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Australian Senate
Economics Committee
Parliament House
CANBERRA ACT 2600

Attention: Mr Peter Hallahan
Secretary

INQUIRY INTO THE EFFECTIVENESS OF THE TRADE PRACTICES ACT 1974 IN PROTECTING SMALL BUSINESS

The Small Business Development Corporation (SBDC) is an independent statutory authority established to assist and promote the growth and viability of the small business sector in Western Australia. The SBDC has been a keen participant in the ongoing debate into the effectiveness of the Trade Practices Act (TPA), most recently having participated in the Review undertaken by the Dawson Committee.

The SBDC considers that the Dawson Committee Review of the TPA erred in not addressing criticisms by small business organisations that particular sections of the TPA require amendment. Section 46 of the TPA which prohibits misuse of market power and the Part IVA provisions dealing with unconscionable conduct in commercial transactions were identified in many small business submissions to the Committee as being ineffective.

The SBDC has particular concerns with three aspects of the Dawson Committee's Review, and the Commonwealth Government's subsequent response to the Committee's recommendations.

These principal areas of concern for the SBDC are:

- Section 46 of the Trade Practices Act (TPA) requires amendment to strengthen protection for small business against predatory pricing by larger competitors and ensure that the Act protects small firms against misuse of market power.

- The section 50 merger provisions of the TPA are inadequate to protect small retail businesses against the process of 'creeping acquisitions' by major supermarket chains.

- The proposed notification process for collective bargaining by small businesses requires further clarification, and guidelines should be issued as soon as possible by the Australian Competition and Consumer Commission (ACCC).

The SBDC will also comment on whether the unconscionable conduct provisions provide sufficient levels of protection for small business and the effectiveness of Part IVB of the TPA (Industry Codes).

1. Section 46 of the TPA

A major issue in submissions to the Dawson Committee concerned the role of section 46 of the TPA (misuse of market power) and whether it should be amended to afford greater levels of protection for small businesses in their dealings with larger firms. The SBDC advocated for an "effects test" to be added to section 46.

Section 46 prohibits a corporation with a substantial degree of market power from "taking advantage" of that power "for the purpose" of:

- eliminating or substantially damaging a competitor;
- preventing the entry of a person into a market; and
- deterring or preventing a person from engaging in competitive conduct in a market.

The ACCC is hindered in its enforcement of section 46 because proving "purpose" can be difficult. An "effects test" would allow courts to examine the uses of market power having anti-competitive effects, instead of being limited to considering the intent of the conduct. A reverse onus of proof would be placed on large companies to prove that their conduct did not have anti-competitive effects on the market and on small businesses in particular.

The SBDC is aware that issues have been raised about the introduction of an 'effects test' in terms of the impact it may have on firm behaviour and vigorous competition. However, we would argue that more could be done to examine how such a test might be applied to overcome these concerns or to identify alternatives to this proposal that would provide the strengthening needed to section 46. The deliberations of the Senate Economics References Committee are crucial in this respect.

The SBDC believes that the introduction of an "effects test" should be coupled with powers for the ACCC to issue "cease and desist" orders against large firms allegedly engaging in anti-competitive conduct against smaller rivals. These orders would ensure that the alleged conduct could be halted as an interim measure, pending a judgment being made on the conduct by courts, and preventing any further damage to smaller competitors and the market in general.

A weakness of the current system can be the time taken to progress a matter through the courts such that, even if a large firm is found to have misused its market power to engage in predatory pricing, the market may have been significantly damaged and smaller competitors eliminated during the process. "Cease and desist" orders could serve to redress this balance.

As part of the process of promoting competition in a market it may be necessary to take action to protect competitors in that market from substantial damage or elimination as a result of anti-competitive conduct. The SBDC is not convinced that the process of obtaining an interim injunction can address this issue as efficiently as "cease and desist" orders, and would call for further consideration of this matter.

The recent High Court decision in the *Boral* Case (*Boral Besser Masonry Ltd v ACCC*) further weakened the protection afforded to small business by section 46.

The Court found that Boral Masonry Ltd (Boral) did not breach the misuse of market power provisions of the TPA as alleged by the ACCC, overturning a unanimous decision of the Full Court of the Federal Court.

At the time, the ACCC described the judgment as a comprehensive defeat that eroded the ability of the TPA to protect small businesses from the power of large firms. Section 46 cases taken by the ACCC have been difficult to prove and to date there has only been one successful outcome (*ACCC v Universal Music Australia*), which is currently on appeal to the Full Federal Court.

