



House of Commons
Environment, Food and Rural
Affairs Committee

EU proposals for the dairy sector and the future of the dairy industry

Eighth Report of Session 2010–12

Volume II

Additional written evidence

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Environment, Food and Rural Affairs Committee

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Contacts

All correspondence should be addressed to the Clerk of the Environment, Food and Rural Affairs Committee, House of Commons, 7 Millbank, London SW1P 3JA. The telephone number for general enquiries is 020 7219 5774; the Committee's e-mail address is: efracom@parliament.uk. Media inquiries should be addressed to Hannah Pearce on 020 7219 8430.

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Written evidence

Written evidence submitted by Agriculture & Horticulture Development Board (AHDB)

POTENTIAL IMPACT OF EUROPEAN COMMISSION'S MILK PACKAGE FOR DAIRY FARMERS AND THE UK DAIRY SUPPLY CHAIN

1. The Agriculture and Horticulture Development Board (AHDB) welcome the opportunity to provide evidence to the EFRA Select committee. AHDB are an independent levy board funded through statutory levies paid by farmers, growers and in some sector's processors. We aim to improve the efficiency and competitiveness of various agriculture sectors, and cover 75% of total agricultural output, including the dairy sector across Great Britain.

2. AHDB welcome the proposals outlined by the European Commission for written contracts between milk producers and processors, and measures for enhancing transparency in the market. These proposals could help to improve market signals to producers which will help make the market work more efficiently. The rest of this submission is written in the context of actions that could help improve the efficiency of the supply chain and provision of clear market signals to achieve the optimal outcome for all parts of the supply chain.

3. Whilst the use of written contracts between producer and processor is already common place in the UK there is much debate in the industry about whether these contracts hinder the market from operating efficiently. The European Commission proposals could address this issue by ensuring certain common elements are included within contracts.

4. The Milk Development Council, a predecessor body of AHDB, published a report on raw milk contracts back in 2005. This report highlighted a number of problems with raw milk contracts which resulted in poor market signals being sent to farmers. The report suggested that contracts could be improved in a number of areas, which could result in a more efficient and profitable outlook for both producers and processors. In the five years since publication some of the suggestions have been adopted, or partially adopted, but the key issue of pricing and notice periods remain. In the remainder of this document we highlight these issues in more depth.

5. Firstly, the vast majority of contracts do not have clear pricing. Few contracts at producer level look at market indicators when setting the price. Most contracts have a base price that can be moved up or down as the milk buyer wishes. One of the few exceptions to this is the Tesco's contract, which bases prices on costs of production related data. Without a transparent system such as this milk prices can be a cause of conflict between producers and milk buyers. Sometimes deliberate confusion on milk pricing can be created by either side of the industry in order to gain commercial advantage. The relevant market signals for milk pricing are often changed eg sometimes it is milk supply, other times it is return for dairy commodities or even wider market conditions. There is often no clear or consistent agreement on what is important in pricing milk with both sides of the industry trying to gain advantage.

6. Secondly, those buying milk are able to change price at short notice, or even retrospectively without the option of a farmer stopping supplying milk to that buyer. Although there are some contracts where farmers have a three month notice period, such as Robert Wiseman Dairies and the Caledonian Cheese Company, a 12 month notice period is more common. Some buyers even specify specific dates on which people are able to hand in their resignation which mean that it could take as long as 18 months for a farmer to leave their milk buyer. This means that farmers have a weak negotiating position and leads to decisions being imposed on farmers, restricting collaboration in the supply chain. If contracts were set up so that price changes had to be mutually agreed, farmers (and processors) would have the option to end the contract (with an appropriate notice period) if changes are not agreed, and could divert some or all of their milk to another buyer. This would give a more equal partnership between farmers and milk buyers, and make it more likely that farmer representatives would be consulted before processors changed their prices or re-tendered for a supermarket contract.

7. Final, many contracts do not specify milk volumes. Most contracts supplying the liquid milk market will incentivise farmers to produce a level supply by paying more for milk produced during the seasonal trough. However, many contracts do not specify the monthly volume of milk to be produced and this reduces the predictability of supply for processors. Processors suffer as they have a more difficult job managing their plants because they do not know how much milk will be produced and cannot plan properly. Specifying volumes within agreed tolerances would allow clear market signals to be passed back to farmers.

8. The European Commission proposals will be of greatest benefit to the UK dairy industry if they instigate change in the areas outlined without dictating a one size fits all approach. For example the mechanisms for setting prices within a milk for cheese contract could be very different to that within a liquid milk contract. Contracts could specify prices in different ways such as:

- (a) xxppl for the next six months.
- (b) Price formula of AMPE (Actual Milk Price Equivalent)¹ indefinitely.

¹ AMPE calculates the value of a litre of milk at the factory gate if it is turned in to butter and skimmed milk powder at the prevailing prices for those products and allows for the processors costs.

(c) Price formula of MCVE (Milk for Cheese Value Equivalent)² +2ppl indefinitely.

9. The exact details of contracts should vary depending on different circumstances, and it should be left to commercial organisations to decide this. However, key principles should be addressed in contracts, such that that prices should be agreed, and producers should be able to easily and relatively quickly move to another buyer if this isn't the case. This would aid clear market signals and an effective supply chain.

March 2011

Written evidence submitted by NFU Scotland

SUMMARY

- Last year the EU's High Level Working Group on dairy concluded that producers are exposed to unreasonable risk compared with processors and retailers resulting in producers receiving a poor return from the dairy supply chain.
- NFUS believes we must introduce compulsory contracts that are fit for purpose between producers and processors. If the EU Commission allows Member States flexibility, the UK should take the compulsory route, or allow producers to demand a contract.
- Dairy producers must have the ability to form Producer Groups of the scale to allow sufficient negotiating powers to realise effective contracts, include pricing mechanisms that react to the real market, are transparent and reasonable to buyers and sellers.
- An adjudicator must be installed to investigate proactively any abuse of power which undermines the short- and long-term sustainability of the dairy supply chain.
- With effective contracts, a more ambitious processing sector and realistic controls on retailers, the dairy sector will thrive, reducing the reliance on imports and improving our food security. If this opportunity is missed the current decline in milk production is inevitable.

SUBMISSION

EU High Level Group

1. The serious decline in the price paid by milk processors to European dairy farmers in 2008–09 led to a crisis in the European dairy sector. The EU Commission initiated a High Level Experts Group (HLG) to investigate the issues and recommend solutions.

2. The HLG was very clear that producers were exposed to unreasonable risk compared with processors and retailers resulting in producers receiving a poor return from the dairy supply chain. They concluded that there was an urgent need for greatly improved contractual arrangements between producers and processors and that this was only possible if producers could increase their negotiating position.

3. The subsequent Commission proposals recommended that current competition law was inadequate and measures were required to rebalance the bargaining position in the supply chain and improve contractual relationships. They proposed that contracts must include four fundamental issues, namely price, volume, seasonality of delivery and contract length.

4. On Competition law the Commission is critical of the notion of "the relevant market" which they believe is not defined, can only be judged retrospectively on a case by case basis and lacks certainty. The proposal is that producers should legally be able to form Producer Groups up to 3.5% of EU production or 33% of Member State production.

Scottish and UK Situation

5. Twenty years ago there were more than 5,000 dairy farms in Scotland. Today there are fewer than 1,100. The decline is not due to poor efficiency; a recent study undertaken by ADAS and SAC concluded that Scottish dairy farmers were amongst the most efficient in Europe and have one of the highest average EU herd sizes, with major levels of restructuring.

6. In 2009 milk production in the UK fell below 13 billion litres, the lowest level of production since 1971. This is in the context of a buoyant global dairy sector, with global prices historically high and likely to benefit from a growing and more affluent world population. Responding to this opportunity, world dairy production has risen by 20% in the past decade; the EU has increased production by 4%, while the UK has reduced production by 10%.

7. Yet, the UK imports around 40% of its dairy requirements; this equates to roughly 5–6 billion litres of milk, a trade deficit of around £1.3 billion. UK dairy farmers can produce a substantial amount of this milk, if they are given the incentive.

² MCVE calculates the value of a litre of milk at the factory gate if it is turned in to mild cheddar, whey powder and whey butter at the prevailing prices for those products and allows for the processors costs

8. In the past year world dairy prices have increased dramatically. The value of the most commonly traded products of powder, butter and cheese are historically high, and it is generally accepted that these values will become the norm. In Europe and New Zealand producers have benefited from the real market drivers with substantial price increases now reaching over 30ppl. In the UK, price rises to producers have been much slower and much less significant, with producers only recently achieving prices up to an average of 26ppl. The cost of producing a litre of milk is now on average 30ppl. It is more important, however, that producers receive a price that truly reflects the value of their product as indicated by the markets, rather than a price that is simply higher than the cost of production.

9. The reasons for this situation are also clear. The UK market does not react to global market indicators quickly or accurately enough. The current structure of power and competition within the UK supply chain is only possible because of the inability of producers to negotiate reasonable contracts which reflect the true value of dairy products. In broad terms, the balance of power between and within the broad retail and processor sector has driven farmgate prices below their true value and below the cost of production.

10. The retail sector recognises the value of dairy products to attract customers into their stores. Constant and excessive discounting is used to compete to offer the lowest prices. Processors are unable or unwilling to withstand the pressure to reduce prices to the big retailers, as even the biggest processors cannot afford to lose volume sales of the scale controlled by retailers. In turn, processors big and small are offering unrealistically low prices just to retain their market share, but at unrealistic margins. They can do this as long as producers have no effective contracts or sufficient bargaining power to negotiate fair and reasonable terms and conditions.

11. DairyCo figures confirm that the retail sector retained 44% of the liquid margin in 2010 compared to 7.8% in 2000, and as much as 51% of the cheese margin in 2010 compared with 34% in 2000. The retail sector has sufficient margin to allow a fairer distribution of the end value without consumers paying more.

12. The UK processing industry is underpinned by low producer prices, which they control. There is huge potential for processors to access more of the UK market and there are clearly growing opportunities to export more dairy produce, as added value product and as commodity. UK commodity market indicators indicate the value of powder, butter and commodity cheese products are over 32ppl. Currently, UK processors produce small percentages of these products, preferring to produce liquid milk and mature cheese, but due to the dysfunctional UK market these are realising lower values. Processors lack ambition as, although they are unable or unwilling to demand fairer prices from retailers, they can manage margins through cost control, largely raw milk. UK processors have paid the lowest prices for the vast majority of the past decade compared to Europe. In recent years they have also benefited from a very favourable exchange rate, and yet our balance of trade deficit continues to accelerate.

Proposed solutions

13. NFU Scotland's position is clear:

- We must introduce compulsory contracts that are fit for purpose between producers and processors. If the EU Commission allows Member States flexibility, the UK should take the compulsory route or allow producers to demand a contract.
- Dairy producers must have the ability to form Producer Groups of the scale to allow sufficient negotiating powers to realise effective contracts that include pricing mechanisms that react to the real market, are transparent and reasonable to buyers and sellers.
- An adjudicator must be installed to investigate proactively any abuse of power which undermines the short- and long-term sustainability of the dairy supply chain.
- With effective contracts, a more ambitious processing sector and realistic controls on retailers, the dairy sector will thrive, reducing the reliance on imports and improving our food security. If this opportunity is missed the current decline in milk production is inevitable.

March 2011

Supplementary written evidence submitted by NFU Scotland

NFU Scotland welcomes the opportunity to provide further written evidence to members of the House of Commons Environment, Food and Rural Affairs Committee as part of its inquiry into the UK dairy industry.

Written evidence was previously provided in March.

Attached is further evidence for consideration. It is in regard to an initiative instigated by a group of influential dairy farmers, facilitated by NFU Scotland, that proposes a new pricing formula for inclusion in contracts between dairy farmers and their milk purchasers.

DAIRY REPRESENTATIVE GROUP PROPOSAL

Summary

The group believes it has a proposal that could fundamentally alter the dynamics of the UK milk market. It would break the cycle of market failure and allow all producers, irrespective of their supply relationship, to move forward with confidence and greater certainty.

The proposal has been developed involving representatives from every major milk supply relationship in Scotland, as well as technical and legal experts. The proposal rests on **a new, transparent and market-related pricing formula** that it believes must be incorporated into producer contracts.

With valuable assistance from industry partners—in particular DairyCo—the following formula of 20% AMPE (Actual Milk Price Equivalent) + 80% MCVE (Milk for Cheese Value Equivalent) is seen as a fair and reasonable starting point to set a foundation for contracts. It recognises that the market for milk and dairy products will move up and down, and, crucially, it is driven by market fundamentals and not the manipulation of markets by one or more powerful players in the supply chain.

