



Attachment A – Supplementary analysis on net benefits

The Independent Review of the Food and Grocery Code of Conduct (the Code) concluded that there is a substantial imbalance in market power between supermarkets and their suppliers and that the voluntary Code is not achieving its purpose of addressing this imbalance.

The Review considered the following policy options to address these issues:

- **Option 1:** maintain the status quo, to remake the Food and Grocery Code of Conduct (the Code) with no changes.
- **Option 2:** remake the Grocery Code as a mandatory industry code of conduct with meaningful penalties to drive greater compliance to apply to all supermarkets.
- **Option 3:** remake the Grocery Code as a mandatory industry code of conduct with meaningful penalties to drive greater compliance to apply only to the major supermarkets, as proposed in the Final Report.

Note that the option to allow the Code to sunset and not be replaced was not considered comprehensively given this option is likely to have a high net cost to the industry and community. While there may be some cost savings for current signatories to the voluntary Code (i.e. reduced compliance costs of around \$3.6 million annually), there would likely be high costs to suppliers as they would no longer benefit from minimum standards of conduct, and conduct in the industry would be expected to decline. These would significantly outweigh the compliance cost savings.

Treasury has weighed the cost and benefits (qualitative and quantitative) of each of the three options listed above to determine the best solution for the industry.

Option 1: maintain the status quo

The food and grocery industry would continue to be regulated by the Code in its current form without any changes to the provisions. This would not preclude the industry from taking its own initiatives, for example, other retailers or wholesalers could choose to become signatories or implement commercial practices that go beyond the minimum standards set in the Code.

Costs

Maintaining the status quo will likely continue to impose costs on food and grocery manufacturers and suppliers (particularly smaller ones), since there is evidence that the current voluntary Code is not effective in promoting fair commercial dealings between supermarkets and their suppliers. This may also have flow on implications for the people that support them, including employees of suppliers.

The 2022-23 supplier survey suggests that poor conduct is still occurring in the industry.¹ Simple analysis based on the incidence of conduct and the expected costs for suppliers

¹ See Food and Grocery Code Independent Reviewer, [Annual Report 2022-23](#), 2023.

suggests that the harm could be substantial. For example, even under conservative estimates, the harm to suppliers collectively is in the order of \$7 million each year.² Using more realistic assumptions, the harm could be in the order of \$64 million each year.³ This does not include transfers from suppliers to supermarkets, which could be between \$3 million and \$32 million due to late payments and deductions that suppliers have not consented to.⁴ Arguably these also result in net losses since smaller companies are less able to bear such costs.⁵

Maintaining a Code that contains ineffective provisions imposes costs on supermarkets, suppliers and consumers. Inefficiencies will be created in the industry by requiring signatories to maintain processes and procedures that do not adequately address suppliers' concerns. Specifically, it is estimated that compliance costs are in the order of \$3.6 million for the current signatories to the voluntary Code.⁶

Maintaining a voluntary Code may further lead to barriers to cultural change as industry participants may gradually withdraw support for the Code. Many of the suggested changes in the Review, such as improving the good faith provisions and new protections against retribution, directly address supplier concerns and seek to strengthen the commercial relationships between the parties.

Benefits

This option would benefit the current signatories because it would allow them to continue business as usual and would not impose any additional compliance costs.

Signatories have made substantial investments to change their business operations to comply with the Code (such as updating supply contracts, training staff and employing Code Compliance Managers). Maintaining the status quo will allow signatories to continue to operate under current arrangements without the need to modify them. This also provides the industry with greater regulatory stability and certainty.

Conduct in the industry is also much improved compared to before the Code's commencement.⁷

Net Benefit

Compared to the counterfactual of no Code at all, this option is likely to have a net benefit to the industry and community as it has raised the standard of conduct in the industry.⁸

However, the current Code does not adequately address the issues that the Review has identified. In particular, the lack of penalties and the ability for signatories to choose not to be bound by the Code undermine its effectiveness.

Further, the Code's protections need strengthening to address issues that have been raised in relation to the dispute resolution processes, treatment of fresh produce suppliers, and the ability for supermarkets to opt out of their obligations without clearly communicating this to suppliers.

