

Response to the Recommendations of the Legislative Assembly Economics and Industry Standing Committee Report on the Sustainability of the Dairy Industry in Western Australia

(Report No. 8 in the 36th Parliament)

This Government response has been prepared in accordance with Standing Order 277(1) of the Standing Orders of the Legislative Assembly.

Background

The Legislative Assembly Economics and Industry Standing Committee tabled the final report of its inquiry into the sustainability of the dairy industry on 4 December 2003. The Committee is to be congratulated for assembling a comprehensive overview of the complex issues facing the dairy industry within six months of having the matter referred to them by the Legislative Assembly.

The Committee identifies a number of factors that have combined to precipitate a crisis of confidence in the Western Australian dairy industry:

1. Continuing erosion of the price premium for market milk;
2. Lack of farmer market power and the perceived failure of the collective bargaining process to deliver equitable outcomes through a transparent process;
3. Ongoing adjustment issues caused by the need to rapidly adopt to an open market after decades of market milk regulation. Many businesses remain unable to compete in an unregulated marketplace;
4. Low international dairy commodity prices combined with the strengthening Australian dollar have reduced the value of Australian dairy exports by 30 per cent since September 2001. This has rendered Challenge Co-operative unable to deliver benefits that were soon or large enough to match expectations created within industry; and
5. Drought-increased grain prices leading to a substantial increase in costs of production during the 2002/2003 financial year.

The Committee correctly identifies that these problems are being experienced throughout the Australian dairy industry, and are by no means unique to Western Australia.

The Committee's report identifies three major strategies for the dairy industry to overcome these problems and build a sustainable future.

The first is for farmers to ensure that their businesses are structured to be competitive in the international and domestic marketplaces and that they have the capacity to respond to increasing competition.

The second is for retailers to recognise the added costs associated with supplying fresh milk 365 days of the year and to ensure that farmers are sufficiently well compensated for their efforts to continue to do so.

The third is for Western Australian milk processors to continue the shift away from commodity production and into high value export markets. Strong performance by a farmer-owned processor is required to ensure that premiums from those markets are shared with Western Australian dairy farmers.

The Standing Committee has highlighted the large differences in business performance that exist between Western Australian dairy farms. Some Western Australian farms are among the most efficient in the world (Finding 7) and remained profitable under the difficult conditions of 2003 (Finding 52). Others are not economically sustainable under current market circumstances (Finding 7) and need to reassess their viability (Finding 55). The report identifies large differences in milk production costs between farms (Finding 5) as well as large differences between milk prices as a result of differences in milk quality.

The State Government acknowledges that the industry continues to face difficult conditions in the domestic and international marketplace (Findings 1, 4, 17, 29, 37) and shares the Committee's view that direct intervention by Government in the dairy market is not an option in the current legislative and policy environment (Findings 22, 24, 25, 26). However the Western Australian Government will continue to assist dairy farmers to develop collaborative solutions to market issues (Finding 23) and to assist the collective bargaining process (Findings 43, 45). The State Government notes that collective bargaining has had mixed success in Western Australia. The two major corporate processors have taken very different approaches to the development of mature supply chain relationships with their suppliers. Peters and Brownes Foods have used the collective bargaining process as an opportunity to improve communication with their suppliers and to increase farmers' understanding of the processing business. Negotiations between National Foods and their suppliers have been less amicable (Finding 44).

The Committee highlights the relatively low retail prices of dairy products in Western Australia compared to other Australian states. The Western Australian Government agrees that action by retailers will be essential to improve farmer returns from the domestic milk market (Findings 16, 17, 19, 37, 38, 41). The Government will continue to seek constructive ways to engage retailers in the debate on the dairy industry's future within the constraints imposed by the *Trade Practices Act, 1974*.

The Western Australian Government holds the view that the dairy industry's future growth (and that of individual businesses) must be into high value markets (Findings 27, 29, 30, 31, 32). There can be few clearer illustrations of the importance of a high value product mix and stable market relationships than the difference in milk prices paid to suppliers of Peters and Brownes Foods and Challenge Co-operative. The State Government will continue to work with Western Australian dairy processors to identify new product and market opportunities.

The Standing Committee made 22 recommendations for Government action to enhance the sustainability of the dairy industry. A number of those recommendations relate to existing government programs or issues that can be directly addressed by State Government. Considerable progress has already been made toward the implementation of those recommendations as reported below.

Several recommendations by the Committee (Recommendations 13, 14, 15, 16,19 and 20) require the Western Australian Government to seek action from Australian Government Ministers and agencies in areas that lie outside the jurisdiction of State Government.

