

Cuthbertson Brothers

Submission to Select Committee on Agricultural and Related Industries - Inquiry into food production in Australia

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Section 1 Briefing Note

CUTHBERTSON BROTHERS

Summary:

Cuthbertson Brothers believe this matter breaches the Trade Practices Act in that Swift have used their market power to push players out of the sheep and lambskin market. They have also acted in a misleading and deceptive way to achieve these outcomes.

We ask the senate inquiry to call on the ACCC to launch a formal investigation into this matter.

- Legal advice indicates that Swift are breaching the Trades Practices Act
- Unfair tendering process at Longford
- Swift have locked Cuthbertsons out of the Longford Abattoir
- Has potential for significant financial impact on farmers and the broader community - with at least 20 jobs plus \$10 m. at risk to local economy as well as the Tasmanian brand
- Swift's action will force agents (Roberts, Elders etc) out by Swift going direct to Farmers
- Swift have forced Australian Lamb Company out of the market greatly reducing the price and competition of the market.
- Since lock-out Swifts have continued a pattern of activities designed to force Cuthbertson Brothers out of the market, including approaches to Cutbertson's major customer despite claiming to be 'in talks'
- Swift say they are doing all of this to increase the return to primary producers, but won't allow an open tender – how can this be?
- Swift are attempting to control the market and go from price takers, to price makers
- Swift are blatantly using their marker power as well as deceptive and misleading conduct to stop Cuthbertson Brothers from participating in the market.
- Cuthbertson Brothers have taken this to the ACCC but need support to ensure that ACCC have all the information for their investigations.

Section 3 Backgrounder

Cuthbertson:

A great Tasmanian company that has supplied skins and hides to footwear manufacturers throughout the world for over 150 years is being forced out of business by Brazilian owned, US meat processing giant, Swift.

Swifts introduction of a blatantly unfair tendering system for sheep and lamb skins led to Cuthbertson Bros have been locked out of Tasmania's largest abattoir since February this year. This has placed Cuthbertson's operations under a cloud and the livelihood of 20 long term employees. This lock out is threatening financial returns to drought-affected farmers and exports of iconic Tasmanian ugg boots to lucrative US markets.

The action of Swift is clearly in breach of the *Trade Practices Act* and the Australian Competition and Consumer Commission (ACCC) must investigate.

What does the current impasse mean?

A great Tasmanian company, with a proud history of working with the Tasmanian farming community for generations will be lost.

Primary producers are getting an estimated 50 per cent less for their sheep and lamb skins.

Swift have also refused a major exporter from using their Longford facility, costing Tasmanian producers a further \$7 to \$10 per animal.

If this is allowed to continue, it is likely farmers' agents will be the next to be pushed out by Swift.

Once all competitive forces are removed from the market, Swift will seek to deal directly with producers and move from being a price taker to a price maker. They will control the market for export quality lamb products from Tasmania.

Backgrounder:**Who is Cuthbertson Bros.?**

Cuthbertson Bros. was established by the owners of the Blundstone Boot Company - the Cuthbertson family, in 1840.

Until 2007 Cuthbertson Bros. was the supplier of hides to the Blundstone Boot Company for use in their production of high quality footwear which was exported throughout Australia and the rest of the world.

In 2007 Blundstone Boots moved much of their footwear production overseas and Cuthbertson Bros expanded their operations through the purchase of the Neil Edwards

hide and skin processing plant at Launceston. This move saw them shift their focus from hide production to the processing and exporting of lamb and sheep skins.

Until February this year, Cuthbertson Bros. purchased some 80 per cent of the Tasmanian production of sheep and lamb skins for processing and exporting throughout Australia and overseas.

What do they do?

Cuthbertson Bros. receive sheep and lamb skins from abattoirs throughout Tasmania which are taken through a process to preserve them for export. Once this process is complete, the sheep and lamb skins are then graded on their size and weight for export.

They also undertake a similar process for the cow hide market.

Their sheep and lamb skins are sold to car manufacturers, clothing manufacturers and other companies that are willing to pay a premium for high quality Tasmanian sheep and lamb skins.

What happens to Cuthbertson's Sheep and Lamb Skins?

Tasmanian sheep and lamb skins are recognised for their high quality and are particularly sought after in the production of double faced lamb skin products, such as ugg boots.

