Woolworths Limited

Supplementary Submission

to the Senate Economic References Committee ("Committee")

Inquiry into the effectiveness of the Trade Practices Act 1974 in protecting small business

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In response to the invitation issued by the Committee Chair on 15 December 2003 to comment on the decision of the High Court in *Rural Press v. ACCC* (11 December 2003), Woolworths makes the following supplementary submission to the Committee's inquiry into the effectiveness of the *Trade Practices Act* 1974 (**"Act"**) in protecting small business.

In summary, Woolworths offers the following comments: -

(a) The High Court's *Rural Press* decision does not indicate any deficiency in the scheme of section 46; and, arguably strengthens the ACCC position across Part IV of the Act;

(b) The *Rural Press* decision illustrates the important feature of the original Parliamentary intent underlying section 46 when first introduced in 1986, namely, that not all conduct by "big business" should be condemned, and, in particular, section 46 should not prevent large corporations from engaging in conduct that is "*economically efficient*" and which does not represent a "mis*use*" or "*taking advantage*" of substantial market power;

(c) On the facts of the case, the High Court majority found that the ACCC had not shown that Rural Press's undoubted market power had materially assisted the conduct in question, or been (mis)used, when the corporation made threats to launch a new regional newspaper in an area where the corporation had no presence and therefore no power;

(d) In relation to market definition, the ACCC chose to argue very narrow markets in *Rural Press*. While this approach considerably assisted the ACCC's case in relation to the section 45 allegations (on which the ACCC was successful) it also, as the High Court noted,

disadvantaged the ACCC’s arguments in relation to one of the essential elements of a contravention of section 46 – the “taking advantage” requirement (on which the ACCC failed). Given this deliberate strategic decision by the ACCC, *Rural Press* is not a good basis on which to make amendments to section 46 of the Act because the ACCC must make consistent judgements about the operation of markets for the Act as a whole;

(e) It is a mischaracterisation to suggest that the decision in *Rural Press* means that a company can **never** be found to have breached section 46 in a case where, having substantial power in one market, it engages in conduct in a different or second market. There will be many occasions where there is a real link or “material assistance” given to conduct in a second market by the fact of a corporation's possession of substantial market power in another market. Such a case could comprise "*leveraging"* and be in breach of section 46 (an example is the *Parkwood Eggs* case cited by the Full Federal Court in the *Rural Press* case);

(f) On this basis, it is strongly arguable (on the Parkwood eggs Case) that the ACCC's submissions to the Senate Committee (page 23) is clearly incorrect in suggesting that there is a "*gap*" in section 46, since such ‘leveraging’ can be caught by section 46;

(g) Further, a “quick fix” legislative amendment such as that suggested by the ACCC to deal with “leveraging” would remove the “taking advantage” test altogether, and this would have substantial negative consequences for businesses and consumers across Australia, It would discourage larger corporations that have been successful in one market from efficient conduct in entering new markets, competing and innovating in respect of new products and geographic areas;

(h) Woolworths reaffirms its view that commercial and competitive harm will come from modifying section 46 to address the alleged deficiencies suggested by proponents for reform. In particular, the business community, both large and small, will lose more in terms of the guidance derived from the past 17 years of case law, added compliance and legal costs and regulatory uncertainty if section 46 is amended as proposed by the ACCC. (It should not be overlooked that, as Woolworths has previously submitted to this Committee, there have in fact

been 11 cases to date since 1986 where a company was held to possess the necessary degree of substantial market power, on which actions for breach of section 46 are based);

(i) Instead of introducing legislative restrictions intended to protect small business at the expense of free and fair competition, the long term interests of Australian consumers are far better served by the ACCC issuing detailed Guidelines which assist the business community, both large and small, to better understand the ACCC's interpretation of section 46 and how the section will be enforced, particularly in cases concerning previously untested issues;

(j) Any proposed legislative reform, should be limited so as to add a clarifying statement to s.46 to address concerns since the *Boral* decision, to the effect that the test of "*substantial market power*" is intended to mean a lower threshold than that of dominance.

EXECUTIVE SUMMARY

1. The effect of the *Rural Press* decision on section 46 is to clarify the test for "taking advantage" of market power; the case adds nothing to the debate about the factors going to market power nor proof of purpose. The main facts of the conduct considered in the case are set out in the detailed comments attached.