The difficulty for small business arising from the Boral case is that the High Court decided that while section 46 is focused on market conduct directed at competitors or potential competitors, it is not concerned with protecting those competitors as an end in itself.

The SBDC believes that it may also be necessary in promoting and fostering competition in a market to intervene to protect competitors or a class of competitors in that market from suffering damage or being driven out of the market as a result of a larger competitor's actions. The challenge is to find the right balance that will distinguish between the sort of tough but lawful competition referred to by the High Court in the 1989 *Queensland Wire Industries* case and unlawful anti-competitive behaviour which may disadvantage consumers and the market.

As section 46 stands, small firms in the retail sector particularly, have virtually no defence against 'predatory pricing' by larger competitors, provided the larger firm does not price below cost. The effect of the larger firm's pricing practices is likely to significantly damage the smaller firm, or even drive them from the market, but it will be extremely difficult to prove or infer the larger company's purpose was other than to meet competition in its own market.

The SBDC believes section 46 does not function to address predatory pricing conduct because:

- Section 46 might not catch predatory pricing conduct by a firm that at the time of the conduct has less than the substantial degree of market power required by the section – although the firm's purpose in engaging in the predatory pricing is to acquire that very degree of market power.

- Section 46 might not also catch predatory pricing by a firm with a substantial degree of market power if it could be argued that a firm without a substantial degree of market power would have reacted in a similar way to the entry of a new competitor in the market – as happened in the Boral case.

The SBDC believes a case should be made for the insertion of a new and separate section in Part IV of the Trade Practices Act to deal specifically with predatory pricing behaviour by large companies and to close the 'loopholes' that currently prevent section 46 from addressing the issue.

The new section could be drafted in such a way as to prohibit large companies from engaging in practices where the end result (and intent) of those practices has the effect or likely effect of substantially lessening competition in a market. The emphasis must be on "substantially" lessening competition because every commercial contract lessens competition to some extent and competitors seeking to take away business from each other are not acting illegally.

The new section should not, therefore, discourage legitimate business competition in terms of pricing, quality and output, all of which are intended to be part of the competitive process, and can be a legitimate defence to any claims of anti-competitive predatory conduct. The intent of the section would be to stop behaviour going beyond these accepted commercial norms.

The SBDC recognises the inherent difficulties associated with drafting clauses that meet both these requirements, but is also aware of opinion to the effect that this could be achieved. Recent discussions at the July meeting of the Small Business Ministerial Council focused on this very issue – "finding the words" to provide stronger protections for small businesses against predatory pricing without stifling vigorous competition in the marketplace. State and Territory Small Business Ministers committed to work together toward this end. The SBDC would call on the Senate Economics References Committee to actively support this goal.

2. Section 50 Mergers and 'Creeping Acquisitions' in the Retail Sector

The SBDC broadly supported the Dawson Committee's recommendation to retain the current 'substantial lessening of competition' test for mergers being considered under section 50 of the TPA, but believes there is room for amendments to address an evolving potentially anti-competitive issue – 'creeping acquisitions' in the retail sector.

Under section 50, the ACCC has the power to reject corporate takeovers or mergers where an individual acquisition would substantially lessen competition in a market. There is concern among small retailers, however, over 'creeping acquisitions' where dominant retailers buy up a series of small firms over a period of time rather than in a single large acquisition. In many cases, small retailers are willing to sell out because of 'generous' offers made by major chains.

In these situations, each new individual acquisition will not necessarily breach the section 50 merger provisions or significantly alter the major firm's market share, but over time may have the effect of substantially lessening competition in a market.

Independent supermarkets made submissions to the Dawson Committee to change the merger provisions to give the ACCC more power to stop large chains from continuing with small scale acquisitions in these circumstances.

The Australian retail industry has become more concentrated in recent years through consolidations and mergers, with Woolworths and Coles Myer being the dominant players in the market. Small retailers believe that they are disadvantaged by their larger competitors using their market power to obtain better deals from suppliers.

In June this year the ACCC confirmed that it was monitoring relatively small acquisitions by Coles Myer and Woolworths, so-called 'creeping acquisitions', which were intended to increase the companies' respective market shares in small increments. This included scrutiny of large retail chains buying out independent operators and liquor retailers.

The ACCC review has been underway for more than 12 months and is apparently an ongoing process but as yet there are no indications at what point the ACCC can or should view small and often 'insignificant' acquisitions in the wider context.

The SBDC recommends, therefore, that the ACCC be asked to provide to the Commonwealth Government the outcomes to date of its monitoring process plus whatever legal and economic advice it has obtained to determine whether section 50 of the TPA should be amended to deal with 'creeping acquisitions'. This should be done as a matter of urgency before the proposed draft legislation is presented to the Commonwealth Government.

