

**Non Confidential**

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Director Operations 1
Anti-Dumping Commission
55 Collins Street
Melbourne
VIC 3000
AUSTRALIA

SPC Ardmona Operations Limited
ABN 60 004 077 105

Principal Office – Melbourne
50 Camberwell Road
Hawthorn East, VIC 3123

PO Box 3078
Auburn, VIC 3123
Australia

T 03 9861 8900
www.spc.com.au

Email: operations1@adcommission.gov.au

Dear Sir/Madam

SPC has reviewed the “Assessment of the Market Situation Factors in Italy for Prepared or Preserved Tomatoes” (the Report) which was made available on the EPR on 15 July 2015. With the assistance of its trade consultants, Blackburn Croft & Co, SPC provides the following comments.

1. In general, SPC notes that its analysis of CAP payments to growers of tomatoes and the presence of distorting factors has not been contradicted. The Report confirms that: CAP payments have caused distortions at the level of growers and processors, impacted on supply, there are price effects, the PO's have possible exemptions to what could possibly be described as anti-competitive (cartel like behaviour), and border controls have been a factor in maintaining the distortions caused by long standing CAP payments to the growing and processing of tomatoes in Italy.
2. There are two main areas in the Report that SPC strongly disagrees with and request these be given careful consideration by the Commission:
 - a. The subsidy per hectare accessed and used in the Report
 - b. Relevance and accuracy of the use of an econometric approach in determining flow through.

Subsidy per Hectare accessed and used in the Report

3. SPC believes the Report has erroneously used an average amount per hectare derived from a sample (€776per Hectare) rather than the allocation of the amount provided in Regulation 73/2009 allocated over actual areas used for growing tomato. (€2,802 per Hectare).
4. The Report suggests that the subsidy per hectare contained in the application is incorrect:

Second however the estimate of the subsidy per hectare appears to be an overestimate. SPC Ardmona based its estimate on predictions made in a 2007 publication which sought to estimate the effect of decoupling. (Page 23)

5. SPC's application presents calculations over many years (2010 to 2014, not just 2007) taking into account regulations applicable in those years and actual statistics (e.g. raw prices and actual hectares planted) for those years. It does not rely on the 2007 publication for establishing its estimates but uses it to confirm. This has been overlooked in the Report.
6. The age of the referenced document is not relevant as the amount of subsidy paid to tomato processors/growers has remained relatively constant as dictated by regulation 73/2009. However the hectares of tomatoes grown have changed.
 - a) Regulation 73/2009 provides a national ceiling for tomatoes in Italy of €184 million per year (paragraph 20 application).
 - b) The hectares in 2007 recorded as growing tomatoes in Italy were 63,900 Ha as shown in Chart 26b of the application.
 - c) Applying this across the national ceiling for tomatoes gives a figure of €2,879 per hectare in 2007.
 - d) Applying the national ceiling to the expected hectares in 2014 gives a subsidy of €2,802 per hectare.
7. The Report also suggests that subsidy established by SPC '*appears to be an overestimate*'.

SPC has presented various supporting evidences along with its application and references in the document validating its estimates and the approach taken to arrive at the number.

Further expert confirmation of these figures is found in the reference at footnote 10 of the application. It refers to "An impact Assessment of the CAP Reform Health Check on the Italian Tomato Sector" which noted in Chapter 20:

For processed tomatoes Italy chose to maintain the transitional coupled payments at 50 per cent of the national ceiling until the end of 2010. More specifically, during the three-year transition period (2008-2011) a proportion of the subsidy in the amount of EUR1,300 per hectare in 2008 is in coupled form while the other 50 per cent of national ceiling (EUR91,984 million) moves to the single farm payment scheme. The latter amount is distributed to farmers who received historical payments in the reference period of 2004-2006, while the coupled amount of the payments is subjected to the condition that farmers be members of a producer organization and have a contract for processing.(page 222)

8. SPC presented this reference at footnote 25 of the application. Using the same information from paragraph 26 in the application, the hectares used in 2008 for tomatoes was 69,050.
 - a. Applying the coupled part of the tomato ceiling gives 1,332 Euro per hectare (which is similar to the rounded amount in the above extract).