Background

In September 2010, NFUS held a meeting for Scotland's dairy representatives, including producer representatives and members of the NFUS milk committee.

The initiative was motivated by:

- The need to fundamentally address the ongoing and increasingly evident problems within the dairy supply chain, which continue to severely inhibit any confidence and long term future for dairy farmers.
- The work of the E.U. High Level Group on dairy, which was clearly pointing to the need for fundamental changes in the dairy supply chain, with strong indications that contracts, pricing mechanisms and producer negotiation powers would be addressed.
- The clear need for producers to overcome their fundamental weakness, which is the lack of unity. Working together on a common strategy to increase leverage would allow more meaningful, constructive influence by producers on the dairy supply chain.
- The fear that the Scottish dairy sectors is in danger of missing the predicted opportunities in a growing global dairy market. Competing dairy producing regions in Europe and globally are planning major investment strategies, in anticipation of growing markets and increased dairy commodity prices. The UK dairy supply chain needs to motivate producers to produce milk and processors to innovate and market dairy products to be a position to compete.

Fundamentally, the purpose of the initiative was to move the whole debate beyond the same rhetoric and action that has dominated milk politics for over a decade. It was to investigate constructive solutions which could move the whole industry beyond simply analysing the problem and to focussing on trying to fix it.

Why focus on a price formula?

At its first meeting, the group highlighted a number of issues but decided upon four as top priorities:

- Ensuring effective implementation of the supermarket adjudicator.
- Creating a long-term strategy for a sustainable dairy industry.
- Working within Europe to effect change and increase our influence.
- Increase our negotiating power.

A group leader was identified for each of these workstreams. At subsequent meetings of these group leaders, the workstream was focussed even more tightly to maximise the use of resources and to gain maximum impact.

It was clear that lobbying by NFU Scotland for an effective adjudicator is in hand, so the group agreed to prioritise a strategy that could fundamentally change the dairy sector for the better.

Recognising that contracts and pricing mechanisms were implicit in ongoing EU developments, so too initiatives to improve producers' bargaining position, **discussion centred on a single initiative that could lead to the kind of step-change so desperately required. So work began on developing a pricing mechanism.**

We believed that a new pricing mechanism had to be:

- compatible with competition law;
- effective;
- transparent and independently verifiable;
- market driven;
- fair to all parties;

- seen as an opportunity not a threat by the whole supply chain; and
- able to gain acceptance by producers; who would be key in driving its adoption.

THE PRICING FORMULA

With valuable assistance from industry partners—in particular DairyCo—a great deal of research and analysis of historic data was used to investigate potential pricing formulas. The objective was to devise a formula, which reacted to true objective market indicators, using figures that were transparent and could not be subject to manipulation.

The result of this work was the following formula, based on existing market, of 20% AMPE (Actual Milk Price Equivalent) + 80% MCVE (Milk for Cheese Value Equivalent). The working group believes that this is a fair and reasonable starting point to set a foundation for the market which will move up and down, but driven by market fundamentals, not the manipulation of fair markets by one or more powerful players in the supply chain.

Why use AMPE and MCVE—and in those proportions?

The group arrived at this based on the following:

- AMPE (Actual Milk Price Equivalent) is calculated from Butter and Skimmed Milk Powder (SMP) wholesale prices, MCVE (Milk for Cheese Value Equivalent) is calculated using wholesale mild cheddar and cheese by product wholesale prices.
- Globally, SMP, butter and mild cheese are the most commonly traded milk products. They are very responsive to market trends and hence a credible barometer of the real dairy market. They are also regarded as lower value commodity products, therefore ideal to track market trends and set a floor in the market.
- Independent specialists objectively collect the prices used in AMPE and MCVE; they are current being based on spot prices and difficult to manipulate. The values also factor in processing costs and a profit margin. Looking forward the values may also be available from official figures, which are required to be reported to Government, giving even more credibility.
- The Butter and Powder production in the UK is about 10%, cheese (mostly mature and a lesser amount of mild) about 27%, liquid milk accounts for 53%. Justification of the formula's utilisation of SMP, butter and mild cheddar is on two counts.
 - First liquid and mature cheese are added value products which should command a higher price, therefore using our formula as a market tracker to a foundation for contracts is sound.
 - Second, from researching historic figures, the price of liquid milk tracks cheese prices. In simple terms if the cheese market is struggling, less milk goes into cheese manufacture, which is freed up and depresses the liquid sector. When the cheese market is strong more milk goes into cheese manufacture, tightening milk supply, forcing liquid prices up.
- Our current market structure does not encourage milk to be diverted into powder or butter manufacture even when there is a significant price advantage, neither is there a significant effort to add value to gain market share in the lucrative UK market 40% of which is supplied by imports.
- Why 20% AMPE and 80% MCVE? The modelling initially favoured MCVE with a downward adjustment to acknowledge reasonable processor margin. Cheese is a more obvious product, as more is processed in the UK (27%, although as previously stated most is mature) and the MCVE 'graph' is less volatile. However the Group felt that although butter and powder represent only about 10% of the UK market, and AMPE was more volatile, it was reasonable to accept that these commodities did have a significant effect on the market and in influencing the value of raw milk.
- Analysing data over a number of years confirms that our proposed formula has tracked farm gate, cheese and liquid prices closely, but for the most part at a premium of 2–3ppl (see graph below), and currently as much as 6ppl! It is also important to understand that the formula will track the real market for commodity milk products and it is not unreasonable to suggest that added value should generate a premium.
- Analysis of historic figures demonstrates that UK farm gate prices do not follow global trends quickly or accurately enough. There is an argument that our liquid sector buffers the UK from some of the volatility in the global market, which are driven by milk powder, butter products and commodity cheese, but this argument is becoming increasingly difficult to justify.
- Prices paid to EU producers, more exposed to world commodity markets, over the last 10 years have been higher than the UK for all but a few months. AMPE values over the last 10-year periods have been above farm gate price for around 63% of the time and below 37% of the period. Over the last five years 70/30. In other words, producer prices have reacted slowly when global markets have risen and quickly when they have fallen.

How does the formula fit with costs of production?

It doesn't directly. The formula we propose is based on market forces, not costs of production. This was debated at length and the reasons for this approach were as follows:

- It is impossible to argue that producers should be denied the “going market rate” for selling their milk.
- It is likely to be more acceptable to other stakeholders in the supply chain.
- It would ensure that farmers in Great Britain received similar prices as their counterparts in the rest of Europe; having lagged their prices for years.
- It is ultimately producers' responsibility to manage their costs to ensure that the market price allows them to cover costs and reinvest. Where there are specific costs associated by supply chain demands, they must be negotiated beyond the price produced by the formula.
- An average cost of production cannot account for the wide range of systems and regions. It also has the effect of capping the farm gate price, even when market indicators are very positive. Why should farmgate prices be capped around cost of production levels?
- Looking at the modelling of our proposed formula, the trends in terms of pricing and costs do mirror each other. In other words, when input costs are rising AMPE and MCVE tend to in sympathy. There is a lag, but at a global level the market functions effectively by reacting to rises in costs. This is often because these rises have a direct influence on production levels, with supply and demand dynamics then at play.
- The group is open to further refinement, eg a cost tracker that could indicate where extreme cost variations could instigate a force majeure taking effect.

What about competition law?

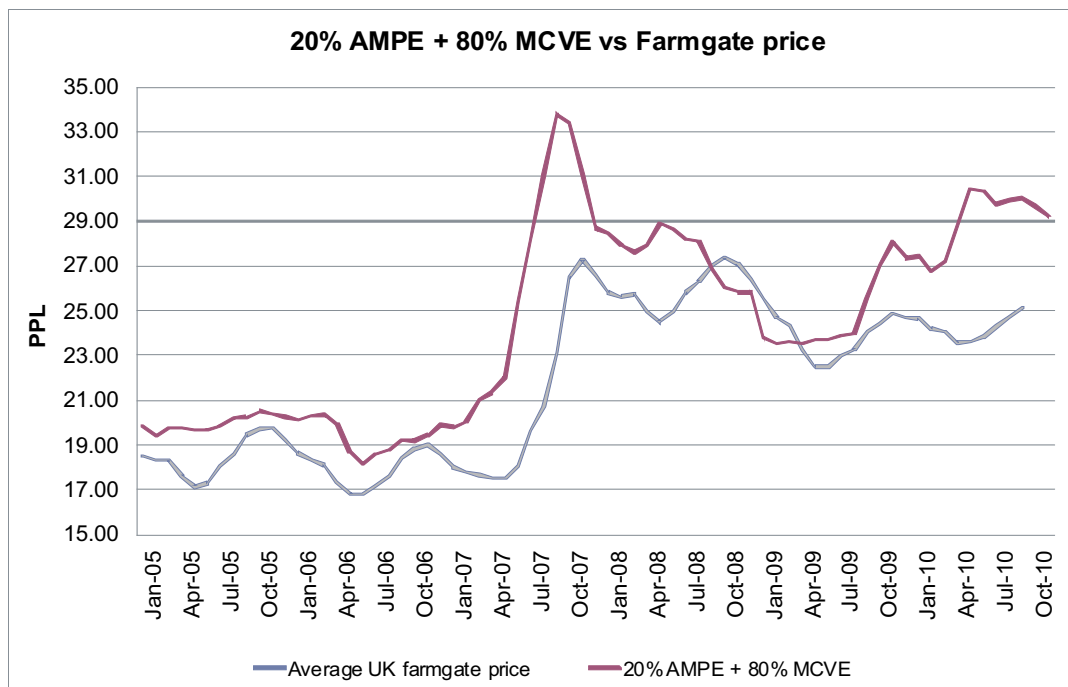
- This was a key initial focus and remains so, given the complexity of competition law.
- However, initial discussions with NFUS lawyers have given us confidence to progress, albeit with care to ensure laudable aspirations remain compatible with the latest interpretation of competition law.
- From the best of our advice, the formula does not appear to be anti-competitive, nor do we see how could it be construed as price fixing/collusion/coercion. Our proposal is that this formula should simply calculate a foundation (subject to pre agreed minimum standards) for the price within a producer's milk contract. The market, not producers, processors or retailers will set this figure.
- Ultimately, no one is (nor can be) forced to adopt the formula, neither farmer, processor nor retailer; we support it because we believe it would create greater trust, confidence and transparency in a supply chain that has lacked all these attributes in recent years. Crucially, this would be a significant step forward in terms of consumer interests; securing ongoing product choice and innovation.
- We believe processors and their supplying farmers will still set their own incentive systems to motivate producers to produce the quantity, quality or to the standards required in specific market circumstances. For example, dedicated aligned producers supplying retailers via liquid milk processors would still be required to fulfil the level profile, adhere to the added protocols of the retailer, and crucially could retain the increased price incentive. Where a processor benefits from particular milk quality then an incentive would still be appropriate.
- This paper has been produced based on our best understanding of competition law. It is designed to provide information to our members and the supply chain so they can make an informed choice on the future direction of the industry.

PROMOTING DEBATE ON THIS PRICING FORMULA

- NFUS believe that we can gain support from UK representative organisations to move this proposal forward.
- The dairy representative group, supported by NFUS, will devote resource to a managed communications plan, ensuring the proposal gains wider industry support and, crucially, buy-in from other links in the supply chain.
- NFUS is fully supportive of the objectives and proposals of the EU HLG, now supported by the Commission—we view this as pre-empting the very issues being developed at an EU level ie strong contracts, transparency and clear pricing mechanisms. We are, however, keen to promote the benefits of all contracts between farmers and processors including a price formula along the lines we propose. If this can be achieved in advance of any new legislation, then this would be a significant achievement by the UK dairy sector.

- If the supply chain fails to react positively to our initiative then we will embrace all the proposals—and potential new regulations—emerging from Europe which may facilitate the introduction of the initiative in any event.

April 2011



Written evidence submitted by Ulster Farmers' Union

The Ulster Farmers' Union represents 12,000 farming families in Northern Ireland. Northern Ireland is the second largest milk producing region in the UK with 1.9 billion litres produced per year. Our industry is in a unique position since we export 85% of the milk we produce and on account of this product mix, we have differing exposures to those in GB.

In terms of the proposed EU legislation, we submitted our views to the High Level Group at all stages of the process, from the very beginning to the most recent consultations, through DARD, Defra and directly through COPA. Most recently we met with European Parliament Rapporteur Jim Nicholson and submitted our views on the report.

