

KIWIFRUIT EXPORT REGULATIONS 1999

IN THE MATTER OF an Appeal By **Southern Fresh Fruits Exports Limited** (“SFFE”) relating to the Decision of **Kiwifruit New Zealand’s European and MEIOSA Collaborative Marketing Committee** (“KNZ”) dated the 7th February 2007, in respect of the SFFE Application to export kiwifruit to Lulu Hypermarket (“Lulu”) in Oman in collaboration with Zespri Group Limited (“Zespri”).

APPEAL COMMITTEE: Sir Brian Elwood (Chairman)
Hendrik Pieters
Ian Greaves

DECISION: 10 April 2007

Status of Appeal

1. The Board of Kiwifruit New Zealand (“the Board”) constituted pursuant to the provisions of the Kiwifruit Export Regulations 1999 (“the Regulations”), has all the powers necessary to enable it to carry out its functions: Regulation 38 refers.
2. One of the functions of the Board is to determine collaborative marketing applications pursuant to Part 4 of the Regulations: Regulation 33 refers.
3. The Board can establish Committees and delegate any of the Board’s functions to any of its committees: clauses 10 and 11 of the Schedule to the Regulations refer.
4. The Board may regulate its own procedures in a way that is consistent with the rules of natural justice: Regulation 31 refers.

5. The Board is required to consider collaborative marketing applications and decide whether to approve a collaborative marketing arrangement: Regulation 28 refers.
6. The Board established committees to consider collaborative marketing applications for the 2007 kiwifruit season and a committee was so established (KNZ) comprising Ruth Lee (Chair) and Mark Bayly to consider the application of SFFE to export New Zealand grown kiwifruit to Oman for retailing by Lulu Hypermarket through service provider Al Jebali Trading LLC (the Oman programme). On 8 December 2006, KNZ had a telephone conference with John Thompson of SFFE and Warren Young of Zespri to consider SFFE's application. KNZ required Zespri to provide substantiation of their claim that Lulu Hypermarket was an existing customer of theirs. This was supplied, and provided to SFFE.
7. KNZ declined the application of SFFE for the Oman programme and advised its reasons by a written decision dated 7 February 2007.
8. KNZ advised all applicants for collaborative marketing approvals that if dissatisfied with a decision of any of its committees relating to collaborative marketing, the Board would allow an appeal to an Appeal Committee of the Board, consisting of members of the Board who had not considered the application at issue. Any right to appeal any decision of the Committee terminated 14 days from the date of the issue of reasons for declining approval. SFFE appealed. The Appeal Committee established for the purpose of considering the SFFE Appeal is that set out in page one of this determination.

Substance of the Appeal

9. By letter dated 9 March 2007 SFFE advised the reasons for its Appeal of the decision and other decisions of other Collaborative Marketing Committees of the Board relating to separate collaborative marketing applications.

10. The Appeal Committee met on 13 March 2007. SFPE and Zespri were invited to meet with the Appeal Committee. SFPE was represented by John Thompson. Zespri was represented by Warren Young.
11. The main submissions in support of the appeal can be summarised as follows:
 - 11.1 Bias, real or apparent, of some members of KNZ, supported the SFPE view that KNZ had predetermined the appropriate number of collaborative marketing arrangements approved, or amount of fruit allocated, at the expense of a principled application of the regulatory objective.

Appeal Committee Response

- The allegation of bias is rejected. No member of KNZ or the Board has any direct personal interest in a collaborative marketing application. Board members, other than the Chairman, are either elected or appointed pursuant to provisions of the Regulations, by kiwifruit producers or New Zealand Kiwifruit Growers Incorporated. In practice they are active participants in the kiwifruit industry and have a general interest in industry issues along with all other active participants. The Chairman is “fully independent” of the industry: see Regulation 36.
- Each application for a collaborative marketing approval is considered on its own merits pursuant to the provisions of the Regulations: see Part 4 of the Regulations.
- A collaborative marketing arrangement is defined by the Regulations as “an arrangement by which a person may export New Zealand grown kiwifruit in collaboration with ZGL.”: see Regulation 2. KNZ and the Board are of the view that the spirit and intent of collaboration envisaged by that definition is generally of a continuous nature from the formulation of the arrangement through to its implementation and completion. The collaboration

requires the parties involved, the applicant and Zespri, to work together on a project. There is no rigid formula to establish a collaborative marketing arrangement and there can be variations to suit the circumstances of individual programmes. The purpose of collaborative marketing arrangements is “of increasing the overall wealth of New Zealand kiwifruit suppliers:” see Regulation 24. SFFE appeared to be of the view that this approach gave Zespri a virtual right of veto over any application for a collaborative marketing approval. Neither KNZ nor the Board are of that view. Zespri must consider each proposal for a collaborative marketing approval in good faith. The powers given to the Board to require Zespri to make a certain volume of kiwifruit available for collaborative marketing (see Regulation 26) and the obligations imposed upon Zespri “to enter into a contract with a collaborative marketing approval holder consistent with the collaborative marketing approval” (see Regulation 29) means that no veto exists and the matter remains in the hands of the Board, should circumstances so require.