The Western Australian Government has acted on each recommendation by making the relevant Australian Government Minister aware of the recommendation and requesting that they take appropriate action. The State Government will work with the Australian Government wherever possible to assist their response to the Standing Committee's recommendations.

Many of the Standing Committee's most important recommendations require the participation of a range of industry stakeholders for their effective implementation. These are recommendations that require long term commitment by government and industry to seeking greater efficiency and innovation in products and markets within the Western Australian dairy sector (Recommendations 8, 10 and 12). While Government can assist these processes in many ways, it will be the actions of committed private sector players that will be most crucial to making these recommendations bear fruit.

Accordingly, it is inappropriate for the Western Australian Government to unilaterally frame detailed responses to any of this group of recommendations.

The Western Australian Minister for Agriculture, Forestry and Fisheries will invite representatives of key industry stakeholders to participate in a forum to identify those groups willing to work with the State Government and each other toward the successful implementation of these recommendations and to map the first steps toward implementation.

The Western Australian Government's responses to specific recommendations are set out below.

Recommendation 1

Federal and State Governments need to frame future industry restructuring and assistance packages so that participants are not penalised through their taxation and social security entitlements.

Issues

The Standing Committee has highlighted the fact that the method of payment of Federal and State Government restructure assistance has sometimes resulted in a reduction of social security payments to dairy farmers (Finding 10).

Government response

The Western Australian Government has noted the Standing Committee's view and will consider taxation and social security eligibility issues in the development of any future assistance packages for agricultural industries.

Recommendation 2

The Government requests the ACCC to determine whether the practice of selling dairy products in Western Australia at a substantial discount to the price in their state of manufacture constitutes dumping or anti-competitive behaviour.

Issues

The Standing Committee report has identified that interstate dairy processors commonly sell manufactured dairy products at a lower price in Western Australia than in their home state (Finding 18).

While this practice benefits Western Australian consumers, it depresses the retail price of dairy products manufactured in Western Australia. This in turn reduces the price paid to farmers for their milk. For example, the low retail price for cheese in Western Australia means that it is now more profitable for Peters and Brownes Foods to sell commodity cheese into a depressed export marketplace than to cut and pack it for local sale. As a result Brownes cheese, recently recognised as amongst the best cheddars in the world, has been delisted from Coles and Woolworths supermarkets in Western Australia.

Government response

The Western Australian Government has sought the opinion of the Australian Competition and Consumer Commission, which advises that there are no legal barriers to “dumping” products from interstate. However, such behaviour may be actionable under Section 46 of the *Trade Practices Act, 1974* if it can be demonstrated to constitute an abuse of market power. This correspondence can be found in Appendix 6 of the Standing Committee report.

The Western Australian Government will ensure that any evidence of abuse of market power actionable under Section 46 of the *Trade Practices Act, 1974* is passed to the Australian Competition and Consumer Commission for investigation.

Recommendation 3

The Government ensures that dairy products eligible for promotion through the State’s “Buy WA” campaign must use milk components derived exclusively from Western Australia, unless those components are not produced in the State.

Issues

Buy WA First requires that all products are at least 50 per cent value added within Western Australia. It does not require that all inputs used by Western Australian food processors be of Western Australian origin. However all dairy products promoted by Buy WA First are required to be made from Western Australian milk.

Correct use of the Buy WA First logo is the responsibility of suppliers and retailers and is not enforced by State legislation. However misleading use of the logo may be actionable under *the Trade Practices Act, 1974*.

Introducing a requirement to define, monitor and enforce Western Australian content limits would divert resources from the campaign’s core function of assisting and promoting industry development in Western Australia.

Government response

The Western Australian Government notes the recommendation and will continue to ensure correct use of the Buy WA First logo within its existing guidelines.

Recommendation 4

The Government ensures that food labeling requirements more adequately define the use of the word 'fresh' so that a product cannot be labeled as 'fresh' if it is made from reconstituted products.

Issues

Food Standards Australia New Zealand defines milk in Standard 2.5.1 – Milk. The standard includes minimum fat and protein requirements for milk and permits the addition of milk components to milk for retail sale in order to comply with those standards.

Other dairy products containing reconstituted milk solids are required to disclose them on the label.

False or misleading labelling of food may be actionable under the *Health Act, 1911*, the *Trade Practices Act, 1974* or state consumer protection legislation.

Government response

The Western Australian Government believes that the existing standards and legislation are adequate to protect both human health and consumer rights. No further action is proposed.

Recommendation 5

Government intervention in the dairy supply chain must adhere to the following principles:

- 1. Intervention is made on the basis of measurable industry outcomes. These must advance the industry's strategic goals, and not support the retention of inefficient or outmoded business practices; and*
- 2. Any intervention must not weaken the competitiveness of Western Australian processors in either interstate or overseas markets.*

Issues

State Government endorses the principles suggested in Recommendation 5.

