Food fight in Aisle 3: Grocers, suppliers clash over need for code of conduct in Canada

A fair practice rulebook for the grocery industry has worked in other jurisdictions but here it's a political hot potato

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Call for code of conduct as food fight between Canada's grocers and suppliers mounts. PHOTO BY ILLUSTRATION BY BRICE HALL/NATIONAL POST

Autumn is the arguing season in the Canadian grocery business. It's when supermarkets traditionally meet with their suppliers to negotiate product orders, going back and forth on fees, flyer sales, shelf placement, sales targets and late-delivery penalties.

This year, one of the key negotiations to watch involves Walmart Canada. The big-box chain infuriated its suppliers this summer by announcing new fees to help cover its $3.5-billion infrastructure upgrade. Those fees — 1.25 per cent charged on the costs of goods suppliers sell to Walmart, plus another five per cent on goods sold into its e-commerce channel — are set to start next week.

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Manufacturers have been pushing back in discussions with Walmart, but a common response has apparently been: "Pay it or don't ship," according to Food and Consumer Products of Canada (FCPC), a major industry association that represents supermarket suppliers.

"They're just digging in, which is really too bad," FCPC chief executive Michael Graydon said this week, though he added later that some of his members have found Walmart willing to provide "something in return" for the higher fees, including extra orders.

But the fees have set off something of a proxy war. The main grocers and food manufacturers have been reluctant to speak publicly about the mounting tensions in their sector, preferring to stand back and allow their respective industry associations to trade barbs.

On behalf of suppliers, FCPC has called the Walmart fees "diabolical" and warned that rising fees and fines are starting to threaten the future of manufacturing in Canada. Walmart declined to comment on "confidential business dealings," but repeated its refrain that its fees are fair and reasonable, since its $3.5-billion expansion will lead to higher sales for suppliers.

Shoppers leave a Walmart in Winnipeg. The big-box chain infuriated its suppliers this summer by announcing new fees to help cover its $3.5-billion infrastructure upgrade. PHOTO BY KEVIN KING/WINNIPEG SUN/POSTMEDIA NETWORK

FCPC, as well as the Canadian Federation of Independent Business, Canadian Federation of Agriculture and associations for dairy processors, bakers and small grocers, believe the ultimate solution is for the federal government to implement a grocery industry code of conduct that would lay out a set of fair business practices to guard against bully tactics, but the Retail Council of Canada — which represents the big grocers — said that could lead to higher profits for multinational food brands and higher prices for consumers.

In Canada's consolidated grocery market, suppliers say they have little choice but to accept what they believe is unfair treatment, including late payments, exorbitant listing fees to get product on shelves and fines for little delivery mishaps, unexplained charges and extended promotions on products that suppliers didn't agree to, but still have to pay for.

FCPC wants a code similar to a model used in the United Kingdom, which would require written, enforced contracts for all supply agreements — not always common in Canadian grocery — as well as rules against raising fees outside of contract negotiations.

Without a code, FCPC said, it's likely that the other, highly competitive supermarket chains in Canada will soon follow Walmart's lead, forcing more discounts from suppliers, squeezing margins, eating into budgets for innovation and factory upgrades, and, eventually, pushing major manufacturers to close their aging Canadian facilities and consolidate operations in the United States.

The Retail Council of Canada (RCC), which represents Walmart as well as the big three Canadian grocery chains — Loblaw Cos. Ltd., Sobeys' parent Empire Co. Ltd. and Metro Inc. — suggested that a code would add more obligations for grocers, putting them at a disadvantage in negotiations with massive consumer product companies including Kraft Heinz Co. and Coca-Cola Co.

Representatives for suppliers say the grocery code of conduct would enforce fair business practices, but grocery reps say a code would lead to higher prices for consumers. PHOTO BY POSTMEDIA NETWORK

"If (supplier) margins are going to be increased — and it seems that a lot of their focus is on margins — then either grocery margins will be squeezed or consumers will pay more," RCC spokesperson Karl Littler said.

"There's no question that the parties are looking at this from a different end of a telescope. Their argument is, 'Your moves hurt our margins.' And our argument is, 'Your moves to actually put an obligation on us are aimed at actually squeezing our margins and increasing yours.'"

