Public benefits and detriments of collective bargaining by Tegel's chicken growers

Prepared for the New Zealand Tegel Growers Association

by Emma Ihaia

2 SEPTEMBER 2021

Table of contents

Tables

Definitions

ACCC	Australian Competition and Consumer Commission
CPI	Consumer Price Index
[	]
FMA	Farm Management Agreement
NPV	Net Present Value
NZTGA	New Zealand Tegel Growers Association
R&M	Repair and Maintenance
TSS	Tegel Shed Standard

Executive summary

This report examines the public benefits and detriments associated with the collective activities that would be permitted under the authorisation sought by the New Zealand Tegel Growers Association (NZTGA). The permitted activities would allow growers to collectively negotiate with Tegel, discuss and exchange information with other growers on matters relating to negotiations with Tegel, enter into agreements that are collectively negotiated, and implement collectively negotiated agreements.[1]

We find that the benefits of the authorisation are highly likely to outweigh the detriments.

The relevant markets for chicken growing services

We find three relevant geographic markets for the supply of chicken-growing services: Auckland, Taranaki, and Canterbury. We define these markets as being within two hours' drive of the Tegel processing factories due to animal welfare impacts of transporting the chickens.

Chicken farms require specialised shedding, which means that their services fall into a separate market from other farming types.

The relative bargaining power of Tegel and the growers

The limited number of chicken processors and the need to make significant [ ] investments that conform to the specific shed requirements of Tegel all create an imbalance of bargaining power between individual chicken growers and Tegel. Growers face the risk that their investments will be stranded if they are unable to secure a supply arrangement with Tegel. As a result, Tegel hold strong buyer power in negotiating with chicken growers.

Collective bargaining shifts the imbalance of bargaining power to some extent by enabling growers to pool resources and engage specialised staff to negotiate with Tegel. However, Tegel is likely to retain significant bargaining power in the negotiations, as the growers still require a supply agreement with Tegel to recover the cost of their investments.

If an authorisation is granted to allow collective activity to continue, payments from Tegel to growers may be somewhat higher than if the authorisation is not granted, however the difference is likely to be limited.

Collective bargaining provides transactional cost savings

We estimate that collective bargaining between NZTGA and Tegel would result in transactional cost savings in the range of $1.4 million to $3.1 million over the ten-year period of the proposed authorisation. These costs savings arise because collective activity avoids bilateral negotiations between each individual grower and Tegel, including bilateral negotiations for contractual disputes and contractual variations.

Collective bargaining by the NZTGA members is likely to have other efficiency benefits

Collective bargaining has resulted in a sophisticated agreement between Tegel and growers that is likely to have efficiency benefits.

In comparison to the short-term agreements with simple payment structures that were in place prior to collective bargaining, the current [ ] agreement provides [

[1] Further details of the proposed arrangements are described in NZTGA's authorization application.

] and a sophisticated payment structure. The payments specified in the collective agreement include a [ ]

[ ] reduces the risk to growers associated with making a significant specialised investment – for a new "greenfield" farm, a chicken grower would need to invest around [ ] million plus land costs to build [ ] to house the chickens. The sheds are built according to Tegel's specifications. By reducing the risk associated with this upfront investment, the agreement that has resulted from collective bargaining reduces the cost of providing growing services (by reducing the cost of capital), gives new growers the certainty that they need to invest, and gives Tegel the incentive to maintain or expand demand.

[ ] included in the agreement will have the effect of motivating growers to deliver high-quality growing services and [ ]

The authorisation will provide efficiency gains regardless of whether Tegel negotiates with the NZTGA

If the Commission authorises collective activity, Tegel may choose to continue to engage with NZTGA (as it has in the past) or it could instead choose to negotiate individually with growers. Regardless of which approach Tegel takes, we find that growers will act collectively, which will result in efficiencies. With growers working together to develop their positions and knowing what position each would be taking in bilateral negotiations, the outcomes would be similar to the situation where Tegel agrees to a collective negotiation. That is, the terms of individual contracts would be likely to be similar to what would be agreed through collective negotiation, the cost of preparing them would be similar to the costs under a collective negotiation approach, and the contract sophistication would also be comparable with that achieved through collective negotiations. [ ]

Wealth transfers to growers from collective bargaining result in a public benefit

If grower payments are higher with collective bargaining than without, then any wealth transfer from Tegel to growers that results from collective bargaining constitutes a public benefit because Tegel is foreign owned. It is difficult to estimate how grower payments would differ with and without collective bargaining. However, [ ] Using this information, we estimate that the authorisation would lead to a public benefit of up to [ ] through a wealth transfer to growers.