Government response

Any proposed intervention by the Western Australian Government in the dairy supply chain in response to the Standing Committee's recommendations or other initiatives will be tested against the principles laid down in Recommendation 5.

Recommendation 6

The Government facilitate the farm and processing sectors to develop a more collaborative approach in order to increase their efficiency.

Issues

The Standing Committee identifies opportunities for the processing sector to increase efficiency by collaborating on infrastructure use and market and product development .

Government response

The Department of Agriculture will continue to work with dairy processors to identify opportunities for mutually beneficial collaborative projects. These activities draw on the resources of the Department's Trade and Development Division as well as a specialist Dairy Business Development Manager.

The Department of Agriculture and the Department of Industry and Resources will continue to seek new export market opportunities for Western Australian dairy products through its trade offices and hosting of international trade delegations.

The State Government will facilitate an industry forum to identify new collaborative opportunities for the Western Australian dairy industry (see Recommendation 8).

Recommendation 7

The Government initiate a research and development partnership with industry to assist dairy farmers to reduce their costs and develop strategies for change relevant to different dairy regions and farm business circumstances.

Issues

The Western Australian Government endorses the Standing Committee's view that increasing efficiencies are the key to the sustainability of the Western Australian dairy industry in both domestic and export markets (Finding 20) and that the Western Australian industry must maintain a critical mass of efficient dairy farmers so that its small production base is not further diminished (Finding 40).

The Committee also notes that the most effective contribution Government can make to a sustainable dairy industry in a competitive market will be through its scientific and trade resources to increase the participation and competitiveness of Western Australian dairy exporters (Finding 35).

Government response

The State Government currently invests \$1.5 million annually in research and development for the Western Australian dairy farm sector.

That investment will be supplemented by around \$500,000 from dairy industry research funders Dairy Australia and Western Dairy during 2003/04, clearly demonstrating the value that the dairy industry places on that work.

The Department's work currently encompasses strategies to reduce production costs through improved pasture and grazing management, opportunities to increase milk returns through higher milk quality and the implementation of best management practices to reduce the environmental impact of dairy farming.

The Department of Agriculture is working with Dairy Australia, Western Dairy and industry stakeholders to ensure that its new round of dairy research and development continues to be relevant to industry needs.

Recommendation 8

The Government convene a dairy stakeholders council to improve access to and use of processing infrastructure, and to assess options to increase flexibility of product mix in response to market opportunities.

Government response

The Western Australian Minister for Agriculture, Forestry and Fisheries will convene an industry forum of invited key stakeholders to address these issues.

Recommendation 9

The Government directs Western Power Corporation to cost 3-phase power projects to dairy customers on the basis of district infrastructure investment that anticipates further local power system upgrades by neighbours.

Government response

The Minister for Agriculture, Forestry and Fisheries notes the recommendation and has drawn it to the attention of the Minister for Energy for consideration.

Recommendation 10

The Government invites Dairy Western Australia and other industry stakeholders to participate in a feasibility study into development of a dairy transport services company.

Government response

This recommendation will be a key agenda item for the industry forum proposed under Recommendation 8.

Recommendation 11

The Government facilitates exploration of a single marketing desk as a basis for improving collective bargaining practices by dairy farmers.

Issues

The Standing Committee report highlights the weak market position of dairy farmers relative to milk processors and retailers (Findings 45, 47).

Government response

The State Government is assisting the Western Australian Farmers Federation to investigate the legal and competition issues associated with single desk marketing of milk along with other mechanisms to increase the effectiveness of collective negotiation by dairy farmers.

The Western Australian Government notes that there are widely diverging views on the merits of single desk marketing within the dairy industry. Government involvement in single desk marketing or any other form of market intervention would be dependent upon strong industry support for such action.

Any Government intervention in milk marketing would need to comply with the principles set out in Recommendation 5.

Any Government intervention in milk marketing would also need to comply with Western Australia's obligations under the National Competition Agreement.

Recommendation 12

The Government support institutional arrangements to stimulate Western Australian dairy exports, especially high value-added products. These arrangements must include:

1. *A study to clearly define Western Australia's sustainable competitive advantages and to develop a strategy and marketing plan to maintain and exploit those advantages;*
2. *Using the resources of the Government, including Western Australia's trade offices, to advance business relationships in Western Australia's existing and future dairy markets;*
3. *Facilitating industry development of an increased range of products for new and existing markets;*
4. *Conducting a feasibility study of broadening the scope of the Wine Industry Centre for Excellence to include dairy and other liquid foods; and*
5. *Increased collaboration between Western Australian exporters to improve their efficiency in servicing key markets.*

Government response

Scoping the competitive advantage study will commence at the industry forum proposed under Recommendation 8.