Littler said it's mutually beneficial for retailers and suppliers to not always have written supply agreements, since grocers don't want to be subject to "heavily boiler-plated" standardized contracts from multinational food producers, nor do supermarkets want to be penned into similar universal agreements written by major suppliers.

"The system seems to work pretty well for suppliers overall. We're not seeing a crying need for this (code of conduct)," he said. "Obviously, we're always open to discussion. If they were to articulate this perhaps a little more precisely and define what it is and what it isn't, then that's a discussion that could be had, sure."

But FCPC dismissed the RCC's suggestion that a code would lead to higher food prices.

"I get frustrated that they won't look at this, won't do the research, won't investigate the opportunity. They just make an assumption, which is wrong," Graydon said. "It's about time they wake up and start to look at the feasibility of a collaborative solution."

All this arguing sounds familiar to Paul Dobson, a professor of business strategy and public policy at the University of East Anglia in Norwich, England, who studies food retail competition and consumer policy in the U.K.

"It just reminded me of exactly the same arguments that came about in Britain," he said. "The retailers are saying, 'This is all going to be doom and gloom and it's going to lead to price inflation because we won't be able to negotiate aggressively.'"

But in the U.K., those price increases never came.

"It's a bit rich to say that it's definitely going to lead to higher prices. There's no evidence of that," Dobson said. "As long as retailers follow the code, they're still allowed to negotiate … aggressively."

The U.K.'s Groceries Supply Code of Practice came into force roughly a decade ago, after the country's competition commission conducted a lengthy investigation into unfair practices in the market.

The commission found that grocers in the U.K.'s consolidated market were heaping risks and unexpected costs on suppliers, which was "likely to lessen suppliers' incentives to invest in new capacity, products and production processes … If unchecked, these practices would ultimately have a detrimental effect on consumers."

The U.K. code, overseen by an adjudicator, requires that retailer-supplier agreements be laid out in writing, and that retailers pay on time and give advance notice if products will be dropped or orders reduced. The code also stopped certain penalties being placed on suppliers, including policies that forced suppliers to compensate stores for when products spoiled or went missing.

Dobson said retailers in the U.K. “acquiesced” to the code. “It created a level playing field, where you didn’t have to be a really nasty retailer and beat up suppliers to a greater extent than your rival.”

In Tesco PLC’s annual report this spring, the U.K.-based grocer included an entire section on its compliance with the code, saying that the purpose of the code was to “embed the overarching principles of fairness and lawfulness” into the commercial relationship between retailers and suppliers.

A survey by the Grocery Code Adjudicator’s office, which enforces the code, found that 36 per cent of U.K. suppliers reported compliance-related issues with retailers, a big improvement from 2014, the first year of the survey, when 79 per cent of suppliers had issues.

“I can imagine why the retailers are fiercely against any form of regulation, because that’s what businesses try to do. They don’t like to be regulated,” Dobson said. “But I keep looking at Britain and seeing it’s a very good role model that’s been created here. It works and hasn’t created adverse effects.”

A Tesco store in the Kensington district of London. The code of practice has not lead to a hike in food prices in the U.K. as predicted. PHOTO BY SIMON DAWSON/BLOOMBERG

Australia’s Food and Grocery Code of Conduct is another often-cited model, which also hasn’t impacted food prices in the five years since it was implemented, according to observers in the country. Unlike the U.K., the Australian code is voluntary, but three of the country’s four main grocers have signed on.

“Just because there’s a code in place doesn’t mean supermarkets now have no power,” said Gary Mortimer, a business professor at the Queensland University of Technology in Brisbane who focuses on food retailing and consumer behaviour.

“(The code) has reduced, to some extent, the power imbalance. It has derived a more equitable, mutually beneficial relationship between supermarkets and suppliers. But it certainly hasn’t increased prices to the consumer.”

The Australian Competition and Consumer Commission (ACCC), which oversees the code, found that by curtailing fees and penalties, the code drove supermarkets to work with suppliers to find ways to reduce waste and better manage their systems internally.

“It turned the focus to competing on the basis of their operations, rather than relying on squeezing suppliers to compete,” said Mick Keogh, deputy chair at the ACCC. “The code has basically said to them … if you want to compete, you better compete by getting your systems in order.”

