



Department
for Environment
Food & Rural Affairs

Consultation:

Contractual relationships in the UK dairy industry

June 2020



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Any enquiries regarding this publication should be sent to us at

[\[dairycontractconsultation@defra.gov.uk\]](mailto:dairycontractconsultation@defra.gov.uk)

or

Department for Environment, Food and Rural Affairs
Dairy Team
Seacole Block
2nd Floor
2 Marsham Street
London SW1P 4DF

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1. Background

This consultation is in response to concerns raised that primary producers, including dairy farmers, tend to occupy positions of relative market weakness in the food supply chain. Consensus among agricultural producers in the UK is that unequal bargaining power with processors and retailers can expose farmers to unfair treatment, with the potential to undermine equitable price transmission along the chain.

A number of other nations have introduced regulations in an attempt to stabilise markets and address systemic imbalances. In the European Union, thirteen member states including France and Spain have introduced laws on compulsory written milk contracts between farmers and processors. The Scottish Government recently [published their analysis](#) of the dairy supply chain and application of Mandatory Written Contracts (MWC) across the European Union, to evaluate the impact of the contracts where they have been adopted. Further afield, the Australian government has recently introduced a mandatory dairy code of conduct.

In 2012 a voluntary code of best practice on contractual relationships in the dairy sector was agreed by industry. It set out minimum standards of good practice for contracts between producers and purchasers. A [consultation and impact assessment](#) regarding mandatory written contracts was undertaken the same year, as part of an assessment of the implementation of the EU Dairy Package. Separate consultations were also carried out by the Scottish, Welsh and Northern Ireland (NI) Governments. The results showed a preference for allowing sufficient time for the voluntary code to take effect. The right to review the situation of contractual relationships was reserved and, if necessary, to reconsider the introduction of legislation on contracts if, after a reasonable period of time, the desired changes had not been achieved by the industry.

In 2016 a formal call for evidence was launched to explore the case for extending the remit of the Grocery Code Adjudicator (GCA). The role of the GCA is to make sure that the largest domestic retailers treat their direct suppliers fairly and lawfully by enforcing and monitoring compliance with the Groceries Supply Code of Practice. The GCA is recognised as an exemplary modern regulator with an international reputation. It is helping to strengthen relationships in the supply chain for the benefit of consumers, retailers and other food businesses.

This process revealed stakeholder evidence of poor contractual relations in the dairy sector. A small number of respondents highlighted the challenge posed by variations to specifications or contract terms, especially if imposed at short notice. Others raised the difficulties producers face in trying to terminate their contracts within a reasonable period, if significant changes are made to prices or contract terms. This evidence suggests a potential pattern of unfair or unclear terms and conditions in contracts between producers and processors, that could limit the ability of farmers to budget effectively, manage price volatility and run profitable businesses. This evidence suggests that the voluntary code is not having the desired impact in terms of improving supply-chain relations.

The UK Government's response to the Groceries Code Adjudicator Call for Evidence ([published on 16 February 2018](#)), included a commitment to consult on the introduction of mandatory written contracts using powers in EU legislation. As the UK has left the European Union, we are instead now seeking new domestic powers to introduce any legislation. The use of domestic powers will allow us to be considerate of the specific nature of the UK dairy sector, although the broad principles of the EU legislation will likely still prove relevant.

The recent COVID-19 pandemic has further highlighted the difficulties sometimes faced by dairy farmers, most notably in relation to sudden price changes. Whilst the problems experienced by the sector were wider than those related exclusively to contractual practice; we would encourage respondents to submit their views on which contractual measures, if any, would improve the resilience of the dairy industry should similar situations arise in the future.

This is a UK wide consultation, undertaken by DEFRA with the agreement of the Devolved Administrations. We recognise that there are significant differences between the dairy supply chains in Great Britain and Northern Ireland. Great Britain's dairy sector is internally well-integrated and operates across internal borders. In Northern Ireland there is a highly integrated cross border supply chain with the Republic of Ireland (RoI). RoI dairy co-operatives own approximately 60% of the processing capacity in Northern Ireland and it is estimated that approximately 35% of milk produced in Northern Ireland is transported to RoI for processing.

