industry input, these estimates may have fallen short. According to one major retailer, 'the cost of implementing the code has been significant. It would certainly exceed the significant multiple that the government estimated'.<sup>642</sup>

Interestingly the cost considerations appear limited to those borne by business, it is a 'business regulatory compliance cost estimate'.<sup>643</sup> According to Treasury, the potential burden on the regulator and its budget are not directly factored in. Rather, Treasury:

*... would in the process of developing [the code] talk to the ACCC about [whether] a certain process was going to be unduly burdensome to regulate or not – but this doesn't feed into the formal cost calculations because those calculations are based on the impact on the business, not the regulator.*<sup>644</sup>

More substantively, the most obvious downside of a voluntary code was highlighted, namely that initial signatories could decide to opt-out at any stage. If this was to occur though, the mandatory option could be adopted or, as Treasury put it, that was something government 'could consider'.<sup>645</sup> Yet, as recorded already in this report, from a commercial-political perspective, opting out, according to MSC and other interviewees, was a highly improbable scenario.

In setting out the benefits of the voluntary option, the RIS also dealt with a range of aspects of the proposed code that had loomed large in the consultation, namely:

- the extent to which there was flexibility in the way in which conduct obligations were expressed and imposed;
- the need for an overarching good faith obligation and whether it should apply to suppliers also, and not just retailers and wholesalers;
- the structure and some of the terms of the proposed dispute resolution processes; and
- whether there should be pecuniary penalties for code breaches.

On each of these matters, submissions made both in the Treasury consultation and subsequent Senate inquiry, as well as the views expressed in our interviews and the resolution reached on issue, are outlined below.

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<sup>642</sup> Transcript of interview, MSC representative, p. 17.

<sup>643</sup> Transcript of interview, Treasury, p. 13.

<sup>644</sup> Transcript of interview, Treasury, p. 13.

<sup>645</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 25.

i. FLEXIBILITY

According to the RIS, the aim was to create a code that was prescriptive enough to limit ‘undesirable retailer behaviour’, yet flexible enough ‘to support mutually beneficial supply agreements’,<sup>646</sup> thereby ensuring the best deals for consumers:<sup>647</sup>

*The intention of any Government action is not to prevent hard bargaining and vigorous competition, but rather, to ensure that market distortions do not compound and have a longer-term detrimental impact on consumers or the grocery sector more broadly.*<sup>648</sup>

With regard to commercial flexibility, the ‘for’ argument primarily relied on by Treasury echoed the RSR position that the exemptions in the proposed code struck the right balance between ‘flexibility and safeguards’. Indeed, according to the Roundtable:

*Any failure to allow for such limited flexibility would, in the RSR’s collective view, create a real possibility of perverse or unintended outcomes.*<sup>649</sup> (Such outcomes were not identified or elucidated upon).

This was a position that Treasury saw as supported by the NFF and Business SA, albeit on the condition that retailers were obliged to act in good faith. The NFF in fact had argued that:

*Exemptions do reduce the effectiveness of a Code of conduct because in an ideal world they would not be there, however such allowances reflect commercial reality and should be used sparingly. But, they amount to a variation from the (original) terms of trade and this generally has relatively greater commercial consequences for suppliers than retailers.*<sup>650</sup>

For its part, Business SA had emphasised the need to limit the potential for harm:

*Business SA acknowledges the code needs to allow for commercial flexibility but if it is genuinely trying to reduce instances of supermarkets using power to unreasonably impact suppliers, it needs to ensure it puts an appropriate onus back on supermarkets to act in good faith.*<sup>651</sup>

Treasury certainly acknowledged that there was opposition to the RSR view: ‘several submitters, including Growcom, New Zealand Food & Grocery Council, Australian Manufacturing Workers Union, and Australian Dairy Farmers, raised concerns that the scope for retailers to avoid the key restrictions in the code was too broad.’<sup>652</sup> In the words of some of these opponents:

<sup>646</sup> Treasury, FGCC consultation paper, 2014, p. 1.

<sup>647</sup> Treasury, FGCC consultation paper, 2014, p. 7.

<sup>648</sup> Treasury, FGCC consultation paper, 2014, p. 7.

<sup>649</sup> RSR submission, Treasury, FGCC consultation paper, 2014.

<sup>650</sup> NFF submission, Treasury, FGCC consultation paper, 2014, p. 13.

<sup>651</sup> Business SA submission, Treasury, FGCC consultation paper 2014, 12 September 2014, p. 4.

<sup>652</sup> ES FGC Regulation 2015, p. 15.

*It is of interest that many of the protections in the draft Code can be overridden if the 'relevant grocery supply agreement provides' otherwise. These and similar clauses would seem to undermine the intent of the protections.*<sup>653</sup> (New Zealand Food & Grocery Council)

*... the ongoing imbalance of power within the retailer-supplier relationship leaves open the possibility that suppliers will simply be forced into agreeing to broad exemptions at the negotiation stage, rendering them ultimately no better off.*<sup>654</sup> (Australian Manufacturing Workers Union (AMWU))

As far as Treasury was concerned, however, changes had already been made to the proposed FGCC in an attempt to address these concerns, particularly with regard to clauses permitting unilateral and retrospective variations. The intention behind such changes was to strengthen protections for suppliers while permitting adequate commercial flexibility for retailers and wholesalers and Treasury was satisfied that the right balance had been struck in that regard.

In the minds of some suppliers at least, these amendments evidently were not sufficient. Concerns regarding the acceptable level of flexibility were examined by the Senate Inquiry into the proposed Code. Treasury told the Committee that a voluntary code was preferable to a mandatory one because 'in some respects' it 'provided greater flexibility':

*In particular, this code provides that retailers must offer to vary agreements to suppliers to bring them into line with the code and allow suppliers to seek binding arbitration for disputes by an independent third party. Were the code to be mandatory rather than voluntary, such provisions may be considered to be an acquisition of property, which the Constitution would then require to be done on 'just terms'.*<sup>655</sup>

However the Senate Committee noted that the Law Council of Australia SME Committee rejected the suggestion that exceptions concerning retrospective and unilateral variations in GSAs were necessary to protect commercial flexibility. Rather, the SME Committee argued in its submission that there should be no exceptions.<sup>656</sup>

This was a view supported by the Office of the NSW Small Business Commissioner<sup>657</sup> and the Mareeba District Fruit and Vegetable Growers Association Inc.<sup>658</sup> Further, the ADF suggested that the many exceptions contained in the proposed voluntary Code, 'imply a greater emphasis on commercial flexibility than ensuring fair trading'.<sup>659</sup>

<sup>653</sup> New Zealand Food and Grocery Council submission, Treasury, FGCC consultation paper, 2014, 12 September 2014, p. 2.

<sup>654</sup> AMWU submission, Treasury, FGCC consultation paper, 2014, September 2014.

<sup>655</sup> Ben Dolman, Acting General Manager, Treasury, Proof Committee Hansard, 21 April 2015, p. 25.

<sup>656</sup> Law Council of Australia, submission 3, Treasury, FGCC consultation paper, 2014, p. 5.

<sup>657</sup> Office of the NSW Small Business Commissioner submission 8, Treasury, FGCC consultation paper, 2014, p. 2.

<sup>658</sup> Joe Moro, President, Mareeba District Fruit and Vegetable Growers Association Inc., Proof Committee Hansard, 21 April 2015, p. 1.

<sup>659</sup> ADF, Submission 4, attachment 1, Treasury, FGCC consultation paper, 2014, p. 12.

In the end, neither Treasury nor the Senate accepted what could be seen as having been the majority view (amongst submitters at least) that in its proposed form, the FGCC would trade flexibility for fairness. It is a view that will be tested again in the forthcoming review of the Code, in 2018.

ii. GOOD FAITH

As mentioned above, the provision of a 'good faith' clause was viewed by some as a check on the flexibility built into commercial negotiations under the Code. According to Treasury:

*On balance, the submissions received via the consultation process were supportive of the inclusion in the Grocery Code of an obligation to act in good faith. Given the focus of the Code on improving dealings in the sector, the benefits deriving from such inclusion were assessed as outweighing any negligible costs, noting that it is an overarching obligation that already exists at common law.<sup>660</sup>*

Clearly, and not surprisingly, there was strong support for an obligation on retailers to act in good faith. However, there were also qualifications, suggesting that for some, while a good faith provision may have been seen as necessary, it was not necessarily sufficient.

The Tasmanian Farmers and Graziers Association (TFGA), for example, supported the inclusion of a good faith provision,<sup>661</sup> but went on to say that:

*Allowing pecuniary penalties to be enforced by a court, as opposed to just punitive penalties, would have a more influential effect on ensuring retailers adhere to the Code, the agreements and the duty of good faith.<sup>662</sup>*

The Small Business Development Corporation of WA (SBDC) highlighted the difficulty in defining the concept of good faith and drew attention to some of the implications of a lack of understanding as to its meaning:

*An obligation to act in good faith is not an easy concept to define nor is it clearly understood by any who seek to rely on it in their commercial relationships. In the SBDC's opinion, it has the potential to create a false sense of security among small business owners as they may believe it to be the panacea to any issue or dispute that may arise under a contractual arrangement with another party.*

*The SBDC's experience is that small business owners are typically unclear on what constitutes good faith (as well as what doesn't) and may ultimately be disappointed that it does not provide an effective remedy to enforce their rights or resolve their disputes.<sup>663</sup>*

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<sup>660</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 18.

<sup>661</sup> TFGA submission, Treasury, FGCC consultation paper, 2014, September 2014, p. 5.

<sup>662</sup> TFGA submission, Treasury, FGCC consultation paper, 2014, September 2014, p. 6.

<sup>663</sup> SBDC submission, Treasury, FGCC consultation paper, 2014, September 2014, p. 5.

The subjective and amorphous nature of the good faith concept was reflected in our interviews. Dawson explained that the provision was included in the RSR draft of the code, having had the benefit of feedback from the UK as to its importance as ‘a bit of a catch-all’ (that is to cover gaps that emerge in the more detailed provisions).<sup>664</sup>

Interestingly though there is a difference, and potentially an important one, between the way in which the good faith provision is incorporated in the UK Code and its incorporation in the FGCC. In the latter it is a free-standing obligation, additional to the other obligations in the Code. This could be taken to suggest that it operates as a catch-all, imposing obligations (albeit unspecified beyond the general parameters of ‘good faith’), additional to those specified in the rest of the Code. By comparison, in the UK, a ‘Principle of Fair Dealing’ is included upfront, and in that way is seen to infuse and inform, rather than add to, the other provisions of the GSCOP.<sup>665</sup> As the GCA explained in our interview with her, ‘the Code... has an overarching principle of fair dealing, but what that actually means is interpreted by each individual section of the code underneath it. So I can’t say that “this is unfair”, if there’s actually nothing underneath to link it.’<sup>666</sup>

The difference in these approaches not a matter of mere semantics. It may be material in relation to the degree of certainty that is associated with, and hence the degree of practical usefulness, of the concept of good faith in each Code. This is reflected in comments by John Noble of British Brands Group who recalls that when GSCOP was introduced there was concern about the potential breadth of the Principle of Fair Dealing and in general a collective sigh of relief when, upon her appointment, the GCA made it clear that this was not a stand-alone provision and was simply there to inform other parts of the Code.<sup>667</sup>

Evidently, when it comes to ‘good faith’ there is a wide range of interpretations as to its meaning. We asked interviewees what they understood it to mean, and in response we heard:

*The key purpose of the Code is to build trust in the trading relationships. The specific provisions address many of the retailer behaviours that were undermining trust. But beyond these the good faith provision is a catch all that sets a standard for the overall trading relationships, based on honesty and genuine negotiations. If behaviours emerge that are not covered by the specific Code provisions but could arguably be in breach of good faith then the regulator has a basis for investigation and action.*<sup>668</sup>

*Unconscionable is something so bad it goes against good conscience, whereas we’re not just talking about not doing that, we’re talking about something much more clean and pure than that, and that’s where I see good faith.*<sup>669</sup>

<sup>664</sup> Transcript of interview, Gary Dawson, pp. 41-2.

<sup>665</sup> According to an experienced legal advisor to suppliers in the UK, the principle was drawn from the European Directive on unfair contract terms (p. 16).

<sup>666</sup> Transcript of interview, Christine Tacon, p. 3.

<sup>667</sup> Transcript of interview, John Noble, British Brands Group, p. 21.

<sup>668</sup> Transcript of interview, Gary Dawson, pp. 46-7.

<sup>669</sup> Transcript of interview, MSC representative, p. 4.

*It's a terrific value, isn't it? To do something in good faith. And when someone says - actually carries out what they say they're going to do or commit to. So I would offer that in good faith is that, is adhering to the commitments..<sup>670</sup>*

*..it's about treating the other party, giving them an opportunity to respond to the position and actually in a manner that gives them an opportunity to have a voice in the transaction and not a take it or leave it type position, and [it's about being] fair..<sup>671</sup>*

*...it's clarity of the expectations ... that doesn't mean that you're [not] going to have tough conversations ... [but] clarity of expectations, it allows me to make the choice. Either you choose to play, and this is the cost and the reward of playing, or we make the choice to not play, and that's the cost, the downside of not playing. I think that's really all you can ask. Because I think each person walks in each other's shoes. You recognise the pressure that your retailers are under in terms of, they are providing the results that they need to provide, and also on the flip side, it's not personal, it's not emotional, it's just around how do we deliver better outcomes. There's transparency of the metrics.<sup>672</sup>*

*Very practically it means staying at the table, very practically it means maintaining an open dialogue and being willing to participate whilst not lording threats or enacting threats over one or other.<sup>673</sup>*

*I think the other thing about the notion of good faith to me is around fairness; whatever we discuss, is the outcome fair?<sup>674</sup>*

*It goes to this notion of doing the right thing, and I think it's difficult to say what good faith is; it's much easier to say what bad faith is, and if you were telling people the things that are not acceptable as well as it helps address that point of what is acceptable.<sup>675</sup>*

*...good faith is a very broad vehicle church ... and the way I describe it to large or small suppliers is that a retailer must take your interests into consideration as well as theirs roughly. It, kind of, has to be mostly fairish and if I'm smiling and you're crying then maybe it's not been done in good faith, if your mum were to say, darling, that's not right, it might be a bridge of good faith. So there should be equal risk, equal reward, not equal in the broadest sense, but I need to be aware of your circumstances and my circumstances and make a decision based on both, particularly if I'm the big guy and you're the small guy, I need to be conscious of that and act in good faith.<sup>676</sup>*

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<sup>670</sup> Transcript of interview, CEO of MGA, pp. 25-6.

<sup>671</sup> Transcript of interview, interviewee who consults to grocery businesses, p. 37.

<sup>672</sup> Transcript of interview, senior representative of a larger supplier of packaged goods to the MSCs, p. 40.

<sup>673</sup> Transcript of interview, MSC representative, p. 19.

<sup>674</sup> Transcript of interview, CEO of major packaged goods supplier to the MSCs, p. 39.

<sup>675</sup> Transcript of interview, MSC representative, p. 21.

<sup>676</sup> Transcript of interview, director of a consultancy that advises suppliers, pp. 24-5.

*...if I'm smiling and you're crying then maybe it's not been done in good faith.*<sup>677</sup>

In the GSCOP, the 'Principle of Fair Dealing' is framed as follows:

*A Retailer must at all times deal with its Suppliers fairly and lawfully. Fair and lawful dealing will be understood as requiring the Retailer to conduct its trading relationships with Suppliers in good faith, without distinction between formal or informal arrangements, without duress and in recognition of the Suppliers' need for certainty as regards the risks and costs of trading, particularly in relation to production, delivery and payment issues.*<sup>678</sup>

Treasury also recognised that while some stakeholders, such as the NSW Small Business Commissioner, felt that the good faith obligation should apply only to retailers,<sup>679</sup> several others advocated a reciprocal provision that would extend to suppliers as well. As one of our interviewees saw it, from the perspective of suppliers, a reciprocal obligation had the advantage of enabling them to set the standard for what it meant or should mean:

*...look, if you want to teach your children not to pick their noses then don't pick your nose yourself - - - it's not nice, so don't do things to them that you wouldn't want them do unto you, so why would you not act in good faith as a supplier?*<sup>680</sup>

Costco made the argument in favour of a reciprocal good faith obligation on the grounds that large suppliers possessed significant bargaining power, and that this should be recognised by such a code.<sup>681</sup> The MSCs might have made a similar point in their confidential submissions, but as one MSC representative told us, ultimately his organisation accepted the argument that the good faith obligation should not be mutual 'because the Code was about retailer behaviour, not about the whole-of-industry behaviour'.<sup>682</sup> However, he also pointed out there is a provision in their GSAs that requires the supplier to act in good faith and, when questioned about this by some suppliers, his response is that 'they will still have a lower threshold of good faith behaviour than we have because in our case the onus of proof is on us, to prove that we behaved well. ... [T]hat onus isn't placed on the supplier with regard to the GSA'.<sup>683</sup>

Others too, including those from the farming and produce sectors, argued for extending the good faith obligation to suppliers, albeit on fairness grounds:

*The TFGA supports the inclusion of the duty of faith provision, as it should have the capacity to improve commercial relationships. To make sure this does occur, it would be prudent to ensure*

<sup>677</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 24.

<sup>678</sup> GSCOP, cl 2.

<sup>679</sup> Small Business NSW Commissioner submission, Treasury, FGCC consultation paper, 2014, September 2014, p. 4.

<sup>680</sup> Transcript of interview, director of a consultancy that advises suppliers, 32.

<sup>681</sup> Costco submission, Treasury, FGCC consultation paper, 2014, p. 5.

<sup>682</sup> Transcript of interview, MSC representative, p. 8.

<sup>683</sup> Transcript of interview, MSC representative, p. 8.

*compliance from both parties from the beginning, so no party is seen to be at disadvantage.*<sup>684</sup>  
(TFGA)

*In the spirit of building relationships, the NFF believes the need for good faith dealing applies equally to suppliers – irrespective of where the market power is considered to reside.*<sup>685</sup> (NFF)

Ultimately, Treasury considered it problematic to impose obligations on parties that were not themselves opted into the code. Nevertheless, Treasury noted that:

*... to address the concerns of stakeholders raised during consultation, the Grocery Code provides that when a court is assessing whether a retailer has contravened the obligation, it may consider whether or not a supplier has acted in good faith.*<sup>686</sup>

### iii. DISPUTE RESOLUTION

A key purpose behind the development of the FGCC was:

*...to provide an effective, fair and equitable dispute resolution process for raising and investigating complaints and resolving disputes arising between retailers or wholesalers and suppliers.*<sup>687</sup>

The dispute resolution processes provided for in the Code only come into play at the instigation of suppliers. There is no equivalent process for wholesalers or retailers.<sup>688</sup> Despite this, some question how many suppliers would actually rely on these mechanisms, and when. As one supplier told us:

*You don't go to a marriage counsellor every time you don't agree with something do you? It's the same philosophy in business. ... Now people are scared about relationships in business because you can get power through a relationship or you can get an advantage. Bull shit. You earn your relationship, right.*<sup>689</sup>

Another expressed doubts about whether suppliers – particularly smaller suppliers – would notify a dispute under the Code; in part because of the complexity of the process, and in part because of ongoing concerns about unintended negative consequences:

*I'm just cynical that suppliers would go to those lengths. Because things happen very rapidly, when you're doing business. ... I don't know if they would go through the dispute resolution for fear of that retribution.*<sup>690</sup>

<sup>684</sup> TFGA submission, Treasury, FGCC consultation paper, 2014, p. 5.

<sup>685</sup> NFF submission, Treasury, FGCC consultation paper, 2014, p. 7.

<sup>686</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 18.

<sup>687</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 2.

<sup>688</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 18.

<sup>689</sup> Transcript of interview, CEO of a major fresh produce supplier to a MSC, p. 35.

<sup>690</sup> Transcript of interview, CEO of MGA, p. 31.

Treasury reported 'broad support' for a clear and effective dispute resolution mechanism, however it also acknowledged that amendments had been made to the initial draft in response to concerns raised about this aspect of the proposed code during the consultation process.<sup>691</sup>

The debate surrounding these amendments further illustrate the disparate concerns amongst stakeholder groups.

One such amendment was the requirement that, 'if a complaint is found to be trivial, vexatious, or lacking in substance, notice in writing should be provided to the supplier.'<sup>692</sup> Such notice must advise of the reasons for the conclusion reached, and there is provision for the supplier to seek internal review and/or mediation/arbitration if they are not satisfied with the outcome.

This amendment was presumably sought by retailers, anticipating perhaps and seeking to limit the number of frivolous claims lodged. However the NSW Small Business Commissioner argued that 'it unfairly places the decision-making power in relation to commencing dispute resolution processes firmly with the retailer.' The Commissioner went on to note that such a clause may discourage suppliers from using the dispute resolution processes provided under the Code - a cause for concern, 'given that there is evidence that many small suppliers are hesitant to raise complaints at all'.<sup>693</sup>

In line with this, stakeholders reportedly perceived, 'the proposed mechanisms to be 'too weak' and not 'fair or equitable' due to placing too much discretion in the hands of major retailers'.<sup>694</sup> The SBDC stated that while it 'strongly supports the inclusion of access to dispute resolution mechanisms under the Grocery Code', it had, 'some reservations that the threshold set by the Grocery Code will create a barrier for suppliers seeking to resolve their disputes using either the internal or external process.' The SBDC went on to state in its submission that:

*... the SBDC does not believe that retailers should be the decision maker on whether a supplier's concern is appropriate for this course of action.*

*To ensure better equity and fairness, the SBDC believes that an independent third party arbitrator should review a supplier's claim and make a judgment on whether it has merit and could be appropriately resolved through the dispute resolution processes available under the Grocery Code.*<sup>695</sup>

In accord with this, the NFF argued that:

*... the Code provides for dispute remedies (excluding money penalties) but many suppliers question the independence of the dispute resolution process and even more may not have*

<sup>691</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 19.

<sup>692</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 19.

<sup>693</sup> Small Business NSW Commissioner, submission Treasury, FGCC consultation paper, 2014, p. 4.

<sup>694</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 19.

<sup>695</sup> SBDC submission, Treasury, FGCC consultation paper, 2014, September 2014, pp. 5-6

*sufficient confidence to test it for fear of subsequent retribution. This situation points to the need for an independent supermarket commissioner or ombudsman.*<sup>696</sup>

There has also been criticism targeting the complexity of the process. As one dispute resolution expert noted:

*My focus is always on the issue of dispute resolution but the way in which this is framed in terms of the rights of suppliers, well ... it's almost a roadblock to a supplier's success because the language and the manner of drafting creates almost impenetrable barriers.*<sup>697</sup>

Even Billson (otherwise a fervent supporter of every aspect of the Code) concedes that there are potential weaknesses in the dispute resolution framework. However, he clearly saw a real need for suppliers to have alternatives to litigation:

*... we all know if a small business gets in a commercial blue and ends up in court they're gone, they're just going to lose or they'll be starved out. So I was trying to put in place machinery to – where a dispute arose, get it sorted quickly.*<sup>698</sup>

When asked about whether suppliers, small ones particularly, would use the system in the FGCC for resolving grievances, he acknowledged that 'there was a contest about how good [that system] was.'<sup>699</sup> He disclosed that his 'original design' was in fact to use the SBFE Ombudsman for FGCC-related dispute resolution 'but sequencing played against me'.<sup>700</sup> The legislation establishing that office had not yet been passed and thus yet again, it seems, the need to drive through a 'solution' to the MSC-supplier problem overrode any consideration that might have delayed the process, even if it might have made (in the eyes of some) for a better outcome.<sup>701</sup>

Concerns about the use of external mediator/arbitrators as opposed to an industry specific ombudsman were raised by the former PGCC Ombudsman in his testimony to the Senate Inquiry into the FGCC: 'the industry needs, and the public interest requires, a genuine independent oversight mechanism in relation to the commercial transactions in the produce and grocery industry.'<sup>702</sup>

It seems however that independence alone is not viewed by some as sufficient, if this independence comes without industry knowledge. This became evident in our interview with a major MSC fresh produce supplier to one of the MSCs. When asked whether he knew that the MSC had an external mediator that he could contact regarding possible breaches of the Code the supplier responded, 'Yeah I am but I'm not – I don't think that a farmer growing xxx is going to go to xxx, is my point'.<sup>703</sup>

<sup>696</sup> NFF submission to Treasury, FGCC consultation paper, 2014, p. 6.

<sup>697</sup> Transcript of interview, Robert Gaussen, p. 42.

<sup>698</sup> Transcript of interview, Bruce Billson, p. 17.

<sup>699</sup> Transcript of interview, Bruce Billson, p. 38.

<sup>700</sup> Transcript of interview, Bruce Billson, p. 38.

<sup>701</sup> Kate Carnell AO commenced as the inaugural SBFE Ombudsman on 11 March 2016, a year after the FGCC took effect.

The functions and powers of the Ombudsman are set out in *Australian Small Business and Family Enterprise Ombudsman Act 2015* <https://www.legislation.gov.au/Details/C2015A00123>

<sup>702</sup> Robert Gaussen testimony, Senate Economics Legislation Committee Inquiry, *Competition and Consumer Act 2010—Competition and Consumer (Industry Codes—Food and Grocery) Regulation 2015*, Tuesday, 21 April 2015, p. 10.

<sup>703</sup> Transcript of interview, CEO of a major fresh produce supplier to a MSC, p. 34.

In his interview for this research, Robert Gaussen elaborated on why he thinks his role as PGCC Ombudsman was, to his mind, a success. His reasoning goes beyond independence and places greater emphasis on relationship building:

*I would just try and get through to people that I was genuine, I'd look them in the eye, I'd shake their hand ... Doesn't matter if it doesn't go anywhere, I'm here to be talked to and I can help you understand how the processes go, I can't give you advice as to the merit of your dispute, I made that always very clear ... but in terms of the process, the process of what the codes about, what you can do under the code, how to put together a case under the code I can help you with all those things.<sup>704</sup>*

In conjunction with the importance of building trust with suppliers Gaussen emphasised the need to establish similarly strong relationships with the MSCs, to everyone's benefit; and the potential power of employing informal channels as well as formal channels to achieve mutually beneficial outcomes:

*The deal was very simple. If – whatever complaints in relation to their conduct I would ring the nominated person who was very, very senior for both of them at the time, ring one of them – of the particular company – and I'd lay out what the dispute was and they'd have at least 48 hours to come back to me and they always did and in almost every occasion it was well and truly fixed by the time they got back. But I would – the agreement was I did not report that as a dispute, I reported it as an enquiry but it wasn't recorded as a mediation and when we came to publish the disputes it wasn't a dispute because it never went to mediation or that's what they wanted out of it. And they also liked the fact they could learn about things they didn't know about, they liked the early warning system that I could provide and also they didn't have to deal with highly spirited and very upset people, I was their filter.<sup>705</sup>*

In the case of one of the suppliers whom we interviewed, he said that if he did suspect a breach of the Code he was more likely to contact his category manager, 'and if that doesn't work I'll find – I'll bloody drive in there and find an answer'.<sup>706</sup> When pressed as to whether or not he knew that the MSC had a code compliance manager the supplier laughed and responded, 'I don't spend my time worrying about that kind of thing. I'm not – I'm discounting it but, I would hate to think that I would have to have access to something like that.'<sup>707</sup> Ultimately, for this supplier, it all came down to mutual trust with his buyer, arguably something that can be supported by, but not prescribed, under any formal code.

The debate as to whether or not the Code should be overseen by an ombudsman was played out in the submissions to Senate Economic Legislative Committee. While some such as Gaussen, the ADF and the Office of the Australian Small Business Commissioner (OASBC)<sup>708</sup> argued in favour of an ombudsman, others, including the ACCC, were more sceptical. Certainly, as became evident in our interviews, this was one element of the regulatory intervention to which the MSCs were vehemently

<sup>704</sup> Transcript of interview, Robert Gaussen, p. 27.

<sup>705</sup> Transcript of interview, Robert Gaussen, p. 18.

<sup>706</sup> Transcript of interview, CEO of a major fresh produce supplier to a MSC, p. 34.

<sup>707</sup> Transcript of interview, CEO of a major fresh produce supplier to a MSC, p. 35.

<sup>708</sup> The OASBC has now been superseded by the Australian Small Business and Family Enterprise Ombudsman.

opposed. When it was pointed out to one MSC representative that the collaboration between Coles and Woolworths on the RSR could be seen in some ways as unprecedented – a collaboration between two fiercely competitive and culturally different rivals – and asked about what brought them together in this endeavour, we were told:

*I would say probably the prospect of an Ombudsman, a heavy-handed instrument being imposed on the marketplace, as opposed to something that would achieve the right outcome but be more manageable in the marketplace.<sup>709</sup>*

For the OASBC, having the SBFE Ombudsman assume responsibility for the resolution of disputes under the Code would be a low cost ADR alternative.<sup>710</sup> Gausson also made the argument that an industry-specific ombudsman was a cost effective alternative to arbitration or litigation. Gausson particularly stressed the need for a dedicated industry-specific ombudsman who could build up a body of knowledge that could be drawn on over time. The ACCC told the Committee, however, that it was better suited to advising suppliers on the best avenue by which to resolve their disputes, including when litigation was the preferred or necessary course.<sup>711</sup>

Gausson reasoned that during his time in the PGCC Ombudsman role he was often able to work with MSCs and wholesalers to resolve a dispute without having to identify the complainant, and that the preservation of this anonymous compliant avenue would be a valuable asset for the Code.<sup>712</sup> However again the ACCC, countered, questioning just how realistic this suggestion was and telling the committee that it was, 'rare that you are able to get into the issues without understanding who the parties are'.<sup>713</sup>

Separate to the Senate inquiry some at the ACCC have suggested there is value in having a single point of contact for dealing with disputes that arise under the Code:

*So ADR general works well. There are different tools and, of course, you have to ask yourself, really, if Commonwealth Government has gone to the level of setting up a small business commissioner, unfortunately called a small business ombudsman, but a federal one, then why do we have multiple dispute resolution [mechanisms] – clearly, to my mind, the logical thing is to collapse all of those into the one body and ... give them to the ombudsman.<sup>714</sup>*

However the interviewee was cautious about just what an ombudsman's role might be, or be perceived to be:

<sup>709</sup> Transcript of interview, MSC representative, 3.

<sup>710</sup> Office of the Australian Small Business Commissioner, Submission 2, SELC review of the FGC Regulation, 2015, pp. 1-2.

<sup>711</sup> Nigel Ridgway, Executive General Manager, Consumer, Small Business and Product Safety, ACCC, Proof Committee Hansard, 21 April 2015, p. 18.

<sup>712</sup> Robert Gausson, private capacity, Proof Committee Hansard, 21 April 2015, p. 11.

<sup>713</sup> Scott Gregson, Executive General Manager, ACCC Consumer Enforcement, Proof Committee Hansard, 21 April 2015, p. 22.

<sup>714</sup> Transcript of interview, senior representative of the ACCC, p. 38.

