Sir Daryl Dawson
Chairperson
Trade Practices Act Review
c/- Department of Treasury
Langton Crescent
PARKES ACT 2600

Dear Sir Daryl

REVIEW OF THE *TRADE PRACTICES ACT 1974*

Thank you for the opportunity to make a submission on the review of the *Trade Practices Act 1974.*

I am supportive of the need to review the Act, reflecting our election commitment to "prevail on the Commonwealth and other State Governments to jointly produce a discussion paper on the implications of introducing anti-trust laws similar to those in the United States of America". I would recommend the review committee carefully consider the anti-trust laws in the United States in its deliberations on this significant issue for Australian businesses and consumers.

While the submission supports the general approach taken in Parts IV and VII of the Act, and in particular to the sections dealing with mergers and authorisations, I am supportive of:

- the imposition of more severe penalties where this leads to greater international consistency;

- interim cease and desist measures; and

- for firms with substantial market power, I tentatively support a reversal of the onus of proof and the introduction of an effects test.

I appreciate the issues raised in the review of this Act are complex and the successful introduction of these new proposals will in part be dependent on their design. I would therefore encourage your committee to release a position paper for public comment and consultation.

Please contact Dr David Morrison, who is the Director of Structural Policy at the Department of Treasury and Finance, if you would like to discuss any aspects of this submission in further detail.

Yours sincerely

ERIC RIPPER MLA
DEPUTY PREMIER; TREASURER;
MINISTER FOR ENERGY

SUBMISSION BY THE TREASURER OF WESTERN AUSTRALIA TO THE REVIEW OF THE *TRADE PRACTICES ACT 1974*

It is important that trade practices legislation is reviewed periodically to take on board lessons from its previous application and advances in knowledge of the dynamics of economic activity.

Overall, the general approach taken in Parts IV and VII of the Act, to intervene where commercial transactions interfere with the 'fair' operation of the market, is supported. It is apparent that some economic forces take a long time to exert themselves and in the interim economic outcomes may be improved by targeted interventions. It is possible that these interventions may come at some cost to investment. However, on balance it is likely that restricting the unfair practices of unfettered competition will produce a more innovative economy with a higher quantity and quality of investment.

For example, the introduction or development of new technology may be prevented by practices that deter new entry into a market or that cause a firm to exit even though that firm's technology is superior to the technology currently utilised in the industry.

While the general approach taken in the Act is appropriate, the Act appears to be difficult to apply in practice given the difficulty in distinguishing between practices that are unfair and practices that are vigorously competitive. The classic example here is predatory pricing where it is difficult to discern whether a firm is following a deliberate strategy to price below avoidable cost in order to cause another firm to exit the market.

It is understood that the debate in regard to the review of the Act is that some parties want to see the merger law relaxed and the Act amended to reduce the Act's impact on the commercial transactions between businesses. In particular, they want greater protection from potentially negative publicity. Other parties are satisfied with the current merger law but are frustrated with the lack of deterrence. They want to see a reversal of the onus of proof, a strengthening of the remedies available under the Act and possibly the introduction of an effects test to replace the purpose test. There has also been a call by some parties to attempt to balance the playing field by allowing greater tolerance for smaller parties working together to counter the market power of larger parties.

This submission focuses on each of the areas above with the exception of the issue of adverse publicity, given that this is an issue best left for the business community and ACCC to comment on. The comments in this submission are made in the context of the following terms of reference:

- does the TPA inappropriately impede the ability of Australian industry to compete locally and internationally?

- does the TPA provide an appropriate balance of power between competing businesses, and in particular businesses competing with or dealing with businesses that have large market concentration or power? and

- does the TPA promote competitive trading which benefits consumers in terms of services and price?

Specific comments in regard to the petroleum and retail industries are provided in the attachments.

Does the TPA inappropriately impede the ability of Australian industry to compete locally and internationally?

The Act does not appear to inappropriately impede the ability of Australian industry to compete locally and internationally. In arriving at this conclusion consideration was given to the main argument for greater tolerance of mergers, which is that since Australia is a relatively small economy, to be internationally competitive firms need to command a relatively greater share of the domestic market to achieve economies of scale.

Consideration was also given to the main counter-argument, which is that more intense competition in the domestic market may strengthen the ability of firms to withstand and counter the competitive pressures in the international market place.

However, this debate is not pursued in this submission. The Act should provide for this debate to be had in the courts, whereby over time prosecutors and defendants can prepare their arguments based on the latest research in this area.

In reviewing whether the merger law is impeding firms from expanding internationally it is useful to consider two general scenarios:

- the domestic companies face substantial import competition and wish to merge to compete more efficiently both domestically and internationally; and

- the domestic companies do not face substantial import competition but wish to merge to more successfully expand internationally.