- 11.2 KNZ took into account irrelevant considerations by considering a lack of Zespri support for the SFFE application as relevant.

Appeal Committee Response

- See the general comments under 11.1 above.
- KNZ’s decision was not made for the reason that Zespri did not support the SFFE application. The application was declined because of:
 1. A lack of collaboration by both SFFE and Zespri.
 2. The arrangement was for a sale of significant volumes of kiwifruit into an existing Zespri customer.
 3. There was no evidence to show how the proposed programme would operate to the benefit of kiwifruit “growers”.

- 11.3 KNZ was of the view that a potential reduction in Zespri's supply and/or profit was enough to rule out the SFPE's application.

Appeal Committee Response

- KNZ did not decline the application for that reason. The substantive reasons are set out in paragraph 11.2 above.
- It was for SFPE to show how its proposal would achieve the purpose "of increasing the overall wealth of New Zealand kiwifruit suppliers." KNZ was of the view that the "likely outcome is that Lulu will seek to purchase New Zealand grown kiwifruit at the best possible price and this could see Zespri and SFPE competing with each other. The result could be a reduced return to the New Zealand grower." (emphasis added)

- 11.4 KNZ and its other committees has assumed that deriving monopoly advantages requires confining marketing to one organisation or to parties working in a tight relationship.

Appeal Committee Response

- KNZ made no such assumption.
- The New Zealand kiwifruit industry structure is in large measure determined by the Regulations which allow for the consolidation of the New Zealand kiwifruit crop for export by Zespri as distinct from that for the local market (including Australia). The export crop is sent to distant markets where it is to be marketed alongside kiwifruit from other countries in a highly competitive environment. Zespri has a global strategy to achieve premium returns from premium quality fruit under its registered Zespri brand. In considering collaborative marketing applications it is appropriate to consider the impact upon the Zespri global strategy in so far as that strategy was likely to be adversely affected through New Zealand grown kiwifruit being available in the market from differing

sources. Competitive forces could drive down prices with an adverse effect upon “the overall wealth of New Zealand kiwifruit suppliers.” It was for SFFE to satisfy KNZ that two sources of supply of New Zealand grown kiwifruit into the same market would not have that effect but would likely achieve the purpose “of increasing the overall wealth of New Zealand kiwifruit suppliers.” KNZ was not persuaded on the material made available to it by SFFE that that would be the case.

- 11.5 KNZ and the other collaborative marketing committees of the Board drew erroneous assumptions on substitution which were not backed by evidence and took an overly simplistic approach.

Appeal Committee Response

- KNZ noted
 1. That SFFE was seeking to sell significant volumes of kiwifruit into an existing Zespri customer.
 2. That there was no evidence provided to show how the sales from the proposed arrangement would be “ring fenced” so as not to undermine existing Zespri sales.
 3. That the likely outcome would be competition between SFFE and Zespri and result in a reduced return to the New Zealand grower.
- In the absence of evidence from SFFE that its in-market arrangements would ensure such would not eventuate, it was open to KNZ to express such a reservation about the outcome from SFFE selling of Zespri branded kiwifruit in the same market and to the same retailer.

- 11.6 The purpose of collaborative marketing to increase the overall wealth of New Zealand kiwifruit suppliers is a “long-run” concept and should not focus on short term returns. KNZ failed to take account of the perverse

incentives created by persistent rejection of collaborative marketing efforts.

Appeal Committee Response

- Collaborative marketing as established by the Regulations is seen by KNZ and the Board as a broadly based concept allowing for innovative marketing arrangements to be developed having either/or both a short or longer term horizon. A requirement of the Regulations is that such arrangements would be undertaken in collaboration with Zespri.
- KNZ has not adopted a short term approach to the approval of collaborative marketing arrangements which can create important marketing opportunities for the kiwifruit industry. The marketing innovations which can be accommodated through a collaborative marketing approval have not as yet been fully developed to their potential either in the short or longer term.
- KNZ and the Board has not persistently rejected collaborative marketing efforts but has, within the limits of its functions as set out in the Regulations, sought to encourage the development of collaborative marketing arrangements. The Board has encouraged Zespri to see collaborative marketing as an important marketing tool. For its part Zespri has:
 1. Acknowledged the importance of collaborative marketing.
 2. Appointed a full-time Collaborative Marketing Manager.
 3. Assured the Board that the satisfactory performance of Zespri's obligations under the collaborative marketing regime have been included in its International Marketing Manager's Key Performance Indicators.
- The number of collaborative marketing programmes and the volume of fruit sold under collaborative marketing programmes depends on the quality of the applications that are received by the Board and their compliance with the relevant Regulatory requirements.