Collective bargaining is highly unlikely to result in allocative efficiency losses

If collective bargaining leads to higher payments from Tegel to growers (relative to a state without collective bargaining), and Tegel passes on the reduction though lower wholesale prices, the change in prices per bird will not be significant enough to result in a demand expansion. We estimate that the maximum reduction in grower payments if the authorisation is not granted is [ ] cents per bird**.** Even if this were passed on in the form of lower wholesale prices, such a limited price change is highly unlikely to drive an expansion in demand

and, as a result, Tegel would have limited incentives to reduce wholesale prices. **[**

]

The public benefits of the authorisation are highly likely to outweigh the detriments

In summary, we find that the public benefits of the authorisation is highly likely to outweigh the detriments because:

- collective bargaining provides transactional cost savings, including in the negotiation of contractual variations and contractual disputes,
- collective bargaining allows for a more efficient contract than would occur without the authorisation,
- if payments are higher with collective bargaining, then the wealth transfer from a foreign-owned company (Tegel) to chicken growers would provide a public benefit, and
- any difference in the level of payments to growers between the scenarios with and without the collective is unlikely to be passed on to end consumers, and even if it was, is so small that it would not drive a significant change in allocative efficiency.

Our conclusions are consistent with prior decisions by the Commerce Commission and the ACCC

Our conclusion that the public benefits of collective bargaining are likely to outweigh the detriments is consistent with previous authorisation decisions made by the Commerce Commission and the Australian Competition and Consumer Commission (ACCC)

In 2017 the Commerce Commission authorised an application by the Waikato-Bay of Plenty Growers Association to engage in collective bargaining with Inghams. The ACCC has authorised similar chicken growing collective arrangements in Australia, where it highlighted that collective bargaining can lead to more efficient agreements.

In addition, the ACCC has recently introduced a class exemption that allows collective negotiation without first having to seek approval. The class exemption applies to businesses and independent contractors who form, or are members of, a bargaining group and who each had a turnover of less than $10 million in the financial year before the bargaining group was formed.

1 Introduction

The New Zealand Tegel Growers Association Incorporated (NZTGA) has asked Castalia to examine the public benefits and detriments associated with collective activity that would be permitted under an authorisation sought by NZTGA members. If granted, the authorisation would allow growers to collectively discuss and negotiated with Tegel, discuss and exchange information with other growers matters relating to negotiations with Tegel, enter into agreements that are collectively negotiated, and implement collectively negotiated agreements.[2]

In this report, we first briefly describe the roles of the chicken growers and processors and summarise the existing collective agreement that specifies the terms on which chicken-growing services are provided (Section 2). We then assess the public benefits and detriments of collective activity (Section 3) by identifying the relevant markets, examining the relative bargaining power of the parties with and without the proposed authorisation, assessing likely outcomes in the factual and counterfactual scenarios, and considering efficiency gains and losses of the collective activity that would be permitted under the authorisation. Finally, we provide some concluding remarks (Section 4).

2 Context

Tegel outsources the growing of broiler chickens to independent chicken growers. Tegel provides the chicks, as well as feed, medication, litter material and cleaning services.

The NZTGA has previously negotiated with Tegel on behalf of the growers that are members of three regional associations in the Auckland, Taranaki, and Canterbury regions. The resulting collective agreement has a total term of [ ] and includes payments to compensate growers for [ ]

The NZTGA is seeking authorisation from the Commerce Commission to continue to collectively negotiate on behalf of NZTGA members and, more generally, to continue to support its members to negotiate effectively with Tegel.

2.1 Overview of the chicken growing and processing businesses

2.1.1 Tegel is the largest chicken processor in New Zealand

Tegel processes more than 50 per cent of chicken meat produced in NZ. The company is fully owned by the Philippines poultry company Bounty Fresh Foods, through Bounty Holdings New Zealand Limited (BHNZL). BHNZL's revenue was $602 million in the 12 months to December and $638 million in the previous year.[3]

---

2 Further details of the proposed arrangements are described in NZTGA's authorization application.

3 Bounty Holdings New Zealand Limited Annual Report for the year ended 31 December 2020.

Inghams is the second-largest chicken processor in New Zealand, with revenues of $385 million in the 2020 financial year.[4] Van den Brink Poultry Limited (Brinks) is the third-largest chicken processor in NZ and is a private company.

Tegel, like other chicken processors in New Zealand, outsources the growing of broiler chickens to independent chicken growers. Tegel has a hatchery in each of the three regions in which it operates major chicken processing facilities (Auckland, Taranaki and Canterbury). From those hatcheries, Tegel supplies the growers with day-old chicks, and provides the necessary feed, medication, litter material and cleaning services.

2.1.2 Chicken growers rear Tegel's broiler chicks for meat production

Approximately 100 farms grow Tegel's broiler chickens.[5] These growers rear the chickens in accordance with Tegel's specifications. Growers provide specialist shedding as well as labour and management expertise. The chicken-growing farms are typically owner-operated, with some of the larger farms employing one to three staff.

