Tasmanian Suppliers Collective Bargaining Group

Submission to the Senate Select Committee –

Agriculture and Related Industries –

Dairy Issues Hearing

10 a.m. Tuesday 6 October – Devonport

Convention Centre

Devonport Tasmania

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TASMANIAN SUPPLIERS COLLECTIVE BARGAINING GROUP (TSCBG)

Submission to Senate Select Committee on Agricultural and Related Industries – Inquiry into food production in Australia – Dairy Issues

Tuesday 6 October 2009
(Federation Room, Devonport Convention Centre),
145-151 Rooke St, Devonport

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Section 2 Introduction

Introduction

The Tasmanian Suppliers Collective Bargaining Group thanks the Senate Select Committee for its interest in conducting this Inquiry.

This submission will demonstrate:

1. The economic and social circumstances liquid milk suppliers to National Foods Limited are in as a result of company action;
2. The companies culture of sustained unfair and unreasonable treatment of its liquid milk suppliers;
3. The liquid milk suppliers need for fairer contract terms;
4. The capacity of National Foods Limited to pay a renegotiated milk price and the willingness of the liquid milk suppliers to reach a mutually fair outcome
5. The need for stronger legislative requirements ensuring all primary producers and other Australian small and medium businesses have protection from large, insensitive multinational companies.

Section 3 Background Briefing

- **Overall Brief – The Issues**

Background Briefing - The Issues

Tasmanian Suppliers Collective Bargaining Group (The Group)

The Group is a collective of now 90 plus dairy farming members throughout Tasmania that has and is supplying liquid milk product to National Foods Limited. Some very loyal Group members have been supplying liquid milk product to the Company and its predecessors for up to 50 years.

The suppliers are now in dire or threatened with dire financial and social circumstances due to very biased Company contact arrangements and more recently an unreasonable and unsustainable liquid milk price offer from National Foods, which the Company is showing no interest in negotiating. The Companies actions and the plight of suppliers requires urgent resolution.

- The suppliers are seeking an improved liquid milk price offer, at least to cover costs of production and supply;
- A renegotiated liquid milk supply contract, preferrably with independent third party participation;
- Investigation of these matters by the Australian Competition and Consumer Commission (ACCC); and
- Clearer, more precise and effective legislation extending ACCC powers to ensure these or similar matters cannot be repeated.

What does the current milk price impasse mean?

National Foods Limited is attempting to rip off its Tasmanian milk suppliers by offering an exorbitantly low price for liquid milk, significantly below production costs.

Milk suppliers had been receiving 49 cents per litre for milk during the last financial year. National Food's offer is 29 cents per litre yet the average cost of production and supply is 39.8 cents, obviously higher in some circumstances. See Liquid Milk Production / Supply Costs

Many suppliers have not signed contract agreements primarily on the basis of the offer, and while they have no contract National Foods is paying them 20.4 cents per litre. The suppliers have incurred and continue to incur significant fixed costs in the development and maintenance of the essential infrastructure required to produce milk to a level that complies with National Foods requirements. See Section 4 legal letter to the company

In July and August milk suppliers lost substantial income, figures for example for individual suppliers include; $600,000, $280,000, $320,000, $180,000 etc.

A National Foods executive has advised at a meeting in Melbourne that "it has no obligation to maintain farmers as a sustainable business". Appallingly it added "if the farmers make losses so what". This can be supported by Statutory Declarations if necessary.

So the position is the Company has made a ridiculously low offer which the producers can't financially sustain and the Company doesn't care.

The suppliers for a long time have been frustrated and constrained by the Company's contract arrangements and this milk price offer has "tipped them over the edge".

The suppliers have no choice other than conduct a National Campaign highlighting their predicament and warning other liquid milk suppliers throughout Australia of what to expect.

What are the major contract issues facing suppliers?

The National Foods liquid milk supply contract is completely company biased leaving virtually no leeway for suppliers.

As indicated milk suppliers have substantial fixed costs in establishing and maintaining a dairy to the quality required by the Company.