Until the impasse, Cuthbertson Bros. who purchased some 80 per cent of the sheep and lamb skins produced in Tasmania sold their produce to an exclusive manufacturer agent in Melbourne - Dynasty.

Dynasty is the manufacturer agent for Henan Prosper - the world's largest tannery located in the Henan Province in China.

Henan Prosper are the world's leading manufacturer of lamb skin based products processing up to 10 million skins per year, with the top 10 per cent of this production being used to produce ugg boots for international brands such as Timberlake, Billabong, Hugo Boss, UGG and EMU brands - the bulk of which is from Cuthbertson.

How does the sheep and lamb market work in Tasmania?

If a producer wishes to sell their livestock, there are two ways this can be done. Livestock can be auctioned at regular livestock sales held throughout Tasmania or sold directly to an abattoir.

If livestock is purchased at an auction, the purchaser owns the livestock outright.

However if the livestock is sold to an abattoir in Tasmania, it is sold either directly by the producer or by an agent such as Roberts or Elders acting on the producer's behalf, on the basis of weight and grade.

The weight and grade method of sale is a system whereby sheep and lambs are processed in the abattoir, then weighed and graded once processed. Through this method the skins remain the property of the primary producer.

Traditionally, sheep and lambs sold through the weigh and grade method were assessed for their skins prior to processing in the abattoir.

This involves potential buyers making a judgment on the value of the sheep or lamb skin on the basis of the length, size, colour and type of skin. The potential buyers then tender their prices through an open process with the highest bidder generally securing the sheep and lamb skins.

This money is then paid directly to the primary producer or the agent that represents them.

How many abattoirs are there in Tasmania?

There are two main sheep and lamb abattoirs in Tasmania, both owned by Swift.

At Longford, the Swift facility is the only supplier of export grade sheep and lamb produce in Tasmania.

Swift also own a facility at Devonport, which processes product for the Tasmanian market.

The vast majority of Tasmanian sheep and lamb is processed at Swift Longford and Swift Devonport. There are other smaller local abattoirs located throughout Tasmania at Cressy, Smithton (cattle only), Cygnet, Collinsvale and Flinders Island.

Swift also own and operate the King Island abattoirs which is currently under threat of permanent closure. This has required the Tasmanian Government's intervention.

What has happened to other exporters?

Producers such as Australian Lamb Co, which exports Tasmanian lamb throughout the nation and the rest of world on the basis of its reputation for high quality product can only process at Longford or ship the livestock to Melbourne for processing.

Australian Lamb Co is one of the nation's main lamb exporters and has been informed by Swift it can no longer process at Longford, forcing the company to send its stock to Melbourne adding between \$7 and \$10 per animal.

What has happened?

Until recently, prospective sheep and lamb skin buyers would arrive at the Longford abattoir on a daily basis. This had occurred for many years. However in early February, Cuthbertson Bros. were refused entry to tender for sheep and lamb skins.

What were the events leading up to Cuthbertson Bros. being refused entry?

In December last year, Swift entered the skin buying market by retaining a Melbourne based skin buyer and processor, Mr John Knox.

Neither Mr Knox nor his representatives, attended the abattoir to price sheep and lamb skins, instead Swift abattoir administration provides all the tendered prices from other buyers to Mr Knox each day.

Mr Knox then simply tenders between five and 10 cents per skin higher than the prices offered.

Since December, this has seen the amount of skins purchased by Cuthbertson Bros. fall to nearly nil.

After unsuccessfully attempting to resolve this issue, Cuthbertson Bros. attended Swift Longford each day, but instead of putting forward a tender to the Swift administration, decided to tender directly to the owners of the skin - the primary producer or their agent.

On February 9, 2009 Cuthbertson Bros. were refused entry to Swift Longford operations making it impossible for them to price the product.

Cuthbertson Bros. have also been threatened that the same lock out will occur at Swift Devonport.

What is the problem?

Swift are using their market power as well as deceptive and misleading conduct to stop Cuthbertson Bros. from participating in the market. They are seeking to control prices and force other participants out of the market.

Until Cuthbertson was locked out of Swift Longford operations, they purchased some 80 per cent of sheep and lamb skins produced in Tasmania.

The removal of a significant player from the Tasmanian market means that the prices for skins is likely to fall significantly (by an estimated \$3 to \$4 per skin) so producers will lose out.