Tegel supplies feed, fresh bedding material, cleaning, shed sanitation and litter removal services. The growers pay for operating expenses such as gas and electricity, but these are largely passed through at cost to Tegel.

Tegel delivers day-old chicks to the growers for rearing. However, Tegel retains ownership of the chickens while they are at the growers' premises. Once the chickens have reached the required weight, Tegel collects the chickens from the growers and transports them to its local processing facilities. Farms are located close to the processing plants because of animal welfare considerations relating to the transportation of the chickens between the farms and the processing plants.

In addition to the land, the specialist shedding required is a significant investment for growers. For example, NZTGA estimates the cost of building a new chicken farm in line with Tegel's requirements to be approximately [ ] plus land cost.[6] Land requirements to meet boundary restriction criteria from neighbouring properties mean that new farms are typically a minimum of 25 hectares, whereas historically this was four hectares.

2.1.3 Distribution of processed chicken meat

Tegel's processed chicken meat is distributed through four key sales channels:[7]

- **Retail groceries**: supplied to the main supermarket chains as well as to independent butcheries and retailers
- **Quick Service Restaurants (QSRs)**: a range of fresh and frozen products are supplied
- **Food services/industrial**: includes hotels, restaurants, caterers, and distributors, as well as for the purpose of further processing for value-added products

4 Ingham's 2020 Annual Report.

5 We note that the exact number of members may vary over time. However, for the purposes of the calculations in this report, we have assumed an average of 100 growers.

6 [ ]

7 Tegel Annual Report 2018.

- **Export**: Tegel exports to Australia, the Pacific Islands, United Arab Emirates, Hong Kong and the Philippines. In 2018, Tegel's exports totalled $89.6 million, which was equivalent to 16% of Tegel's revenue from domestic and exported poultry products.

2.1.4 Tegel has made losses in the last two years

Financial statements for BHNZL show that Tegel made losses for each of the last two years – in the 12 months to December 2020, BHNZL made a loss of $25 million, and for the prior year the loss was $90 million.[8] The discovery of a poultry virus in Otago hen farms in 2019 meant that Tegel was unable to export chicken meat to Australia. Tegel estimated at the time that it would lose $60 million to $70 million annually while the ban was in place.[9]

2.2 NZTGA and the collective agreement

The NZTGA was formed in 2006, and its current membership comprises:

- The Canterbury Poultry Meat Producers' Association Incorporated
- Auckland Meat Chicken Growers Association Incorporated
- Taranaki Broiler Growers Association Inc.

Between them, these three associations represent around 100 individual growers.

2.2.1 NZTGA has previously negotiated with Tegel on behalf of the members of three regional associations

One of the objectives of the NZTGA (as set out in its rules of association) is to carry out negotiations with Tegel. The relevant negotiations cover the Farm Management Agreement (FMA), and any changes to the terms and fees. Negotiations have been led through the NZTGA, with matters for decision being taken to each regional executive and then to their full regional grower meeting.

Negotiation through the NZTGA has resulted in significantly lower negotiation costs, both for Tegel and the growers. (For our estimates, see section 3.5.1).

NZTGA does not require that its members adopt the collective agreement. Members can choose to negotiate directly with Tegel instead.

The Association's role extends beyond negotiation with Tegel. Other objectives of the NZTGA are to "obtain and disseminate information regarding new techniques, procedures and practices in relation to best practice for the production of meat chickens."[10]

2.2.2 Obligations of Tegel and growers under the FMA

Tegel's obligations

The FMA requires that Tegel provides day-old chickens, fees for medication and vet care, cleaning services, bedding material, advisory services, pickup and drop off, and local government resource consent assistance. The FMA also requires that Tegel must

---

8 Bounty Holdings New Zealand Limited Annual Report for the year ended 31 December 2020.

9 https://www.stuff.co.nz/business/117136975/tegel-losing-millions-after-virus-discovery-shuts-down-australian-export-market

10 Rules of the New Zealand Tegel Growers Association Incorporated, clause 18(c).

provide reasonable endeavours to ensure Tegel growers have the same opportunity to earn similar net income per square meter as other growers in the region.

Grower obligations

The grower is responsible for internal roading, water quality and supply, internal shed environmental conditions, litter management, labour, and sheds, and is required to have insurance. The grower must exclusively use Tegel for supply.

2.2.3 Payments specified in the FMA

[

]

3 Assessing public benefits and detriments

To assess the public benefits and detriments associated with collective bargaining, we:

- Identify the relevant markets,
- Assess the relative bargaining power of chicken growers and Tegel in those markets, in the scenarios with and without collective bargaining,
- Identify the relevant factual and counterfactual scenarios,
- Quantify the transactional cost savings associated with collective bargaining and identify other efficiencies,
- Examine the wealth transfer that results from any difference in payments between the factual and the counterfactual, and
- Consider how allocative efficiency is affected by collective bargaining.