Without amendment, the current Code risks continuing to impose compliance costs without adequately delivering benefits for suppliers. This will mean that suppliers are likely to innovate

² See Annexure 1 for the assumptions underlying these calculations.

³ Ibid.

⁴ Ibid.

⁵ The Regulatory Impact Statement for the Payment Times Reporting Scheme estimated that moving to a 30-day payment time for payments from larger businesses to smaller businesses would deliver an annual net benefit of \$522 million to small businesses and \$313 million to the Australian economy. See Department of Industry, Science, Energy and Resources, [Payment Times Reporting Scheme: Regulatory Impact Statement](#) (OBPR ID: 24466), 4 May 2020, p. 22.

⁶ See Annexure 1 for the assumptions underlying these calculations.

⁷ See Food and Grocery Code Independent Reviewer, [Annual Report 2022-23](#), 2023.

⁸ See Food and Grocery Code Independent Reviewer, [Annual Report 2022-23](#), 2023.

less, reduce investment, shrink or exit the market. The market does not work effectively and efficiently, and the overall welfare of Australians diminishes.

Evaluation of Option 1	Compared to the counterfactual of no Code at all, Treasury has concluded that Option 1 is likely to have a net benefit. However, this option is the least beneficial of those considered given the voluntary Code is not effective, with losses to suppliers of at least \$7 million annually (and up to \$64 million), despite substantial compliance costs in the order of \$3.6 million. Option 1 is therefore not recommended.
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Option 2: remake the Grocery Code as a mandatory code to apply to all supermarkets

Remaking the Code as a mandatory code applying to all supermarkets would extend the coverage of the Code. This would mean that all supermarkets, including smaller second tier supermarkets would be subject to the Code.

A mandatory approach may allow for more stringent provisions to be introduced since supermarkets will be bound by these whether they agree with them or not. This option may also involve including civil pecuniary penalties and infringement notices in the Code, which would drive greater compliance.

Costs

This approach may impose significant regulatory costs on second tier or smaller supermarkets in circumstances where there is little evidence of problems in respect of their dealings with suppliers. In particular, the purpose of the Code is to address significant bargaining power imbalances between supermarkets and their suppliers. There is little, if any, bargaining power imbalance between smaller supermarkets and their suppliers.

If all supermarkets were included, compliance costs for smaller supermarkets are estimated to be around \$150,000 initially and then around \$50,000 annually. If all retailers were covered, this would result in annual compliance costs upwards of \$100 million across all smaller retailers. Imposing unnecessary regulation on these entities may reduce their ability to compete and would restrict growth in Australia's concentrated food and grocery market. It would also act as a barrier to entry for new players, and may ultimately undermine competition in the industry, to the detriment of suppliers and consumers.

There is also a risk that some of the additional costs imposed by the Code, and an improvement in bargaining power of suppliers, will increase grocery prices for consumers. It is difficult to quantify this impact as it is unclear how much supermarkets will be able to pass through these costs. The current environment of relatively high inflation and cost-of-living pressures is likely to reduce supermarkets' ability to pass these costs on, especially if supermarkets continue to be under scrutiny from the media, the Government and the Australian Competition and Consumer Commission (ACCC).

Benefits

This approach would ensure there is a consistent minimum standard of behaviour across the industry. Extending the coverage of the Code may allow suppliers to be protected in their dealings with a wider number of supermarkets.

A mandatory code avoids the risk of signatories potentially withdrawing from the code in the future. Civil pecuniary penalty provisions can also be applied to the Code without fear that it may deter future signatories or lead to existing signatories withdrawing. This would allow the ACCC to effectively enforce compliance and deter breaches of the Code.

If a mandatory Code can address the losses experienced by suppliers under the current voluntary Code (see discussion under Option 1 above), there is the potential for a mandatory Code to bring significant benefits, in the order of tens of millions of dollars.