Whilst the majority of milk produced in Great Britain is sold within the domestic market, Northern Ireland has an export orientated market meaning that the Northern Ireland dairy supply chain is much more dependent on returns from the global commodity markets. The structure of the processing sector also varies across the UK, with a higher prevalence of co-operatives operating in Northern Ireland.

2. Purpose of the consultation

As previously mentioned, evidence gathered during the GCA Call for Evidence suggests that unfair practices have persisted in the dairy industry. The purpose of this consultation is to seek your views on how contracts are used within the dairy sector and your views on the need for legislation in this area.

With the nature of farm support due to change in the future, greater business stability will be required, and we seek to encourage a shift from practices which encourage short term thinking to those which create a sustainable, modern and thriving industry.

3. The consultation process

Who will be affected by this proposal?

3.1 This consultation is directed at anyone interested in the regulation of activities that take place in the dairy sector. This consultation will be of particular interest to you if you are involved in:

- producing milk for onward sale to a processor; or
- purchasing milk for processing; or
- activities associated with the production, sale or processing of milk; or
- activities for the benefit of the dairy industry.

Timing and duration of this consultation

3.2 The consultation period will commence on **23 June 2020** and will be open to responses for a period of twelve weeks.

3.3 **The consultation period will end at midnight on 15 September 2020.** We will not consider any responses received after that date.

Responding to this consultation

3.4 Please respond to this consultation using the citizen space consultation hub at Defra:

<https://consult.defra.gov.uk/agri-food-chain-directorate/contractual-relationships-in-the-uk-dairy-industry>

By email to: dairycontractconsultation@defra.gov.uk

Or

Department for Environment, Food and Rural Affairs
Dairy Team
Seacole Block
2nd Floor
2 Marsham Street
London SW1P 4DF

Please provide relevant views, evidence and explanation so that proper consideration of alternatives may be given, including any cases where you have reason to comment upon or challenge anything in this consultation.

4. After the consultation

4.1 Responses received by 15 September 2020 will be analysed and taken into account by all UK administrations in considering the measures necessary to improve contractual practice in the dairy sector. Responses will be made available to the relevant teams of policy officials in the Devolved Administrations, who may share analysis and conclusions with senior and ministerial colleagues. After the consultation, a summary of the responses to this consultation will be published and placed on the UK government website at www.gov.uk/defra.

4.2 The summary will include a list of names and organisations that responded but not personal names, addresses or other contact details. However, information provided in response to this consultation document, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes e.g. Freedom of Information Act 2000 (FOIA) and the Data Protection Act 2018.

4.3 If you want information, including personal data that you provide to be treated as confidential, please say so clearly in writing when you send your response to the consultation. If we receive a request for disclosure under the FOIA, we will take full account of your explanation, but we cannot provide an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as a confidentiality request.

4.4 This consultation is being conducted in line with the “Consultation Principles” as set out in the Better Regulation Executive guidance which can be found at <https://www.gov.uk/government/publications/consultation-principles-guidance>.

4.5 If you have any comments or complaints about the consultation process, please address them to:

By e-mail: consultation.coordinator@defra.gsi.gov.uk, or in writing to:

Consultation Co-ordinator, Defra: Seacole Block, 2nd Floor, 2 Marsham Street, London SW1P 4DF.

5. About you

This consultation is primarily directed at dairy farmers and milk purchasers, however we know that other businesses, organisations and individuals are involved with, or take an interest in, the dairy sector. The questions below are intended to take account of this diversity and put your responses in perspective with those of other respondents.

a) Are you:

- A producer
- A processor
- A retailer
- A representative organisation
- Other (please specify)

b) If you are a representative organisation, which part of the supply chain do you represent?

- Farmers
- Processors
- Retailers
- Consumers
- Other (please specify)
- Not applicable

c) Where is your business registered?

- England
- Northern Ireland
- Scotland
- Wales
- Other (please specify)
- Don't know

d) If you are a producer, where is your milk typically processed?

- England
- Northern Ireland
- Scotland
- Wales
- Other (please specify)
- Don't know
- Not applicable

e) If you are a producer, are you currently signed up to a contract that complies with the voluntary code?