3.1 Relevant markets

We find that the relevant markets are for broiler chicken growing services in each of the three regions served by members of NZTGA (Auckland, Taranaki and Canterbury).

3.1.1 Other farming services are not close substitutes

Tegel has specific requirements for growing sheds that would not be satisfied by structures on other types of farms. In other words, services provided by other types of farms would not provide a sufficient close demand-side substitute to fall in the same market as chicken growing services.

Regarding supply-side substitution, a farmer of other animals would need to make significant investments in order to supply chicken growing services to Tegel, given the specific growing shed requirements.

As a result, we would not expect significant demand or supply-side substitution to occur in response to a small but significant and non-transitory increase in the price of broiler chicken grower services by a hypothetical monopolist. Therefore, we conclude the relevant markets includes broiler chicken growing services, but not other farming services.

3.1.2 The geographic markets are shaped by animal welfare considerations

As the Commission explained in Determination NZCC37:

> *Animal welfare considerations mean that broiler chickens are not transported long distances from the growing farm to the processor, which tends to limit the extent of the geographic market. As a result, growing farms located more than a two hour drive from a processor are not typically effective substitutes for nearby farms.*[11]

As a result, we find the following relevant markets:

- A market for the supply of broiler chicken growing services in Auckland, encompassing the area that is within two hours' drive of the Tegel processing factory in Henderson,
- A market for the supply of broiler chicken growing services in Taranaki, encompassing the area that is within two hours' drive of the Tegel processing factory in New Plymouth, and
- A market for the supply of broiler chicken growing services in Canterbury, encompassing an area that is within two hours' drive of the Tegel processing factory in Hornby.

3.2 Bargaining power in the relevant markets

Growers make a significant investment in shedding required to provide growing services to Tegel and need to secure an agreement with Tegel to fully recover costs. As a result, Tegel holds strong bargaining power relative to individual growers.

With collective bargaining, growers pool their resources to negotiate a collective agreement, which may reduce the imbalance of power to some extent. However, as growers still require a supply agreement with Tegel to avoid stranded assets (and are not seeking an authorisation to collectively boycott) Tegel will retain significant bargaining power even if the authorisation is granted.

3.2.1 Without collective bargaining

Tegel has monopsony power for growing services provided by most NZTGA members

NZTGA members face limited options in terms of the processors they can supply. In Taranaki, growers have no other processor other than Tegel to whom they can sell broiler chicken grower services. In Auckland and Canterbury, growers may have the option to switch to supplying Brinks, but this option is likely unviable. [

[11] NZCC, pp 11-12.

]

We understand from NZTGA that in recent years no farmers have switched from supplying Tegel to supplying Brinks. We note that four of the farms that supply Tegel are based in the Waikato and could potentially supply Inghams, however these farms are a minority.

In some areas Tegel has options to acquire growing services from non-NZTGA growers

In some areas, a bilateral monopoly exists (Taranaki), while in others Tegel could potentially acquire growing services from growers that currently supply other processors.

Tegel, given the specific requirements for shedding, may prefer to acquire services from growers that already supply Tegel. However, in some areas Tegel could choose to accept growers from other processors. As noted above, we understand that four growers switched from Inghams to Tegel in 2018.

The hold-up problem provides Tegel with strong bargaining power

Growers make significant long-term investments that are specific to raising broiler chickens and meeting Tegel's required standards. As a result, growers face the risk that their assets will be stranded if they are unable to secure a supply arrangement with Tegel. This hold-up problem results in an imbalance of bargaining power in favour of Tegel for existing growers and can lead to under-investment by potential new growers. Effectively, the value to an individual grower of obtaining a contract with Tegel exceeds the value to Tegel of contracting with an individual grower. Currently [

]

As the Commission has previously commented, chicken processors (like Tegel) "dictate the terms on which chicken growers provide services."[12]

3.2.2 With collective bargaining

Collective bargaining does not remove the hold-up problem

Collective bargaining shifts the imbalance of bargaining power to some extent by enabling growers to pool resources and engage specialised staff to negotiate with Tegel. Even so, given that there is no boycott activity sought in the authorisation, Tegel is likely to retain significant bargaining power in negotiations, as growers need to recover the costs of the significant and specific investments they make in meeting Tegel's shed standards.

In Australia, despite the presence of collective bargaining the ACCC identified significant concerns with contract terms in the chicken meat industry. This finding prompted the ACCC to announce in December 2020 that it will further investigate potential unfair contract terms.[13] This finding indicates that collective bargaining does not fully address the imbalance in bargaining power between growers and processors.

[12] Commerce Commission Decision 658 (2008) at 236 and 237.

[13] ACCC, *Perishable agricultural goods inquiry*, 10 December 2020

While collective bargaining may somewhat increase the payments available to chicken growers, it seems unlikely that chicken growers will earn significantly more with collective bargaining than it would if an authorisation were not granted.