*I was in - yesterday for example – Shepparton, and someone said, “You know, there needs to be an ombudsman to make a decision about what these prices are.” I tried to explain, well, you know, constitutionally you can’t have an ombudsman who just sits down and decides who’s right and who’s wrong. We’ve got this thing called the constitution. It might not suit you today, but I tell you what, if the cops charge you for something you really want to know that there’s a court system and a legal representation, so just be careful what you ask for.<sup>715</sup>*

Despite the overall objections of the ACCC and others, however the Senate Committee ultimately believed that:

*In light of the benefits an ombudsman would bring to the operation of the Grocery Code and the grocery sector more generally, we believe there is a strong case for the appointment of an independent ombudsman to oversight the Grocery Code, with funding provided by the government. The ombudsman should have formal capacity to refer businesses for further assistance to relevant industry, Commonwealth, State or Local government bodies, including the ACCC.<sup>716</sup>*

In line with this the committee supported the OASBC proposal that FGCC-related disputes should fall within the ambit of the SBFE Ombudsman’s office,<sup>717</sup> saying that this, ‘would be a sensible policy that would strengthen the operation of the Code’,<sup>718</sup> which would ‘result in efficiency and organisational benefits’ rather than creating a new Ombudsman position to provide oversight for the FGCC.<sup>719</sup> At the time of writing such proposed reforms do not appear to have developed further but may be revisited in the 2018 review.

Despite the concerns raised by and recommendations made on the part of small business in particular, the MSCs view prevailed with regard to the evidentiary requirements imposed on suppliers in any dispute resolution process. The following position was taken in the RIS, laying the burden very much at the feet of suppliers:

*Importantly, following consultation, it was clarified that a supplier provides sufficient particulars of its complaint or dispute about a unilateral or retrospective variation of the agreement if it provides particulars of the detriment that has been or will be caused to the supplier. The supplier also needs to point to the provision of the Grocery Code alleged to be breached and the remedy sought.<sup>720</sup>*

It is notable that in the UK a very similar debate had been played out, in relation to the question whether the GSCOP should be administered and enforced by an independent ombudsman or by the competition authority, then the OFT. This was a question that occupied the minds of many submitters to the CC’s 2006-2008 inquiry and, as in Australia, views were divided. But in the end, unlike here, the

<sup>715</sup> Transcript of interview, senior representative of the ACCC, p. 34.

<sup>716</sup> SELC, *FGC Regulation*, 2015, p. 27.

<sup>717</sup> SELC, *FGC Regulation*, 2015, p. 28.

<sup>718</sup> SELC, *FGC Regulation*, 2015, p. 28.

<sup>719</sup> SELC, *FGC Regulation*, 2015, p. 28.

<sup>720</sup> Treasury, *FGCC Final Assessment RIS*, 2014, p. 19.

CC's view (which government supported, over the fierce opposition of the retailers) was that there should be an independent ombudsman.

Amongst the submitters to the CC inquiry, many parties (including the Association of Convenience Stores, suppliers, supplier organisations, non-governmental organisations and primary producer organizations, and consumers) questioned whether the OFT was the best authority to supervise and enforce retailer compliance with the proposed code, and in addition, whether the monitoring authority should have a proactive role in reviewing retailer practices more generally. These submissions supported the establishment of an ombudsman.<sup>721</sup>

By contrast, submissions from retailers supported the continued involvement of the OFT in this role. Morrisons said that the costs of an ombudsman would be excessive, relative to the consumer detriment arising from supply chain practices. Certain retailers (Waitrose, Morrisons) suggested that the burden of the costs of the ombudsman, should one be established, ought to be weighted towards retailers which are the subject of complaints and disputes. Some retailers (Asda, Waitrose) took the view that there was a danger of 'regulatory creep' (ie the ombudsman extending its remit to non-competition issues).<sup>722</sup>

Interestingly and in contrast to the position of the ACCC in the Australian debate, the OFT itself recognised that a dedicated body with industry expertise, which would build working relationships with supplier associations and retailers and monitor compliance and promote best practice, would have advantages. It suggested that this entity could also raise the profile of the GSCOP. Indeed, so strong was the OFT view that the Code's enforcement should not be part of its bailiwick, a former senior representative of the agency recounted in his interview with us: 'I jokingly said when the UK Government was introducing it that if the OFT was running it, we should see it as an opportunity to create employment on a Scottish island.'<sup>723</sup> Light heartedness aside, he explained:

*I really didn't want it to contaminate our brand. I was against it being something that was part of the competition and consumer protection regime. I believed it would be better to have a separate regulator that could get more involved in understanding the industry. I also thought that any law or such code addressing the treatment of suppliers should have as its overriding objective, the improvement of value for the consumer at the end of the food chain, as opposed to being about allocation of profit within the food chain. Having orderly supply arrangements and efficient contracting and avoiding legal disputes is in the consumer's long term interest. So I certainly would have a preference for that, because I think it is less confusion in the public mind as to who is doing what and why.<sup>724</sup>*

In our interview, reflecting back herself on why GSCOP administration is best carved out of the responsibilities of the competition authority, the GCA noted that individual disputes between retailers

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<sup>721</sup> CC 2008 report, p. 242.

<sup>722</sup> CC 2008 report, p. 242.

<sup>723</sup> Transcript of interview, former senior representative of the UK OFT, p. 19.

<sup>724</sup> Transcript of interview, former senior representative of the UK OFT, pp. 19-20.

and suppliers just would not register as a priority for the authority and this was particularly so given that, as in Australia, by and large competition is seen to be working, at least at a horizontal level, in the grocery sector in that country.<sup>725</sup> This view was echoed by Noble from British Brands Group:

*...the OFT had its prioritisation principles and our experience was that they were reluctant to get into the nitty-gritty of enforcing day-to-day. They had many other markets they were looking at, mergers to deal with, consumer protection duties – they had a huge task and trying to get something on their prioritisation principles was always very difficult, particularly if it was seen by them as being a spat between a retailer and supplier with difficult-to-assess implications for the shopper and the consumer. We would say that just one practice, when multiplied over the whole range of different categories and across different retailers, the impact on the consumer gets quite significant. But trying to demonstrate consumer harm to get over the prioritisation principles was always very, very difficult. And so I think the Competition Commission recognised that limitation and said, “Well the only way that we’re going to get this monitored and enforced is by having a dedicated enforcer whose job won’t be distracted by other things and isn’t subject to the same prioritisation principles...”<sup>726</sup>*

Noble supports his argument in favour of the GCA over the competition authority as enforcer of a code by pointing out that, somewhat oddly, in the UK it is the CMA that has jurisdiction over the requirement to have written supply agreements while the GCA has jurisdiction over the remainder of the Code. Tacon has notified the CMA about allegations that some of the retailers are failing in the written supply agreements obligation, but:

*... the CMA [has] done little in the areas it is responsible for and is unlikely to. It’s got bigger fish to fry. So that is quite an interesting dichotomy where one area, enforced by the CMA, is not being enforced and another area where you’ve got Christine being very engaged, very active and collaborative in her regulatory activity.<sup>727</sup>*

Noble’s view on why the competition authority was not given responsibility for administering most of GSCOP is supported by other UK commentators. An experienced legal advisor to suppliers told us:

*When the OFT had responsibility for the prior version of the code [a reference to SCOP] .. I think it was perceived to have no interest in doing anything about it whatsoever. So there was a view that the OFT has had the job already once and has failed to do anything with it. So it needed to be somebody else to have any credibility. So you’re right, the natural place for it would have been the OFT. And that’s to do with a number of things. It’s easy to be hard on the OFT. But you have an agency with numerous functions. There is a contest on its resources. Taking it outside of there, you could create somebody who has dedicated resources and you’ve got to remember the GCA is funded by the retailers, it’s not funded by government.<sup>728</sup>*

<sup>725</sup> Transcript of interview, Christine Tacon, p. 11.

<sup>726</sup> Transcript of interview, John Noble, British Brands Group, p. 33.

<sup>727</sup> Transcript of interview, John Noble, British Brands Group, p. 34.

<sup>728</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, pp. 17-18.

She also made the point that there is a merit in having funding for GSCOP enforcement that is ‘ring-fenced’ and not in a “central pot” that constitutes the budget for the competition authority: ‘the problem is if you put it in the OFT central pot and you say “okay, we’ll give you extra budget to do it,” unless you’d ring fenced that budget in some way, there’ll be something sexier or more exciting...’.<sup>729</sup> Priorities for these authorities range from year to year, sectors go in and out of vogue ... and, she observes, this was the case with the OFT and SCOP enforcement. There just came a point ‘where they just went, do you know what? We’re not interested in this anymore.’ There are always other calls on their attention: ‘yes, grocery’s important ... but I can’t see them getting back to cases like that, unless they’re in an online environment, which is what they now regard as a priority...’<sup>730</sup>

Tacon also made the point that, in her view, what was needed in the role was not the enforcement approach or mentality of an agency otherwise generally tasked with determining liability and imposing sanctions, but rather a more collaborative approach of bringing and working together with parties to find a compromise solution to issues of concern – an approach similar to that taken by the former PGCC Ombudsman. Tacon distinguishes in this regard between her *modus operandi* when performing educative and monitoring functions and when acting in an investigative capacity but even in relation to the latter she takes a collaborative approach, as evinced by the guidance on investigations that she has published.<sup>731</sup> As she pointed out to us, when she was being considered for the position, she put the question to the government: ‘were they looking for someone who would roll up their sleeves and get involved or [did they want] a retired judge?’<sup>732</sup> Clearly she was in the former category and, having met Tacon, evidently the government ultimately decided that it wanted the more hands-on approach that she promised.<sup>733</sup> Apparently, however, the advert for the position read as if the government was ‘looking for an ex-Judge who’s going to adjudicate disputes’.<sup>734</sup> That initial intention perhaps explains also the name given to the role.

Having reviewed the various submissions, the CC found favour predominantly in the OFT view, namely ‘that a dedicated body with industry expertise, which would build working relationships with supplier trade associations and retailers and monitor compliance and promote best practice, would have advantages.’<sup>735</sup> The CC went on to explain that ‘given the importance of involving stakeholders in the process of establishing an Ombudsman scheme’<sup>736</sup> it would seek undertakings from all retailers that it had decided should be covered by the GSCOP to support and fund the ombudsman scheme. However, if retailers failed to agree to these undertakings, it recommended that the government should take the necessary steps to create an ombudsman.

<sup>729</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 41.

<sup>730</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 42.

<sup>731</sup> See Grocery Codes Adjudicator, *GCA policy: Continuing the collaborative approach during an investigation*, at <https://www.gov.uk/government/publications/gca-collaborative-approach-during-an-investigation>.

<sup>732</sup> Transcript of interview, Christine Tacon, p. 12.

<sup>733</sup> See Transcript of interview, compliance manager at a major UK retailer, P. 17: the government wanted ‘somebody that understood the industry and was able to give an independent view with some authority. The supermarket world and the supplier world is quite a complex one and the farming world is quite complex; I think what Christine was able to bring was experience from those environments that people would say, yep, this is not just a pure civil servant in here doing the absolute black and white, this is much more about somebody that has a reasonable understanding.’

<sup>734</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 18.

<sup>735</sup> CC 2008 report, [11.333-6].

<sup>736</sup> CC 2008 report, [11.343].

Perhaps not surprisingly, securing retailer agreement on such a scheme proved impossible. In some parallel with the MSC alliance that stood behind the FGCC and opposed a mandatory code in Australia, the UK retailers spoke with one voice in opposition to the establishment of the GCA. As Noble of British Brands Group recounts, when the CC asked the supermarkets to set up the ombudsman scheme themselves, ‘they said no.’<sup>737</sup> And why would they have said otherwise, he asks somewhat rhetorically. ‘It [was] going to cost them money, they saw it as extra regulation. Delay isn’t a bad policy... so by not agreeing they prompted a five, six year delay ... in public policy terms you can say that’s a result!’<sup>738</sup>

Hence the government set up the GCA itself – explaining in part the time between the GSCOP coming into effect in 2010, and the establishment of the GCA in 2013.<sup>739</sup> Indeed, in the period following the CC’s 2008 report, economic conditions had toughened and, fearing that this would prompt retailers to place suppliers under even greater pressure, the CC took the view that the case for ombudsman oversight was even stronger a year out from the publication of its report.<sup>740</sup> The UK government evidently agreed but it also stuck to its guns that the ombudsman scheme would be funded by imposing a levy on the retailers, an aspect of the UK model that the MSCs here quite clearly wanted to avoid being replicated. For the British government, this was seen as ‘smart’ regulation – making ‘sure that the people who are creating the problem are tasked with sorting it out and paying if necessary rather than the taxpayer doing it.’<sup>741</sup>

What is notable about this sequence of events is the parallels between UK and Australian developments. In the UK there was a voluntary code (SCOP from 2010) and evidently it failed, in large part due to non-compliance by the supermarkets and notwithstanding that there was oversight by the competition authority, the retailers having given undertakings to be bound.<sup>742</sup> The next step was for government to intervene and create a dedicated enforcement and compliance architecture. In Australia it could be said that we are at stage 1, in UK terms, with a voluntary code to be enforced by the ACCC. The MSCs opposed the establishment of a specialist ombudsman scheme, just as did the supermarkets in the UK. The question in due course will be whether we reach UK stage 2 ...

#### IV. PENALTIES

At the time that the RIS was published, the CCA did not provide for pecuniary penalties or infringement notices for contraventions of an industry code, or for the creation of regulations that prescribe penalties for the contravention of an industry code. The RIS noted, however, that the Government was proposing to introduce pecuniary penalties for breaches of the Franchising Code

<sup>737</sup> Transcript of interview, John Noble, British Brands Group, p. 15.

<sup>738</sup> Transcript of interview, John Noble, British Brands Group, p. 35.

<sup>739</sup> The other explanation for the delay was that the GCA’s establishment required the passage of primary legislation and it kept slipping on the parliamentary timetable given other more pressing legislative priorities at the time (Transcript of interview, experienced legal advisor to suppliers in the UK, p. 26).

<sup>740</sup> CC News Release 08/09, *CC publishes code of practice order*, 26 February 2009.

<sup>741</sup> Transcript of interview, John Noble, British Brands Group, p. 36.

<sup>742</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 24: ‘people regarded that code as dead letter ... so you know, if you attempted to point to compliance with it, people felt that you would be laughed at and that there were practices continuing...’.

and to allow the ACCC to issue infringement notices for breaches of a civil penalty provision of that Code, and that for these changes to take place it would be necessary to amend the CCA.<sup>743</sup> These amendments have now come into effect. As of 1 January 2015, the regulation making a prescribed code under the CCA can now include provision for civil penalties up to a maximum of 300 penalty units (\$54,000 as of 2017). The FGCC does not currently contain any such provision therefore, as things stand, financial penalties cannot be imposed for breaches of the Code.<sup>744</sup>

One of the questions raised, but not extensively explored, in the RIS was whether provision should be made for pecuniary penalties for breaches of the FGCC. The issue was looked at in more depth by the Senate Committee. The Committee noted that while submitters were 'generally supportive of the Grocery Code', one of the key concerns was the adequacy of the penalties that could be applied where there was a breach.<sup>745</sup> The NSW Farmers Association suggested 'an appropriately graduated approach to enforcement', viewing this as a way to encourage:

*...desired behaviours from market participants', i.e. the ACCC could employ infringement notices for minor transgressions, or pursue pecuniary penalties through the courts where determined appropriate.*<sup>746</sup>

However a representative for Treasury suggested that to introduce penalties might prove a disincentive for companies to sign on to the Code:

*... this is the first time anybody has come forward with a voluntary prescribed code. And whether - so when a supermarket signs up to the code, they are voluntarily submitting themselves to a whole range of court enforceable remedies. And the question there is whether also applying the penalties in that situation would be - I guess (a) likely to encourage more industries to use that approach (b) would it actually encourage support of the code itself.*<sup>747</sup>

When asked about the subject in our interviews, a former and a current MSC representative both opposed the introduction of penalties, in part because they saw the Code as having a different, more positive, purpose than black letter law:

*I've always said no, because the law is the – the backdrop is where the law is. And the law has several and – and penalties. So penalties should apply in civil law. I don't think they should apply in a code, which is trying to be proactive.*<sup>748</sup>

<sup>743</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 22.

<sup>744</sup> See CCA, ss 51AE (2).

<sup>745</sup> SELC, *FGC Regulation*, 2015, p. 7.

<sup>746</sup> NSW Farmers submission 7, pp. 9-13, cited in SELC, *FGC Regulation*, 2015, p. 14.

<sup>747</sup> Transcript of interview, Treasury, p. 36.

<sup>748</sup> Transcript of interview, Robert Hadler, p. 51.

*...you spend every day in here as traders building trust with customers and your traders. It's about losing that trust and about your reputation, it's got very little to do with fines in my view.*<sup>749</sup>

Yet another MSC representative saw penalties for Code breaches as unnecessary because:

*There's injunctions, there's compensation if somebody suffered loss or damage, there's also the action that the ACCC could take for unconscionable conduct [or] misleading and deceptive conduct. ... [I]n my view, if you're breaching the Code in a material and serious way, there probably is an avenue for you to be financially penalised.*<sup>750</sup>

He also foresaw a possible added compliance burden in the event that penalties were available:

*There's people raising the Code when it's actually not really that relevant. And I just wonder whether we'd have to spend more time on it if there were financial penalties involved, and I'm not really sure.*<sup>751</sup>

And he argued that, while penalties and associated reputational damage:

*...concentrate the mind, more of the board and senior management and so on, operationally in the commercial team what frightens them probably more than anything else is the prospect of additional red tape, additional administrative difficulty in doing day-to-day business, additional reporting requirements let's say or something like that or additional audits that may happen – that type of thing. Something that gets in the way of the day-to-day job is probably much more in the minds of buyers because literally in this type of business there isn't enough hours in the day, it's full on so anything that slows down the process of going to market is something that frightens buyers.*<sup>752</sup>

A further perspective on why penalties may not be appropriate for code enforcement or if imposed, the importance of penalties being proportionate, was offered by a commentator from the UK. His argument was that high financial sanctions should be available where it is necessary to engender general deterrence and that that is particularly so where the rate of detection of the impugned conduct is low (as in the case of cartel conduct, for example). It is material in this context not to confuse deterrence and compensation in the design of a penalty regime – the focus must always be on whether the overall system delivers 'value for the consumer', not on whether individual suppliers are harmed.<sup>753</sup>

However, several submitters did advocate for penalties. Gaussen, the former PGCC Ombudsman, told the Senate Committee that:

<sup>749</sup> Transcript of interview, MSC representative, p. 24.

<sup>750</sup> Transcript of interview, MSC representative, p. 13.

<sup>751</sup> Transcript of interview, MSC representative, p. 14.

<sup>752</sup> Transcript of interview, MSC representative, p. 44.

<sup>753</sup> Transcript of interview, former senior representative of the UK OFT, p. 20.

*... any code of conduct that has no adequate enforcement regime will not be a successful code of conduct. The words that appear in this code are good words. The content and intention of what is being described in this code are great, and they are needed and are long overdue. But there is no obligation on anyone to do anything, even if they sign up to it, because of the system under which there is no enforcement.*<sup>754</sup>

Gaussen also suggested that an industry-specific ombudsman should have the power to refer disputes to the ACCC, and vice versa. In its submission, however, the ACCC suggested such matters 'might be better suited to dispute resolution rather than litigation'.<sup>755</sup> Instead the ACCC emphasised the role of the audit power provided for under the FGCC, allowing the agency to identify and respond to breaches, even in the absence of a complaint:

*In a sector where there have been ongoing observations that suppliers are reticent to bring problems to the ACCC's attention for fear of retribution by stopping of a supply agreement or a holiday, however it is characterised, the audit power enables the ACCC to reach in and check the books of those who subject themselves to the discipline of the code. This allows the ACCC to get the information we believe would identify problem behaviour without individuals needing to identify themselves.*<sup>756</sup>

In our interviews with the ACCC there was support for the introduction of penalties for FGCC breaches. One representative said:

*...for me, that's like why are we bothering with some of these, because what are we going to do, get a court order that says don't do this? That might look good for a lawyer, but I'll tell you what, for your average fruit and vegetable grower it means, huh, they broke the law so you took them to court to do what, so the judge said don't break the law? How does that work? What's that about? So, you know, without penalties they're a bit pointless.*<sup>757</sup>

When asked why the ACCC had not pushed previously for penalties for FGCC breaches, the same representative expressed frustration, replying: 'We have. We have – we have - we have – we have.'<sup>758</sup>

Former Chairman Graeme Samuel AC took a similar stance:

*Let's look at the code as being no more or less than a regulation or a law. If you're going to have a law that requires you to do certain things and it requires you not to do other things and you're going to disobey the law, then there's got to be a consequence. And the consequence*

<sup>754</sup> Robert Gaussen, Proof Committee Hansard, 21 April 2015, p. 10

<sup>755</sup> SELC, *FGC Regulation*, 2015, p. 15.

<sup>756</sup> Nigel Ridgway, Executive General Manager, Consumer, Small Business and Product Safety, ACCC, Proof Committee Hansard, 21 April 2015, in Senate Economics Legislation Committee Inquiry, *Competition and Consumer Act 2010 (Competition and Consumer (Industry Codes – Food and Grocery) Regulation 2015*, March 2015, p. 16.

<sup>757</sup> Transcript of interview, senior representative of the ACCC, p. 32.

<sup>758</sup> Transcript of interview, senior representative of the ACCC, p. 36.

*has got to be more than a naming, that you've breached. More than a court conviction – court adjudication. ... A declaration that you've breached. There has to be a penalty.*<sup>759</sup>

The lack of penalties for FGCC breaches is in stark contrast to the position in the UK where the GCA has power to impose fines up to a maximum of 1% of the relevant retailer's UK turnover over a 12 month period.<sup>760</sup> The UK Secretary of State for Business, Innovation and Skills had noted in 2012 that while the proposed legislative framework at that time only granted the GCA the power to 'name and shame', he had reserved the right to introduce fines if these measures proved insufficient.<sup>761</sup> On 29 January 2015 the UK government took this next step to shore up the potency of the GSCOP, the Secretary saying:

*This important final step will give the Groceries Code Adjudicator the power it needs to address the most serious disputes between the large supermarkets and their direct suppliers.*

*I created the Groceries Code Adjudicator to ensure a fair deal for those who supply goods to supermarkets such as farmers and small businesses. I am pleased today to be giving the Adjudicator the final element in a set of powers that will give this new body all the tools it needs to succeed in this challenging and important role.*<sup>762</sup>

In its report on the 2016-17 review of the GCA, the UK government noted that it had received submissions from some large retailers expressing concern about the potential size of the penalty available for breach of the GSCOP, and arguing that reputational damage alone would be a sufficient deterrent. Others were reported as indicating that the penalty was 'an important signal of how seriously the Code is being enforced' and overall, the report found 'broad support' for the sanction as a 'very powerful tool to use against non-compliant retailers'. Reflecting this, it was concluded that the current maximum financial penalty should be retained.<sup>763</sup>

### iii. Option 3: do what the farmers want

The discussion in the RIS about the third option is brief relative to the other two options, and the second (voluntary) option in particular. The primary movers for the mandatory option were, as noted by Treasury, the various representative farmers' associations at national and State levels, including the ADF:

<sup>759</sup> Transcript of interview, Graeme Samuel AC, p. 63.

<sup>760</sup> Article 2, *Groceries Code Adjudicator (Permitted Maximum Financial Penalty) Order 2015/722*.

<sup>761</sup> Rebecca Smithers, "'Unfair' supermarkets could face hefty fines under new watchdog", *The Guardian*, 5 December 2012.

<sup>762</sup> Press Release, 'Fines for supermarkets move a step closer' Department for Business, Innovation & Skills, Groceries Code Adjudicator and The Rt Hon Dr Vince Cable, 29 January 2015, <https://www.gov.uk/government/news/fines-for-supermarkets-move-a-step-closer>

<sup>763</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [90]-94].

*They raised concerns that the major supermarket chains may opt-out at a later date; other major retailers may choose not to opt-in; and that the Code does not cover the whole grocery supply chain.*<sup>764</sup>

The precise words of the ADF in their submission were as follows:

*While the Code is admittedly a step in the right direction, ADF believes that it lacks scope and is not sufficiently comprehensive. In this submission, ADF will bring attention to significant gaps in the Code including but not limited to the need for an Ombudsman, penalties, establishing a Code that is mandatory, and an Effects Test.*<sup>765</sup>

Other stakeholders, while favouring a mandated approach, were prepared to concede a voluntary code was better than nothing. This was the tenor of the AMWU's submission, for example:

*As a general proposition we strongly support the introduction of a mandatory code as we believe that the "opt-in" component of the Code is highly problematic. While we consider it an important first step to have the Code prescribed under the Act, the voluntary nature of the Code weakens it considerably.*<sup>766</sup>

In response, Treasury emphasised:

*The Retailer and Supplier Roundtable (RSR) strongly opposed a mandatory code, highlighting that such a move would be inconsistent with the Government's red tape reduction agenda.*<sup>767</sup>

The discussion of pros and cons that then followed identified two pros and two cons, in effect cancelling each other out. Benefits of the third option were greater certainty that all supply relationships would be covered and compliance was mandatory and there was also the 'key' advantage that bound parties would be subject to obligations 'which they would not accept voluntarily.'<sup>768</sup> Costs were that it may not be appropriate to impose mandatory obligations on parties that 'were not directly considered during the initial formulation of the code' (i.e. all retailers other than the MSCs and possibly also Metcash). This could lead to 'unintended consequences' (which were unspecified). Plus there would be higher compliance costs all round – for industry and government.<sup>769</sup>

Tellingly, at this point, Treasury re-emphasised the seemingly irrebuttable proposition that a mandatory code 'would not have the benefit of implicit support by those that are bound, and ... (therefore) may be less supportive of it and less willing to be bound.'<sup>770</sup> As a proposition grounded in the psychology of human behaviour, if not common sense, it is difficult to quibble with this reasoning.

<sup>764</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 26.

<sup>765</sup> ADF submission covering letter, Treasury, FGCC consultation paper, 2014.

<sup>766</sup> AMWU submission, Treasury, FGCC consultation paper, 2014, p. 4.

<sup>767</sup> RSR response to Treasury, FGCC consultation paper, at [2].

<sup>768</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 27.

<sup>769</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 27.

<sup>770</sup> Treasury, FGCC Final Assessment RIS, 2014, p. 27.

But equally it belies the smarts of the MSCs in deploying a collaborative strategy to find a political solution to the problem caused by their own bad behaviour.

## 8. In practice to date

As at the date of writing, the FGCC has been in place for just over two years. An official review looms in 2018. It is appropriate and timely then to stand back and reflect on how the Code has worked in practice to date. In essence the aim of the FGCC is to change behaviour, principally by its retailer signatories but also to some extent the behaviour of suppliers. That reflection gives rise to a number of questions:

- to what extent is there awareness and understanding by suppliers, and those dealing most directly with them on behalf of the retailers, of the existence and provisions of the Code?
- to what extent and in what ways are the provisions of the Code being drawn upon, either directly or indirectly, in the context of supply negotiations and in dispute resolution?
- to what extent is exclusion of price from the Code an issue?
- are there counteracting factors that are detracting from the use of the Code provisions for either of these purposes?
- are there reinforcing factors that are facilitating or supporting the use of the Code provisions for either of these purposes?

Each of these questions is addressed in turn below and where relevant, comparisons with and insights from the UK experience are drawn upon. Such comparisons are elaborated on in the context of the specific purposes of the FGCC and having regard to the upcoming review of the Code in 2018, in the final Part of the report.

### I. Awareness and understanding

It almost goes without saying that for the FGCC to have any impact in practice a crucial precursor is that the representatives of both suppliers and the retailer signatories involved in supply negotiations and disputes are aware of and understand its provisions.

For the retailers, the Code's obligations would have entailed a significant upfront investment of time and resources in internal adjustments, including in relation to the preparation and dissemination amongst their suppliers of the paperwork involved in GSAs, the appointment of a CCM, and perhaps most significantly, in the training of their buying team. According to some, the MSCs got on board with taking the necessary steps and making these adjustments post-haste. Coles is said to have been quicker off the mark in this regard than Woolworths but the latter is observed as increasingly getting with the program:

*...you speak to the senior leadership team within Coles or Woolworths, and I've spoken to both recently, I genuinely believe that they think they are doing the right thing, Coles particularly, and we've been very publicly saying we think Coles have taken this whole code thing way more seriously than what they have, in fact, taken it way more seriously than*

*Woolworths and they've put resources internally in place to be able to manage it, they've trained their staff reasonably well, unlike Woolworths that haven't, so I think they genuinely are endeavouring to take it seriously..*<sup>771</sup>

...

*Well, I think Coles acted quicker and in a more structured way. I think that's happening now with Woolworths...*<sup>772</sup>

...

*Coles have taken that incredibly seriously. And I think Coles was very pleased that the ACCC implicitly recognise that they've taken this very, very seriously. I don't think other supermarkets haven't, I just think that Coles have been a public leader for a bit longer...*<sup>773</sup>

With regard to resourcing implications for the MSCs, we have been told by representatives of both Coles and Woolworths:

*... the cost of implementing the code has been significant. It would certainly exceed the significant multiple that the government estimated, but we have spent half a million dollars on IT systems ...*<sup>774</sup>

*So I think the impact statement said that it was going to cost us \$60,000, something like that. I can tell you that it's probably more the million – two ...*<sup>775</sup>

*... we did the original estimates in good faith, but they were just estimates. And I think they were wildly wrong. We looked at the likely cost of dealing with complaints when they arose, and so on, but if none have arisen, there have been no costs. On the other hand, I would suggest that we dramatically understated the likely cost of training and repeated training, and producing associated materials.*<sup>776</sup>

As one MSC interviewee noted, a new computerised system had to be put in place to monitor and record transactions in line with Code requirements. However despite this, 'you have to record it in writing as well as a requirement of the code, so it is difficult. I mean, a grocery supply agreement is not just a single document.'<sup>777</sup>

In short, when it comes to the increased work load of category managers, we were told that they:

*... needed to spend a lot more time capturing and recording. I think it brings an awareness of what they're doing and what they're saying in their emails and their conversations, which isn't*

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<sup>771</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 33.

<sup>772</sup> Transcript of interview, Gary Dawson 2, p. 8.

<sup>773</sup> Transcript of interview, former senior representative of the UK OFT, p. 24.

<sup>774</sup> Transcript of interview, MSC representative, Coles, p. 17.

<sup>775</sup> Transcript of interview, MSC representative, p. 23.

<sup>776</sup> Transcript of interview, MSC representative, p. 20.

<sup>777</sup> Transcript of interview, MSC representative, p. 17.

*necessarily a bad thing, but it has required enormous expenditure on IT infrastructure, on training.*<sup>778</sup>

By contrast, other retailers reported less disruption or additional expense as a result of signing up to the FGCC:

*... we're just doing training about the code and then investigating alleged breaches of the code but I wouldn't say [work in relation to compliance has] significantly increased.*<sup>779</sup>

In relation to training initiatives specifically, it is apparent that this has been taken very seriously by the MSCs. One MSC representative involved in the Code-related training program in his organisation outlined the measures put in place for this purpose as follows:

*We initially trained some 800 people, which included all of the buying personnel irrespective of what level they were at, plus any supplier-facing person in other parts of the business, such as replenishment, such as marketing, and so on. And that was ... face-to-face training with handouts and takeaways and guides on how to interpret and apply the Code. We then produced an electronic training module, which is an annual refresher, which each buying person has to complete – call it a licence to operate – and it's ... collectively managed and ticked off. We've then done subsequent training, we've done two or three offsite half-day training where we've taken the entire buying team away and we talked about the Code. We've also done [training] business segment by business segment (so [by] meat and produce and deli and so on). [E]ach of those individual training sessions were half a day [sessions with] live examples of the Code, live examples of real life situations, where an interpretation of the Code has been required. And you can workshop that, and then have people express their views and build their understanding through looking at some real life stuff. And we've produced [a] manual [on the Code], and we're just busy reproducing the next edition of the manual. And obviously I talk and meet buying teams on a regular one-on-one basis, [and] on a more ad hoc basis, to talk [to] issues on the Code as well.*<sup>780</sup>

He went on to explain that his organisation also seeks feedback from their suppliers regarding the awareness amongst buyers of the FGCC. He reported that this feedback indicated a high level of buyer recognition of the Code: 'they are very well versed'.<sup>781</sup>

A different representative stated:

*...whenever someone seeks advice from us ... the[se] are really good opportunities to train people because it's the application in a particular situation and in context, which makes everything very real for the buying team. So it's part of our everyday work, compliance work, as well as we obviously have a very structured program. You're not allowed to actually*

<sup>778</sup> Transcript of interview, MSC representative, p. 17.