CONTRACTS

1. From the outset, the UFU have called for a soft-touch and non legislative approach to contracts as applied here in Northern Ireland. Statutory contracts would not be welcomed by our membership. Contracts are essentially already in place, with producers unable to switch between suppliers on the one hand and guaranteeing continuity of collection and supply on the other.
2. The NI Dairy Industry is dominated by co-operatives and farmers sit on the Boards of the main processors. The type of Contract which were being prescribed by the HLG would have favoured producers who supply multiple processors, and we stated that this would not be an issue in Northern Ireland with farms putting into only one processor.
3. Our unique Product Mix should be taken into consideration.
4. We are the only region in the UK which has an auction system and this determining price for a large percentage of our farmers. This will have knock-on effects to any possible contracts.
5. The Commission proposed a "non-paper" on the application of the proposals to different types of co-operatives and the UFU welcomes this.

In summary, the UFU welcomes Defra's agreement that Member States should be free to choose whether to or not make contracts compulsory and the voluntary establishment of recognized producer organizations. The UFU calls for Defra to adopt this stance and to be applied regionally.

BARGAINING POWER AND TRANSPARENCY

6. Producer-processor-retailer supply chain—within the report recognition is made that the producer processor-retailer supply chain is not functioning correctly. Moves to address each area are a step towards dealing with the producer-processor part, but the UFU expressed disappointment that retailer side is lacking.

7. On 8 February during the debate in the European Parliament, Jim Nicholson MEP (High Level Group Rapporteur) said that the EU must “push processors and producers to take responsibility, but retailers need to take responsibility—they need to be controlled.”

8. Since late last year, the UFU have been holding meetings with all major retailers. We have cited the rapid rise in input costs and the impact upon on-farm production costs and the effect of non-functioning retailer returns. As stated in the opening paragraph, as 85% of the milk we produce is exported, NI farmers should be reaping the rewards of a booming commodity market. Yes despite this, the majority of our farmers are only breaking even.

9. In mid-2009, the retailers made it clear that the then poor milk price was the result of amongst other reasons, a depressed commodity market. Furthermore, the UN Food and Agriculture Organisation (FAO) confirmed last week that Global dairy prices leapt up more than any other group of food commodities in January.

10. This problem is not unique to NI and GB and should be reflected in the HLG Report. We stressed this in our input to the report compilation under a heading of calling for a supermarket adjudicator, but I feel that we draw more attention to it through the HLG report. The UFU believes that Contracts alone will not deliver the amount of transparency which is required. An amendment should be made to specifically refer to retail margins within the malfunctioning supply chain. Perhaps calling for greater transparency on retailer margins is a suggestion.

SOFT LANDING REPORT

11. In 2008, when the transition to the abolition of quota and associated soft landing was discussed, the UFU were quoted as calling for the transition period to be properly managed, and done so in accordance with prevailing market conditions. Therefore, the Commission’s proposal to consider the use of further tools to stabilize the markets in the event of serious imbalances would be in line with our own policy.

PRODUCTION POST-2015

12. The UFU has concerns about the Republic of Ireland drive to increase milk production by 2020 by 50%, set out in the recent document Harvest 2020. Should contracts be used to control volumes in one member state and not in another, this could create a lack of uniformity which could impact upon NI in terms of competitiveness. With NI being the only UK region having a land border with another Member State, we could be at a competitive disadvantage.

March 2011

Written evidence submitted by the British Retail Consortium (BRC)

1.0 INTRODUCTION

1.1 The British Retail Consortium (BRC) is the trade association of the retail sector and is the authoritative voice of the industry to policy makers and to the media. The BRC brings together the whole range of retailers across the UK, from independents to large multiples and department stores, selling a wide selection of products through centre of town, out of town, rural and online stores.

1.2 Our membership includes all the major food retailers, who between them account for over 90% of the UK’s grocery sales. We are therefore at the forefront of discussions regarding the future of food policy, the way in which consumers buy and consume food and the way in which goods are sourced, packaged and sold in UK stores.

2.0 RETAILERS AND THE UK DAIRY MARKET

2.1 Although dairy sales are important part to supermarkets, UK retailers are not the only buyers in the market. Approximately half the milk produced in the UK is used as liquid milk, most of that will be sold in supermarkets and convenience stores but a significant proportion, over 20% will be used in hospitality and catering or sold through doorstep deliveries. The remaining half of milk produced in the UK is used for manufacturing for butter, cheese, yoghurt and skimmed milk powder. Again retailers will sell a proportion of butter, cheese and yoghurt through their own brands but a part will be used for manufactures’ brands in further processing and in catering and hospitality.

2.2 It is clear from the above that whilst retailers’ position in the UK dairy market is important they are not the only buyer and not the only ones who will influence the profitability of the sector. Many of the dairy

products are globally tradable commodities and the price is determined outside the UK market. It is interesting to note these factors were cited as key to the high levels of profitability in 2008–09 but not in the current projections for this year.

2.3 The impact of retailers on the dairy sector's profitability is best demonstrated through their dedicated supply chains. A number of major retailers have established these to obtain supplies of liquid milk, working with groups of farmers. These have proved extremely effective for both farmers and retailers, providing security and predictability for both parties. The security of these arrangements helps farmers plan and invest for the future. Dairy industry data shows farmers in these chains are receiving the highest milk payments but this in itself is not enough to help the whole of the dairy sector as only a part of the UK's milk production is required to supply retailers

3.0 PROPOSALS FOR WRITTEN CONTRACTS

3.1 It is important to stress that individual dairy farmers do not have contracts with retailers as they are not direct suppliers to them. Where retailers have set up dedicated supply chains the direct relationship is between the dairy and the retailer although the retailer will agree standard terms with the dairy that must be included in the contract between them and the farmer.

3.2 Having said that, aside from the logistical issue of dairy contracts, retailers generally support the use of written contracts. They reinforce certainty in supply arrangements and help manage volatility.

3.3 Those retailers covered by the Groceries Supply Code of Practice (GSCOP) are already under an obligation to ensure that all terms of any agreement with a supplier are recorded in writing. GSCOP also imposes a number of contractual requirements on retailers, including notice of variation of contracts, provision of information to suppliers and the right to independent arbitration if disputes cannot be resolved with the retailer.

3.4 GSCOP was written to address concerns which had been raised in the Competition Commission's inquiry into the grocery sector. GSCOP has been operating for a year and feedback from our members is that there have been very few problems. Where issues have been resolved with the retailer's compliance officer they have been dealt with without the need to refer them to arbitration.

3.5 The dedicated supply chain contracts with dairy farmers, negotiated through the dairies, are transparent. It is clear to the farmer what is required in terms of supply and methods of production. The price the farmer receives for his milk is clear as is the review mechanism. Transparency is also demonstrated in the dairy industry figures published for milk prices to farmers which show retailers pay the top prices in the market.

4.0 FUTURE FOR THE UK DAIRY INDUSTRY

4.1 We are not in a position to comment on the impact of phasing out production quotas but the overall prognosis for UK dairy farmers is positive. An increasing, more affluent global population will drive an increased demand for dairy products. The UK has an advanced, efficient dairy sector that is well placed to meet increasing global demand.

4.2 Retailers recognise that securing long term, sustainable UK supply chains requires appropriate investment and certainty. They are providing this by working closely with groups of producers, most notably in dedicated supply chains. We have provided practical examples in the attached document, partners in the supply chain.

4.3 Closer supply chain working ensures milk is produced in a manner that meets consumers' requirements in terms of animal welfare, sustainability and environmental criteria. Farmers receive a good price for their milk to allow them to invest in their farm and the assurance of working with a reliable customer.

4.4 Retailers are continuing to see what more they can do to support the UK dairy sector, through arrangements for cheese and other product supplies. They also continue to promote UK produce through the Assured Food Standard and clear information on country of origin. Retailers are currently the only companies that are committed to the industry principles on country of origin labelling agreed with the Minister of State at the end of 2010.

4.5 These measures reinforce retailers' long term support for the UK dairy industry. It would help dairy farmers if other parts of the food sector were as clear in their sourcing policy and support for UK production. That aside the UK dairy industry is well placed to compete in the market and whilst there is likely to be further consolidation the future for the dairy sector is positive.

Written evidence submitted by the Food and Drink Federation (FDF)

I am writing in response to EFRA Select Committee's inquiry on EU proposals for the dairy industry. The UK food and drink manufacturing industry is a committed customer of UK farmers, purchasing around two-thirds of the country's agricultural production.

The Food and Drink Federation (FDF) supports the gradual phasing-out of dairy production quotas to ensure greater competitiveness in the sector. We are therefore pleased to see the European Commission's report on the dairy market situation concludes that there is no reason to revisit this decision.

In that context it should be noted that shortages of skimmed milk powder, butter, butter oil and other dairy ingredients continue to arise. During the last 18 months, suppliers have at times struggled to fulfil contracted deliveries, with adverse consequences for the competitiveness of UK food and drink manufacturers who need access to adequate supplies of raw materials that are safe, of high quality and are competitively priced.

FDF members recognise that the dairy industry is going through a transitional period. But at the same time there is an urgent need for improved public data on the dairy sector comparable to the USDA system with greater transparency regarding production, processed products, public and private stocks and consumption. This would help to mitigate speculation which results in market volatility, improving the competitiveness of the dairy sector and ensuring greater security of supply.

March 2011

Written evidence submitted by Asda Dairy Link

POINTS TO NOTE

- The Asda DairyLink scheme was launched in 2004. We were the **first major supermarket to establish a dedicated and segregated liquid supply of milk**. The 256 DairyLink farms only supply Asda, through our milk processor Arla.
- Our dairy farmers are paid a 1.75p per litre premium above the Arla standard price. This equates to **an extra £21,000 per year for the average Asda DairyLink farmer**. We currently pay 27.75p per litre to our dairy farmers.
- To date the scheme has produced almost four billion pints of milk and paid out more than **£15 million in milk premiums** to the dedicated dairy farmers.

SUPPORTING BEST PRACTICE IN THE DAIRY INDUSTRY

- In 2007 we piloted DairyLink "best practice" meetings to bring farmers together to discuss their businesses and the dairy sector. Following positive feedback, the project was extended across the UK. Best practice is shared and attendees are invited to discuss any issues they are encountering on their farms and any successes they are having. It is also an opportunity for the farmers to feedback on what they need from Asda.
- DairyLink farmers have access to expert advice sessions about practical issues affecting their work. For example, we have offered courses on the prevention of lameness, a serious animal welfare issue. Participating farmers have seen a reduction in incidences of lameness amongst their animals.
- We run the annual DairyLink Farmer of the Year competition to recognise the farmers who have really developed and invested in their business. The 2010-winner was Adam Ball of The Spod farm in Alton, Staffordshire. Over the last five years Adam has increased the number of cows, doubled the farm's acreage and increased profits sevenfold.
- In 2008 the Asda Dairy Link scheme received the "Innovation Award" at the **RSPCA Good Business Awards**. This was in recognition of the broad range of innovative but practical and business-focussed initiatives within the scheme to improve the welfare of dairy cows.

April 2011

Written evidence submitted by First Milk

First Milk welcomes the opportunity to respond to this Inquiry and are happy to provide additional information as requested.

In addition to the information supplied in this Memorandum, we have supplied an Appendix, which covers a backgrounder on First Milk.

In summary, our views on the Dairy Package are:

MILK CONTRACTS

A. Member states can make the use of formal written contracts compulsory. Although, contracts will remain voluntary at EU level. Co-operatives will be exempt from any requirement for compulsory contracts at a member state level

1. We have written contracts with our farmer members and producers on milk supply contracts and would support the establishment of arrangements, which would see the requirement for contractual arrangements between dairy farmers and processors across the EU.

B. Where a member state decides that every delivery of raw milk between a farmer and processor shall be covered by a written contract, that contract will fulfil the following conditions:

- The **price payable**, which will be static and set out in the contract OR vary only on factors that are set out in the contract (ie a formula or linked to specified market indicators).
- **Volume** which may, or shall be delivered and timing of deliveries.
- **Duration** of the contract, with **termination** clauses.

2. Our pricing structure is aimed at providing transparency, reflecting market returns and providing a flexible range of offerings.

3. From 1 April 2010, we have had a Market Related Pricing mechanism in place which splits our farmer members into three separate milk pools based on “end use” for milk—liquid, cheese and balancing (milk can be sent to liquid or cheese customers) pools. Previously all market returns were added together, with all members receiving the same standard litre price each month.

4. The objective of Market Related Pricing is to enable greater transparency, with members now paid the market price their milk achieves net of the costs directly associated to serving a specific customer or customers.

5. As market returns increase/decrease, the price paid to members supplying that market changes accordingly. Pool price levels and return on investments (related to previous acquisitions that were part-funded by member capital retentions) are agreed by our main Board where farmer directors are in the majority.

6. In April 2011 we launched an “International Contract” for non-members that has full transparency. A price tracker mechanism is linked to market returns for Skimmed Milk Powder and butter and based on quoted Dutch prices for both of these products.

