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SUBMISSION TO THE RETAIL TRADING HOURS COMMITTEE WESTERN AUSTRALIA

April 2003

1 Preamble

This submission is not intended to be comprehensive. In writing it I have drawn on other work I have done elsewhere.

I also do not intend to provide the statistical status and trends of the Western Australian market. I am confident that the Retail bodies will provide those for the Review.

I intend to contest the theory of the benefits of further trading hours deregulation, and to indicate other factors such as the Trade Practices Act that affect the market situation.

It is for the Government to determine the actual hours provision, taking into account the interests of the various business and community stakeholders.

I contend that further trading hours deregulation is not necessary for consumers and will be bad for competition. It will have detrimental social and economic effects.

We must acknowledge that a viable and thriving independent sector in the retail industry is desirable of itself and that it has an economic and social value that should not be lost.

In retailing, this independent sector is most at threat in Australia in the supermarket sector, where the critical mass essential to its survival is under threat. This critical mass is also vital to a viable independent wholesaling sector. The two are inseparable, and this fact is reinforced in smaller isolated markets like WA.

However the trend is also emerging in non-supermarket retail sectors, and that problem needs to be addressed to prevent such crises emerging there too.

In Western Australia the sensible balanced approach of successive State Governments on trading hours has ensured the largest independent retailing sector in the country.

This is a circumstance unique to Western Australia.

The case has not been made that the cost of significantly diminishing the independent sector in Western Australia is justified by greater economic or social benefits.

The idea that deregulated trading hours elsewhere in Australia have generated greater benefits than costs is an assertion. If the rest of Australia had WA's policy instead, based on the WA experience it is likely that a much larger independent sector would be in place, without any significant loss in consumer service.

There can be no misunderstanding of the importance of the present policy.

Nor should there be any misunderstanding of how badly big business supermarket chains want to deregulate trading hours so that they can drive the independents out of business.

Market concentration entails the dominance of the market by the few. In other words fewer competitors result. At the heart of this trend lies the danger that the destruction of competitors will result in the destruction of competition.

It should not pass unnoticed that the State with the largest independent sector, Western Australia, has managed the issue of trading hours better than the rest of Australia.

In my view, there is a clear link between the dominance of the majors, and the extent of trading hours deregulation.

Western Australia has been much better than other State governments in assessing these matters in the past. Other State governments need to take much greater account of the social and economic impacts of deregulated trading hours than has previously occurred.

2 Core Proposition 1

It is important that the Retail Industry and its Associations supports progressive change which is in the Community's interest. However, it is also important that the Community does not support change which is harmful to the Retail Industry, particularly Small Business.

Lifestyle and values

The trading hours debate is as much about lifestyle and values as about commerce. Lifestyle is about the importance of a day off, a day of rest. Sunday has traditionally been that day off when children, family and friends can be together.

The retail trade, particularly small business, is not some separate group to be exploited and sent off to a 7-day a week / 24-hour trading day, while everyone else enjoys a 5-day, 38-hour working week.

Small business owners and staff have to be on the job for a full trading week. In contrast, big business oligopolies in the retail sector can roster casual and part-time staff to cover extended hours.

The big nationals and competition

Australia has a dangerously high concentration of retail power oligopolised by a few majors. This is not healthy. The big players in the retail business are strong lobbyists to governments. Their trade organisations are well-funded, well-connected, publicity machines.

Smaller retail associations, which represent a very large number and variety of small and medium businesses, do not agree with the push for unfair deregulation of trading hours.

The claim that the consumer demands widespread deregulation and Sunday Trading is a myth. There is little evidence of significant consumer demand for *all* retailers to be on a 7-day trading week or a 24-hour trading day.

The market share growth of big retail business is often at the expense of small retail business and such destruction can result in monopoly. Monopolies are not good for the Community.

The Community needs small business as much as it needs medium and big business. The extremist position of a 7-day week / 24-hour trading day actually leads to less competition because of the closure of small business and greater market share for the oligopoly of major nationals. It will lead to more monopolies, more concentration of power and economic might.

This eventually leads to higher prices, less employment and less competition.

Recommendations

- No further deregulation of trading hours;
- As a General rule, trading should not be on a Sunday (as a principle). For some industries, such as the hospitality industry, there are legitimate exceptions to the no-trading on Sunday principle;
- Any government review of trading hours must take into account the following:

    - Lifestyle needs and quality of life in the industry affected;
    - Small business needs and views;
    - Economic concentration and monopolisation trends in competition, whether local, regional, state or national;
    - Australian business content in the industry or sector;

- Core hours (which retailers must trade) should not (as a general principle) be less than 40 hours. There will be exceptions, such as weekend markets;
- Maximum hours should not (as a general principle) be more than 74 hours. This allows for instance, for a very generous 8 to 8 trading day, five days per week, with 8 to 10 on the sixth day;
- Against clear State criteria, the right to vary the general principles should vest in Local Councils, who must consult the local community and all interested parties fully. The State should consider whether the Minister would need to preserve a veto right in these matters;
- Core (40) and Maximum (74) hours may be concentrated in as few days as the retailer wishes, unless the Local Council objects, in which case the retailer must be open at least five days (with obvious exceptions such as markets.). Hours should be spread in any pattern the retailer wishes, over the six allowed days of trading. (Obviously, these freedoms are likely to be restricted by most leases, but there should be no statutory restriction on when a retailer opens and closes);
- Shopping centres should not be able to require their tenants (via leases) to match the hours a general shop may choose to trade.