3.3 Counterfactual scenario (authorisation not granted)

We find that without an authorisation, the FMA will unlikely persist in its current form and would be replaced by a simpler agreement that is individually negotiated but based on a standard form agreement.

The Commission has previously indicated that it would not investigate the existing collective agreement, but that further collective negotiation would require an authorisation. As a result, we assume that the collective agreement (the FMA) would remain valid even if an authorisation for further collective negotiation is not granted. However, the costs and delay of amending, maintaining and applying the contract through individual negotiation means that the FMA is unlikely to be workable in the counterfactual.

Instead, a simpler, shorter-term contract that is individually negotiated is more likely to prevail. Contracts that are individually negotiated are likely to be shorter than the existing contract, reflecting Tegel's stronger bargaining power in the counterfactual. [

]

The collective agreement is unlikely to persist without the authorisation Without an authorisation, necessary variations to the agreement cannot be negotiated collectively

Without an authorisation, any contractual issue that arises with the FMA could not be addressed through collective negotiation. Tegel previously negotiated with the collective through NZTGA to achieve a 2017 variation to the FMA.

Examples of the types of contractual issues that would need to be addressed in future include:

- **Amending the contract to clarify unclear clauses**: For example, [

  ] However, negotiating amendments individually with each grower would be costly, reducing Tegel's incentive to improve the contract. Even if Tegel negotiates individually, it may end up with different amendments for different growers, which would then increase the cost of maintaining the contract going forward. Moreover, growers may be reluctant to agree to amendments without the reassurance that the NZTGA has reviewed the changes.

- **Amending the contract to reflect changed circumstances: [**

]

In future, changes that may trigger the need for contract amendments include:

- Changes in economic conditions, trading conditions, or both,
- Changes in requirements by wholesale customers,
- New Tegel shed standards, and
- Animal welfare matters.

[

]

Without the authorisation, individual negotiation to agree on variations to the contract will be time consuming and costly for both Tegel and growers and may result in different variations being agreed with different growers. Some efficiency-enhancing amendments to the FMA that would occur with the authorisation would not occur in the counterfactual.

The sophistication and complexity of the FMA means that it requires substantially more administration and maintenance than a simpler contract. NZTGA meets routinely with Tegel to engage with Tegel on the growers' behalf to discuss matters relevant to the chicken growing services, including discussions on contractual matters such as [

][14]

Without the authorisation, Tegel would need to engage with individual growers to address these types of issues. Doing so would be significantly more costly than addressing the issues with the collective. [ ] is an example of the types of issues that arise with a complex agreement.

Currently, the FMA exists in a context where growers can engage collectively with Tegel. However, without an authorisation the agreement is unlikely to be workable.

Without an authorisation, the existing FMA would likely be unstable

The increased costs of implementing, maintaining, and amending the contract without the authorisation provide Tegel with less incentive to retain the FMA, because it may be able to achieve lower pricing through individual bargaining. This will likely make the current contract unstable. For example, [

]

[14] See paragraph 8.33 (e) of the NZTGA's application for an authorization.

If the FMA is not renewed for some growers, any continued supply to Tegel by those growers would require individually negotiated agreements

[

3.3.1

] The individual agreements are likely to be simpler and shorter than the FMA

A complex agreement is unlikely to be practicable without an authorisation for collective activity. As a result, a simpler form of agreement is likely to be put in place.

The new individual agreements are likely to have shorter terms, reflecting that (1) without collective bargaining Tegel is in a stronger bargaining position, and (2) longer term agreements would typically need to be more complex in order address a range of circumstances that may arise over the term of the agreement.

We understand that prior to collective bargaining by the NZTGA, grower contracts had a simple payment structure and that the term of the agreement was two to three years. Individual agreements in the counterfactual may not be as simple as the agreements that existed before the FMA, as they can adopt some aspects of the contract that were developed collectively. However, over time, individual contracts will likely evolve towards a simpler form.

3.3.2 Grower payments in the counterfactual

[

]

Growers have varying circumstances, which may lead to individual growers accepting a variety of different price terms. While economic modelling could be used to estimate prices that growers may be willing to accept, the modelling would rely on a range of assumptions. [

]

3.4 Factual scenario (authorisation is granted)

In the factual scenario, Tegel may choose to continue to engage with NZTGA (as it has in the past) or it could instead choose to negotiate individually with growers. Regardless of which approach Tegel takes, we find that growers will act collectively.

3.4.1 Collective activity will occur in the factual scenario, regardless of whether Tegel engages with NZTGA

We examine two possible factual scenarios: Factual 1 where Tegel negotiates with NZTGA and Factual 2 where Tegel chooses not to negotiate with a collective and instead negotiates with each individual grower.