The Department of Agriculture and Curtin University are currently reviewing strategies to strengthen food technology research and product development in Western Australia.

The State Government will seek advice from dairy processors on how it can most effectively assist their efforts in export market and product development through the industry forum proposed under Recommendation 8.

Recommendation 13

The State Government urge the Federal Government to use part of the tax windfall created by the DSAP to provide additional assistance to rural communities adversely affected by deregulation.

Issues

The Standing Committee estimates that the Australian Government has received a \$400 million tax windfall from the Dairy Structural Adjustment Program (Finding 34).

Government response

The State Government fully supports this recommendation. The Western Australian Minister for Agriculture, Forestry and Fisheries has written to the Australian Treasurer to request his consideration of this recommendation.

Recommendation 14

The Western Australian Government request the Federal Government to direct the

ACCC to:

1. *Resume monitoring of margin distribution within the supply chain for liquid milk. This will provide some much needed transparency to milk price negotiations and bring legal and public pressure to prevent exploitation of farmers;*
2. *Determine whether the practice of negotiating milk tenders on a national basis is an unfair restriction of trade on those processors who only trade in one state; and*
3. *Provide advice on possible mechanisms for raising retail prices that increase margins through the industry chain to dairy farmers that will not be subject to prosecution under the Trade Practices Act 1974.*

Issues

The report by the Australian Competition and Consumer Commission into the impact of deregulation on the Australian milk industry concluded that the dynamics of that market had changed substantially as the result of deregulation. The Standing Committee identifies developments highlighted in that report including the growth in market share of generic milks (Finding 16) and the tendering process for supply of generic milks (Findings 17 and 37) as continuing to act against the interests of dairy farmers.

The weak market power of dairy farmers relative to processors and supermarkets is a major theme of the Standing Committee's report (Findings 11, 19, 36,41)

The Standing Committee report presents evidence that the fundamentals of margin distribution in the fresh milk supply chain have changed to the detriment of dairy farmers since the Australian Competition and Consumer Commission ceased price monitoring in December 2000 (Finding 38).

The Western Australian Government shares the Standing Committee's belief that a resumption of milk price and margin monitoring by the Australian Competition and Consumer Commission is the best mechanism to increase transparency in the fresh milk supply chain.

The Australian Competition and Consumer Commission only undertakes such monitoring at the direction of the responsible Australian Government Minister.

Government response

The Western Australian Minister for Agriculture, Forestry and Fisheries has written to the Australian Minister responsible for the Australian Competition and Consumer Commission urging that the Minister consider renewed monitoring of prices and margins within the dairy supply chain by the Australian Competition and Consumer Commission using its powers under the *Prices Surveillance Act, 1983*.

Recommendation 15

The Government request the ACCC to find ways to improve transparency in supply chain transactions and equity of participation in supply chain negotiations for market milk.

Issues

The Western Australian Government believes that monitoring of prices and margins by the Australian Competition and Consumer Commission is the most effective tool available to increase transparency in the dairy supply chain.

Government response

The Western Australian Minister for Agriculture, Forestry and Fisheries has written to the Australian Minister responsible for the Australian Competition and Consumer Commission. He has urged that the Minister consider renewed monitoring of prices and margins within the dairy supply chain by the Australian Competition and Consumer Commission using its powers under the *Prices Surveillance Act, 1983*.

Recommendation 16

The State Government request the Federal Government make changes to the Trade Practices Act 1974, particularly to make unconscionable conduct provisions more readily actionable by the ACCC.

Issues

The *Trade Practices Act, 1974* is currently undergoing review as a result of the recommendations of the Dawson Report.

Government response

The Western Australian Minister for Agriculture, Forestry and Fisheries has written to the Australian Minister responsible for the Australian Competition and Consumer Commission. He has requested information on proposed changes to the Act and an outline of how those changes are expected to increase the level of protection offered to small business.

Recommendation 17

The Government uses provisions under a Loan Bill to enable the establishment of a Section 120(1)(c) loan facility for Western Australian cooperatives.

Issues

The Western Australian Government is close to finalising arrangements for the establishment of a Section 120 loan facility for Western Australian cooperatives. This initiative will bring significant benefits to a number of Western Australian industries.

Government response

The Western Australian Government established an inter-agency Committee in 2001 to develop a proposal for a loan facility for co-operatives that qualified for income tax deductions under Section 120(1)(c) of the *Income Tax Assessment Act 1936*.