3 Core Proposition 2

It is not in the interests of Western Australia to submit to the dictates of the NCP on Trading Hours deregulation. In any event, the NCP has been found to be flawed.

Competition Policy has two main aspects. One is the regulatory aspect – the Australian Competition and Consumer Commission (ACCC) and the Trade Practices Act (TPA). The other is the promotion aspect – through the National Competition Policy (NCP).

The current policy

NCP was drafted at the height of economic rationalist ideology, as a one size fits all methodology designed to impose competitive pressure on everything from the utilization of water to the marketing of eggs and distribution of electricity. At the heart of its approach was a ‘big is beautiful and the small are expendable’ philosophy.

An extensive Senate inquiry conducted during 1999 clearly showed that the benefits of NCP largely accrue to medium and large business and those residing in metropolitan areas. Those in small business and those in the regions have felt the burden. The Committee found:

At the individual level, the costs are often immediate and easily identified, while the benefits are long term, less easily defined, and do not always go to the party bearing the costs.

I agree that in theory competition should result in an efficient allocation of scarce resources and should result in consumers paying lower prices for commodities.

The problem with the implementation of NCP has been the under-recognition of the costs of implementation of the policy. The focus has been almost solely on the economic pricing consequences, with too little attention paid to the economic structural effects (small business) and to social and environmental impacts. That has its own costs, which have at times exceeded the supposed economic benefits.

The Senate Committee also commented:

The Committee found a clear need for a proper quantification of the benefits and costs of the policy – social, environmental and economic. The lack of data for benchmarks or performance criteria for evaluation of the policy is one of the greatest shortcomings of the implementation of NCP.

The public interest test - social and environmental impacts

NCP includes a public interest test but it has been construed extremely narrowly and has been under-utilised.

The Senate Committee found that the public interest test was dominated by economic assessment, ahead of the harder to measure intangible attributes in the social and environmental areas.

It is relatively easy for economists to estimate the economic impacts of the deregulation of one industry or the instigation of competition in another.

It is a much more difficult task to attribute a value to the social and environmental impacts of those sorts of changes. But the conduct of such an assessment is essential if the real costs and benefits of the implementation of a policy are to be known.

The NCP has paid too little heed to externalities. Full costing requires the larger social and environmental costs to be factored in and, in the case of small business particularly, the larger economic costs to be factored in.

Instead the NCP focuses on net costs. As an example, there are pollution and social costs in using brown coal in energy generation in preference to other fuels that exceed the net cost of the brown coal itself. Or as another example, in deregulating pharmacies so that big business takes over the sector, with the loss of those small business networks and skills.

‘Public interest’ is an all-encompassing term that must not just refer to dollars.

Note that the NCP does not necessarily mean that the jurisdiction is always required to implement deregulatory actions. It may well be that as a result of the State's NCP regulatory review processes, the State or Territory may decide it is in the public interest to *retain* some or all of the regulatory provisions.

Such an outcome need not risk loss of NCP payments through rejection by the NCC as long as the review processes are transparent and objective.

Recommendations

That the NCP recommendations to deregulate trading hours in WA be rejected.

4 Competition Theory

The role of competition in the market place is not just the improvement of prices, products and choice, but the preservation of a diversity of competitors, even where some are identifiably less efficient than others.

Economists, such as those of the University of Chicago[1], tell us that "societies that promote vigorous competition among private companies have lower prices, better products, and greater consumer choice"[2]. These characteristics are not altruistic, but arise from enlightened self-interest. Those same economists also accept that not every successful competitor needs to be at the same standard of economic efficiency.

Lower prices are an effort on the part of a company to gain new customers or retain existing customers through offering goods or services at cheaper prices than their competitors. Better quality products, or new products are an effort on the part of the company to maintain their present customer base or obtain new customers through a reputation for quality service or product. Greater choice is the product of competition in any given market, with a number of companies offering a range of products or services in an attempt to attract and satisfy the customer.

While the most important measure of effective competition is whether the market satisfies the needs of the consumer, that can in some circumstances be provided by a benevolent monopoly. However, society as a whole would be very much the poorer if it did not have the diversity and opportunity that many competitors bring to the market place.

When one company begins to dominate any given market, or when a small group of companies work themselves into a position of dominance, this is not necessarily an example of market failure in the formal sense of that phrase, but it can still be an undesirable social and economic outcome.

Dominance of a market occurs when a company, or a group of companies, are able to exercise excessive market power.

The ACCC defines market power as:

> "The ability of a firm to behave persistently in a manner different from the behaviour that a competitive market would enforce on a corporation facing otherwise similar cost and demand conditions. That is, market power is the ability of a firm or firms profitably to divert prices, quality, variety, service or innovation from their competitive levels for a significant period of time[3].

This type of market power, in a situation of dominance, is beyond the reach of other competitors in the market, leaving them at a serious disadvantage.

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[1] "The Economics of Antitrust", article from *The Economist*, May 2nd 1998, pp 66-68.
[2] Federal Trade Commission (US), "Promoting Competition, Protecting Consumers: A plain English Guide to Antitrust Laws", web-site, http://www.ftc.gov/bc/compguide/index.htm
[3] The Australian Competition and Consumer Commission (ACCC), Submission to the Joint Select Committee on the Retail Sector, Submission no. 191, p 26.

There are three areas in which market dominance and the exercise of market power can be exercised, one relating to the competitors in the market, one to the suppliers, and the other relating to the consumers.