3. Collective Bargaining for Small Businesses

The Dawson Committee recommended that a 'notification' process to the ACCC be introduced for collective bargaining by small businesses and farming bodies in their dealings with large firms. The process will provide that bargaining notified to the ACCC will be legal after 14 days unless the ACCC opposes it. A "transaction value" of $3 million will provide a definition of small business.

Collective bargaining agreements are constrained by the TPA because they will often involve arrangements between competitors as to the price at which goods are bought and sold. However, in the case of small businesses negotiating with big business, there may be community benefits in such bargaining to provide countervailing bargaining power.

The ACCC has previously recognised this issue and the TPA provided for the authorisation of collective bargaining arrangements, albeit relatively few in number and also required to go through a cumbersome authorisation process to obtain approval.

There is uncertainty surrounding the approval process for proposed new collective bargaining arrangements. It has been claimed in some Commonwealth Government circles that for the first time, local corner stores will be able to compete with suppliers like Coles Myer on price, while retail tenants should be able to better negotiate collectively with big landlords.

This seems to be an overly optimistic assessment of how small businesses might access the notification system. Small corner stores are unlikely to be able to join with other small operators to access comparable buying prices with Coles Myer, although it is conceivable that a group of Retravision dealers, for example, could readily take advantage of the notification process.

The rural and regional small business sector is likely to benefit from collective bargaining. Farmers and suppliers are likely to be able to collectively negotiate some contracts and prices with large supermarket chains. Small retailers, however, may find that the collective bargaining process has no direct application to their needs.

The ACCC recently renewed authorisation for Inghams Pty Ltd to continue to conduct collective contract negotiations with its chicken growers in South Australia for five years.

In Western Australia, the ACCC authorised CSR Limited (CSR) and its independent small business carriers to use a concrete cartage job allocation system because it believed the public benefits gained from the system are likely to outweigh the anti-competitive detriment.

At the same time, the ACCC issued a draft decision proposing not to authorise collective bargaining arrangements proposed by the Queensland Golden Casket Agents' Association (lottery agents) seeking authorisation to conduct negotiations on behalf of its members in relation to the terms and conditions of agency agreements and arrangements.

The Dawson Committee recommended that the notification process should be available only to small businesses in negotiation with big business, where experience has shown that collective bargaining may do little or no harm to the competitive process and may generate public benefit.

It appears that the collective bargaining process might be used by some retail buying groups, primary producers and suppliers, cartage contractors, newsagents, hotels (negotiations with TAB and Sky Channel), health service providers (for collective negotiations with health funds and suppliers), travel agents (negotiations with major airlines) and a range of businesses dealing with large or dominant firms in their particular market.

However, there are no guidelines to support this supposition. It might be that the notification process for collective bargaining is unlikely to be of assistance to a broader range of small businesses dealing with larger suppliers where there is no expectation that the arrangement will lead to some form of public benefit.

It is difficult to envisage that retail tenants, for example, might be able to use the process to negotiate collectively with big landlords. There are also expectations that independent petrol stations would be able to negotiate collectively with oil companies and smash repairers might negotiate better deals with insurance companies.

The problem for small business is that no-one knows yet how the process will work and whether the ACCC will apply the same criteria currently used in determining authorisation to evaluate proposed collective bargaining arrangements, and what will be the costs associated with the process. The small business sector requires some degree of 'certainty' about the process before it can evaluate whether the benefits are likely to be as tangible and widespread as claimed by some Commonwealth Government circles.

Accordingly, the SBDC recommends that the ACCC produce guidelines for small business (on a similar basis to those to be produced for unconscionable conduct), setting out the processes to be followed and clarifying the circumstances in which collective bargaining is likely to be endorsed by the ACCC.

4. Part IVA - Unconscionable Conduct

The SBDC provides the following comments on whether Part IVA of the TPA deals effectively with unconscionable conduct.

The unconscionable conduct provisions dealing with commercial transactions, section 51AA and section 51 AC, were introduced as a result of the imbalance of bargaining power arising between small and large businesses and are intended to protect small businesses regularly dealing with larger firms. Taken overall, the TPA has been successful in protecting some retail tenants, franchisees and primary producers through the operation of section 51AC. The reach of section 51AA, however, has proved to be very limited to the point where it is regarded as singularly weak and unable to provide any real levels of protection for small business.