In addition, the decision by Swift to stop processing Australian Lamb Co. livestock will mean producers will be likely to wear a further \$7 to \$10 per animal on the cost to ship them to Melbourne.

How does this breach the *Trade Practices Act* with regard to misuse of market power?

By divulging to their own agent prices being offered by competitors, Swift has obtained an unfair advantage in the market place. Hence, Swift through its market power is eliminating or substantially damaging its competitors by misleading and deceptive conduct.

Swift continues a pattern of acting in a manner which is an abuse of their market power as well as being deceptive and misleading.

This has seen Swift:

- approach Cuthbertson Bros. main customer, Dynasty, offering to sell sheep and lamb skins directly despite claiming to participate in negotiations with the Tasmanian Farmers and Graziers Association.
- move to significantly undercut the price for salting and shipping skins to Melbourne down from \$3 to \$2 per skin, despite an estimated cost ranging between \$2.30 and \$2.80.
- infer to some members of the farming community, that if Cuthbertson price their skins, they may or may not process the lambs.
- refuse to price skins which have been priced by Cuthbertson Bros..
- threatening to 'do the same' to Cuthbertson at their Devonport facility.

All these actions have occurred in a backdrop of Swift claiming they do not wish to participate in the skin market and they are simply acting to ensure farmers get the best price for their product.

Have there been any negotiations between Swift and Cuthbertson Bros.?

Yes, the Tasmanian Farmers and Graziers Association have attempted to organise two meetings.

Meeting one - February 18, 2009

At the first meeting which was also attended by another Tasmania skin market participant, Beasey as well as a number of farmers agents, Swift refused to attend.

During this meeting, the agents declared they had a conflict of interest as they are dependent on Swift for part of their income. The TFGA also declared a conflict of interest as they receive their fee from primary producers via Swift.

Despite this, the meeting resolved to support Cuthbertson Bros. acknowledging Swifts' introduction of the blatantly unfair tendering system.

Subsequent to the meeting, the agents have responded to the declaration of a conflict of interest by the TFGA, writing a joint letter to express their concern at the organisation's failure to negotiate on behalf of the farming community.

The TFGA have responded with a letter accusing the agents of making defamatory claims.

Meeting two - March 16, 2009

In response to a failure to resolve the matter and after being pressured by the State Government, the TFGA General Manager organised a second meeting, this time attended by two representatives from Swift and two representatives from Cuthbertson Bros.

No agents or other representatives of the farming community were invited to attend.

At this meeting, Swift argued they did not want to participate in the skin market and they wanted to increase the price to farms for skins to protect trade at Swift Longford and stop product being shipped to Melbourne for processing.

TFGA proposed a 'floor price' to address this, whereby Swift would set a floor price for skins, thus ensuring an appropriate return to farmers while ensuring Cuthbertson Bros. entry to the site to tender.

Both parties agreed to consider this proposal. Cuthbertson Bros. wrote agreeing to the floor price, provided there was a return to an open and transparent tendering process.

A week later Swift rejected the proposal outright.

What did Swift do while they were considering the floor price option put by the TFGA?

While Swift claimed to be considering the floor price option at Longford, the company made two approaches to Bill Stevens, Manager of Dynasty in Melbourne - an exclusive agent for Henan Prosper and long term major customer of Cuthbertson Bros..

At the first meeting on March 17, 2009, Swift asked why Dynasty was not purchasing Tasmanian skins from John Knox.

Dynasty Manager, Bill Stevens explained the skins varied in quality, were in small lot numbers and he had been purchasing skins from Cuthbertson Bros. for years.

Mr Stevens said he had a business practice of not dealing with competitors.

The next day, March 18, 2009 Swift representatives returned, stating to Mr Stevens, Dynasty could buy all the Tasmanian and Victorian production he wanted, but if he only bought from them.

Mr Stevens responded stating he had an excellent relationship with Cuthbertson Bros. and it was improper of him to deal with Swift on an exclusive basis.

Why not deal directly with agents and farmers?

The logistics of attempting to deal with each individual farmer or agent on every sheep and lamb in Tasmania being sent to the Longford Abattoir is time consuming and cost prohibitive.

It is simply not economically viable to undertake this.

The most practical solution is for all sheep and lambs to be assessed at one central site.

Traditionally this has occurred at the Longford Abattoir prior to processing at the facility as this is the most practical spot for this to occur.

