

Senate Committee Submission

Inquiry into competition and pricing in the Australian dairy industry

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Summary

Therefore the Trade Practices Act 1974 should be altered to facilitate farmers collectively bargaining with multiple corporations in situations where there is no effective competition.

The unconscionable conduct provisions the Trade Practices Act 1974 must be altered to reflect the changes in the marketplace caused by globalisation and processor consolidation, which has resulted in a severe reduction in the bargaining position of an individual farmer. In Section 51 AC, the burden of proof must shift from “a person” having to prove in court that a “corporation” has engaged in unconscionable conduct when seeking the supply of goods or services, to the “corporation” having to prove that they have NOT engaged in unconscionable conduct when seeking the supply of goods or services from a “person”. In practice, this will ensure that corporations would have to record and be able to prove that they have acted in good faith during contract negotiations and that contracts are easily understood and equitable.

Background

Geographical boundaries of food markets have changed from regional to national and many are now global in nature. These dynamics are increasing in pace and complexity and have significant implications for farm businesses, including a severe loss of bargaining power.

During the 1980's food manufacturing corporations became more concentrated and companies grew in size allowing them to develop links with global sources of capital. This process enabled manufacturers to reorganise and rationalise along industrial lines by closely coordinating production and processing, meaning that local (spot) markets were replaced with integrated or coordinated markets. In this capital dominated global market, few farmers have the time or expertise to market or process their own products nationally or internationally, therefore farmers have become reliant on corporations (often multi-national) for contracts so they can gain access to the wider economy. As a result, food production has changed from farmers selling products by exchange on an open market (auction) to signing production contracts with a corporation.

Widespread use of production contracts has resulted in the locus of decision making moving up the supply chain from farmers to processors, and now increasingly to retailers. Agricultural production contracts are generally aimed at modifying grower behaviour through the use of incentives and/or penalties to facilitate the delivery of products of specific quality and quantity. Contracting systems tend to reduce the flexibility, bargaining and decision making power of farmers while increasing the flexibility, bargaining and decision making power of the corporation due to their connection with the consumer and their global reach. Increased reliance on specialised production contracts often involves substantial investment by farmers in land, specialist equipment and infrastructure. This commitment may lock farmers into a contract system and limit their future bargaining power. In this increasingly common situation, farmers have a relatively subordinate role, where the central mechanism of control is the production contract. This also shifts production risk towards farmers and at the same time reduces their profit margin since a greater share of the profit from the final sale typically occurs at the retail end.

Production contracts in practice – lack of competition

The use of production contracts does not necessarily result in farmers losing money and going bankrupt. In fact, many farmers are happy with their contact relations with large corporations. However, satisfaction with the contracting system is dependent on two key factors, competition between processors (having other options) and fair and equitable contracts. In many instances this is not the case as there is often little functional competition and contracts are becoming increasingly complicated and significantly favouring the corporation. This illustrated by the current situation in the Tasmanian dairy industry.

Firstly dairy farmers have had significant change imposed through rapid exposure to global economic forces due to government deregulation culminating in July 2000, which resulted in fewer, bigger farms, higher stocking rates, greater use of feed supplements, conversion of land to pasture, as well as more debt and not other production options as they can only produce milk.

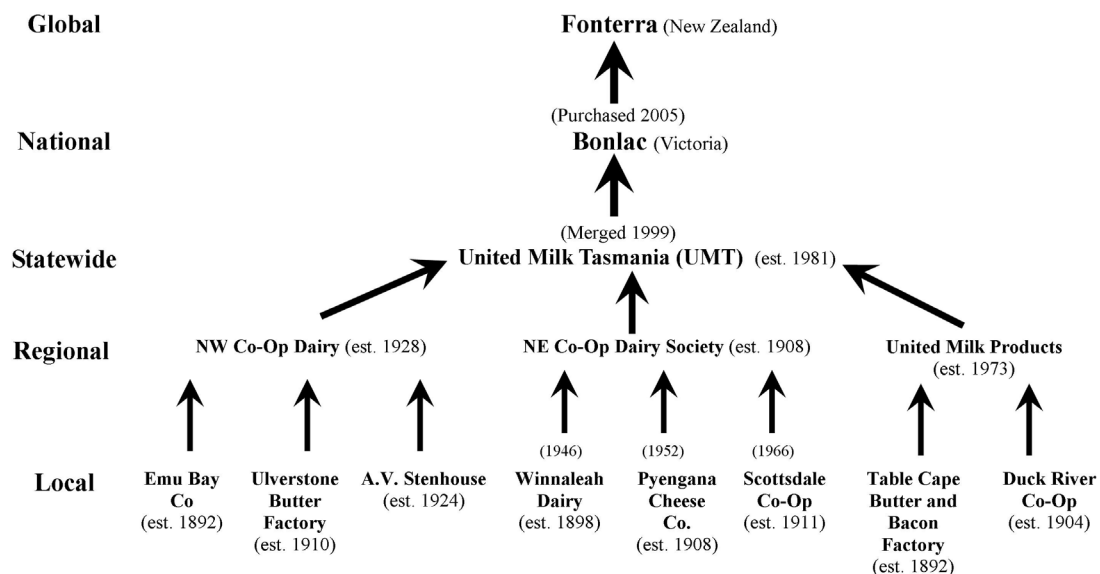
Moves towards deregulation and deregulation itself also accelerated the long term trend of horizontal consolidation of milk processing cooperatives/companies, in effect shifting the locus of manufacturing business decisions from local actors to regional (1908-1973), statewide (1981), national (1999) and finally global (2005) (Figure 1). This process has resulted in Fonterra being the major Tasmanian player with approximately 65% of the market for milk. The second biggest processor National Foods (25%) has also effectively reduced competition by the purchase on Hillwood Cheeses, King Island Dairy and Lactos.

