

choice



Australian Food and Grocery Council

**Supplementary submission to the
Senate Economics Committee Inquiry on
The impacts of supermarket price decisions on
the dairy industry**

April 2011

SUPERMARKET OMBUDSMAN – OUTLINE FOR DISCUSSION

Summary:

This is a joint supplementary submission from CHOICE and the Australian Food and Grocery Council to the Senate Economics Committee's inquiry into the impacts of supermarket price decisions on the dairy industry. It provides an outline of options for further discussion around the establishment of a Supermarket Ombudsman, and follows earlier individual submissions to the inquiry from both organisations.

Options for the establishment of a Supermarket Ombudsman can be characterised as ranging from the 'standard' form of Ombudsman in an Australian context (consumer-facing and independent with no regulatory powers) to the UK's Groceries Code Adjudicator (supply-chain facing, sits independently within the Office of Fair Trading and administers a strengthened mandatory code).

Rather than suggesting functions based entirely on existing models, the most useful approach is likely to be one that identifies what is 'missing' from supermarket competition issues in Australia and works backwards. For example, key issues identified through the recent milk discounting debate include the need for a more proactive focus and follow-through on competition concerns, greater transparency around pricing and the capacity to address retailer market power where it results in anti-competitive behaviour. This document is an outline for further discussion, and it is proposed that any implementation of an Ombudsman should be subject to a thorough and detailed process of policy development and consultation by Government.

Overview of key functions:

- **Leadership** - ensuring that competition and fairness is driven at a national level through a constant and proactive focus on these issues beyond political cycles, unlike the ACCC, which is concerned with issues across the whole economy; bringing a higher profile and increased level of transparency to the investigation of these issues.
- **Addressing industry and consumer concerns** – handling supermarket-related complaints from suppliers and consumers and ensuring greater transparency around pricing and costs along the supply chain through a strengthened Produce and Grocery Industry Code of Conduct; publicising guidelines on how to comply with the Code of Conduct; engaging in education and awareness campaigns for consumers (may also assist with an education campaign under the proposed National Food Policy).
- **Compliance** – adjudication of disputes under a strengthened Produce and Grocery Industry Code of Conduct (see 'Avoiding duplication' below); monitoring compliance with the Competition and Consumer Act, conducting preliminary investigations and, where there is reason to believe a contravention has taken place, referring matters to the ACCC for investigation and enforcement. Possible power to make "binding references" to other Commonwealth agencies requiring investigation and potentially recommending action; could require agencies to investigate matters within a specified timeframe and report back.
- **One stop shop** – directing queries to appropriate agencies where these fall outside the Ombudsman's scope.
- **Research** - researching systemic issues and potential market failures and educating consumers and industry on competition and fair-trading issues in the grocery industry; using research to challenge the power imbalance that makes smaller players reluctant to provide evidence against larger businesses (an issue raised in the ACCC's Grocery Inquiry and noting the small number of complaints to the current Produce and Grocery Ombudsman); recognising that in circumstances of significant market power, a lack of complaints may represent evidence of very significant market failure rather than an absence of one; commenting on notifications, applications for authorisation and mergers.
- **Recommending changes** – making recommendations to Commonwealth and State governments on the reform of legislation that restricts competition in the grocery sector based on actual experience with suppliers, retailers and consumers.
- **Sunset clause** – in-built review point, for example after five years, to assess whether the Ombudsman is effective and/or is still required.

Key issues:

- **Funding model:** propose a combination of statutory base funding plus retailer funding using a formula which will take into account the size of retailers as well as the number of complaints involving them and requiring resolution. Statutory base funding from Government would enable the Ombudsman to fulfill its monitoring, education and research functions, while retailer funding would provide an incentive for retailers to deal with disputes and complaints effectively and improve customer service. It is not proposed that consumers or small businesses would be required to pay fees in order to bring complaints to the Ombudsman for resolution.
- **Budget:** under the proposed model, the Ombudsman's funding would vary depending on the volume of complaints handled. This is likely to have minimal impact relative to the turnover of Australia's major supermarkets, particularly if the Ombudsman can be shown to take actions that result in lower prices in some instances, as has been suggested with reference to the UK model.
- **Governance:** would depend on whether the Supermarket Ombudsman sat within the structure of the ACCC (but as an independent office) or as a completely stand-alone office. The former model aligns with the UK scheme in which the Adjudicator will be appointed by and sit within the Office of Fair Trading, which will set the Adjudicator's annual budget. In this arrangement, it is proposed that the Ombudsman would report directly to the relevant Federal Minister rather than to the head of the ACCC. In the latter stand-alone model, the independence of the Supermarket Ombudsman would be assured through the appointment of an independent chair along with consumer representation, for example in the form of a council with oversight.
- **Coverage:** threshold for coverage of retailers could be based on annual turnover (as in UK model) or supermarket store size (as in Australian unit pricing model).
- **Avoiding duplication:** suggest that the Supermarket Ombudsman would take over the Produce and Grocery Industry Code of Conduct (currently outsourced to private mediation firm) so would not be duplicating costs. This code would be significantly strengthened (and made mandatory), similar to the UK model, thereby providing the Ombudsman with an enhanced adjudicating function. Administrative duplication would also be minimised if the Ombudsman sat within the structure of the ACCC, similar to the UK model. Not proposing any duplication of prosecution functions, although information-gathering powers for investigations would be required, and could be streamlined if the Ombudsman sat within the structure of the ACCC.