The Group is seeking to renegotiate the Clauses of the contract that it believes is unfairly weighted in favour of the Company.

The contract is attached to Section 6 of this submission. Primary concerns of suppliers are contained in the legal letter of advice to the Group in Section 6 as follows;

> **"The contract document should be written in such a way that all parties understand what their obligations and entitlements are by reading the document. The way this contract is worded however there are a number of instances where National Foods reserve to themselves the right to essentially make or change the rules and the contract processes. A Number of examples of this are found in the definition section of Clause 1.1. For example;**
>
> **a) The milk supplier audit procedure "is a procedure that is" as prescribed by National Foods) from time to time";**
>
> **b) The "milk supplier performance review procedure" is also a procedure which is to be "prescribed (by National Foods) from time to time";**

c) **The "specifications" means not only the specifications set out in Schedule 1 but those as may be "amended from time to time" (by National Foods).**

For better protection to the individual producer there should be a clear requirement upon National Foods that they must not unreasonably make changes (that however may be implied by law) and there needs to be an appropriate dispute resolution mechanism in case their proposed changes are ones that will unreasonably impact upon each producer's profitability.

The advice continues:

"Clause 1.2 (of the contract) specifies that **the company you are (the producers) contracting with, National Foods Australia Pty Ltd, is merely acting as agent for three other companies. That has two significant effects.**

The first , and least important, I suspect, **is that it means that if (producers) have any claim it will not be against National Foods Australia Pty Ltd but against one or all of the three named companies. Of greater significance however is the fact that it means that all of your (producers) liabilities under the contract are not merely liabilities to National Foods Australia Pty Ltd but liabilities to each of the additional three named companies.**

For example Butterfields Specialty Foods Pty Ltd could sue you (producers) for loss and damage that it incurs in its gourmet foods production if it could establish that it has suffered some form of loss due to any breach by you (producers) of any term under the contract........**The potential liability of each producer is a potential liability to the three identified corporate entities".**

There are also difficulties with;

Clause 2 which sets out the producers obligations regarding the quality of milk that producers must supply and the basis of the payment by National Foods, for that milk.

These **obligations**, under Clause 2.7(b), **to supply a minimum quantity of milk per month and the penalties producers must pay National Foods if that minimum quantity is not supplied is a major concern and the point of many complaints from producers.**

The advice indicates "You will no doubt be doing your best to produce the appropriate quantity but **if for any month there is a shortfall it seems to me harsh that you actually have to pay National Foods money in supposed compensation of their loss. That overlooks the fact that National Foods most likely would not actually suffer a loss.**

For example, if one farmer was below their minimum requirement for a month but another farmer has an oversupply National Foods could not assert that they have suffered a loss yet the farmer with the shortfall would still have to pay compensation.

Interestingly however Clause 2.4 provides a discretion to National Foods whether to buy over contract milk. There is no obligation.

> Clause 5.3 enables National Foods to conduct its own milk supplier audit to monitor what it calls the supply chain and allows it to impose upon producers what it describes as an improvement program that they must comply with.
>
> **"Clause 7.4 effectively means the terms of the contract is the term set out in the second schedule plus an additional three months. The last sentence essentially says that for the last three months the price, volume and other general matters will be determined by National Foods.**
>
> **This is nonsensical in that "if the contract effectively is for a period ending 3 months after the referred date all of the contract terms should apply for that period and producers should not be at the whim of National Foods for the last 3 months."**

There are also concerns with Clauses 8.2, 9.1 (which prevents producers from transferring or assigning the Agreement without written consent), 12 and **18.9 (which provides that the Agreement embraces the entire agreement between the parties. The fact that producers may have had discussions with National Foods, or raised objections to what they are doing, is contractually irrelevant).**

Clause 18.9 is a major concern in that many of the producers' complaints relate to discussions and perceived agreements with National Foods field officers regarding additional infrastructure development, increased herd arrangements and milk pricing assurances. These arrangements are often based on precedent.

What are National Foods reasons for their milk price offer?