Providing suppliers with greater financial returns and stability will also allow them to invest more in research, development and innovation. This can contribute to technological and efficiency improvements, which can reduce production costs, and downstream prices. This ultimately benefits consumers where suppliers can offer lower priced products and/or greater product choice.⁹ This benefit is common to all options but is likely greatest for Option 2.

Net Benefit

Compared to the counterfactual of no Code at all, there is no clear net benefit for the industry and the community from Option 2. It will likely improve outcomes for suppliers. However, there will be increased compliance costs from applying the Code to all supermarkets that may not deliver fully offsetting benefits. Increased regulation that is not well targeted towards addressing problematic behaviours in the industry may lead to inefficiencies and increased costs in consumer products. It may also have the perverse impact of reducing competition in the supermarket industry.

<p>Evaluation of Option 2</p>	<p>Compared to the counterfactual of no Code at all, Treasury has concluded that Option 2 could have high benefits in terms of uniform compliance across the entire supermarket industry. However, much of this benefit is likely to be offset by the disproportionate costs imposed on smaller supermarkets to meet new compliance requirements, which could undermine competition in the industry. Hence, it is unclear whether this would provide a net benefit. Moreover, it would deliver a lower net benefit than Option 3.</p> <p>Option 2 is therefore not recommended.</p>
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Option 3: remake the Code as proposed in the Final Report

This option would involve adopting all 11 recommendations of the Final Report, including making the Code mandatory with penalties, enhancing the dispute resolution provisions, and introducing new protections against retribution and for fresh produce suppliers. It also proposes amendments to provisions in the Code which allow supermarkets and suppliers to agree exceptions to supermarkets’ Code obligations.

Costs

There will be some increased compliance costs from implementing all recommendations in the Final Report. There are several new obligations for supermarkets that will raise compliance costs, as outlined in Annexure 2. However, these are largely incremental changes to existing Code obligations and are not expected to impose significant additional compliance costs. Initial estimates suggest that the incremental compliance costs total around \$485,000 annually on average over the next 10 years.¹⁰

The application of high penalties and infringement notices is likely to lead to greater compliance with the Code by supermarkets. This could potentially lead to higher compliance

⁹ ACCC, Submission to the Consultation Paper, 29 February 2024. See also evidence to the House of Representatives Standing Committee on Economics, which suggests that supermarket concentration is decreasing suppliers’ willingness to invest in long-term productivity improvements (House of Representatives Standing Committee on Economics, Better Competition, [Better Prices: Report on the inquiry into promoting economic dynamism, competition and business formation](#), March 2024, p. 182.

¹⁰ Ibid.

costs. However, all supermarkets claimed they are already complying with the Code, and most stated they have already implemented practices that are consistent with the additional protections recommended. Further, all supermarkets already have significant legal resources dedicated to compliance with the Code, meaning they are well-placed to ensure compliance with the new obligations in a low-cost manner.

There is also a risk that some of the additional costs imposed by the Code, and an improvement in bargaining power of suppliers, will increase costs for consumers. It is difficult to quantify this impact as it is unclear how much supermarkets will be able to pass through these costs. The current environment of relatively high inflation and cost-of-living pressures is likely to reduce supermarkets' ability to pass these costs on if supermarkets continue to be under scrutiny from the media, the Government and the ACCC. Offsetting this, the ability for suppliers to earn a reasonable return could actually result in lower prices over time, as discussed below.

Benefits

This option will deliver a range of benefits to suppliers by improving the operation of the Code. The proposed changes will give suppliers greater certainty and transparency in commercial dealings with supermarkets. Making the Code mandatory with heavy penalties will drive greater compliance and enforcement by the ACCC. Along with other proposed amendments, this will improve supplier trust in the Code, and their use of the Code.

For example, the dispute resolution mechanisms under the current code are highly underutilised and suppliers are unable to resolve their disputes in a timely and cost-effective manner. The preferred model seeks to increase independence, impartiality and authority in the process to give suppliers greater confidence their complaints will be resolved without fear of retribution. Potential downsides of moving to a mandatory Code have been avoided by obtaining the in-principle agreement of the current signatories to continue to offer arbitration and compensation up to \$5 million under the mandatory Code.