2. Woolworths' cautions against using the *Rural Press* decision to justify any amendment to section 46 to change the test for "taking advantage" of market power. Amendments intended to weaken or remove the "*taking advantage*" requirement will result in the penalising of more efficient competitors (both large <u>and</u> small) by simplifying the section to issues of "power" and "purpose" only. Such a legislative change would be completely contrary to the intent of Parliament behind the 1986 TPA amendments which were concerned to see that large, less efficient firms did not engage in predatory conduct that damages competitors and consumers but not to jeopardise efficient competitive conduct by business generally.

3. Similarly, the *Rural Press* decision does not mean an amendment to section 46 is needed to expressly prohibit the "<u>leveraging of market power"</u>. Contrary to the ACCC's submissions on this point, section 46 already is capable of catching the "*leveraging*" of market power from one

market to another as demonstrated in the *Parkwood Eggs case* (which was cited by the Full Federal Court in the Rural Press case). For prohibited "*leverage*" to occur, there must be a **connection** between the company's power and the conduct in question – that is, the conduct that contravenes the other elements of section 46 must also in some way be **assisted by** the company's market power. (The Concise Oxford Dictionary defines "*leverage*" to include "*power, mechanical advantage gained by use, of lever; means of accomplishing a purpose, power, influence*").

4. In *Rural Press* in the High Court the ACCC did not prove its allegations regarding this element of "use" of any of the matters which made up Rural Press' power, - and that was the critical feature of its failure to convince the High Court majority of a breach of section 46. (The ACCC of course succeeded under section 45 of the Act over the same conduct) and 'strengthened' the ACCC's position on anti-competitive conduct in the area of 'exclusionary provisions'.

5. The failure by the ACCC to prove the section 46 allegations in *Rural Press* does not mean that in other cases, such a connection between conduct in a different market and the defendant's market power cannot be made good. In such a case, a "*leveraging*" of power can be established. However, a "quick fix" legislative amendment, such as that proposed by the ACCC to deal with "*leveraging*", would remove the "*taking advantage*" test altogether and have wide reaching and drastic anti-competitive effects as it would discourage larger corporations from efficient conduct in entering new markets, competing and innovating in respect of new products and geographic areas. **Such a change would be a rejection of the purposes behind the 1986 amendments, and would pose real risks to consumers who will be the ultimate victims of a less efficient economy.**

6. Woolworths supports the recent submission to the Committee of the National Competition Council that the Act enshrines protection of competition not competitors and it should not be amended to favour special interests, to the detriment of overall consumer welfare. This has been the fundamental principle which has been consistently emphasised by Courts, Parliament

and commentators (except those seeking to further their own special interests, at the expense of free and fair competition which is in the long-term interests of all consumers).

7. Any reform of section 46 limited to an amendment to section 46 to clarify that "*a substantial degree of market power*" is a lower threshold than "*dominance*" is however, supported as providing a legislative endorsement of judicial interpretation.

ADDITIONAL COMMENTS ON THE *RURAL PRESS* DECISION

Woolworths' interpretation of the decision

8. The core issue in *Rural Press* was whether a company, which possesses a monopoly in a particular market and enjoys considerable financial and organisation assets in that market, can be said to have "*taken advantage*" of its market power when it threatens to enter a new market, in which it has no existing presence or assets, in this case, to launch a new regional newspaper.

9. As the Committee would be aware, Rural Press made the threat to launch a new regional newspaper in a new market to compete with a rival, unless the rival withdrew paper, which it had begun to circulate in the market, where Rural Press had enjoyed a monopoly.

10. A majority of the High Court (Kirby J dissenting) held that making those <u>threats</u> did not contravene section 46. It is important to note that the High Court found that there was a breach of section 45 by Rural Press. This is similar to the decision in the recent Universal Case in which, although a breach of section 46 was not proven, the music companies were held to be in breach of section 47. These cases demonstrate that section 46 is not the only section of the Act available to small businesses to address anti-competitive conduct by large corporations.