With regard to competitors, the dominant group or company in a marketplace can wipeout or buy-out its smaller competitors, and effectively eliminate their competition, creating a situation of market monopolisation, or in the case of a group, market oligopoly.

In other words, they don't just eliminate competitors, but in the end they can eliminate competition itself.

With regard to suppliers, in a market where market power exists, suppliers face problems when the company possessing market power uses this power to demand selective discriminatory discounts on purchases. Small or vulnerable suppliers may fall victim to changes in contract or trading terms with little to no negotiation in the process.

With regard to consumers, with the elimination of competition and the establishment of monopoly or oligopoly, the benefits of competition of lower prices, better products, and greater choice that flow on to the consumer are eliminated or reduced. This is because the monopolist "can restrict output and raise prices so as to increase their own profitability at the expense of consumers"[4], who are left with little choice but to purchase from the monopolist.

Looking at this scenario, dry economic theorists might claim that this is the market at work, with inefficient players being eliminated and the more efficient companies expanding their share of the market as they defeat their competition.

In their eyes, any dominance or monopoly that one player is able to exert in the market is purely temporary because the high profits that they are able to extract from an anti-competitive market will attract new competitors[5].

They would also claim that market forces serve to eliminate "firms that are inefficient or fail to respond to the changing wants and needs of consumers (which) will be replaced through the entry of more efficient and responsive firms"[6].

Under this theory, free markets will themselves erode monopolies, and serve to keep the market efficient through the elimination of those companies that cannot capitalise on efficiency gains and adapt to the changing needs of the market.

The Chicago theorists make the further claim that a company may not actually seek to raise prices once they have established a dominant position, because this would attract other competitors to the market. (Over the long run that may indeed occur, but in the real world barriers to entry act to stop or delay this happening.) They may instead seek to forestall competition by setting prices, which while still high, might still be as

[4] "The Economics of Antitrust", p 67.
[5] ibid, p 67.
[6] ACCC Submission 191, p 22.

though they were engaged in a competitive market[7], thus not obviously disadvantaging the consumer.

Perfect competition, as expressed in economic theory, does not exist in markets such as those subject to this inquiry.

The abuse of market power can result from predatory or intimidatory pricing, to fix pricing levels in a particular market. Then there is the practice of demanding prices and terms from suppliers which results in a forced differentiation between their retail customers, a differentiation the supplier would otherwise not have contemplated.

Suppliers themselves may charge retail customers of similar standing different prices for goods of like grade or quality[8]. The questions that are posed by Ann Everton, law lecturer at Leeds University, become especially relevant in instances of dominance and excessive market power in the marketplace:

> "Should or should not free competition be encouraged to the point that it leads to the further increase of an already sizeable monopoly, and hence to the very destruction of competition? Secondly, should or should not some limit be set to the promotion of free competition in order to ensure that the competition also be fair?"[9]

Governments in various countries have found it necessary to adopt one of three possible broad policy approaches when dealing with the problems of market power and dominance within the marketplace.

In contrast to other industries in Australia, it could be argued that retailing has mostly been subject to the laissez-faire approach – to mostly leave the market well alone. This can result in situations of dominance and subsequent oligopoly or monopoly, as well as disparities in wealth and income distribution. It leaves markets free, but it opens the door to them quickly becoming unfair.

The public supervision approach has lost favour in Australia, where strict regulation of key or sensitive markets, possibly through government ownership of key industries, has declined. Industries such as electricity, water, or telecommunications, are in this category, and restricted licensing systems such as for pharmacies and liquor.

Much of the work of the ACCC and Australian Governments covers the regulatory approach, where the government recognises the imperfections of real markets, and takes responsibility for ensuring that competition among the private firms within the market is sustained. Yet the government does not interfere with the decisions of price and output.[10]

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[7] ibid.

[8] Everton, Ann R. "*Price Discrimination – A Comparative Study in Legal Control,* Leeds University, 1976, p 1.

[9] ibid, p 2.

[10] "Antitrust Overview", by Charles E. Mueller, Editor Antitrust Law and Economics Review, web-site, http://webpages.metrolink.net/~cmueller/I-overvw.html

The stated purpose of the *Trade Practices Act 1974* is to promote competition and fair-trading within the marketplace, as well as providing some form of protection for consumers.

The approach adopted in Australia is very similar to that of other OECD economies, in that many countries may possess laws that have 'monopolisation', 'abuse of dominance' or 'misuse of market power' provisions that do not directly prohibit monopolies or the possession of market power, but the abuse of this privileged position[11].

At the OECD Competition Policy Roundtables in 1996, the preamble to the United States paper stated that:

> "Size or power alone is not illegal, the firm must have engaged in certain monopolistic or anti-competitive conduct; and some monopolies will escape condemnation under the statute because they were a consequence of success in the market, untainted by impermissible conduct"[12].

However, there is an important underpinning to this statement. While size or power alone are not only not illegal, but are highly desirable because of economies of scale, nevertheless size alone *is* a signal to be alert to the potential for an abuse of market power.