<sup>779</sup> Transcript of interview, interviewee that consults to / advises grocery businesses, p. 2.

<sup>780</sup> Transcript of interview, MSC representative, p. 18.

<sup>781</sup> Transcript of interview, MSC representative, p. 15.

*operate in a buying role unless you've done the training, hence it's called "licence to operate". And we get the data all the time on particular teams, and whether they've done the training, and so there is actual follow-up.*<sup>782</sup>

These internal messages about the importance of the FGCC are said further to be reinforced by the most senior levels of management:

*I think one of the great things last year, something that really works, is when [names of senior managers] talk to the entire community about these issues, and why it's so important to our business, and why you have to have read the Code back to back as well. But they all do do it. And I think you need that senior management buy-in to really then push it right throughout the organisation, when you are as big as us. I'm sure it would be perhaps a simpler task if you were a bit smaller. But we have to attack it from very many angles.*<sup>783</sup>

For suppliers, again the AFGC has played an important leadership role, in working to bring the Code to the attention of its members and in educating and training them in its provisions. As explained by a director of NextGen, the AFGC's chosen training provider:

*...we started a dialogue with the AFGC about two years ago around the code, there's – they'd identified through observing the UK code that the code in its' own right isn't going to change behaviour unless both manufacturers and retailers truly understand it and manufacturers enforce it to all intents and purposes all – it's not their position to enforce it but endeavour to live and breathe by it forcing the retailer to acknowledge and change behaviour. And one of the learnings was that supplier training was critical so they went to market to look at who could help them, we were chosen as a partner to develop and then deliver the training for Australian suppliers, all of them, and we've subsequently also then worked extensively with those suppliers on adjusting, reviewing, amending their position with retailers in the context of the code.*<sup>784</sup>

Dawson recounts, with some (arguably deserved) pride that all of the 200 members of AFGC are aware of the Code and that across the association's membership, they have had over 2,000 people undertake code training.<sup>785</sup> He also considers that awareness across the broader supplier community would be high 'because the retailers, Coles in particular but now Woolworths ... are working it into more of their communications'.<sup>786</sup>

At the same time, Dawson readily concedes that awareness is much greater amongst larger suppliers than smaller suppliers and this would be consistent with the fact that the majority of the AFGC's

<sup>782</sup> Transcript of interview, MSC representative, pp. 18-19.

<sup>783</sup> Transcript of interview, MSC representative, p. 19.

<sup>784</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 7.

<sup>785</sup> Transcript of interview, Gary Dawson 2, p. 1.

<sup>786</sup> Transcript of interview, Gary Dawson 2, p. 1.

membership are in the former category as well as being companies with their own army of internal and external compliance and legal teams.

At the time of our interview with NextGen they reported that, 'we've trained in excess of 150 suppliers and best part of 1600 individuals and we are working extensively and in detail on their terms with about 35'.<sup>787</sup> By 2017 this number had increased to 258 with NextGen reporting that, 'underlying Code understanding has improved significantly over the past 12 months'.<sup>788</sup> This is reflected in the findings of a 2017 survey conducted by the AFGC, with 89% of respondents reporting that they had a solid understanding of the FGCC, up 15% on 2016.<sup>789</sup> Furthermore, 91.9% stated that their business had now completed the AFGC / NextGen industry training.<sup>790</sup> Moreover, those participating in the training ranged from, 'a small father and son show ... all the way though to ... three training sessions for Coca-Cola'.<sup>791</sup> Smaller suppliers were catered for through full day group training sessions, whereas larger organisations often opted for in-house company-specific training.

Dawson acknowledges that being aware of the Code is one thing, but understanding its provisions sufficiently and having the wherewithal to apply it in actual negotiations is another: 'so there would be awareness that it exists but actually knowing enough about it to work it into their negotiations, probably less so'.<sup>792</sup> This might be contrasted with an account we received from a MSC representative who reported to us that:

*...some very small suppliers who run their own business by themselves, and they may or may not have a legal background, but they can be quite pedantic in terms of some of the particular wording of the Code, such as not wanting us to buy us a free lunch in clause 6.3 or whatever it is. And you go through those things, and you work through everything and it all goes away. The very large suppliers, of course, have significant legal resources and it takes some time to put a GSA together with them.*<sup>793</sup>

NextGen is very cognisant of the underlying power imbalance between suppliers and MSCs in the context of Code-related negotiations. The primary goal of the training therefore is to ensure that suppliers understand the obligations created by the Code and the ways that they can benefit from it, and to teach them to recognise behaviour that should not be considered acceptable. As a NextGen director told us:

*...in the training we use some horrible analogies ... we talk about Stockholm Syndrome in training so we say you've lived in Stockholm all your life, perfectly normal behaviour, and we*

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<sup>787</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 8.

<sup>788</sup> NextGen, 'FGCC – What Should You Be Doing?' presentation to AFGC conference, 2017, slide 4.

<sup>789</sup> AFGC, *Annual Food and Grocery Code of Conduct Survey Report*, 2017, p. 6.

<sup>790</sup> AFGC, *Annual Food and Grocery Code of Conduct Survey Report*, 2017, p. 8. Albeit, this is not surprising given that the survey was conducted by the AFGC of its members.

<sup>791</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 8.

<sup>792</sup> Transcript of interview, Gary Dawson 2, p. 3.

<sup>793</sup> Transcript of interview, MSC representative, p. 15.

*use your mum test, if you told your mum this would your mum say it's normal? Well, no, because she doesn't understand, that's because she lives in London not Stockholm.*<sup>794</sup>

The AFGC recognised parallels between the UK and Australian grocery code experiences, learning from the UK that for such a code to be effective its implementation had to be accompanied by cultural and behavioural change; changes best achieved through education and training.

The UK has a similar, although not identical, champion for suppliers to the AFGC in the British Brands Group. As its director John Noble says, British Brands Group is 'is a trade organisation, it represents brand manufacturers and its mission is all about creating the best climate possible in the UK for brands to be created, sustained and to thrive, bringing their many benefits to individuals, society and the economy.'<sup>795</sup> Funded by membership fees, the primary objective of the Group up until recently has been to champion brands – to commission studies, examine the interrelationship between brands and responsible business, contribute to the media, educate policy makers and the like.<sup>796</sup> However according to Noble this focus has shifted in the past three years and British Brands Group is now 'doing an awful lot of training on GSCOP'. Unlike the AFGC, which outsources this to NextGen, the British Brands Group, 'was the first in the market on GSCOP training'. This in turn has created an alternative revenue stream for the Group.<sup>797</sup> It has also meant a diversification in British Brands Group's membership as increasingly SME suppliers are seeing the benefits for them in a trade association that can help with interpretation and use of the GSCOP, that can 'act as a sounding board [as to whether] there's a breach... provide advice lines and provide a route to the adjudicator if members want to alert her to something but don't want to alert her themselves..'.<sup>798</sup> As another advisor to UK suppliers points out:

*...historically, British Brands Group's members were big multinationals. Actually, what it's done is it's taken this role of champion of the code to some extent, but in doing so, it's also said, look, actually we want to work with suppliers other than our big members. So they've kind of put together more attractive membership packages that are cheaper, that are intended to get smaller people in. They're willing to do stuff without charge for smaller people, run them through their training courses, so that they have tried to reach out in that way, as they see it as a significant issue.*<sup>799</sup>

Noble is clearly passionate about the code training enterprise: 'we want all the suppliers to understand GSCOP and be confident in using it.'<sup>800</sup> According to the British Brands Group website, a full day course includes training on the GSCOP and the reasons it was introduced, what it covers, the implications of the GSCOP for day-to-day trading relationships, the role of the GCA, and advice on

<sup>794</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 11.

<sup>795</sup> Transcript of interview, John Noble British Brands Group, p. 2.

<sup>796</sup> Transcript of interview, John Noble, British Brands Group, pp. 3-4.

<sup>797</sup> Transcript of interview, John Noble, British Brands Group, p. 5.

<sup>798</sup> Transcript of interview, John Noble, British Brands Group, p. 7.

<sup>799</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, pp. 22-23.

<sup>800</sup> Transcript of interview, John Noble, British Brands Group, p. 6.

how suppliers can safeguard against unfair trading practices. More generally, the Group promises to help suppliers 'tip the balance back in their favour'.<sup>801</sup>

Training and education on the GSCOP is also provided through the office of the GCA. In addition, GCA supplier mornings are held regularly, providing an opportunity for Tacon to update suppliers on the work being undertaken by her office and any recent relevant developments, and to answer questions.<sup>802</sup> An annual GCA conference provides further opportunity for updates, education sessions and the chance for suppliers to attend workshops on code-related or other relevant issues. The GCA also regularly publishes best practice statements, case studies and newsletters and, like the AFGC, conducts and publishes results of annual surveys of code awareness and compliance.<sup>803</sup> Unlike the AFGC or NextGen, the GCA also works with the retailers' CCOs. This arguably allows Tacon to close the loop in a way that the AFGC is not able. As Tacon puts it:

*So people anecdotally telling me that there's issues – through feedback from training programs, the survey, listening to suppliers at events means that I can say these are my major issues and talk to Code Compliance Officers and then ask them to report back to me quarterly on what they're doing about these issues.*<sup>804</sup>

This informal process allows Tacon to identify and address key issues early on, as well as act as an intermediary between retailers and suppliers in ensuring there is common understanding of how Code-related issues should be addressed. She also makes use of the media – the trade press in particular – to disseminate as widely as possible information about the GSCOP and how it is working. But she does so in a way that is intended to be constructive and educative, rather than accusatory and critical – for example, Tacon regularly publishes and in turn the media covers case studies of issues that have arisen and which have been resolved in the industry through her intervention. In doing so she will identify the relevant retailer but only with its prior agreement, having given the retailer the opportunity first to review the text.<sup>805</sup> Her approach in this regard appears to won over many in the industry:

*...whenever you see her talking you know she's always very keen to be fair and to the point, she's not emotional or subjective or partisan; I think she's got a very good media position and media voice, and she tends to only engage when she really needs to, so she's not using it willy-nilly here and there...*<sup>806</sup>

*...if you read The Grocer [a reference to a UK retail grocery trade magazine], there's something in there most weeks about her and her activities. She has that kind of publicity and that profile. And again, having an adjudicator who's willing to sort of do that engagement on a regular basis means*

<sup>801</sup> British Brands Group, Full Training: A one-day course designed for direct suppliers to supermarkets at <http://www.britishbrandsgroup.org.uk/grocery/training/full>

<sup>802</sup> News story: GCA supplier mornings, 3 March 2017 <https://www.gov.uk/government/news/gca-supplier-mornings>

<sup>803</sup> See GCA website <https://www.gov.uk/government/organisations/groceries-code-adjudicator>

<sup>804</sup> Transcript of interview, Christine Tacon, p. 27.

<sup>805</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 29.

<sup>806</sup> Transcript of interview, John Noble, British Brands Group, p. 42.

*you get that profile on an ongoing basis that you can't get if the OFT had it or if the CMA had it. They just won't do that, they can't do that.*<sup>807</sup>

The education, training and profile-raising initiatives of the GCA were resoundingly endorsed in the recently completed review reported on in July 2017, even if it was noted that there was still work to be done amongst suppliers, in respect of which there appeared to be an expectation that trade associations would do more to contribute to GSCOP training of their members.<sup>808</sup>

## II. Using the Code

Early assessments by some are that the FGCC's provisions relating to the negotiation of terms and conditions of supply have had an impact. For a start, it immediately changed the rules of the game, particularly as to unilateral and retrospective variations which are now off limits (at least in certain circumstances), and key interviewees reflected in general terms on how this was changing the behaviour of buying personnel:

*...the effectiveness of the voluntary code is the extent to which it influences behavioural change or drives the behavioural change ... Now, obviously we won't know that for some years probably but there's some evidence of it changing already. Very encouraging signs ... within the retailers already...*<sup>809</sup>

*So the two things that we co-defined in principles and in the provisions of the code, was to prevent unilateral action and retrospective action. So that fundamentally changed the behaviour of the retailers.*<sup>810</sup>

At the same time it is apparent that behavioural change by buyers is not just being driven by the requirements of the FGCC, but by MSC senior management who regard the principles of the Code as consistent with an overarching strategy to improve supplier relations. As one senior MSC representative told us:

*... the code principles that are there, and the prescriptive bits that go with it that are in there, are a base operating premise that is something short of where we want to be as a business anyway in the normal course of everyday trading. So they state fundamental principles that were no different from our internal code of conduct that every buyer signs and every staff member signs, and had signed, up until that date, to have it be fair and reasonable and dealing with suppliers in the proper manner. So the Code wasn't doing or setting anything that wasn't already at least a minimum standard that we expected of ourselves.*

...

<sup>807</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 21.

<sup>808</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [69]-[72].

<sup>809</sup> Transcript of interview, Gary Dawson, p. 44.

<sup>810</sup> Transcript of interview, Robert Hadler, p. 27.

*I'm not sure it has done anything to change Aldi's mode or method of growing the market either, because they equally look to have open, clean and very efficient relationships with their suppliers. So I'm not sure that the Code cost them anything in terms of joining, nor would it change their behaviour necessarily if they left.*

*... To some extent, if we opted out of the Code tomorrow, it wouldn't probably change the practices that we've now embedded in our business, the principle of everything being agreed in advance, everything being agreed in writing, right, and no unilateral changes to anything, of course. We should be operating that way anyway, so we wouldn't necessarily change.<sup>811</sup>*

Even if, as suggested by this account, the FGCC is superfluous given pre-existing or current strategies by retailers in relation to suppliers, it does appear to be playing a useful reinforcement role. Further, it is evident that MSC management are taking steps, not just to ensure their staff are aware and understand its provisions, but to enforce it internally:

*...we are – and the business is all over the Code. So you do get in a bit of trouble if you are not doing the right thing or perceived to not be doing the right thing.<sup>812</sup>*

According to Dawson at least, the behaviour shift at the coal face is not just on account of rules in the Code but, significantly, due also to the threat of escalation to the CCM. This manager is independent of the buying team and, under the Code provisions, the designated first port of call for suppliers who have grievances that have not been possible to resolve by direct recourse to buying personnel:

*... what we've found is that the, dare I say, the, not the, well, the threat, the suggestion that if this particular issue is not resolved we might have to take it to the code compliance manager is generating quite a visceral reaction amongst the relevant supermarket staff.<sup>813</sup>*

This appears to be supported by the approach taken in supplier training by NextGen's in which the importance of including the language of the Code in their communications with the MSCs, words such as 'good faith', 'reasonable', 'timely', etc.<sup>814</sup> is emphasised. Interestingly, accounts from MSC representatives suggest that not only are suppliers increasingly willing and able to draw on Code provisions in their dealings with buyers, and do so in an appropriate way, but that there are some seeking to use it in ways that were never intended. This is hardly surprising, they reflect:

*... I do think that suppliers do feel quite empowered with the Code. They are quite quick to raise it ... and often probably not quite in the right circumstance. But ... we'll look at it and go, mmm, but let's see what the issue is and make sure we can resolve it.<sup>815</sup>*

...

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<sup>811</sup> Transcript of interview, MSC representative, p. 5.

<sup>812</sup> Transcript of interview, MSC representative, p. 14.

<sup>813</sup> Transcript of interview, Gary Dawson, p. 54.

<sup>814</sup> NextGen, 'FGCC – What Should You Be Doing?' presentation to AFGC conference, 2017, slide 11.

<sup>815</sup> Transcript of interview, MSC representative, p. 14.

*... if you think of the number of sellers in the market and there's many thousands of those... some may understand [the Code], but others might not, but think it's a point of leverage and use it for purposes that it wasn't intended for. So, I think, it's better understood and lived up to by everybody that's in the trade today than it ever has been and that will continue to ... improve as time goes by. But not everybody thinks about it the same way. Like any piece of law or regulation, some people think it's there to serve a different purpose than ... what I might think it's there to serve.<sup>816</sup>*

In addition, it is apparent that suppliers are benefitting from the transparency and certainty that is the result of having a GSA provided for by the FGCC. Suppliers can now proceed on the basis that:

*... if you've agreed to a set of trading terms and you've agreed to it and you've signed it, that that's it. There's nothing else over and above. So you will deliver this and we will deliver this for you. At this cost. So you've got a signed set of trading terms, I suppose.<sup>817</sup>*

Dawson, in particular, is buoyed, in a measured way, by signs that suppliers have grown in confidence in their negotiations. He puts this down to suppliers now knowing that there are standards that apply across the sector, standards that can be insisted upon, not as a matter of special treatment for the individual supplier but as a matter of universal application dictated by the Code. In terms of the 'massive information asymmetry' as between retailers and suppliers in the industry, the increased transparency and predictability resulting from the Code is 'shifting the dial a bit in the right direction.'<sup>818</sup> In the first year after the Code having taken effect, he recounted as follows:

*... we've had a lot of anecdotal feedback of small and – small through to large, really, companies utilising it in those negotiating discussions and because if you think about it, previously – particularly as a small supplier, I've got no visibility of what happens in this room if all my competitors are in here, all I know is what I'm selling and what they're telling me in terms of what they're buying. Now of course you've got quite a bit of insight into what happens across the industry because it's detailed there and you've also got stronger grounds to push back and say, well, no, I don't think that's reasonable. Now, will all suppliers feel confident in using it? Well, of course not and will it work in every case? No..<sup>819</sup>*

A year on (in our second interview with him), Dawson's account was much the same – the Code is giving suppliers the capacity and basis on which to push back in negotiations with buyers. Although it is taking time (as might be expected), increasingly suppliers are working out how the terms of the FGCC relate to the specifics of the terms negotiated with their buyers – they are really starting to see its 'practical relevance'.<sup>820</sup>

<sup>816</sup> Transcript of interview, MSC representative, p. 15.

<sup>817</sup> Transcript of interview, CEO of MGA, p. 23.

<sup>818</sup> Transcript of interview, Gary Dawson, p. 48.

<sup>819</sup> Transcript of interview, Gary Dawson, p. 44.

<sup>820</sup> Transcript of interview, Gary Dawson 2, p. 4.

This is further supported by NextGen's finding that the number of trading terms reviewed in light of the FGCC increased to 83 in 2017, up from 37 the year before. Outcomes from these reviews included the re-negotiation of waste charges; the re-negotiation of freight charges, improvement in payment terms, agreement to change listing decisions; and increased notice being given on deletions and decisions on deletions being reversed.<sup>821</sup>

However there is still room for improvement. NextGen reported that while some buyers were doing better with their range review criteria this was 'still hit and miss'; quarter, half and year end 'asks' were still happening; and there were still reports of, 'ambiguity around retrospective claim time frames'.<sup>822</sup>

Despite the increased level of awareness about the FGCC reported in the recent AFGC survey, only 61% of supplier respondents knew who the CCM was at Woolworths, with this number dropping to 54% for Coles and 24% for Aldi. However, this was up from 41.2 and 45.1% respectively with regard to the CCMs for Woolworths and Coles in 2016.<sup>823</sup> Perhaps more importantly, the AFGC survey report found that suppliers are still hesitant to raise issues with CCMs, and that where they have done so, the outcomes (according to the survey respondents) have not always been satisfactory.<sup>824</sup>

Survey responses regarding retailer code compliance also were not consistent. Woolworths appears to have improved their compliance since 2016, however less than 60% of those surveyed felt that Woolworths consistently or mostly conformed to the Code. And while Coles fared better at around 65% compliance in 2017, this was drop from 80% the year before. Perceptions of Aldi's compliance have fluctuated; however by 2017 they were seen to be on par with Coles.<sup>825</sup> By contrast, while buyers' knowledge about the Code was shown to have improved when compared to the 2016 survey results, on average only just over 10% of respondents reported that any retailer had a 'very good' understanding of the FGCC.<sup>826</sup>

Dawson emphasises that it is the Code's provisions relating to supply agreements and retailer conduct that are most being taken out for a run, the provisions as to dispute resolution less so:

*...I don't think there's a lot of activity at the dispute resolution level. I'm not aware of any, to be quite honest. There may be some but I'm not aware of it. There haven't been a lot of complaints referred to the ACCC or inquiries. So the feedback we get is that it's being used mostly commonly and most effectively at the negotiating level, which is pretty much what we expected.*<sup>827</sup>

There have been similar accounts of the effect of the GSCOP in the UK. The head of British Brands Group observes, for example, that since the Code's introduction retailer buyers are:

<sup>821</sup> NextGen, 'FGCC – What Should You Be Doing?' presentation to AFGC conference, 2017, slide 5.

<sup>822</sup> NextGen, 'FGCC – What Should You Be Doing?' presentation to AFGC conference, 2017, slide 6.

<sup>823</sup> AFGC, *Annual Food and Grocery Code of Conduct Survey Report*, 2017, p. 9.

<sup>824</sup> AFGC, *Annual Food and Grocery Code of Conduct Survey Report*, 2017, p. 10.

<sup>825</sup> AFGC, *Annual Food and Grocery Code of Conduct Survey Report*, 2017, p. 11.

<sup>826</sup> AFGC, *Annual Food and Grocery Code of Conduct Survey Report*, 2017, p. 12.

<sup>827</sup> Transcript of interview, Gary Dawson, pp. 2, 3.

*...more wary, more responsive. In the negotiation if ever there is a hint of GSCOP coming up then I think alarm bells ring in the buyer's ears. This really puts them on notice that they've got to be very careful about this.*<sup>828</sup>

However, he also observes that the change has been particularly notable since the appointment of the GCA:

*And definitely you see the changes that have been happening since Christine's powers came in. It's been really quite dramatic. I would point to the fact that there had been no arbitrations before she was appointed, the previous code was found not to work and nothing happened really between 2010 and 2013. Then as soon as she arrives we saw things change. It would be interesting to look at how code compliance officers changed because my sense is that they suddenly became more senior, more influential within the companies. The code compliance officer was now on the line. I think you can see just through the code compliance officer approach and how code compliance office departments have been staffed how seriously the Code was and is being taken.*<sup>829</sup>

In Australia, Dawson is also confident about the role of the CCMs. As mentioned above, from his observations, suppliers are becoming 'more willing or more open' to using that channel, again largely as a mechanism for obtaining added leverage in negotiations. That, he quite rightly observes, is a notable development 'because traditionally they have been very wary about – because of the relationship prior – very wary about any other channel, let alone going to the ACCC'.<sup>830</sup> In a similar vein, another interviewee points out:

*... the point at which you start using code language is the point at which it is likely to maybe get taken a little more seriously purely because, if they don't, the likelihood of it getting reported internally increases and the buyer doesn't want to get reported internally.*<sup>831</sup>

These positive signals should not be taken to suggest, however, that there are not ongoing issues and concerns, including ones that are meant to be headed off by the Code. Dawson cites delisting (and the associated question of category average margin), 'paying for positioning' (in the context of so-called range reviews), and early settlement discounts as examples of issues about which there is a degree of consternation at present, and is aware that the ACCC is looking into at least some of these. According to NextGen, there are also 'quarter, half and year end "asks" still happening and 'ambiguity around retrospective claim time frames'.<sup>832</sup> In his customarily understated and careful way, he describes the situation on such matters as 'an ongoing discussion ... [involving] a bit of back and forth

<sup>828</sup> Transcript of interview, John Noble, British Brands Group, p. 37.

<sup>829</sup> Transcript of interview, John Noble, British Brands Group, p. 37.

<sup>830</sup> Transcript of interview, Gary Dawson 2, p. 4.

<sup>831</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 29.

<sup>832</sup> Neil Rechlin, 'FGCC - What Should You Do?' presentation to AFGC conference, 2017, slide 6. But he also acknowledges progress on renegotiation of waste charges and freight charges, improvement in payment terms compliance, a significant reduction in claims, agreement to change listing decisions and increased notice on deletions and decisions reversal.

around interpretations of what the code provisions mean and should mean'<sup>833</sup> (an account that highlights lawyers as beneficiaries of the Code as much as anyone...).

On the issue of delisting, for example, this practice is permitted under the Code but only for 'genuine commercial reasons'.<sup>834</sup> This raises the issue of what might constitute such reasons. According to the FGCC provisions, these include a failure by the supplier to meet agreed quality or quantity requirements; a failure of the product to meet the retailer's commercial sales or profitability targets, as notified to the supplier in the GSA; or a persistent failure on the part of the supplier to meet the retailer's delivery requirements as set out in the GSA.<sup>835</sup> Of particular concern is whether these provisions legitimately include failing to meet 'category average margin' and if so, how that margin is calculated. It is stipulated in the Code that 'delisting as a punishment for a complaint, concern or dispute raised by a supplier is not a genuine commercial reason.'<sup>836</sup> Such matters are currently the subject of an active dialogue between at least some suppliers and their buyers, he reports, and it is evident that they are matters that the ACCC is looking into also.<sup>837</sup> Dawson postulates that once this issue has been ironed out it would have been the Code that in effect resulted in rewriting the rules on delisting.

Delisting and range reviews were also the subject of the ACCC's 2017 audit of compliance with the FGCC, and the 2017 AFGC survey of its members previously referred to also highlights issues with these practices as being of ongoing substantial concern, together with issues relating to requirements to fund retailer margin shortfalls, requirements for lump sum payments over and above what had been agreed, and excessive retailer charges.<sup>838</sup> Consistently with the survey findings, the ACCC audit revealed a range of issues relating to the failure to give suppliers reasonable notice of delisting, not providing genuine commercial reasons, and not advising suppliers of the right to have the delisting decision reviewed.<sup>839</sup> A MSC representative explained to us what this involved from their perspective, an explanation suggesting that as perceived by this organisation, current delisting issues are more in the nature of issues with form rather than substance:

*[The ACCC] asked for the records of the last 20 range reviews that we've done, and they looked at how well we had conducted those and communicated those, and done the various steps on time and effectively. And we found issues and faults where we had written ...matters that weren't necessarily precisely containing the right words that they should have. We had one part of the process that was reliant on a system notification that went to, when we stop buying a product from the supplier, and that became also the notice of delisting to the supplier, so that didn't leave sufficient time. Notwithstanding the fact we'd had that*

<sup>833</sup> Transcript of interview, Gary Dawson 2, p. 6.

<sup>834</sup> FGCC, cl 19(1)(b).

<sup>835</sup> FGCC, cl 19(2).

<sup>836</sup> FGCC, cl 19(4).

<sup>837</sup> Michael Schaper, Deputy Chair (ACCC), 'Current Food & Grocery Issues: An ACCC Perspective', presentation to AFGC conference, 2017, slide 9.

<sup>838</sup> AFGC 2017 Annual Food and Grocery Code of Conduct Survey, pp.17-18.

<sup>839</sup> Michael Schaper, Deputy Chair (ACCC), 'Current Food & Grocery Issues: An ACCC Perspective', presentation to AFGC conference, 2017, slide 10.

*conversation and discussion with the supplier beforehand, we hadn't necessarily had it in writing, and we hadn't – we've done so with a notice of the right to review by a senior manager. So some of those were running late. So there were some technical points like that. None that said that we hadn't done the thing in a fit and proper manner, just that we hadn't necessarily executed it 100% right in a number of instances out of the 20.<sup>840</sup>*

Uncertainty and debates concerning the meaning and correct application of the wording of the Code's provisions are perhaps not unexpected in this early phase, and it can also be anticipated that these are issues that will be ironed out over time. Certainly this is borne out by the UK experience. Surveys conducted by the GCA show consistent falls in the proportion of suppliers experiencing issues with the language of the Code. In 2016, the proportion had decreased from 79% in 2014 and 70% in 2015 to 62%, albeit notably still a high percentage even after seven years of the GSCOP.<sup>841</sup> The top three issues with respect to the Code provisions concerned delay in payments (30%), variations of supply agreements (26%) and compensation for forecasting errors (25%).<sup>842</sup>

Again, arguably with some merit, Dawson makes the point that it is the Code that has provided the platform for the airing and testing of matters that previously have been 'difficult to raise or impossible to raise' and, if raised by a supplier, have been 'just dismissed'. Indeed, the very process of entering into GSAs, as required by the Code, gave suppliers the opportunity to raise or revisit 'a whole raft of things'<sup>843</sup> that previously had simply been prescribed unilaterally by buyers or left open, to be changed as and when buyers saw fit. In the UK it is evident that there has also been an ongoing process of interpreting and clarifying the practical implications of the code in that jurisdiction. A compliance manager with whom we spoke at one of the major retailers saw this as 'inevitable with any piece of legislation'.<sup>844</sup>

A more critical assessment from another commentator, also close to current developments, is that there are some 'issues live right now that are absolutely 100% provable as breaches of the code – 100%'.<sup>845</sup> For him it is not a matter of interpretation, it's black and white: some retailers on some issues are flagrantly in breach. The issue of early settlement discounts and late payments is, for him, a 'case study' of this:

*... so suppliers give the retailers a percentage off invoice discount for early settlement, so I give you 2% discount off invoice for you to pay me in 14 days, so when would you expect they get paid? Fourteen days? Oh, you fool. In Stockholm we'll pay you in about 40, but we'll take the 2% as well, okay. So you think it would be fairly straightforward, I give you 2%, you pay me in 14, if you don't pay me in 14 I don't give you the 2%, but if you don't give me 2% I'm going to delist you for a start so your call. So, and this is not just one or two suppliers, this*

<sup>840</sup> Transcript of interview, MSC representative, pp. 22-23.

<sup>841</sup> News story, GCA achieving significant progress for suppliers, 27 June 2016, <https://www.gov.uk/government/news/gca-achieving-significant-progress-for-suppliers>

<sup>842</sup> GCA, *GCA Annual Survey Results 2016*, YouGov, p. 20.

<sup>843</sup> Transcript of interview, Gary Dawson 2, p. 6.

<sup>844</sup> Transcript of interview, compliance manager at a major UK retailer, p. 25.

<sup>845</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 46.

*is 99% of suppliers that have got either agreed payment days and or early settlement discounts in place that aren't paid on time.*<sup>846</sup>

Not unexpectedly, when we raised the topic of late payments with our MSC interviewees, we received a somewhat different perspective, explaining that this was an issue that mostly arose with small suppliers who are still using paper invoices:

*Obviously, suppliers have been raising issues. We haven't had a lot, but with newsagents in particular, people ... who hadn't gone digital and who would deliver an invoice, say, with their block of papers to a petrol station, have had trouble getting their payments on time. So they might be on seven-day terms, for example. That's quite hard, actually, practically, when those invoices can get lost. And they don't often have Internet access. ... And so we've had some concerns around paper-based suppliers in particular.*<sup>847</sup>

Referring to the recent report by the SBF E Ombudsman on the late payments problem for suppliers generally,<sup>848</sup> the same MSC representative went on to say:

*...that was a good opportunity for us to review how are we are going in this important area. We do understand that from a cash flow perspective for smaller suppliers we need to get this right. And there's still work to be done. We identified this in terms of our processing. ... Also, in reality I think, payment terms have stayed the same for a long, long time. And it was a good opportunity with people shining the torch on it as it were for us to go, hang on a second, yes, we still do have these people in the paper-based world; what can we do to help them, when ideally we would like them all to be digital, because then we can process everything more quickly.*<sup>849</sup>

### III. Exclusion of price

Whether or not the issues described in such accounts are a matter of interpretation to be worked out over time, thereby clarifying for all the scope and effect of the Code, it is clear that there remain aspects of the supply relationship that the FGCC does not and cannot touch and that this is seen as highly problematic. Price and price increases over time are the most obvious of these. In a report of findings from the recent AFGC survey of suppliers regarding the FGCC, previously referred to, it was noted that, '[w]hilst price is not included in the FGCC it was raised by multiple respondents as a significant issue for members'.<sup>850</sup> The price at which a retailer will buy from a supplier does not feature anywhere in the Code, and deliberately so. On the one hand, this is hardly surprising. Were the situation otherwise, it would have been tantamount to price fixing - by regulation, no less – and could have the effect of increasing prices for consumers. For these reasons, Dawson makes it clear, the ACCC was opposed to any suggested inclusion of price in the Code from early on:

<sup>846</sup> Transcript of interview, director of a consultancy that advises suppliers, pp. 46-47.