11. The High Court majority in Rural Press properly held that it is not enough that a corporation has substantial market power and that an illegal purpose of deterring competition exists since section 46 requires that the methods chosen by which that purpose is pursued must <u>depend upon a misuse of market power</u> or that they be "<u>materially facilitated</u>" by the firm's market

power. This reasoning is important as it ensures that conduct that is merely reflective of ‘economic efficiency’ is not a prohibited activity by larger firms when entering new markets.

12. The majority rejected the ACCC's argument for "taking advantage" of market power, because it turned on "purpose" and "rationale" rather than use of market power. The ACCC advanced the proposition that the relevant question was "would the company be likely to engage in the same conduct" in the absence of its market power. The ACCC argued that Rural Press' conduct "would" not have been rational "but for" its market power and "its desire to protect it".

    The High Court majority rejected the ACCC argument on the basis that the relevant question is not to ask whether it is likely that the company "would engage in the same conduct" in the absence of its market power but to ask whether it "could engage in the same conduct". The majority found that Rural Press could have engaged in the same conduct even if it lacked market power and that it was an error to confuse the "purpose" of making the threat with the issue of "taking advantage" of the firm's power.

13. The High Court did, however, accept the ACCC’s submission that conduct can constitute a "taking advantage" of market power if the conduct is "materially facilitated" by the corporation's market power. In other words, the High Court has held that conduct can be a "taking advantage" of market power in breach of section 46 if it is "made substantially easier" by that market power. This is also an important clarification to section 46 which assists in its future interpretation by businesses.

14. The ACCC’s argument in Rural Press has now been put forward as a submission, that an amendment to the "taking advantage" limb of section 46 require courts to consider whether a corporation has taken advantage of its market power by reference to, inter alia, the question of whether the corporation "*would*" act in the same way without market power. This essentially would require the Courts to "second guess" the individual business strategy of the corporation and in effect for the Courts to exercise business judgment on the businesses hypothetical alternative strategy. The ACCC's proposal appears to take no account of economic efficiency considerations and gives priority to the **purpose of the conduct** over that of whether there is

really a **leveraging** of market power- since leveraging does require the use of a "lever" to bring the power to bear, not merely a purpose.

15. Woolworths submits that this amendment would place a significant burden on large corporations and would <u>tend to simplify the section to issues of power and purpose only</u>

Woolworths emphasises the critical importance of retaining the "taking advantage" element as set out in its Supplementary Submission of 16 September 2003.

16. Many competitive actions by firms with substantial market power may be held to be a "taking advantage" on the ACCC's proposed test. It is always possible that competitive conduct by a large firm (such as discounting, bulk purchasing, introduction of new product lines, development of new technology or entry into new markets) will be found by a court to be undertaken with a purpose of preserving the corporation's substantial market position.

In other words, it is quite possible that it would be held that the corporation "would not" have engaged in the conduct without substantial market power.

17. An example is illustrative. Take a corporation with substantial market power (for example a domestic airline with 70% market share) that starts a low-cost brand to better compete with a new rival. This large scale investment would be done, presumably, with the purpose of preserving the company's market position. Under the ACCC's amendment, this may constitute an illegal "taking advantage" of market power. This is because, if the airline was one of many airlines in a competitive market, it <u>would</u> not have had the incentive to invest in this way to preserve its substantial market position. . The competitive nature of the market is enhanced and consumers benefit from this additional competition.

18. Consequently, the ACCC's suggested amendment would be an undesirable result by amending the "taking advantage" test under section 46 of the Act.

Is an amendment required to deal with "leveraging" market power?

19. The ACCC claims, in its media release on the *Rural Press* decision (11 January 2003) that "*the decision has not addressed the Full Federal Court's decision that the leveraging of market power between markets does not constitute a misuse of market power*."

20. Contrary to this claim and as noted above, the *Rural Press* decision expressly confirms that a true leveraging case can be pursued under section 46. In the *Rural Press* case, the Full Federal Court <u>expressly</u> <u>contemplated</u> that leveraging of market power <u>could</u> comprise a breach of section 46, if the right facts were proven:

> "*In theory, there might be circumstances where the use of facilities devoted to market A by a party which has power in that market, for use in market B, could be said to involve a use of market power derived from market A. For example, if the threat made here by the appellants were carried out, and printing and distribution of the new Riverland paper meant that the appellants could not service the Murray Bridge market because of the diversion of resources to the Riverland, then (depending upon the evidence in the case) it might be said that the appellants could not have acted in this way in the Riverland market if there had been effective competition in the Murray Bridge newspaper market. Nothing like this has been suggested [by the ACCC] in the present case*." [2002] FCAFC 213 at para 146.