7. In order to facilitate this contract, we set up a partnership with Eilers & Wheeler (E&W), an established international supplier of dairy products, to buy milk and process into butter and powder to sell on the world market. E&W purchase the milk from farmers and sell the product, while First Milk manages producer contracts and toll processes the milk.

8. Producers have a lifetime membership of First Milk unless they breach our rules. While our standard resignation notice period is twelve months, members can provide six months notice and buy themselves out of their contract by paying compensation equal to 2% of the previous twelve months milk cheques up to the date they leave.

9. It is important to recognise that we have had a very limited number of members requesting that we review our milk price contracts. The focus from producers is much more on business performance. However, as a result of these EU Commission proposals and to ensure continued best practice, we are undertaking a consultation with our farmer representatives, and through this exercise we will be looking to capture the views of our wider membership.

C. A contract will not be required if the farmer supplies a co-op—but ONLY if the co-op statutes contain provisions with the same objective as the Commission’s “contract requirements”

10. We have written contracts in place with all producers who supply us with milk and believe that this is the best route to follow for processors in the UK.

PRODUCER ORGANISATIONS

D. The Commission proposes to allow producer organisations to negotiate contract terms, including price jointly, or for some of its members’ production to a dairy:

- POs will be subject to **quantitative limits** at EU and member state level.
- The PO must notify the **competent authority** of the member state **to register as a legal entity**.
- Strict clauses are set out in the regulation that will **restrict the activity of the PO** so as to **prevent price fixing**, and other distortions of competition.

11. Our primary focus is on maximising returns for our farmers. In order to ensure this happens in practice, farmers are in the majority around our Boardroom table.

12. Therefore we are uncomfortable with the proposal that dairy co-ops may be required to negotiate contracts with Producer Organisations (POs) that form amongst their membership. This proposal would put members and their co-op in an impossible position if a co-op member was also a PO member, and the PO was undertaking a contract negotiation that may directly undermine the value and security of the same farmer's investments in the co-op. The last thing we need is anything that undermines farmer confidence in investing in their company's own value-added activities.

OPERATION OF THE DAIRY MARKET

13. We have seen from the oral submissions that there is clear disagreement between Dairy UK and the NFU on whether the UK dairy market is working. While there appears to be a perception from a large number of producers that the dairy market is not working for them, rather than repeat previous arguments and counter-arguments, we believe that it is better to focus on some common ground for all stakeholders in the industry to move forward together.

14. The starting point is that the dairy industry provides products that promote health and wellbeing, helps sustain rural communities and plays a vital role in land stewardship. However, what is undeniable is that the dairy industry also faces some enormous challenges, such as economic difficulties for players in the supply chain, the environmental impacts of climate change, climate policy, and changing demands from civil society and from retailers.

15. A project called Dairy 2020 was launched earlier this year that is taking a holistic approach to sustainability because currently, despite the plethora of excellent single-issue initiatives eg the Milk Roadmap, there is no sense of a coherent future vision for the industry.

16. First Milk alongside Forum for the Future (a NGO focused on sustainable development), Volac, Defra, Dairy UK, DairyCo the NFU, Asda and some individual dairy farmers are on the steering group for this project. However, the main work of the project will be undertaken through a series of workshops over the summer that involve a group of around 40 stakeholders drawn from retailers, NGOs, industry associations, government, dairy processors (UK and international), food manufacturers, banks, consultants, farmers, and academics.

17. The Dairy 2020 project aims to answer the question "what does a sustainable dairy industry look like, and what contribution can it make to a sustainable world?". In order to be able to answer its central question, and to do so in a way that galvanises meaningful action, the project outputs include:

- A short vision statement.
- A set of scenarios, exploring the different possible worlds in which the dairy industry may have to operate in 2020.
- Risks and opportunities for the dairy industry for achieving that vision in different possible futures.
- Recommendations for action that will enable a sustainable dairy industry to thrive in 2020. These recommendations will be targeted throughout the industry, taking into account the collective action needed from farmers, processors, retailers, policy makers and beyond. The recommendations will relate to both long-term aspirations for a sustainable dairy industry and short to medium-term achievable goals to ensure continued momentum and tangible outputs.

The scenario development work will begin in May, with recommendations for action before the end of this year.

May 2011

APPENDIX

FIRST MILK BACKGROUNDER

We are the largest farmer-owned dairy business in the UK, supplying 15% of the milk produced in England, Scotland and Wales. We are an integrated business, and are major players in the liquid milk, cheese and ingredients markets. We are the UK's Cheddar specialists—one in every four packs sold in this country is made by us.

Our members' farms stretch from Central Scotland to the South of England and from West Wales to East Anglia. We have production sites in Wales (Wrexham and Haverfordwest), England (near Carlisle) and Scotland (Campbeltown and Arran). We also have a joint venture powder and butter facility at Westbury in Wiltshire. Our head office is in Glasgow.

Our business strategy puts farmers first.

Unlike some private companies or plc's, our primary focus is on **maximising returns for our farmers**. How we deliver this is underpinned by our other four strategic drivers: **Growing our brands**—increasing our market share, distribution and margin; **Diversifying our product base**—constantly looking for new markets, new customers and new products; **Lowering our cost to serve**—continually reviewing how and what we do, so that we can be more cost effective; **Seeking value in partnerships**—working with compatible businesses to grow and diversify

We also provide two unique services to our members: First Milk Academy is a platform to enhance farmers' skills in order to achieve better margins. We run this through business clubs (with support from DairyCo) and development workshops.

Through First Milk Direct we have set up a strategic partnership with Anglia Farmers, the UK's leading agricultural buying group. This saves farmers time and money and allows our farmers to purchase a range of products from fertiliser to fuel and telephones to insurance cover. We also offer direct links to renewable energy specialists and work with supply chain partners on a pioneering bull calf scheme.

Written evidence submitted by Kathleen Calvert

Philip Clarke recently announced that "Tesco will be more open," when record profits were announced.

When I contacted Tesco not long before this, a Customer Service Manager replied saying that unfortunately, Tesco were unable to provide me with any further information regarding their business other than what is available on their website. Acknowledging how annoying this may be for me, as I most likely required further information than is available.

I was also offered their sincere apologies for any disappointment and inconvenience this may have caused me, and it was hoped I would find all the information that I required. I am now wondering how "Open" Tesco now are.

I am a Dairy Farmer's wife and a WI member. I am from a long line of Dairy farmers and so have a keen interest in securing a long-term future for British Dairy Farming.

I have already written to a number of retailers, processors, politicians and people with influence, and received various useful responses, had several letters printed in local and regional mainstream and farming press, and have also spoken at local and County meetings, with good feedback.

As the UK's largest retailer with the ability to handle large volumes of milk procured at the most competitive price, Tesco's current policy of paying a Premium Price to a number of contracted dedicated milk suppliers with a price review every six months has led to others becoming heavily reliant on these price review to set their own base prices. This is usually several pence lower than what Tesco refer to as their "Premium Price" due to the fact that it is above the "going rate" whether or not the "going rate" is a sustainable rate.

Tesco's lead as major price setter sends a signal to others and their unspoken message therefore indirectly affects all other British Dairy Farmers whether Tesco's own contracted suppliers or not, and with the largest percentage of the retail market by far this also allows Tesco an extremely powerful hold over all British Dairy Farmers.

Tesco do not publish their costings, and a company employed by Tesco calculates these. They use only information supplied by Tesco's own selected suppliers, normally selected for being on the most cost effective transport routes, and who comprise only approx 7% of UK dairy farms so cannot be considered as representative of UK milk production costs.

With a large amount of power and financial capability Tesco also have the ability to undercut less significant milk retailers, to play processor against processor, and push prices down to unsustainable levels.

Procuring the largest volumes of milk from one or two large processors gives the ability to pressurise these processors into driving down prices for fear of the loss of a large proportion of their business.

The problems now apparent in the Dairy supply chain are a result of the lack of introduction of an impartial statutory regulation when the Milk Marketing board was broken up. The MMB was considered to be a statutory monopoly even though in its entirety it was far smaller than the modern day Tesco.

Despite being a much larger entity with staggering financial size, power, and influence over dairy farmers, Tesco is still only one part of a massive retail industry meaning they are not a monopoly and cannot be considered to operate unfairly under outdated competition commission rules, even though they can be considered as an oligopoly.

This has led to the intended free market becoming distorted, with producers bearing the full force of massive retailer power.

Increases to producers are rarely more than 1ppl whatever the market situation, often in fractions of a penny, usually from a future date. As buyers began to cautiously increase prices earlier this spring realising the serious implications of not increasing prices, Tesco then set a price that was slightly above the "going rate" and any market gains were then retained higher up the chain at the expense of producers.

Whenever the market is going down, there is no hesitation in reducing prices paid to suppliers and the "free market" is used only as a tool to reduce prices paid to producers while the "going rate" which is related to a distorted market, is used to hold market increases higher up the chain.

The 2ppl Tesco paid its dedicated suppliers in its April price review appears to be based on the minimum amount necessary to remain just on top of the market, which may be for PR purposes and also to create a ceiling.

Many non-dedicated producers are also supplying milk at a much lower price for dairy products sold by Tesco, and supermarkets are able to use special offer strategies designed to confuse and mislead customers.

Tesco appear to be a major force in driving the milk price further and further down to unsustainable levels well below the cost of production putting the future of the British milk supply at serious risk as short-term interests of consumers are met by unrealistic prices that ease the end basket price of their weekly shop, and help reduce inflation.

I am also extremely concerned that Tesco did not feel it necessary to support the NFWI Mission Milk event in November that was set up to bring all interested parties together to establish a long term future for British Dairy Farmers and British Milk production.

This would appear to highlight a lack of genuine concern for British Dairy Farmers and for this reason and the reasons I have given above, Tesco ought not be afforded any prestige or recognition for their personal contract arrangements, which ought not to be considered as a suitable model to follow.

I would also be interested to hear the opinion of a body language expert on David North during his appearance before the EFRA committee.

May 2011

Written evidence submitted by DairyCo

1. DAIRY COSTS OF PRODUCTION

In terms of DairyCo *“calculating the costs of production to work out if milk price was greater than production costs”*. I can confirm that AHDB/DairyCo collect information on costs of production through a service called Milkbench+. This service enables individual farms to benchmark themselves across a variety of performance indicators and cost areas. Data derived from the benchmarking service is provided to dairy levy payers on a confidential basis, and we have not published headline figures on our website or elsewhere.

Whilst we have not published Milkbench+ figures I am happy to confirm that the data indicates that:

- There is a very large variation in full economic costs on dairy farms in GB, whatever their type or the production system employed.
- Averaged by region, farmgate milk prices were typically at least one pence per litre below our detailed full economic cost of production estimates in 2010–11.
- However, it is important to note that the participants on Milkbench+ are self-selecting, and would not necessarily considered to be a representative sample of all dairy farms.

We will be publishing more detailed general commentary on costs of production, returns and drivers of profit (for those who are making a profit) in the sector in the first annual Milkbench+ report that will be available by November 2011.

2. PRICE FORMULAS VS “ORDINARY” CONTRACTS

In terms of analysis by DairyCo on *“whether farmers on a price formula would have done better than farmers on an ordinary contract over the past few years”*. I am happy to provide you with a copy of the graphs below which we produced at the request of the NFU Scotland. This data was provided to compare the average farmgate price for a litre of raw milk (as published by Defra) with different indicators for the UK wholesale value of litre of milk when processed into different dairy commodities.

The graphs were not an attempt to answer the question posed in your e-mail. This is because there are existing contracts within GB which have a price formula either relating to costs of production or an indicator of market value which are included in the average farmgate price. The graphs we produced compare the average farmgate price received by farmers (including those on a formula based contract) with a theoretical indicator of market value.