National Foods in an open letter released and reported by media, see Section 5;

1. Rejects it is abusing market power
2. Refers to claims made by a small group of dairy farmers in Tasmania
3. Appreciates there are difficult times in the industry indicates they are acutely aware of the impact current world dairy prices are having on farmers in Tasmania and elsewhere

4. "While National Foods can't control global commodity prices, it is important to us that farmers who supply our milk are treated fairly"
5. "The price National Foods is offering is, in fact higher than any other major milk buyers in Tasmania an 10 – 20 % higher than that being paid by our major competitor, depending on the suppliers milk intake"
6. We are paying a premium price to reflect our need for a flat supply of milk year round
7. National Foods followed the global commodity price at the request of the producers group
8. "while the farm gate milk price rose by more than 50 % between 2007 – 2009 the supermarket price increased around 10 %"
9. the commodity price has now slumped and the whole is affected
10. "We, as a viable business, have to produce and sell our product at a competitive price"
11. "There has been substantial growth in milk supply in Tasmania, with too much now being produced at farm level in relation to both market requirements and processing capacity"
12. National Foods actually pays two prices to milk suppliers, one milk, one cheese for international market etc.

What is the supplier group's response to National Foods?

The open letter is overweight on spin and underweight on fact

1. If National Foods are not exercising undue pressure on its suppliers it should explain
2. The 'small group of farmers' supplies approximately 40 million litres of National Foods 42 million litres annual liquid milk requirement

   Does 'small' used in this way reflect National Foods attitude to producers per sae
3. Implies that National Foods is treating producers fairly. The actual price offer 25 % below cost of production is hardly fair. The world dairy prices do not impact on Tasmanian milk, it is solely used for the local Australian market
4. Again fairness to producers is claimed. National Foods seem to recognize this is a key factor and contrary to their actual behaviour
5. They are not offering a higher price. National Foods adoption of a 'model farm' concept is spurious. They are not

actually comparing 'apples with apples'. NOTE: The 'model farm' concept is explained clearly later in this submission.

There is no justification for the higher price of 10 % let alone 20 % above the major competitor

6. National Foods claim they pay a premium. They have done so previously but now they are not even offering a break even point to producers. Pricing is explained later in this submission

7. National Foods did follow the global commodity price. But they did so to prevent suppliers leaving them in droves for their major competition, when last years suppliers had an option to leave

8. Is National Foods suggesting they have bought the market price down as the price to farmers has fallen?

   This is not reflected in the fact that the offer is 29 cents per litre to producers yet sells for more than $2 per litre retail

9. The whole industry is not affected by the slump in the world market, the industry is affected by actions such as National Foods price offer

10. The comment that National Foods needs to be a viable business to be competitive is ironic. Clearly they care about themselves but don't care about the viability of the small producers who supply them.

    How can National Foods remain viable if it sends farmers to the wall?

11. Is it not the same market

12. **In previous years National Foods actively encouraged producers to increase production. They encouraged farmers to expand and convert farms to dairying. The core of their oversupply problem is their loss of the Betta Milk contract.**

Do National Foods actions complement company policy?

No.

Kirin Holdings, National Foods parent company based in Japan has published and is proud of its **Corporate Social Responsibility Policy.**

The policy (Section 5 this submission) refers to **Integrity** as a key value of Kirin's identity statement. It **defines integrity** as

> **"maintaining a fair-minded and earnest stance towards all business activities. The things we each hold important".**

Kirin's Group Action Declaration is;

> **"To contribute to the sustainable development of society while carrying out business activities in an environmentally conscious manner;**
>
> **To contribute to a better quality of life for people around the world."**

National Foods published **Code of Conduct** states: (refer Section 5 of this submission)

> **"Every day we are faced with making a number of business related decisions. The Code of Conduct provides a framework and a resource to help us with these decisions. As a National Foods employee you are accountable for making decisions that are consistent with our Values, our Policies and the Law. This Code should be read in conjunction with Company Policy and procedures"**
>
> **For each decision you make you should ask yourself;** Questions including
>
> - **How would I feel if this were done to me or a member of my family?**
> - **Would I be proud to explain my actions to my fellow employees or my family?**
> - **How would I feel if my actions were on the front page of the newspaper or tonight's news?**

Kirin Holdings and National Foods spin and rhetoric do not match their insensitive implementation strategies.

