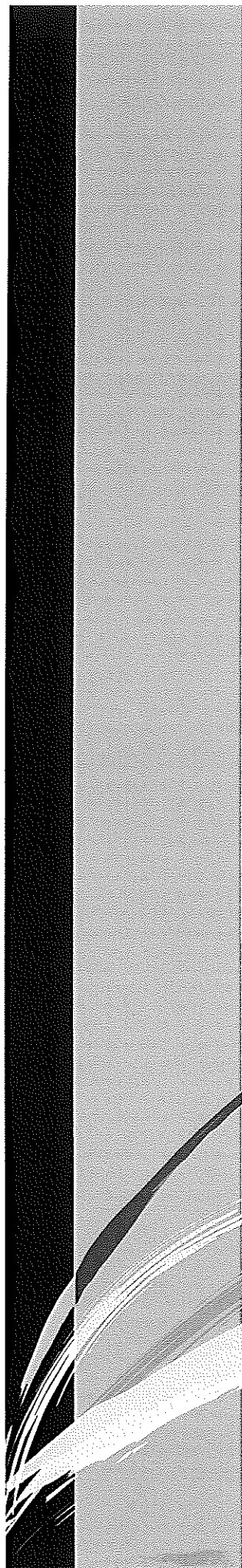




Government of Western Australia
Department of Treasury and Finance

Inquiry into the Chicken Meat Industry Act 1977

April 2010



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OVERVIEW

On 25 February 2010, the Economic Regulation Authority (ERA) released an issues paper discussing matters relating to the Inquiry into the *Chicken Meat Industry Act 1977* and calling for submissions from interested parties.

This submission outlines the Department of Treasury and Finance's (DTF) response to certain matters raised in the ERA's issues paper. The DTF is mindful that it is not well placed to comment on industry specific issues, however, the comments provided in this submission are intended to highlight microeconomic policy constraints in Western Australia's (WA) chicken meat industry.

The DTF is committed to the development of better regulation through the Regulatory Gatekeeping Unit, as well as reducing the burden of existing regulation on businesses and consumers, through its red tape reduction agenda. Addressing regulatory constraints and reducing the level of unnecessary or poorly designed regulations on WA businesses and consumers can make a significant contribution to increasing the economic performance and growth prospects of the state.

OPERATION OF CHICKEN MEAT INDUSTRY ACT 1977

Act provisions

The WA chicken meat industry has operated under the direction of state legislation since the introduction of the *WA Chicken Meat Industry Act 1977* (the Act). When introduced in 1977 it was clear that the major objective of the legislation was the stabilisation of the chicken meat industry following a large increase in consumer demand. In particular, the Act was established to provide broiler chicken growers with countervailing measures to match the market power of chicken meat processors. The Act achieved this through establishing compulsory collective contracting system between all growers and chicken meat processors as well as establishing a Chicken Meat Industry Committee (the Committee) to oversee relations between producers and processors of chicken meat. The Committee was also charged with the responsibility for determining the average price paid for broiler chickens.

National Competition Policy Reforms

Initially functions carried out by the Committee included approval of growing premises, facilitation of the dispute resolution process and determination of the average price of broiler chickens. However, as a result of several legislative reviews, most notably the National Competition Policy (NCP) review and commitments, the functions and prescriptions of the Act have been paired back. One of the NCP commitments focused on identifying legislation that restricted competition, to review and where appropriate, reform that legislation. Compliance with such legislative reform led to amendments being passed in December 2003 under which prescribed growing agreements, together with standard growing fees and the committee's dispute resolution power, apply only where growers and their processor agree. That is, individual growers and their processor may opt out of the statutory centralised bargaining and dispute resolution process. Restrictions on entry to the processing sector were also removed.

Despite these reforms the National Competition Council (NCC) stated in its 2004 NCP Assessment that 'the requirement that incumbent growers have first right of refusal to meet growing capacity increases sought by processors is a potential restriction on the opportunity for new growers to enter into the Western Australian industry'. The NCC ruled that ultimately the first right of refusal provision does not directly restrict entry into the chicken growing industry, as processors are free to not renew or cancel contracts with an existing grower.