COMMENTS ON THE SUBMISSION BY THE NATIONAL COMPETITION COUNCIL

21. Woolworths is broadly supportive of the recent submission to the Committee by the National Competition Council ("**NCC**") (Submission No. 14 on the Committee's website).

22. In particular, Woolworths agrees with the NCC's position that:

> "*legislation that genuinely promotes the interests of the wider community provides the foundation for a flexible, responsive and internationally competitive economy. In contrast, regulation that only serves the interests of certain groups, industries and occupations often represents a cost to the community as a whole. The Council has encountered instances where possibly well meaning legislation aimed at reserving market segments for smaller business from perceived market dominance of large players has had adverse impact for community welfare.*
>
> "*the Council would urge the Committee, if it is considering implementing "other measures" to assist small business, to do so in a manner that does not introduce discriminatory restrictions on competition that involved trading off benefits for the community in order to protect the interests of certain groups, industries or occupations. We ask that ... any proposals that the Committee makes to advance the interests of small business do not have perverse effects that reduce competition or allow re-imposition of restrictions that reduce consumer welfare*".

Nowhere is this recommendation more relevant and more critical than in the Australian Food Retail Industry. For some years vociferous sectoral interests have aggressively insisted on protection from free and fair competition at the cost to consumers of high prices, lower services and more inconvenience.

A STATUTORY CHECKLIST OF FACTORS FOR SECTION 46?

23. Woolworths is aware that the Committee is considering recommending that the ACCC implement a checklist of factors to section 46 to provide guidance on the issue of whether a corporation has "substantial market power".

24. The test for market power is well established by economic and legal authority. The factors that may be included in such a list, such as market shares, entry barriers and freedom from constraint are already considered by the Courts in section 46 cases.

25. The core issue that appears to be driving many of the proposals to amend section 46, including the introduction of a checklist, is the perceived effect of the *Boral* decision. There is a view that the *Boral* decision has limited the operation of section 46. As Senator Brandis said to Mr. Roger Corbett during public hearings (30 September 2003):

> *"I take a fairly conservative view of this. If it were not for the Boral case, which I think did confine the section rather surprisingly, I would have been happy enough with section 46."*

26. As previously submitted, Woolworths does not consider that the emotive response to the facts in the *Boral* case warrants legislative, as opposed to administrative, reform of s.46. That case dealt with a corporation that acted to defend its own position in a fierce price war, in a competitive market, in which its market share was slightly above 20%. That such a corporation was found to not possess “substantial market power” under section 46 should not, in Woolworths' view, be a basis for wholesale legislative reform at the insistence of certain sectional interests purporting to represent small business.

27. Further, nowhere in the High Court's *Boral* decision is it suggested that predatory pricing cannot, in the appropriate circumstances, be caught by section 46. Indeed, the opposite is suggested. The Federal Court, per Gyles J, in *ACCC v Qantas* [2003] FCA 125, confirmed that the High Court has left open the possibility that predatory pricing is caught by section 46.

28. Nevertheless, there is a misconceived position put by some, including the Fair Trading Coalition, that *Boral* has limited section 46 to oligopolies and has resuscitated a defacto form of the old "dominance" test under section 46. To put this view to rest and while this is not Woolworths' interpretation of the *Boral* decision, Woolworths would not object to an amendment to s.46 as follows:

"46 (3A) For the avoidance of doubt, a corporation may possess a substantial degree of power in a market even if it is not in a position to dominate that market."

29. Woolworths considers that this amendment would satisfactorily address the perceived shortcomings of the *Boral* decision, while preserving the sound policy basis on which section 46 was introduced.

30. Such an amendment, unlike many others that have been proposed to the Committee, would not unduly distort or deter competition in Australian markets to the advantage of sectional interests, intent on being protected from the rigours of open and fair competition but to the detriment of overall Australian consumer welfare.

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