<sup>847</sup> Transcript of interview, MSC representative, p. 24.

<sup>848</sup> SBF E Ombudsman, *Payment times and practices inquiry: Final report*, April 2017.

<sup>849</sup> Transcript of interview, MSC representative, pp. 25-25.

<sup>850</sup> AFGC 2017 Annual Food and Grocery Code of Conduct Survey, p. 21.

*... the fact that you don't have anything in here about price is quite deliberate.*

*It came up, certainly there is some of our members who felt it should extend to that, but I think it was pretty clear in the discussions we had with the ACCC that, well, an industry code really can't go to something that is a matter rightly for commercial negotiation between two parties and, so for us in here that was quite a clear distinction in our minds so we weren't confused about that, but it's obviously an area where there's a lot of tension as you would expect in a dynamic market.<sup>851</sup>*

As another interviewee explains:

*... the code doesn't specifically touch on price because the code is the – is now fully administered by the ACCC, the ACCC have a very simple remit which is to do right by consumers in Australia. If this were – if there were a mechanic within this to facilitate suppliers or retailers or both to put their prices up that would arguably be contra to what the ACCC is trying to do, they're trying to increase competition and protect the consumer's rights, so having something in here that enables prices to go up or indeed price – legal ability to put prices up just wouldn't sit logically and comfortably with the ACCC's remit, totally understand and get that. So hence there's nothing in here at all about price increases.<sup>852</sup>*

The situation pertaining to price is the same in the UK. It is not covered by the GSCOP. As the GCA explained in our interview with her: 'our Code doesn't have anything to do with price... since when has this country ever interfered with pricing!'<sup>853</sup> She cited this as one reason against extending the Code to primary producers as indirect suppliers to retailers, pointing out that 'my role has nothing to do with price ... if you extend it [the Code and her role], down to the primary producer [as some commentators have been calling for], it still has nothing to do with price. And, actually, the primary producer's main concern is the price.'<sup>854</sup>

On the other hand, it needs to be acknowledged that, for suppliers, price is a significant omission from the FGCC, whether for good reason or not, and it strikes at the heart of the question whether, in the current climate, there are sufficient incentives for ongoing supplier investment and innovation. As one of the experienced supplier consultants we interviewed told us:

*... if you go to speak to a number of suppliers and you say, right, give me your top 10 – the list of top 10 things that cause you sleepless nights and angst. There'll be things around supply chain changes, changes to promotional plans, range reviews, the top of that list will be the ability to generate price increases over time so that it's often the single biggest issue that suppliers wrestle with, they've not been able to get a price increase through...the retailers are pushing very hard now for zero price increases, so I've seen in writing from retailers unnamed*

<sup>851</sup> Transcript of interview, Gary Dawson, 2016, p. 41.

<sup>852</sup> Transcript of interview, director of a consultancy that advises suppliers, pp. 16-17.

<sup>853</sup> Transcript of interview, Christine Tacon, pp. 5-6

<sup>854</sup> Transcript of interview, Christine Tacon, pp. 5-6. See also Transcript of interview, compliance manager at a major UK retailer, p. 18: 'It does not cover price, and the biggest concern, for example, in the dairy world is what is the price of milk?'

*that they will accept your new products if you commit to, a, no price increase under any circumstances for the next two years and any subsequent price increase that goes through that they agree to allow you to put through, all of the cash generated out of that price increase must be reinvested back into that retailer. ..The code doesn't address price increases ... so as a result you're sitting there as a supplier going, right, I've been smashed over the head anyway to give the lowest possible price on this new product, this innovation, I now can't put any price increases through for two years and any subsequent price increases they deign to approve, all of the money I make doesn't pay for my increased cogs, it goes back to the retailer as promotional funds or whatever it might be. So to all intents and purposes I can never generate a material offset against cogs increases or indeed a profit increase so why would I innovate, why would I bother innovating in – in fact the only way this is going to make sense is for me to offshore manufacturing. So I think this is the crack in the dam that potentially will force ever more suppliers to go, you know what, it's just not worth my while investing in innovation, creativity, I'll just offshore it to Indonesia, to India, bring it in on a ship, sell it under contract and be done, there's only 20 odd million people in Australia, who cares? Which is bad for us.<sup>855</sup>*

And from another experienced advisor to suppliers, emphasising again the significance of the challenges facing suppliers in securing price increases:

*There is a point, a very important point, it is not in the Code at all. And that's about the price increase. So many companies are struggling like hell because they've not been able to put any price increase in the market for two, three, four, five years. So they are suffocating. So sometimes it's not only the big Woollies or Coles pushing you or bullying you. The fact that they just said no to price increase, what do you do? How do you fight it? So there could be a point on the Code. But again, what could that be? Because at the end of the day, the commercial principle is very simple. If you buy and sell here, we need to agree on two things. We need to agree on the what, for that service or whatever, and the how much. You cannot have somebody coming from the sky and saying, I decide the price and you have to accept the price.<sup>856</sup>*

Dawson does not shy away from the reality that 'the biggest issue' facing not just suppliers, but retailers as well, is 'the relentless pressure just to stay competitive – retail price, deflation and rising costs.'<sup>857</sup> On this front, he freely admits that the Code has no bearing and will not ease the pressure. But he is sanguine: 'there are things the code can do and there are things the code can't do and I think we have been clear on that from the start.'<sup>858</sup> He concedes that 'plenty' of the AFGC's members wanted price dealt with in the Code but, realistically, that was never on the table. Leverage on price is in effect down to the individual supplier and the extent to which it is able to stay ahead on

<sup>855</sup> Transcript of interview, director of a consultancy that advises suppliers, pp. 12-14.

<sup>856</sup> Transcript of interview, experienced advisor to suppliers, p. 42.

<sup>857</sup> Transcript of interview, Gary Dawson 2, p. 10.

<sup>858</sup> Transcript of interview, Gary Dawson 2, p. 10.

understanding of consumer preferences and trends, and sufficiently differentiate its product in the eyes of consumers and in turn retailers – the Code ‘can’t do all the heavy lifting’! Take for example this supplier’s pragmatic approach to the pricing of his premium brand product by the MSCs:

*So we’ve always been in and out of supermarkets because we’re premium. What happens is our product sells very well, even at a premium because it’s not expensive anyway. What’s the difference for a lot of the consumers between paying, say, for example, \$5 ... and paying \$9 ..., even though the percentage difference is large, to a lot of consumers it doesn’t matter if they like what they see. But because we’re at the high price point, being de-ranked from one of the supermarkets, and the other one will pick us up and then we’re there for a while, then we get de ranked from them. So because we won’t exactly sell to their price points we move in and out. So within that context we do well in the commercial markets but they can always find a cheaper product to put in, instead of our product, in a supermarket shelf to a slightly different market.<sup>859</sup>*

...

*... consumers go chasing brands so you’ll see that when either supermarkets or mass merchants go completely no-brand, they do well for a while because they get extra margin or extra profit on their private label, but then the foot traffic falls away. So then they’ve got to bring brands back in to bring people back into the stores, and the supermarkets oscillate from that all the time.<sup>860</sup>*

As a former Managing Director of a major consumer goods manufacturer (now a consultant to suppliers) sees it, the key is for suppliers to realise that they have power in their relationship with the MSCs, and to learn how to use that power effectively when negotiating with buyers:

*So the key concept, the fundamental thing is, the balance of power is not related to the relative size. I’m not saying it doesn’t count, of course it counts. But it’s not that important. What’s important is the concept of relevance and uniqueness.<sup>861</sup>*

He also has been quoted as saying:

*Suppliers need to understand what they are facing. Don’t wait for the code to save you, but adapt your business to the balance of power model now.<sup>862</sup>*

An appreciation of this imperative was reflected in the comments of a representative from a large supplier to one of the MSCs. When asked about imbalances in bargaining power and the role of regulation in redressing it, he said:

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<sup>859</sup> Transcript of interview, CEO of major packaged goods supplier to the MSCs, p. 6.

<sup>860</sup> Transcript of interview, CEO of major packaged goods supplier to the MSCs, p. 9.

<sup>861</sup> Transcript of interview, former managing director of a major consumer goods manufacturer, p. 17.

<sup>862</sup> Sue Mitchell, ‘Grocery code won’t save suppliers, says former Kellogg boss’, *SMH*, 13 March 2015.

*If you are in a position of strength, clearly you have the balance of power. If you utilise the essence you have, whether it be brand, investment, all the tools of the trade we have. Conversely, if you don't that's where it becomes very difficult. Now the regulatory intervention to help small suppliers, I think in a lot of cases is there to support either poor structural businesses, poor business behaviour, or just lack of knowledge of the way things work, and the way you can reshape your business to give you back the balance of power in a negotiation. We've learned that over time. We've learned through many adversarial negotiations that haven't gone well, that we have to reshape our approach and reshape our either investment strategy or ways of working with [our MSC] and all our other business partners. And so that's something that regulatory influences don't really have an impact on. It's how you learn as a business and how you evolve your business.<sup>863</sup>*

Similar advice is dished out by another advisor to suppliers, this time in the UK:

*I don't believe that this code can be a panacea to everything. It won't be and I think [there needs to be] some expectation management for everybody in the industry, which is to say, look - you still live in a competitive world. You're still going to have trade hard. You're still going to have negotiate hard and nobody is going to give you a free pass on any of this stuff. You still have to do all of that.<sup>864</sup>*

Reflecting on the lobbying for indirect suppliers to be included in GSCOP (just as it was with the FGCC), a UK commentator is also accommodating of the exclusion: 'it's just simpler ... [and] if there's an effect on indirect suppliers, you ought to see the pull through from direct suppliers. But you can't fix the whole world!'<sup>865</sup>

Moreover, price is an issue that, for suppliers, will be affected not just by the size and power of the MSCs as buyers (matters which the FGCC cannot alter), but will also be affected by the degree to which suppliers have access to and are competitive in export markets which in turn will depend to some extent on the dollar. In addition, the nature of the product and its stage in a product cycle will be material. As a MSC representative explained to us, suppliers that have products in high growth categories marked by innovation will be in a materially different position to those that are in 'the commodity category that's very low growth, very low innovation'. 'The nature of the relationship [between the supplier and its buyer] will depend ultimately [on] whether the category's growing or whether the supplier has got great brands or bringing some innovation [to the retailer]'.<sup>866</sup>

That said, Dawson notes an expectation of a return to food inflation in the UK in coming years, if not this one, and it could be significant, 3-4%. This will be driven, he says, by the fact that the retailers are 'needing some topline growth'.<sup>867</sup> He points out that as there is not much more margin, if any, to squeeze out of suppliers, that (at least according to his anecdotal feedback), 'price rises are being

<sup>863</sup> Transcript of interview, senior representative of a larger supplier of packaged goods to the MSCs, p. 33.

<sup>864</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 44.

<sup>865</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 43.

<sup>866</sup> Transcript of interview, MSC representative, p. 28.

<sup>867</sup> Transcript of interview, Gary Dawson 2, p. 14.

approved commonly' (a possible reference to some tacit coordination as between the MSCs) and he wonders aloud whether Australia will follow a similar inflationary trajectory...

*...most of our retailers are populated with senior executives from the UK. They do watch the trends in the UK and that's what I mean about the unknown around that competitive piece at the moment with Woolworths getting momentum back having invested a lot in price, sacrificed margin, which way does it go? Do they simply both of them try and claw back - do the traditional thing, claw back margins from their suppliers or do they look to, I guess, repair that margin in other ways?<sup>868</sup>*

Over time, Dawson also accepts that the Code will only continue to remain relevant if it is adapted and refined to reflect and deal with actual behaviours in the marketplace and changes in these over time. Those behaviours in turn, and the degree to which they matter to suppliers, will be affected inevitably over the long run by structural shifts. In respect of the latter, this is not just a matter of continuing encroachment by Aldi on MSC market share or even the entry of other discounter retailers or a second wholesaler, as has been foreshadowed in the press.<sup>869</sup>

Looking even further ahead, there will be the disruptive effects of e-commerce which has been slower to date to affect grocery than other retail markets in Australia. In the UK, there will be the impact of currency change post-Brexit.<sup>870</sup> And perhaps more in the medium to long term there will be Amazon – the talk of many across the country in the retail sector at large. 'That's certainly one to watch... and probably the biggest influence on the market to come', Dawson observes. It will cut out the retailer, facilitating direct relationships between suppliers and consumers, and it will also generate for Amazon if not also the suppliers who use its platform, a significant new source of consumer data that to date suppliers have had to in effect pay retailers for. These are dynamics that, for Dawson, 'changes the equation.'<sup>871</sup> The same observations are made of developments in the UK:

*We actually had a major UK retailer come in here and speak two or three weeks ago. And what came across very vividly listening to him, they are dealing with an industry that needs significant reshaping to deal with the new world and the new consumer preferences. So they have a base of large stores, designed for a world where people did a once a week big shop in a big supermarket. We're now in a world where a pretty high proportion of UK customers order groceries online and then top up in convenience stores. And it just means a very radical reconfiguration - and if you think, if you then track that back to the supply chain, well that means much smaller ranges, much more complicated distribution chain. It's a different thing. You'll see a whole different set of problems play out.<sup>872</sup>*

<sup>868</sup> Transcript of interview, Gary Dawson 2, p. 14.

<sup>869</sup> See Madeleine Heffernan 'Aldi's arch rival Schwarz Group confirms Oz interest', *The Age*, 21 November 2016; Madeleine Heffernan, 'Australia set for a new grocery wholesaler', *SMH*, 6 June 2016.

<sup>870</sup> Transcript of interview, compliance manager at major UK retailer, p. 26.

<sup>871</sup> Transcript of interview, Gary Dawson 2, p. 13.

<sup>872</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 45.

## IV. Counteractions

Despite these mostly positive reflections on the early impact of the FGCC on both retailer and supplier attitudes and behaviour, there are also grounds on which optimism is to be tempered.

### (a) Code confusion

First, there are some who point to a degree of confusion amongst smaller suppliers, those whom the Code was particularly intended to benefit, and who do not have the back up of in-house and/or external lawyers to sort through the maze of 'rules' that now apply to matters that for a long time have been dealt with through informal conversation and a handshake.

For a layperson, the Code itself is hardly a readily digestible resource – some 36 pages and 42 clauses of dense legislative-style text. Sensitive to the 'difficult challenge' that this represents for suppliers (for those new to the business in particular), we were told by a MSC representative that:

*We take a great amount of care in ensuring that both the conversations we have with suppliers when they are setting themselves up, and the written covering letter that we send out to them, say "go and get all of the advice that you need, take whatever time you require to be comfortable with this and go through it". And we recognise the fact that there's some 15 pages there of a written agreement. And a lot of them do take sufficient care, and a lot of them, even the small suppliers, use their solicitor to have a look and come back with particular questions. ...*

*... [C]umulatively it can take me five or six hours to negotiate a GSA agreement ... But it works on backwards and forwards; one day, two weeks later you're doing the next bit, and so on and so on. So lots of iterations. ... [Y]ou're going through it point by point, you're going through it clause by clause. So each party, at least at the end, has a very strong understanding of what they read into each of the Code clauses. And it's no different with small suppliers, if they choose to have a discussion... [I]f they choose to ask and query individual clauses, we're very happy to go through them. It takes time, but it works.<sup>873</sup>*

*...I think the ACCC's website on the Code is a really good resource, and ACCC does need to continue to make sure everything is in plain English, setting out things by issue, and making it easier. And I think the AFGC provide a lot of good support and do a lot of good work in educating small suppliers. And it still does. So they do have go-to points where if they are confused about, "I don't feel like I'm being treated fairly, what's the right path?" I think they know where they can go. And ... through Fair Trading, we'll get questions as well. And we take them very, very seriously and respond very quickly, as does our code compliance*

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<sup>873</sup> Transcript of interview, MSC representative, pp. 16-17.

*manager. So I do feel that although it can be bewildering, we have really good intent to help them.*<sup>874</sup>

Then there is the overlay of the MSCs' own internal codes or charters which, while themselves simpler and more user-friendly (the Coles Supplier Portal is a one page online document that includes links to the company's product ranging and shelf-allocation principles and its complaints handling procedure),<sup>875</sup> might still create uncertainty as to which rules apply to which circumstances and when and to whom to complain. Further, out in the ether somewhere, for some suppliers, there may be consciousness also of other laws intended to protect them, laws that they might understand have something to do with abuse of market power and unfair trading, not to mention, general laws of contract also. A possible case of too much 'help' to be helpful? The following observations from interviewees with extensive experience in dealing with or advising suppliers appear to suggest as much:

*... there's far too much of this quick-fix solutions and viewing some medium such as codes as solutions for every problem under the sun, whereas in actual fact, in my view, they're actually creating greater uncertainty for parties.*<sup>876</sup>

*I think it's not accessible, there's nothing in there about how you go about it or how you do it, it would scream effort and cost and it also doesn't say that there's a person who knows what they're doing from a retail perspective in there. ... I also think there are just too many already settled ways of being able to get your grievances up or – there are always going to be times that people don't agree and you need some third party, but there are just too many other easy alternatives, why would you do that?*<sup>877</sup>

When a senior representative of AMWU was asked whether any suppliers were unhappy about the transition from a 'handshake' approach to more formalised agreements under the Code he replied:

*As soon as you put it down on paper and you start getting lawyers involved and third parties trying to make a decision as to what you meant when you said you'd do that, that's when it becomes a lot more complicated.*<sup>878</sup>

As mentioned above, our interview with a major fresh produce supplier to a MSC revealed degree of antipathy amongst small suppliers regarding formal rules and processes as a way of doing business. It appeared that he had little awareness of – or interest in – the provisions of either the FGCC or the MSC's own code of conduct, or the dispute resolution processes available to his company: 'I don't

<sup>874</sup> Transcript of interview, MSC representative, pp. 16-17.

<sup>875</sup> Coles Supplier Portal, Coles Supplier Charter <https://www.supplierportal.coles.com.au/csp/wps/portal/web/ColesSupplierCharter>.

<sup>876</sup> Transcript of interview, interviewee that consults to / advises grocery businesses, p. 5.

<sup>877</sup> Transcript of interview, MSC representative, p. 20.

<sup>878</sup> Transcript of interview, senior representative of AMWU, p. 43.

spend my time worrying about that kind of thing. ... I would hate to think that I would have to have access to something like that.<sup>879</sup>

### (b) Cultural change and competitive pressure

Secondly, at a more fundamental level, and potentially compounding the confusion factor, is the unavoidable reality that adherence to the provisions and processes of the Code involves a step-change in standards and expectations for all involved. On paper the Code anticipates if not demands a significant change in the nature of the commercial relationship, at least for some suppliers. Suppliers are intended by the Code to have more bargaining power and to use it. For some if not most suppliers, evidently, this is an idea that will take some getting used to and what's more, there appears to be a high degree of scepticism as to whether the Code will change anything at all. An interviewee who has conducted training with a large number of suppliers points out in this regard that:

*...the biggest challenge is suppliers read through the code, going, yeah, that's great, wouldn't it be super if? But there is an immense amount of cynicism in the marketplace, they've been beaten over the head for so many years so hard, relentlessly without apology that the retailers turning around saying, no, no, you misunderstood us, we never meant it that way and we are truly going to change the way that we do business and we are going to be the good corporate citizens that we are supposed to be. Unsurprisingly there's decades of scars and bruises where the suppliers are going, oh, I'll believe that when I see it, crack on, so there's that dynamic, which is a challenging one to overcome.<sup>880</sup>*

He hastens to add that, cynicism aside, suppliers still harbour considerable fear about dire consequences if they are to attempt an exercise in the leverage that the Code is supposed to give them:

*There's also the – you can't underestimate the level of fear within suppliers, if you are a \$50 million supplier, so a small supplier, you're probably privately owned, you probably employ maybe 40, 50 people and you maybe have a small factory, you maybe have a couple of production lines and if you're fortunate enough to supply Woolworths and Coles you know that if you were to put your head above the parapet and say you nasty people, you're doing something wrong and you were to get delisted, two things would happen; first, you'd lay off half your workforce; the second thing that would happen is the other retailer would go you know what, I've just seen that you've been thrown out of that other retailer, you know what I'm going to do, you are this close to the edge of the grave, you give me a whole load of money or I'm going to give you the last little nudge and you'll be in the grave. And the retailers do that without batting an eyelid, they will abuse the position where they suddenly realise that they're not just half of that supplier's business, they may be 90% of that supplier's business and will leverage their position. So as a supplier you can't afford to rock this boat, you can't afford to*

<sup>879</sup> Transcript of interview, CEO of a major fresh produce supplier to a MSC, p. 35.

<sup>880</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 10.

*have all of your eggs in one basket, you can't – so you've got to – if they say jump, you politely ask how high. So the whole concept of putting your head above the parapet saying I think you're being horrible to me and I'd like you to desist is a brave position to put yourself, which is why the ACCC doesn't get anywhere near the number of phone calls, emails and letters as they would like to get or even deserve to get purely due to the fear of the consequences.*<sup>881</sup>

All in all, however, notwithstanding these dynamics, the interviewee's reflection on the initial phase of the Code's implementation from a supplier perspective is positive, albeit also realistic about the time it will take for substantive change in both psychology and practice to seep through:

*...we've got off to a good start, suppliers are getting it, there's still a lot of fear, trepidation, concern, cynicism, retailers starting to nudge in the right direction a little bit, sometimes, but we're on a journey, it took five years in the UK, we're a year in..*<sup>882</sup>

In terms of step change, if suppliers are intended to have more bargaining power, buyers are intended to have less. Working against this is the ingrained practice, culture even, of driving as hard a bargain as possible. Hard bargaining is part and parcel of competition. The competitive climate in which the MSCs are operating is tough and all the signs are that it is only going to get tougher. The 2017 IBIS World report 'Supermarkets and Grocery Stores in Australia' predicts that in addition to the continued growth of Aldi and Costco, other large foreign grocery retailers including AmazonFresh, and the two German Schwarz Group's supermarket brands, Lidl and Kaufland, will further intensify price competition in the market over the next five years, placing increased pressure on Coles and Woolworths.<sup>883</sup> Capturing this sense, in March 2017 Woolworths CEO Brad Banducci was quoted as saying that growing competition had destroyed the supermarket 'duopoly' that Woolworths had enjoyed with its rival Coles.<sup>884</sup>

Other experienced observers of the Australian grocery scene point to parallels between developments here and in the UK:

*The UK market is less concentrated than the Australian market, with more players generally. As with Australia, the UK has also witnessed the entry of limited assorted discounters (Aldi, Lidl, Netto). Even with a limited range, these discounters have grown rapidly and had a huge (positive for consumers) impact on the incumbent supermarket behaviour.*<sup>885</sup>

Offering a contrasting perspective, in late March 2017 David Errington, an analyst with broker Bank of America Merrill Lynch, was reported as saying that Coles and Woolworths could expect their sales to grow by up to 5% in the coming five years, as a result of a softening Australian economy. According to Errington, history shows that MSCs benefit from tougher economic conditions, with people opting to

<sup>881</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 10.

<sup>882</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 67.

<sup>883</sup> 'Spotlight on Australia's supermarkets and grocery industry', *RetailWorld*, 24 March 2017.

<sup>884</sup> Madeleine Heffernan, 'Woolworths warns prices will rise on surging electricity costs', *The Age*, 28 March 2017.

<sup>885</sup> Transcript of interview, former senior representative of the UK OFT, p. 14.

eat at home more. He further stated that the active cutting of prices by the MSCs had already curtailed encroachment by competitors like Aldi and Costco. Errington described the threat posed by Amazon as 'over-played', noting that in all the discussions Merrill Lynch had had with suppliers, not one had said they had been approached by the online retailing giant:

*We don't see Amazon being a major threat to supermarkets, particularly over the coming five-year period...*

*Australians' preference to buy food online is at relatively low levels and the time required for a new participant to establish the necessary distribution and supplier capabilities in Australia is lengthy.*<sup>886</sup>

Merrill Lynch is of the view that the growth of the discounters (i.e. Aldi and Costco) has slowed as a result of adjustments made by Coles and Woolworths, and that from here on their growth will be on par with overall industry rates.<sup>887</sup> The real threat, according to these reports, was to independent grocers including butchers and green-grocers:

*Over the next five-year period the major supermarkets will continue stepping up their competitive offer in order to continue gaining market share at the expense of the independents and specialists that we see slowly exiting the Australian market.*<sup>888</sup>

Price however, remains an important weapon in the MSC battle to retain their dominance, and as Aldi approaches 10% of national market share it is showing no signs of easing off on the pressure. In May 2017 the German discounter launched, 'Good Different', the company's biggest Australian brand campaign in 16 years. The primary aim is said to be, 'promoting the discount retailer's differences and challenging the conventions of supermarket retailing in this market.'<sup>889</sup> Aldi Australian CEO Tom Daunt is reported as saying;

*After 16 years of establishing ourselves as a trusted place for the weekly shop, it's now time for us to build on this success and tell Australians what makes us different, and why we will continue to be different.*<sup>890</sup>

And it appears this difference will remain tightly tied to price:

*While other supermarkets might offer temporary markdowns and promotional pricing, ALDI's unique promise of permanently low prices saves shoppers both time and money.*<sup>891</sup>

Meanwhile Coles has been reported as having told suppliers that customers would not accept price increases, with suppliers in turn reporting that it was close to impossible to get price increases from

<sup>886</sup> Catie Low, Supermarkets to prosper from softening economy', *The Age*, 30 March 2017.

<sup>887</sup> See also a UBS report finding referred to in C Kohler, 'Shoppers cool on Aldi, Woolies rebounds', *The Age*, 5 April 2017 to the effect that Aldi is 'losing momentum.'

<sup>888</sup> Catie Low, Supermarkets to prosper from softening economy', *The Age*, 30 March 2017.

<sup>889</sup> 'Aldi reveals new business strategy', *RetailWorld*, 19 May 2017.

<sup>890</sup> 'Aldi reveals new business strategy', *RetailWorld*, 19 May 2017.

<sup>891</sup> 'Aldi reveals new business strategy', *RetailWorld*, 19 May 2017.

the MSCs, even as energy and input prices increase.<sup>892</sup> Therefore, while there may be scope for competition on quality, range and service, it is evident that for the MSCs, price remains a, if not the, most significant lever for maintaining performance on profit margins. As noted in the 2017 IBIS report, this goes against overseas trends, where product differentiation rather than price reductions has appears to have become the preferred competition strategy.<sup>893</sup>

Price has certainly been instrumental in Woolworths' recent turnaround. In January 2017 it was reported that, for the first time since 2009, analysts were predicting that Woolworths would 'beat Coles' on the like-for-like sales growth measure. This was attributed to both a return of focus, and a return on investment, by Woolworths, having divested itself of the highly unsuccessful Masters Home Improvement Stores.<sup>894</sup> This reported 'victory' is said to have come at a cost of more than \$1 billion that had been invested in lower food prices over the year, leading to a 13.9 % reduction in supermarket earnings.<sup>895</sup> In April 2017, Woolworths CEO pointed out that the company has invested \$1 billion in 12 months to lower prices as part of its turnaround strategy, but is reported to have 'said it wasn't yet where it needed to be. "We felt we needed to get trust on price. And we're a year into our journey of doing that, but still have a long way to go."<sup>896</sup>

Coles is not taking this challenge lying down, with CEO John Durkan reportedly declaring in the face of Woolworths' billion dollar investment that Coles would be 'competitive forever' and 'never give up'.<sup>897</sup> When analysts asked Durkan to explain what they suggested was arguably an irrational response with little chance of ensuring ongoing profitability he reportedly responded:

*I go back to the fact that I think it's been an unusual year in terms of price adjustment but we've also had the rollout of a major competitor in two different geographies [a reference to Aldi's recent expansion to other states]. I can't say that won't happen twice but it would be unusual. What I do see is that there's plenty of room to grow in this marketplace for all players.<sup>898</sup>*

Advantage over rivals on retail price will arguably continue to have to be derived largely from negotiations on wholesale price, all the more so while other costs (particularly energy costs) continue to rise. As one journalist recently observed, 'what is becoming increasingly clear is the war in the aisles is taking its toll on the bottom line for Australia's two largest supermarkets chains.'<sup>899</sup>

This competitive pressure means that there may be tension between the letter and spirit of the Code, on the one hand, and the messaging and target-setting by senior management, not to mention the personal consequences for buying personnel of failing to reach target, on the other. Seasoned industry watchers point out that this is no different to the tension that has always existed between

<sup>892</sup> Catie Low, 'Supermarkets to prosper from softening economy', *The Age*, 30 March 2017.

<sup>893</sup> 'Spotlight on Australia's supermarkets and grocery industry', *RetailWorld*, 24 March 2017.

<sup>894</sup> Madeleine Heffernan, 'Coles might need to splash cash after Woolworths 'wins' Christmas', *SMH*, 20 January 2017.

<sup>895</sup> 'Woolies cuts its way to sales victory', *AAP*, 22 February 2017.

<sup>896</sup> C Kohler, 'Shoppers cool on Aldi, Woolies rebounds', *The Age*, 5 April 2017.

<sup>897</sup> Catie Low and Patrick Hatch, 'Wesfarmers vows Coles will be competitive forever', *The Age*, 16 February 2017.

<sup>898</sup> Catie Low and Patrick Hatch, 'Wesfarmers vows Coles will be competitive forever', *The Age*, 16 February 2017.

<sup>899</sup> Catie Low, 'Coles, Woolworths, Aldi in battle for diminishing shopper dollars', *The Age*, 28 January 2017.

doing what may be 'right', from a moral or ethical standpoint, and the harshness of commercial reality in an organisation and environment where profit rules, and often with brutal repercussions for individuals:

*... [it] is an absolute fact, I can prove it factually: a gap between the intent of what the management team are trying to achieve in context of code and the behaviours at a buyer level. Now, the senior guys swear blind they're not aware of that behaviour at a grass roots level, I think there is an element of conscious deniability about that because the targets and KPI's put in place by the senior team on the buying team are in many instances unattainable without poor behaviour. Then let's say hypothetically within dry grocery or grocery general you've got your impulse teams that look after chips, chocolate and the like and that group, tick, achieve their targets. Then within that, biscuits, yep, achieve their targets, chocolate down. You're the chocolate buyer, what now? So everyone else above you has achieved their targets, you're the one guy or girl in that team that hasn't, it isn't about whether you get your bonus, it's whether you're in the building in four weeks' time and it's as simple and as brutal as that. It starts at the top, so if you're delivering a 5.7 EBIT last year and you've got to deliver a 5.85 this year you've got to cascade that down. Again, I'm not a retailer, I'm not employed by retailers, have never been employed by a retailer, but sitting external to them and being close to the industry we don't believe, in our opinion, that the targets that they currently are striving for, or indeed this new financial year, we don't believe that they can easily be achieved through good everyday practice or behaviour. And the reason for that is that a percentage of historical profit has been, and a material percentage of historical profit, pre-code profit, has been generated through behaviour that your mum would say isn't right or reasonable. So that isn't going to go away, that's profit that was last year's profit, I've got to lap that this year so how do I lap dirty money? It's impossible, well, it's not impossible. Where's all this future growth going to come from? So when there isn't top line growth and there's price deflation, the only place it's going to come from is the suppliers.<sup>900</sup>*

For Dawson, just about mid-way into the second year of Code operation, the industry is at a critical juncture in terms of competitive dynamics and this will truly test the robustness of the FGCC.