Thus the current situation sees only three players in the Tasmanian market and all prices are based on the decision of the largest, Fonterra. Furthermore decisions about price are controlled by head offices in New Zealand (Fonterra), Japan (National Foods, Kirin Holdings) and the UK (Cadburys).

When the Trade Practices Act was enacted in 1974 there were three major Tasmanian Regional co-operatives as well as other players like Lactos, Cadburys and fresh milk

operations. In this new situation individual farmers are in effect pitted against global corporations. While farmers can form collective bargaining groups with each of three major processors, their bargaining ability is limited if there is no alternative market for their milk with other processors. The only way that there can be balance in this situation is for farmers to have the ability to collectively bargain with all three processors simultaneously.

Figure 1. Consolidation of dairy processing operations and the year of their Establishment (est.), merger or purchase.



Recommendation 1

The Trade Practices Act 1974 should be altered to facilitate farmers collectively bargaining with multiple corporations in situations where there is no effective competition.

Production contracts in practice – unconscionable conduct

As detailed above, Tasmania dairy production is dominated by multinational corporations without functional competition. Contract negotiations are typically one sided and on the basis of “take it or leave it”, with some negotiation strategies that could be viewed as unconscionable conduct.

Tactics include (but are not limited to) threats, coercion, deceit and contracts that are hard to understand and significantly weighted in favour of the corporation. Rather than present details of discussions I have had with individual farmers in regards to these tactics, I will present extracts from the Proof of Hansard, Senate Select Committee on Agricultural and Related Industries, Devonport, Tasmania, Tuesday 6, October 2009

Threats...

Mr Beattie—It is anecdotal, of course, but what we are hearing is that they are using the tactic of saying: 'Other farmers have signed; therefore, you might as well sign. You'll miss out on future payments if you don't sign.'

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Mr Perkins—They are still collecting the milk. I have heard a few veiled threats—but I do not treat that very seriously—that they would go and pick the milk up from others, that they would discard our producers and get it off Fonterra. Of course, it would be totally unconscionable that they would do that but, having said that, I do not put too much past them right now.

Coercion...

Senator COLBECK—Issues of threats to withhold payments or not make payments such as the no-disadvantage back payments are mentioned in a couple of the individual farmer precis. Is that a relatively regular occurrence?

Dr Abbott—In terms of withholding payments?

Senator COLBECK—With respect to signing a contract or that being the outcome.

Dr Abbott—It has only occurred with the new contracts that have gone out. A lot of the farmers in the Circular Head area have not seen our contracts yet. It was implied to those who were up for renewal of contracts that they would not receive their back payments. By signing these new contracts we are signing for a future and we are giving up the right to anything that was owed to us in the past.

Deceit...

Mr Beattie—The process is that you sign a contract and get it witnessed, and they sign it and witness it and send one copy back to you. We received our copies about four or five days before the end of that contract year. So they held onto those contracts and none of us actually knew whether they had accepted our contracts or not. That is representative of the behaviour that this company demonstrates.

Contracts significantly weighted in favour of the corporation...

Mr Wilson—If you commit and sign up for a period longer than one year—two, three or five years—there are additional payments, and those additional payments are expressed in extra cents per litre, but that is extra payments based on an unknown base price. From my point of view, it would be very dangerous to sign up for a longer term contract when you do not know what price you are signing up for. If everyone signed up for five years, they could take three cents off the base price, add a three-cent premium and we are all locked in.

Potential legal actions

If the ACCC is not willing to pursue allegations (due to whatever reason) then there is a distinct power imbalance, as the financial and legal resources of the corporation far outweigh that of the individual farmer, or even any farmer collective bargaining group. Furthermore, due to the nature of dairy farming (long planning horizons and high debt) any single producer pursuing a corporation through the courts would be bankrupted if an alternative outlet for milk production could not be found. If the ACCC is willing to pursue allegations then the farm business or businesses are still at risk as the legal action could drag on for a number of years. Therefore there is little incentive for corporations to negotiate in good faith, especially if those who benefit from one-sided negotiations reside in another country.

Recommendation 2

The unconscionable conduct provisions the Trade Practices Act 1974 must to be altered to reflect the changes in the marketplace caused by globalisation and processor consolidation. In Section 51 AC, the burden of proof must shift from farmers having to prove that a corporation has engaged in unconscionable conduct to corporations having to prove that they have NOT engaged in unconscionable conduct. In practice, this will ensure that corporations would have to record and be able to prove that they have acted in good faith during contract negotiations and that contracts are easily understood and equitable.

Other industries

The current situation in the Tasmanian dairy industry also has parallels in other Tasmanian primary production industries. Markets are dominated by global corporations.

Meat processing – Swift (JBS, Brazil).

Processing potatoes and vegetables – McCains (Canada), Simplot (USA).

Poppies – Glaxo Smith Kline (UK), Tasmanian Alkaloids (Johnson and Johnson, USA).

Similar tactics in contract negotiations as those alleged to have been used by National Foods are sometimes in operation, and the primary producers are specialised, heavily in debt and without alternative markets for their produce.

This is a personal submission

by Dr. Shane Broad