

Chapter 2

The bill and the determinants of 'predatory pricing'

2.1 Predatory pricing occurs where a firm deliberately sells at unsustainably low prices in an effort to cost their competitors out of the market, before raising their prices later on. Senator Fielding explained in the Second Reading Speech of the Trade Practices Amendment (Predatory Pricing) Bill 2007 that the practice of predatory pricing not only affects small businesses, but also Australian families through higher prices in the long term. He highlighted the domination of Coles and Woolworths in supermarkets and petrol retail, and their 'strong presence' in the non-prescription medicine and healthcare and toiletries market. These companies' profits increased by 'up to five per cent' last year, while food prices in Australia are rising 'at double the inflation rate'. Senator Fielding deduced that there has been 'a growing lack of competition in these markets'.¹

2.2 Currently, the courts may prosecute a company for predatory pricing under Part IV, section 46 of the *Trade Practices Act 1974* (TPA) relating to 'misuse of market power'. Subsection 46(1) states that 'a corporation that has a substantial degree of power in a market shall not take advantage of that power for the purpose of eliminating or substantially damaging a competitor'.² However, the section contains no explicit reference to 'predatory pricing'.

2.3 The bill seeks to insert a new section 46AA, which states that 'a corporation must not engage in predatory pricing' in the 'market for groceries', the 'market for the sale of fuel' and the 'market for pharmaceutical products'. It would establish several factors than a court may have regard to in considering whether a corporation has engaged in predatory pricing. These include: goods that are priced 'less than their cost'; the prices offered by competitors; the period of time for which the good is offered at an 'unreasonably low price'; whether the corporation is selling the good at higher prices in other markets; and the extent of competition in the market.³

2.4 On two counts, the bill establishes a lower threshold for the courts to make a finding of predatory pricing under section 46. First, the bill would extend the current threshold test of corporations with 'a substantial degree of power in a market' to include corporations with 'substantial financial power in a market'. Second, the bill seeks to enable the courts to find that a corporation has engaged in predatory pricing 'even where the corporation has no intention of recouping the costs of its predatory

1 Senator Steve Fielding, Second Reading Speech, *Senate Hansard*, 18 June 2007, pp 49–50.

2 *Trade Practices Act 1974*

3 Trade Practices Amendment (Predatory Pricing) Bill 2007

conduct'.⁴ The following section examines some important developments in the consideration of these threshold issues of 'financial power' and recoupment.

The Boral case, the Senate Economics Committee report and 'recoupment'

2.5 In February 2003, the High Court delivered its finding on the *Boral Besser Masonry v ACCC* case.⁵ The ACCC claimed that Boral was guilty of predatory pricing. It argued that one of Boral's competitors had left the market as a result. The High Court disagreed, noting that Boral did not have the market power to recoup the losses it sustained when it dropped its prices. Justices Gleeson and Callinan found that this capacity was not 'legally essential' to a finding of predatory pricing.⁶ This was the first opportunity for the High Court to consider the issue of predatory pricing under section 46.

2.6 In April 2003, the Review of the *Competition Provisions of the Trade Practices Act* ('the Dawson Report') inquired into, among other matters, the misuse of market power provisions in section 46 of the Act. The ACCC highlighted the difficulty of demonstrating a company's anti-competitive purpose, and proposed that the section take into account the anti-competitive effect of company behaviour.⁷ However, the Dawson Report argued against amending section 46. It noted the High Court's decision in the *Boral* case and recommended that interpretation remain a matter for the High Court. The government agreed, acknowledging the 'extensive consideration' given to the section in past reviews.⁸

2.7 In March 2004, the Senate Economics References Committee reported on the effectiveness of the *Trade Practices Act 1974*. The report recognised that one factor that may indicate predatory pricing is if the corporation plans to recoup its losses. However, there was disagreement in the evidence as to whether a corporation needs to be able to recoup its losses for a court to find it guilty of predatory pricing. The committee concluded:

...while evidence of a corporation's intention to recoup losses may well contribute to the proof of an allegation of predatory pricing, there is nothing in s.46 which makes recoupment an element necessary to prove predatory pricing. The Committee considers that the Act could be improved by stating

4 Trade Practices Amendment (Predatory Pricing) Bill 2007

5 [2003] HCA 5

6 *Boral* para 130 per Gleeson CJ and Callinan J.