Why not assess the livestock just prior to arriving at Longford?

This option is being used with a temporary inspection site set up adjacent to the Longford facility but Swift have responded and are now requiring producers and agents to agree to Swift to tender the sheep and lamb skin or they will not process the livestock.

In addition, there is nervousness from farmers to use the site as they fear they may not get their livestock processed by Swift if they get a skin price from Cuthbertson Bros.

Swift have repeated to farmers and agents, that if Cuthbertson Bros. price skins through this arrangement they will not price the skins.

What is happening now?

Where possible, Cuthbertson Bros. are inspecting livestock prior to shipment to Swift.

However, many producers are missing out on the opportunity for Cuthbertson Bros. to tender for their sheep and lamb skins – as they are too far away or the flock is simply too small to inspect.

Cuthbertson Bros. have agreed to work with agents and producers to ensure sheep and lamb skins are priced where possible, but this is not sustainable in the longer term.

What needs to be done?

Swift need to allow Cuthbertson Bros. on site at Longford so they can inspect livestock and tender their prices through an open and transparent tender process.

What does this mean for producers and Tasmania?

As the purchaser of some 80 per cent of sheep and lambskins in Tasmania, the withdrawal of Cuthbertson Bros. from the market means producers are likely to receive significantly less for their product as there is less competition, which is estimated to be between \$3 and \$4 per skin.

Couple with this the additional cost of exporting sheep and lambs to the mainland at a cost of between \$7 and \$10 per animal and the farmer is between \$10 and \$14 worse off.

The action, also runs the risk of killing off valuable export markets where Tasmanian branded meat is sold at a premium because of its high quality and disease free status.

Cuthbertson Bros. estimate the cost to the Tasmanian economy is around \$10 million per year.

What do Swift argue?

Swift argue their action is done on the basis of maintaining prices to primary producers as well as protecting the numbers of livestock that is processed through them as opposed to shipping to the mainland.

However, their actions would seem to indicate this is not their aim as:

- they have continually refused an open tendering process
- they have rejected a 'floor price' tender process
- they have approached Cuthbertson Bros' major buyer with an 'exclusive deal'
- they are refusing to process sheep and lambs at Longford, unless the right to tender skins is handed over to them
- they have significantly cut the costs of salting and shipping lambskins to the mainland, to a price of \$2 which is between 30 and 80 cents below cost recovery for Cuthbertson to provide the same service.

In addition to this, since Swift Australia refused to process the Australian Lamb Companies lamb, exports of sheep and lamb from Tasmania have significantly declined.

What has happened at a political level?

The Australian Senate, Tasmanian House of Assembly and Tasmanian Legislative Council have all moved motions in support of Cuthbertson Bros. In all cases the motions have been unanimously supported.

The Tasmanian Government has been monitoring Swift's actions.

What is the ACCC doing?

The Hobart office of the Australian Competition and Consumer Commission (ACCC) is investigating this matter, but at this stage Swift are refusing to discuss the matter with them.

**Section 11 Minter Ellison - Misuse of
Market Power**

ACCC brings Federal Court action for Misuse of Market Power

12 December 2008

In addition to the recent amendments passed by Parliament to the misuse of market power prohibition, the ACCC has taken the rare step of commencing Federal Court proceedings in alleging the misuse of market power against companies in the Cement Australia group. The proceedings are particularly significant in their allegation of a misuse of market power through the *acquisition* of a particular product.

Background – misuse of market power under section 46

Section 46 of the Trade Practices Act (TPA) prohibits corporations with a substantial degree of power in a market from taking advantage of that power for a prescribed anti-competitive purpose. These purposes include eliminating or substantially damaging a competitor, preventing entry into any market, or deterring or preventing competitive conduct in any market.

Usually, a misuse of market power manifests in conduct in the supply (or refusal to supply, price discrimination or predatory pricing) of particular goods or services. However, a misuse of market power can also manifest in the acquisition of goods or services, for example where a monopsonist or oligopsonist limits the ability of other corporations to effectively compete by tying up limited supplies of an essential input.

