

Trade Practices Act Review

A submission by the

New South Wales Co-operatives Council

SUMMARY

1. This submission has been prepared by the New South Wales Co-operatives Council to raise issues relevant to co-operatives for the consideration of the Review Committee. The submission does not purport to represent the views of the Minister for Fair Trading or the New South Wales Government.

2. The Cooperatives Council seeks a revised and extended Notifications process for cooperatives registered and regulated under State Cooperatives legislation. The Council submits that a wider range of matters should be covered under a revised Notifications process for cooperatives, including:

- horizontal agreements between members;
- exclusive dealing arrangements, including third line forcing;
- price agreements between members for the acquisition or supply of goods or services through the cooperative;

recognising that efficient dealing between small members and large market participants enhances competition and provides demonstrable public benefit.

3. The Cooperatives Council submits that there is a case for extended immunity from competition laws for registered cooperatives on three grounds:

i. Transparency, equity and democracy are protected in the institutionalised collective form of cooperatives through State legislation to minimise any detriment from cooperative action.

ii. Through aggregation and leveraged bargaining power, cooperatives generate net public benefit, notably in wider consumer choice, lower prices, better quality goods and services and greater sustainability of smaller businesses.

iii. The small size of individual cooperatives and their limited influence in the market make them unlikely to have any appreciable anti-competitive impact on the market as a whole, testified to by the low incidence of authorisations and notifications from cooperatives under the Trade Practices Act to date or action on the part of the Australian Competition and Consumer Commission (ACCC).

Co-operatives Council

4. The NSW Co-operatives Council is established under the Co-operatives Act 1992 with functions:

- (a) to encourage the development and integration of the co-operative sector;
- (b) to advise and make recommendations to the Minister on the following

matters:

- any action to be taken for promoting co-operative principles and for encouraging and assisting in the formation of co-operatives
- policies for the administration of the Act and the regulations
- the regulations to be made under the Act
- such other matters as may be referred to the Council by the Minister or as may be prescribed;

- (c) such other functions as may be conferred or imposed on the Council by or under this Act.

Co-operatives Act 1992 (NSW)

5. The NSW Co-operatives Act is similar, in its core provisions, to legislation operating in the other Australian States and Territories. The regulatory regime administered by the Registrar of Co-operatives requires registration of each co-operative's Constitutional Rules which must satisfy the test for equity and transparency before they come into effect.

6. Co-operatives have existed in Australia and elsewhere for a very long time. They are characterised by a common bond of mutual interest and interdependence, the institutionalisation of which requires rules and governance that in their very form raise Trade Practices Act issues. An example of this can be seen in s. 78 of the NSW Act .

7. ***78 Members etc may be required to deal with co-operative***

(1) The rules of a co-operative may contain provisions that require a member

to have any specified dealings with the co-operative for a fixed period and to enter into a contract for that purpose.

(2) A co-operative may, if authorised by its rules, make a contract with a member containing provisions that require the member to have any specified dealings with the co-operative for a fixed period.

(3) In particular, any such provisions of the rules or a contract may require a member:

- (a) to sell products through or to the co-operative, or*
- (b) to obtain supplies or services through or from the co-operative, or*

- (c) *to pay to the co-operative specified sums as liquidated damages for any failure to comply with a requirement authorised by this section.*
- (4) *Any sum so required to be paid to the co-operative as liquidated damages is for the purposes of section 80 (Charge and set off of co-operative) to be to be a debt due from the member to the co-operative.*
- (5) *A contract authorised by this section is binding on the co-operative and all other parties even though but for this Act the contract would be invalid as being in restraint of trade.*
- (6) *Rules authorised by this section are authorised even though, but for this section, the rules might be invalid as being in restraint of trade*

Co-operatives in the Marketplace

8. A cooperative is a democratic organisation owned and controlled by the people it serves who join together for a common benefit. A cooperative may be formed for the provision of goods or services to members or for the supply of goods or services to the general public. Cooperatives are based on the values of self-help, self-responsibility, democracy, equality, equity and solidarity. These are put into practice through seven cooperative principles, set out in Section 6 of the Cooperatives Act 1992 (NSW). These are:

- Voluntary and open membership
- Democratic member control
- Member economic participation
- Autonomy and independence
- Education, training and information
- Cooperation among cooperatives
- Concern for the community.

9. A registered cooperative may carry out any activity or activities contained within its rules. These activities will reflect the nature of the cooperative's involvement in areas such as – primary production, manufacturing, trading, community or social activity.

10. Co-operatives originally predominated in agricultural industries, however, they now have a presence in the production and supply of a broad range of goods and services. They also conduct purchasing activities on behalf of members as well as providing markets for the supply of members' goods and services.