Speaking in March 2017, he said:

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<sup>900</sup> Transcript of interview, director of a consultancy that advises suppliers, pp. 33-38. Cf the cooperative model of some supermarket chains in the UK which are structured as a partnership. Each employee has part-ownership of the company, a share of its annual profits, and a say in how it is run. All staff regardless of their position in the company receive the same percentage payout which is directly tied to the company's profits. Employees are partners and hold the management and board to account while providing broad strategic direction for the business. There are no external shareholders. We interviewed the Manager (Compliance) for one of these cooperatives. As one of the 60 partners, she spoke with passion about what having a personal stake in the business means in terms of both the benefits and responsibilities:

*What it means is that we share in the rights and the responsibilities so we have rights as employees and partners, but we also have responsibilities to ensure that the company continues to grow, develop, evolve and handed onto the next generation... It doesn't suit everybody, but it is a company that people want to join to. The benefits are huge, but there are also responsibilities. And you do have to be committed because if you don't do your job right, somebody is going to be saying to you, "Hey, you're not doing your job right. You are wasting my company's money and that's my bonus." It used to be epitomised by stickers by the light switches, saying, "Switch off. You're burning my bonus," which was that it was everyone's responsibility to save the last bit, and that was how it was epitomized. It is a challenging environment, but it's great. (Transcript of interview, Compliance manager at a major UK retailer, p. 2)*

*But if you shift to looking at what about commercial outcomes I do think there's a question that - we won't - I suppose we won't really know the answer to that until later on this year because we've reached this point in the market where Woolworths have sacrificed an enormous - well, almost half their margin to invest in price, to regain sales momentum, which they've done. Everyone expects Coles to respond to that, which they're doing, and traditionally to claw back margin the retailers have gone to suppliers, either asked for it voluntarily or pressured them in order to claw back margins. So I think we're at a critical point and obviously we're watching that really carefully through the rest of this year and there's quite a bit of analyst commentary on this and so forth. But the expectation - let me put it this way; the expectation amongst suppliers is that both retailers will put pressure on them in terms of margin transfer. I mean, my sense from talking to our members and suppliers generally is that for various reasons there would be quite a bit of resistance to any further margin transfer, partly because there's not a whole lot of margin left to give and, of course, things like energy costs are chewing up some of that margin already, deflation in the retail environment, and partly because their position - they feel their position has been strengthened by the provisions in the code. So I do think the code is playing a part in that. But I accept that it's far from certain how that's going to play out through this year. I think this year is a critical one in terms of the competitive environment.<sup>901</sup>*

There are other perspectives, however. From the perspective of major multinational suppliers, the Australian market is a very different one today to the market 15 years ago. Whereas previously it was a 'high growth' environment, today it is 'low growth'<sup>902</sup>. Previously, 'it was a very comfortable existence between supplier and retailer. Prices went up 2-5% every year and frankly, costs were passed on right through the line.'<sup>903</sup> Now there is more competition between retailers and, by global standards, prices are too high. This 'creates tension... and that tension goes back up the line.'<sup>904</sup> Suppliers, accustomed 'to a certain style of behaviour, a certain level of growth and certain level of profitability, become compromised [and] there is a period of readjustment ... of the price and structure of the profit transfer and that's driven some tension and some pain'.<sup>905</sup> As a result, the nature of 'the conversations' between suppliers and buyers are different. Retailers, he explained, are under 'a lot of pressure... to deliver attractive results [and] shareholder returns. That's going to drive some tough conversations'.<sup>906</sup> But, he was quick to add, 'I don't think the tough conversations are unreasonable'.<sup>907</sup> For a multinational, they are the same conversations that they have had with retailers in other markets overseas, and in that sense the developments in Australia are familiar and just a reflection of developments in the market.

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<sup>901</sup> Transcript of interview, Gary Dawson 2, p. 9.

<sup>902</sup> Transcript of interview, senior representative of a larger supplier of packaged goods to the MSCs, p. 34.

<sup>903</sup> Transcript of interview, senior representative of a larger supplier of packaged goods to the MSCs, p. 36.

<sup>904</sup> Transcript of interview, senior representative of a larger supplier of packaged goods to the MSCs, p. 36.

<sup>905</sup> Transcript of interview, senior representative of a larger supplier of packaged goods to the MSCs, p. 36.

<sup>906</sup> Transcript of interview, senior representative of a larger supplier of packaged goods to the MSCs, p. 34.

<sup>907</sup> Transcript of interview, senior representative of a larger supplier of packaged goods to the MSCs, p. 34.

From the perspective of the MSCs, they are evidently in a process of constantly reviewing and adjusting their strategies in response to the competitive pressures and there are signs in both organisations that this includes a new or renewed focus on building relationships with suppliers. According to the account we received from one MSC, this is not just about strategic change, it is about cultural change. Whereas previously, 'everyone was just watching numbers, watching numbers, watching numbers',<sup>908</sup> there is now a top down effort to make the end customer the primary focus of the business and a key aspect or lever in this is engagement with suppliers. This was emphasised repeatedly in our interviews with MSC representatives:

*[O]ur real differentiator that we're trying to build is our culture, so we're trying to take our suppliers with us. We're trying to work with suppliers ... to make sure that they understand what are customers are telling us so that they can help us on that journey. We need to partner with them to develop the right products at the right price points for customers to buy, and to grow.*<sup>909</sup>

*[W]e definitely wanted to, with all the different media going on, actually change the relationships with our suppliers. I think there'd been a period just generally where there hadn't been as much of a focus on partnership and we wanted to renew that. [W]e're all in this together, we need each other, all of the negotiations we have reflect that. [W]e can't just do things alone ...*<sup>910</sup>

Another MSC representative went further, explaining that 'no retailer survives without their suppliers ... [Y]ou can't treat your suppliers badly and then expect to get good outcomes for your customers. The two just don't, it doesn't work'.<sup>911</sup> But he also pointed out that the challenge for a large retailer lies in achieving consistency of approach in the treatment of suppliers: 'we're quite a large group of people trying to interact with another large group of people, and that, in fact, is 500 odd folks in buying, interacting with many thousands across, 4,000 plus suppliers'. Meeting this challenge, he explained, is not just a matter of training and retraining buyers in the content of the FGCC; it's about instilling a real appreciation of 'the intent of the Code' but also teaching 'communication skills, focussing on emotional intelligence' and emphasising that, at the end of the day, the goal is for the MSC to be and be seen to be 'good to do business with'.<sup>912</sup> Further, positive feedback from suppliers is being built into 'key performance indicators' for buying teams and that 'has a direct impact on [the buyer's] bonus. [S]o ... if you are ... getting regular negative feedback from suppliers, you've got a real risk.'<sup>913</sup>

If rebuilding of relationships with suppliers is indeed to be a genuine focus for the MSCs, then it may be expected or hoped that trust, cooperation and good faith in supplier dealings will be driven

<sup>908</sup> Transcript of interview, MSC representative, p. 22.

<sup>909</sup> Transcript of interview, MSC representative, pp. 5, 8.

<sup>910</sup> Transcript of interview, MSC representative, p. 37.

<sup>911</sup> Transcript of interview, MSC representative, p. 4.

<sup>912</sup> Transcript of interview, MSC representative, pp. 6-7.

<sup>913</sup> Transcript of interview, MSC representative, p. 9.

internally by the corporate leadership of these businesses, and will not require or may simply be reinforced by the demands of an external instrument such as the FGCC.

### (c) Continued political pressure?

Finally, if the change in culture on which the Code's true effectiveness is premised is to penetrate the industry, on both sides, it is arguably material to consider whether the political pressure that was so instrumental in the FGCC's instigation will continue (should it need to). It goes without saying perhaps that politics is reactive, and it is difficult if not impossible to predict the possible factors that might reignite the embers in Canberra. A further outbreak of 'bad' behaviour by one of the MSCs, potentially caused by increasing intensification of competition, might well have such effect, particularly if it were to incite investigation and proceedings by the ACCC, with attendant publicity. One would like to imagine that, given the experience of the past few years, MSC leadership will be on its guard to prevent such occurrences and certainly on accounts from the MSCs themselves, vigilance is being exercised in this respect. That said, based on any track record review of corporate misconduct generally, such imaginings are readily contradicted. If Dawson's predictions of food inflation are borne out, that too may well have a stirring effect, and the possibility of an ACCC inquiry into retail grocery prices mark II at some stage in the future cannot be discounted entirely.

However, as recent history also tells us, there may be factors beyond MSC control, including further farmer outcry responding to strains likely to be ongoing in the agricultural sector, and that may cast the political spotlight back again on the size and power of our two largest grocery chains. This prospect is borne out to some extent in the UK where in a review being undertaken in relation to the GCA, there has been a call for evidence as to whether her remit should be extended to primary producers.<sup>914</sup> It is true that in Australia key actors in the Code's genesis are no longer on stage: Dawson, Billson, and at some point in 2018, Sims too may have exited (his term expiring next year, albeit he may well be re-appointed). However, with the exception possibly of Billson (whose replication as a champion for small business is hard to conjure), there is no reason at this stage to think that their replacements as well as other influential figures, Barnaby Joyce and independent Senator Nick Xenophon amongst them, will not continue to play a role in supermarket politics.

## V. Reinforcements

Compensating to a degree for some of the factors cited above as counteracting the positive impact of the FGCC to date, there are several factors that appear to have assisted in reinforcing its impact, at least in its first two years of operation. The role of the ACCC in this regard appears to have been particularly influential.

In relation to its role with respect to industry codes, it was determined from the outset that the ACCC would create guidelines offering 'some practical guidance for bodies in the market looking to develop

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<sup>914</sup> See further Part 7 of this report.

industry codes'.<sup>915</sup> The intention was not only to set out the legal implications of codes, but to offer 'a practical experience guide to what works, where – a code that's credible as opposed to a code that lacks rigor or credibility'.<sup>916</sup> Further, Graeme Samuel AC quite early in his role had contemplated the possibility of the ACCC formally endorsing voluntary codes that were consistent with these guidelines. However, as one ACCC interviewee reported, 'we came to a landing that there was more risk associated with [this] than was acceptable.'<sup>917</sup>

The ACCC nevertheless continued to provide guidance, particularly to 'small business industry associations that wished to develop voluntary codes'.<sup>918</sup> The aim was to 'provide some kind of framework of fairness for small business dealing with larger businesses particularly, then voluntary industry codes can be part of the framework'.<sup>919</sup> A similar approach has been taken by the OFT in the UK, assisting trade associations in drafting codes to achieve sufficient specificity and customisation to the issues of their sector, while at the same time ensuring that the code does not raise barriers to entry or engender anti-competitive coordination.<sup>920</sup>

The ACCC has the capacity to audit various aspects of industry codes, and we have been told the ACCC will be doing so in relation to the FGCC, 'as part of our active audit program schedule.'<sup>921</sup> Our understanding is that audits are scheduled to occur annually and look at compliance with the 'behavioural requirements of the code'.<sup>922</sup> The supermarkets are forewarned of upcoming audits and under their audit powers the ACCC is entitled to request access to certain documents and information that businesses are required under the Code to keep. This in turn tells the ACCC, 'about the behaviour of the entity that's regulated, about the supermarket,'<sup>923</sup> without having to rely on complaints or reports from third parties:

*So really it allows us – without having to rely on named complainants or any individual example that identifies someone who might otherwise be given a supply holiday, to test behaviour on this or that aspect of the code via a particular supermarket and complaint data that comes to us, information that comes to us telling us that there might be a problem on this or that aspect allows us to target those audits ...'<sup>924</sup>*

As previously noted, the Code allows for code-related complaints to be made directly to the Commission and potential breaches may be investigated using the full arsenal of ACCC compulsory information gathering powers. In line with this the ACCC website provides suppliers with an overview of the obligations and key protections that suppliers are afforded under the FGCC. The ACCC also makes clear that if a supplier has:

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<sup>915</sup> Transcript of interview, senior representative of the ACCC, p. 2.

<sup>916</sup> Transcript of interview, senior representative of the ACCC, p. 2.

<sup>917</sup> Transcript of interview, senior representative of the ACCC, p. 2.

<sup>918</sup> Transcript of interview, senior representative of the ACCC, p. 2.

<sup>919</sup> Transcript of interview, senior representative of the ACCC, p. 4.

<sup>920</sup> Transcript of interview, John Noble, British Brands Group, p. 29.

<sup>921</sup> Transcript of interview, senior representative of the ACCC, p. 28.

<sup>922</sup> Transcript of interview, senior representative of the ACCC, p. 28.

<sup>923</sup> Transcript of interview, senior representative of the ACCC, p. 28.

<sup>924</sup> Transcript of interview, senior representative of the ACCC, p. 28.

*... concerns that a retailer or wholesaler has done something that's prohibited under the Code or you just have a general enquiry about the Code, then you can always contact the ACCC. We can investigate and if it's necessary, take enforcement action.*<sup>925</sup>

Enforcement action includes a range of orders, declaratory, injunctive and compensatory in nature, even if at this stage pecuniary penalties are not yet on the table (a matter likely to feature in the upcoming review, as previously noted).

Our research revealed high support generally for having ACCC oversight and enforcement action as a backstop that would shore up the Code, giving it teeth if not bite. As pointed out in Part 5 of this report, at the time of the Treasury consultation and the Senate inquiry, there were some who argued for a separate dedicated Ombudsman-style monitor and watchdog – the UK model. As former PGCC Ombudsman Robert Gaussen has repeatedly argued, ‘you need an ombudsman, you need someone to oversight it’.<sup>926</sup> Early on, at least under Carnell’s leadership, the AFGC had also supported going down a similar road to that taken in the UK. However when it became clear that this would not be an option, under Dawson, a more pragmatic approach was adopted:

*...the AFGC certainly put proposals that was under my predecessor, for a mandatory code similar to what's been done in the UK with its own statutory watchdog, code ombudsman... I come into this role, the then government made it clear they weren't willing to amend the Act to do that and so, I suppose, from my point of view and my board's point of view it was a matter of, well, what can we usefully do that will make it – that will improve the environment for our members ...*<sup>927</sup>

However others voiced strong opposition to following the UK’s lead. As one former senior MSC employee said:

*... our fear was that we were going to get something like the UK model, where it was very prescriptive. And it was funded by retailers. And there was an ombudsman that would just keep issues alive. Whether it was perceived or real. I remember talking to Rod Sims about that, he said, “What’s the problem with the UK model?” I said, “Well, we don’t want to have to pay for an ombudsman, who’s just going to kick us every day....” I don’t mind the regulator doing his job, but at the end of the day, we don’t want a code that’s designed by regulators. We want a code that’s designed by industry that will avoid unintended consequences and actually work – allow retailers and suppliers to work together.*<sup>928</sup>

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<sup>925</sup> ACCC website, Food and Grocery Code of Conduct, <https://www.accc.gov.au/about-us/tools-resources/social-media/transcripts/food-and-grocery-code-of-conduct>.

<sup>926</sup> Transcript of interview, Robert Gaussen, p. 38.

<sup>927</sup> Transcript of interview, Gary Dawson, 2016, p. 29.

<sup>928</sup> Transcript of interview, Robert Hadler, p. 19.

*We wanted fast track low cost dispute resolution process. We didn't want a government designed ombudsman process that would cost a lot of money and take a lot of time and probably not result in any satisfactory outcome.*<sup>929</sup>

From the time of the Code's inception, the ACCC has been at pains to ensure the industry knows it is on watch. Its 2015 Compliance and Enforcement Policy highlighted code monitoring and possible enforcement as a priority. And in September 2015, only a matter of months after the Code took effect, the agency fired a warning shot across the bows of the Code signatories, Sims using the press to report that the agency:

*... has concerns as to the manner in which some retailers, in particular Woolworths and Aldi, are presenting new Grocery Supply Agreements (GSAs), which might give the impression that the supplier is not able to negotiate the terms of the GSA.*<sup>930</sup>

Woolworths appears to have been less than impressed with the ACCC's resort to the media to ventilate such concerns, complaining that the ACCC had only raised additional – and minor – concerns about the wording of Woolworths' and Aldi's supplier contracts, 'just hours before contacting the media'.<sup>931</sup> Indeed, it was evident from our interviews that, within the MSCs, there is a view by some of being singled out, victimised even, by the ACCC on account of simply being 'big':

*... if we take one small step they're all over us, and ... that's explained by the fact that [as] Rod Sims said the other day, "we are focussed on big business because that's where we think we can generate the most noise in terms of the messages, but also ideally because you will reach more consumers". But if it's going to work well across the market and everyone is going to compete and have to raise to the same standard, I do think there needs to be a bit more parity in enforcement approaches. By all means keep your eye on the big businesses, but don't let the rest of the market just do other things, because it's very frustrating for our people as well. Why are we doing the right thing and others aren't? Can we complain about them? Will anyone listen to us if we complain?*<sup>932</sup>

Moreover, MSC accounts of ACCC intervention of the kind in this instance suggest that, from the MSC perspective, the agency can take something of a nit-picking approach and one that, at times, is disproportionate to the issue at hand:

*Unfortunately, the ACCC, because of the nature of the organisation and the nature of the Code, they have to be fairly legalistic in their interpretation and their ability to look at the Code, and performance against the Code. And the audit that they do, or the next audit that they do, probably again will be quite detailed, but directly towards the wording of the Code, as opposed to how well it's interpreted, or how well it's applied. And it becomes a real challenge*

<sup>929</sup> Transcript of interview, Robert Hadler, p. 48.

<sup>930</sup> 'ACCC investigates claims Woolworths, Aldi 'off to a bad start' under supermarket code of conduct', *ABC Rural News*, 24 September 2015.

<sup>931</sup> Catie Low, 'Aldi and Woolworths accused by the ACCC of misusing grocery code', *The Age*, 24 September 2015.

<sup>932</sup> Transcript of interview, MSC representative, p. 34.

*to meet the absolute provisions of certain parts of the Code that are very prescriptive, although the spirit of the thing may well have been properly in place, and the outcome may well have been perfectly happy between the two parties, it may look on paper that the notification has been a week too late, or something else that's relatively minor in the scheme of things, but technically might be a breach of the Code.*<sup>933</sup>

Other commentators too, when asked about the ACCC handling of the matter concerning new GSAs by Woolworths and Aldi, are critical, describing it as evidencing the ACCC's propensity to make 'short term shrill use of the media', an approach thought to be damaging in the long run in securing buy-in by retailers to the Code.<sup>934</sup> In a more tempered response Aldi was quoted as saying it would respond to the specific issues raised by the ACCC and that:

*Aldi's commitment to sign and implement the Food and Grocery Conduct Code before any other major supermarket is testament to our business values and dedication to quality supplier relationships. The spirit of the code reflects Aldi's current practice with suppliers, forging long-term sustainable relationships.*<sup>935</sup>

Then, in late 2016, the ACCC reported concerns about the way that Aldi, Coles and Woolworths were treating suppliers when delisting products, with Sims telling an AFGC forum that, 'some delist notices did not include any real reasons for delisting and where reasons were provided, they were typically very general in nature'. Sims went on to make clear that the ACCC had already raised such concerns with all three supermarkets, and said that retailers would need to improve the way they notified suppliers about delisting if they wanted to avoid breaching the FGCC.<sup>936</sup>

Aside from code-specific activity, there is no doubt that the ACCC's demonstrated capacity and willingness to take the MSCs to court for unconscionability has been influential in reinforcing the value of the Code, in the eyes of the retailers at least. Reports are that the investigations and proceedings in both the Coles and the Woolworths' suits had a potent impact on the personnel of those organisations, both at senior management and operational levels.

*Oh, they [the ACCC unconscionability actions] had a significant impact. From the Wesfarmers board right down, I mean, that is a terrible thing for the ACCC to be calling out against the company.*<sup>937</sup>

*It had a big impact ... it caused a lot of people who were in the business at that time, to become quite introspective. And you know, we were running flat out, probably at the time, the world's biggest turnaround. And not that it is right, but you know ... the pressure's there...*<sup>938</sup>

<sup>933</sup> Transcript of interview, MSC representative, p. 13.

<sup>934</sup> Transcript of interview, former senior representative of the UK OFT, p. 10.

<sup>935</sup> Catie Low, 'Aldi and Woolworths accused by the ACCC of misusing grocery code', *The Age*, 24 September 2015.

<sup>936</sup> 'Major supermarkets draw ACCC ire', *News.com.au*, 8 November 2016.

<sup>937</sup> Transcript of interview, MSC representative, p. 22.

<sup>938</sup> Transcript of interview, MSC representative, p. 54.

As previously highlighted, that despite succeeding in its defence to the ACCC's unconscionability action, Woolworths' leadership was nevertheless at pains to emphasise its commitment to higher standards in the future is also telling in this regard.

The capacity and effectiveness of the ACCC in fulfilling its mandate as Code and unconscionability watchdog depends of course on the willingness of suppliers to turn in their buyers, and the historical record suggests that this will continue to be problematic. Indeed, when we asked an interviewee who had trained and advised a large number of suppliers in the FGCC provisions about whether any of them had reported concerns about Code compliance to the ACCC his response was not encouraging: 'none, not one!'.<sup>939</sup> This is in contrast to an account given by an ACCC representative at a subsequent AFGC conference, reporting as at May 2017 that there had been '17 complaints and 24 inquiries' relating to the FGCC.<sup>940</sup> These numbers could have been higher were it not, according to the supplier trainer whom we interviewed, for:

*...the level of fear within suppliers ... which is why the ACCC doesn't get anywhere near the number of phone calls, emails and letters as they would like to get or even deserve to get purely due to the fear of the consequences.*<sup>941</sup>

Such concerns are reflected in supplier responses to the 2017 AFGC survey referred to previously. With regard to impediments to raising an issue with the ACCC, 62.2% were not confident that their confidentiality would be maintained, and 69.5% feared retribution.<sup>942</sup> Having spoken to ACCC staff himself about the matter, our interviewee was of the view that the ACCC did not even have the basis for a reasonable belief of a potential breach that would enable it to exercise its compulsory information-gathering powers to investigate:

*I sat down with the ACCC and said "All you need – just go in and pluck 10 contracts off the shelf and go and look at the payment and you'll find nine, guarantee, nine of those out of 10 will be in breach." "We can't do that." "Why can't you do that?" "Well, because we don't know where to look." "Grab any 10." "Well, which 10, we need – we can't go in on suspicion."*<sup>943</sup>

This account, suggesting that the ACCC may lack the will and/or the resources to act in response to supplier complaints regarding Code compliance is not dissimilar to the response we received from the COSBOA CEO when we asked him about ACCC receptiveness and capacity to respond to small business complaints generally:

<sup>939</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 46.

<sup>940</sup> Michael Schaper, Deputy Chair, ACCC, 'Current Food & Grocery Issues: An ACCC Perspective', presentation to AFGC conference, 2017, slide 9.

<sup>941</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 10-11.

<sup>942</sup> AFGC 2017 Annual Food and Grocery Code of Conduct Survey, p. 19.

<sup>943</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 46-7.

*You ring them up, you get nothing. And it's not like everything is their call, and they would need a lot of resources, so if you ring them up, very rarely you get listened to, very rarely.*<sup>944</sup>

This view is also evident in the AFGC survey. 54% of suppliers surveyed, when asked about reasons for not raising an issue with the ACCC, said they didn't think the ACCC could do anything, 21.6% thought the behaviour would be viewed as a normal way of doing business, and 10.8% believed the issue would not be taken seriously, with a further 10.8% stating that they didn't think the concern was important enough for the ACCC to get involved.<sup>945</sup>

The approach taken by the code enforcer is seen as critical by commentators to the effects of a code such as the FGCC.<sup>946</sup> It is evident that the approach taken by the GCA in this respect, with its emphasis on education, collaboration, and informal mediation, is seen in a highly positive light. Tacon's non-confrontational consensus-building approach, in particular, is seen by some in the UK as having made suppliers more willing to speak out:

*... the climate of fear thing has changed somewhat. When we working on the 2008 enquiry, there was genuinely fear on the part of suppliers to have any kind of contact with the process. So suppliers actually had to go to the CMA, to the CC at the time and say, look, use your statutory mandatory powers to send us information requests, because we will then feel more able to respond. If you don't use your mandatory powers, actually we won't answer. Whereas now, if the GCA holds a conference, you'll look at the attendee list. There's half a dozen, a dozen supplier representatives there who seem to be quite happy to be openly seen to be interested in the topic.*<sup>947</sup>

In the review of the GCA completed in July 2017, the majority of respondents, from both large retailers and suppliers, expressed the view that the GCA 'has been highly effective in exercising its existing powers through a combination of ensuring better Code related information for suppliers, promoting collaboration with large retailers, and using investigatory and regulatory powers.'<sup>948</sup> There had been some criticism that the GCA had not undertaken more investigations, exercising her formal powers, over the three period under review. However, this criticism was far outweighed by the view from across the sector that the GCA's 'lighter touch' approach, with hallmarks of awareness raising, education, and relationship-building was what made the GCA, in the words of the report on the review, 'an exemplar for modern regulation.'<sup>949</sup> Tacon's personal style, marked by professionalism and fair-mindedness, was also highlighted as instrumental in the highly positive response received to the review. As the report noted: 'the current Adjudicator has created a level of trust with the large

<sup>944</sup> Transcript of interview, CEO of COSBOA, p. 20.

<sup>945</sup> AFGC, *Annual Food and Grocery Code of Conduct Survey Report*, 2017, p. 19.

<sup>946</sup> Transcript of interview, former senior representative of the UK OFT; Transcript of interview, experienced legal advisor to suppliers in the UK, p. 44.

<sup>947</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 40.

<sup>948</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [66].

<sup>949</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [82].

retailers, without which, some responses highlighted, it was more likely that issues would have remained hidden.<sup>950</sup>

Tacon's approach in handling and the outcomes of an investigation into Tesco for GSCOP breaches (referred to further below) also has attracted favourable comment from a range of commentators, focussing on how Tacon was balanced in her findings, recognising that the transgressions uncovered in the investigation were a minority of instances in a large complex organisation in which it is simply impossible to get everything right all of the time. Some of these same commentators who are also familiar with the ACCC, question whether it's more aggressive and litigious approach will be as effective and suggest that it may even have counterproductive effects:

*I think one of the problems in Australia is that the ACCC is a very shrill organisation that – it basically shouts first and finds the facts later. ...in the UK, you do not get that sort of behaviour by regulators... so I worry that if the ACCC is not going to be balanced about how it enforces it [referring to the FGCC]... I certainly think that that's the sort of thing that in the long-term could really mean that the supermarkets ...just become weaker at bargaining on behalf of consumers with suppliers.<sup>951</sup>*

*[From the perspective of those running supermarkets] even making the best efforts to treat suppliers well, it is difficult to get everything right all the time in a fast-paced, highly competitive environment. With intense competition, supermarkets need to purchase as efficiently as possible and the pursuit of that can result in mistakes being made. Conversely a retailer that caved into everything a supplier says would not be very competitive, and the customer would not get as good a deal. The important thing is that the ACCC, a bit like the grocery code adjudicator, when an issue comes up, can be proportionate about it. So they probably want to ask themselves ... three questions. First, what percentage of the overall set of agreements is affected; second what is the impact on consumers; and third what is the impact on suppliers. It also needs to understand the company policy, and what efforts the company has made to get compliance with that policy.*

*... so I think it's really important that ... the ACCC [is] looking at this as a long-term change program and being supportive of the direction of travel, as opposed to an opportunity to impose sanctions even with minor errors.<sup>952</sup>*

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<sup>950</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [80].

<sup>951</sup> Transcript of interview, former senior representative of the UK OFT, pp. 5-6.

<sup>952</sup> Transcript of interview, former senior representative of the UK OFT, pp. 17-18.

## 9. Up for review and looking ahead

As previously mentioned, it was decided that the FGCC should be reviewed earlier than the five years generally allowed before such reviews. A three year time period, providing for a review in 2018, was settled upon. An early review was said by Treasury to be ‘appropriate’.<sup>953</sup> Reasons were not given for that assessment. But it was almost certainly a matter discussed and agreed with key stakeholders, at least the AFGC and MSCs, and in the circumstances, given the degree of angst surrounding the issues that culminated in the Code, the sense that a timely ‘look back’ was appropriate is hardly surprising. That the FGCC was voluntary, and the first of its kind in this respect, may have also contributed to the view that there should not be a five year wait. If the Code was not living up to expectations then consideration would need to be given to follow up action – mandating the Code in particular – and after all, as the preceding account makes clear, such action was promised / threatened should the voluntary option be seen to have failed to have ‘fixed the problem’.

These good reasons for a review in 2018 aside, it should be acknowledged also that in the scheme of things, three years is not a long time to bed down a wholly new, and in some respects, novel set of industry arrangements. This is particularly so given that as a result of the transitional provisions, for some suppliers, the Code would not have affected their supply terms and conditions for some months (in some cases, over a year) until after the FGCC took effect. It should be borne in mind further that in effect the transactional requirements of the Code necessitated not just a change in the way of operating but arguably a wholesale shift in culture, on both the MSC and the supplier sides of the equation. Cultural change is by its nature a slow process.

Given these considerations, it is fair to say that while the 2018 review should produce some useful insights, deeper reflections on the implications of the Code for supermarket-supplier relations and regulation of the sector more generally may take longer to emerge. This is consistent with comments of one experienced observer of developments in both the UK and Australia:

*... it may be difficult to observe [the true effectiveness of a code] in a three year timeframe, simply because there's so much effort by all of the supermarkets going into – getting in compliance with the code...and you only really know when it's working when things go wrong.*<sup>954</sup>

It should also be acknowledged that there will be difficulties with reviews of this nature at any stage in isolating the impact of regulation vis-à-vis the impact of other factors operating in and affecting the industry. As one UK supermarket representative told us in response to a question about the effect that the regulatory developments have had on supermarket-supplier relations in that country:

*...it's very difficult to isolate the impact of the GSCOP and the GCA, separate to everything else that has been going on in the environment at the same time, so you can't identify what*

<sup>953</sup> Explanatory Statement, *FGC Regulation 2015*, p. 37.

<sup>954</sup> Transcript of interview, former senior representative of the UK OFT, p. 23.