The first scenario is unlikely to be a concern to the ACCC given that, in making its decision, it must take into account the actual and potential level of import competition in the market. In practice it is apparent that the ACCC has only rarely prevented acquisitions where there was import competition. In this regard, the following statement by Professor Fels is noted:

> "In the last ten years the Commission has not opposed any mergers where imports make up ten per cent or more of the market." (p5, The Trade Practices Act, Are We Becoming a Branch Office Economy?, April 2002)

The second scenario is unlikely given that if an Australian company is looking to sell internationally it is also likely to be facing import competition. Nevertheless, in the absence of significant import competition, there may be a net public benefit in allowing the merger if the increase in output resulting from the international expansion more than offsets the efficiency loss from any reduction in output or ongoing productivity gains in the less competitive domestic market.

However, in this situation the Act allows for the authorisation of otherwise illegal trade practices provided the applicant satisfies the ACCC that there are likely to be real net public benefits as a result of the acquisition.

Specifically, s. 90(9A) of the Act states that, in weighing up the public interest test when considering whether to grant an authorisation, the ACCC must have regard to whether the authorisation would result in a "significant increase in the real value of exports" and any "significant substitution of domestic products for imported goods". It must also take into account "all other relevant matters" relating to the international competitiveness of any Australian industry. Such other relevant matters may include the possibility that the merged entity will use higher prices from the domestic market to subsidise their overseas venture.

Given that authorisations are available if there is a well argued net public benefit there appears to be little reason to change the Act.

In conclusion, it is not apparent that the Act inappropriately impedes the ability of Australian industry to compete locally and internationally.

Does the TPA provide an appropriate balance of power between competing businesses, and in particular businesses competing with or dealing with businesses that have large market concentration or power?

In an efficiently operating market it is expected that small firms will find it difficult to compete or deal with larger firms that may benefit from greater economies of scale. It is likely that the smaller firms in such a market would either compete in terms of quality of service rather than price, specialise in some part of the market not touched by the larger firms, or go out of business. Consumers should benefit as a result of these dynamics.

However, in a market where there is an uneven balance of power between competing businesses it is likely that larger firms will have greater opportunity to use their market power illegally, through for example, exclusive dealing, refusal to supply or predatory pricing. Options for better deterring larger businesses from using their market power illegally are discussed in the next section.

With respect to smaller firms that are competing or dealing with much larger firms, the authorisation process is an appropriate way for firms to argue that certain arrangements, such as collective bargaining provisions, are in the public interest. Presumably, such firms would need to argue that prices would be lower as a result of their arrangement.

Some parties have proposed changing the Act by introducing a concentration threshold below which small firms engaged in collective bargaining in a market involving very large competitors would not need to seek authorisation. This proposal is not supported because it would interfere with market forces that drive firms to achieve optimal scale in an industry. However, a proposal that accelerated the consideration of applications for authorisation would be supported.

In conclusion the Act provides an appropriate process whereby small businesses can seek authorisation for strategies that counter the market power of larger businesses as long as these strategies are in the public interest. However, the application of the Act could be improved by streamlining the processes associated with granting authorisations.

Does the TPA promote competitive trading which benefits consumers in terms of services and price?

A major concern is that the Act's application may not be effectively establishing clear rules for what is acceptable and what is unacceptable trade practice. As mentioned earlier, distinguishing between vigorously competitive conduct and illegal conduct is difficult and this distinction may be best arrived at through the application of case law over time. However, if clearly illegal transgressions are not being prosecuted for whatever reason or if firms do not consider the Act to be a sufficient deterrent then consumers will suffer in terms of higher prices or lesser quality services.

There are difficulties associated with proving that the Act has been contravened, the length of time involved in arriving at a decision, and the fact that penalties are only in the form of pecuniary fines. Various proposals attempt to better deter illegal conduct, such as:

- reversing the onus of proof so that the defendant rather than the prosecutor is required to prove innocence;

- replacing the purpose provision with an effects provision whereby it would be sufficient for a prosecutor to demonstrate that the effect of what one firm had done had harmed another; and

- strengthening the remedies available under the Act, such as giving courts the power to order firms to "cease and desist" anti-competitive behaviour or to divest a portion of their assets; and to provide the option of criminal trials in exceptional cases with penalties in the form of jail terms or substantial fines.

In addition, there are proposals to limit the time available to courts to issue their decisions.

Whether these proposals are needed depends on the extent of the problem and the effectiveness of the proposals, which are issues better left for the ACCC to argue. However, a number of preliminary comments can be made on each of these issues (specific comments in regard to the petroleum and retail industries are provided in the attachments).

First, international consistency is important and if multi-national firms are viewing Australia as a 'soft-touch' in terms of its competition law then if this is not corrected, Australian consumers will suffer. For example, the United States, Canada and Japan regularly impose criminal sanctions for collusion. The committee is encouraged to give careful consideration to proposals that promote international consistency in the application of remedies for illegal trade practices. In particular the call by the by the ACCC for the inclusion of jail sentences for officers of corporations as a remedy against such breaches is supported.

Second, where there is clear evidence of a practice that has substantively harmed a competitor, and where there are reasonable grounds for assuming that this harm was the result of an illegal practice, then the proposal to give Courts the power to order a firm or firms to 'cease and desist' their anti-competitive practice makes sense. It is envisaged that the order would be an interim measure before a final decision were reached. Of course, the issue of what are 'reasonable grounds' for intervention is one that will need careful consideration by the review committee.