Section 46 of the TPA specifically states that any corporation with a substantial degree of power in a market shall not take advantage of that power for any of three enumerated purposes:

(a) *Eliminating or substantially damaging a competitor of the corporation or of a body corporate that is related to the corporation in that or any other market;*
(b) Preventing the entry of a person into that or any other market; or
(c) *Deterring or preventing a person from engaging in competitive conduct in that or any other market.*[13]

Section 50 of the TPA prohibits acquisitions that have the effect or likely effect of substantially lessening competition[14]. By this means, the Act is attempting to curb the elimination of competition in the marketplace through the acquisition of competitors. In determining the extent to which the acquisition lessens competition in a market, a number of matters must be taken into account, such as:

- Entry barriers to the market;
- Market concentration levels;
- The power of competitors in the market;
- The likelihood the acquisition would result in the acquirer attaining market power;
- Market dynamics, such as growth, innovation and differentiation of product;
- Whether the acquisition would remove a substantial market competitor; and

[11] ACCC Submission, ibid, p.44; Australian Retailers Association (ARA), Submission to the Joint Select Committee on the Retailing Sector, Submission 57, Volume 2, p 43.
[12] ARA Submission, ibid, p 44.
[13] *Trade Practices Act 1974,* Section 46(1), Subsections a, b & c.
[14] *Trade Practices Act 1974,* Section 50(1).

- The nature and extent of vertical integration in the market[15].

When the level of concentration is taken into account, ACCC guidelines state that where the post merger market share of a merged firm is 15% or more, and the share of the four or fewer largest firms is 75% or more, the Commission will want to investigate the merger further before being satisfied it does not result in a substantial lessening of competition[16].

Mergers are therefore readily dealt with under this law, and under ACCC guidelines. Small accumulative incremental or 'creeping' acquisitions, which have the same effect as mergers in reality, are not.

The United Kingdom Office of Fair Trading (OFT), in their *Competition in Retailing* report suggest that when trying to analyse questions of competition in retailing, a certain framework should be taken[17].

The United Kingdom, under its *Fair Trading Act 1973*, empowers the Office of Fair Trading (OFT) to investigate monopoly situations in one of two possible monopoly situations, these being:

- Scale Monopoly – one person or firm controls 25% of the supply or acquisition of goods or services of a particular kind; and

- Complex Monopoly – where a number of firms together make up 25%.

These 25% thresholds do not indicate market dominance in themselves. Instead they act as a trigger for the OFT to refer the matter for investigation by the Monopolies and Mergers Commission into the ramifications of the market share that a company holds, and whether it results in negative effects on competition or the consumers[18].

The use of national market share data is less commonplace in the United States, where competition authorities take a more local and regional focus when considering market concentration levels following the merging of companies[19].

This is markedly different from the approach of the ACCC, which has indicated that, in the retailing sector at least, the major chains are national competitors, and ACCC decisions are made at a national level. The result of the ACCC stance with regard to the major chains is that the market is defined nationally, as opposed to any statewide, regional or local definition[20]. That is a failing.

In analysing the theory above, the Trading Hours Review Committee need to determine whether further deregulation benefits big business at the expense of small business, and why they would consider that a useful outcome.

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[15] *Trade Practices Act 1974,* Section 50(3), Subsections b - i.
[16] ACCC Submission 191, p 27, footnote 44.
[17] London Economics, Competition in Retailing, research paper prepared for the Office of fair Trading (UK) by London Economics, September 1997, p 8.
[18] ibid, p 49.
[19] ACCC Submission, ibid, p 49.
[20] ACCC Submission, ibid, p 32.

5 The Market

The Retail Trading Hours debate provokes a war of words between the supermarket superpowers of retailing, and the opposing coalition of independent supermarket and independent wholesaler interests.

To a single supermarket owner in a country town, the market **is** that town, and its catchment area. To one of the major chains, the market ranges from that very town to the whole country.

Along with these geographical distinctions go sectoral distinctions. The various specialist categories of retail compete with each other in each retail sector, be they butchers or florists. They also compete with multi-sectoral retail conglomerates covering all retail categories.

In certain markets and retail sectors, the independent retail sector is under threat. Without detracting at all from the strengths, professionalism and consumer benefits offered by the major retailing chains, we have to face the fact that if a viable independent sector is to be retained in each of the retailing sectors, then competition policy must be tightened up.

I accept the evidence that in a few regional markets within the supermarket sector, the expansion of major retailers has probably reached saturation point. In one or two regions it might even have exceeded it.

In other regional markets it is also evident that there are still opportunities for the major retailers to expand.

Western Australia offers the greatest opportunities in Australia.

A Viable Independent Retail Sector

In designing competition policy we have to determine a set of values and principles which should guide our laws and behaviour.

First amongst these should be the recognition that monopolies or oligopolies inherently contain within them a capacity for the abuse of market power, and should usually be resisted where they emerge, or monitored where they already exist. Therefore a situation such as we have in the Australian supermarket industry nationally, where an oligopoly is present, has to be acted upon.

Secondly, we must acknowledge that a viable and thriving independent sector in the retail industry is desirable of itself and that it has an economic and social value that should not be lost.

In retailing, this independent sector is most at threat in Australia in the supermarket sector, where the critical mass essential to its survival is under threat. However the trend is also emerging in non-supermarket retail sectors, and that problem needs to be addressed to prevent such crises emerging there too.

In Western Australia the sensible balanced approach of successive State Governments on trading hours has ensured the largest independent retailing sector in the country.

There can be no misunderstanding of the importance of that policy. Nor should there be any misunderstanding of how badly big business supermarket chains want to deregulate trading hours so that they can drive the independents out of business.

It is desirable that the Review Committee takes as its central mission in deciding on Trading Hour recommendations that its first responsibility is to ensure the preservation of a viable independent sector in retailing.