- b. Applying the balance to be paid as a single payment gives 1,332 Euro per hectare.
 - c. This total 2,664 Euro is consistent with the calculation shown above for 2007 and 2014 (2802 per hectare or 38.4 Euro/tonne paid by the EU) .
 - d. The processors payment of around 88 Euro tonne gives a total revenue to the grower of around 126 Euro/tonne
9. It is worth highlighting that the same reference mentioned above, which affirms SPC's calculation and assessment of the impact on canned tomatoes, was also the first title in the References section on page 34 of the Report.

SPC re iterates that the subsidy rate derived in the application is appropriate (as it bases it on EC regulations applicable and actual data) and validated by many other publications on this matter.

10. The Report seems to suggest that the subsidy paid to the growers is lower using data from the Italian Farm Accounting Data Network.

The Italian Farm Accounting Data Network (FADN) database however suggests that in 2011 the average CAP payment per hectare was in fact much less at 775 €/ha, (sic) for farms located in the plain of Emilia Romagna, one of the main production areas of processing tomatoes in Italy.

However, this information on subsidy per hectare does not appear to have been independently sourced from the FADN for Italian farms but owes its providence to the Solazzo ¹reference and the analysis done in that paper.

Therefore the accuracy of the subsidy (€776/ha) can only be established if the data used to establish this number is reliably reflective of tomato farms providing an input to like goods and importantly is reconcilable to the national payment to the Tomato Industry.

11. The Solazzo paper describes the data used was from a sample of farms which included some tomato growers

The analysis of the economic impact of the greening measures is based on a sample of 453 farms, of which 36 are processing tomato farms located in the plain of Emilia Romagna region. Data is from the Italian FADN 2011 and describes land use, yield, output prices and specific costs per activity at farm level. [Emphasis added]

12. This shows that the sample of farms that was selected for establishing the subsidy was relatively small and that the designated tomato farms in the sample were less than 10% of the total farms.

It is unclear how the subsidy calculated using such a small sample can be relied upon and how the sample data measures up against actual accounting data which should be used.

13. Further, The Solazzo paper also shows that multiple crops are grown on tomato farms. The inclusion of tomato farms with multiple crops, receiving different subsidy payments

¹ References to citations in the Report have been copied where relevant

for different crops, creates an averaging effect and further lowers the subsidy calculated in the sample.

It must be asserted, that the hectare subsidy for tomatoes is what needs to be considered in this investigation.

14. To emphasize the averaging effect of other crop payments on the average subsidy per hectare, a benchmarking study of a typical Italian farm by agri benchmark² shows that a typical farm in Emilia Romagna (the same area as the sample from FADN) has 30 hectares in tomatoes and 62 hectares in other crops. This mix gives an average subsidy in the benchmarking study of 1,200 Euros per hectare.

But only the tomato subsidy (Euro 2800/ Ha) needs to be taken into account as relevant for assessing market situation.

15. Importantly, it should be highlighted that the Report does not attempt to reconcile this rate of subsidy (776 euro/ Ha) to the national amount paid to the Tomato industry or the national ceiling set by regulation EC Regulation 73/2009. It also does not present any validation of the amount compared to various other literature highlighting higher amounts.

Surprisingly, the report omits a discussion on the specific National Ceiling in Italy for Tomatoes which continued in 2014 [para 13 and 20 of the application]. This information gives a per hectare payment of €2802 as shown in this submission para 6. This is vastly different from the 776 Euro/ha (or 10.6 euro/ton) used in the report. No explanation is given in the report for believing that 776 euro should be used in calculations.