- **Strengthened Produce and Grocery Industry Code of Conduct:** amend the current Code to require that:
 - All retailers' contracts with their suppliers include a fair dealing clause.¹
 - Retailers are prohibited from making retrospective adjustments to terms and conditions of supply (unless where this has been provided for).²
 - Retailers are required to enter into binding arbitration to resolve any dispute with a supplier.
 - Retailers are required to keep written records of all agreements with suppliers on terms and conditions of supply.
 - The Ombudsman publishes guidelines on specific provisions of the Code of Conduct when necessary and advises the relevant Minister on the operation of the Code of Conduct.

¹ Note the unfair contract terms provisions in the Australian Consumer Law (Schedule 2 to the Competition and Consumer Act) only apply to standard form contracts. Arguably, not all contracts between the grocery stores and suppliers would fall within this category.

² See page 338 of the 'Report of the ACCC inquiry into the competitiveness of retail prices for standard groceries', July 2008 which refers to instances where the major supermarket chains engaged in practices which could 'lead to an inappropriate risk allocation in some circumstances'.

Counterfactual – what difference would the Ombudsman actually make?

- The fact that some of the recommendations of the 2010 Senate Economics Committee inquiry into the dairy industry have not been followed up, including those concerning the ACCC monitoring market power and impacts of generic products, point to significant information gaps in the analysis of anti-competitiveness in the Australian supermarket sector. A Supermarket Ombudsman would have been on the case following the last inquiry.
- The significant confusion around who is paying what along the milk supply chain (farm-gate prices versus processor margins versus retailer costs) and various claims around potential impacts point to a general lack of transparency and clear evidence in the current milk debate. An Ombudsman would be well-placed to have shed light on some of these issues at an early stage, rather than operating under the veil of secrecy associated with the ACCC.
- The ACCC is rightly concerned with issues throughout the entire economy, whereas a Supermarket Ombudsman would be very specifically focused on supermarket issues. As arguments for the UK equivalent have noted, it is one thing to have relevant laws and regulations in place (the UK Grocery Supply Code of Practice), it is quite another to ensure they are promoted and followed.
- Without the establishment of a Supermarket Ombudsman, the Produce and Grocery Industry Code will continue in its current voluntary, low-profile form (note it received only 10 complaints over its last financial year of operation).
- Arguments associated with the UK Code Adjudicator are that the increased level of transparency and certainty between retailers and suppliers in relation to contracts will in turn mean consumers benefit from increased investment and innovation by suppliers, in the long run feeding through into better quality products, more variety and lower product prices in some cases.

Hypothetical case study: Juice Supplier ABC

Juice Supplier is one of the main leading brands of fresh orange juice in Australia and currently sells its 1L fresh orange juice to Retailer XYZ at a wholesale cost of \$1.50 which then retails for \$2.50. On 1 April 2011, Retailer XYZ tells Juice Supplier that it intends to sell its juice in a promotion for \$1.60 for the period 2 April 2011 to 9 April 2011 and that it will only be paying Juice supplier \$1.00 for its product during this period. Retailer XYZ tells Juice Supplier that if it does not agree to these terms, Retailer XYZ will be promoting the other major suppliers of fresh juice (and providing them with the best shelf positions) but not Juice Supplier's products.

Under a strengthened Code of Practice and the 'fair dealing' clause, Retailer XYZ would have been required to provide reasonable notice of its intentions to Juice Supplier to engage in such a promotion. This is assuming that under the written terms and conditions of supply there was provision made for Juice Supplier funding a promotion in such conditions.

Under the proposed model, Retailer XYZ could ask the Ombudsman to arbitrate the matter. The Ombudsman could depending on the circumstances decide to direct that Retailer XYZ provide Juice Supplier with a rebate of a particular amount given that there was only a short period of notice provided.

Under the proposed model, if this type of conduct occurred frequently, the Ombudsman would have published guidelines outlining how reasonable notice should have provided. This is especially significant where products concerned have a short shelf life.

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