

GUIDE TO MILK SUPPLY AGREEMENTS AND THE DAIRY INDUSTRY CODE OF CONDUCT

TALKING POINTS FOR CONTRACT DISCUSSIONS

Last reviewed May 2021

A Milk Supply Agreement (MSA) is about choices. It is an agreement between two parties: suppliers and processors. A processor makes an offer; a supplier chooses to accept or not. Suppliers should consider the key points that affect them and their farm business to help make the right choice.

These talking points are designed for dairy farmers to be used as a guide in MSA negotiations with processors.

The guide considers supplier and processor interests, and incorporates the requirements for milk supply agreements specified under the Dairy Industry Code of Conduct.

It is intended to be used in conjunction with Dairy Australia's Guide to Milk Supply Agreements and the Dairy Industry Code of Conduct – Checklists 1 and 2.

This package of resources is designed so that suppliers negotiating new milk supply agreements, or renegotiating existing agreements, can feel confident about putting an arrangement in place that best suits their business.

1. The Dairy Industry Code of Conduct (The Code)

The first requirement in the Code of Conduct is; **processors and farmers must deal in good faith.**

To put it simply, *good faith* means that you must act honestly, reasonably and not arbitrarily with each other or for some irrelevant purpose, and that the parties must act co-operatively to achieve the purpose of the agreement. This does not mean you have to act in the interests of the processor, nor do they have to act in your interests. It does not mean that the parties cannot 'drive a hard bargain' and it will not save you from a poor commercial deal.

As of 1 July 2020, the wording of any new, altered or renewed milk supply agreement needs to be aligned with the Dairy Industry Code of Conduct. As of 1 January 2021, all contracts must be compliant with the Code.

2. Getting to know your processor

In a 'getting to know you' conversation, suppliers should find out what the processor has to offer ('What's in it for me?') and what the processor is looking for ('What do you need?').

Strength of the milk company/processor

You want to understand the processor business and its strengths and opportunities. Consider how you rate the processor in areas of trust, reputation, integrity and honesty.

- Tell me about the security of the company – does it have a strong backing, a robust business plan, which markets does it supply, track record?
- Why choose this processor, what are the milk supply options, what is the market value of my milk supply with them?
- What is the diversity of the processor's product mix, and how is that a good fit for my system? What are their end use contracts (fresh, market, export or manufacturing milk) and am I comfortable with them?

PROCESSOR EXPECTATIONS

- Factors of milk supply, volume, location, milk quality and production curve
- Operators with a good, secure whole farm business
- A value proposition for the supplier that is solid, simple and transparent
- A business that is clean and tidy in the milk collection area
- A supplier who understands the terms of supply
- Suppliers who demonstrate respect and reliability
- A supplier who aims to build a business relationship
- Alignment of goals – opportunity to expand or reduce supply, changing supply curve, production parameters (milk composition, A2, organic).

3. Terms and conditions

In simple terms a contract is not just about milk price – the whole package needs to be considered. Does it suit your farm? Does it suit your milk supply?

Check the sticky bits

- Minimum supply
- Clawback (payback terms on finances)
What is the availability and what are the terms of finance? What about flexibility of price?
- Milk quality demands, flexibility and support.
What is the level of help with problem solving, identification and remediation of milk quality issues?
- Payment terms (fortnightly, monthly or bimonthly payments). What are the payment terms and will they vary?

Identify any trigger points to renegotiate

- Is there a notice period to leave mid-term or change companies?
- How will the milk supply agreement be affected/reviewed if my circumstances change such as herd size, ownership, milk supply, quality, seasonality, market signals?

Understand the exit strategy

- Are there any 'hooks', e.g., delayed incentive payments, loan conditions, that are holding back ability to move companies?
- What are the implications if milk supply needs to cease mid-term of the milk supply agreement, due to retirement, personal circumstances, death, or other unplanned events?

4. Milk quality

What are terms for quality standards? These terms need to be clear and simple.

- What are the parameters and value of penalties?
- What level of support is provided?
- What is the quality criteria? Is there flexible testing and when – daily, 10-day periods, monthly, or greater?
- What after-hours support is provided for emergency testing?

5. Milk price

Milk price is important, but not the only important factor.

- How do milk quality and seasonality relate to farm production costs and current practices?
- The cost to change milk curve and/or quality – what costs would it create/reduce to meet the change?
- How would these changes impact on profit margin?

From here, there are a number of questions and varieties of milk price that need to be pursued by the supplier to determine the total package on offer from the processor.

- Is an Income Estimation Sheet readily available, and how will all milk payments, costs and incentives be clearly shown and explained?
- Is this a payment system aiming for a monthly 'flat supply' of milk?
- How will this provide an optimum return, if you require calving all-year-round on my farm?
- What are the penalties, allowances for milk supply at +/- 10%, daily, weekly, monthly?
- How does your milk payment system, and the monthly pay rates, provide the best return on my farm with seasonal calving?

FOR FURTHER INFORMATION

Download the Cash Budgeting Tool:
dairyaustralia.com.au/cashbudgetingtool

- Does the monthly milk price pay the same rate per milk solids for every month?
- What is the regularity of milk payments – fortnightly, monthly, bi-monthly? When are penalties, loadings, bonuses calculated and paid?
- What options are available if the supplier seeks to change to a different regularity of payment?
- How is milk payment based? On litres, or solids and component composition? How does this match your market demands?
- What is your minimum price and for what period is it likely to be paid? Is there a schedule of prices? How does this share the rides of ups and downs in forward planning? What is the certainty of this milk price?

FOR FURTHER INFORMATION

For the definition of minimum price, specifying what's included and excluded from this price, visit the ACCC website: acc.gov.au/business/industry-codes/dairy-code-of-conduct/minimum-price-under-the-dairy-code

Milk price - incentives, bonuses, penalties

- What is the range of milk quality reward payments, bonuses and penalties?
- What is the productivity incentive and how is it based?
- Are there any incentives paid for growth, or support for expansion?
- What is the collection cost, or volume charge and how is it a part of the milk price?
- What other incentive payments are available?
- With regard to the HACCP On-Farm Food Safety Plan, what are the support, payments, rewards, or penalties for non-compliance?
- What is the level of support from field staff for the development and compliance of the HACCP On-Farm Food Safety Plan?
- Are there any other service fees, costs or charges?

FOR FURTHER INFORMATION

Visit the DA Risk Management Tool on Dairy Farm Safety at: risk.dairyaustralia.com.au



This project is supported by the Department of Agriculture, through funding from the Australian Government.

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Dairy Australia Limited ABN 60 105 227 987
E enquiries@dairyaustralia.com.au
T +61 3 9694 3777
F +61 3 9694 3701
dairyaustralia.com.au