16. The Solazzo paper suggests that if the model was tasked to look at the processors then the model (and presumably data collection) would have been different. In the conclusion it noted:

However, this paper aims to assess the differences and the effects of the three proposals discussed in the technical and political process that will lead to the final document of the 2014-2020 CAP. Secondly, the model assumes that market prices are stable and not affected by modifications. Likely variations in the commodity market prices can modify the strategies of processing tomato producers and induce different production decisions. Finally, the model focuses on the agricultural phase without considering the downstream supply chain. A study of strategies which processing industries could use to face the new market and policy scenarios would be an interesting development of the model.

This emphasises the poor use of the Solazzo data for the purpose of establishing a market situation.

17. It is our understanding that the information in the FADN data base is only available on an aggregated basis for a group of farms or for farms within regions. At this level of aggregation information relating to individual farms cannot be identified. Therefore the

² Tomato A New Crop at <http://www.agribenchmark.org/horticulture/sector-country-farm-information0/tomato/country-information.html>

only source representing the payments would be the national budget as directed by Reg 73/2009.

18. EC, Government of Italy, Producer Organisations and exporters have not cooperated in providing data pertaining to actual payments despite requests by the ADC.
19. Adopting data from a 2011 data set aimed at an assessment that is not specifically related to like goods (and the FADN sample is not) and is based on small sample does not add to the robustness of the investigation.
- 20. Therefore whilst SPC agrees with the Report's findings of tomato growers benefiting from the subsidies leading to distortion in raw material prices, SPC reiterates that the amount of subsidy received by tomato growers (as the investigation requires) is far greater (estimated at 2,802 Euro per hectare) than the 'average' value of 776 Euro per hectare in the Report which is distorted by the mix of crops and is based on a small sample size.**

Relevance and accuracy of the use of an econometric approach in determining flow through

21. In Final Report 217³ the Commission explained its approach to investigating a market situation:

The information gathered in relation to agricultural support programs in Italy was requested by the Commission for two purposes:

- a) to investigate whether, by virtue of policy programs applying to the cultivation of tomatoes in Italy, there is a situation in the Italian domestic market for prepared or preserved tomato products that renders domestic sales unsuitable for determining normal values in accordance with s. 269TAC(2)(a)(ii); and
- b) to assess whether the records of exporters of prepared or preserved tomatoes reasonably reflect competitive market costs associated with the production or manufacture of like goods in accordance with the provisions of Regulation 180(2) of the Customs Regulations 1926⁴ (page 30)

22. And also in Case 217 at page 27 the Commission noted:

The influence of government does not, in itself, mean that a 'market situation' exists. The Commission needs to examine the effect such influence has on the market and the extent to which domestic prices are distorted and unsuitable for proper comparison with corresponding export prices

23. SPC's second disagreement with the Report is that it seeks to examine the effect of the subsidy by using a flow through test based on an econometric model using data that is borrowed from Solazzo Report.

³ Alleged Dumping of Preserved or Prepared Tomatoes Exported from Italy

⁴ Replaced by Regulation 42 (Customs(International Obligations) Regulation 2015

SPC asserts that the flow through test is not relevant in determining market situation, is contradictory to the intent of the Act, and its outcome is unreliable in determining market situation.

24. Use of flow through test is not relevant as this test is associated with a countervailing investigation and not market situation investigations.

In the Commission's other assessments of market situation, an accounting and or econometric test does not seem to have been applied in determining market situation. For example in Silicon⁵ case, the uplifted price of one of the distorted inputs (electricity) was not, as far as can be determined, subject to a flow through test either on an accounting basis or by using an econometric approach to assess if the final product was able to increase in price.

Rather the price of electricity was uplifted to a benchmark price in a constructed normal value. That is the non-competitive input was seen as having an effect on the price of the like good.

To guess what the likelihood of the adjusted price of the like good (silicon metal) being sold at that theoretical unsubsidised price is not what a market situation analysis requires.

As long as the effect of the adjusted competitive input (electricity) was to increase the price of the like good (silicon metal) using the available accounts of the manufacturer it was sufficient to show that the market situation exists.

