Submission to
Senate Economics References Committee

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

September 2003

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1. EXECUTIVE SUMMARY

To enable the Trade Practices Act 1974 to protect small to medium retailers and facilitate a fair market –

- The 'effects test' provision of Section 46 should not be applied;
- The definition of unfair conduct should be applied to Section 51AC as recommended in the Reid Report;
- A mandatory industry code of conduct for tenancy issues should be established by key stakeholders including the ACCC;
- In line with the recommendations made in the Trade Practices Act Review (April 2003), small retailers should be able to collectively bargain with shopping centre management/ownership on tenancy issues;
- A national body with appropriate powers should be accessible to all Australian small to medium retailers to ensure a mandatory code is effective.

2. INTRODUCTION

2.1 The Australian Retailers Association

The ARA is the nationwide voice of the Australian retail industry.

The ARA's membership comprises approximately 11,000 retail businesses, which transact an estimated 70 percent of the nation's retail sales and employ around three quarters of the retail workforce of 1.1 million people.

ARA members operate around 40,000 retail outlets across the nation. Approximately 10,000 or 95 percent of the ARA's members are small businesses (i.e. employing less than 20 staff) operating in only one state.

3. OBJECTIVES

In this paper, the ARA will address sections 1(a) to 1(d) of the terms of reference of the Inquiry, illustrating how smaller retailers are disadvantaged in relation to tenancy issues and how the Trade Practices Act 1974 could be made more effective to ensure fair practice relating to tenancy.

4. SMALL BUSINESS

Each store is treated as a discreet unit by landlords, even if it is part of a national chain. In relation to tenancy issues, chain retailers can be considered as specialty small to medium enterprises (SMEs) as they must deal with shopping centre management and landlords in every operating location.

5. KEY ISSUES RELATING TO INQUIRY TERMS OF REFERENCE POINTS 1(A) TO 1(D)

1(a) Whether section 46 of the Act deals effectively with abuses of market power by big businesses, and if not, the implications of the inadequacy of Section 46 for small businesses, consumers and the competitive process.

In competitive environments, there are always tensions between competitors, suppliers and consumers. From time to time this leads some businesses to allege the misuse or inappropriate use of market power.

To establish that a business has misused its market power, it must be proven that it did so for a proscribed purpose (for example, to eliminate a competitor or to prevent a competitor from entering a market).

Some businesses mistakenly believe that adding an 'effects test' provision to Section 46 of the Trade Practices Act would address concerns about grossly unfair conduct.

However, the ARA view is that an 'effects test' is ill founded and that grossly unfair conduct can and should be dealt with under section 51AC of the Act.

Competition by its very nature can harm a competitor. Firms aim to increase their market share (and can do that without misusing their market power) and as a result some competitors may exit the market.

Under an 'effects test', this natural function of a competitive market could be construed as a breach. This oversimplifies the many factors that may cause a business to exit.

Under an 'effects test', a retailer that is small by national standards but large in a local market could be charged with misusing its market power simply by extending trading hours, enhancing its product range or offering a new service, if the effect was that an even smaller competitor was harmed.

Further, allowing retailers who are unable to compete in the dynamic retail sector to use an 'effects test' would protect and condone inefficiency, and create an environment where consumers would be forced to pay for these inefficiencies.

The ARA believes adding an 'effects test' to Section 46 of the Act would potentially stifle effective competition; result in higher prices and less choice for consumers; cause a lack of innovation and differentiation among retailers; and result in an inefficient and tardy retail sector. The imposition of an 'effects test' is therefore not in the best interests of the Australia public and economy.

1(b) Whether Part IVA of the Act deals effectively with unconscionable or unfair conduct in business transactions

Part IVA of the Act does not currently deal effectively with unfair conduct.

The ACCC has not addressed retail tenancy matters with sufficient vigor under the new Section 51AC provisions. Although there have been a number of cases seeking to apply the new provisions to tenancy issues, none have been pursued.