- Yes
- No
- Don't know
- Not applicable

f) If you are a producer, please specify the volume of milk you produce (annually).

- Under 500,000 litres
- 500,000 – 1 million litres
- 1 million – 3 million litres
- Over 3 million litres
- Not applicable

g) If you are a purchaser, where is your milk typically processed?

- England
- Northern Ireland
- Scotland
- Wales
- Other (please specify)
- Don't know
- Not applicable

h) If you are a purchaser, do all of your milk contracts comply with the voluntary code?

- Yes
- No
- Don't know
- Not applicable

i) If you are a purchaser, please specify the volume of milk you buy (annually).

- Under 50 million litres
- 50 – 250 million litres
- 250 – 500 million litres
- Over 500 million litres
- Not applicable

j) Are you currently a member of a cooperative business?

- Yes
- No
- Don't know

6. Consultation questions

Contractual reform – your opinion

The existing Dairy Contracts Voluntary Code of Practice (VCOP) has been adopted by businesses covering 85% of UK milk production and is generally accepted to have introduced better contractual conduct where it has been strictly adhered to. However, given its voluntary nature, levels of compliance with the VCOP are not considered to be uniform across the industry.

1. Have you, your business, or your members, experienced issues with dairy sector contracts, for example where contract terms have not followed the example set by the voluntary code? Please give examples to explain your answer.

- Yes, prior to 2012 and during the past 5 years
- Yes, prior to 2012 only
- Yes, only in the last 5 years
- No
- Don't know

2. Legislation, rather than voluntary measures, is needed to ensure that standards are consistent across the supply chain. To what extent do you agree with this statement? Please give reasons for your answer.

- Strongly agree
- Agree
- Neither agree nor disagree
- Strongly disagree
- Disagree
- Don't know

Legal requirement to contract in writing

The use of written contracts reinforces certainty in supply arrangements. Whilst written contracts are already commonplace in the United Kingdom between dairy producers and purchasers, they are not currently a legal requirement.

3. Should trading relationships between producers and purchasers always be covered by a written contract? Please give reasons for your answer.

- Strongly agree
- Agree
- Neither agree nor disagree
- Strongly disagree
- Disagree
- Don't know

Variation within the UK

The UK dairy industry spans all four constituent nations operating within a single internal market, but the respective dairy sectors have certain differences.

4. Legislative regulations are often applied uniformly across all UK nations. Is there any reason why a different approach should be taken? Please give reasons for your answer.

- Yes
- No
- Don't know

Pricing mechanisms

The lack of reliable dairy pricing information has emerged as one of the major issues facing dairy farmers. More transparent pricing can facilitate greater trust between business partners and ensure negotiations happen on an equal footing. Increased certainty, both in terms of price certainty for producers and supply certainty for processors, is likely to strengthen the entire industry.

Most milk prices are set in the UK through buyers' discretion, meaning that the milk buyer has the power to set and modify the milk price, at times with little notification. Certain pricing practices can allow a degree of market responsiveness, and it is not the intention to undermine flexibility in the marketplace, but rather to introduce a greater degree of transparency to procedures concerning price.

Pricing mechanisms are often tailored to the business model they serve. Cooperatives, for example, may operate using a different pricing methodology to others. Whilst businesses should be free to adopt the most appropriate pricing mechanisms for their operations, each should be fair, transparent and agreed to by both the producer and processor.

5. Any future legislation should introduce a legal obligation to include a price/price calculation mechanism in a contract. To what extent do you agree with this statement? Please give reasons for your answer.

- Strongly agree
- Agree
- Neither agree nor disagree
- Strongly disagree
- Disagree
- Don't know

There are various means of including price information in a supply contract. It may also be appropriate that a contract offers a mixture of options to cover different portions of the supply.

6. In order to achieve transparency, the methodology behind any price mechanism must be detailed within a contract. To what extent do you agree with this statement? Please give reasons for your answer.

- Strongly agree
- Agree
- Neither agree nor disagree
- Disagree
- Strongly disagree
- Don't know

Volumes and timings

Whilst, ultimately, global commodity markets will always influence UK prices, volatility is also linked with variability in supply. An option to specify volumes ahead of time may enable more accurate supply management.