With regard to the proposals to reverse the onus of proof and introduce an effects test, these proposals have sufficient merit to warrant careful consideration. Reversing the onus of proof means removing the presumption of innocence. There is a public interest argument that the presumption of innocence should not apply to businesses with substantial market power. However, it may be overly onerous to apply this proposal to all businesses. It is understood that the ACCC already has greater evidence-finding powers than would be allowed in criminal actions, and these greater powers may be sufficient when applied to most businesses.

A move away from the 'purpose test' towards an 'effects test' may be another appropriate measure to deter the illegal use of market power by large businesses. As with the proposal to reverse the onus of proof, it may be appropriate to only apply the 'effects test' to businesses with substantial market power. This would reduce the risk associated with dissuading competitive behaviour that is in the best interest of consumers but which may result in substantive harm to other firms. However, it is recognised that it will be challenging to design an 'effects test' as it is difficult to distinguish between competitive and anti-competitive behaviour.

In summary, this submission supports:

- the imposition of more severe penalties where this leads to greater international consistency;

- interim cease and desist measures where these are warranted; and

- for firms with substantial market power, this submission gives tentative support to a reversal of the onus of proof and the introduction of an effects test.

As the issues raised in the review of the Act are complex and the successful introduction of new proposals would depend on their design the review committee is encouraged to release a position paper for public consultation.

TRADE PRACTICE CONCERNS IN THE PETROLEUM INDUSTRY

An area of concern for the Western Australian Government is the capacity of the *Trade Practices Act 1974* to address conduct within the petroleum industry that may be anti-competitive. For example the State Government has previously raised concerns over the practice whereby a vertically integrated wholesaler sells fuel to an independent retailer at a price that is significantly higher than the price that the product is sold by the wholesaler at its own retail sites. Although this practice would place the independent retailer at a significant competitive disadvantage, it is unclear whether it constitutes a breach of the Act.

In the province of Quebec in Canada, legislation has been specifically enacted to address this issue in the context of petroleum product prices. The following is a section from that legislation which prohibits such conduct[1]:

> "Where, in a given zone, an enterprise sells gasoline or diesel fuel at retail for a price that is lower than the cost to a retailer in that zone of purchasing and reselling that product, the enterprise is presumed to be exercising its rights in an abusive and unreasonable manner, contrary to the requirements of good faith, and to have committed a fault against the retailer"

The Western Australian Government acknowledges that such matters are best addressed at a national level and consequently would support a strengthening of the provisions of the Act to more effectively address the misuse of market power. The inclusion of an 'effects test' to assess the impact on competition of such practices would be an important step in maintaining a competitive balance in markets where competition is otherwise restricted.

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[1] An Act Respecting Petroleum Products and Equipment, Quebec, Canada s.67

ATTACHMENT 2

TRADE PRACTICE CONCERNS IN THE RETAIL INDUSTRY

The Australian retail sector has a high degree of concentration. In the face of an ongoing accumulation of market share by larger corporations, the Western Australian Government supports small retailers and their national peak bodies who have questioned the efficacy of the *Trade Practices Act 1974* to uphold competitive market conditions.

Two Commonwealth Parliamentary inquiries have recently been undertaken into the fairness of national retail market trading and approaches adopted in overseas economies to regulate business conduct.

(a) Finding a balance – towards fair trading in Australia. The (Reid) Report by the House of Representatives Standing Committee on Industry, Science and Technology; May 1997.

The Committee received 278 submissions including one from the Council of Small Business Organisations of Australia claiming that anti-trust laws in the United States of America limited the market shares of the three largest food retailers to 17% of the market.

The Reid Committee made no reference to the capping of market share in its recommendations but included an amendment to the TPA to give the ACCC power to undertake representative action against market power abuse; and

(b) Fair Market or Market Failure? A review of Australia's retailing sector. The (Baird) Report by the Joint Select Committee on the Retailing Sector; August 1999.

The Committee received over 300 submissions. Davids Ltd, an eastern States wholesaling company supplying to the independent grocery sector, suggested:

> "to tilt the playing field in the interests of fair competition and in the public interest the Government must cap the market share of the chains through amendments to the *Trade Practices Act 1974* or through the introduction of US anti-trust style laws to break up the monopoly power of the chains."

Foodland Associated Limited (FAL), which supplies a major portion of stock to the Western Australian supermarket groups and independents, also submitted that product costs and choice in rural towns could only be protected in the public interest with the imposition of a limit on the growth of the retail chains. The Managing Director of FAL, Mr Barry Alty, stated that "a market cap would be the only insurance against the survival of the independent sector".

Other small business interests claimed that in the US, the body of anti-trust laws ensured wholesalers/suppliers are required to sell their products to retailers at the same price irrespective of the quantities ordered.

The Western Australian State Government remains concerned that domestic markets are dominated by a small number of large corporations. This situation has the potential to have a detrimental effect on consumers and small business.

Through these inquiries and in responding to the issues presented to members of the State Government, small retailers have identified their preference for US type anti-trust laws being included in the Act.