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Reference "NZTGA Provisional Authorisation"

This letter sets out Van Den Brink Poultry Limited's submissions in relation to the New Zealand Tegel Growers Association's ("**TGA**"):

- Application for Authorisation of a Restrictive Trade Practice ("**Authorisation Application**"); and
- Application for Provisional Authorisation of a Restrictive Trade Practice ("**Provisional Authorisation Application**").

For the reasons outlined below, we are very strongly opposed to TGA's Authorisation Application for the Proposed Arrangements (as defined in paragraph 1.19 of TGA's Authorisation Application). In particular, we do not believe it is appropriate for the Commerce Commission to grant authorisation for TGA, on behalf of its members, to collectively discuss and negotiate with Tegel Foods Limited ('Tegel') growing fees and other terms and conditions of its members' chicken growing contracts with Tegel for a period of ten years. The Proposed Arrangements will not result in a net public benefit that outweighs the lessening of competition likely to result from the Proposed Arrangements.

As we do not consider that the Commerce Commission should grant authorisation for the Proposed Arrangements, it follows that we also oppose TGA's Provisional Authorisation Application.

Proposed arrangements likely to result in increased costs for end consumers

In TGA's Authorisation Application, it submits that "would not result in any detriment of losses in allocative efficiency resulting from higher consumer prices for chicken". In our view, TGA has not provided sufficient rationale to support this statement. In contrast, we consider that the granting of an authorisation or provisional authorisation for the Proposed Arrangements will increase the price of chicken for the end consumer. If an authorisation or provisional authorisation is granted, TGA will be able to exert inappropriate price pressure on Tegel. The costs of growing services across all growers will ratchet up, which is unjustified as growers have different cost structures, and each grower represents a different cost/benefit to Tegel. Accordingly, Tegel will have no option but to pass on the increased costs to its trade customers through a price increase. To retain their margin, Tegel's trade customers will then increase their price to the end consumer. Therefore, to the extent that there are any benefits TGA claims will arise out of the Proposed Arrangements eventuate, these will be outweighed by the likelihood that the cost for the end consumer will increase.

Authorising a cartel is inappropriate

We submit that granting authorisation or provisional authorisation for TGA, on behalf of its growers, to discuss and negotiate with Tegel growing fees and other terms and conditions of its members' chicken growing contracts with Tegel as though they are one grower is inappropriate for the following reasons:

1. No two growing farms are the same, due to the level of investment made by the grower, the scale of the grower's farm (i.e. a small farm could have 3 small sheds, a large farm 10 large sheds), and the cost per chicken the grower incurs to supply chicken rearing services (i.e. larger farms have economies of scale). The grower's resulting cost structure is something that will impact any growing services agreement made with Tegel. Each grower's cost structure will be different.

2. Tegel's total cost per chicken from each grower will be different, due to the 'cost to serve' that it incurs for each respective grower. Tegel's cost to serve is impacted by the scale of the grower's farm (i.e. how cost effective it is to catch chickens per collection visit), the grower's mortality rate, the proximity of the grower to the processing plant (i.e. transport costs), and how much support from Tegel's agricultural team is required to address problems that arise with the chickens.

3. Regional land prices and labour rates differ dramatically from region to region. A farm located in Auckland will have a land price considerably higher than a farm located in Taranaki or Canterbury, and its labour rates will also be higher (i.e. due to the higher cost of living in Auckland).

4. In some regions (e.g. Auckland, Waikato and Canterbury) there are at least two chicken processing companies operating. This means that, if growers are unhappy with the terms of their supply agreement with Tegel, they may be able to change the company they supply growing services to. For example, in the last few years several of Ingham's growers have terminated their services agreements with Ingham's and begun to supply to Tegel.

Cartel not contemplated by existing services agreements

In good faith, Tegel entered into a supply of chicken growing services agreement with each individual grower. The terms of each agreement were agreed upon by both parties. To subsequently allow individual growers to band together and form a cartel to negotiate on key terms of an individual services agreement would be an unfair, unilateral decision in favour of one party. Accordingly, the formation of a cartel should remain a banned, restrictive trade practise.

Tegel should retain the prerogative to choose whether it negotiates with a collective of growers or not.

Wealth transfer will not result in a public benefit

TGA describe a public benefit of being able to form a cartel as (in clause 1.24 of their Authorisation Application):

> *"Any wealth transfer from Tegel to growers that results from collective bargaining constitutes a public benefit because Tegel is foreign owned. Although there are difficulties in estimation, Castalia estimates that the authorisation would lead to a public benefit of up to [ ] through a wealth transfer to growers. (This is perhaps more correctly viewed as the prevention of a wealth transfer from growers to Tegel's shareholders that would otherwise occur in the counterfactual)."*

To the extent that the Commission accepts that a wealth transfer from Tegel to growers resulting from collective bargaining is a public benefit, the Commission will also consider any effects outside New Zealand that may ultimately feed back to New Zealand. Tegel's shareholders, who the growers are dependent on, took considerable risk when they invested in Tegel in 2018. Shareholders need to make a profit to remain viable and to be able to trade through crises like Covid-19 and Infectious Bursal Disease ('IBD'), both of which Tegel's shareholders encountered within 15 months of acquiring the company. IBD resulted in Tegel losing its export business from October 2019 through to June 2021. This represents a very large financial cost to the shareholders and it will take them many months to rebuild this significant part of their business. To the extent that the Commission accepts that the Proposed Arrangements will result in a wealth transfer that is of benefit to New Zealand, it should also consider the detriment that would arise for both the growers and New Zealand more generally if Tegel was not financially successful and shut its doors.

Conclusion

We are strongly opposed to TGA being granted authorisation or provisional authorisation for the Proposed Arrangements, in particular for TGA to, on behalf of its members, collectively discuss and negotiate with Tegel growing fees and other terms and conditions of its members' chicken growing contracts with Tegel for a period of ten years.

We consider that there is a high risk that any increased costs that Tegel faces as a result of such collective bargaining will be ultimately passed on to the end consumer. TGA has not sufficiently addressed this potential detriment in its Authorisation Application or Provisional Authorisation Application.

In good faith, Tegel entered into individual chicken growing contracts with its growers, and its growers accepted the terms of those agreements. It should therefore remain Tegel's prerogative to decide whether or not it wants to negotiate with a group of growers.

The apparent public benefits arising from wealth transfers described in TGA's application are not quantifiable and, as highlighted above, disregard the financial burden that Tegel carries in its relationship with growers. It is in Tegel's interest to ensure that its growers remain financially viable. This can be achieved through the terms of the 'free market' supply of growing services agreements currently in place, without the need for a 'restrictive trade practice' such as the proposed TGA cartel to be authorised or provisionally authorised.

Yours sincerely

Michael Sheridan
Chief Executive Officer
Van Den Brink Group