Figure 1

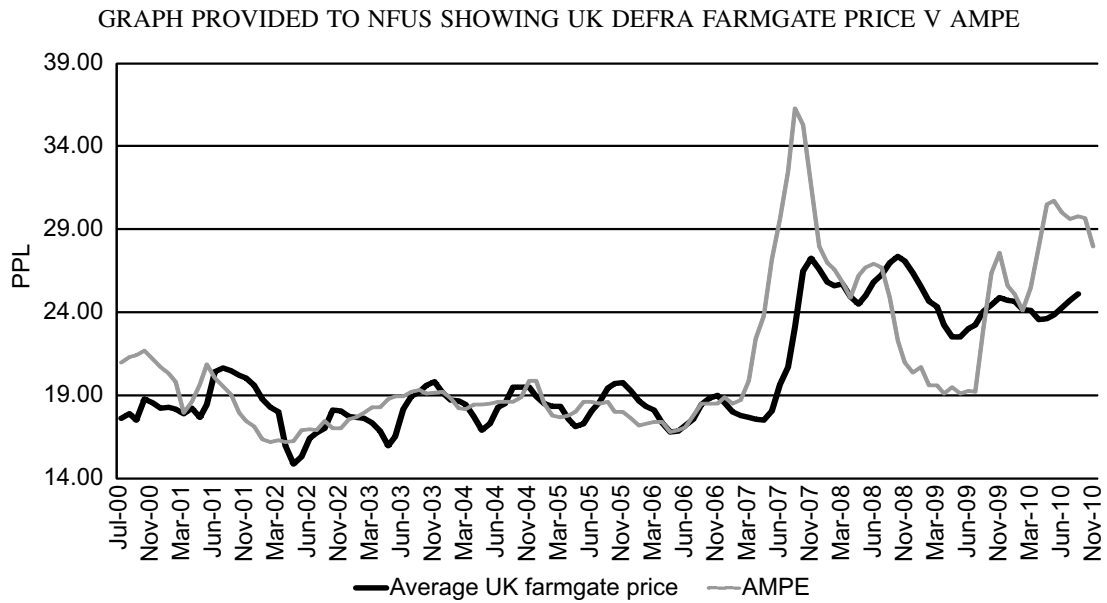


Figure 2

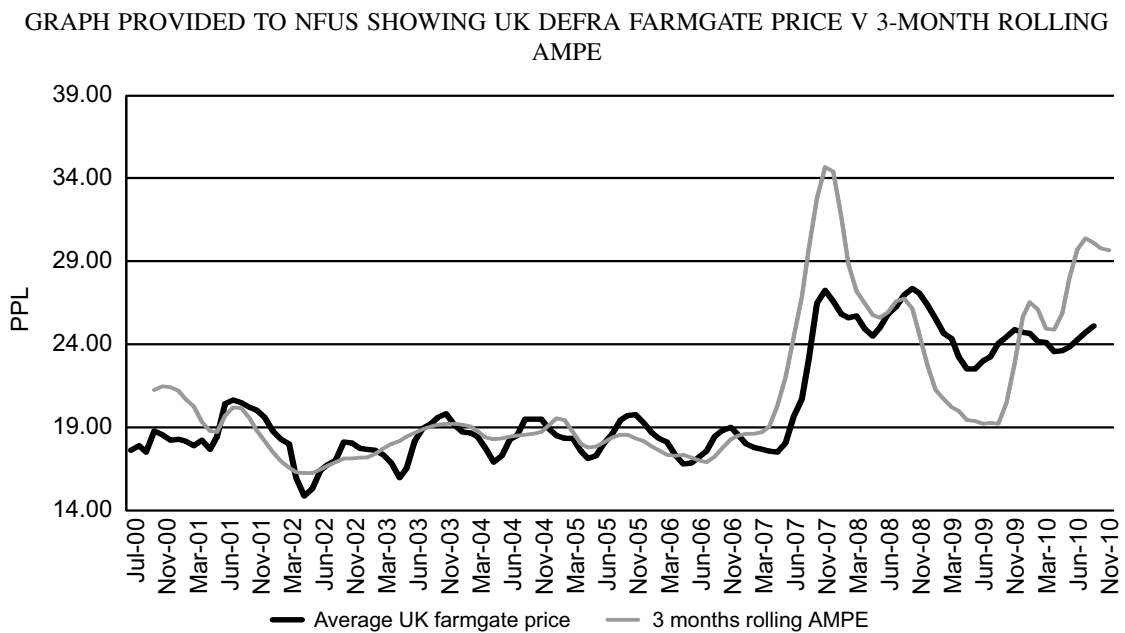


Figure 3

GRAPH PROVIDED TO NFUS SHOWING UK DEFRA FARMGATE PRICE V 6-MONTH ROLLING AMPE

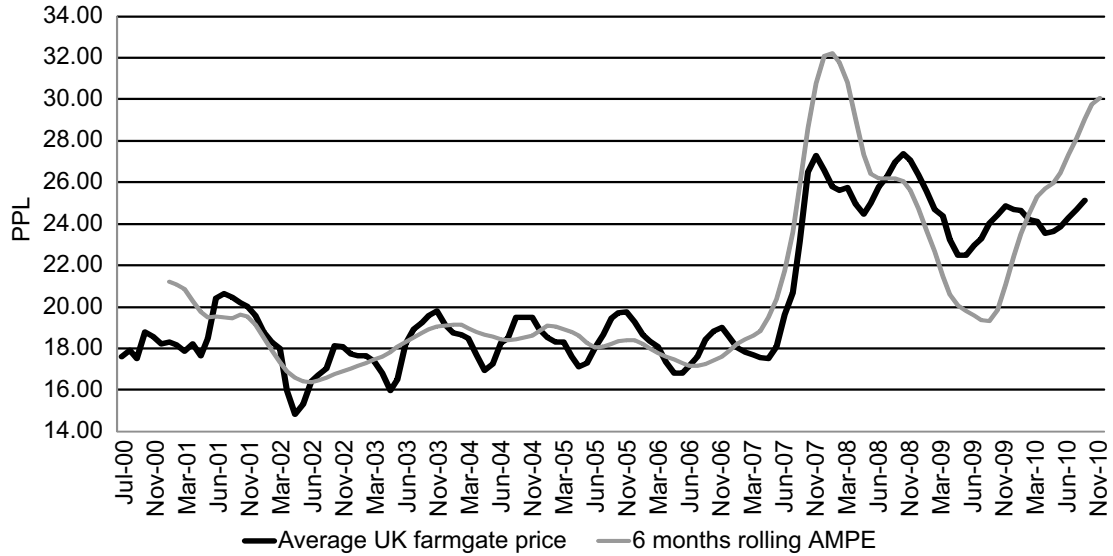


Figure 4

GRAPH PROVIDED TO NFUS SHOWING UK DEFRA FARMGATE PRICE V 1 YEAR ROLLING AMPE

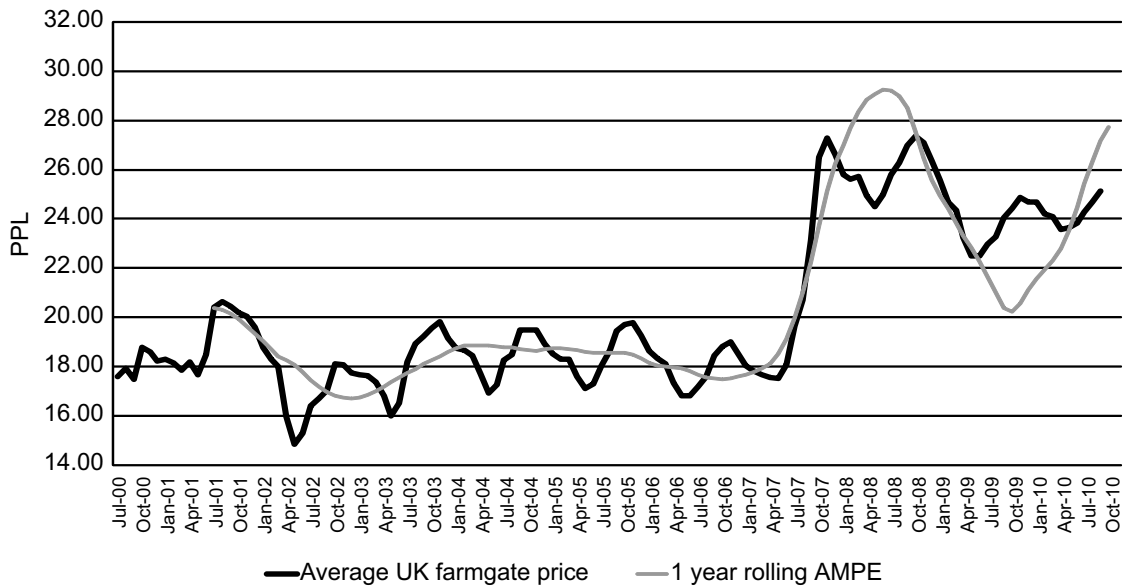


Figure 5

GRAPH PROVIDED TO NFUS SHOWING UK DEFRA FARMGATE PRICE V CHEESE CONTRACTS

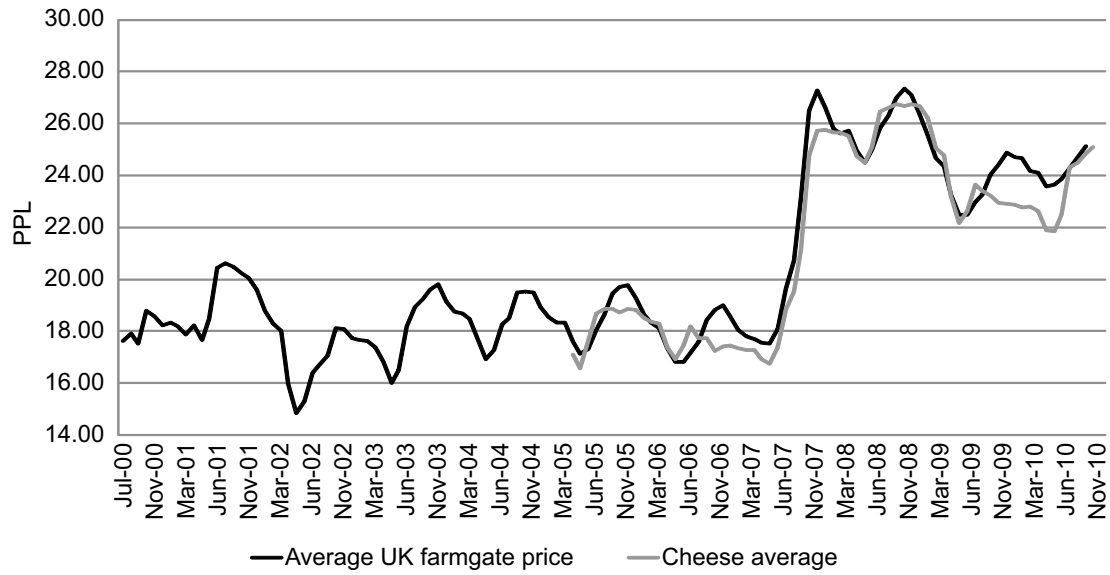


Figure 6

GRAPH PROVIDED TO NFUS SHOWING MCVE V CHEESE CONTRACTS

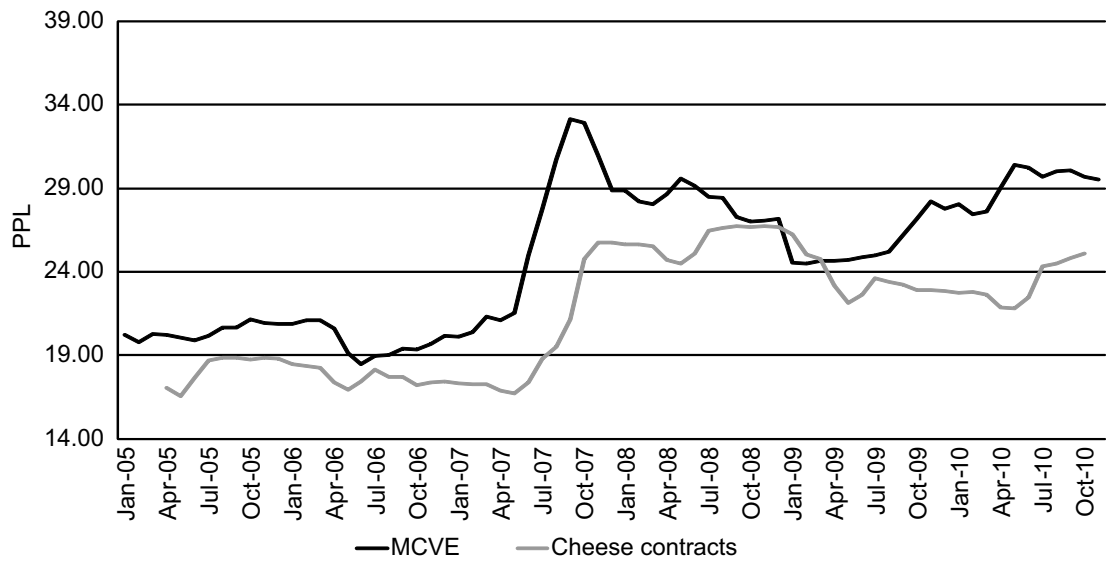


Figure 7

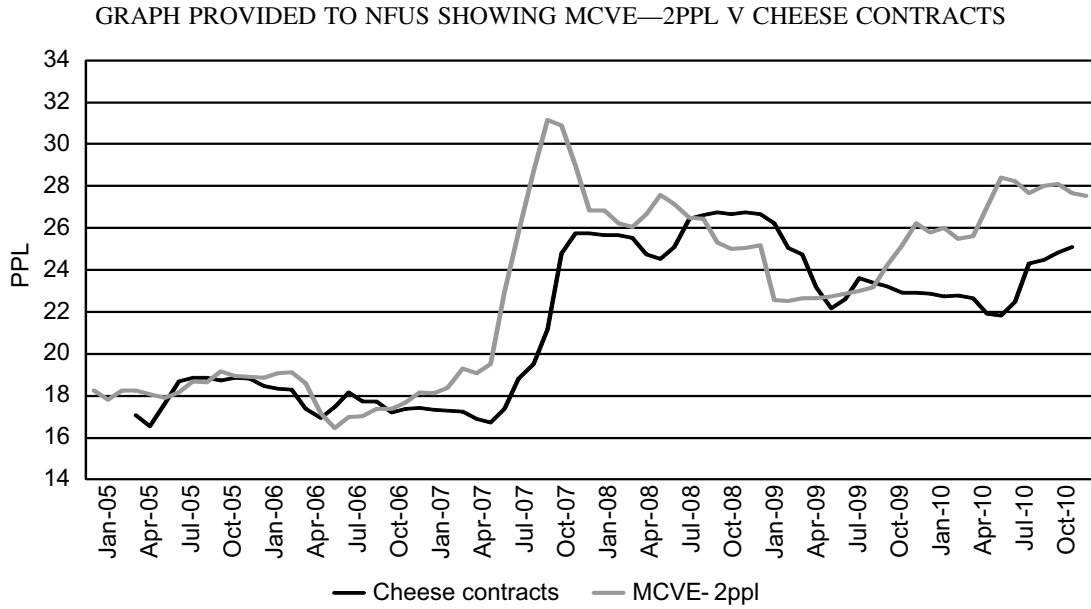


Figure 8

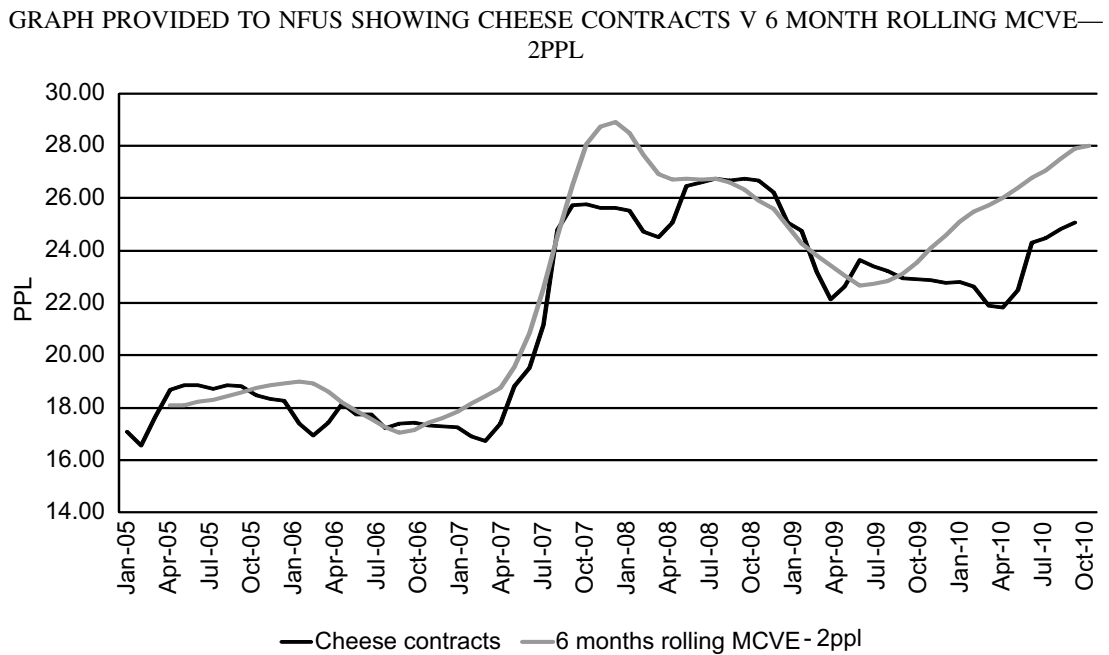


Figure 8a

GRAPH PROVIDED TO NFUS SHOWING 6 MONTH ROLLING MCVE—3PPL V CHEESE CONTRACTS

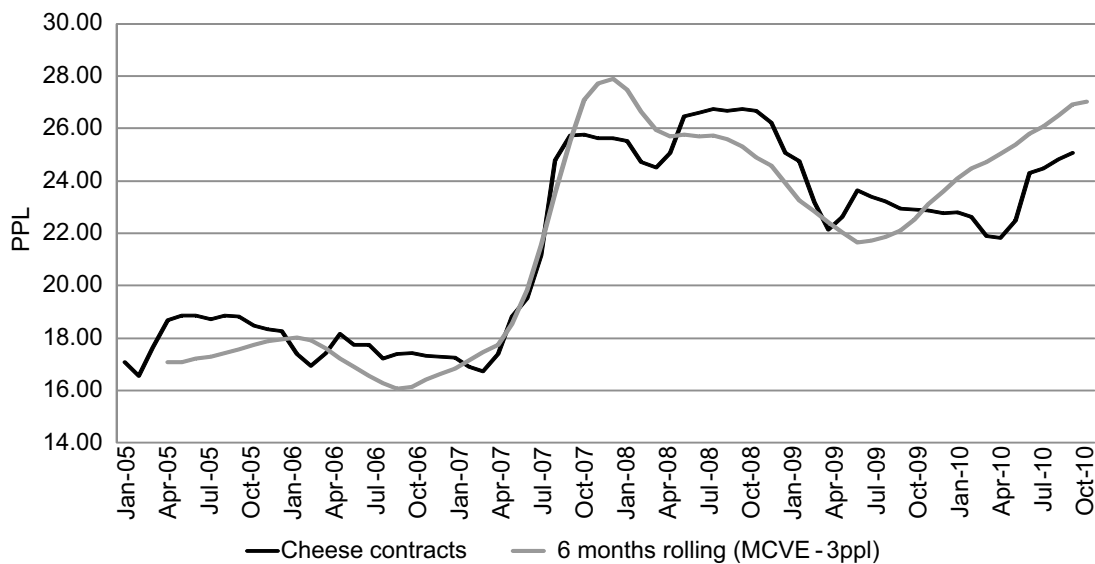
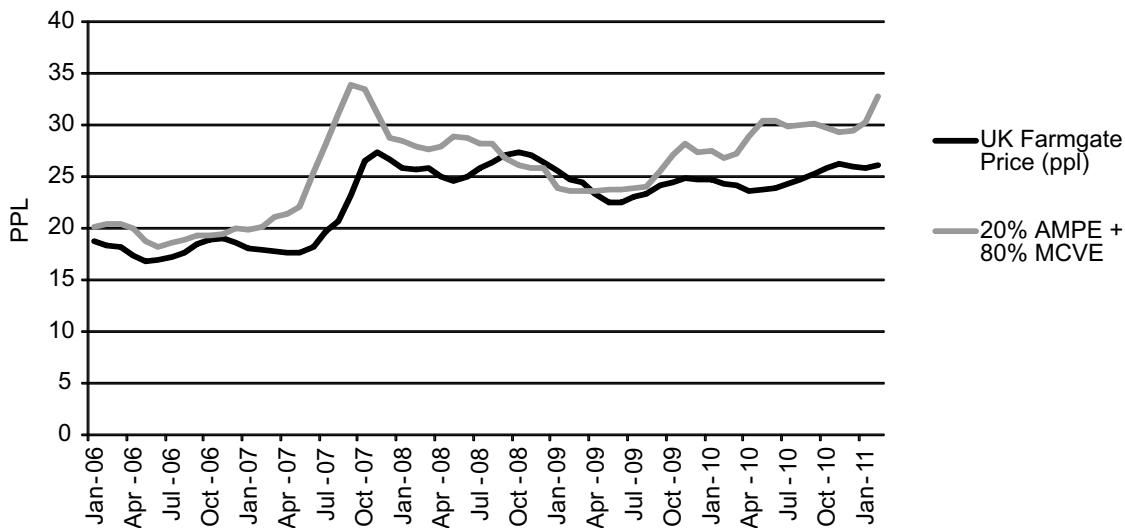


Figure 9

GRAPH PROVIDED TO NFUS SHOWING UK DEFRA FARMGATE PRICE V AMALGAMATED AMPE & MCVE FORMULA



NOTE

AMPE—Actual Milk Price Equivalent.

MCVE—Milk for Cheese Value Equivalent.

June 2011

Written evidence submitted by the Office of Fair Trading

DAIRY SECTOR AND COMPETITION LAW: OFT RESPONSE TO EFRA COMMITTEE

1. INTRODUCTION

The Committee has requested information on the application of current UK and EU competition law to the dairy sector, including what collective behaviour between producers is already permissible, and how the sector might be affected by the EU Commission's legislative proposal for a provision under agricultural law to allow producer organisations (POs) of dairy farmers to negotiate contract terms, including price (i.e. allowing price-fixing agreements), jointly for some or all of its members' production with a dairy processor, subject to appropriate quantitative limits expressed as percentages of EU and national milk production.

2. CURRENT COMPETITION LAW IN EU AND UK

2.1 *Competition law in general*

Competition is at the heart of any successful market economy. It provides a stimulus for businesses to improve their performance and to reduce their prices in order to gain an advantage over rivals and win more business. It encourages the development of new or improved products or processes and increases economic growth and living standards.

Stopping businesses from colluding to fix prices ensures choice for consumers and prices that reflect the costs of production. Both UK and European competition law prohibit anti-competitive agreements and abuse of a dominant position, as well as preventing mergers which are likely to substantially lessen competition in the relevant market.³ This paper focuses on the application of the prohibition on anti-competitive agreements which is most relevant for consideration of the Proposals. To the extent that the merger regime and the prohibition on abuse of dominance are of interest to the Committee, Annexe 2 provides a brief overview of the relevant law in this area.

Competition law does not however, prevent all forms of horizontal co-operation. The EU Courts, as well as the EU and national competition authorities, recognise that—except for price-fixing agreements and/or agreements aimed at limiting output or sharing markets or customers which are generally regarded as *per se* restrictive of competition—many forms of horizontal co-operation are generally beneficial, as they may foster innovation, allow the commercialisation of new products, facilitate efficient sales or reduce distribution costs.