Similarly in the case of canned tomatoes, once the key ingredient (raw tomatoes) price and supply is established to be distorted, the effect of the adjusted input cost (based on the known payment per hectare) needs to be established using a constructed normal value

25. If an economic model was used to see if the Chinese domestic price of silicon metal could increase to recover the uplifted cost it is likely that the elasticities of supply and demand would lead to a speculation that such a price increase was not possible or was insignificant. Therefore a market situation may not have been found.

Undertaking a speculative approach by estimating producer's, manufacturer's, and consumer's reactions can result in erroneous outcomes apart from probably creating an unobtainable threshold in future market situation claims.

The Commission should expect that the market situation found in the Chinese cases could be reviewed if it decides to replace its own accounting based assessment with a speculative analysis. The Commission will be aware that in reaching a decision on the investigated facts it should be careful that its analysis is not undone by guessing what the response will be in the affected market.

26. Further, SPC asserts that the outcome of the econometric model cannot be relied upon due to the inaccuracy of the data used.

⁵ REP 317 Silicon Metal – People's Republic of China

27. Firstly, the model bases its analysis on data from 2011 that predates the investigation period and the data is not sufficiently related to the like goods as explained in the submission earlier.
28. Secondly, the flow through test cannot be reliably used when there is a relationship between the supplier of the input and the processor of the input.⁶

The Report establishes that the Tomato industry in Italy is characterized by cooperatives and vertically integrated processors. The Solazzo analysis is based on a sample in the Emilia Romagna region where the Report itself refers to vertical integration of growers and processors.

'The northern area is characterized by the presence of large self-processing cooperatives, while the southern area is characterized by a high number of mostly small private companies.'

Therefore, this presents a problem in using the Solazzo data and has the distinct possibility of tainting the data and making the flow through analysis unreliable.

In situations where related parties are involved a flow through test is ignored because of the problem of identifying the influence on transactions because of the relationship.

There has been no attempt to identify and exclude possible related parties in the sample.

29. As the Commission noted in Silicon⁷

*The Commission considers that any assessment of whether a situation in the domestic market has rendered those sales unfit for proper comparison should not be limited to individual analysis of the relevant domestic and export prices. **More importantly, and ultimately central to that consideration, is an understanding of the characteristics of the respective markets into which those sales are made***

30. The Report's observation that a significant increase in raw material costs will not affect pricing is unrealistic and unreasonable.

The canned tomato industry operates with thin profitability margins. If raw material cost increases cannot be recovered in selling prices then it would impact on the profitability and eventual viability of processors in the industry. Processors will lose volumes as they exit unprofitable lines setting off a spiral of increasing unit costs as economies of scale are lost.

31. Further, as the Report states the Italian tomato processors have for many years benefited from a subsidy and have been producing products using distorted input costs. This means

⁶ See Mexico –Olive Oil for a summary of pass through at 7.130. In a subsidy investigation the presence of related parties negates the need for a pass through test .Page 12 of the Report refers to large self-processing cooperatives-being related parties See also the Report's Sorrentino at p221.It does not matter if the pass through test is applied for market situation purposes and not for countervailing purposes as the possible influence of related parties remains the same.

⁷ Ibid page 30

that it may be impossible to establish accurate elasticities of supply and demand for the flow through modelling leading to further speculation on the results.

The presence of EU payments under the CAP (producer payments commenced in 2001 replacing minimum prices) has allowed tomato producers to benefit from a long standing market situation which has included border protection. This in turn has meant the domestic market for canned tomatoes has historically been distorted as in 2014.

32. As mentioned in the application:

La Doria statement in 2011 Annual Report ‘... The key role played by the 2011 introduction of the European Horticultural Reform (OCM) which resulted in a decrease in tomato production.

The reform aimed at avoiding excessive production, which was the main cause of the final canned tomato price pressure. As from 2012, market conditions have significantly improved for the group and are reflected in the final tomato product sales price increase and higher volumes both in Italy and abroad.

