Dissenting Report by Senator Nick Xenophon

Competition laws – the butter knife needs to be replaced with a sword of Damocles

1.1 Australia's competition policy is in need of urgent repair. The fact that we can find ourselves in a position where two retailers control approximately 75 percent of the grocery market clearly demonstrates that the remedies available under the *Competition and Consumer Act 2010* (CCA) do little to deter anti-competitive behaviour. The Competition and Consumer Amendment (Misuse of Market Power) Bill 2014 aims to give the courts the power to order the divestiture of a corporation where that corporation has misused its market power. The effect of this bill would be a powerful disincentive for corporations to abuse their market power.[1]

1.2 It is therefore incredibly disappointing the committee recommended this bill not be passed. While the majority report analysed the effect of the bill and the practical consequences of a divestiture power, the committee failed to examine the state of competition in Australia's retail markets. By not examining why and how a handful of corporations have been able to establish such wide reaching control over our retail markets, we are leaving ourselves vulnerable to higher prices and less variety in goods and services in the long run.

Australia's retail sector

1.3 The current state of the Australian retail sector was described by the Master Grocers Association in its submission to the inquiry:

> The retail ownership landscape in Australia has changed dramatically over the past 30 years. Small businesses, particularly independent retailers, have been faced with the ever increasing threat and challenge of two giant supermarkets, Coles and Woolworths, growing at an unabated pace, using their ever increasing market power and dominance to crowd out existing retailers and to block out new competition. Nowhere else in the world is there such a hyper – concentration of two massive supermarket retailers![2]

1.4 MGA's submission continued:

> It is highly questionable that the growth of Coles and Woolworths is simply due to the allegedly greater expertise, business acumen and skills they exercise in the market place. It is the effect of oversaturation of areas with numerous stores that results in the crowding out of their competitors where

1 Explanatory Memorandum, p. 2.

2 Master Grocers Australia, *Submission 6*, p. 5.

> in most circumstances there is ample room for the larger and smaller stores to compete on a level playing field.[3]

1.5 Australian competition policy is failing to keep pace with the increasing presence of anti-competitive behaviour and the serious consequences that flow on from this, both for consumers and businesses alike.

The case for reform

1.6 A well-known example of the market power of the 'big 2' supermarkets was the milk price war in 2011 when Coles announced it was selling Coles brand regular and low fat milk for $1 a litre. Woolworths followed suit immediately, also cutting the price of its home brand milk. Other retailers cut prices soon after.

1.7 More recently Woolworths has begun selling its home brand bread for 85 cents a loaf. This move will has already put great pressure on independent bakers and supermarkets who cannot compete with bread being sold at what appears to be below the cost of production. The impact of selling bread for 85 cents per loaf on the retail industry was explained by Mr Jos de Bruin, Chief Executive Officer of Master Grocers Australia, during the committee's public hearing on 2 October 2014:

> **Mr de Bruin:** … we believe that (anticompetitive price discrimination) is a misuse of market power. It creates what we call a 'waterbed effect': the cheaper the chains buy a product for, the higher the price it is for anyone else to buy. Call it whatever you wish, whatever technical term they use around trading terms—'promotional buys', 'scan deals', 'volume', 'settlement discounts'—it does not matter: there is a strict net cost that they arrive at and ultimately it is the smaller people that pay here.
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> **Senator XENOPHON:** Just further to that, a practical example is the issue of the 85c bread. I have spoken to a number of your members. I spoke to the Asplands up in Townsville who have been speaking about this nationally. You cannot buy bread, even some of your bigger members do not get bread, anywhere within cooee of 85c. There is the fear that, whatever the big bakeries are providing the bread at, if it is 85c, it does have a waterbed effect in for Coles and/or Woolies to get it that cheap means that other retailers in the supply chain have to pay more? Is that what you are saying?
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> **Mr de Bruin:** I cannot tell you how many phone calls, emails, texts I have had about bread in the last week. It was absolutely in override last week. Clearly our members around Australia see this behaviour as predatory—predatory because there is a sense that Woolworths and Coles are not losing a cent. They claim they may be and if they are they are cross subsidising it with additional margins in store. Our members have said, 'Yes, well, they will make a decision in their own right whether they match it or not.' But when they match it they will be losing a minimum of 35c a loaf and in volume terms in grocery terms that is a massive amount of margin that

3 Master Grocers Australia, *Submission 6*, p. 8.

> comes out of their business that will affect employment and will affect their business in ways that Woolworths and Coles would not understand. The consumer does seek cheap bread out there. I am not sure that the consumer actually sees what the ramifications of that cheap bread may be in the medium to long term. But, as I said before, we do view it as predatory. It may be legal but we believe it is immoral.[4]

1.8 SPAR Australia Ltd in its submission to this inquiry confirmed concerns regarding the level and concentration of market power in Australia's retail industry:

> The issue of misuse of market power is one that SPAR has first-hand experience of in terms of suffering commercially from market power abuse and seeing first-hand the total incapacity of the current legislative and regulatory framework to address it.
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> It is interesting to note that since the 2008 Grocery Inquiry conducted by the ACCC and its examination of the retail grocery market and the power of the two supermarket chains Coles and Woolworths and the power of Metcash as a wholesale provider to the independent sector, not much if anything has changed.
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> Coles and Woolworths continue to dominate the retail sector and Metcash continues to dominate the wholesale independent sector, with the ultimate loser being the Australian consumer with small independent family owned business being collateral damage along the way.[5]

1.9 SPAR's submission also pointed out the unmistakable truth: sections 46(1) and 46(1AA) of the CCA do not go far enough to prevent anti-competitive conduct. Section 46 prohibits the misuse of market power, stating:

> (1) A corporation that has a substantial degree of power in a market shall not take advantage of that power in that or any other market for the purpose of:
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> (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;
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> (b) preventing the entry of a person into that or any other market; or
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> (c) deterring or preventing a person from engaging in competitive conduct in that or any other market.