7. The volume of milk to be supplied should be fixed in the contract. To what extent do you agree with this statement? Please give reasons for your answer.

- Strongly agree
- Agree
- Neither agree nor disagree
- Disagree
- Strongly disagree
- Don't Know

8. If you agree that the volume of supply should be fixed, please include an indication of an appropriate tolerance for variation (+/- X%). i.e. By how much either way should a contracted supply be allowed to vary.

- <1%
- >1%- <3%
- >3% - <5%
- >5% - <10%
- >10%
- Don't know
- Not applicable

9. If you agree that the volume of supply should be fixed, on what timescales should volumes be calculated? Please give reasons for your answer.

- Monthly
- Annually
- Other (please explain)
- Don't know
- Not applicable

10. What options should be available to treat volumes outside these tolerances? Please give reasons for your answer.

- Refusal to accept
- The right to set a lower price for excess volumes
- Other (please explain)
- Don't know

Duration of contracts

11. The terms of a contract should establish a minimum duration for supply arrangements. To what extent do you agree with this statement? Please give reasons for your answer.

- Strongly agree
- Agree
- Neither agree nor disagree
- Disagree
- Strongly disagree
- Don't know

12. If you agree that a minimum duration for supply should be established, please indicate your preference for the length of this period:

- 6 months
- 12 months
- More than 12 months
- Other (please explain)
- Don't know
- Not applicable

13. Should there be a maximum contract period after which the contract must be refreshed and reviewed?

- Yes
- No
- Don't know

14. Where a contract is established using a fixed price mechanism, what should be the maximum length of this contract? Please give reasons for your answer.

- Up to 1 year
- Up to 2 years
- Up to 3 years
- Other (please specify)
- Don't know

Termination of contracts

If parties to a contract are presented with major alterations to the supply terms, it is important that it is possible for them to terminate their contracts within a reasonable period. Equally, however, businesses require stability of supply to develop long-term business strategies. Evidence suggests greater certainty around termination clauses is required.

15. Termination clauses should be mandatory in all contracts. To what extent do you agree with this statement? Please give reasons for your answer.

- Strongly agree
- Agree
- Neither agree nor disagree
- Disagree
- Strongly disagree
- Don't know

Termination of contracts – on the part of the producer

16. If you agree that termination clauses should be mandatory, please indicate your preference for the minimum notice period for a producer to terminate the contract.

- 1 month
- 3 months
- 12 months
- Other (please explain)
- Don't Know
- Not applicable

17. Please indicate your preference for the maximum notice period for a producer to terminate the contract.

- 6 months
- 12 months
- Other (please explain)
- Don't know
- Not applicable

Termination of contracts – on the part of the purchaser

18. If you agree that termination clauses should be mandatory, please indicate your preference for the minimum notice period for a purchaser to terminate the contract.

- 1 month
- 3 months
- 12 months
- Other (please explain)
- Don't know
- Not applicable

19. Please indicate your preference for the maximum notice period for a purchaser to terminate the contract.

- 6 months
- 12 months
- Other (please explain)
- Don't know
- Not applicable

Variations in agreement

A lack of contractual flexibility risks introducing detrimental consequences for either, or both, parties. We do not intend to create any legislative measures that undermine business responsiveness, but where alterations in existing contract terms are desirable it is important they are made fairly.

20. All parties should be able to request changes to the terms of a contract, with that change only coming into force if agreed unanimously. To what extent do you agree with this statement? Please give reasons for your answer.

- Strongly agree
- Agree
- Neither agree nor disagree
- Disagree
- Strongly disagree
- Don't know

21. Before any agreed changes are implemented, what should be the length of a mandatory minimum notice period?

- 1 month
- 2 months
- 3 months
- Other (please explain):
- Don't Know

22. Any mandatory minimum notice period to vary a contract should be set longer than any minimum termination notice period. To what extent do you agree with this statement? Please give reasons for your answer.

- Strongly agree
- Agree
- Neither agree nor disagree
- Disagree
- Strongly disagree
- Don't know

Charges and premiums

Bonuses and deductions are a vital part of managing the character and composition of milk supply. Bonus payments for constituent content, seasonality or specific production methods are an effective way for processors to incentivise farmers to provide what the market demands. However, a lack of transparency relating to the application of price amendments (such as testing methods for quality assessments, or retrospective application of deductions) means they can be applied unfairly.