Market Power - (horizontal integration or market concentration).

Market concentration entails the dominance of the market by the few. In other words fewer competitors result. At the heart of this trend lies the danger that the destruction of competitors will result in the destruction of competition.

Competition in any retail sector is best served by a diversity of competitors and a lowering of real barriers to entry. Barriers to entry include the difficulty independents have in securing prime sites, particularly in regional shopping centres.

Creeping acquisitions have allowed the majors to achieve a market size which might have been prohibited by the ACCC if those acquisitions had been aggregated into one purchase, which could therefore have fallen foul of existing merger provisions in the TPA.

In Australia, deregulated trading hours have contributed materially to retail power concentration.

6 The Trade Practices Act Fails Retailers

Retail Trading Hours cannot be assessed in isolation of the Trade Practices Act. The Review Committee will need to recognise that retail trading hours deregulation provides another means whereby the large and powerful can oppress other retail businesses.

Some questions arise from that consequence. Is that in the interests of the consumer and of competition in the longer term. And if it might not be, does existing law and regulation act to prevent abuse and deleterious consequences?

I am guided in my approach by three dominant observations, namely that

- The Trade Practices Act 1974 as amended (TPA), and the Australian Competition and Consumer Commission (ACCC), have achieved much greater levels of competition and consumer protection than would have occurred in their absence;
- The TPA can deliver greater and freer competition, and greater consumer benefits, if it is strengthened further;
- The TPA fails to give the ACCC sufficient legislative backing to enable them to fulfil their responsibility to small business.

In my view, there is a real failure to understand that if you want more competition, if you want a freer market, if you want current artificial political constraints on certain industry sectors lifted, if you want greater consumer confidence in the market – then you need a strengthening of the Act, not a weakening of it.

Strengthening the Act has a number of threads. Missing from the Act are a number of elements that are successfully used in foreign jurisdictions - such as USA anti-trust laws, or UK scale or complex monopoly mechanisms.

Also missing from the Act is sufficient attention to social and environmental needs, in view of their relevance to modern public policy.

Providing adequate powers to break up corporations is necessary in the public interest. It is strange that many in business laud the dynamism of competition in the USA, but resist the notion of divestiture (anti-trust) powers.

It is as if the contribution of those laws to an effective market can somehow be ignored. Anti-trust laws in the USA have been a vital power providing a restraining corrective effect and contribution.

The TPA would benefit from further reform and additional powers. The structure of the Act does not need significant change.

Although it rightly has elements that are industry- specific, or oriented to ‘black letter law’, the TPA should largely be principles based, confer a high degree of flexibility and discretion on the ACCC, and have general application across society and the economy.

The Act's philosophical underpinnings need to reflect the reality that Australian social, economic and environmental values and policies are intertwined. Therefore an Act that promotes fair and effective competition and consumer protection, must adequately address relevant social and environmental considerations as well as economic ones.

As an example, pricing cannot be considered in isolation of the effect of externalities. The long-term costs to the society and the environment of the failure to apply full costing, or to disclose unsafe, unhealthy or unsustainable practices in the provision of goods and services, have to be addressed.

The object of the TPA is to 'enhance the welfare of Australians through the promotion of competition and fair trading and provision for consumer protection.'[21]

The notion of 'welfare' must take into account not only economic but also social and environmental factors. Australia's competition and consumer protection laws must seek to deliver the maximum economic, social and environmental benefits for this generation and future generations.

The TPA continues to provide an effective mechanism for balancing the needs of large, medium and small firms, and consumers, but that must be done with a long-term perspective in mind, and with a view to benefiting society as a whole.

Until the TPA is strengthened it is unwise to consider deregulating trading hours. There is no countervailing regulation.

Section 46 a failure

The High Court's recent decision in the Boral case has significant implications for small business and for Australian consumers.

Until regulatory law is tested, its force often rests as much on moral suasion and perception as on the black letter. That is why the character and style of the chairman of the ACCC is so important, because threat and posture do help keep companies on the straight and narrow. Once the law is tested, it is a different matter.

As they did with the Hughes Wakim and Mabo cases, by exposing serious deficiencies in the law, in the section 46 sense, first in Melway and now in Boral, the High Court has told parliament that a key part of the competition law is ineffective.

Academic and small business experts have long complained that section 46 of the Trade Practices Act, which prohibits predatory pricing, is weak. They are right. Far from doing small and medium business a disservice, the High Court has done them a favour. This case will pressure the parliament to tighten up the TPA regime.

Predatory pricing is a big problem for small and medium businesses, both upstream and downstream. From a public policy point of view the issue is that the destruction

[21] Section 2 TPA

of competitors, if taken to its logical conclusion, can result in the destruction of competition. That is why market power has to be regulated and constrained.

What the Boral case says is that conduct by a powerful competitor that is predatory in economic terms and anticompetitive in nature may not be caught under section 46 of the Act. Despite its powerful market position, Boral was deemed by the High Court to lack the necessary market power—the ability to `give less and charge more'.

The court made a distinction between monopolistic power prior to predatory pricing, which would be an abuse, and the monopolistic power that results from successful predatory pricing. The problem is that if you let the latter happen, the regulator has failed. That is why section 46 must be toughened up to prevent companies from achieving such monopolistic power.

A business alleging that another business has engaged in anticompetitive conduct must presently show there was an intention to eliminate competition. Proving that intention is notoriously difficult because it is so hard to get behind the big corporate shield and find the smoking gun.