11.7 Each of KNZ's decisions were based on errors of fact or drew erroneous conclusions not supported by the evidence.

Appeal Committee Response

- The Appeal Committee found no material errors by KNZ. The SFPE application was short on sufficient detail to enable KNZ to establish precisely what it proposed or its effect upon the Zespri global or country specific marketing strategy. There was no evidence of collaboration between SFPE and Zespri and the application form completed by it clearly stated there had been no collaboration.
- The applicant had not addressed in sufficient detail the Regulatory parameters of the collaborative marketing regime or established how its proposal would or could increase the overall wealth of New Zealand kiwifruit suppliers.

11.8 Generally SFPE makes allegations about the operation of the collaborative marketing regime and the roles of the Board and Zespri.

11.8.1 The Board is furthering Zespri's commercial agenda at the expense of the Regulatory purpose.

Appeal Committee Response

That is not so. See earlier comments at 11.1 of this determination about the purpose of collaborative marketing.

11.8.2 Collaborative marketing applications must be considered in light of the statutory purpose, not for commercial preferences of Zespri.

Appeal Committee Response

The commercial preferences of Zespri are not relevant to the consideration of collaborative marketing applications. What is relevant is the Zespri marketing strategy to sell the substantial New Zealand kiwifruit export crop in world markets which are dynamic and changing and increasingly competitive.

11.8.3 SFPE made numerous attempts to constructively engage with relevant Zespri officials, yet received an uncooperative response.

Appeal Committee Response

There was no evidence of SFPE's attempt to "constructively engage" with Zespri officials. Mr Thompson for the applicant said he had tried to telephone Zespri officials, left messages but received no reply. That he interpreted as an uncooperative response. The failure to respond to telephone messages is regrettable if that is what occurred. However constructive engagement should extend beyond leaving telephone messages. No attempt was made by the applicant to engage with the Zespri Collaborative Marketing Manager nor provide further details in writing as to how the applicant saw its proposals operating in practice. There was no specific evidence before the Appeal Committee that Zespri had in fact acted in an uncooperative manner.

11.8.4 It is the Board's task to determine whether an applicants proposed programme increases the overall wealth of New Zealand kiwifruit suppliers. If the Board determines that grower wealth would benefit as a result of an application, then Zespri is required pursuant to Regulation 30 to work constructively with the applicant and enter into a collaborative arrangement consistent with the approval. The Board's approach inverts this process.

Appeal Committee Response

This submission is not accepted. It is for the applicant to bring forward sufficient information to persuade the Board or its Collaborative Marketing Committees as appropriate that the collaborative marketing proposal it is advancing will achieve the Regulatory purpose of increasing the overall wealth of New Zealand kiwifruit suppliers. This is a significant requirement not satisfied by mere assertion but by considering in some detail the existing marketing arrangements in the market the collaborative marketer wishes to enter and the effect of the proposal on those marketing arrangements. The Board has consistently recommended that applicants seeking collaborative marketing approvals engage fully with Zespri with a view to gaining an understanding of Zespri's marketing strategy in the relevant market and by discussion identify how the applicant's proposal can be accommodated without conflicting with Zespri's market strategy with possible negative impact on the overall wealth of New Zealand kiwifruit suppliers. To that end the Board has established a Collaborative Marketing Advisory Working Group consisting of its Chief Executive and Zespri's Collaborative Marketing Manager to facilitate communication between the applicant and Zespri. This advisory working group's involvement is triggered on receipt of a collaborative marketing application, and prior to consideration by the relevant collaborative marketing committee. In this instance the applicant submitted a number of pro forma applications for collaborative marketing which were considered by the Advisory Group. On 29 November by email from the Board's Chief Executive SFPE was advised of the Advisory Group's indicative view on each of the pro forma applications. This gave SFPE the opportunity to initiate discussions with Zespri and provide more detailed information about the proposal so that it could be fully assessed. No discussions eventuated and no detailed information was provided.

11.8.5 Increasing the overall wealth of New Zealand kiwifruit suppliers is not necessarily the same as increasing the wealth of the Zespri shareholders.

Appeal Committee Response

This submission is accepted and is the approach adopted by the Board.