23. A contract must contain, in clear and unambiguous language, all terms and conditions relating to payments and deductions. To what extent do you agree with this statement? Please give reasons for your answer.

- Strongly agree
- Agree
- Neither agree nor disagree
- Disagree
- Strongly disagree
- Don't know

Exclusivity

The majority of UK milk contracts operate as exclusive supply arrangements, where the supplier is legally bound to sell the entirety of their milk production to a single buyer. Whilst exclusive supply arrangements can often be mutually beneficial, the

imposition of such arrangements can sometimes prove overly restrictive to farmers and possibly undermine expansion opportunities. [Recent Scottish Government research](#) has examined exclusivity in further detail¹.

24. Exclusivity clauses should be prohibited. To what extent do you agree with this statement? Please give reasons for your answer.

- Strongly agree
- Agree
- Neither agree nor disagree
- Disagree
- Strongly disagree
- Don't know

Further provision

There may be further deficiencies in the contractual terms and manifestly one-sided clauses that can unfairly disadvantage parties; specifically in the event of unexpected occurrences. For instance, some contracts lack any legal certainty about what happens in *force majeure* scenarios or uncertainty about what constitutes *force majeure* scenarios, e.g. death of farm operator, processor insolvency etc. We would be interested in hearing views on these.

25. Are there any additional clauses which should be mandatory in contractual terms? Please provide details.

26. Are there any additional clauses which should be prohibited in contractual terms? Please provide details.

Confidentiality

Whilst certain contractual details are justifiably subject to confidentiality, certain confidentiality clauses can be used to undermine transparency. We are aware that, in some circumstances, changes to a contract are presented to producers who are then prevented from consulting with their professional or legal advisers before signing. This risks compelling farmers to enter into new agreements they have been unable to properly analyse.

¹ <https://www.gov.scot/publications/impact-mandatory-written-dairy-contracts-european-countries-potential-application-scotland/pages/2/>

27. Should regulations be introduced to cover confidentiality clauses? Please give reasons for your answer.

- Yes
- No
- Don't Know

28. If you agree that regulations should cover confidentiality clauses, which confidentiality clauses should be prohibited, and which (if any) are acceptable? Please give details.

Dispute resolution

Where contractual disputes arise, effective resolution procedures are required and we are very interested in views on the options available. Arbitration can sometimes be a costly and time-consuming process and other forms of third party determination may be appropriate (where both parties consent) as an alternative means of resolving disputes.

29. Please provide your views on the most effective means of dispute resolution and whether this should be binding or advisory.

Producer organisations

Recent evidence, from research carried out by the Scottish Government on the introduction of contractual regulations and their impact across the EU, suggests that the introduction of Producer Organisations alongside legislation helps improve the bargaining balance across the supply chain.

30. The promotion of Producer Organisations should be considered alongside legislation. To what extent do you agree with this statement? Please give reasons for your answer.

- Strongly agree
- Agree
- Neither agree nor disagree
- Disagree
- Strongly disagree
- Don't know

Impact on business

Defra undertook a provisional impact assessment to measure the potential impacts on businesses across the UK as a result of any proposals to bring in new legislation for contracts in the dairy sector. One-off costs from familiarisation with the new legislation and re-issuing compliant contracts were identified as a burden for processors and producers in the first year. Ongoing costs will result from any necessary revisions that require the contract to be re-issued. We would like your views on these impacts to inform a more detailed impact assessment.

31. Are you aware of any impacts to businesses which could arise from the introduction of dairy contract regulation?

Please give reasons for your answer, including any additional annual costs or savings for your business and any specific impacts in one or other parts of the UK.

Transition period

We realise the introduction of any new regulations may require a change in ways of working and therefore, should legislation be introduced, we would like to provide purchasers and producers with an adequate amount of time to become familiar with any changes before they enter into force.

32. How much time would you estimate you need to be ready to implement new legislation and enter into new contracts? Please give reasons for your answer.

- 12 months
- 24 months
- 36 months
- Other (please explain):
- Don't know