This should lead to a significant increase in the group’s profitability and overall to a more balanced market context, in terms of supply and demand’

La Doria was also the subject of an analyst’s Report (March 2014) which concluded:

‘... the key role played by the 2011 introduction of the European Horticultural Reform (OCM) which resulted in a decrease in tomato production. The reform aimed at avoiding excessive production, which was the main cause of the final canned tomato price pressure. As from 2012, market conditions have significantly improved for the group and are reflected in the final tomato product sales price increase and higher volumes both in Italy and abroad. This should lead to a significant increase in the group’s profitability and overall to a more balanced market context, in terms of supply and demand.’

La Doria’s 2014 annual report:

*Strong profits in 2014 were principally generated due to higher margin product growth, greater industrial efficiency and improved overhead cost absorption on the basis of increased production volumes, **the ability to transfer the increased costs of a number of agricultural raw materials onto sale prices** and, finally, the reduced procurement costs of some ingredients, packaging materials and of energy. Page 9*

Tomato-based products

The tomato-based product market in 2014 was impacted significantly by the 2013 summer processing campaign which featured a considerable drop in the quantity of fresh tomatoes processed to 4.1 million tonnes, reducing 12.8% compared to 4.7 million processed in 2012 and 19.6% compared to the average for the 2008-2012 five-year period of 5.1 million tonnes.

2013 summer tomato production featured significantly higher raw material costs. Amid a contraction in supply, low sector stock levels and increased raw material costs, finished product prices rose in 2014.

In the final months of 2014, the tomato-based product market was impacted by the summer processing campaign, which featured on the one hand lower fresh tomato

and tin plate costs and lower production yields on the other. Approx. 4.9 million tonnes of fresh tomatoes were processed in Italy, increasing on 4.1 million tonnes processed in 2013 and in line with the average for the 2009-2013 five-year period (4.9 million tonnes). Page 11⁸

33. Therefore La Doria has acknowledged that the regime for providing payments to tomato growers has affected prices, supply and demand factors and demonstrates the conditions required for a market situation.
34. Further the above statements also highlight that La Doria was able to pass on the price increase, which contradicts the Report's assessment.
35. **Distortion of raw prices has been established by the report. The effect of actual increased costs when the distortion is eliminated is what must be examined for the purposes of market situation. Speculating on the outcome as to whether the nonsubsidised input price can be passed through because of the estimated constraints of supply and demand elasticities is misplaced.**
36. A strong preference is to use accounting information, for the undistorted input cost and seeing if the impact on the sell price would be higher.

Conclusion

In summary SPC would reiterate that whilst it agrees with the Report's findings on the distortionary effects caused by CAP, Producer Organisation activities and border controls mechanisms in place, SPC asserts that the level of subsidy is far greater than that presented in the Report. The subsidy rate of Euro 776/ha is not reconcilable to the national ceiling for tomatoes in Italy, is not based on large sample size and is not representative of the like goods.

Secondly SPC believes the Commission will make an error if it relies on the econometric model for its evaluation of the impact of an increased input price on canned prices and therefore market situation. It is unreasonable and unrealistic to conclude that the canned price/volume will not be significantly impacted by the quantum of distortion established by the presence of subsidies, PO activities and border controls mechanisms. Speculating on the outcome of whether the nonsubsidised input price can be passed through because of the estimated constraints of supply and demand elasticities (instead of using actual accounting data) is misplaced and is a risk to current and future use of market situation in a trade remedy action. It is worth pointing again that La Doria has recognised that the payments to tomato farmers benefit the industry and price increases can be passed on.

SPC suggests adjusting the raw prices upwards, in line with the practice in other cases to establish constructed normal values. SPC is able to provide further commentary if any of the above requires clarification.

⁸ Source: LA DORIA S.p.A. 2014 ANNUAL REPORT, [http://www.gruppoloria.com/public/Bilancio2014\(ing\).pdf](http://www.gruppoloria.com/public/Bilancio2014(ing).pdf)