11. Co-operatives in Australia are engaged in a wide range of activities. A significant number are formed by primary producers for processing and manufacturing of rural agricultural products such as meat, sugar, tobacco, etc, grain milling, cotton ginning and dairy products manufacturing. There are also trading co-operatives for farm and construction machinery wholesaling, farm produce and supplies trading; fish wholesaling co-operatives; for water supply and providing other

services to agriculture, such as cane harvesting. Co-operatives are also engaged in book and periodical publishing, selling handicrafts, providing taxi services and some services to business such as advertising, administrative and business management services. In rural areas, there are also co-operatives operating supermarkets and grocery stores. In the area of Human Services, co-operatives provide aged care and childcare services, housing and holiday accommodation such as ski clubs. Co-operatives are also engaged in creative arts and operating museums, performing arts venues, radio stations, and sports grounds and facilities.

12. There are nearly 2400 co-operatives registered under State co-operatives legislation. The turnover of all co-operatives is estimated at around \$ 4.5 billion. Most co-operatives have an annual turnover of less than \$ 1 million. In NSW, 70% of the co-operatives have an annual turnover of less than \$ 1 million. Around 3.5% of co-operatives have an annual turnover of over \$ 10 million with only 0.5% being large co-operatives with a turnover of over \$ 100 million.

The case for cooperatives

13. There is a respectable body of scholarship and business management practice pointing to strategic collaboration as decisive to sustained competitive business performance in the face of fast-paced, volatile and increasingly connected and crowded markets. For examples, see the writings of Harvard Professors Michael Porter and Rosabeth Moss Kanter and the OECD's work on innovation and knowledge-based economies. Organisation in the form of cooperatives with active membership rules provide a long-established and internationally-recognised vehicle for successful business performance in this modern competitive environment.

14. Collective bargaining and aggregation for scale are core activities of cooperatives. An efficiently functioning cooperative is not so much a restraining influence upon the competitive rivalry among its members, as a positive mechanism for small individual businesses to rebalance market forces and in doing so, enhance competition and efficiency and produce other national interest outcomes such as sustainable small enterprise, employment, export growth and so on.

15. A trading co-operative presents in the marketplace in much the same way as a trading corporation. But unlike the corporation, its essential operating rules are subjected to the provisions of the Trade Practices Act because its members are treated as individual or separate economic entities. By entering into the co-operative, the members are signalling their intention to operate as one integrated force. So it is argued that too much focus on the form and governance of the combination of the members could well inhibit full appreciation of the economic effect of the co-operative in the competitive marketplace.

16. Classical examples of the collective bargaining nature of co-operatives include horizontal agreements amongst members to supply goods or services in combination and at an agreed price. This facilitates the achievement of some balance in bargaining power where the acquirer is a larger economic entity than any of the members who would otherwise be acting alone. Another example is where the co-operative acquires goods or services on behalf of members acting in combination. The identification of the supplier will usually follow the invitation of competitive bids and the securing of

the “best offer” will be dependent on the co-operative ensuring that all members deal with the successful bidder for the period of the contract. Unless the underlying rules of governance were able to secure the effectiveness of negotiated arrangements, the *raison d’etre* of the co-operative and its efficiency objectives would be un-achievable.

17. International examples reinforce this argument. Policy considerations in the US recognise that rural production markets are comprised of large numbers of small suppliers with a concentration of larger buyers. Markets of this nature are imperfect because of the disparate bargaining power of the participants and the poor exchange of information between suppliers when those same suppliers operated individually rather than collectively. Hence, policies tended to recognise that agricultural co-ops provided net public benefits by enabling these small (often individual) suppliers to aggregate and provide a more equitable balance of bargaining power in these markets. Equitable bargaining power addressed some of this market failure and in this way was pro-competitive.

18. Agricultural co-operatives in the US have been entitled to exemption from the rigours of competition laws because they represent a politically acceptable response to market failure in rural industry. The combined effect of the Capper-Volstead Act, Agricultural Fair Practices Act and the Robinson Patman Act permits agricultural co-operatives to engage in collective bargaining, and price fixing (but not predatory price fixing or price enhancement). They cannot engage in boycotts, coercive conduct or impose exit barriers upon members, nor can they require members to supply 100% of their product, however, rebates to encourage patronage are acceptable.

19. In other jurisdictions, as outlined in the submission by the ACCC¹, various forms of authorisation for some anti-competitive conduct are available in respect of businesses wherein there is no appreciable effect upon competition because of their size or influence in the market. These “small business” authorisations argue that there is justification for a notification process to be available for a broader range of anti-competitive practices. The broader availability of the notification process is dependent upon the applicant being a small business in a market with a concentration of larger counterparts. In essence, it would be available in the same type of market wherein co-operatives have been permitted to operate as a collective bargaining agent in the US.