Particular tenancy issues can be addressed via specific legislation, including the draw-down of Section 51AC into State and Territory Retail tenancy laws. It is critical for the development of this specific legislation and its provisions that the ACCC pursue cases of breaches of Section 51AC.

The issue of retail tenancy is a clear example of developing specific legislation to deal with an identified problem, without impacting on the wider competitive environment.

It is the ARA's view that such specific treatment would more effectively address the challenges faced by small business.

The ARA supports the Australian Senate Economics Committee in its suggestion that the ACCC consider issuing guidelines to clarify its approach to Part IVA.

The ARA recommends that tenancy issues should be considered during the development of guidelines to provide for the rights of retail landlords and tenants in relation to unfair conduct.

The recommendations in the Report by the House of Representatives Standing Committee on Industry, Science and Technology, May 1997 (Legislation protection against unfair conduct, recommendation 6.1) call for the repealing of the existing Section 51AA and the incorporation of a new provision proscribing unfair conduct in commercial transactions.

The ARA strongly supports recommendation 6.1, which set out a reasonable and accessible definition of 'unfair'.

Victoria has adopted parts of the 6.1 definition of 'unfair' in their 2003 amendments to the Victorian Fair Trading Act (see Section 32W).

The following issues contribute, directly or indirectly, to causing unfair conduct that may affect small business, and should be considered by the ACCC when considering how section 51AC might apply.

- Government planning laws, in restricting the development of shopping centres, create anti-competitive franchises for shopping centre owners/developers. While such laws have been assumed to be for the public benefit, their resultant franchises are fiercely defended and held by the shopping centre owners holding the franchises.

- A by-product of Government planning laws is that in areas where there were originally two centres (e.g. Hornsby, Morley and Frankston), the dominant landlord in each case now controls both centres.

- The anti-competitive forces characteristic of the franchises impact negatively on small and specialty retail tenants' businesses in those centres. A retail tenant is often captive to a particular centre when there is no suitable alternate space for that type of retailer in the centre's catchment area.

- High and escalating occupancy costs (for many small and specialty retailers, lease fees are now the largest operating cost, ahead of retailing's traditionally largest operating cost, labour) and other practices brought about by those anti-competitive forces have reduced the proportion of funds deployed on labour by those tenants and hampered their ongoing capacity to employ.

- Planning laws have restricted development to expansion of existing centres – particularly regional ones - rather than allowing any greenfield sites. Such expansions have resulted in a lower sales per square metre, reducing tenants' gross profits and further exacerbating their capacity to employ.

- The anti-competitive forces result in the following unfair symptoms:

  - rents in excess of tenants' capacity to pay and which ignore the principle that rent is the economic surplus after all costs and profit have been taken into account.
  - landlords can invade the privacy of a tenant's financial affairs and misuse the tenant's turnover figures to squeeze the last drop of rent out of them on the ruse that the turnover information is required for other purposes.
  - landlords treat outgoings as profit items rather than cost-recovery.
  - landlords withholding relevant information from valuers used to consider a fair market rent e.g. incentives, rent-free periods and fit-outs.
  - disturbance of a tenant's right to 'quiet enjoyment' e.g. casual tenants, demands regarding fit outs, etc.
  - expropriation of goodwill in unreasonably refusing to renew a lease, or holding tenant to ransom at lease end.
  - non–disclosure of details of outgoings such as 'management fees'.
  - demanding of fixed formula rent increases e.g. 5 percent p.a. or CPI plus 1.5 percent, while all other economic indicators grow at a far lower rate.
  - landlords forcing tenants to contribute to advertising costs.

1(c) Whether Part IVB of the Act operates effectively to promote better standards of business conduct, and if not, what further use could be made of Part IVB of the Act in raising standards of business conduct through industry codes of conduct.

To protect retail businesses, a retail tenancy leases code of conduct should be made mandatory under section IVB of the Act.