1.10 Section 46(1AA) on the other hand prohibits a corporation that has a substantial market share from supplying or offering to supply 'goods or services for a sustained period at a price that is less than the relevant cost to the corporation of supplying such goods or services' for the same purposes as those listed in section 46(1).

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4 Mr Jos de Bruin, CEO, Master Grocers Australia, *Proof Committee Hansard*, pp. 9–10.

5 SPAR Australia Ltd, *Submission 5*, p. 3.

1.11 The Harper Review has already identified the limits of requiring proof of the purpose of damaging a competitor and the 'effects test' would be a much needed reform. The draft report released by the Harper Review explains the arguments in favour of an 'effects test':

> As a matter of policy, competition law ought to be directed to the effect of commercial conduct on competition, not the purpose of the conduct, but it is the anti-competitive effect of the conduct that harms consumer welfare; and
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> As a matter of practicality, there can be difficulties in proving the purpose of commercial conduct because it involves a subjective enquiry, whereas proving anti-competitive effect is less difficult because it involves an objective enquiry.[6]

1.12 The draft report also makes the following proposition in relation to reforming section 46:

> The Panel proposes that the primary prohibition in section 46 be re-framed to prohibit a corporation that has a substantial degree of power in a market from engaging in conduct if the proposed conduct has the purpose, or would have or be likely to have the effect, of substantially lessening competition in that or any other market.[7]

1.13 In that context, this amendment would be even more effective if an effects test was implemented. To date, even where anti-competitive conduct has been identified, prosecutions by ACCC have been few and far between with only 18 cases brought in the past 38 years. Successful prosecutions are even fewer and further between, with the courts siding with the ACCC in only 11 of the 18 cases.[8]

1.14 While enforcement of these provisions is an issue, one must also question whether the penalties currently available under the CCA are sufficient to deter anti-competitive conduct. Many submitters to this inquiry quite rightly pointed out that divestiture of a corporation is not a straightforward matter and that it would have large scale ramifications on the business operations of a corporation. Ms Caroline Coops of the Law Council of Australia explained to the committee:

> …business assets are rarely capable of easy dissection. For example, whilst individual grocery stores are easy to identify they need to access wholesale supply and are often reliant on internal distribution centres or external third-party distributors in order to operate efficiently. A major internal

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6 Competition Policy Review, *Draft Report*, September 2014, http://competitionpolicyreview.gov.au/files/2014/09/Competition-policy-review-draft-report.pdf (accessed 25 February 2015), p. 206.

7 Ibid, p. 210.

8 Ibid, p. 210.

> distribution centre for a large grocery operation cannot practically be cut in half to keep servicing stores that may be divested.[9]

1.15 However, the threat of divestiture would act like the sword of Damocles in that a corporation would be even more wary of abusing its market power with a potential divestiture sanction. Given the state of our grocery sector in Australia (as well as other sectors with high concentrations of market power), the penalties available under the CCA are acting as more of a butter knife than a sword. They are more of an inconvenience or nuisance and do little to discourage large corporations from abusing their market power.

1.16 The fact that similar divestiture powers exist overseas in the United States, Canada, the European Union and the United Kingdom demonstrates other jurisdictions take addressing anti-competitive behaviour seriously. It is true that to date these powers have only been exercised by consent in the US and have not been exercised at all in the EU and Canada. However, I do not accept that this means these powers are not useful as demonstrated in my discussion with Mr William Reid from the Law Council of Australia during the committee's public hearing:

> **Senator XENOPHON:** …In the EU and Canada these laws have been in place for a number of years but have not been used. I do not know whether you have had the opportunity to do research on this but do you consider that simply having such a law on the statute books would act as a sword of Damocles? When a large corporation is managing risk, would it think not only could it cop a fine but the court, if it is so minded, could order a divestiture which would be incredibly painful and messy for the corporation?
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> **Mr Reid:** I am not aware of research that has been done in relation to that. In Europe, of course, there is a different situation from our own in that the regulator imposes the penalty and makes the initial decision in relation to a contravention. The regulator has never done that. In that context, one might assume that businesses in Europe do not seriously consider it a threat in relation to dealing with the regulator, its track record having been never to have imposed this sanction. Perhaps there is more uncertainty in our system. Where a court is invested with this power and has it at its disposal, that may remain a more credible threat for business into the future than would be the case otherwise.[10]

1.17 There is an increasing groundswell of public opinion including from the small and medium business sector to see meaningful reform in the area of Australia's competition policy. A divestiture power should be an integral element of such a reform package. Whilst I acknowledge there are some concerns about this bill, I believe it is necessary for it to be passed in order to protect the long term interests of

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9 Ms Caroline Coops, Chair, Competition and Consumer Committee, Law Council of Australia, *Proof Committee Hansard,* p. 1.

10 Mr William Reid, Member, Competition and Consumer Committee, Law Council of Australia, *Proof Committee Hansard,* p. 4.

Australian consumers and small businesses. This bill, if passed, will irrevocably change the corporate culture of some large corporations for the better.

Recommendation

1.18 That the bill be passed.

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