FCPC and other industry advocates in Canada have been calling for a similar code here for several years, but have stepped things up after COVID-19 underscored the importance of a strong food supply chain. FCPC CEO Graydon said the government appears to be taking the request seriously.

“They’re certainly doing their homework,” he said, adding that he and two of his major manufacturing members met with Agriculture Minister Marie-Claude Bibeau this week. “COVID had a lot to do with changing the opinions.”

But it appears that despite heightened interest from the federal government in recent weeks, a Canadian version isn’t close at hand.

On Tuesday, Innovation, Science and Industry Minister Navdeep Bains’ office criticized the fees charged to suppliers, but then said the federal government isn’t planning on moving forward with a code.

“It is disappointing to see grocers impose these costly fees,” John Power, the minister’s spokesperson, said in an email. “However, we recognize that terms of sale are generally the exclusive domain between suppliers and buyers, and that these fall under areas of provincial jurisdiction.”

Power said the government is encouraging the provinces and territories to “examine this matter.”

The response confused some in the industry, who noted that the three main Canadian grocers, and their U.S.-based competitors, operate in markets across the country.

“Is the minister saying that we are going to have a different code in each province and territory?” asked Gary Sands, senior vice-president at the Canadian Federation for Independent Grocers.

Sands has been at the forefront of the push for a code of conduct in Canada, and wrote a letter, co-signed by seven other industry associations, to three cabinet ministers last week that asked the government to commit to a grocery code in the upcoming Throne Speech.

Independent grocers, while not directly involved in the supplier-supermarket dispute, have argued that when the big grocers squeeze manufacturers, there’s less money left over for them to spend on promotions with smaller retailers.

“That reply (from Bains’ office) is extremely disappointing,” Sands said in an email. “First, we have been discussing this issue with the federal government and the Competition Bureau for years.”

The Competition Bureau said it was aware of calls for a code of conduct, but noted the Competition Act doesn’t not give the bureau the authority to seek an enforceable code.

“Therefore, it would be inappropriate to comment further,” bureau spokesperson Jayme Albert said in an email.

In 2017, the Competition Bureau issued a position statement on commercial relationships in the grocery sector, following an investigation into Loblaw’s supply policies, including “ad collision” rules that penalized suppliers with deductions when their products were featured in promotions on another retailer’s flyer within a week before or after Loblaw promoted the same product. Another policy penalized suppliers if they offered a product to a competing store without first offering it to Loblaw, the bureau found.

The Competition Bureau concluded its investigation by noting there was "insufficient evidence" that Loblaw's supplier policies lessened or prevented competition substantially. The report also noted that during the bureau's investigation, Loblaw had informed its suppliers it would stop enforcing the policies in question.

The bureau also noted that the reality for suppliers in the Canadian market is that they are all dependent on a small set of grocers for the majority of their business.

"A supplier is likely to lose a greater percentage of revenue than its largest customer if the parties cease doing business," the bureau found.

But the bureau recognized that hard bargaining from big grocers may be pro-competitive, resulting in lower prices for consumers.

"Complaints regarding an imbalance of bargaining power do not, on their own, raise concerns under the abuse of dominance provisions of the (Competition) Act," the report said.

There's a line between driving a hard bargain and anti-competitive conduct, the bureau said. To figure out the difference, the bureau said the focus "will remain squarely on whether the overall intent of the conduct is to either harm the competitiveness of another firm or firms, or to harm the competitive process."

The provinces don't seem to want to take on a code of conduct either. In a statement Tuesday, the Ontario government pledged its support for suppliers, but stopped short of accepting the federal government's call to further explore the possibility of a code.

Agriculture, Food and Rural Affairs Minister Ernie Hardeman said he was committed to "better understand these pressures and the potential solutions" in the sector.

“Our government is hopeful that these retailers are working with their suppliers to recognize the challenges that everyone is facing at this difficult time and I am available to assist if needed,” he said in a statement.

Some in the industry say a provincial system could work, since so much of the country’s manufacturing is concentrated in two provinces: Ontario and Quebec. But others say it’s more complicated.

“The food supply chain in Canada is national. It is very much integrated. It crosses provincial borders. We can’t say this is like a local hardware store having a dispute with their supplier,” Sands, with the independent grocers, said. “Are we honestly supposed to accept that a national, integrated industry is going to have different codes of conduct in different provinces, or, in some, not at all? How does that work?”