Does National Foods have the capacity to pay more to its milk suppliers?

National Foods clearly has the capacity to increase its liquid milk price offer to producers and the capacity to pay them

- Dairy Globe, a weekly newsletter of major events in the domestic and world dairy markets reported on 10 August 2009, (full item in Section 4)

  "National Foods to merge with Lion Nathan - Kirin's Australian operations will soon be renamed Lion Nathan National Foods Pty Ltd. .... the existing ion Nathan senior management team to become its senior management team, with Robert Murray current CEO and MD of Lion Nathan, as the new CEO of Australian Operations

- Merger benefits better than expected .... **Kirin has reported that National Foods EBITDA improved from just $21 million in the first half of 2008 to $48 million to first half**

2009, which is exclusive of restructuring costs, but also reflect the mixed outcomes from a saving in milk prices, better unit prices ....

Over the full year Kirin estimates that it can save $50 million in costs from the integration of the two businesses"

National Foods results show a full 2009 forecast year of an EBITDA of $178 million.

It is also interesting to read a **transcipt** of a **teleconference** with **National Foods on Kirin Holdings website** (see Section 5). **Kirin President and CEO** asked **National Foods** on page 11 **"Why did you raise your earnings projections for National Foods Limited compared to initial targets?** There is no answer on the website, yet **in response to a further question from Kirin, page 12 "Please give us some idea of the improvement you have in mind for now and for subsequent fiscal years? National Foods Limited advised, we are currently reviewing synergies with the merger. That said we raised earnings for 2 reasons, first that personnel reductions are proceeding better than expected and second that we have been able to cut procurement costs ahead of schedule.**

In addition National Foods has recently completed **plush new head offices** in Melbourne, the **company can afford these** premises but it **can't afford to pay milk producers a fair and reasonable price for their hard work.**

Can milk producers explain clearly National Foods milk pricing compared to Fonterra?

Yes. See paper from John Wilson in Section 4.

The paper explains the differences with Fonterra and National Foods

Fonterra's market is more in line with the export market, producing products such as cheese, butter and powders, which can be manufactured and stored with no need to move the next day. This gives the producers opportunity to produce milk at times of the year when it is more cost effective.

Contrast this with **National Foods who market primarily into the domestic market, with mainly shelf life products such as liquid milk, yoghurts and soft cheeses.** They **require a constant flow of milk** every day for manufacture of these products. **Ensured constant milk flow adds additional** feed, power, labour and herd **costs.** Producing through adverse weather and prevailing feed prices through harsh winter conditions.

There lies the difference.

National Foods is modeling their price on Fonterra's price expecting contracted farmers to provide year round milk at the same price structure as spring calving farms.

What is the Model Farm concept National Foods refers to?

The 'Model Farm' concept is solely a creation of National Foods, it had no input from farmers in its development.

The "Model Farm" is best described in an evaluation by Grant and Melanie Rogers in Section 4 of this submission.

In summary:

- **National Foods is claiming to pay their suppliers a premium over Fonterra. However to achieve this suppliers need to adhere to strict criteria with regards to quality and daily production**
- **National Foods has heavy penalties Fonterra does not**
- **All bonuses paid by achieving this are included when calculating any comparison with Fonterra**

THAT IS;

- **National Foods are not paying the same price for the same quality milk;**
- **The company claim to account for step up but the examples in the evaluation show by not back paying these to July first as Fonterra do they can completely erode their premium to a point of putting their suppliers in a negative position;**
- **Finally the company have capped contract volumes with the impact on farm values and development.**

A clear case of smoke and mirrors.

What is the average cost of National Foods suppliers liquid milk production?

The Group has consistently indicated its average production cost across the year is 39-8cents per litre (10cents higher that the current price offer by National Foods).