*was the impact of the financial crisis or what was the impact of that movement, as opposed to that, and the whole lot has to be seen in tandem. Yes, it has an influence. Would it have happened without it? You can't say. It's very difficult to isolate it from that point of view.*<sup>955</sup>

At the time of making the Regulation, the Government identified a range of matters that should be considered for the purposes of the review:

- *the extent to which retailers and wholesalers have become bound by the code;*
- *levels of compliance with the code by retailers and wholesalers bound by the code;*
- *whether the purposes of the code (see clause 2 of the code) are being met;*
- *the extent to which the code assists in addressing any imbalances in the allocation of risks between retailers, wholesalers and suppliers;*
- *whether there are any further measures that would improve the operation of the code with respect to the matters mentioned in the two previous paragraphs;*
- *the interactions between the code and the Horticulture Code of Conduct;*
- *how the code compares with overseas regulation of commercial relations between retailers, wholesalers and suppliers;*
- *whether the code should be mandatory or voluntary;*
- *whether the code should include civil penalty provisions;*
- *whether retailers, wholesalers and suppliers should be bound by the code, and if so, to what extent;*
- *whether the code should be repealed or amended and, if so, the timing of any such repeal or amendment;*
- *the products that should be covered by the code.*<sup>956</sup>

No doubt there will be submissions from across the grocery industry as well as from others providing Treasury, which will conduct the review, with input on all of the matters identified above and Treasury can be expected also to consult with the ACCC. For the purpose of this report, however, we have chosen to focus on what would appear to be the overarching matter for consideration in the context of the review, namely 'whether the purposes of the code are being met'. Addressing that question subsumes in turn several of the other questions identified in the review list.

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<sup>955</sup> Transcript of interview, compliance manager at a major UK retailer, p. 27.

<sup>956</sup> Explanatory Statement, *FGC Regulation 2015*, p. 37.

Clause 2 of the FGCC identifies the purpose of the Code as being:

*(a) to help to regulate standards of business conduct in the grocery supply chain and to build and sustain trust and cooperation throughout that chain; and*

*(b) to ensure transparency and certainty in commercial transactions in the grocery supply chain and to minimise disputes arising from a lack of certainty in respect of the commercial terms agreed between parties; and*

*(c) to provide an effective, fair and equitable dispute resolution process for raising and investigating complaints and resolving disputes arising between retailers or wholesalers and suppliers; and*

*(d) to promote and support good faith in commercial dealings between retailers, wholesalers and suppliers.*

The extent to and ways in which each of the elements of this purpose are being met are considered below. This consideration draws and elaborates on the findings and analysis in Part 6 of the report but again supplements it to the extent relevant and seen as helpful in this exercise, with an account of and comparisons with the code experience in the UK.

In the UK the GSCOP has been in place for seven years and the GCA for just over three years. At the outset it is perhaps notable to observe that in Australia the discourse surrounding the need to regulate supermarket-supplier relations has been as much if not more about fair trading than competition (albeit often with a link between the two). In the UK, by contrast, the primary if not exclusive focus originally and continues to be on competition and efficiency in the supply chain (as ultimately in aid of consumer welfare) justifying the introduction of the GSCOP and the establishment of the GCA.<sup>957</sup> This was clear in the CC's 2008 report which called for the GSCOP and the GCA, was confirmed repeatedly in our UK interviews, and is reiterated in the recently completed review of the GCA, referred to below. These regulatory interventions were rationalised solely on competition grounds, to address market failure caused by supply chain practices that were viewed as transferring excessive risks to suppliers, in turn dampening incentives for innovation and investment and consequently resulting in consumer detriment, through a potential lack of choice and quality.<sup>958</sup> As one interviewee, an experienced legal practitioner, recounted:

*[The UK Code is] explicitly stated as a solution to a competition problem. It's explicitly not about fairness or anything else; it's about a market failure...it was about consumer welfare, it wasn't about fairness to competitors, it wasn't about fairness to all small suppliers or anything*

<sup>957</sup> See, e.g., Competition Commission News Release 33/06, *Groceries Issue Statement*, 15 June 2006, in Seely, p. 22.

<sup>958</sup> CC 2008 report, [9.66]-[9.67]. See also Transcript of interview, John Noble, British Brands Group, p. 35; Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [28].

*else. ... It was explicitly stated as: this will harm consumer welfare in the medium term because choice and innovation will suffer. And that's what we're trying to fix.*<sup>959</sup>

This is not to discount the influence of 'a mood around fairness' and a 'mood around the impact on farmers'<sup>960</sup> even if, as in Australia, the policy response did not ultimately address at least the latter. Correspondingly, there are views amongst UK commentators to the effect that codes and ombudsmen of the kind adopted in the UK and Australia reflect the reactivity of politics, and a 'political choice' about the need to protect small business and have in fact 'nothing to do with competition'<sup>961</sup> and, further, that the empirical evidence supporting risks to dynamic inefficiency in upstream grocery supply chains is weak.<sup>962</sup>

It is also relevant to note that in the UK there is no counterpart to the business-to-business fair trading provisions in the CCA. Perhaps reflecting this and the fact that the GSCOP is an instrument that was created by the CC, the emphasis on competition as distinct from fair trading or other equity-related considerations is readily apparent in the statement of purposes relevant to the GSCOP. The text of the Code is contained in a Schedule to an Order made by the then CC pursuant to its powers under the *Enterprise Act 2002*, the Groceries (Supply Chain Practices) Market Investigation Order 2009. The background to the Order states that the Order is made:

*... for the purpose of remedying, mitigating or preventing the adverse effects on competition concerned and for the purpose of remedying, mitigating or preventing detrimental effects on customers so far as they have resulted from, or may be expected to result from, the adverse effects on competition.*<sup>963</sup>

Following three years of the GCA's operation (the same time frame applicable to the FGCC review), the UK government conducted a review of the performance of the GCA to date, in which submissions were sought from stakeholders on the Adjudicator's performance, how much her powers have been exercised, how effective she has been in enforcing the GSCOP, whether to make orders relating to information gathering in investigations, whether to amend or replace the order that confers power on the GCA to impose financial penalties, whether some or all of the GCA's functions should be transferred to another public body and whether to close down the GCA.<sup>964</sup> The results published in 2017 constitute an unambiguous commendation of the GCA and her work over the review period, finding that the GCA has been effective in the role of administering and enforcing GSCOP and concluding that there was 'evidence of a positive shift in the relationship between large retailers and

<sup>959</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 15.

<sup>960</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 3

<sup>961</sup> Transcript of interview, former senior representative of the UK OFT, p. 3.

<sup>962</sup> Transcript of interview, former senior representative of the UK OFT; Transcript of interview, compliance manager at a major UK retailer, p. 9.

<sup>963</sup> CC, GSCOP (The Groceries (Supply Chain Practices) Market Investigation Order 2009, UK, p. 2.

<sup>964</sup> Department for Business, Energy & Industrial Strategy and Groceries Code Adjudicator, *Groceries Code Adjudicator: statutory review*, 18 October 2016, <https://www.gov.uk/government/consultations/groceries-code-adjudicator-statutory-review>.

direct suppliers and an end to some of the unfair trading practices that were prevalent before the Adjudicator was appointed.<sup>965</sup>

As mentioned previously, the government has called also for evidence on the question whether to extend the remit of the GCA to indirect suppliers, which predominantly means primary producers and farmers.<sup>966</sup> This reflects the continuing preoccupation with the plight of the primary production sector, and the political heat that it generates, notwithstanding that in neither the UK nor Australia have the Codes to date been extended to indirect suppliers and nor is it clear that these instruments would be appropriate or effective in addressing the myriad of challenges facing farmers. As a UK commentator pointed out in our interview with him:

*...when you go along to the conferences and meetings, people are talking about the prices that primary producers get. And there are two issues [with] that. Because the code does not talk about price, the adjudicator has no powers to determine the prices that people get paid. And the second thing is, it doesn't protect primary producers if they go through a secondary supplier. Because it's a direct relationship with the supermarket and the secondary supplier. So there are apparent gaps, [but] the pressures and the push to have someone deal with this, are sort of misdirected, because this architecture is not dealing with the policy issue.<sup>967</sup>*

At the time of writing this report, the Department of Business, Energy & Industrial Strategy and Groceries were analysing feedback received and the results of the review on the GCA's remit extension were yet to be released.

## I. Trust and cooperation

Decoded, whether and the extent to which this element of the FGCC's purpose is being fulfilled is in essence a question of whether and the extent to which the Code is changing behaviours in the buyer-supplier relationship and arguably in ways that reflect not just the letter but the spirit of the Code (bearing in mind that the Code itself does not prescribe 'trust and cooperation'; rather such relational qualities are implicit in many of its provisions). As mentioned previously, given that behavioural change of this nature and on this scale means changing deeply ingrained expectations and ways of operating and interacting, it may well be just too soon to draw any firm conclusions as to the fulfilment to date of this purpose. However, based on our research and the analysis and findings set out above, it is possible to make at least the following observations.

As pointed out in Part 6, any behavioural change is predicated upon both buyers and suppliers being both aware of and understanding the provisions of the FGCC and their implications in the context of

<sup>965</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [7].

<sup>966</sup> Department for Business, Energy & Industrial Strategy and Groceries Code Adjudicator, *Groceries Code Adjudicator: extending its remit*, 18 October 2016, <https://www.gov.uk/government/consultations/groceries-code-adjudicator-extending-its-remit>.

<sup>967</sup> Transcript of interview, director, leading UK economics consultancy, pp. 17-18. See also Transcript of interview, compliance manager at a major UK retailer, p. 18 supporting the view that GSCOP should not be extended.

supply negotiations, agreements and, as relevant, disputes. On the buying side it is evident that the retailer signatories, the MSCs at least, have gone to considerable lengths to ensure that awareness of and training in the FGCC penetrates all relevant corners of their sizeable organisations. Reports from the UK are to similar effect as regards the seriousness with which the retailers have taken on their obligations under GSCOP, noting at the same time that that Code is mandatory and that there was a notable pick up in compliance response once the GCA was appointed in 2013. Tacon recalls that upon passage of the Code in 2010, retailers took steps to introduce written supply agreements and train their buyers. She is less certain that CCOs were appointed and she has doubts as to the extent to which these roles had any prominence in the actual operation of supply arrangements. Upon her appointment, however, ‘all of a sudden a lot of the CCOs changed when they realised how much I was going to be asking them to do’ and those retailers who had not taken action in this respect, acted with speed to get these appointments in place.<sup>968</sup> A similar observation was made by the UK consultant:

*... on the back of the code and the adjudicator, the large supermarkets are investing much more heavily in staff training programs ... that’s prompted by the adjudicator and the code being more rigidly enforced, rather than being something that they’re doing unilaterally.*<sup>969</sup>

A compliance manager at one of the major grocery retailers in the UK told us that their employer ‘has been supportive of the code ... it’s been very supportive of the GCA and will continue to do so.’<sup>970</sup> She explained that while the retailer already had a code of practice that aligned with the spirit of GSCOP, the formal instrument has required considerable tightening up and monitoring of processes, as well as much more systematic training of staff, and auditing of complaints and responses to them. She saw this as a positive development.<sup>971</sup>

*It [referring to GSCOP] has brought some clarity around the way we operate and how other supermarkets are operating. It has given us some things to have a look at, and out of all these things, it doesn’t harm to have a look at your own processes again, and say, “Okay, have we got it absolutely right? Can we do any better?”*<sup>972</sup>

Notably, in the recently completed review of the GCA, it was noted that while there had been opposition initially to the establishment of the GCA by large retailers, concerns about the administrative burdens and the potential inhibition of commercial practices, such concerns had not been realised. Indeed, in responses to the consultation for the review, the large retailers indicated that they saw ‘the GCA as having a beneficial impact on the groceries market, by increasing scrutiny over retailers’ compliance with the Code, increasing understanding of the Code by all parties and increasing awareness amongst large retailers of supplier concerns’. As noted in the report, one large

<sup>968</sup> Transcript of interview, Christine Tacon, p. 13.

<sup>969</sup> Transcript of interview, director, leading UK economics consultancy, p. 22.

<sup>970</sup> Transcript of interview, compliance manager at a major UK retailer, p. 12.

<sup>971</sup> Transcript of interview, compliance manager at a major UK retailer, p. 14.

<sup>972</sup> Transcript of interview, compliance manager at a major UK retailer, p. 19.

retailer has pointed out that ‘ “by focusing on improving efficiencies and removing uncertainty from the supply chain, the Adjudicator has reinforced the impetus for change in the industry”’.<sup>973</sup>

On the supply side, the picture is much more mixed, in both Australia and the UK. At home, courtesy to a significant extent of the efforts of the AFGC, a large number of suppliers have been told about, if not received training in, the Code. That said, the AFGC membership represents only a small fraction of the overall supplier community – some 200 businesses are members of the association, out of a sector that encompasses some 3,000-4,000 businesses (ie only approx. 5%).<sup>974</sup> Moreover, as Dawson acknowledges, larger suppliers are likely to be disproportionately represented amongst those who have benefitted from training – whether AFGC-provided or self-initiated harnessing internal and/or external legal resources.

The head of the AFGC equivalent in the UK, the British Brands Group, was less optimistic about the level of awareness among its members, ‘we want all the suppliers to understand GSCOP and be able to use it and we’re rather shocked, shall we say, that they’ve been rather slow off the mark.’<sup>975</sup> That said, an annual survey conducted by the GCA indicated that as of 2016, 45% of large suppliers had received training on the Code, as compared with 29% of small and 28% of medium size suppliers. For 42% of respondents, this training was being conducted by an external agency or consultancy, 35% by the GCA’s office and 26% by a trade association.<sup>976</sup> Of those who had not received training, 56% reported that they either did not know training was available or did not know how to access or who provides it.<sup>977</sup>

Lack of awareness in both jurisdictions may in part just be a product of time. We certainly got this sense from our interviewees in the UK where the GSCOP has been in place now for seven years, a compliance manager at one of the major retailers reflecting that ‘...awareness from the supply base is good...the trends over the last couple of years are all going in the right direction, in terms of awareness, in terms of number of issues being raised.’<sup>978</sup>

In her 2015-16 Annual Report the GCA reported that, at least with regard to the GCA annual survey, awareness among suppliers had doubled, increasing from 574 in 2014 to 1,145 in 2016. Respondents in 2016 included 978 direct suppliers (representing 85% of the total), 163 indirect suppliers and 41 trade associations.<sup>979</sup> Overall awareness of the GCA among direct suppliers increased from 71% to 78% between 2015 and 2016, however the level of awareness varied across the sector. Earlier annual reports highlighted the lack of supplier awareness of the GCA as a key issue that was to be targeted.<sup>980</sup>

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<sup>973</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017,

<sup>974</sup> Transcript of interview, Gary Dawson 2, p. 1.

<sup>975</sup> Transcript of interview, John Noble, British Brands Group p. 6.

<sup>976</sup> As these percentages exceed 100% in total it may be assumed that a small proportion of respondents may have sourced training from more than one training provider.

<sup>977</sup> GCA, *GCA Annual Survey Results 2016*, YouGov, pp.13-14.

<sup>978</sup> Transcript of interview, compliance manager at a major UK retailer, p. 21.

<sup>979</sup> *GCA Annual Report 2015-16*, p. 17.

<sup>980</sup> *GCA Annual Report 2013-14*, p. 10; *GCA Annual Report 2014-15*, p. 50.

While these figures suggest awareness is increasing it is worth noting the potential for self-selecting bias to creep into the findings:

*... so what about all the people who didn't fill out a questionnaire? Because [if] I know nothing about GSCOP, I won't bother filling in the questionnaire. So my feeling is that actually the levels of awareness are lower than her YouGov survey would indicate.*<sup>981</sup>

Moreover, in the July 2017 report on the GCA review, it was noted that there was significant work to be done in improving awareness of the GSCOP and increasing the number of suppliers trained on the Code.<sup>982</sup> Evidently, this is seen as an ongoing project.

In addition, the apparent high awareness amongst large suppliers relative to small suppliers is not as troubling as it might first seem. This is because, as one UK observer put it, larger suppliers 'can be the canary in the mine'. She went on to explain:

*A lot of the practices that happen in the supermarkets are not - we're not really talking about things that happen bilaterally in any single individual relationship. If a grocer has a policy of behaving in a particular way, if they do something in particular, they'll do it across the board and chances are that it will be beating up the small suppliers even harder than it's beating up the large suppliers, who can't actually stand up for themselves to a degree. So if there is something that a big supplier is willing to speak about as an issue that is badly affecting them, you can pretty much bet that it's affecting the smaller supplier who won't speak up even more. So it's a way of actually exposing some of these issues that will not get exposed, because small suppliers more struggle to speak up... it's been bigger suppliers who are willing to keep the pressure up.*<sup>983</sup>

It is also clear that the GCA herself has been highly instrumental in the UK in generating awareness and understanding of the implications of the GSCOP, not just amongst suppliers but as if not more importantly, amongst retailers – using the CCOs, with whom she has cultivated a close working relationship, as a key channel into these organisations. For example, Tacon holds quarterly meetings with these managers at which she reports back on issues that she has been hearing in the industry and seeks their input and views. Minutes of these meetings are published on the GCA website.<sup>984</sup> It is expected that managers will report back to her on issues she has raised at the next meeting and her reflection on this approach is that 'the Code Compliance Officers have all been listening to what I've been saying and taking it backstage to resolve.'<sup>985</sup>

<sup>981</sup> Transcript of interview, John Noble, British Brands Group, p. 39.

<sup>982</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [8].

<sup>983</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, 22.

<sup>984</sup> See e.g. <https://www.gov.uk/government/publications/meeting-record-december-2016-quarterly-meetings>.

<sup>985</sup> Transcript of interview, Christine Tacon, p. 14.

Tacon also holds regular 'Supplier mornings',<sup>986</sup> and publishes quarterly newsletters,<sup>987</sup> best practice statements<sup>988</sup> and case studies,<sup>989</sup> all of which are intended not only to raise the profile of GSCOP and her work but to guide industry participants in developing ways of working that are in compliance with the Code – measures reported on as having positive effects in the recent review.<sup>990</sup> It is notable that the GCA does all this despite being a part-time appointee only (she works three days per week) and having an office run on a skeletal staff made up of government secondees and contractors. Tacon's office is wholly funded by a levy on the retailers which for 2016/17 was £2 million.<sup>991</sup> For the Tesco investigation, an external law firm was contracted to assist the GCA and as some have pointed out, 'hiring an external law firm to run a regulatory investigation is suboptimal because they don't know how to do it.'<sup>992</sup> The question of funding and staff for the GCA was canvassed in the recent review and it was concluded that given the GCA had proven to be so effective, the current resourcing arrangements should be seen as sufficient.<sup>993</sup>

As mentioned above, the GCA also conducts annual surveys, similar to but more extensive than the AFGC annual survey of its members previously referred. This acts as a mechanism by which to collect information on current Code-related concerns and uses the results of these, which are presented at an annual conference, to help her set her top priorities and generate discussion in the industry about how specific practices and code compliance generally can be improved. There is significant participation in these surveys – in 2016, the survey was completed on behalf of 921 direct suppliers, 105 indirect suppliers and 44 trade associations.<sup>994</sup> In addition to collecting data on levels of awareness of GSCOP, the surveys canvasses views on:

- readiness by suppliers to raise issues with the GCA;
- reasons for not raising an issue;
- awareness of the availability of training and extent to which suppliers are being trained on the Code;
- extent to which suppliers have written supply agreements with designated retailers;
- extent to which suppliers know who and where to find a retailer's CCO; and
- experiences with specific issues such as aspects of retailer practice that are having the most negative impact.

One of the innovative aspects of these surveys is the publication of a 'league table' reflecting respondent supplier views on change in retailer practice over the last year and overall assessment of

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<sup>986</sup> News story, 'GCA Supplier Mornings' 3 March 2017, <https://www.gov.uk/government/news/gca-supplier-mornings>

<sup>987</sup> GCA, Newsletters, <https://www.gov.uk/government/collections/gca-newsletters>.

<sup>988</sup> GCA, Best Practice Statements, 24 January 2017, <https://www.gov.uk/government/collections/gca-best-practice-statements>.

<sup>989</sup> GCA, Code clarification case studies, 14 June 2016, <https://www.gov.uk/government/collections/code-clarification-case-studies>.

<sup>990</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [10], [64]-[72].

<sup>991</sup> Department for Business, Energy & Industrial Strategy and Groceries Code Adjudicator, *Groceries Code Adjudicator: statutory review*, 18 October 2016, Part 1.

<sup>992</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p.39.

<sup>993</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [73]-[74].

<sup>994</sup> GCA, *GCA Annual Survey Results 2016*, YouGov.

Code compliance. In the 2016 survey results, for example, Aldi was ranked highest, 98% rating the retailer as either complying consistently well or mostly with the Code, whereas Morrisons ranked lowest, with 80% across these criteria.<sup>995</sup> Tacon reflects that it is this particular aspect of the survey that has had ‘the biggest impact’ – retailers are now competing with each other to rank well on the GCA survey and in the eyes of their suppliers in relation to GSCOP compliance.<sup>996</sup>

In addition to the GCA survey findings and the ‘league table’ rankings, all grocery retailers operating under the GSCOP must publish the summaries of their GSCOP compliance that they are required under the Order to submit to the CMA. The British Brands Group in turn reviews these published summaries and publishes them on their website. In their most recent review the Group found that while retailers were ‘broadly’ meeting the statutory requirements the reports provided, ‘little in the way of insight or elucidation.’<sup>997</sup> The review also stresses that this self-reporting by the retailers provides, ‘just one perspective and in a formal compliance context’ and that the GCA survey is complementary in its provision of an additional viewpoint.<sup>998</sup>

The impact that Tacon has had on awareness in the industry and in prompting retailers to take steps to ensure compliance with the UK Code is reflected on positively by industry observers:

*... one of the things that Christine Tacon has done well is to raise awareness of the issues, to get people around the table and discuss things and to the extent that supermarkets are putting in place, structures internally and training and compliance programs to raise awareness inside the supermarkets of the code and how they should apply this. That is likely to reduce the need to launch investigations.*<sup>999</sup>

These sentiments were echoed in the 2016-17 review of the GCA, emphasising that Tacon’s approach of raising awareness and engaging with parties across the sector had almost certainly reduced the need for formal action by way of investigations and arbitrations to be taken to a greater extent and had allowed the focus to be on engendering voluntary compliance.<sup>1000</sup>

As also noted in Part 6, being aware of or even trained in a new set of rules, no matter how practical or applied the training or accomplished the trainers, does not necessarily translate into appreciation of how to ‘use’ the rules to proper or best effect in the setting of an actual negotiation or dispute. Such appreciation is also inevitably going to take time and various kinds of regular reinforcement (examples of which are available from the UK experience) to infiltrate in a practical sense. This is particularly so given the not unexpected levels of scepticism, cynicism even, amongst suppliers, referred to above.

<sup>995</sup> GCA, *GCA Annual Survey Results 2016*, YouGov.

<sup>996</sup> Transcript of interview, Christine Tacon, p. 13.

<sup>997</sup> See, eg, the Aldi summary for 2015-16 in British Brands Group, ‘Retailers’ GSCOP reports for 2015-16: a review of retailers’ published reports on compliance’,

<http://www.britishbrandsgroup.org.uk/upload/file/GSCOP%20retailer%20compliance%20report%202015-16.pdf>

<sup>998</sup> British Brands Group, ‘Retailers’ GSCOP reports for 2015-16: a review of retailers’ published reports on compliance’,

<http://www.britishbrandsgroup.org.uk/upload/file/GSCOP%20retailer%20compliance%20report%202015-16.pdf>

<sup>999</sup> Transcript of interview, former senior representative of the UK OFT, p. 32.

<sup>1000</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [45]-47].

In the short time that has passed since the FGCC taking effect, however, there appear to be signs that, amongst some suppliers at least, the Code's provisions are being used. This is in the sense at least of providing them with a basis on which to raise and test matters relevant to their trading terms and conditions in a way that was not previously seen as possible, for whatever reason. As the UK adjudicator notes, simply having a Code – or perhaps an adjudicator – has had a positive impact:

*But people were saying to me, just having me there is making a difference and things are better, they see changes... they are noticing it. And I think that most of them like to feel I'm making a difference, but the market is very hard. The competition is tough.*<sup>1001</sup>

It is arguable that Tacon underestimates the positive impact she has had and, in particular, how favourably her collaborative approach in working with CCOs and in turn as an intermediary between these representatives of retailers and suppliers is seen, a feature of her effectiveness to date remarked on in the recently completed review of the GCA.<sup>1002</sup> Indeed, according to one of our interviewees, the GCA is seen to have been so effective that there are now proposals to replicate the model in other sectors.<sup>1003</sup> She points out that for a role of this nature to be effective, you need someone:

*... who knows enough about the industry, knows enough about where the skeletons are buried, can take a softly softly approach... that dialogue [between the GCA and industry members] does make a difference and I think that having someone who can engage that meaningfully is more useful than having an ex-Judge who sat there waiting to see if there was any dispute that can come in for you to tackle.*<sup>1004</sup>

At least for one observer close to suppliers – the head of the British Brands Group – the GCA's approach has given the CCO role real meaning and enabled it to be used effectively as a conduit for mediating on issues as they arise in supply arrangements (including on issues that are not strictly covered by the GSCOP):

*We always knew the code compliance [officer role] would be there but we never really envisaged how it might work, and I thought it was a flash of inspiration and skill that Christine was able to get the relationship going with code compliance officers. I think it's brought a huge, huge benefit and the reason for it is that suppliers don't want an antagonistic relationship either individually or necessarily through the regulator. They'd much rather see things worked out in this area in a collaborative, positive way if at all possible, and that's exactly what Christine is doing with the code of compliance officers. But she's been very firm about what her areas of focus are and where she's looking to them to come up with improvements. I think it's very telling that she got a voluntary agreement, for example, on*

<sup>1001</sup> Transcript of interview, Christine Tacon, p. 24.

<sup>1002</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [10]-[106].

<sup>1003</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 12, referring to the proposal for a 'pub adjudicator'.

<sup>1004</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 19.

*forensic auditing for 8 of the 10 designated retailers. In strict terms, you could argue that it was not entirely a GSCOP matter, but it was her relationship with the [code compliance officers] and her listening to suppliers saying these forensic audits were giving huge problems, that she was able to broker an agreement. That, for me, is testament to her role and skill. If she didn't have that collaborative arrangement she would be limited to taking on one or two issues a year in the form of big investigations which are very costly and no doubt challengeable. As it is, she has instead five priority areas of focus, more than double what might be achievable otherwise. It is so much better to be able to deal with concerns with the cooperation of code compliance officers, and so that's why I think it is an inspiration, to be honest.*<sup>1005</sup>

Another interviewee describes the approach taken by GCA in using the CCOs to air supplier concerns and stave off the escalation of disputes as follows:

*...having a channel to resolve some of these things without escalating them is really quite effective, and she can do it in a way that individual suppliers can't, so she can go say "look, I'm hearing stuff about what you're doing on third party packaging, can you explain to me what it is you're doing? I'm not using my formal powers, but I'd quite like to understand what you're up to." Oh, okay, let's see, okay best practice would be to do this, can you go away and look at it. I'm not using any of my formal powers, I'm not going to put a case study in place, but actually can you think about best practice and here are principles of best practice to do that." That's the kind of outcome you can achieve with her in that role that you couldn't achieve in any way, really.*<sup>1006</sup>

It appears that this approach is paying off for suppliers in the UK, if not also for retailers given that, as pointed out in the 2017 review, the 'current, collaborative process is highly regarded and a means that has, to date, avoided any further, full investigations'.<sup>1007</sup> One supplier advisor told us that as a result of the GCA's activities:

*...there's certainly much more confidence on the supplier's side. Commercially, there's all sorts of pressures. But in terms of confidence to engage the code. Anecdotally, plenty of people will tell me we've raised the code in negotiations and actually, it's been effective in getting it all - so I've heard back from more than one. There is now a little cottage industry of people who train suppliers on the use of the code, which didn't exist until the last two or three years. So people are seeing some value in that. There has certainly been much more interest on supply. So I think in 2010, you were still looking at quite a sceptical audience. I*

<sup>1005</sup> Transcript of interview, John Noble, British Brands Group, p. 40.

<sup>1006</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 20.

<sup>1007</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [92].

*think 2013 sort of changed the perception of it on the supplier's side and I think the launch of the Tesco investigation, it changed it again.*<sup>1008</sup>

On the buyer side, the same interviewee also saw change:

*I think people's views and people's behaviours of what is acceptable has shifted.*

..

*I mean yeah, the fact that these buyers are trained the whole time on this stuff, it doesn't go without having an impact, it does.*<sup>1009</sup>

It may be too early to say whether the positive changes in UK retailer-supplier relations that are attributed to the role being played by the GCA are likely to be replicated in Australia. Arguably not, given that the ACCC is unlikely to play a similar role. Its role is clearly as enforcer rather than as mediator in relation to the FGCC. This raises the question whether in fact a dedicated ombudsman-style scheme should be introduced here. As recounted above, many pressed for it in the FGCC consultation by Treasury and it was recommended by the report of the subsequent Senate inquiry. No doubt, it is an issue that will be revisited in the forthcoming review.

The extent to which early experiences with the FGCC instil confidence in suppliers to continue in the vein of using the Code, and in turn strengthen trust and confidence in their relationship with their customers and in the Code itself, is likely to depend very much on how MSC personnel respond to suppliers raising Code-related issues. To the extent that such personnel show a receptiveness to listen to and act on concerns raised in relation to the application of the Code provisions, such confidence is likely to grow. This in turn requires that buyers themselves see the FGCC as a positive development.

To the extent that retailer responses are dismissive of or result in what appears to the supplier in question to be an exercise in semantic interpretation (so as to require legal input even perhaps), the inverse will apply. This too, and with it the slow pace of cultural change, is evident in the UK, suggesting not unexpectedly that responses will vary across the industry and even within individual retail organisations:

*If you speak to some of the hardened old-school buyers, some of the people who have worked for supermarkets for a long time, they would tell you that she's [the GCA] ruined the grocery sector, closed off a revenue stream....*<sup>1010</sup>

The necessarily snail's pace development of more trust and cooperation in these relationships will not only depend on the experience in and outcomes of actually using the FGCC, however. Other communications, actions and initiatives of the MSCs that bear on supplier relationships in general are

<sup>1008</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 30.

<sup>1009</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 45.

<sup>1010</sup> Transcript of interview, John Noble, British Brands Group, p. 36.

likely to set a tone or create an environment that is either conducive to or damaging of these relationships and the extent to which the Code is able to play a meaningful role in strengthening them. By way of illustration, as previously highlighted in this report, there has been the episode of the Woolworths Chairman promising 'higher standards' while at the same time standing behind the company's decision to defend allegations of unconscionability on the ground that a scheme such as 'Mind the Gap' was a normal and by implication acceptable mode of doing business. Such an episode is likely at best to send a mixed signal, at worst to engender further cynicism and potentially have the effect of undermining the efficacy of the Code.

In the UK it is material to note in this regard that the GCA not only works with and through the CCOs who she describes as her 'mouthpiece' but she has also asked for and been given for each designated retailer, a CEO or 'board level contact' and for listed companies, has annual meetings with the chairman of the board's audit committee (a person she points out is 'acutely aware of what the regulator can do and of risk').<sup>1011</sup> It is to be expected that this helps to ensure that the messages about the importance of Code compliance are as much top down as bottom up. As Tacon explains, these contacts are important to ensure that retailers have a culture conducive to compliance and that is critical because 'you can say everyone is trained in [the Code], but [then be] putting pressure on your buyers, such that the only way they can achieve what you've asked them to achieve is by breaking the code.'<sup>1012</sup> This view is supported by experienced consultants in the UK who observe that 'at board level, the issue of supplier relations and goods violations is something that boards care about... is the prime driver of what they do..'<sup>1013</sup> They also remark that the introduction of substantial fining powers for the GCA would have concentrated the minds of retailer boards even further.<sup>1014</sup>

Like the ACCC, the GCA also has powers to launch formal investigations relating to alleged breaches of GSCOP and significantly but, unlike the ACCC, since April 2015 has had the power to impose a maximum financial penalty of 1% of the relevant retailer's UK turnover.<sup>1015</sup> As noted previously, the UK Secretary of State for Business, Innovation and Skills, Vince Cable, had said in 2012 that he reserved the right to introduce pecuniary penalties if naming and shaming measures alone provided insufficient to bring about industry change.<sup>1016</sup> In response to the outcome of the Tesco investigation Cable was reported as saying:

*This is an historic day for the groceries code adjudicator and shows we have created a regulator that has real teeth.*

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<sup>1011</sup> Transcript of interview, Christine Tacon, p. 17.