The Department of Agriculture has been driving the creation of this facility with the assistance of specialists from the Department of Treasury and Finance, the State Solicitor's Office, Treasury Corporation and other relevant organisations. The Department has been working to create a system that:

1. satisfies the requirements of the *Income Tax Assessment Act* and other State and Australian legislation;

2. has no impact on the State Government's net debt nor its net budget position;
3. is administratively cost effective; and
4. provides cooperatives with a flexible capital raising option.

The Western Australian Government strongly supports the establishment of an appropriate loan facility in principle. Legal and policy issues associated with implementation of the scheme are at an advanced stage of review.

Recommendation 18

The Government conducts an analysis of the roles of cooperatives and collective bargaining groups in increasing dairy farmer market power. This analysis must include recommendations to the ACCC on measures to increase the role and effectiveness of collective negotiation of market price.

Issues

The Australian Competition and Consumer Commission advises that the Dawson review undertook a comprehensive study of the role of collective bargaining in strengthening the market power of small businesses and that the review's recommendations will result in changes to the relevant sections of the *Trade Practices Act, 1974*.

Government response

The Department of Agriculture is working with Edith Cowan University to scope the requirements for such a study.

A contract for the conduct of the study is expected to be finalised by the end of March 2004.

The State Government is assisting the Western Australian Farmers Federation to investigate the legal and competition issues associated with single desk marketing of milk and other mechanisms to increase the effectiveness of collective negotiation by dairy farmers.

Recommendation 19

The Western Australian Government requests the Federal Government to allow dairy farmers access to Farm Help Re-establishment Grants, regardless of their DSAP entitlement, provided that they meet the standard means test.

Issues

Dairy farmers who meet the means test requirements are currently eligible for assistance under Centrelink's Farm Help program. However re-establishment grants are currently reduced by the equivalent of a dairy farmer's Dairy Structural Adjustment Program entitlements. This means that most Western Australian dairy farmers would not be eligible for any re-establishment assistance. The Standing Committee notes that DSAP payments have not always been used effectively (Finding 50), and may not be available to assist a managed exit from the industry.

Government response

The Western Australian Minister for Agriculture, Forestry and Fisheries has written to the Australian Minister for Agriculture, Forestry and Fisheries to ask for his consideration of this recommendation.

Recommendation 20

The Western Australian Government requests the Australian Government to allow dairy farmers to take their remaining DSAP entitlements as a lump sum exit payment. These payments should be recognised as redundancy payments for taxation purposes.

Government response

The Western Australian Minister for Agriculture, Forestry and Fisheries has written to the Australian Minister for Agriculture, Forestry and Fisheries to ask for his consideration of this recommendation.

Recommendation 21

The Western Australian Government make immediate application for a rural financial counselling service under the Federal Government's Short-Term Industry Adjustment Projects Scheme within the Rural Financial Counselling Service Project. The State and Federal Governments establish a long-term rural financial counselling service in southwest Western Australia to support adjustment decisions in dairy and other rural industries.

Issues

The Standing Committee reports that some farm businesses are unlikely to be viable under current market conditions (Finding 7), that some businesses did not properly assess their business position at the time of deregulation (Finding 51) and that restructure funds were not always spent wisely (Finding 50). As a result, a number of businesses now find themselves in the position of needing to reassess their viability (Finding 55).

The Western Australian Government agrees that the availability of an independent Rural Financial Counsellor in the South West would help industry to address this issue.

Applications for support under the Rural Financial Counselling Scheme must come from community groups rather than government.

Government response

The Department of Agriculture has assisted industry to complete the necessary application for Australian Government support of a Short Term Industry Adjustment Counselor with support from the Western Australian Farmers Federation.

The Western Australian Minister for Agriculture, Forestry and Fisheries has written to the relevant Australian Government Minister to express his support for the application.

Recommendation 22

The Government ensures that any unspent funds from the State Dairy Assistance Package are used to assist the further development of the dairy industry and in particular support the cost of implementing the Committee's recommendations.

Issues

The State Dairy Assistance Package was completed on 30 June 2003. There are no surplus funds available for reallocation.

The Legislative Assembly Economics and Industry Standing Committee's report on the Sustainability of the Dairy Industry in Western Australia provides a unique picture of the Western Australian industry three years on from milk market deregulation.

The report contains important information on the wide variation in farm costs, milk prices and profitability that exist in the Western Australian industry, and insight into the forces that shape domestic and export markets.

Most importantly, the report's findings and recommendations will provide guidance to the Western Australian Government in addressing future structural adjustment, industry development or market development issues for the dairy industry.