These types of beneficial forms of co-operation (such as co-operatives, grouping together to purchase inputs, to share expensive equipment, or to engage in joint marketing or R&D, etc) are generally permitted under competition law, particularly when the companies involved do not have market power such as to restrict competition in the market to the detriment of consumers, or where, like in agricultural and some other markets, each producer is tiny relative to the overall market. In these circumstances, the said forms of co-operation are either unlikely to breach the prohibition on anti-competitive agreements in the first place or they may meet the criteria for exemption.⁴

As a general rule, both under EU and UK competition law, if the parties to an agreement are competitors that together have 10% market share or less, there will be no appreciable restriction of competition, unless the agreement contains a provision which directly or indirectly fixes prices, shares markets or limits production.⁵

It is not uncommon that some forms of co-operation occur in the context of or with the assistance of trade associations or other industry bodies. Current competition law does not prevent this. Nor does it prevent horizontal competitors from discussing all aspects of their business with each other. However, discussions that strayed into and/or facilitated exchanges of future, and in some circumstances current, commercially sensitive information between competitors (such as on prices and volumes) would be problematic and likely to fall foul of competition law.

Also, participation in setting up non-binding and freely accessible standard terms for industry contracts would be unlikely to give rise to restrictive effects on competition as long as participation in the actual establishment of the terms concerned was open to all competitors. Current competition law does not prevent trade associations and other industry bodies from co-ordinating these or, for instance, from promoting a standard contract to its members. Although the OFT is not in a position to offer a general view in this regard (as the issue may turn on the specific terms included in any such contracts), it would think that in principle the promotion of a standard contract by a trade association, without more, is unlikely to breach competition law

³ Articles 101 and 102 TFEU, Chapter I and II of the UK Competition Act 1998 and the Enterprise Act 2002.

⁴ In accordance with Article 101(3) of TFEU or section 9(1) of the Competition Act 1998 in UK law, an agreement will not be prohibited under Art 101(1) and/or Chapter I of the Competition Act 1998 if it (a) contributes to (i) improving production or distribution, or (ii) promoting technical or economic progress; while allowing consumers a fair share of the resulting benefit; and it (b) does not (iii) impose on the undertakings concerned restrictions which are not indispensable to the attainment of those objectives, or (iv) afford the undertakings concerned the possibility of eliminating competition in respect of a substantial part of the products in question.