Historically, the ACCC has commenced relatively few proceedings for misuse of market power, largely because section 46 represents a relatively high threshold of TPA breach. An applicant must establish not only that the respondent has a substantial degree of power in a market (which has essentially been interpreted as a freedom from competitive constraint), but also that the respondent took advantage of that power (acted in a manner that it could or would not have been able to act were it subject to competitive pressures), and that the conduct had one of the proscribed anti-competitive purposes. The difficulty in establishing a misuse of market power has led to criticisms from both the ACCC and the small business lobby that section 46 provides inadequate protection against predatory and other anti-competitive conduct by larger companies.

These concerns have led to the government's introduction of the *Trade Practices Legislation Amendment Act 2008* (Cth) (Amendment Act) to reform to the misuse of market power provisions of the TPA, which were recently passed by Parliament. Amongst other things, the Amendment Act aims to strengthen section 46 of the TPA by clarifying and expanding the circumstances in which a corporation has 'taken advantage' of its market power, and clarifying that, in a predatory pricing context, a corporation can have a substantial degree of market power even though there is no proof that the corporation is able, or will be able, to recoup losses incurred from pricing below cost.¹

¹This amendment has been introduced in response to long-held concerns that the High Court's decision in *Boral* (2003) requires proof of an ability to recoup losses from below-cost pricing to establish a breach of section 46 for predatory conduct.

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Other articles in this edition: December 2008

Amendments to the Cartels Bill and Immunity Policy

On 3 December 2008 the Australian Government introduced into Parliament an amended version of its legislation to criminalise cartel conduct under the Trade Practices Act. The proposed cartel laws are supported by revised investigation, prosecution and immunity policies of the ACCC and Commonwealth DPP. How do the revised laws and policies differ from earlier drafts? What are the practical implications for Australian business?

Information sharing by competition regulators - are Australian executives exposed to foreign criminal laws?

Significant attention has been paid to the exposure of individual directors and officers to imprisonment under the Trade Practices Act. However, little attention has been given to an amendment quietly introduced in 2007 that permits the ACCC to share 'protected information with foreign competition authorities. Whilst the amendment has yet to be publicly tested, it has the potential to expose Australian executives to criminal proceedings in *foreign* jurisdictions - regardless of whether criminal sanctions are introduced in Australia.

ACCC's Revised Merger Guidelines

On 21 November the ACCC released a final version of its revised merger guidelines. The guidelines set out the analytical principles applied by the ACCC when assessing whether a merger is likely to substantially lessen competition under section 50 of the Trade Practices Act. This article provides an analysis of the practical consequences for Australian business, with a focus on the simplification of the notification thresholds applied by the ACCC.

Balancing environmental responsibility and consumer protection

Awareness of environmental responsibility and action to reduce environmental impact continues to grow and reflect itself in marketing strategies. However, such strategies must ensure consumers are not likely to be misled or deceived, contrary to section 52 of the Trade Practices Act. What principles should sales and marketing teams apply to ensure that their 'green claims' remain compliant with the Trade Practices Act? How is this illustrated in recent ACCC enforcement activities?

Misleading or deceptive conduct legal update: component pricing

Last month, the Federal Government passed the *Trade Practices Amendment (Clarity in Pricing) Bill 2008* (Bill). The Bill essentially amends the *Trade Practices Act 1974* (TPA) to regulate the use of 'component pricing'. In short, where a corporation makes a price representation to consumers, it may only use a component price if it also 'prominently' specifies the 'single figure' price payable for the good or service (where a single figure price is quantifiable).

For an overview of the Bill and its requirements, please refer to the Minter Ellison News Alert 'Government passes Bill to govern component pricing under the TPA' available ([click here](#)).

Third party access to Pilbara railways

There have been a number of significant developments in recent months in a series of applications for third party access to railway services in the Pilbara region of WA. This article considers the Treasurer's decision to declare particular 'all points' services provided by the Goldsworthy, Hamersley and Robe railways, the High Court's decision that services provided by the Mount Newman and Goldsworthy railways are not an exempt 'use of a production process', and the ARTC's interstate rail access undertaking.

International report: NZ legal update

An update of developments in competition law from across the Tasman, including mergers, cartels and regulatory reforms.

International cartel enforcement

The impending introduction of criminal cartel laws in Australia can be considered against the backdrop of significant cartel enforcement activity internationally in 2008.

About the author



Geoff has extensive knowledge of the gas and electricity sectors, with particular experience advising on regulatory, competition and commercial aspects of mergers and acquisitions and other transactions.

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