11.8.6 In order to achieve the objective of Part 4 of the Regulations the Board should consult with Zespri and the applicants to explore whether a collaborative arrangement that increases supplier wealth can be achieved.

Appeal Committee Response

To the extent that the submission suggests that it is a Board function to consult with Zespri and collaborative marketing applicants to explore whether a collaborative marketing arrangement that increases supplier wealth can be achieved, it is not consistent with the Regulatory functions of the Board, “to determine collaborative marketing applications in accordance with Part 4”. It is for the applicant to consult with Zespri as part of the process involved in developing a collaborative arrangement between the two. It is not for the Board or its Collaborative Marketing Committees to act as a go between or intermediary to see if a collaborative marketing arrangement can be achieved.

The Oman Decision

12. SFPE’s submission in support of the Appeal contained three elements:

- KNZ made an error of fact considering the application to be one to supply kiwifruit just to Lulu Hypermarkets whereas SFPE intended to market to the wholesale distributor Al Jebali and other food service outlets.

- There is an opportunity to gain a stronger presence in the Oman market that is being only served through a third party, and provides an opportunity to earn greater returns.
- Oman is a market not being explored by Zespri, yet it is a market which offers strong returns.

Appeal Committee Comment

The Appeal Committee was not satisfied that KNZ had made an error of fact. The information made available in the application and subsequently was not clear as to intent and was based upon an incorrect assumption that Zespri did not sell directly into Oman or via a third country. There was uncertainty about the applicant's programme and how it would be managed in a situation where its proposed principal client was already supplied with New Zealand grown kiwifruit direct from Zespri's Dubai based distributor. This was contrary to the applicant's view that the programme it proposed would give New Zealand growers access to the Oman market through Al Jebali and the Lulu hypermarkets. The information on SFFE's collaborative marketing application was also unclear as to the manner in which its programme would be operated in Oman. In part this may have been caused by its lack of knowledge as to the then existing arrangements in Oman for the supply of New Zealand grown kiwifruit through the Zespri agent in Dubai. In part it could have been caused by SFFE's failure to adequately communicate its intentions and undertake discussions with Zespri through Zespri's Collaborative Marketing Manager and thereby develop a collaborative marketing opportunity which could be seen to increase the overall wealth of kiwifruit suppliers.

The Appeal Committee when discussing the appeal submissions with Mr Thompson formed the distinct impression that what SFFE intended to achieve and how it was to be achieved was still being developed and modified.

Outcome of the Appeal

13. The Appeal Committee is not persuaded that SFFE has established any grounds to justify the Appeal Committee referring the Oman application back to KNZ for further consideration. There is too close an approximation between the availability of New Zealand grown kiwifruit in Oman through an established Zespri agent without there being evidence of careful consideration being given to how SFFE's marketing intentions could be implemented without disruption or potential disruption to the current supply of and price received for New Zealand grown kiwifruit. That left, in the view of the Appeal Committee, considerable doubt about how this market is best developed for the future. The Appeal is not upheld.

General Observations

14. The Appeal Committee noted SFFE's enthusiasm to develop a kiwifruit supply line to its end users, but without adequate research into existing market conditions and arrangements for NZ grown kiwifruit such that the risks to the overall wealth of New Zealand kiwifruit suppliers through approval of its application, had not been properly considered. Given the lack of interaction between SFFE and Zespri for which SFFE has primary responsibility to initiate, it was not the Appeal Committee's function to try and stitch together an arrangement which would satisfy the Regulatory purpose of collaborative marketing. There may well be opportunities in the Oman market for additional sales of New Zealand grown kiwifruit which could be developed collaboratively between SFFE and Zespri. As the 2007 marketing season has begun it may well be too late for SFFE to commence discussions relevant to this season. However the opportunity does exist for SFFE to undertake more in market research and to enter into discussions with Zespri to see if they can work together on a project or projects which can be seen to increase the overall wealth of New Zealand kiwifruit suppliers. SFFE should be prepared to document its proposals in sufficient detail to enable both Zespri and the Board

or its relevant collaborative marketing committee to be satisfied that that Regulatory requirement could be satisfied or would likely be satisfied.

If SFPE's concern is with the current environment for the export marketing of New Zealand grown kiwifruit then those concerns should be addressed not through the collaborative marketing regime but in other places.

SFPE is assured that the Board expects Zespri to consider approaches from those seeking collaborative marketing approvals in a considered and open minded manner having regard to the Regulatory purpose of collaborative marketing arrangements.

For and on behalf of the Appeal Committee

A handwritten signature in dark ink, appearing to read 'Brian Elwood', with a stylized flourish at the end.

Sir Brian Elwood
Chairman