'Cost of production' for each farm business is the sum of all dairy farm costs including the imputed value of unpaid labour, depreciation and finance costs divided by the annual milk production. See Dairy income and cost summary Section 4.

In 2007-8 the split, autumn or all year calving herds had average total dairy costs of 44.5cents per litre and the spring calving herds had costs of 42 cents per litre. Since 2007-8 the price of farm inputs such as grain, fertilizer and fuel have declined. It is therefore expected that the for 2009-10 total farm costs will be less than 2007-8.

The above supports the Groups average production costs figure.

Is the Group aware of the milk prices being paid to suppliers by National Foods in other Australian States?

Yes. In New South Wales producers are being paid 57 cents per litre. Generally they are in the last year of a two year contract.

In Queensland we know of prices in September to 59 cents per litre. On top of this grain costs are close to 50% below that of Tasmania.

September's Tasmanian price is around 20.4cents per litre.

Tasmanian producers' experience suggests producers in those States will shortly be afforded the same treatment and low price offer, but they have the option of somewhere to go, given the competitive markets.

Given the low milk price currently being received by producers, has the supermarket retail price reduced similarly?

Australian Bureau of Statistics (ABS) confirm that the average **retail milk price in six cities has fallen 7% on average** from their recent peak price.

The **milk price paid to typical Tasmanian dairy farmers** has **fallen by around 42%** since the peak price in 2007-8.

ABS retail milk **date is only available up to June 2008 so the fall in the milk price paid to dairy companies for 2009-10 is not yet reflected** in ABS price data. See Section 4.

Is the Group contemplating a formal complaint to the ACCC?

Yes. The Group has obtained an initial legal briefing and a legal letter has been sent to National Foods.

The initial legal brief suggests National Foods has potentially contravened the provisions of Point IVA of the Trades Practices Act exercising unconscionable conduct. It is also quite possible that other Sections of the Act have been contravened.

The Group proposes to seek formal Senior Council advice with a view to lodge a formal completion with the ACCC.

The matter raises the broader question of the current capacity of the Trades Practices Act to effectively protect small and medium businesses from unfair and unreasonable conduct by larger, dominant companies. The prosecution success rate is poor.

The group will be pursuing government action to legislation is this regard.

Have many of the Group's farmers experienced specific difficulties with National Foods dominating attitude?

Yes. Various individual submissions highlighting producers specific difficulties and National Foods dictatorial treatment will be presented to the Committee.

The submissions will include one from Circular Head milk producers highlighting eight cases of unfair treatment. One written submission from Victoria suggesting National Foods don't care for the farmers attitude is a cultural issue within the company.

Also the **concerns of producers Noel Young and John Jones** follow;

Mr. Young has a dispute which highlights his **agreement with National Foods representatives has not been honoured. In fact National Foods have applied a penalty of $43,000 for excess milk production in 2008.**

Mr. Young is disadvantaged substantially financially and the matter has still not been resolved.

Mr. Jones' situation highlights the encouragement given by National Foods representatives to increase milk production and the Company's inconsistencies.

Mr. Jones' headed National Foods message is 2005 that they needed more summer and winter milk. The company was offering higher pricing for those months. Mr. Jones built a new dairy and over time imported an extra 120 head of cattle at a cost of more than $180,000.

Now National Foods have taken money from these months and placed it back in the spring months.

National Foods do not understand that producers cannot change their herd around in a month of two.

This example of disregard and inconsistency by the company **highlights the need for substantive changes to the current National Foods contract.**

The contributions from Messrs. Young and Jones are included in Section 4 papers.

Has the group received public sympathy and support?

Yes. Public support has been overwhelming, largely as a result of the very significant media coverage within Tasmania and the growing interstate media interest.

Across Party political support is very encouraging, particularly that of the Tasmanian Premier and the Minister for Primary Industries and Tasmanian Senators.

The Suppliers Group wish to take this opportunity to thank all for their support and again expresses its appreciation for the Select Committee's interest in conducting this Inquiry.