20. Co-operatives in Australia and other jurisdictions are an institutionalised means of aggregation for market participants with similar objectives. They facilitate collective negotiation by presenting a managed incorporated entity with built in equity and transparency features. As an entity with a strong focus on benefits to members, they also provide a more efficient means of communicating market information to individual supplier members in terms of price, quality, demand and product development.

21. Co-operatives formed under State legislation provide the same institutionalised system for collective bargaining based upon co-operative principles and subject to a regulatory regime which serves principles of accountability, transparency and equity. This regulatory regime provides checks and balance to the

¹ ACCC submission to the Review of the Trade Practices Act, Part 4.2

behaviour of cooperatives, as well as defining precisely cooperative entities and the nature of active membership rules that scope their cooperative agreements.

Co-operatives and the Trade Practices Act

22. In order to operate as they were intended, co-operatives need to be able to engage in a range of practices that potentially breach the Trade Practices Act. Those practices are:

1. Collectively negotiate on behalf of members through the co-operative entity the terms of supply to a buyer.
2. Horizontal price fixing by requiring members to supply to the co-operative at a particular price.
3. Fixing prices [to a lesser extent] by requiring the co-operative to sell at a particular price and requiring members to sell at the same price if they sell outside the co-operative.
4. Exclusive dealing by requiring members to provide to or acquire from the co-operative a predetermined amount of product or service.
5. Third line forcing by requiring members to acquire goods or services from another body as part of the negotiated supply arrangement through the co-operative.

23. Practices 4 & 5 are able to be accommodated within the existing Trade Practices Act regime through the notification process, with Practice 5 (third line forcing) subject to an adjusted notification procedure.

24. Practices 1 – 3 are also able to be accommodated within the Trade Practices Act regime through the more complex and expensive authorisation process.

25. The authorisation process has been avoided as much as possible because of the following factors:

- The onus, and hence the attendant difficulty, is upon the applicant to prove net public benefit in a fairly specialised field of law and economics.
- The high costs of an authorisation represented by -
 - Application costs
 - Professional preparation costs
 - Opportunity costs over the length of time for the process to be concluded.
- Uncertainty of the outcome.

26. These factors inherent in the authorisation process militate against applications by co-operatives and the lack of a simpler process is a real barrier for co-operatives in carrying out the functions for which a co-operative was designed.

Proposal

27. The Council wishes to place before the Review the proposition that the process of enhancing the performance of Australian small enterprises should receive special recognition in the administration of the Trade Practices Act. In particular, the role of co-operatives in providing a mechanism for the achievement of small business efficiencies and competitive energy is, in the Council's view, worthy of special consideration.

28. Specifically, the Cooperatives Council seeks a revised and extended Notifications process for cooperatives registered and regulated under State Cooperatives legislation. The Council submits that a wider range of matters should be covered under a revised Notifications process for cooperatives, including:

- horizontal agreements between members;
- exclusive dealing arrangements, including third line forcing;
- price agreements between members for the acquisition or supply of goods or services through the cooperative;

recognising that efficient dealing between small members of large market participants enhances competition and provides demonstrable public benefit.

29. Co-operatives, as an institutionalised aggregation of market participants warrants the same consideration for an extended notification process as obtains for small business because of the generalisation that can be made about their size and because of the net public benefits that are available through an organisation that is formed within the co-operative regulatory regime.

30. Co-operatives, before they may be formed must demonstrate that they comply with the 7 co-operative principles set out in section 6 of the Cooperatives Act (1992) NSW) as outlined earlier.

31. Primarily, a co-operative provides an equitable and transparent means of aggregation for smaller market participants and provides a leveraged bargaining power in an imperfect market. Increased bargaining power through collective action has not of itself, in past authorisation applications, been seen as a net public benefit. But, public benefit results from a market where participants are more equitably balanced by delivering lower prices, better choice or better quality products.².