A voluntary code requires both parties to act in good faith and good will, however, there has been a lack of commitment from the Shopping Centre Council of Australia (SCCA) in this area to date. Examples of successful voluntary codes of practice include the *ARA Supermarket Scanning Code of Conduct* and the *Jewellery and Timepiece Industry Code*.

In the area of tenancy, retailers have been unable to engage the SCCA in agreeing a code of conduct on a voluntary basis. The ARA developed a draft Outgoings Code (appendix A), using best efforts to be fair and reasonable, that was rejected by the SCCA without any offer of negotiation.

Further, the NSW Code of Practice for Retail Tenancies, which was agreed on a voluntary basis with the Property Council of Australia and the ARA, failed because key landlords (including Westfield, AMP and Lend Lease) refused to include in their leases certain principles as agreed in the code.

An example of this is that although the code banned ratchet clauses, some landlords continued to apply them. The impact of a ratchet clause was to prevent the rent going down even when the review mechanism allowed for a reduction.

Codes have an advantage over state-based regulation as they provide a cost effective way for small businesses that deal in a number of states. The uniform treatment of issues in a code of conduct applied nationally is a much more efficient way of managing tenancy issues than using state-based legislation.

The ARA supports the development of a national mandatory code developed by relevant stakeholders including the ACCC. The Franchising Code is an example of a successful code developed in a similar way (appendix B).

1(d) Whether there are any other measures that can be implemented to assist small businesses in more effectively dealing with anti-competitive or unfair conduct.

ARA Proposal 1 – Appropriate national body to oversee tenancy issues

The ARA proposes that a scheme similar to that operating in Victoria should be introduced for all of Australia's smaller retailers alongside a mandatory retail tenancy leases code of conduct.

Alongside the Retail Leases Act 2003 Victoria, small retailers are supported by a Small Business Commissioner established under the Small Business Commissioner Act 2003 in Victoria.

The Commissioner has a number of powers and responsibilities under the Retail Leases Act 2003 Victoria, which include providing mediation, commencing proceedings for offences against the Retail Leases Act and providing advice and assistance on retail tenancy matters.

To ensure a mandatory national code of conduct is effective, a similar service needs to be available for Australian smaller retailers, whereby investigative and mediation powers relating to tenancy issues are held by an appropriate national body.

ARA Proposal 2 – Collective bargaining for small retail tenants

In line with the recommendations made in the Trade Practices Act Review (April 2003), small retailers should be able to collectively bargain with shopping centre management/ownership on tenancy issues.

The ARA, and other groups of retail tenants, should be granted authorisation to negotiate on behalf of smaller retailers.

Such an arrangement would be in line with authorisations granted to a number of other industries that are able to handle price negotiations on behalf of their members.

The SCCA's 17 members (and particularly their six most dominant members) operate across State borders and can exploit inconsistencies in legal requirements.

Small businesses must be able to collectively negotiate across State borders if they are to consult more fairly with shopping centres.

Tenancy issues are often worth $5,000 to $15,000 for individual smaller retailers, but could grow to $5 million to $15 million if considered collectively across State borders. The ability to negotiate collectively provides small businesses with a fairer level of protection against the sophistication and huge resources of prime shopping centres.

6. RECOMMENDATIONS

To enable the Act to protect small to medium retailers and facilitate a fair market, the 'effects test' should not be applied; the definition of unfair conduct should be applied to 51AC as recommended in the Reid Report; a mandatory industry code of conduct for tenancy should be established; a body with investigative and mediation powers should be accessible to all Australian small to medium retailers to ensure a mandatory tenancy code is effective; and collective bargaining should be facilitated for small retailers negotiating tenancy issues with shopping centre management/ownership.

The favourable resolution of these issues in the Act is crucial to counteract the anti-competitive conditions smaller retail tenants face in occupying shopping centre space.

The ARA would welcome the opportunity of appearing before the Committee to put forward evidence to support this submission.