

GROCERIES MARKET INVESTIGATION

Summary of the round-table discussion with primary producers concerning the Supermarkets Code of Practice held on 5 December 2007

Background

1. The purpose of the round-table discussion was to allow the Competition Commission (CC) to gather views on a confidential basis from a range of primary producers¹ on the operation of the Supermarkets Code of Practice (SCOP) and how it might be amended in the light of the CC's provisional findings on supply chain issues.

Focus on transfer of risk and unexpected costs

2. There was overall agreement that the CC had been right to focus on the transfer of risk and unexpected costs by the supermarkets to suppliers as the practices most likely to give rise to concern and which needed to be addressed in the remedies phase of the inquiry. This was particularly the case for retrospective charges and charges sought for matters beyond the producers' control. The supermarkets' approach to cost-sharing on waste product was a special source of concern. The waste was often generated by poor buying policies but the supermarkets could require a supplier to share the cost, sometimes retrospectively, because of the threat that their contracts would be re-tendered and their investment in supporting those contracts lost.
3. On risk transfer, the producers explained that, as they already carried the risk for the vast majority of the product life cycle, it was doubly unfair for the large supermarkets to attempt to load them with even greater risk. They were always vulnerable to unexpected events such as a recent outbreak of foot and mouth disease. In such circumstances producers sometimes did not enjoy contractual protection—the contracts they had might not include actual order volumes and might have mechanisms for price setting (based on prevailing market conditions) rather than firm prices.
4. The producers also identified a range of other types of behaviour undertaken by the large supermarkets which remained of concern to them:
 - A lack of willingness to enter into bilateral negotiations with suppliers. The supermarkets regularly took a take-it-or-leave-it approach to negotiations, including key issues such as price, order volumes and retrospective amendments. Instances in which the supermarkets sought significant contributions from processors to continue the trading relationship, gradually eroding the returns being earned by the producers and altering key trading arrangements without notice and on a unilateral basis, were cited.
 - Introducing a lack of certainty in their direct dealings with the producers, encompassing order volumes, prices and even the loss of contracts altogether, which was leading some producers to exit particular markets or switch to other products.

¹Farmers or growers of produce, which is either used as the raw ingredients for processed food or sold by retailers in unprocessed form.

- Rejecting batches of produce on spurious quality grounds when their shelves were full, only to accept them the following day when the shelves were empty.
 - The tendency of the supermarkets to react to short-term shortages by importing produce, sometimes from un-inspected sources while imposing a rigorous inspection regime on UK suppliers.
 - Using price comparisons with importers to drive down the prices of UK producers although the importers could only meet a lower standard of quality.
 - Using the UK supply sector to subsidize imports, for example, in cases where imported produce was more expensive than identical product sourced from within the UK, although the two were retailed at the same price. There was also a concern expressed that foreign animal welfare standards often differed to that required of UK producers. These differences led to differing prices and potentially misled consumers. It was suggested that any independent monitoring entity should be able to address these sorts of producer concerns.
5. Generally, the producers pointed to a continual downward pressure on the supply chain, by the supermarkets, driven by purely short-term profit-making considerations and demanding increasingly tight terms which the producers felt unable to withstand. Their acquiescence served to encourage the supermarkets further until producers were forced to exit the market (as had happened recently in the milk sector and pig processing industry).

Extending the range of the Supermarkets Code of Practice

6. The producers agreed that the SCOP should cover all the major multiple retailers, with coverage determined on the basis of outlet floor space or turnover. In practice, the second tier retailers adopted similar patterns of behaviour to the large supermarkets and some producers found that smaller retailers could often be more difficult to deal with, possibly because they did not enjoy the benefits conferred by the size of the large supermarkets and possibly because they had to follow their prices. Limiting the SCOP to a subset of the retail sector inevitably added a cost to those retailers included that was not borne by their competitors; this could in itself be regarded as anti-competitive.
7. It was also important that processor/primary producer relationships were brought within the ambit of the SCOP; the processors were as able to dictate prices and other contractual terms as were the large supermarkets. This left the primary producers in the position of being price takers, regardless of the economic environment and how this might impact on the cost of bringing particular products to market. In addition, the SCOP could also usefully be extended to intermediaries such as wholesalers and marketing agents, whose actions could have a significant impact on the primary producers, and to intermediary 'category managers' who purchased specific types of produce for re-selling to the supermarkets; their buyer power was very similar to that of the large supermarkets.