This is not the first time it has become necessary for the Australian parliament to address this issue. Prior to 1986, the provisions of the Trade Practices Act caught only the predatory pricing of a monopolist or near monopolist. Realising that the threshold was very high under that version, the parliament enacted the present section 46 with a view to lowering the threshold to include not only monopolists or near monopolists but also those corporations with a substantial degree of market power.

In talking of substantial market power, reference was made to the terms `large', `weighty' or `big'. Accordingly, the ACCC and small business believed that powerful corporations with a large market share and considerable financial strength were on notice that their conduct could be within section 46 and therefore in breach of the Trade Practices Act.

The Boral case shattered this belief. The High Court has said that a substantial degree of market power covers only those corporations that are able to set prices unilaterally without fear of losing custom. But which corporations can set prices unilaterally without fear of losing custom? In the absence of collusion, only a monopolist or a corporation that is in a controlling or dominant position in a market can raise prices without fear of losing custom. It is certainly not the case that duopolists and oligopolists would ordinarily have this ability.

In a duopoly or oligopoly situation, absent of cartel-like behaviour, no single competitor is able to raise prices unilaterally without fear of losing custom. In short, there is now a considerable hole in the protection afforded under section 46 against abuses of market power by large and powerful corporations.

As section 46 now effectively applies only to the conduct of monopolists and near monopolists, small businesses have no protection against those other large and powerful corporations choosing to throw their weight around.

Two possible measures could overcome this problem and still maintain fairness. The first is to remove the requirement to show intention and to instead show that the actions of the alleged perpetrator have had the effect of damaging competition. The second is to get behind the corporate veil by changing the onus of proof where the ACCC pursues the matter. The onus would fall on the defendant, not the applicant, to show that there was no purpose of eliminating competition.

A system of protecting and rewarding whistleblowers who provide evidence about collusive and anticompetitive conduct should also be considered.

The ACCC should be given a power to grant cease and desist orders against companies involved in anticompetitive behaviour. Such a power would allow intervention on behalf of small firms who are being harmed by the behaviour of a large competitor.

Rather than wait years for a court to determine the legality of a firm's behaviour, a cease and desist power would allow early intervention before the competitor was driven out of business. Further, there is a case for section 46 to have specific prohibitions against predatory pricing. Another route of interest is to also toughen up and broaden section 51AC.

In the face of the failure of the TPA WA’s trading hours policy helps even up the odds for small and independent retail businesses.

Other TPA Reforms needed

In many respects, Australia's approach to the TPA is similar to that of other OECD countries; in other ways it is not. Missing from the TPA is a number of elements that are successfully implemented in foreign jurisdictions, such as the US antitrust or divestiture laws and the United Kingdom scale or complex monopoly mechanisms.

The United Kingdom Fair Trading Act uses a figure of 25 per cent as constituting a fair market power strength measure. Boral, with at least 30 per cent of the market, would have officially been under market watch in the UK - a measure that usefully ensures better market behaviour.

The point of the US antitrust laws, as interpreted by the US courts, is to prevent unreasonable and unfair methods from being employed by companies establishing a position of substantial market power or reinforcing a position of substantial market power.

Big business roar approval at the dynamism of the American market but fiercely condemn a major contributor to that dynamism - that is, the effects of antitrust laws.

We need them in Australia. A practice should be deemed illegitimate if it restricts competition in a significant way or is likely to harm consumers through increased prices, reduced availability of goods or services, lowered quality or service, reduced diversity or stifled innovation.

A stronger TPA will be good for Australia. What is needed is for legislation to be enacted to prevent the High Court's Boral decision from being used by big business to justify open season against their small business competitors.

Free and fair competition needs a strong regulator empowered by a strong Act. It needs an agreed national Competition Policy, but one that accords with social and environmental values, not just economic values; and one that recognises that industries and regions have a value worth more than the sum of the profits to be made out of them.

To accompany good existing powers restraining anti-competitive mergers and acquisitions, the ACCC needs powers to address existing dominant monopolies, including an undue concentration of market power achieved by small ‘creeping’ acquisitions. The ACCC or the Courts should be given a power to order divestiture where an ownership situation has the effect of materially limiting or substantially lessening competition.

Without these, small and independent business needs all the help they can get. By and large WA’s governments have recognised this with their current trading hours policy.

Senator Andrew Murray

Appendix[22]

Withholding of national competition policy payments to state governments

1. Background - Overview of Commonwealth National Competition Policy Payments (NCPP) to the States and Territories

- At the April 1995 Council of Australian Governments (COAG) meeting, the Commonwealth and the States concluded the *Agreement to Implement the National Competition Policy and Related Reforms*.
- Under that Agreement, the States are eligible for three tranches of ongoing NCPPs.
- The NCPPs commenced in July 1997 at an annual level of $200 million, and increased in July 1999 to $400 million in 1994-95 prices. The third tranche commenced in July 2001 at an annual level of $600 million in 1994-95 prices. The Agreement specifies that the NCPPs be paid quarterly and be distributed to the States on an equal per capita basis.
- Subject to satisfactory progress in the areas to be reviewed by the National Competition Council, the Commonwealth will provide the States with NCPPs estimated to total $739.8 million in 2002-03.