In the past, Tegel has negotiated with the NZTGA, and has indicated that it would support an authorisation application by NZTGA members. [

]

Factual 1 – Tegel negotiates with NZTGA If Tegel does choose to continue to engage with NZTGA, the FMA would remain in place, but would likely be amended in at least two ways. Firstly, the price terms may be renegotiated to account for changes in market conditions. Secondly, unclear clauses would be amended to improve clarity [

]

As discussed in section 3.2.2 above, collective bargaining does not significantly change the bargaining position of growers relative to Tegel. Therefore, we would not expect a significant difference between the price terms in the factual and the counterfactual. [

]

Factual 2 – Tegel does not negotiate with NZTGA

Alternatively, Tegel may refuse to negotiate with NZTGA if the Commission grants an authorisation. In this scenario, growers will likely still share information and act collectively, given the large cost savings that they can achieve through coordinating. This situation will achieve many of the benefits of collective bargaining while not requiring Tegel to engage with the collective. With growers working together to develop their positions and knowing what position each of the other growers will take in bilateral negotiations, the outcomes would be similar to the likely outcomes if Tegel had agreed to collective negotiation. That is, all individual contracts would be similar to the contracts that would result from collective negotiation, the cost of preparing them would be similar to the cost under a collective negotiation approach and the contract sophistication would also be similar as with collective negotiation.

[

]

The ACCC has recognised that collective bargaining can still provide public benefits, even if the other bargaining party refuses to engage with the collective. For example, the ACCC granted an authorisation in 2020 to enable the NSW Minerals Council and coal producers that export coal through the Port of Newcastle to collectively negotiate with Port of Newcastle Operations Pty Ltd (PNO) on the terms and conditions of access to the Port, even though the PNO submitted that it would not participate in collective negotiations. The ACCC's reasoning included that even if the PNO did not engage with the bargaining group, the members of that bargaining group would have greater input into the terms and conditions of any agreements, than they would without collective bargaining, and industry-wide issues would be resolved more quickly.[15]

Although Factual 2 is a possibility, we adopt Factual 1 for the remainder of our analysis. We adopt Factual 1 because Tegel has negotiated collectively with NZTGA to date, and [

] In any case, we do not expect that the benefits and detriments would differ materially between the Factual 1 and Factual 2.

3.5 Benefits and detriments of collective activity

We estimate that collective negotiation provides public benefits of:

- In the range of $1.4 million to $3.1 million (Net Present Value), of transactional cost savings

[15] ACCC Determination on Application for authorisation AA1000473 lodged by NSW Minerals Council and mining companies to collectively negotiate with Port of Newcastle Operations Pty Ltd all terms and conditions of access relating to the export of coal from the Port of Newcastle, 27 August 2020, Authorisation number: AA1000473.

- Up to [ ] per year through a wealth transfer from Tegel's foreign owners to New Zealand chicken growers, and
- Efficiencies from enabling and supporting more sophisticated contractual arrangements than would occur with individual negotiation

We find that allocative efficiency losses are highly unlikely to be significant because prices for chicken meat will not be significantly lower in the counterfactual than in the factual.

3.5.1 Public benefit from transactions cost savings

The total contract negotiation costs of a collective agreement will be lower than the total costs of negotiating the contracts with individual growers. Table 3.1 contains indicative estimates of the ten-year NPV of the collective agreement and the individual agreement. We estimate that the collective agreement is likely to result in transaction cost savings of approximately $1.4 million to $3.1 million over the ten-year period of the proposed authorisation. The lower end of the range estimates the transaction cost savings if the existing agreement remains in place in the counterfactual for a period of 5 years and individual contracts are then negotiated. The upper end of the range estimates the cost savings where the existing agreement is replaced upfront with individually negotiated contracts that have a term of three years.

Table 3.1: Estimate of contract negotiation costs

	Individual negotiation (summed across NZTGA members) in the counterfactual – 3 year contract term	Individual negotiation (summed across NZTGA members) in the counterfactual – negotiated 5 years from the authorisation decision	Negotiation costs in the factual
Cost of negotiating agreement	[ ]	[ ]	[ ]
Annual cost of maintaining agreement	[ ]	[ ]	[ ]
10-year NPV including upfront negotiation costs of collective agreement	$4,041,000	$2,235,000	$679,000

As is discussed in section 3.5.3, the collective agreement will likely be considerably more sophisticated than the agreement that would be adopted without collectively bargaining. As a result, the costs of negotiating and maintaining the collective agreement (including variations to the agreement and negotiation of contractual disputes) will be higher than the costs of a single agreement with individual chicken growers. However, when summed across all NZTGA growers, the total costs of individual negotiations are considerably higher than the costs associated with the collective agreement.

We used the assumptions listed below to produce the contract negotiation cost estimates contained in Table 3.1.