Section 51AC covers transactions of goods and services under a $3 million threshold and is very broad in its scope. The section provides a wide range of matters courts may consider in determining whether conduct is unconscionable, without in any way limiting other matters a court can take into account. The provisions of section 51AC were made deliberately broad, rather than trying to encapsulate all likely examples of unconscionable conduct, so that courts have flexibility to examine any matters where unconscionable conduct is alleged to have occurred.

The ACCC has taken a relatively small number of court cases to test the effectiveness of section 51AC and has not yet lost a case litigated under the section. The ACCC's focus has been to establish sufficient precedents through the medium of test cases so that small businesses can enforce their own rights under section 51AC through the courts. It would be premature, therefore, to argue that, in itself, section 51AC is not adequate to the task of providing protection for small businesses against unconscionable conduct. More time is needed before a determination can be confidently made on this issue.

However, although the ACCC's regime of test cases has been a positive step towards increased levels of protection for small businesses, it is already very clear that the complexity and costs associated with litigation are still powerful deterrents to many small businesses from pursuing their legal rights against larger competitors – and there are many more cases in the marketplace than the 15 or so matters pursued by the ACCC.

Notwithstanding that state jurisdictions now have the capacity to draw down the unconscionable conduct provisions, which is intended to give small businesses easier and less expensive access to justice, the SBDC is concerned that the protections available under section 51AC are not and will not be utilized to the fullest extent possible because of the complexity and costs associated with taking private litigation.

The SBDC believes there is a need for increased funding for the ACCC to take more cases on behalf of small firms that are unable to exercise their legal rights, particularly against predatory and unconscionable conduct directed against them by larger companies. If section 51AC is to achieve its original goal of influencing firm behaviour and therefore work in a preventative fashion, this will be a necessity. It would also be appropriate for increased funding for the ACCC to seek leave to intervene in court proceedings where a small business has exhausted its funds and is unable to see a matter through to resolution before the court.

5. Part IVB Industry Codes

Part IVB of the TPA allows for the making of mandatory and voluntary industry codes regulating dealings between both suppliers and consumers as well as between participants in an industry.

Codes of conduct can play an important role in ensuring that there are good practices and dispute resolution agreements in place in industry sectors where large and small firms are likely to encounter friction and pressures in their business dealings with each other. The SBDC is supportive of the use of codes of conduct as an alternative to regulation.

Voluntary codes, however, have not been generally successful in resolving frictions within industry sectors. The ACCC, for example, has been working to produce agreement on voluntary national codes of conduct for smash repairs and retail tenancy issues, so far without success.

Whilst, the SBDC supports the concept of voluntary industry codes of conduct serving as a means of co-regulation, a half way measure between industry self regulation and mandatory government regulation, it is not convinced that this measure has proven effective in providing adequate protections for small businesses. The ACCC's proposal for a much expanded role for voluntary industry codes in place of prescriptive regulation is something the SBDC considers should be approached with real caution.

The SBDC strongly believes that provisions for prescribing industry codes of conduct under the TPA must be retained to fill the breach where a voluntary industry code of conduct has failed to meet its objectives or where behaviour has been shown to warrant more heavy handed intervention by Government. The knowledge that codes can be prescribed also has the advantage of serving as a powerful incentive to industry to get behind voluntary codes.

The SBDC understands that the ACCC is currently actively discussing industry codes with nearly 40 industry groups – ranging from informal consultations, including working parties formed either to develop or review a code of practice such as the Car Rental Industry Code, or to review the effectiveness of a particular code, such as the Franchising Code or the Australian Direct Marketing Code.

In the short term, the SBDC recommends that the ACCC publish guidelines for business and industries setting out criteria that need to be met for the establishment of a successful industry code, and detailing how ACCC endorsement can be obtained for these codes.

The ACCC has informally identified some of the successful core elements for industry codes but these need to be defined and clarified. In particular, the SBDC would like to see more information available in the public domain regarding the following criteria:

- stakeholder consultations;
- code administration;
- complaints handling;
- independent review of complaints handling decisions;
- sanctions for non-compliance; and
- review of the Code.

The SBDC also recommends that the ACCC be required to report to the Commonwealth Government within 12 months on the extent of industry uptake of its proposed endorsed codes of conduct scheme, and what the Commission perceives to be industry 'black spots' that are likely to require prescriptive codes under the TPA. In this way some preliminary assessment of the efficacy of the ACCC's proposal can be made.

The SBDC would be pleased to provide any further clarification of its views if required and Ms Juliet Gisbourne, Director, Policy and Business Liaison, can be contacted on (08) 9220 0204 or email gisboj@sbdc.com.au.

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MANAGING DIRECTOR

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