Changes to improve protections against retribution are important to ensure suppliers exercise their rights in respect of the Code. Improved protections for suppliers of fresh produce and to ensure supermarkets can only agree exceptions where suppliers also benefit, will also improve commercial dealings between suppliers and supermarkets.

The Review has also sought to retain commercial freedom between parties, with appropriate safeguards, as stakeholders argued that this provides benefits to both suppliers and supermarkets. The proposals will improve supplier understanding of these provisions, and any agreement to deviate from them, in a low-cost way.

Addressing the issues raised by the Review will benefit the whole grocery industry, by setting effective standards of business conduct to support healthy negotiations and dealings between the parties.

Providing suppliers with greater financial returns and stability also means suppliers have the ability to invest more in research, development and innovation. These types of investments are essential to achieving technological and efficiency improvements, which can reduce production costs, and hence, downstream prices, or lead to new types of products. This ultimately benefits consumers where suppliers can offer lower priced products and/or greater product choice or higher quality products.

Introducing meaningful penalties is also expected to drive greater compliance. As discussed under Option 1, current losses to suppliers are estimated to be between \$7 and \$64 million. Given the potentially high penalties, it is expected that these breaches would reduce significantly. Even a halving of the incidence of current breaches would offset the incremental compliance costs multiple times over.

Net Benefits

Implementing all the recommendations in the Final Report may involve some incremental cost increases for the industry but this will likely be more than offset by the improved effectiveness of the provisions and the Code’s ability to better support healthy commercial dealings in the industry.

In particular, the recommendations in the Final Report are expected to increase confidence in the Code, increase supplier understanding of their rights under the Code, increase suppliers’ willingness to exercise their rights under the Code, increase compliance, and contribute to a more effective Code that works to protect suppliers and contribute to a more sustainable and vibrant grocery industry.

Further, under Option 3 there will be greater scope for suppliers to invest more in their businesses which will be in the long-term interests of consumers.

Evaluation of Option 3	<p>Compared to the counterfactual of no Code at all, Treasury has concluded that Option 3 is likely to have high benefits in terms of improved standards of behaviour across the dominant players in the supermarket industry. It also offers a higher net benefit than the voluntary Code. The costs imposed on industry to meet new compliance requirements will be incremental and the expected benefits are likely to greatly outweigh the total compliance costs.</p> <p>Treasury recommends Option 3 as it has the highest net benefits of all the assessed options.</p>
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Annexure 1 – Assumptions Underlying Cost Calculations

Compliance cost estimates

- These have been calculated using estimates of labour and legal costs required to comply with the various obligations under the Code, including:
 - Costs of a supermarket appointed Code Arbiters/Mediators
 - External legal costs
 - In-house legal costs
 - Costs of training staff
 - Compliance with reporting requirements
 - Staff compliance with obligations.

Estimates of harm

- Incidence of harmful conduct and number of suppliers was taken from the [2022-23 Annual Report](#) of the Food and Grocery Code Independent Reviewer.
 - Incidence of harm is expressed as a percentage of suppliers that have experienced a certain type of harmful conduct in the preceding year. To be conservative, it is assumed that each supplier that indicated they had experienced a certain type of harmful conduct only experienced it once in that year.
- To determine total annual harm per supermarket, the incidence of harmful conduct for each supermarket for each form of harmful conduct (as a percentage of suppliers) was multiplied by the estimated harm from the relevant conduct (see below assumptions), multiplied by the number of suppliers for each supermarket. Total annual harm per supermarket was then summed to get total annual harm.
- For each of the 7 most frequent complaints listed in the [2022-23 Annual Report](#) of the Food and Grocery Code Independent Reviewer, estimates of harm were determined using the following assumptions.
 - Where a supplier's price negotiations were not concluded in 30 days, this was assumed to cost a supplier between \$5,000 (lower bound) and \$33,815 (upper bound) annually. It was assumed that this delays price increases by 30 days. The lower bound is a conservative estimate. The upper bound is based on an estimated average supplier's value of goods multiplied by a monthly component of CPI.
 - Where a product was delisted without reasonable notice, this was assumed to cost a supplier between \$5,000 (lower bound) and \$10,000 (upper bound) per annum. These are likely conservative estimates of harm.
 - Where a supplier was required to fund an unreasonable promotion, this was assumed to cost a supplier between \$5,000 (lower bound) and \$10,000 (upper bound) per annum. These are likely conservative estimates of harm given that promotions occur often and suppliers claimed this conduct occurs frequently.
 - Where a supermarket reduced distribution without reasonable notice, this was assumed to cost a supplier between \$5,000 (lower bound) and \$10,000 (upper bound) per annum. The supplier costs from this could be much higher though.
 - Where a supermarket delisted a product without commercial reason, this was assumed to cost a supplier between \$10,000 (lower bound) and \$100,000 (upper bound) per annum. The supplier costs from this could be much higher though.
 - Where a supermarket made a late payment, this was assumed to cost a supplier between \$5,000 (lower bound) and \$78,439 (upper bound) annually. The upper