Transaction costs in the factual:

In the factual, we assume that NZTGA collectively negotiates an updated agreement with Tegel after the authorisation. The update would allow the parties to amend clauses in the existing agreement that are unclear and could give rise to future disputes. [

] We estimate the upfront costs of updating the FMA, including in-house hours of NZTGA and Tegel, and external legal fees.

We estimate annual costs in the factual by estimating the annual hours spent by NZTGA reviewing and implementing the agreement based on information provided to us by NZTGA. We assume that Tegel spends the same amount of time annual on similar activities. We also estimate the annual legal advice costs to NZTGA and Tegel.

We use the following assumptions:

- [
-
-
-
-
-]

Transactions costs in the counterfactual:

We estimate annual costs in the counterfactual by estimating the annual hours spent by each individual grower and by Tegel to review and implement individually negotiated agreements (including variations and contractual disputes). We estimate the hours required on the basis that the agreements would be much simpler than the existing FMA. We also make assumptions on the annual average legal costs of individual growers and Tegel.

We calculate costs for a scenario where the existing agreement remains in place for all growers initially, but that after five years individual contracts are negotiated and implemented. We separately calculate costs for the scenario where all growers move to individually negotiated contracts upfront and these contracts are renegotiated every three years. These scenarios both reflects our reasoning in section 3.3 that the collective agreement is likely to be unworkable without the authorisation due to the complexity and associated costs [
]

We estimate the costs of negotiating the agreements, including in-house hours of Tegel, hours required by each individual grower, and external legal and other professional fees. [

]

We use the following assumptions:

- [
-
-
-
  –

  [16]

  –

  –

  –]

We have calculated the NPV of the transaction costs savings using a discount rate of five percent, reflecting the default rate used by the Treasury.[17]

We note that if an alternate counterfactual is used where the existing FMA remains in place for the entire 10 years, the average annual costs of maintaining the contract would be significantly higher than the costs we have modelled due to the complexity of the FMA. Although we have not modelled that counterfactual because we find it implausible (for the reasons discussed in section 3.3), we expect that the transactions costs in the counterfactual would be significantly higher than in the factual.

3.5.2 Public benefit from wealth transfer

Tegel is foreign owned, which means that if payments from Tegel to growers are higher in the factual than the counterfactual, then any reduction in Tegel's profits and increase in growers' profits is a public benefit.

---

[16] https://www.payscale.com/research/NZ/Industry=Chicken_Egg_Production/Salary

[17] https://www.treasury.govt.nz/information-and-services/state-sector-leadership/guidance/financial-reporting-policies-and-guidance/discount-rates

Based on the discussion above in section 3.4, we find that a positive wealth transfer of up to approximately [ ]

3.5.3 Public benefit from more efficient contractual terms

As well as resulting in transactional cost savings, collective bargaining can lead to more efficient contracts than in the situation where chicken growers negotiate individually with the processor. Under collective bargaining, the growers can pool resources to fund specialist advisors and share information to develop more sophisticated and efficient contractual arrangements.

As identified by the ACCC in the *Baiada* decision:

> … collective bargaining may allow for more effective negotiation, where the negotiating parties have a greater opportunity to identify and achieve business efficiencies that better reflect the circumstances of both the Applicants and Baiada. Collective bargaining is likely to improve their input into contractual negotiations with processors to achieve more efficient outcomes.
>
> Collective bargaining is likely to enable members of the bargaining group to become better informed of relevant market conditions, which is likely to improve their input into contractual negotiations with processors to achieve more efficient outcomes.[18]

The current collective agreement (the FMA) is an example of how more sophisticated and efficient contractual arrangements can be negotiated by a collective. For example:

- [ ]
- The collective agreement helps to address the hold-up problem by reducing the risk to growers, thereby reducing the risk of under-investment.[19] If Tegel chooses to increase its supply of chicken meat and requires either existing or new growers to invest in more shedding, that investment is more likely to occur under the [ ] agreement that has been negotiated by NZTGA.
- [ ]

As discussed above, in the counterfactual the sophistication of the FMA is unlikely to be maintained, and over time the contract will evolve to a simpler form. In addition, efficiency-enhancing amendments are less likely to be made in the counterfactual than in the factual.

3.5.4 Allocative efficiency losses

Whether there are allocative efficiency losses will depend on:

- Whether the payments to growers in the counterfactual are lower than in the factual

[18] ACCC, Determination - *Application for authorization lodged by South Australian Baiada Growing Group in respect of collective bargaining with Baiada Poultry Pty Ltd*, 20 December 2017, para. 22-23.

[19] Ellingson, T. and Johannesson, M., *"Is there a hold-up problem?" Scandinavian Journal of Economics 106(3)*, 2004, 475-493.

- If payments are lower, then whether Tegel would pass those cost savings on in the form of lower wholesale prices, and
- Whether retailers then also choose to pass the lower wholesale prices on to consumers.