7 Australian Competition and Consumer Commission, 'Dawson Report—Preliminary response: criminal sanctions major step forward for competition policy', Press Release, no. 74, 16 April 2003, <http://www.accc.gov.au/content/index.phtml/itemId/347733> (accessed 10 July 2007).

8 The Hon. Peter Costello, 'Commonwealth Government response to the review of the competition provisions of the Trade Practices Act 1974', Commonwealth of Australia, <http://www.treasurer.gov.au/tsr/content/publications/TPAResponse.asp> (accessed 10 July 2007).

that recoupment is a factor which the courts may examine when considering allegations of predatory pricing.⁹

2.8 However, the committee argued that the absence of an intention to recoup losses should not invalidate an allegation of predatory pricing. In other words, the issue of recoupment should not constitute a threshold for 'misuse of market power' in a predatory pricing case. The committee recommended an amendment to the TPA stating that:

where the form of proscribed behaviour alleged under s.46(1) is predatory pricing, it is not necessary to demonstrate a capacity to subsequently recoup the losses experienced as a result of that predatory pricing strategy.¹⁰

2.9 The Trade Practices Legislation Amendment Bill (No. 1) 2007 is the government's legislative response to the March 2004 report. It does not propose that the courts may consider recoupment as an issue in a predatory pricing case, nor does it state any limitation on the courts in the absence of a recoupment strategy. The government bill therefore enables recoupment as a factor that the court can consider in determining whether below cost prices are indicative of a misuse of market power.¹¹ Senator Fielding's bill states that recoupment is not essential to prove predatory pricing—which reflects the current law.

The Senate Economics Committee report and the issue of 'financial power'

2.10 Another key issue raised in the March 2004 Senate Economics Committee's report relates to the section 46(1) threshold of a 'substantial degree of power in a market'. The committee received a proposal from the Law Council of Australia to lower the threshold by including reference to 'a corporation with substantial financial power'. This recognised that firms with financial power—but without market power—can engage in unilateral predatory pricing. Importantly, both the Law Council and the Business Council of Australia acknowledged in their evidence to the committee that there may be definitional difficulties with the term 'financial power'.¹²

2.11 The ACCC argued in its submission to the Senate Economics Committee that 'financial power' should not be part of the section 46(1) threshold, but one of the factors contributing to a determination of 'substantial power in the market'. The High Court, in its 2003 ruling in the *Rural Press* case, had expressly disagreed that financial

9 Senate Economics References Committee, *The effectiveness of the Trade Practices Act in protecting small business*, p. xiii.

10 Senate Economics References Committee, *The effectiveness of the Trade Practices Act in protecting small business*, p. 19, recommendation 3.

11 See Allens Arthur Robinson, 'Amendments to Trade Practices Act 1974 (Cth) to protect small business', *Focus*, June 2007, p. 2.

12 Senate Economics References Committee, *The effectiveness of the Trade Practices Act in protecting small business*, pp 20–21.

power was a component of market power. However, the committee agreed with the ACCC and recommended that section 46 of the Act be amended to state that:

in determining whether or not a corporation has a substantial degree of power in the market for the purpose of section 46(1), the court may have regard to whether the corporation has substantial market power.¹³

2.12 On the issue of 'financial power', therefore, the Trade Practices Amendment (Predatory Pricing) Bill 2007 goes beyond the Senate Economics Committee's March 2004 recommendation. The government did not accept the committee's recommendation on this matter and the Trade Practices Legislation Amendment Bill (No. 1) 2007 contains no reference to the term 'financial power'.

13 Senate Economics References Committee, *The effectiveness of the Trade Practices Act in protecting small business*, p. 23.