bound estimate was based on an average 30-day delay and current interest rates. This harm is simply a transfer from the supplier to the supermarket and has not been included in the cost estimate.

- Where a supermarket made deductions that a supplier had not consented to, this was assumed to cost a supplier between \$500 (lower bound) and \$1,000 (upper bound) annually. This is likely an underestimate of actual harm to suppliers from this conduct given suppliers claim this occurs frequently. This harm is simply a transfer from the supplier to the supermarket and has not been included in the cost estimate.
- These assumptions likely underestimate the total likely harm given it only includes estimates for the 7 most frequent complaints and estimates for these are conservative. Further, it does not account for unreported harms.

Annexure 2 – New obligations recommended under the mandatory Code and their associated costs

- Requiring supermarkets to:
 - Have systems in place for their senior managers to monitor the commercial decisions made by their buying teams and category managers in respect of a supplier who has pursued a complaint through mediation or arbitration; and
 - Ensure that the incentive schemes and payments that apply to a supermarket’s buying teams and category managers are consistent with the purpose of the Code.

The estimated additional costs from this requirement are expected to be low since complaints are not frequent and two of the supermarkets already have these processes in place, though there will be some ongoing costs from these requirements.

- Requiring that all exceptions to Code obligations should be subject to a reasonableness requirement that considers the benefits, costs and risks to the supplier and the supermarket, and protects against exceptions that are not in a supplier’s interest, with the supermarket bearing the onus of proof that any exception is reasonable. This is an incremental change to the Code, which already requires exceptions to Code obligations to meet a reasonableness test. Hence, the additional costs from these measures are likely low, though ongoing costs are estimated to be moderate on the assumption that buyer teams will be spending more time satisfying these requirements.
- Requiring supermarkets to provide suppliers a simple guide to any exceptions that are included in all new grocery supply agreements. This could be done in a standardised way, which would result in low initial implementation costs and low ongoing costs.
- Requiring that grocery supply agreements for fresh produce include the basis for determining prices. There could be transitional arrangements for this requirement to manage compliance costs, but this is not anticipated to be a costly measure to implement, given it is not overly prescriptive. The compliance costs for this are likely to be low, with some minimal implementation costs and very low ongoing costs.
- Requiring supermarkets to keep records relevant to the following obligations under the Code:
 - Incentive schemes for buying teams and category managers are consistent with the purpose of the Code;
 - That systems are put in place for senior management supervision of supplier relationships where there has been a formal complaint;
 - Attaching a simple guide to all new grocery supply agreements about the Code protections that are being contracted out of in the agreement;
 - Written consent provided by a supplier to any set-off amount that is not otherwise provided for in the grocery supply agreement;
 - Documents recording systems that monitor compliance with confidential information requirements;
 - Retailers’ ranging principles and shelf space allocation principles; and
 - Documents recording staff training on the Code provided.

The first three categories of records relate to new obligations under the Code. However, the cost of record-keeping is likely to be low given the obligations are not overly prescriptive. There are likely to be upfront costs of setting up record-keeping processes.

The final four categories of records relate to existing obligations under the Code. As these requirements relate to existing obligations the cost of keeping records is expected to be low.