32. A better match of bargaining power using collective negotiation has been seen to deliver the following net public benefits:

² ACCC, Rural Industry and the Trade Practices Act: a guide for rural producers, August 2002 at p30

- ❑ The promotion of cost savings resulting from the elimination of the need for individual legal and financial advice for suppliers that are cooperatives when entering into supply contracts with buyers. This will be reflected in lower prices to consumers³.
- ❑ Economies of scale which deliver cost savings and then lower prices to consumers⁴.
- ❑ Fairer contractual terms in commercial arrangements. The leveraged bargaining position from collective bargaining through a co-operative will result in fewer harsh and unconscionable contractual terms. This will in turn reduce potential litigation costs and enhance supply continuity by reducing potential insolvency problems faced by parties under unfair contracts⁵.
- ❑ The likelihood of increased competition in a particular market with a consequent reduction in price for consumers⁶.
- ❑ Better information and benchmarking in an industry. Co-operatives provide their members with better information because they are guided by co-operative principles and a regulatory regime to encourage transparency and accountability. Co-operatives will often impose standards or accreditation for members to ensure confidence in the quality of the product being supplied. This leads to a better quality product for consumers and a self-regulating benchmarking system⁷.
- ❑ Industry stability can be enhanced by collective arrangements that tend to promote price stability and eliminate wide price fluctuations. Investment in markets with certainty and stability is more likely, whereas a market with wide seasonal or regional fluctuations can create information costs for participants and discourage long term investment⁸.
- ❑ Enhanced research and development investment is available through aggregation under a co-operative model. As part of their commitment to co-operative principles, co-ops contribute to research and development both in their respective industries as well as in management by providing a range of educational opportunities for members and by direct investment in research efforts⁹.

33. The registration process for co-operatives involves an approval process of the entity's constitutional rules to ensure compliance with the Co-operatives Act 1992 and co-operative principles. Both the rules and the regulatory regime are designed to promote democratic control and transparency as well as allowing for open and voluntary membership. The approval process for rules is guided also by competition principles and the Registry of Co-operatives may reject rules that coerce members to supply 100% of their product to the co-operative or that coerce members to refuse to deal with other parties (boycotts). The system of registration and rule approval militates against activities which can only produce a public detriment by reducing the number of participants in the market and creating a barrier to entry in a market. [cf Darwin Radio Taxis Case].

³ Authorisation applications by Premium Milk Supply & Mater Misericordiae Hospital.

⁴ Authorisation applications by Mater Misericordiae Hospital, and In re Rural Traders Co-operative (WA) Ltd & Ors (1979) ATPR 40.110

⁵ s51AC Trade Practices Act, ACCC, Rural Industry and the Trade Practices Act: a guide for rural producers, August 2002, Chapter 3

⁶ Authorisation application by Australian Dairy Farmers Federation

⁷ Authorisation applications by Australian Dairy Farmers Federation, Premium Milk Supply, CSR, Australian Sugar Milling Council

⁸ Authorisation application by Golden Circle

⁹ Authorisation application by South Australian Oyster Growers Association

34. The concession to small business by the ACCC in its submission and the net public benefits available through the institutionalised collective form of a co-operative establishes a strong claim for a less onerous path to immunity from competition laws than through the authorisation process.

35. The ACCC in its submission suggests a broader availability for small businesses of a notification process for collective negotiation and associated practices which potentially breach s45 of the Act. Problematic in the ACCC's option is the definition of small business as an eligibility criterion for this concession¹⁰. The small business concession is primarily founded upon the premise that anti-competitive conduct by organisations or individuals of this size is unlikely to have any significant anti-competitive conduct in the market.

36. A high proportion of co-operatives would probably fit most criteria for small business, as indeed would the members of those co-operatives. On this basis alone co-operatives ought to receive the same consideration. However, the argument that co-operatives should have the concession of a broader notification process is stronger than the simple argument to support a small business concession. The case for a concession for co-operatives draws on the argument that an aggregation under co-operative principles and subject to its own regulatory regime will readily deliver net public benefits. Further, unlike in the case of small business, definitional problems are avoided as the Cooperatives Act defines registered cooperatives.

37. The Cooperatives Council supports a broader Notification process in respect of co-operatives. The Council supports the process suggested in the ACCC's submission whereby immunity is not immediate upon notification, but would occur after 30 days to allow an opportunity for the ACCC to object after an assessment of matters such as the size or market influence of a particular co-operative and whether the co-operative operates with or in a system with exit or entry barriers.

38. In summary, the Cooperatives Council submits that there is a case for extended immunity from competition laws for registered cooperatives on three grounds:

- i. Transparency, equity and democracy are protected in the institutionalised collective form of cooperatives through State legislation to minimise any detriment from cooperative action.
- ii. Through aggregation and leveraged bargaining power, cooperatives generate net public benefit, notably in wider consumer choice, lower prices, better quality goods and services and greater sustainability of smaller businesses.
- iii. The small size of individual cooperatives and their limited influence in the market make them unlikely to have any appreciable anti-competitive impact on the market as a whole, testified to by the low

¹⁰ ACCC submission to the Review of the Trade Practices Act, at pp126-127

incidence of authorisations and notifications from cooperatives under the Trade Practices Act to date or action on the part of the ACCC.

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