Link between reform progress and NCP payments

- Each State's NCPPs are subject to that State *making satisfactory progress* with the implementation of specified reform conditions in the Agreement. Prior to the scheduled payment of NCPPs each year, the National Competition Council assesses whether each State has met these conditions and provide a report for consideration by the Commonwealth.
- Where satisfactory progress has not been made by a particular jurisdiction on a certain reform program, the NCC may recommend to the Commonwealth that it withhold a portion of the NCP payments which would otherwise flow to the State or Territory; the Commonwealth is not required to comply with the NCC's recommendations.
- <u>Note that 'progress' does not necessarily mean that the jurisdiction is always required to implement deregulatory actions.</u> It may well be that as a result of the State's NCP regulatory review processes, the State or Territory may decide it is in the public interest to *retain* some or all of the regulatory provisions. Such an outcome need not risk loss of NCP payments through rejection by the NCC as long as the review processes are transparent and objective.
- The attached letter from the NCC to the Treasurer of 18 November 2002 identifies a number of reform areas where Western Australia's application of the competition reform principles were found wanting in 2002; note that in these instances, the NCC did not recommend any penalisation of WA's NCPP entitlements as additional review processes are in train.

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[22] The Parliamentary Library has assisted me in gathering this material together

*Precedents for withholding NCP payments to the States and Territories**

Circumstances under which funds withheld	Outcome and comment
YEAR: 1998-99 **ISSUE: Domestic rice marketing** **STATE: NSW** - In 1998, the NCC recommended to the Treasurer that all the States and Territories, except New South Wales, receive their full allocation of 1998-99 NCP Payments. - In relation to NSW, the Council has recommended that if domestic rice marketing arrangements are not reformed by 31 January 1999 — as recommended by an independent review group in 1995 — then $10m should be deducted from its remaining 1998-99 NCP Payments. - This penalty reflected the costs imposed on consumers from maintaining the domestic arrangements. Source: Federal Treasurer's Press Release 21 August 1998	- The Treasurer announced he would delay until early 1999 any decision on whether New South Wales will have its NCP Payments reduced to enable the working party to complete its task and enable the Treasurer to take the outcome into account in making a decision.
YEAR: 1999-00 **ISSUE: Water** **STATE: Queensland** - $14.83m in NCPP to Queensland was suspended on recommendation of the National Competition Council's June 1999 second tranche NCP assessment. - Commonwealth accepted NCC's assessment that Queensland was unable to demonstrate compliance with a specific water reform commitment. Source: Federal Treasurer's Press Release 22 Feb 2000	- In February 2000, the Federal Treasurer announced his decision to reinstate $14.83m in suspended National Competition Policy (NCP) payments to Queensland. - This followed a supplementary NCC assessment, recommending that the penalty be removed because Queensland was now committed to preparing new guidelines for determining ecological sustainability and economic viability of investments in rural water projects. - These were consistent with the COAG water resource framework.
YEAR: 2000-01 **ISSUE: Motor transport** **STATE: NT** • The Northern Territory had 5% of its payments suspended in late 2000 due to its failure to introduce the national driver demerits point scheme • The Treasurer said at the time that these amounts may, however, be restored following a positive assessment by the Council in December 2000.	

Source: Federal Treasurer's Press Release 3 Nov 2000	
YEAR: 2000-01 **ISSUE: Rail and urban water** **STATE: Queensland** - Queensland was penalised with a 10% NCPP funding suspension due to its failure to put in place an adequate Community Service Obligation framework to address competitive neutrality concerns arising from the operation of Queensland Rail - and a further 5% suspension in relation to insufficient progress being made in implementing of two part tariffs for urban water charges - these suspensions amounted to approximately $12.9m.	
YEAR: 2000-01 **ISSUE: Liquor licensing** **STATE: Victoria** - In the area of liquor licensing in Victoria, it has been Labor policy to 'close the legislative loopholes which allow large retailing chains to accumulate more than eight per cent of the total number of packaged liquor licences' and reinstate and strengthen the eight per cent cap limit on market concentration in other area of retail liquor licensing. - Following a review by the Office of Regulatory Reform (ORR) in Victoria, the State Labor Government stuck to its commitment on liquor. According to the National Civic Council, 'the National Competition Council retaliated with threats of withholding millions of dollars in National Competition payments to the state'. Source; National Civic Council, *Newsweekly*, 14 July 2001	- In May 2001, the State Government introduced legislative amendments to uphold the 'eight per cent cap'' on packaged liquor licences'. - According to the National Civic Council, 'under the new law, the major chains must divest those liquor licences they hold above the eight per cent cap. The National Competition Council backed down on the threat to withhold NCP payments. It was a victory for small business and common sense'.
- Queensland's NCPPs for 2001-02 and 2002-03 were reduced by $270 000 each year following the Federal Treasurer's acceptance of the NCC's recommendation to reduce the State's payments by these amounts because of the 'Townsville City Council's lack of progress in respect of two-part water pricing reform'. Source: Federal Treasurer's Press Release 6 December 2002	- The NCC was to revisit this recommendation as to following the Queensland Competition Authority's consideration of the latest cost effectiveness study commissioned by Townsville City Council. - All other States and Territories received their full NCPPs for 2002-03.

* note that in many cases, suspended payments were eventually been paid out following follow-up State Government reforms.

ATTACHMENT

Ref:aj1001.3A
18 November 2002
The Hon Peter Costello MP
Treasurer
Parliament House
Canberra ACT 2600

Dear Treasurer

Completing the 2002 assessment of governments' progress with implementing the National Competition Policy and related reforms: Western Australia and South Australia

In my letter to you of 19 August 2002 on the National Competition Council's recommendations on the allocation of competition payments for 2002-03, I noted that the Council was unable to make a recommendation on competition payments for Western Australia and South Australia at that time.