<sup>1012</sup> Transcript of interview, Christine Tacon, p. 32.

<sup>1013</sup> Transcript of interview, former senior representative of the UK OFT, p.27.

<sup>1014</sup> That said, such matters are clearly relative. As another interviewee pointed out, when Tesco was facing a criminal investigation, including potential jail terms for individuals, in a recent Serious Fraud Office matter this would have had to have been 'much higher up the food chains in terms of Tesco's concerns than the code' (Transcript of interview, experienced legal advisor to suppliers in the UK, p. 29).

<sup>1015</sup> The GCA's power to issue a financial penalty was brought into effect by the Groceries Code Adjudicator (Permitted Maximum Financial Penalty) Order 2015 which came into force on 6 April 2015.

<sup>1016</sup> Rebecca Smithers, "'Unfair' supermarkets could face hefty fines under new watchdog", *The Guardian*, 5 December 2012.

*Last week I secured the final agreement in government to proceed with legislation to enable the regulator to impose hefty fines for those supermarkets found guilty of mistreating suppliers.<sup>1017</sup>*

Such powers and potential sanctions too no doubt play a role in sharpening the attention of retailer senior management on the consequences of falling short in performance on code compliance.

To date the GCA has held only one investigation – into delayed payments and payment for positioning by Tesco. She found a breach of GSCOP in respect of the former, but not in respect of the latter. After a two year investigation that involved extensive information gathering, in her lengthy report released in January 2016, Tacon found that the breach with respect to delayed payments had arisen in only a minority of instances and was ascribable to a range of factors, including data input errors and duplicate invoicing but also and more significantly for senior Tesco management, due to the retailer's focus on meeting financial targets:

*It was clear from the evidence that a major focus of the Tesco commercial team during the investigation period was on hitting budgeted margin targets. A percentage margin target was a key element of many of the Joint Business Plans (“JBP”) which Tesco negotiated with suppliers on a periodic basis. Payments to maintain the margin target were requested from suppliers by Tesco regardless of whether the planned growth had been achieved and regardless of whether Tesco had delivered on its own JBP commitments. I found that the direction being given to Tesco's buying team as to the status and enforceability of JBP targets was contradictory and unclear. I received internal Tesco emails which encouraged Tesco staff to seek agreement from suppliers to the deferral of payments due to them in order temporarily to help Tesco margin. I also saw internal Tesco emails suggesting that payments should not be made to suppliers before a certain date in order to avoid underperformance against a forecasted margin. I found that Tesco knowingly delayed paying money to suppliers in order to improve its own financial position.<sup>1018</sup>*

Tacon further found that ‘cultural’ factors were at play:

*One of the key cultural factors which contributed to delay in payments was the apparent reluctance of some Tesco buyers to pro-actively engage in the resolution of payment disputes. There were times when Tesco did not appear to even attempt to resolve supplier concerns before unilaterally deducting money from suppliers. I found the delay that resulted from a failure by Tesco to fully engage in resolving difficulties to be unfair and unreasonable. Buyers frequently sought to use money owed to a supplier as leverage in negotiations for future agreements or promotions. I found that Tesco acted unreasonably when seeking to*

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<sup>1017</sup> Matthew Weaver, ‘Tesco under investigation by new regulator over dealings with suppliers’, *The Guardian*, 5 February 2015.

<sup>1018</sup> GCA, Investigation into Tesco plc, 26 January 2016, p. 6.

*bring the resolution of debts into other commercial negotiations and delaying payment of monies owed until other negotiated terms were agreed.*<sup>1019</sup>

The GCA did not have the power to financially sanction the company retrospectively but she made a series of recommendations directed at preventing the recurrence of the practices in question, required Tesco to provide a detailed implementation plan within four weeks of the report's publication and to then report quarterly on compliance with the recommendations.<sup>1020</sup>

Demonstrating arguable parallels with Coles's response to the ACCC's unconscionable conduct action, the GCA's investigation and findings elicited a positive and constructive response. Tesco chief executive Dave Lewis reportedly said Tesco had changed substantially:

*Over the last year we have worked hard to make Tesco a very different company from the one described in the GCA report. The absolute focus on operating margin had damaging consequences for the business and our relationship with suppliers. This has now been fundamentally changed.*<sup>1021</sup>

Evidently this was more than just words. At the Food and Drink Federation Convention in London in late June 2016 Tesco Chief Product Officer Jason Tarry again emphasised the importance of rebuilding trust and transparency with suppliers so as to ensure that the company could provide the best service to their customers:

*Crucially, we want to do this by working with our partners in a simple and straightforward way which is good for our customers, good for our suppliers, and good for Tesco. So, over the last year, we've put in place a number of measures to help improve the way we work with our suppliers.*<sup>1022</sup>

Steps taken reportedly included the introduction of a 'Fair for Farmers Guarantee' in support for British dairy farmers; and the announcement of the first long-term contracts for potato farmers and packers, worth £12 million (\$20.6 million) over three years. A supplier survey subsequently conducted by the GCA that included approximately 500 Tesco suppliers found 65% of respondents had seen an improvement in the way Tesco operates, making Tesco the most improved retailer in that survey.<sup>1023</sup> This is consistent with the positive report from British Brands Group's John Noble about the impact of the GCA's investigation into Britain's biggest grocery retailer on the situation for suppliers generally:

*... the Tesco investigation made a huge impact for suppliers. Before it, money would be unilaterally deducted from trading accounts for all sorts of reasons, and trying to get that money back when it had been wrongly deducted could be a real struggle and not always*

<sup>1019</sup> GCA, Investigation into Tesco plc, 26 January 2016, p. 7.

<sup>1020</sup> The five recommendations of the GCA were: (1) Money owed to suppliers for goods supplied must be paid in accordance with the terms for payment agreed between Tesco and the supplier; (2) Tesco must not make unilateral deductions; (3) data input errors identified by suppliers must be resolved promptly; (4) Tesco must provide transparency and clarity in its dealings with suppliers; and (5) Tesco finance teams and buyers must be trained in the findings from this investigation.

<sup>1021</sup> Emma Simpson, Tesco knowingly delayed payments to suppliers', *BBC News*, 26 January 2016.

<sup>1022</sup> 'International news: Tesco improves supplier relations', *RetailWorld*, 8 July 2016.

<sup>1023</sup> 'International news: Tesco improves supplier relations', *RetailWorld*, 8 July 2016.

*successful – you might need to negotiate a solution; you may get a better deal later on but not actually get your money back. Now such deductions are much more difficult and that, for me, has a huge impact on suppliers' certainty of doing business. That was a big win, I think, for Christine too and absolutely on message on what the code's all about. It was a prevalent practice.*<sup>1024</sup>

Another interviewee sees the Tesco case as having had a positive impact in raising the profile of the GSCOP and the GCA generally:

*For whatever reason, it attracted a lot of attention and interest and I'm finding people coming to me, which I haven't had for years, where people come to me and say, well, we understand more about the code, can you come in and train us, can you come talk to us. It's been a slog trying to persuade people that they ought to be interested in it and actually, it's the other way around now. And you know, smaller national suppliers who are not the people who are usually on top of this stuff are now following it closely anyway.*<sup>1025</sup>

Noble is also highly complementary of the way in which Tacon handled the investigation and reflects that the outcomes that she secured would not have been secured by the CMA:

*...generally speaking [suppliers] ...feel that the Tesco investigation and the way that she dealt with the findings in her report where she was direct and forthright was spot on. And I can't see how else you would have got that report in the public domain without an independent adjudicator. I cannot see the CMA producing a report like that. And it hit the nail on the head. It has, I think, changed the ten designated retailers' way of trading significantly for the better.*<sup>1026</sup>

Others too, despite having initially harboured scepticism about the need for and potentially anti-competitive effects of the GCA, are favourable in their view of the balanced way in which Tacon approached her findings in the investigation:

*I was impressed with the report on Tesco. ... What's good about it is that the GCA documents all of the problems clearly. It then says that Tesco has agreed to address all these issues. It also acknowledges that Tesco is a big supermarket and that these are a minority of instances and that in the majority of relationships there is no problem. So it is balanced and reasonable report, trying to solve a problem sensibly and without sensational headlines.*<sup>1027</sup>

Back in Australia, news that the ACCC is investigating possible code breaches is also likely to be material, either in reinforcing or in weakening FGCC-related trust and confidence amongst suppliers, depending again to some extent on MSC reactions to these investigations and their outcomes.

<sup>1024</sup> Transcript of interview, John Noble, British Brands Group, p. 38.

<sup>1025</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, pp. 31-32.

<sup>1026</sup> Transcript of interview, John Noble, British Brands Group, p. 41. See further the positive reflections on the handling of the investigation and its outcomes in Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [52]-[57].

<sup>1027</sup> Transcript of interview, former senior representative of the UK OFT, p.5.

Equally the approach taken by the ACCC in its handling of these investigations is likely to affect retailer attitudes to the Code.

## II. Transparency and certainty

There can be no quibble that the advent of written supply agreements with a set of terms and conditions that must cover the ground stipulated by the FGCC and that cannot be altered within the life of the agreement, except with the consent of the supplier, constitutes a step change in supermarket-supplier relations, and arguably for the better. The certainty provided by such agreements must enable suppliers to plan for their business in a way that would not have been or seen to have been as possible under former less formal and less stable or secure arrangements. The way in which such certainty is now manifested and its benefits for small suppliers particularly were extrapolated by a MSC representative in the following terms:

*...the small suppliers, what they get now is the certainty of trading with us. So they have published, that they can look at, the 18 months ahead. They can look at when that range next is going to be looked at, and when their products may or may not be at some risk of de-listing. And they can look at the performance, and they get details from us on how well the product is going relative to the rest of the category. They have published, in front of them, our principles for laying our products on the shelf and how much space we'll give and where we'll give space for particular items, and how much space they will get relative to their volume of sales. They get notification of when a review is about to come up, and basically three months' notice to say, your product is at risk, a noted risk of deletion; come and tell us what you want to do with your range. And then get a notice with sufficient time to have a decision, if it goes against them, reviewed by a senior manager. So suddenly you have a whole lot of concrete, set rules that a small supplier can apply to their business without having to beg or plead or appear to be doing anything other than exactly what's permitted to them. So it's quite a strong platform for small suppliers. Whereas, as you say, large suppliers could do that for themselves anyway, and use that ability to come and argue with us. But suppliers, small suppliers, now have that encoded as a right for them to come and do that, too. So it's actually very good from a small supplier point of view.<sup>1028</sup>*

As far as we are aware, there is no publicly available data on the extent to which there has been compliance by the FGCC signatories with the requirement to have written supply agreements. Results from the 2017 AFGC survey of its members indicated that substantial proportions of supplier respondents saw no improvement in the extent to which there were written supply agreements with their retailer from the previous year (34% for Coles, 43% for Woolworths and 40% for Aldi). Then again, data from the UK suggests that an expectation of 100% compliance in this respect would be overly optimistic. In that jurisdiction, despite the GSCOP having been in place for seven years, as of 2016 the GCA survey indicated that the highest level of compliance with the written supply agreement

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<sup>1028</sup> Transcript of interview, MSC representative, p. 9.

obligation was by Aldi and that was only in respect of 69% of the suppliers who responded to the survey. That said, amongst all retailers, the survey showed improved levels of compliance from the previous year,<sup>1029</sup> and the compliance manager at Waitrose whom we interviewed reflected that overall the impact of written supply agreements has been significant for suppliers, in terms of providing much greater certainty of the terms and conditions under which they are trading.<sup>1030</sup>

The banning of unilateral and retrospective variations to such agreements under the FGCC is also a particularly material and positive development for suppliers in terms of enhanced certainty. The significance of this change in the Australian context is mirrored by the experience in the UK where the GCA, when asked what the GSCOP is essentially trying to achieve, responded: 'it's about transparency at the outset'. She went on to explain that the Code is trying 'to make sure that retailers treat their supplier fairly' and 'fairness is about not doing things to people retrospectively' and 'if you are going to make any unilateral changes that you give people reasonable notice'.<sup>1031</sup>

An experienced advisor to suppliers put the benefits to suppliers of this kind of fairness in the following terms, pointing out at the same time that it is an approach embedded in the business model of retailers like Aldi independently of the Code:

*So if you've got clarity upfront, the chance of getting hit with all sorts of random stuff later, it does help the small suppliers as well, because they've clarity. They know what they're signing up to. And it might be a hard bargain, but they can take a cold hard look at that and kind of go, is it worth my while to do? And if the answer is it's not, then it's not and then the supermarkets have to think harder about what bargain they offer. I mean, it's a way it's the model that German discounters trade on. So people will say to me, actually, trading an Aldi or a Lidl is really straightforward. They have a limited range, they struck a deal with you at the outset, it's no frills, it's pretty simple, but they stick to it. And you kind of know upfront, do I want to do it, or do I not want to do it? I can plan for that, I can deal with that.*<sup>1032</sup>

Similar observations were made by a MSC representative:

*... [the Code] strikes a balance between pointing out very clearly what the base rules are for trading and operating, and therefore if someone with their eyes open chooses to come to a mutual agreement with us, to interpret the Code in a given way in relation to one particular aspect of going to market, I think that's fine. I think it's what the Code intends. It doesn't intend to have something imposed on anyone. So ... [M]any of the provisions are enabling provisions; the parties may agree to do this, or they may agree to do that. It doesn't force anything on either party, but it does make them look at things with their eyes open when they go to make an agreement.*<sup>1033</sup>

<sup>1029</sup> GCA, *GCA Annual Survey Results 2016*, YouGov, p. 17.

<sup>1030</sup> Transcript of interview, compliance manager at a major UK retailer, p. 10.

<sup>1031</sup> Transcript of interview, Christine Tacon, pp. 1-2.

<sup>1032</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 38.

<sup>1033</sup> Transcript of interview, MSC representative, pp. 7-8.

As reflected in these comments and as previously highlighted in this report, the relevant provisions as to variations and other aspects of retailer conduct (for example, as to various types of supplier payments or contributions to retailer costs), allow for agreements to deviate from the starting position - that variations and payments are not permissible. These provisions are accommodating of such conduct as long as the deviating provision in the agreement is explicit and unambiguous, and reasonable in the circumstances, and reasonable notice of the intended variation has been given. It is thus necessary to consider to what extent such accommodations are undermining the benefits that the FGCC is intended to deliver insofar as redressing the retailer-supplier imbalance in bargaining power.

A similar approach is taken in the drafting of the GSCOP which was highly influential in the Australian drafting process and, as explained in Part 6 of this report, allowing for such deviations was seen by the drafters in both jurisdictions as crucial to preserving commercial flexibility. Indeed, in the UK, one of the reasons for including the Code in a schedule to the Order made by the CC was that, in that form, it could be amended more readily.<sup>1034</sup> This was seen as important to create the flexibility needed to deal quickly and effectively with any unintended consequences.<sup>1035</sup> However, it should also be pointed out that in that jurisdiction, a substantial role is played by the GCA in facilitating agreement between retailers and suppliers as to what is 'reasonable'. This is to be contrasted with the experience under the former SCOP that preceded the GSCOP and was voluntary in nature and lacked any independent oversight or enforcement mechanism. In a 2004 report on that earlier Code, the OFT noted that the concept of 'reasonableness' was 'seen by suppliers to allow the supermarkets to interpret the Code to the detriment of suppliers, leading to uncertainty about some of the Code's key provisions and increasing reluctance to complain.'<sup>1036</sup>

In Australia, there is no informal arbiter as to reasonableness equivalent to the GCA and 'flexibility' in this context might as well as be read as code for 'bargaining'. Reaching any agreement by its very nature involves bargaining and therein lies the rub, at least as far as small but also possibly large suppliers are concerned. Notably, we heard from our MSC interviewees that in fact some small suppliers have greater bargaining power than their larger counterparts given that such suppliers:

...have many avenues to sell their products ... from the corner store through to the bespoke specialty [store], online delivery.<sup>1037</sup>

Moreover, some small suppliers with niche or distinctive brands are said to have particular power:

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<sup>1034</sup> In fact in the UK there is the arguably odd situation where some of the provisions, including those relating to the duty to have written supply agreements, appoint and train staff and the dispute resolution scheme are contained in the Order itself. Whereas the GSCOP appears as Schedule I of the Order and contains the relevant definitions, along with the provisions dealing with specific terms of agreements and retailer conduct such as the variation of supply agreements and promotions.

<sup>1035</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 10.

<sup>1036</sup> OFT press notice 28/04, 'OFT publishes supermarkets code review', 20 February 2004.

<sup>1037</sup> Transcript of interview, MSC representative, p. 21.

*... if you are the sole supplier of arrowroot powder and someone wants to bake a cake, it's very difficult [for a retailer] to delete that product, even though it may not be a major selling item in your store.<sup>1038</sup>*

MSC representatives also express the view that some large suppliers have greater bargaining power than their retail buyers, but point out that generalisations in this regard are hazardous as the competitive dynamics vary so much from one product category and even one brand to another:

*...we would say we have unequal bargaining power and we're on the lower end of the stick. We're playing against big global giants like Unilever and they might have a must stock product, that kind of thing. But then you might hop to another product that is in the same aisle and the dynamics will be completely different. So you can talk broadly about oligopolies in our economy, but I find it hard to engage with when I don't know what particular market I'm looking at – because I think it changes so much depending on that.<sup>1039</sup>*

The merits of any such arguments aside, the asymmetry in bargaining power between retailers and suppliers in the grocery sector in Australia as currently structured, is an undeniable reality and given that the FGCC of itself cannot alter the imbalance, it would seem that retailers remain in much the same position as previously, that is a position of being able to 'bargain' in favour of Code deviations in supply agreements and on so-called 'reasonable' terms that are weighted in favour of retailer interests. Such terms may not in fact be reasonable from a supplier's perspective which then raises questions as to what role the overarching requirement of good faith might have to play and also what a supplier can or may be prepared to do about the perceived unreasonableness (questions discussed below). It is perhaps notable in this respect that in the period between 2010 when GSCOP took effect and 2013 when the GCA was appointed in the UK, in the absence of a dedicated enforcement structure, the Code is said to have been used to imposed unreasonable terms on suppliers (just as the SCOP had ten years prior). As one experienced supplier advisor told us, during that period:

*...what the retailers did was use the code and the need to have terms in writing in some ways as an excuse to sort of force unfavourable terms and conditions on the supply base. They said: "oh you've got to sign these because the code requires you to", which is not the case. And they would draft in some cases quite aggressively, to try to maximise... their position.<sup>1040</sup>*

The terms that suppliers were being asked to sign up to were not in breach of the UK Code, because as the interviewee explained:

*...the code provides carve outs, right. The code says, "you will be liable to pay for full costs unless you agree otherwise, or, you will be liable" - so there's always scope in the code to agree otherwise. And so you're not having true agreement, you're having suppliers being*

<sup>1038</sup> Transcript of interview, MSC representative, p. 9.

<sup>1039</sup> Transcript of interview, MSC representative, p. 27.

<sup>1040</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 27.

*asked to sign T's and C's they don't necessarily feel they have a choice but to sign. So there was a little bit of opportunism actually, around 2010.*<sup>1041</sup>

If the UK experience is any guide it may be the case that, while the FGCC may have generated enhanced transparency and certainty and in this sense be working in a way consistent with this element of its purpose, that is not to say that it has changed or will change circumstances for suppliers in any substantive sense. Terms that are 'negotiated' may still be unfair (provided they are negotiated in good faith, are not unconscionable and do not constitute a misuse of market power, of course) but it may simply be the case that the unfairness is now more transparent and more certain.

If indeed this is the situation then there may be grounds for considering a reduction in the flexibility in the Code provisions and making them more prescriptive, with fewer carve-outs and qualifications. However, as the account provided of the Treasury consultation on the FGCC in Part 5 of his report makes clear, any such attempt is likely to be met with substantial opposition from at least the MSCs. It may well be supported by some supplier and other groups, consistent with the positions taken in the earlier consultation. Whether it is opposed or supported by the AFGC remains to be seen. However, given the pivotal role played by that organisation in this process to date, its position on the matter (which in turn can be expected to be informed by its members, and may also be affected by the turn over at the top of the association) is likely to be crucial. AFGC leadership may well have to negotiate itself between its various categories of members on this front if, as might be expected, larger members favour the retention of flexibility (commensurate with their greater degree of bargaining power with the MSCs) whilst members of the AFGC's SME Forum are less enthusiastic.

The AFGC's position aside, if a considerable tightening up of the provisions means losing the support of the MSCs, serious consideration may need to be given to mandating the Code. And, as would be evident from prior sections of this report that has not been an approach previously entertained by government. The politics entailed in such a course of action, both within government and in government's relations with 'big business', is likely to be complex. With Billson no longer in the mix (described by Dawson as having 'been one of the strongest advocates of the Code'<sup>1042</sup>), it is far from clear whether, aside from the Nationals and Joyce in particular, there would be any individual champion within current government ranks for such a course. That said, there remain members of the cross-bench concerned about the size and power of the MSCs and with the composition of Parliament at present, their influence is not to be discounted. As Dawson pointedly remarked in his final week at the AFGC, in looking ahead to the 2018 review:

*... beyond the coalition when you look at the views in the cross-bench of the Senate there are some very, very strong views there about the market power of the major retailers... [i]n the Labor party there are very strong views as well... the Labor Party and Nick Xenophon are already starting the process of getting feedback and gauging where to next.'*<sup>1043</sup>

<sup>1041</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 27.

<sup>1042</sup> AFGC Media Release, 'Food and Grocery Code of Conduct now in effect', June 2015.

<sup>1043</sup> Transcript of interview, Gary Dawson2, p. 21.

If the UK experience is any indicator, the possibility of the Code becoming mandatory cannot be discounted. As one interviewee observed of the UK experience:

*... originally the code was voluntary. It was self-regulation. And the supermarkets were expected to voluntary comply with it. There was a mechanism which said in the event that this isn't working, then we might need someone to enforce it. And that's why we've ended up with an adjudicator.*<sup>1044</sup>

As Christine Tacon said: 'I know they started off with a voluntary code of practice. ...And it, didn't work. So the next thing to do was to take it, refine it and say that this has become law now'.<sup>1045</sup>

### **III. Effective, fair and equitable dispute resolution**

It is difficult to assess the effectiveness of the FGCC's dispute resolution processes at this juncture given that, on the accounts that were available for this research, it appears that, aside from a smattering of 'referrals' to the CCMs of the MSCs, those processes have not been extensively invoked to date. While one MSC representative was unable to furnish us with exact numbers, at the time of our interview she reported that the number of disputes that the company had dealt with under the Code was 'negligible'.<sup>1046</sup> Another MSC representative recounted that 'we've only had one code complaint in two and a half years' and, interestingly, it appears that the complaint was not dealt with pursuant to the FGCC dispute resolution processes but rather it was 'easily managed through the small business Ombudsman [referring to the SBFE Ombudsman]'.<sup>1047</sup>

There are several possible interpretations of this so far minimal use of the FGCC dispute resolution mechanisms. One is that few disputes have arisen and this in turn may reflect favourably on the role being played by the FGCC provisions at the stage of negotiating GSAs, in influencing the way in which both buyers and suppliers approach these negotiations. As far as its influence on buyer approaches is concerned, this interpretation is supported by accounts from some MSC representatives:

*...one of the effective parts of the Code has been to get to us a place where disputes are solved before they arise, not afterwards, where we have buying teams and others coming to me, especially, and to their team leaders, and saying, "I'm thinking of doing this, but I'm having this conversation with a supplier today, what do you think?" And that's one of the heightened awareness things that have come from all the training we've done on the code and it's a great help ... Think of it as a law though, the purpose of the law is not to fill up the gaols, the purpose of the law is to keep people out of gaol, isn't it? That's what this is doing, I think.*<sup>1048</sup>

<sup>1044</sup> Transcript of interview, director, leading UK economics consultancy, p. 17.

<sup>1045</sup> Transcript of interview, Christine Tacon, p. 10.

<sup>1046</sup> Transcript of interview, MSC representative, p. 13.

<sup>1047</sup> Transcript of interview, MSC representative, p. 10.

<sup>1048</sup> Transcript of interview, MSC representative, p. 17.

Another possibility is that, as previously mentioned, many suppliers remain unaware of the availability of these processes. Yet another is that they are aware but are choosing not to employ the dispute resolution framework and resources established under the Code for the purposes of resolving grievances with their buyers.

Of the possible interpretations, past history could be taken to suggest that the third is a highly likely scenario. But a conscious choice not to use the Code dispute resolution provisions may be explicable on various grounds also. One possible ground (albeit admittedly one likely to attract a contest of views) is that, for large suppliers at least, such provisions and processes are simply not necessary as a way to resolve issues that arise at either the negotiating table or in the enforcement of contracts. They have sufficient bargaining power to look after themselves. This view is certainly held by some in the UK:

*... who is protected by the code in the UK? ... these are companies like Coca-Cola and these are not small companies. These are global multinationals who don't appear need the protection of the state in their negotiations with the supermarkets...*<sup>1049</sup>

...

*...clearly, the very large suppliers, it's [referring to GSCOP and the GCA] not as relevant to them. The balance of power is on their side.*<sup>1050</sup>

A further possible explanation for the low take up of the FGCC dispute resolution provisions, more likely to apply to smaller suppliers, is that the Code's particulars and paperwork requirements are just too onerous and represent a substantial disincentive to making a complaint or notifying a dispute pursuant to the FGCC. The formalism of the Code processes in this regard was certainly pointed to by some of our interviewees as a difficulty for small suppliers particularly.

Notably, under the UK Code, there are no provisions equivalent to those in the FGCC requiring the provisions of particulars by suppliers as a condition of notifying a dispute. Rather, without prescription as to form, the GSCOP simply provides that:

*A Dispute will arise under the Code when a Supplier informs the Code Compliance Officer that the Supplier believes that the Designated Retailer has not fulfilled its obligations under the Code, and that the Supplier wishes to initiate the dispute resolution procedure set out in this Article 11.*

*Whenever a Supplier contacts the Code Compliance Officer regarding an alleged breach of the Code by the Designated Retailer, the Code Compliance Officer will inform the Supplier of its right to initiate a Dispute under Article 11(2) above, and confirm whether the Supplier*

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<sup>1049</sup> Transcript of interview, director, leading UK economics consultancy, p. 20.

<sup>1050</sup> Transcript of interview, compliance manager at a major UK retailer, p. 10.

*wishes to initiate a Dispute. In the absence of the Code Compliance Officer requesting confirmation, a Dispute will be deemed to arise.*<sup>1051</sup>

Another possible reason why the FGCC dispute resolution process is apparently not being used to any significant extent may relate to the fact that, at various stages in the process, the relevant dispute resolution representative, be it the CCM or a more senior individual (on internal review) may decide not to engage with the matter being 'satisfied that the complaint is vexatious, trivial, misconceived or lacking in substance'.<sup>1052</sup> As highlighted in Part 5 of this report, in the context of the Senate inquiry, several submissions registered concerns that such provisions placed or would be seen by suppliers to vest all power in the hands of the retailer with respect to dispute resolution.

There are no equivalent provisions in the GSCOP. In the UK the only consequence of the GCA reaching the view that a supplier complaint was 'vexatious or wholly without merit' is that, instead of the arbitration costs being borne by the retailer, 'costs will be assigned at the arbitrator's discretion'.<sup>1053</sup> A view about vexatiousness or lack of substance is not a reason that can be invoked by the CCO not to investigate. As one compliance manager for a UK supermarket chain told us:

*...you have to report concerns, whether or not they are found to be justified or not. So, if a supplier has a general concern, it's still reported, or if it's actually, you say no, it's out of scope or it's not reasonable, then we still have to report it.*<sup>1054</sup>

At the time that the FGCC's dispute resolution design was subject to consultation, concerns were also expressed about the use of external mediators/arbitrators who may lack industry knowledge. Such concerns may also be inhibiting the use of the FGCC's processes for resolving disputes, and again, they are concerns that have been headed off in the UK. In that jurisdiction the GCA plays a similar role to the role that was played by the PGCC Ombudsman in Australia. Under the GSCOP, if disputes cannot be resolved at the level of the retailer's CCO, then there is no requirement for escalation to a more senior rank in the retail organisation. The supplier may submit an arbitration request and arbitrations are conducted by the GCA.<sup>1055</sup> The GCA in turn is clearly a person with in-depth knowledge of and front line experience in the industry. As she told us herself:

*I have been [in] FMCG, I've been in farming and I've worked as a retailer and as a production engineer, I am passionate about supply chains. And I just want this to get better. I have no vindictiveness against any of the retailers. I actually think we have a fantastic food supply network in the UK, but it's not perfect, and I'd like to get involved to make things better.*<sup>1056</sup>

<sup>1051</sup> GSCOP, art 11(2)-(3). The GCA's [Guidance on raising issues, and disputes and the escalation process](#) (1 April 2014) also suggests that a supplier need to do little more than contact the CCM with a concern that the Code has been breached in order to initiate a dispute resolution process.

<sup>1052</sup> FGCC, cl 35(2), cl 38(5).

<sup>1053</sup> GSCOP, art 11(7).

<sup>1054</sup> Transcript of interview, compliance manager at a major UK retailer, p. 22.

<sup>1055</sup> GSCOP, art 11(4)-(5).

<sup>1056</sup> Transcript of interview, Christine Tacon, p. 12.

To listen to Tacon talk, her understanding of and passion for the industry is hard to miss and as she acknowledged: 'I think it has to be a passion if you want to do it and a passion to make a difference... I really want to make the supply chain perfect.'<sup>1057</sup> In the 2017 review of the GCA, respondents also took the opportunity to comment favourably, not only on her deep knowledge of the sector, but also her personal style in carrying out her role, one marked by 'professionalism, care and consideration', engendering the trust and confidence of both retailers and suppliers who deal with her.<sup>1058</sup>

In addition to the possible concern about the prospect of a mediation/ arbitration being conducted by an 'outsider', there is not inconceivably a concern by suppliers relating to the cost (aside from the time involved) of any such process. In the UK all costs of GCA arbitrations are borne by the retailer in question,<sup>1059</sup> so cost concerns are clearly not an inhibiting factor, whereas here, the question of costs falls to be determined by the rules of the Institute of Arbitrators and Mediators Australia (a provision of the FGCC not likely to be helpful or comforting to a supplier contemplating the possible use of this as a mechanism for resolving a dispute).<sup>1060</sup>

Unlike in Australia, there is also no separate recourse in the UK to the competition authority – the Competition and Markets Authority (CMA) – in relation to disputes or allegations of breach of the Code. When asked as to why not more use is being made of the arbitration procedures under the GCA (there have been only four to date), the supplier advocate, Noble, pointed out that in effect 'it's a last resort... [if] you've been delisted, your relationship is dead, you've got nothing to lose...'.<sup>1061</sup> Similar observations were made by a legal advisor to suppliers in the UK:

*I don't think anybody on the supply side seriously believes that actual adjudications on bilateral disputes is ever going to be a significant feature of life. It's just not. It doesn't make commercial sense for it to be. So as I understand it, there are two arbitrations on Christine's book at the moment. Both related to delisting. So you could see a situation where somebody's got nothing to lose, you might as well have that - use that toolkit. But it's not something that anybody sensible is going to want to do, where they have an ongoing commercial trading relationship. You're going to either resolve it beforehand through some other channel or you're not going to escalate at that point. Because you know that commercially, it could be hit back. So what matters are two things; one is the informal discussion that's ongoing and the other thing that matters in terms of ultimate sanction is the power to do investigation on endemic issues.*<sup>1062</sup>

Not unrelated to concerns about the administrative burden imposed on suppliers in raising a dispute under the FGCC, there may be a perception amongst Australian suppliers that there are other, less formal less burdensome and possibly more effective more expeditious routes to the same end.