We estimate that the maximum reduction in payments per bird in the counterfactual as compared with the factual is [ ] cents per bird using the maximum payment reduction in the counterfactual of [ ]**.** This level of price reduction would be so insignificant that it would not result in a material expansion in demand. As a result, Tegel would have little incentive to pass lower grower fees on through lower wholesale prices.

Moreover, because Tegel has made losses in recent years and it is [ ], Tegel is highly unlikely to pass lower grower payments on in the form of lower wholesale prices.

4 Conclusions

We find that the benefits of collective bargaining are highly likely to outweigh the detriments.

Collective bargaining provides transactional cost savings but, more importantly, enables more efficient agreements. We also find that if the collective agreement results in higher grower payments than the counterfactual, then the wealth transfer from Tegel to growers is a public benefit.

Allocative efficiencies losses from collective bargaining are likely to be low. If grower fees are lower with individual bargaining and if these are passed on by Tegel in the form of lower wholesale prices (which seems unlikely), the effect on retail prices is likely to be very small.

Our conclusion that the public benefits of collective bargaining are likely to outweigh the detriments is consistent with previous decisions by the Commerce Commission and the ACCC.

The Commerce Commission authorised an application by the Waikato-Bay of Plenty Growers Association to engage in collective bargaining with Inghams.[20] The ACCC has authorised similar chicken growing collective arrangements in Australia finding a net public benefit. It has also highlighted that collective bargaining can lead to more efficient agreements.[21] In addition, the ACCC has very recently introduced a class exemption that allows collective negotiation without first having to seek ACCC approval. The class exemption applies to businesses and independent contractors who form, or are members of, a bargaining group and who each had a turnover of less than $10 million in the financial year before the bargaining group was formed.[22]

---

[20] *New Zealand Commerce Commission Determination Waikato - Bay of Plenty Chicken Growers Association Incorporated, 2017, NZCC 37*

[21] ACCC, Determination - Application for authorization lodged by South Australian Baiada Growing Group in respect of collective bargaining with Baiada Poultry Pty Ltd, 20 December 2017.

[22] https://www.accc.gov.au/media-release/collective-bargaining-by-small-business-facilitated-by-class-exemption

Appendix A: Expert Qualifications

Emma Ihaia (Lanigan), Castalia Director NZ & Pacific

Emma Ihaia is an economist with 25 years' experience in competition policy and regulatory economics. She has been retained as an expert in the context of competition assessments, merger analyses, legal proceedings, government reviews, and regulatory investigations and consultations.

Emma's experience in competition analysis includes:

- providing expert reports on multiple clearance applications in the New Zealand telecommunications sector,
- providing expert reports on buyer power in the context of New Zealand's grocery sectors,
- expert testimony and reports on price squeeze matters in New Zealand, Australia and Samoa,
- peer reviewing a competition analysis of the fuel market for a competition authority in the Caribbean,
- expert reports on non-discrimination in telecommunications markets, and
- assessing competitive neutrality in the New Zealand parcels market.

Emma has worked for several international economics consultancies, including CRA International and Concept Economics. Emma spent four years on the executive team of a New Zealand regional electricity and fibre network owner. Prior to joining Castalia, she was Director and owner of economic consultancy Link Economics.

Emma holds a Master of the Arts (First Class Honours) in Economics and a Bachelor of Arts (major in Economics, minor in Mathematics) from the University of Auckland.

Appendix B: Declaration made in accordance with the High Court's Code of Conduct for Expert Witnesses

I, Emma Jane Ihaia, of 23 Champion Terrace, Nelson, New Zealand declare that I have read the High Court's Code of Conduct for Expert Witnesses and have complied with it in preparing this report.

Signed:

Date: 3rd September, 2021

Castalia is a global strategic advisory firm. We design innovative solutions to the world's most complex infrastructure, resource, and policy problems. We are experts in the finance, economics, and policy of infrastructure, natural resources, and social service provision.

We apply our economic, financial, and regulatory expertise to the energy, water, transportation, telecommunications, natural resources, and social services sectors. We help governments and companies to transform sectors and enterprises, design markets and regulation, set utility tariffs and service standards, and appraise and finance projects. We deliver concrete measurable results applying our thinking to make a better world.

WASHINGTON, DC
1747 Pennsylvania Avenue NW, Suite 1200
Washington, DC 20006
United States of America
+1 (202) 466-6790

SYDNEY
Suite 19.01, Level 19, 227 Elizabeth Street
Sydney NSW 2000
Australia
+61 (2) 9231 6862

AUCKLAND
74D France Street, Newton South
Auckland 1010
New Zealand
+64 (4) 913 2800

WELLINGTON
Level 2, 88 The Terrace
Wellington 6011
New Zealand
+64 (4) 913 2800

PARIS
64-66 Rue des Archives
Paris 75003
France
+33 (0)1 84 60 02 00

Thinking for a better world.

enquiries@castalia-advisors.com
castalia-advisors.com