⁵ See Commission notice on agreements of minor importance which do not appreciably restrict competition under Article 81(1) (now Art 101(1)). See also OFT Competition Law Guideline on Agreements and concerted practices, December 2004, pages 8 to 11.

provided that contract terms on prices and/or volumes are individually negotiated between processors and producers/co-operatives.

2.2 Application of competition law to the dairy farming sector

EU and UK competition laws apply to agricultural markets as they do to other sectors. There are, however, a number of exceptions/exclusions (which are explained in more detail in Annexe 1 to this paper). Briefly, these relate to certain agreements, decisions and practices of farmers, farmers' associations, or associations of farmers' associations belonging to a single Member State which concern the production or sale of agricultural products, or the use of joint facilities for the storage, treatment or processing of agricultural products, and under which there is no obligation to charge identical prices.

More specifically, for the agricultural exclusion⁶ to apply, only farmers, farmers' associations or associations of farmers' associations can be party to the agreements at issue. For example, an agreement between a group of dairy farmers and milk processors would not qualify for being excluded. Such agreements would still be subject to general competition law.

In addition, the agreements in question need (i) to be necessary for the attainment of all the objectives of the Common Agricultural Policy (CAP) set out in Article 39 of the Treaty on the Functioning of the European Union (TFEU) and (ii) should not cover prices, but concern rather the production or sale of agricultural products or the use of joint facilities for the storage, treatment or processing of agricultural products.

In practice, therefore, despite the exclusion/exceptions described, the majority of the agreements and decisions of farmers and/or farmers' associations are subject to the general competition rules applicable to undertakings.

However, as noted in the previous section, general EU and UK competition law already allow many forms of co-operation between farmers and tend to see them as beneficial. This is particularly the case in respect of agricultural co-operatives. These have generally been recognised as pro-competitive structures⁷ which allow farmers to better compete with other milk suppliers, thus contributing to the modernisation of and rationalisation in the agricultural sector and improving efficiency, to the ultimate benefit of consumers.⁸

Under EU competition rules, a co-operative (within which for example dairy farmers co-operate in the area of production, collection or processing their milk) may also decide on sales volumes and prices, without falling foul of competition law, provided that such decisions are indispensable for the implementation of the agreement (for the integration of other marketing functions and generating efficiencies) and the co-operative does not hold significant market power (which is unlikely if its market share does not exceed 20% in the relevant market—or 15% if the entity in question is limited to joint commercialisation activities—see below).⁹ Above such thresholds there is no presumption of illegality but the potential restrictive and efficiency-enhancing effects will have to be assessed on a case-by-case basis.¹⁰

Some potential forms of co-operation which, absent market power, could be considered as “efficiency-enhancing” without contravening the provisions of the Chapter I prohibition of the Competition Act 1998 and/or of Article 101(1) TFEU, and whilst ensuring CAP objectives are achieved, include:

- Sharing facilities of any kind—milking facilities, milk storage tanks, transport, processing facilities, other common equipment;
- Sharing of skills and knowledge including staff;
- Common marketing or branding of a product to add value which is of some benefit to consumers (but not simply increasing the sale price of a product without such justification);
- Common marketing or branding of a product to ensure availability of that product on the (relevant) market (ensure market access and help maintaining presence in the market if their “genuine” product is specifically desired by consumers); and
- reducing waste of any kind through better management and potential use of all by-products to their highest value rather than for disposal or for commodities.

⁶ Under Schedule 3, paragraph 9 of the Competition Act 1998) and/ or under exceptions under EU Single Common Market Regulation.

⁷ There may be some competition concerns though (which would need to be assessed on a case-by-case basis) in circumstances where there was market power and/or exclusionary membership rules acted as barriers to entry to new competitors, or where membership provides a vehicle for collusion.

⁸ See European Court of Justice judgment of 12 December 1996, Case C-399/93, *H.G. Oude Luttikhuis*, [1995] ECR I-04515; Case C-250/92 *Gøttrup-Klim v Dansk Landbrugs Grovareselskab AmbA* [1994] ECR I-5641 [1996]; Commission Decision of 2 April 2003, Case COMP/C.38.279/F3, *French beef*, OJ L 209, 19.08.2003; Judgment of 15 December 1994, Case C-250/92, *Dansk Landbrugs Grovareselskab AmbA*, [1994] ECR I-05641.

⁹ See the European Commission Q&A document on “How EU competition policy helps dairy farmers in Europe”, Brussels 10.02.2010, in particular the answers to questions 6 to 9. Also, the European Commission “Working Paper on the interface between competition policy and the CAP in the dairy sector”, pages 11 to 18. Both documents are available at http://ec.europa.eu/competition/sectors/agriculture/documents_en.html.

¹⁰ See page 5 of the European Commission Q&A document referred to at note 7 above.

2.3 The application of EU competition rules to forms of co-operation among dairy farmers

The EU has advised that Member States have a great deal of latitude how to shape and apply competition rules to their dairy sectors. EU competition rules do not apply to co-operation arrangements among farmers as far as such arrangements do not have the capability “to appreciably affect trade between Member States”.¹¹

The EU notes that in practice this means that, if a group of farmers with a combined market share of less than 5% and an EU aggregate turnover of less than 40 million euro were to decide to enter into any types of co-operation agreements, EU competition rules would simply not apply to them. (On the other hand, national competition legislation might still apply at these levels where the agreement affected trade in a relevant market within a particular Member State).

Above these thresholds, a more careful, case-by-case examination would be required to determine to what extent an agreement is capable of having a minimum level of cross-border effects within the EU. Absent of such effects, however, even far-reaching forms of co-operation, such as the creation of collective bargaining groups agreeing on prices and quantities of milk to be sold to downstream processors, would not fall under EU competition rules. In such cases, Member States remain free to determine the legality of such agreements under their own competition regimes, taking into account the specificities and structural conditions of the milk supply chain within their territory.

In relation to the interaction between EU and UK competition law, it is worth noting that, when applying national competition law, the UK authorities are under an obligation to ensure that there is no inconsistency with either the principles laid down by the EU Treaty and the European Courts, or any relevant decision of the latter. Also, they must have regard to any decisions, notices and/or clear statements of policy approach by the European Commission.

As explained above, even where EU (and UK) competition rules apply, they allow for sustainable forms of co-operation among dairy farmers as long as they create efficiencies and do not limit competition to the detriment of consumers.

The European Commission has clearly explained in its Working Paper on the interface between competition policy and the CAP in the dairy sector and in a related Q&A document¹² that, for example, a joint commercialisation agreement¹³ between competitors which does not involve price-fixing would in principle only fall foul of EU competition law (i.e. Article 101 TFEU) if the parties to the agreement had some degree of market power. In particular, such agreement would be unlikely to be anti-competitive where participating farmers have an aggregate share of the relevant market that does not exceed 15%.

On the other hand, commercialisation agreements that involve price-fixing will always fall under Article 101(1) TFEU irrespective of the market power of the parties; the main concern being that it entails a co-ordination of the pricing policies of competing producers. That said, the Commission notes that in certain specific circumstances commercialisation agreements between competing undertakings involving a certain level of integration of activities for which price-fixing is indispensable may be exempted under Article 101(3) TFEU provided that certain conditions are met (such as that price-fixing is indispensable for the integration of other marketing functions; that this integration generates substantial efficiencies; that the agreement does not impose restrictions that are not indispensable to the attainment of the alleged benefits; that the parties do not have market power which allows them to eliminate competition, etc).

The Commission further notes that, for example, price-fixing could be exempted, because it is considered as indispensable, in the following exceptional circumstances: i) if a large buyer does not want to deal with a large number of prices and requests a single supply price; similarly, ii) if farmers agree on jointly launching new products, such as a common brand of milk, which can only be credibly achieved if all aspects of marketing, including price, are standardised. This favourable assessment would however depend on the collective bargaining group not holding significant market power (i.e. aggregate market share of the group being below 15%).

In the same working paper, the European Commission also notes that joint production agreements¹⁴ and agricultural co-operatives, where farmers may group together their complementary milk outputs with the aim of producing processed dairy products, are generally to be viewed as pro-competitive, and are unlikely to cause concern provided the parties to the agreement do not have market power in the market on which the restriction of competition is assessed (i.e. the combined market share of the parties should not exceed 20% of the relevant market).

¹¹ *Ibid.*, page 2.

¹² See note 7 above.

¹³ Commercialisation agreements cover co-operation agreements between competitors in the selling, distribution or promotion of their products. These agreements can have a widely varying scope, depending on the marketing functions which are being covered by the co-operation. As far as the milk and dairy sectors are concerned, one of the most relevant types of commercialisation agreements between farmers not integrated in co-operatives refers to the joint selling of raw milk. (Source: EU: “Working Paper on the interface between competition policy and the CAP in the dairy sector”).

¹⁴ By means of a joint production agreement, two or more parties agree to produce certain products jointly or to carry out certain processing activities jointly. Joint production always entails an integration of economic activities, capacities or assets between the parties to the agreement, albeit its nature, scope and form can vary in practice. (*Ibid*)

2.4 What is not allowed under current competition law

Under the existing competition rules, agreements between farmers which seek to fix prices or share markets and/or customers are considered likely to breach competition law, hence they are generally prohibited (although as noted above they may be exempted provided they meet the criteria in Article 101(3) and/or section 9 of the Competition Act 1998). Similarly, agreements to limit supply of production to keep prices high or where the co-operation allows the parties to maintain, gain or increase market power and thereby to cause negative market effects with respect to prices, output, innovation, or the variety or quality of products would be likely to infringe competition law.

2.5 The treatment of POs and farmers' co-operatives under competition law

A PO¹⁵ is a form of co-operation between farmers and more generally producers of certain agricultural products which is defined in Article 122 of Council Regulation (EC) No 1234/2007 (also known as the Single CMO Regulation). In order to be recognised as a producer organisation, the legal entities concerned (or part of them) must meet certain requirements set out in Article 125b of the Single CMO Regulation, such as, for example, having a minimum number of members and cover a minimum volume or value of marketable production to be laid down by the Member State. We understand that POs that are formally recognised benefit from funding from the EU.

In the UK we have not dealt with Competition Act 1998 cases concerning POs. In fact, we understand that, to date, there are no POs in the UK dairy sector. There are, however, some in the fruit and vegetable sector.

A co-operative, on the other hand, is a voluntary association of persons established in order to pursue certain commercial objectives which, unlike a PO, does not need to meet any specific requirements laid down in legislation or to be officially recognised in order to operate as such. Nor do they get specific funding from the EU.

As noted elsewhere in this submission, groups of individual farmers are permitted to group together their complementary milk productions and/or storage facilities to achieve a number of commercial ends, but fixing a collective price is unlikely to be acceptable in competition terms, except for in specific, limited circumstances (see sections 2.2 and 2.3 above).

Co-operatives are treated identically under both EU and UK competition law (and in general terms, the same competition law rules apply to them as they do to private companies) and, as noted above, are generally regarded favourably under competition law.¹⁶ The European Courts as well as DG Comp and national competition authorities have very often emphasised the benefits in terms of efficiency gains that may stem from the establishment of co-operatives.¹⁷

It is noted that cooperative agreements may vary in form and scope, depending on the aims pursued and the level of integration of activities. They may be limited to a production joint venture, or extend to include the distribution of relevant products (i.e. commercialisation agreements). Or, they may take the form of a full-function joint venture in the form of a jointly controlled company that runs one or several production facilities and also carries out joint distribution of the product concerned. In these cases, it is likely that the structural co-operation between the parties would fall under the relevant merger control rules (either at EU or national level), which are distinct from the anti-trust rules (namely Articles 101 and 102 TFEU on anti-competitive agreements and abuse of dominance respectively, and under UK law, the equivalent provisions of Chapter I and II of the Competition Act 1998).

2.6 Advice provided by the OFT to inform and guide farmers on collaboration and co-operation

DG Comp and the OFT have both produced guidance¹⁸ which sets out a number of practical scenarios of the types of co-operation which are already allowed under existing EU (as well as UK) competition rules. In this respect, it is noted that the OFT will likely be updating its currently available guidance in the near future.

Guidance is also already available as part of the EU Vertical Agreements Block Exemption and accompanying guidelines as well as the EU Research and Development and Specialisation Block Exemptions and accompanying guidelines on horizontal co-operation.

Where novel and unresolved issues of competition law arise, notwithstanding the above, businesses may find it useful if competition authorities are able to give opinions on whether particular prospective arrangements

¹⁵ A PO is defined in Article 122 of Council Regulation (EC) No 1234/2007, which describes POs as being “constituted by” and “formed on the initiative of” producers. A PO pursues specific aims which may include: ensuring that production is planned and adjusted to demand, particularly in terms of quality and quantity; concentration of supply and the placing on the market of the products produced by its members; and optimising production costs and stabilising producer prices.