In the 2004 NCP review, the WA Government justified retaining the first right of refusal regulation by arguing that it benefited the community by allowing for the development of a more efficient industry structure. It was suggested that such benefits were evident with WA having the highest average chicken farm size nationally and a high concentration of efficient growers in close proximity to processors. However, the NCC highlighted that barriers to entry usually result in lower rather than higher levels of production efficiency, and that the WA Government had failed to show why the chicken meat industry was 'different' and hence why efficiency was not constrained.

Given that compliance with NCP legislative reforms have removed most of the functions of the Act and have reduced the responsibilities of the Committee, it is considered important that the ERA investigate:

- whether the Act is generally resorted to by both the growers or processors of chicken meat;
- if there is a need for the Committee to determine an average price for broiler chickens. If so, is the model that calculates this price appropriate and is this price referred to in negotiations between growers and processors?; and
- whether the Act promotes an efficient industry structure, as highlighted in the 2004 NCP assessment.

MARKET FAILURE

Identifying Market Failure

Markets should not be regulated unless there is evidence of market failure. There must also be sufficient evidence to demonstrate that the regulatory solutions implemented by government can adequately address the market failure.

In assessing both of these issues it is considered important that the ERA examine, in particular, the following:

- is there any evidence to support the assertion that a processor has excessive market power and misuses that power, such that they are earning above-normal profits?
- is each stage in the vertically-integrated supply chain contestable? If there is no evidence to suggest that significant barriers to entry exist, then it is difficult to justify market power concerns.
- if there are barriers to entry what appropriate mechanisms, for example, legislative tools are available to make the relevant market more contestable?

Further investigation by the ERA will ideally determine whether the chicken meat industry should be regulated and whether these regulations adequately resolve the market failure.

Existing Protection from Market Failure

There are other mechanisms available to ensure that growers are not taken advantage of due to their lack of market power. Provisions within the *Trade Practices Act 1974* (TPA) must be complied with to ensure the welfare of consumers by promoting competition, fair trading and providing for consumer protection.

Negotiation of contracts between growers and processors, as prescribed under the Act, is a key focus of the ERA's Inquiry. The TPA recognises that small businesses (such as growers) are often more likely to have some influence over the terms and conditions in their contracts if they join with other small businesses to collectively negotiate with a larger business (such as processors), rather than individually. Section 88 of the TPA allows for collective bargaining agreements between growers and processors to be established. These collective agreements are overseen by the Australian Competition and Consumer Commission (ACCC) to ensure that they do not limit competition or pose a barrier to entry. Increasingly, it would appear that growers in other jurisdictions are relying on collective bargaining agreements, which have been approved by the ACCC.

Specific provisions in section 46 of the TPA are in place to prevent powerful players from abusing their market power. The TPA stipulates that a corporation with a substantial degree of market power is prohibited from taking advantage of this power to eliminate or damage an actual or potential competitor, prevent the entry of a person into any market, or deter or prevent a person from engaging in competitive conduct in any market.

Section 50 of the TPA prohibits acquisitions that would result in a substantial reduction in competition. Section 50(3) stipulates that the ACCC should determine whether an acquisition will have an effect on competition with the assistance of a non-exclusive list of matters which “must be taken into account” in determining whether an acquisition is likely to substantially lessen competition in the market.

Given these provisions in the TPA, it would be of interest for the ERA to investigate whether the combination of:

- countervailing powers through a collective agreement sanctioned by the ACCC; and
- specific provisions under sections 46 and 50 of the TPA;

provide sufficient protection to growers such that state based regulation (with its unintended consequences) would be unnecessary.

CONCLUSION

The ERA's proposal to further examine the justification for, and unintended consequences of, regulation and the need for any intervention into the WA chicken meat industry is supported. It is particularly important for the ERA to investigate the issue of market failure, specifically the presence and use of market power in the chicken meat industry in WA. Investigation by the ERA will ideally determine whether asymmetric market power exists in the chicken meat industry, and hence whether the industry should be regulated.