<sup>1057</sup> Transcript of interview, Christine Tacon, p. 12.

<sup>1058</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [79]-80].

<sup>1059</sup> GSCOP, art 11(7).

<sup>1060</sup> FGCC, cl 39(4).

<sup>1061</sup> Transcript of interview, John Noble, British Brands Group, p. 39.

<sup>1062</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 19.

Processes available under MSC internal supplier charters or policies may be seen as more user-friendly, for example. This would appear to be the case for at least one MSC, where – at the time of our interview at least – more complaints were reportedly being dealt with under the company’s own pre-existing code than the FGCC.<sup>1063</sup> This may reflect also the MSC’s own preference for use of its internal Charter as the primary mechanism for dealing with supplier grievances given, as one commentator close to the MSC told us, ‘it is a quicker and easier resolution mechanism for them.’<sup>1064</sup> A different MSC representative told us that:

*We have four different mechanisms for our suppliers to resolve issues. And we ask them to put the Code last in that list of things, because if they have to resort to that, it means everything else has failed.*<sup>1065</sup>

The four mechanisms were described in conversation as:

- ‘come talk to the person you deal with’ [i.e. the supplier’s direct contact on the buying team];
- ‘come and talk to a more senior manager’;
- ‘we have an internal person nominated ... on our website as the person to go to with a supplier complaint, and .. an organised form of response that says, within 24 hours you can go to the general manager, within 72 hours you can go to the CEO, and so on and so on, to escalate a complaint and get it fixed’; and
- ‘we then have an externally managed hotline that can be anonymous if the supplier wants it to be anonymous’.<sup>1066</sup>

The same representative reported that ‘none of these [mechanisms] are used to any great degree beyond the initial approach [i.e. to the supplier’s direct contact on the buying team]’.<sup>1067</sup>

Last but by no means least, as recited earlier in this report, on other accounts, suppliers – small ones in particular – continue to harbour considerable reticence to push the bar with their MSC customers for fear of commercially adverse repercussions. They also remain reluctant to approach the ACCC or air their dirty laundry in some other public fashion. Even if the grounds for such ambivalence should be seen as lesser than pre-FGCC if not for any other reason than the MSCs themselves can be expected to be much more wary about meting out or being seen to mete out ‘punishments’, the ‘scars and bruises’<sup>1068</sup> (to which one of our interviewees colourfully referred) are likely to take some time to heal.

Judging by the UK experience, it is arguable that a code of conduct, even a mandatory code of conduct, may not fully mitigate such deeply engrained concerns and attitudes:

<sup>1063</sup> Transcript of interview, MSC representative, p. 13.

<sup>1064</sup> Transcript of interview, former senior representative of the UK OFT, p. 21.

<sup>1065</sup> Transcript of interview, MSC representative, p. 10.

<sup>1066</sup> Transcript of interview, MSC representative, p. 11.

<sup>1067</sup> Transcript of interview, MSC representative, p. 11.

<sup>1068</sup> Transcript of interview, director of a consultancy that advises suppliers, p. 10.

*It's definitely a fear of retribution that comes out. And I know a lot of suppliers think that this is life, this is business, we've got to sort out our own problems. We don't want to go running to teacher.*<sup>1069</sup> (Christine Tacon, GCA)

*...if you can't deal with the supermarkets then if you're a supplier with any kind of scale then you're nowhere in the UK.*<sup>1070</sup> (Policy officer for a UK fair trade organisation)

*...You don't wench on your customer. It's a collaborative, cooperative relationship and as a supplier you are always trying to strengthen that. But yes, there's a realisation and a keen awareness amongst suppliers that actually if you do upset your retail customer there are many, many ways in which they can punish you and over a long time.*<sup>1071</sup> (John Noble, Director, British Brands Group)

There does appear to be some positive movement on this front. As a lawyer with considerable experience in this space noted, in the past 'there was genuinely fear on the part of suppliers to have any kind of contact with the process.' When asked what had changed, she responded, 'it's a normalisation of this issue. So it's no longer nuclear to say, you're beating us up.'<sup>1072</sup> However, in the 2017 review of the GCA, one of the issues seen as representing an ongoing challenge was a continuing 'climate of fear' and ameliorating supplier anxieties about reporting was earmarked as a priority for the GCA to work on in the lead up to the next review, in 2019.<sup>1073</sup>

In acknowledgement of such concerns the GSCOP makes provision for anonymity (albeit not in the context of arbitrations), and the GCA in turn takes steps to minimise the possibility of any single complainant being identified when she is making inquiries or seeking evidence. This is important given the experience under the former SCOP in the UK in respect of which it was reported that suppliers failed to make complaints to the OFT given that that Code prevented such complaints from being made anonymously.<sup>1074</sup> In responding to this experience, in its account of why the GCA should be established, the CC addressed the vexed issue of anonymity in the following way:

*A number of suppliers emphasised the need for the Ombudsman to maintain the anonymity of individuals who made complaints regarding retailer behaviour. It was submitted that suppliers would be unlikely to come forward with information on GSCOP practices unless they could be assured of anonymity. In contrast, a number of retailers were concerned with the anonymity provisions, stating that anonymity will limit the ability of retailers to respond to the proposed investigation and defend its supply chain procedures. Our view is that complainant anonymity should be considered against the role of the Ombudsman in investigating complaints. As set out in the Groceries Report, there is an important distinction between the investigative*

<sup>1069</sup> Transcript of interview, Christine Tacon, p. 24.

<sup>1070</sup> Transcript of interview, policy officer for a UK fair trade organisation, p. 20.

<sup>1071</sup> Transcript of interview, John Noble, British Brands Group, p. 26.

<sup>1072</sup> Transcript of interview, experienced legal advisor to suppliers in the UK, p. 32.

<sup>1073</sup> Department for Business, Energy & Industrial Strategy (UK), *Statutory Review of the Groceries Code Adjudicator 2013-2016*, July 2017, [11]-[16], [60]-[61].

<sup>1074</sup> HC Deb 7 December 2005 c 968, referred to in Seely, p. 12.

*function of the Ombudsman and the dispute resolution function in the GSCOP. A dispute involves a single complaint by a supplier against a retailer, whereas an investigation would follow a period of information-gathering, through which the Ombudsman may identify, for example, a pattern of behaviour or area of concern from a particular retailer or set of retailers. We have reflected this in the undertakings. Given that an investigation will likely cover a broad area of concern, rather than focussing on individual complaints, we do not think that the anonymity of complainants should be a problem for retailers in responding to investigations. We therefore recommend that the anonymity of persons who provide information to the Ombudsman be maintained.<sup>1075</sup>*

To some, anonymity is imperative if investigations are to be successful; ‘...the reason that the GCA is so important in our eyes is that it allows anonymous complaints.’<sup>1076</sup> To others this approach places unnecessary constraints on the Adjudicator, and limits the overall impact of the role:

*... having that strict requirement on confidentiality, not only makes it harder for the adjudicator to do his or her job, but also means that the sector doesn’t really benefit from that learned experience over time.<sup>1077</sup>*

Anonymity of complainants also appears to pose challenges for the compliance personnel in the retailers. To illustrate the difficulties, one compliance manager recounted an episode where there was a complaint about payment terms owing to currency negotiations:

*...we are aware of one supplier that had a concern, they raised it with the GCA, but the GCA couldn’t tell us who the supplier was, so they gave us the broad parameters of what the complaint was around; and we sat there and thought ... “okay, we don’t quite know what this is, we don’t have enough information here to really go and say this is the problem, let’s deal with it”; because it was all anonymous. And it was so hard because we couldn’t even pin it down to which area it was at. And it was so generic. So, then we said to the team “okay, let’s have a look at this topic and see if we can improve”.*

*... another example was one of the comments we received was that currency exchange rates were affecting negotiations – okay, that affects a lot of suppliers. So we did a general reminder on how to approach negotiations where currency exchange rates come into play.*

*So, you’ve got to balance enough information to say, okay, what’s the problem, and be able to do something about it, against protecting the supplier.<sup>1078</sup>*

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<sup>1075</sup> CC, *Undertakings to establish a Groceries Supply Code of Practice Ombudsman Scheme - Response to consultation*, August 2009 [15-16].

<sup>1076</sup> Transcript of interview, policy officer for a UK fair trade organisation, p. 19.

<sup>1077</sup> Transcript of interview, director, leading UK economics consultancy, p. 28.

<sup>1078</sup> Transcript of interview, compliance manager at a major UK retailer, p. 23.

This observation is consistent with the ACCC's position, voiced in the Senate inquiry, to the effect that it is extremely difficult to investigate without knowing who the parties involved in the dispute are.<sup>1079</sup>

The surveys conducted by the GCA, referred to above, provide further insights into supplier readiness to raise issues – at least with the Adjudicator. The results in 2015 and 2016 indicated that in both years 47% of direct suppliers would be prepared to raise issues with the GCA, as would 62% of indirect suppliers (up from 41% in 2015) and 77% of trade associations (up from 64% in 2015), suggesting amongst other things the degree of comfort and security that suppliers have in relation the UK process.<sup>1080</sup> Of those who indicated that they would not raise an issue, the top three reasons were fear of damage to their relationship with the retailer as the reason (56%), fear of retribution (for example by way of delisting) (47%) and fear that their reputation in the wider retail sector would be affected (30%). Only 9% cited the reason as not knowing if the issue is covered by the Code or as seeing the issue as a normal part of doing business.

Notably, Tacon's message to retailers is that having more rather than less issues raised by suppliers is in fact a positive development. She explains that if issues are not being raised to the retailers:

*... it means you've got no idea where your buyers are pushing the boundaries.. If you had 28 people go to the code compliance officer in the last year you're going to have a very good idea... It's a bit like health and safety, where you record your near misses and you hopefully get lots of near misses and that helps [to ensure] you never have a fatality...*<sup>1081</sup>

A similar view was expressed by a senior adviser to one of the MSCs in Australia:

*My view is that MSCs should encourage people to come forward to them first, and only go to the ACCC if that does not resolve the issue. A lot of instances are likely to be errors that the MSC will be keen to correct.*<sup>1082</sup>

But it is also clear that the surveys provide a highly useful tool for the GCA in gathering information on an anonymous basis, in a way that provides suppliers with security in speaking out:

*...the YouGov survey is a bit of a master stroke because, in an environment where suppliers aren't going to speak out publicly, it gives her a measure of how she's doing, it gives her an indication of the things exercising suppliers and it puts in the public domain a list of retailers and their relative performances. And so, I think, the YouGov survey is a valuable initiative.*<sup>1083</sup>

<sup>1079</sup> Scott Gregson, Executive General Manager, Consumer Enforcement, Australian Competition and Consumer Commission, *Proof Committee Hansard*, 21 April 2015, p. 22, cited in SELC, *FGC Regulation*, 2015, p. 14.

<sup>1080</sup> GCA, *GCA Annual Survey Results 2016*, YouGov, p. 9.

<sup>1081</sup> Transcript of interview, Christine Tacon, p. 31.

<sup>1082</sup> Transcript of interview, former senior representative of the UK OFT, p. 22.

<sup>1083</sup> Transcript of interview, John Noble, British Brands Group, p. 42.

#### IV. Good faith

Assessing the extent to which this final element of the FGCC's purpose has been realised to date is the possibly the most challenging. In large part, this is because, as mentioned above, there are highly divergent conceptions of good faith across the sector. As our interviewee responses to questioning on their understanding of the concept bore out, some see good faith as largely entailing considerations of procedural justice – in particular, being willing to listen, clear about expectations and open to negotiation. Others see it as more substantive in character, as requiring that the party exercising good faith take account of the interests of the other party in any negotiation or decision affecting those interests.

The relevant clause in the Code itself provides yet further indicia as meaning, including reference to the meaning of good faith 'under the unwritten law as in force from time to time' and then to three further considerations, namely the exertion of duress, recognition of the need for certainty in the risks and costs of trading particularly in relation to production, delivery and payment, and whether the supplier has acted in good faith. In the GSCOP, the explanation that is provided in relation to the 'Principle of Fair Dealing' (referred to above) refers to 'good faith' which it not itself defined but it is clear that it would entail dealing 'without duress and in recognition of the Suppliers' need for certainty as regards the risks and costs of trading, particularly in relation to production, delivery and payment issues.'<sup>1084</sup>

Reference to the 'unwritten' (common) law in the FGCC is a particularly good example of why several of our interviewees bemoaned the legalistic nature of the Code and the consequence that it is likely, on its own (without sufficiently skilled assistance in interpretation and application), to be largely impenetrable for most suppliers. Even Treasury did not attempt a fulsome explanation of the common law definition in its consultation paper, acknowledging that there 'is no definitive meaning ... there has been considerable jurisprudence and legal commentary surrounding [the concept]'.<sup>1085</sup> But Treasury did offer some pointers, referring to 'honesty, cooperation, reasonableness and fairness' as 'guiding principles ... to assist in determining the obligation on a case-by-case basis'.<sup>1086</sup> Most if not all of the good faith attributes referred to by Treasury are likely themselves be matters in the application of which different results are reached by different interpreters. That said, amongst suppliers at least, there is likely to be a strong intuitive sense as to when certain conduct crosses the line in one of these respects and is sufficiently unreasonable or unfair, say, as to constitute bad faith.

Assessing the extent to which the FGCC has 'worked' in engendering good faith in retailer-supplier relations raises similar considerations to assessing the extent to which it has helped to build and sustain trust and cooperation in such relations – particularly given such qualities are likely to be a function or product of the exercise of good faith. The challenges associated with changing a long-standing culture that has spawned the types of behaviour of concern in the sector again will be

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<sup>1084</sup> GSCOP, cl 2.

<sup>1085</sup> Treasury, FGCC consultation paper, 2014, p. 18.

<sup>1086</sup> Treasury, FGCC consultation paper, 2014, p. 18.

material. These challenges will be aggravated insofar as retailer senior management sends messages, comes up with profit-driven initiatives and sets performance targets with associated remuneration and other career-related consequences for front line buying personnel that weaken incentives to act in good faith. It might be presumed or hoped that MSC management are alive to this and act accordingly. That said, as has been pointed out already, competition amongst retailers is intensifying and costs are rising, generating pressures that just as in the post 2008 period may work against even the strongest commitment to instilling a 'good faith' culture in the MSCs.

## **Appendix A: List of individuals interviewed for the Supermarket Power Project**

### **Retailers**

1. Chief Legal Officer, MSC
2. Head of Trade Relations, MSC
3. Legal Services And Compliance Advisor, MSC
4. Group Counsel, Competition and Compliance, MSC
5. Senior Competition and Consumer Lawyer, MSC
6. Head of Risk and Regulatory Compliance, MSC
7. Director, Customer Transformation, MSC
8. General Manager, Property Manager and Leasing, MSC
9. Director of Property, MSC
10. Assistant to Director of Property, MSC
11. Senior Legal and Regulatory Advisor, MSC
12. General Manager, Legal, MSC
13. Head of Buying, MSC
14. Buyer Category Manager, MSC
15. Former General Manager Corporate Affairs, MSC
16. Former Chair, MSC
17. Managing Director, MSC
18. General Merchandise Manager, MSC
19. Assistant General Merchandise Manager, MSC
20. Consultant to MSC
21. Strategic advisor to MSC
22. Chief Executive Officer, independent supermarket
23. Former Legal Counsel, independent supermarket
24. Managing Director, independent supermarket
25. Chief Executive Officer, grocery industry organisation

### **Government**

26. Former Small Business Minister

27. Deputy Chair, ACCC
28. Commissioner, ACCC
29. Commissioner, ACCC
30. Commissioner, ACCC
31. Former Chair, ACCC
32. Former Commissioner, ACCC
33. Former Commissioner, ACCC
34. Director, Merger & Authorisation Review, ACCC
35. Assistant Director, Mergers and Acquisitions Group, ACCC
36. Former lawyer, ACCC
37. Manager, Competition Policy Unit, Commonwealth Treasury
38. General Manager, Commonwealth Treasury
39. Manager, Markets and Regulation Unit, Infrastructure, Competition and Consumer Division, Treasury
40. Team Leader, Strategy, Environment and Planning Directorate, ACT
41. Former Produce and Grocery Ombudsman

#### **Primary Producers**

42. Chief Executive Officer, national farmers organisation
43. Chief Executive Officer, state farmers organisation
44. Interim CEO, primary producers organisation
45. Senior Policy Manager, primary producers organisation
46. Major fresh produce supplier to a MSC
47. Mango grower
48. Cattle farmer

#### **Suppliers**

49. Chief Executive Officer, grocery supplier organisation
50. Chief Executive Officer, small business advocacy organisation
51. Director, Legal and Regulatory, grocery supplier organisation
52. Chief Executive Officer /Managing Director, manufacturing supplier
53. Former Managing Director, consumer goods manufacturer

- 54. General Manager, consumer goods supplier
- 55. Sales Director, consumer goods supplier
- 56. Director, consultancy advising suppliers

**Consumer groups and advisors**

- 57. Consultant, social science and consumer behaviour
- 58. Representative, residents action group
- 59. Investigative Journalist and Content Producer (Food), leading consumer advocacy group

**UK-based interviewees**

- 60. Grocery Code Adjudicator
- 61. Lawyer at leading law firm that advises suppliers
- 62. Former Head of Office of Fair Trading; Principal, leading economics consultancy
- 63. Director, leading economics consultancy
- 64. Director General, leading UK farmers association
- 65. Director, leading UK supplier association
- 66. Director General, fair trade supplier organisation
- 67. Policy Officer, fair trade supplier organisation

**Other**

- 68. Principal, economic and planning advisory service
- 69. Senior Consultant, economic and planning advisory service
- 70. Senior Business Columnist
- 71. Retail Reporter
- 72. Union Representative

## Appendix B: Template interview questionnaire

**Note:** These questions indicate general topics that may be covered in the interview. If necessary the interviewers may use prompts for discussion in relation to these topics. The questions and prompts will be tailored to the extent necessary to reflect the particular background and involvement of the interviewee in the matters under discussion. There may be topics not identified in this guide that the interviewee may wish to raise. Equally there may be topics identified in this guide that are not canvassed in the interview for various reasons. Several of the questions in this guide refer to clauses of the Food and Grocery Code of Conduct and the Treasury Discussion Paper used for the consultation relating to the code. Copies of the code and Discussion Paper are provided with this guide for ease of reference.

### Context

- In 2008 the ACCC concluded in its grocery inquiry that there was nothing ‘fundamentally wrong’ with the supply chain. Yet just five years later in 2013 major industry stakeholders negotiated a proposed code of conduct to manage and improve retailer-supplier relationships, and in 2015, the prescribed Food and Grocery Code (FGC) was introduced.

What does this apparent shift say about:

- the evidence and/or analysis and findings of the ACCC in 2008?
- developments in the industry, ACCC activity and public discourse surrounding supermarkets since the 2008 inquiry?
- What led to the adoption of the FGC / what were the impetuses for it in terms of what was happening in the grocery industry and in the public discourse surrounding supermarkets?
- Insofar as you are aware of it, describe the process of negotiations in which the major supermarket chains (MSCs), the Australian Food and Grocery Council (AFGC) and any other stakeholders came to draft a proposed industry code and the process of consultation with Treasury in relation to the statutory version.
  - Who led and who was involved in the negotiations?
  - Who was not involved and why? Who actively opposed the process and why?
  - What effect, if any, did the fact that the FGC emerged out of an initiative led by the MSCs and the AFGC have on the framing of its objectives, scope and ultimately its likely effectiveness?
  - What prompted the industry code instigators to approach government with a proposal to have the code prescribed? Or was the approach made by government?
  - What issues, concerns loomed large in the negotiations – were seen as particularly important or difficult, and why?
    - From the industry perspective? Individual stakeholders? Collectively?
    - From the government perspective?
  - To what extent did the final text of the FGC address issues/concerns raised by submitters in the consultation process?
- To what extent should the way in which industry stakeholders worked together on this code ‘project’ be seen as novel? What precedents are there for this type of collaboration in the industry? To the extent that it should be seen as novel or unprecedented, what was it about the circumstances or climate of the time that prompted or was seen as requiring / justifying the collaboration on these particular issues / in this instance?

- How influential were overseas developments, in the UK particularly (code and adjudicator) in the instigation and negotiations over the text of the FGC?

### Objectives

- What were the concerns, issues or problems that the FGC was seen as necessary to address?
- Are there benefits for suppliers in dealing with the MSCs? Were any such benefits adequately reflected in the debate re the code? If not, why not?
- What are the purposes of the code? Views on purposes set out in cl 2?

### Regulatory approach/choice of instrument

- Why was a code (as opposed to other types of regulatory measures) seen as the optimal way to address the issues?
- Whose interests are a code seen as most serving and why?
- Whose interests are a code seen as NOT serving and why?
- How was/is a code seen to interact with relevant laws?
  - Does it cover the ground that would otherwise be covered by:
    - the unconscionability and/or unfair contract prohibitions?
    - the misuse of market power prohibition and/or other prohibitions on anti-competitive conduct?
    - general contract laws?
    - general intellectual property laws?
  - Are its provisions inconsistent with or in conflict with any of these prohibitions?
- Is it justifiable to regulate the grocery sector (by overriding freedom of contract principles) in a way that exceeds regulation of any other sector of the Australian economy? What differentiates this sector from other highly concentrated sectors?
- Are regulatory measures other than or in addition to the FGC required to effectively regulate the grocery sector (deal with the concerns/problems referred to above)?

### Application

- What are the relative merits/demerits of:
  - a voluntary (opt-in) statutory code? (see opt in and opt out provisions in cl 4)?
  - a mandatory statutory code?
  - an industry (non-statutory) code?
  - individual corporate / in-house codes

### Coverage

- What are the merits/demerits of the FGC covering (see definition of 'retailer' in cl 3):
  - MSCs only? Coles and Woolworths? Aldi?
  - All supermarkets – big and small (i.e. independents?)
  - All grocery retailers?
  - Wholesalers? (see definition of 'retailer' in cl 3, which covers wholesalers)
    - Just Metcash or all?

- Should the FGC also bind suppliers?\* If so, should it bind:
  - All?
  - Big vs small?
  - Domestic and international?
- Should the FGC also cover indirect suppliers (ie supplying to an intermediary – a wholesaler, processor, etc. – excluded by definition of ‘supplier’ in cl 3) – which largely means primary producers?
- Should the FGC cover groceries only? Alcohol? Other goods or services sold by supermarkets e.g. petrol, hardware, insurance? See definition of ‘groceries’ and ‘supermarket business’ in cl 3.

### **Grocery supply agreements (GSAs) (Part 2)**

- What were seen the benefits of requiring GSAs in writing? What are the problems, if any, with this? And from whose perspective?
- How are GSAs being created / negotiated in practice?
  - Are the intended benefits being realised?
  - Are problems (unforeseen or foreseeable) being manifested?
  - What form do GSAs take? Standard form vs tailored?
  - What happens if a supplier refuses to or simply fails to sign?
- Views on the FCG requirements relating to what has to be covered by a GSA? Any requirements it should not cover? Any gaps? See cl 8.
- Views on the provisions relating to GSA variations (see cls 9 and 10)?

### **Retailer conduct (Part 3)**

- Views generally on:
  - Scope of conduct covered? Any major gaps?
  - Qualifications on / exemptions / carve outs from prohibitions? Is the right balance struck between need for commercial flexibility and supplier protection?
  - Vagueness of language used for qualifications / exemptions? Impact on certainty?
    - What does ‘reasonable’ mean in this context? How will/should ‘reasonableness’ be determined?
  - Do the qualifications / exemptions / carve outs simply mean that the imbalance in bargaining power will shift more to the negotiations phase associated with the GSA?
- Any specific views on:
  - Payments to suppliers (c1 12)
  - Payments for shrinkage (cl 13)
  - Payments for wastage (cl 14)
  - Payments as condition for stocking or listing (cl 15)
  - Payments for better positioning or an increase in allocation of shelf space (cl 16)
  - Payments for retailer’s activities (cl 17)
  - Payments for promotions (cl 18)

- De-listing (cl 19)
  - Funded promotions (cl 20)
  - Fresh produce standards and quality specifications (cl 21)
  - Changes to supply chain procedures (cl 22)
  - Business disruption (cl 23)
  - Intellectual property rights (cl 24)
  - Confidential information (cl 25)
  - Allocation of shelf space (cl 26)
- Views on an alternative approach as proposed in Treasury Discussion Paper – no disadvantage test?
    - A no disadvantage test would allow the retailer to rely on an exemption provided for in the GSA and engage in certain conduct so long as it does not result in the supplier being materially disadvantaged.
    - This may require any costs imposed on the supplier due to the retailer's exercise of an exemption to be factored in during initial negotiations on the supply agreement or possibly compensation being offered at the time the exempted conduct is engaged in.
    - This approach attempts to maintain commercial flexibility to the extent it is mutually beneficial, while offering safeguards against conduct that may be considered inconsistent with the minimum industry standards.
  - Other alternative approaches?

#### **Good faith (Part 4)**

- What is the rationale for including a general obligation of good faith in the FGC? See cl 28.
- How does the obligation add to the other provisions of the code?
  - Should good faith have been an interpretative provision instead of a standalone duty under the FGC?
- How does the obligation add to the general law on contracts that implies an obligation of good faith in contractual dealings?
- What does 'good faith' mean in practical terms?
- Is the obligation any more than an obligation not to act unconscionably? Does it go beyond the CCA prohibition on unconscionable conduct in B2B transactions?
- Is there a tension between this obligation and the usual cut and thrust of business?
  - Specifically is there a tension between an obligation of fairness and an obligation to compete?
- Are there benefits for competition, the functioning of markets generally, and consumers from the requirement or practice of good faith between retailers and suppliers?
- Should the obligation apply also to suppliers – a mutual obligation?
- Is good faith in business dealings a function of corporate culture? Is it possible to train employees to act in good faith? If so, how?

- Insofar as you can comment, what impact if any has the introduction of a good faith obligation in the Franchising Code of Conduct had on the effectiveness of that code and relations between franchisors and franchisees? Was the introduction of this change to the Franchising code instrumental in its inclusion in the FGC?
- Views on freedom of association clause (cl 29)? What were the reasons for including this?
- Requirement to make contact details for buyers, senior buyers and code compliance managers available to suppliers (cl 30). What were the reasons for including this? Is it something that needs to be regulated?

### **Dispute resolution (Part 5)**

- Requirement that suppliers provide information and documents relating to the complaint or dispute (cl 31). Why was this seen as important to include?
- Code compliance manager obligation (cl 32)
  - Profile of appointees?
  - Level in hierarchy?
  - Why important that CCMs be independent of buying team?
  - What training is there for CCMs? Who is providing the training?
- Complaints – internal process
  - How many and what kinds of complaints to CCMs? Any change since introduction of code? To whom were complaints previously made?
  - What does an investigation by the CCM involve?
  - What kind of complaint would qualify as ‘vexatious, trivial, misconceived or lacking in substance’?
  - To whom are complaints ‘elevated’ if supplier not satisfied? How many complaints have been elevated?
  - How does senior management then resolve the complaint?
- Mediation and arbitration – external process
  - Available as immediate alternative to internal process or as next step after internal process completed. To what extent has this process been invoked? To what extent is it likely to be invoked?
  - What are the benefits of this avenue and for who?
  - What are its limitations and for who?
  - Appropriateness of IAMA as mediation body?
  - Cf dedicated ombudsman as under PGIC?
- Why are there no equivalent processes for retailer / wholesaler complaints provided for? Should there be?

## Enforcement

- Complaints to ACCC and enforcement action under the *Competition and Consumer Act* (CCA) are also available independently of code dispute resolution processes. Why is this seen as important?
- Readiness of suppliers to make complaints and provide sufficient information? Any change in this since 2008 inquiry?
- Adequacy of ACCC appetite for and resources to monitor / audit the industry and investigate?
- Adequacy of ACCC powers to investigate?
- Adequacy of CCA remedies? Compensation, declarations, injunctions, corrective advertising, setting aside or variation of contracts, refunds.
- Should there be civil penalties for code breaches? What should the penalties be? What purpose/s would penalties serve?
- Should there be infringement notices for code breaches?
- Should there be a dedicated ACCC commissioner or separate ombudsman (as in the UK) charged with code enforcement? What would be the benefits / drawbacks of this approach?
- Should the ACCC 'name and shame' in relation to investigations and/or outcomes of investigation? Why would such practices be useful / harmful?

## Compliance and reporting (Part 6)

- Duty to train buying team (cl 40)
  - Profile of buying team members?
  - Level in corporate hierarchy? Direct reports?
  - Turnover in buying staff?
  - What does training involve?
  - How do payment, incentive and performance assessment schemes affect the type of behaviour relevant to the code?
  - What role does corporate culture play? What does this mean?
- Reporting obligations (cl 41)
  - Public access to CCM reports?
  - Who does the CCM report go to?
  - Has any senior management action ensued in response to CCM reports?

## Other grocery-related codes

- How does the FGC differ in its intent, scope and provisions from:
  - the Produce and Grocery Industry Code?
  - the Horticulture Code?
- Does the FGC conflict with the Horticulture Code in any way?
- How should these other codes be judged in terms of their effectiveness and impact?
- Is there an industry code, private or prescribed, in the grocery or other sector that should be regarded as a success? Explain.
- Does the dual operation of the FGC and Horticulture code create imbalances and/or inequities in the overall regulatory system? Explain.

- The grocery sector has now had experience with three different approaches to codes:
  - a voluntary industry code (PGIC),
  - a mandatory prescribed code (Horticulture) and now
  - a voluntary prescribed code (FGC).
 How are these shifts in regulatory approach best explained? Which is the optimal approach and why?

### **Effectiveness**

- Developments in the grocery sector are fluid and fast moving. Are the same impetuses, justifications for the FGC that were present at the time that it was first conceived still present? If not, what has changed and what does this mean for the relevance and likely impact / effectiveness of the code?
- To what extent are mechanisms developed at the same time or since the FGC being used instead of the FGC but to the same ends? E.g. Coles Supplier Charter; Aldi Code of Ethics? Is this duplication a problem?
- Should the FGC have an end date for operation? When should it be reviewed (current plan is for review in 3 years cf usual review time frame for codes is 5 years – why shorter in this context)?
- What factors / requirements determine a code's effectiveness? Relatedly, what are the criteria by which the FGC should be judged in terms of effectiveness?
- How would you assess the effectiveness of the FGC thus far in achieving its purposes, as set out in cl 2?
- What would be the appropriate time frame in which to assess its effectiveness by these criteria?
- Is the FGC having any unintended or unforeseen consequences – positive or negative?
- What degree of regulatory burden (cost) have the FGC obligations imposed? On retailers? On suppliers? Others?
- Cost estimates of the regulatory burden were set out in the Treasury Discussion Paper Regulatory Impact Statement. How were these figures estimated? Are they robust, realistic? Are there gaps?
- How has the FGC affected ACCC workload / impact on ACCC resources? How actively is the ACCC monitoring the industry / compliance with the code?
- How does the FGC and regulation of the grocery sector generally in Australia compare with the approach taken in the UK? In other jurisdictions?