The Council's report for2002 on progress by governments against the National Competition Policy and related reforms (August 2002) identified various areas in which the two jurisdictions had not met NCP obligations. Specifically:

- Western Australia had not met its obligations in relation to:
  - water quality issues and the adoption of the intergovernmental National Water Quality Management Strategy;
  - the regulation of retail trading hours;
  - liquor licensing arrangements;
  - arrangements relating to egg marketing;
  - supply management and marketing arrangements relating to potatoes;
  - registration requirements for occupational therapists; and
  - taxi and hire car regulation.
- South Australia had not met its obligations in relation to:
  - the regulation of retail trading hours;
  - liquor licensing arrangements;
  - barley marketing arrangements;
  - ownership restrictions for dental practices;
  - registration requirements for occupational therapists;
  - water quality and implementation of the National Water Quality Management Strategy; and
  - taxi and hire car regulation.

During the course of the 2002 assessment, the Council had constructive discussions with the two governments and was able to resolve appropriate processes for addressing most of these matters.

As I explained in my letter of 19 August, the matters not resolved for the 2002 assessment were:

- the regulation of retail trading, liquor licensing and potato supply management and marketing in Western Australia; and
- the regulation of retail trading in South Australia.

In relation to this, the Council advised all governments that it intends to complete the assessment of all legislation review and reform activity in 2003, following from CoAG's decision that such activity be complete by 30 June 2002.

The Council will consider activity that is incomplete or inconsistent with NCP principles at the time of the 2003 assessment to not comply with NCP obligations, with consequent adverse competition payment implications. The Council sees no scope for governments to delay the resolution of outstanding matters beyond the 2003 assessment.

In addition to the legislative matters identified for Western Australia and South Australia in the 2002 assessment, the Council found that some governments were not sufficiently advanced with various water reform obligations. The Council undertook to conduct supplementary assessments for four jurisdictions, noting that a finding of unsatisfactory progress may attract an adverse recommendation for 2002-03 competition payments. The supplementary assessments are for:

- New South Wales relating to water sharing plans (December 2002);
- Queensland relating to the independent review of the science of the Condamine-Balonne system (February 2003);
- Western Australia relating to the implementation of the National Water Quality Management Strategy (December 2002 and March 2003); and
- Tasmania relating to asset valuation and cost recovery by urban water service providers (November 2002).

Developments in South Australia since 19 August 2002

The South Australian Government has commenced transitional reform of its retail trading arrangements with a view to implementing more substantial reform by the time of the 2003 assessment. It introduced the Shop Trading Hours (Miscellaneous) Amendment Bill 2002. The Council accepted that this constituted an appropriate transitional reform initiative.

In late October 2002, the Government advised that a Parliamentary Standing Committee had recommended amendments to the Bill, including that the proposed extension of trading hours on weeknights and Sundays should apply only until 30 June 2003. The Government further advised that it had 'rejected the conditions attached to these amendments as another delaying tactic designed to thwart the Government's attempt to introduce more flexibility into shop trading hours in this State'.

Notwithstanding the inability to progress the reforms through the Parliament, the Council considers that the Bill demonstrated a commitment by the Government to the reform of shop trading hours. This commitment has not been matched by the South Australian Parliament. In this context, the Council considers that the most constructive approach is to deal with this issue as part of its final assessment of legislation review and reform activity in 2003.

The Council recommends that South Australia receive the full quantum of competition payments for 2002-03.

Developments in Western Australia since 19 August

The Premier of Western Australia wrote to the Council in early August advising that the Government appreciated the need for reform in the three outstanding legislation areas. The Premier reported that potato marketing was under review, a Ministerial Task Force would be established to review retail trading hours and liquor licensing regulations would be reviewed over 2002-03.

The Council has continued to engage in discussions with the Western Australian Government on these matters. The Council understands that reform options for potato supply and marketing arrangements that better comply with NCP obligations than the policy directions initially proposed in the review's discussion paper are now being considered. However, while the Government has recognised the need to address restrictions on trading hours and liquor licensing, it has to date shown little inclination to remove legislative restrictions and has not provided convincing public interest evidence that the current restrictions offer a net community benefit.

The Council regards Western Australia's approach to the application of competition principles to trading hours and liquor licensing regulation as unsatisfactory. However, given that the final (2003) assessment of legislation review and reform activity will be completed in about eight months time, and that Western Australia is addressing some of the matters that the Council identified as not complying with competition principles, the Council considers that the best approach is to revisit trading hours and liquor licensing, with a view to their final resolution, in the 2003 assessment rather than to conclude on compliance at this time.

The Council recommends that Western Australia receive the full quantum of competition payments for 2002-03.

Water reform

As I have explained above, the Council will conduct a number of supplementary 2002 assessments of various governments' water reform performance. The Council has completed the supplementary assessment for Tasmania, finding that the State has satisfactorily addressed asset valuation and cost recovery commitments for 2002. Given this is the final matter relating to the 2002 assessment for Tasmania, the Council recommends no reduction in 2002-03 competition payments for the State.

I will shortly write to you separately on the Tasmanian supplementary assessment, enclosing a copy of the Council's assessment. I shall advise you of the outcomes of the remaining supplementary assessments as these are completed.

Yours sincerely

Graeme Samuel

President