¹⁶ Some competitive concerns may be raised in certain situations such as those set out in note 5 above.

¹⁷ For example, European Court of Justice judgment of 12 December 1996, Case C-399/93, *H.G. Oude Luttikhuis*, [1995] ECR I-04515; Case C-250/92 *Gøttrup-Klim v Dansk Landbrugs Grovareselskab AmbA* [1994] ECR I-5641 [1996]; Commission Decision of 2 April 2003, Case COMP/C.38.279/F3, *French beef*, OJ L 209, 19.08.2003; Judgment of 15 December 1994, Case C-250/92, *Dansk Landbrugs Grovareselskab AmbA*, [1994] ECR I-05641.

¹⁸ See http://ec.europa.eu/competition/sectors/agriculture/documents_en.html and http://www.of.gov.uk/shared_of/business_leaflets/competition_law/of740.pdf.

would be anti-competitive. In the UK, provided the prospective agreements meet certain requirements, we are trialling a “short-form opinion” tool which may be used for this purpose.¹⁹

3. PROPOSED DEROGATION FROM COMPETITION LAW FOR THE DAIRY SECTOR

The EU Commissioner for Agriculture’s High Level Group on Milk put forward last year a legislative proposal for a provision under agricultural law to allow POs of dairy farmers to negotiate contract terms, including price (i.e. allowing price-fixing agreements), jointly for some or all of its members’ production with a dairy processor, subject to appropriate quantitative limits expressed as percentages of EU and national milk production (the Proposals). It argued that current competition law—which does not generally allow price-fixing agreements, except for in limited exceptional circumstances—was inadequate to address instabilities in the supply chain, highlighted by recent volatility in milk prices and the perceived weak bargaining power of dairy farmers in relation to dairy processors.

In brief, the Proposals would permit groups of farmers to establish formal POs that would be allowed to bargain collectively and agree a fixed price for their milk in derogation from general competition rules. Moreover, as currently drafted, the Proposals would permit the new POs to reach a size that might be unacceptable under current competition law (the Proposals currently suggest a limit of 33% of national milk production or 3.5% of EU milk production). Finally, the Proposals would also provide for standard contracts between milk sellers and purchasers (which Member States could decide to make compulsory in their own dairy markets), increase transparency and facilitate the creation of “inter-branch organisations” made up of participants in every stage of the supply chain.

4. ATTITUDES TO THE MILK PROPOSALS

4.1 *The attitude of the UK and of other Member States to the Proposals*

UK authorities (Defra, BIS and OFT) have reached a joint position that is opposed to key elements of the Proposals²⁰ on the grounds that:

- existing competition law is sufficient to allow UK dairy farmers to collaborate effectively to achieve a number of commercial ends;
- the Proposals may permit the establishment of such large POs that this may have a distorting effect on competition in the sector that would outweigh the benefits to the farmer members of the PO;
- the ability to agree a collective price could itself lead to serious distortions in the market;
- there are more appropriate and effective solutions to the perceived problems, such as more widespread contractualisation (as long as a specific actual price or price recommendation is not included in the standard contract), investment in modernisation and in the development of new co-operatives and/or vertically integrated business models;
- the proposals may also have adverse effects outside this market which should be factored in; more specifically, structural and protectionist approaches in politically strong sectors may undermine the EU’s case for competition internationally, and the costs to EU business from similar protectionism by others could be very high; the proposal will likely weaken the ability of the EU collectively to argue for effects-based competition policy to other jurisdictions, including emerging markets.

DG Comp and the national competition authorities of other Member States follow this view and, in November 2010, a joint resolution of the heads of the European competition authorities was published.²¹

In terms of the agricultural authorities in other Member States, the picture is more mixed. There is a wide disparity in size, concentration and structure between the dairy markets of different Member States. We understand that some agricultural authorities in other Member States are more receptive than the UK to the Proposals and some even want to extend the scope of the derogation from competition law to all agricultural sectors in the future.

4.2 *The concept of the “relevant market” and why it is important*

The concept of the “relevant market” is used by competition authorities as a tool to assess where power lies in a particular market. More specifically it defines the competitive constraints acting on a supplier or purchaser of a given product or service, including actual or potential competitors of the undertaking(s) involved that are capable of constraining that undertaking’s behaviour and of preventing them from behaving independently of effective competitive pressure (for example, by raising prices above the competitive level).

It is very difficult to assess a competitive situation accurately without first identifying the relevant (product and geographic) market. Any other measure would be arbitrary for the determination of market power, or for analysing the effect of particular agreements or conduct. For example, in the case of an agreement affecting the market for the procurement of raw milk, using a measure other than the relevant market concept would

¹⁹ See <http://www.of.gov.uk/OFTwork/competition-act-and-cartels/short-form-opinions/>.

²⁰ Specifically, the provisions to allow POs to reach a certain proportion of national or EU production and to allow collective fixing of prices.

²¹ Obtainable at <http://ec.europa.eu/competition/ecn/milk.pdf>.

prevent a competition authority from taking into account in its analysis the competitive constraints on a certain undertaking of several relevant and significant factors such as the perishability of raw milk, the conditions of competition across different geographic areas, and in particular the costs of collecting raw milk, which are affected by transport distances, the density of farms in a given area, the size of the processing plants, etc. Therefore we believe that a measure based on quantities of production risks permitting strong distortions to arise in the UK (and EU) dairy markets; for example, from the creation of very large POs.

4.3 The origin of the limits in the Proposals

The EU's DG Agriculture and Rural Development has explained that it proposed to move away from the concept of the "relevant market" because it was considered that that concept was a source of uncertainty and too technical and complex to understand by those who are not familiar with competition law. This is because in such analysis the market is not defined in advance, but rather on a case-by-case basis. DG Agriculture argues that a quantitative limit would be more appropriate to achieve the goal of rebalancing bargaining power in the milk supply chain, while still preserving effective competition on the markets.

The published draft of the Proposals on which OFT was asked to comment stated 33% of national production and 3.5% of EU production but it did not contain any explanation as to how these figures had been arrived at.

5. HOW THE PROPOSALS WOULD WORK

5.1 Intervention by a national competition authority

The Proposals, as currently drafted, would allow national authorities to intervene in an individual case to prevent negotiations by a PO below the maximum quantitative threshold, to prevent "competition being excluded or in order to avoid serious prejudice to SME processors". We are not yet clear how this intervention would operate in practice.

Defra, BIS and OFT have argued that the current wording could set too high a hurdle for intervention. For example, there may be few market situations where competition would be completely "excluded", which would restrict the opportunity for authorities to intervene. Moreover, terms such as "excluded" and "serious prejudice" are not routinely used in competition law and hence may create ambiguity. We would also prefer an emphasis on the effects on the market as a whole rather than just on SME processors. We have argued for a softening in the wording; for example, "seriously distorted" instead of "excluded".

The Proposals also allow for the Commission to take the same decision where negotiations cover more than one Member State. Defra, BIS and the OFT have argued that national competition and/or agricultural authorities should also be able to contribute to such decisions.

5.2 The application of the Proposals to co-operatives

The OFT is not involved in the drafting of the legislative proposal, other than providing our views (along with Defra and BIS) through the relevant European channels involved in the legislative process. Our views on how the Proposals apply to co-operatives are based on our interpretation of the current draft wording and only the Commission, who originally put forward the Proposals, could provide a definitive explanation.

Our current understanding is that farmer members of a co-operative, whether or not their co-operative processes their milk, may form a PO of some or all of the farmer members in order to sell their produce to this co-operative. Co-operatives may prohibit such arrangements in their statutes. Co-operatives may choose not to seek recognition as POs, in which case they would be subject to existing competition law in their dealings.

Co-operatives that sell some or all of their milk to another processor or collector may form a PO for these operations and may seek and obtain recognition under Article 122 of Regulation (EC) No 1234/2007. As it is forbidden for two POs to negotiate contracts for the sale of the same milk, a co-operative that takes this step necessarily precludes the possibility of its farmer members forming a PO to sell to the co-operative.

In theory, farmer members of a co-operative could join another PO, or form a new one, and sell to their co-operative. As said, however, a co-operative could prevent an internal PO through making this a condition in its statute. This could forbid members from being part of a separate PO, or at least a separate PO which negotiates the sale of that producer's milk to that co-operative.

Because two POs could not negotiate for the same milk, a co-operative could defend against internal POs by becoming recognised as a PO itself for its milk brokering operations and for negotiating the sale of any of its members' milk to a third party processor.

THE LEGAL BACKGROUND

How competition law specifically applies to the dairy farming sector

EU and UK competition laws (Articles 101 and 102 TFEU, UK Competition Act 1998 and Enterprise Act 2002) apply to agricultural markets as they do to other sectors. There are, however, the following exceptions:

- At EU level, Council Regulation (EC) 1234/2007, of 22 October 2007, establishing a common organisation of agricultural sectors and on specific provisions for certain agricultural products, including milk and milk products (known as the “Single CMO Regulation”); and Council Regulation (EC) 1184/2006 of 24 July 2006—applying certain rules of competition to the production of, and trade in, a number of agricultural products (namely those listed in Annex I to the TFEU)—both provide that the general application of competition rules to the agricultural sector is subject to three exceptions which are specified in Article 176(1) of the Single CMO Regulation. The latter take into account the aims of the CAP and recognise the particular circumstances of and challenges to agricultural markets.

In particular, Article 176(1) provides that Article 81(1) (now Article 101(1) TFEU) shall not apply to agreements, decisions and practices which relate to the production of, or trade in, the products covered by this Regulation, which (i) are an integral part of a national market organisation; or (ii) that are necessary for the attainment of the objectives set out in Article 33 of the Treaty (now Article 39 TFEU). Article 176(1) further states, as exception (iii), that Article 101(1) of the Treaty shall not apply to agreements, decisions and practices of farmers, farmers’ associations, or associations of farmers’ associations belonging to a single Member State which concern the production or sale of agricultural products or the use of joint facilities for the storage, treatment or processing of agricultural products, and under which there is no obligation to charge identical prices, unless the European Commission finds that competition is thereby excluded or that the objectives of Article 33 of the Treaty (now Article 39 TFEU) are jeopardised.

It should be noted that the exceptions above only concern Article 101 of the TFEU, hence Article 102 of the TFEU on abuse of dominance remains fully applicable to the agricultural sector.

- In the UK, the Competition Act 1998 provides an exclusion from competition law for agricultural products that mirrors the exemption in the Single CMO Regulation referred to above. The exclusion (paragraph 9 of Schedule 3 to the Competition Act 1998) is an exclusion from the application of the Chapter I prohibition (which prohibits agreements and concerted practices which prevent, restrict or distort competition) for agreements, to the extent they relate to production of, or trade in, an agricultural product, and:
 - form an integral part of a national market organisation;
 - are necessary for the attainment of the objectives set out in Article 39 of the TFEU (formerly Article 33 of the EC Treaty); or
 - are agreements of farmers or farmers’ associations belonging to a single Member State which concern (i) the production or sale of agricultural products, or (ii) the use of joint facilities for the storage, treatment or processing of agricultural products,
 and under which there is no obligation to charge identical prices.

BASICS OF MERGERS REGIME IN THE UK

Some forms of co-operation may amount to a merger if a party transfers some or all parts of its business to another party in the collaboration. However, unless the collaboration covers 25% or more of the share of supply of goods or services of a particular description or the combined UK turnover exceeds £70 million, the OFT will generally not need to consider it under the Enterprise Act 2002 Mergers Provisions.

The assessment of mergers in the UK is conducted as a two-phase process, with the OFT responsible for the first phase and the Competition Commission (CC) responsible for the second, more in-depth, phase. More specifically, the OFT obtains and reviews information relating to merger situations and has a duty to refer to the CC any relevant merger where it believes the merger results in a realistic prospect of a substantial lessening of competition (SLC). The OFT has discretion not to refer where the parties offer suitable remedies. The CC then decides whether the merger is more likely than not to lead to an SLC (that is, on the balance of probabilities). The CC typically clears about half of the mergers referred to it.

Parties may appeal CC merger decisions to the Competition Appeal Tribunal (CAT).

Under the UK merger regime, it is not obligatory to seek approval before merging but it is strongly recommended to advise the OFT before the merger occurs.

The European Commission examines mergers of businesses with an EU dimension or which have a global turnover above a certain size, including those that may have an impact in the UK. In some circumstances, these can be transferred to the UK authorities for examination.

More details about the UK merger regime are available on the OFT website, including a “Quick Guide to UK Merger Assessment” published jointly by the OFT and the CC in March 2011.²²

²² Available at http://www.of.gov.uk/shared_of/mergers/Quick_Merger_Guide.pdf.