Improving the effectiveness of Supermarkets Code of Practice

8. The producers were keen to see the SCOP made more effective. The large supermarkets had found ways in which to circumvent the provisions of the SCOP in practice while continuing to comply in form. An effective SCOP could give the producers the confidence to invest in greater production, introducing more product variety and newer storage and packing facilities. This would allow the producers

overall to become more efficient and the benefits would naturally be passed on to consumers. Some producers also thought that a more effective SCOP might benefit the retailers, to the extent that it removed abuses in the market and allowed them to compete with each other on a more equal basis.

9. Particular thoughts to emerge during the discussion were:

- The original CC proposals from the 2000 inquiry, which would have prevented the large supermarkets from 'seeking' certain things from suppliers, would offer a better alternative to the present prohibition on 'requiring' them do things.
- It was important that retailer/supplier contracts were properly recorded, even in cases where order volumes and prices were not specified, in order to create a proper audit trail.
- Some elements of a revised SCOP could usefully be aimed at ensuring that those who did the actual buying from producers properly understood the SCOP and were aware of the significant impact that their decisions could have on the producers, particularly over the longer term.
- The primary producers thought that complaints could be handled on an anonymous basis, given that the type of behaviour likely to be the subject of complaint often affected more than one retailer and more than one supplier. There were, however, clear disincentives for individual producers to complain about the behaviour of an individual retailer.
- The suggestion that in the event of a complaint a retailer would not be able to alter the terms of its relationship with a supplier for a specified period was not seen as a practical way of addressing the problem. It would encourage poor performance among suppliers and would be open to abuse by weaker suppliers and might, overall, have an anti-competitive effect.
- It was important not to over-regulate, as this might impose additional costs on the producer sector which could make it uncompetitive with overseas producers.

10. The producers could not identify any of the current SCOP provisions that were unnecessary or which caused problems for them.

Monitoring and enforcement of the Supermarkets Code of Practice

11. The producers regarded it as important that the retailers engaged positively with a revised SCOP and saw it as a mechanism for improving standards rather than a regulatory burden that had to be complied with or even evaded. However, they were agreed that, given the acute competitive pressures on the supermarkets, any amended SCOP needed to be supported by proactive, effective monitoring and enforcement rather than relying, for instance, on a voluntary approach.

12. Particular points to emerge on the nature of the monitoring regime were:

- A monitoring authority needed to be independent, proactive and able to respond to circumstances quickly. Some parts of the UK producer industry were in need of rapid solutions to the problems they faced—in practice it might be possible for the monitoring authority to adopt a less proactive role once these issues had been resolved.

- If the Office of Fair Trading (OFT) were to retain a monitoring role, there would need to be significant change, both in terms of the way in which it worked and the expertise available to it.
 - There were, however, two reasons cited as to why it should not be the OFT: specifically, concern at the way in which the current SCOP had been created and monitored and the benefits of ensuring that there was no conflict between administration of the SCOP and the OFT's wider consumer protection responsibilities. An alternative model was an advisory authority, along the lines of the Food Standards Agency.
 - Were an alternative to the OFT chosen as the monitoring authority, it would be important to ensure that it included representation from all parts of the supply chain, particularly including those with actual experience of the operation of the market. It should also be able to investigate all the links in the food chain.
 - The producers generally preferred a proactive model for monitoring a revised SCOP to the reactive model that had been the practice up to now. There were, however, views that a reactive model could be effective, if complaints could be made anonymously and rigorously investigated.
 - There was agreement to the suggestion that the monitoring authority publish regular reports on its work. These would be useful in naming and shaming poorly-performing retailers and in raising standards and building a culture of best practice across the board. The development of a best practice culture could, in particular, focus on the need for retailers and intermediaries to take a longer-term view of their relationships with the producers and the benefits of establishing a strong producer base.
13. A range of views was expressed by the producers on how the costs of a revised monitoring and enforcement regime should be met:
- They should be met by the retailers, on the basis of size.
 - The costs should be apportioned on a case-by-case basis depending on who was at fault.
 - As a monitoring authority would be delivering benefits to the public as a whole (innovation in the supply chain, greater customer choice, transparent animal welfare standards) it should be publicly funded. A public sector monitoring body would also have greater independence and authority while an annual report to Parliament would aid wider public accountability.
14. The producers thought that there was a definite role that trade associations, particularly smaller ones closer to the concerns of individual firms, could play in presenting issues to a monitoring authority. Equally, however, it was important that the monitoring authority should be able to get to grips with problems on the ground rather than interfacing solely with representational bodies.