

Submission to the Inquiry into Provisions of the Trade Practices Legislation Amendment Bill (No. 1) 2007 and Trade Practices Amendment (Predatory Pricing) Bill 2007

1. Executive Summary

Woolworths is pleased to provide this Submission to the Senate Standing Committee on Economics in respect of the provisions of the *Trade Practices Legislation Amendment Bill (No.1) 2007* and the *Trade Practices Amendment (Predatory Pricing) Bill 2007*.

Woolworths submits that any review of the effectiveness of the *Trade Practices Act 1974* (Cth) (TPA) and, in particular, of any proposed amendments to section 46, must take account of the underlying purposes of the TPA and the highly competitive retail food market in Australia.

Woolworths fully supports an effective section 46 of the TPA and the need for it to encourage efficiency and fairness in the interests of a strong and competitive market economy and for the benefit of all Australian consumers.

It is critical that any legislative changes to the TPA support its underlying purpose by promoting consumer choice and competitive equality to meet consumer demands, unhindered by inadvertent distortion to the operation of healthy and competitive market forces or measures which operate to protect sections of the market from these forces or which reward inefficient or poor business practices or uncompetitive conduct.

2. Trade Practices Legislation Amendment Bill (No. 1) 2007

General

Woolworths has no major objections to the *Trade Practices Legislation Amendment Bill (1) 2007* and believes that it is useful in its objective of clarifying principles which the Australian Courts have, in general terms, considered and applied.

Woolworths believes that in this Bill, the Government is simply including a list of matters a Court can take into account when determining:

- (a) whether a company has substantial market power; and

- (b) if a company has contravened section 46(1) by engaging in "predatory pricing".

These changes clarify what Woolworths understands to be the existing Court's power to take such matters into consideration.

Section 46(4A) – “ Predatory Pricing “

Woolworths' support of the Government Bill to clarify section 46 in respect of so called "predatory pricing", is qualified by the need to ensure the preservation of the key competition principles in the operation of the TPA amendments.

"Predatory pricing" is normally understood as a strategy whereby a business with a substantial degree of power in a market uses that power for an anti-competitive purpose by, for example, selling its products, over a considerable period, below a measure of cost (commonly, below average net variable or marginal cost), in order to drive a competitor(s) out of the market or to prevent or deter them from being or remaining competitive. Generally, the business must have had some prospect of recouping its losses from below cost pricing, by being able later (once its competitors have been driven out of the market) to raise its prices above the competitive level.

It is necessary, however, to appreciate that, with the benefits of both volume based, operational and technological efficiencies, some businesses will have a lower net variable cost than their competitors. It is, therefore, not "predatory pricing" (nor should section 46(4A) be construed) for a company to sell at prices which reflect their lower cost structure.

Nor is it considered "predatory" for any competitor (no matter what their respective size) to reduce their prices to match the prices of another competitor, whether or not all of the competitors in that market do so. So long as competitors with substantial market power are not acting for a purpose prohibited by section 46, no sanction should apply to prohibit such competitors responding to other competitors' pricing.

Further, the fact that, in some locations, a business reduces its prices to meet localised competition, but does not reduce the prices of those products in its other locations, where the same level of competition is not encountered, is not regarded as contrary to the TPA. Localised 'hot spots' of competition do and will always occur, particularly in retail markets, for many reasons.

Woolworths' pricing policy in its supermarkets is to sell competitively, so that our prices are determined by the market and our ability to reduce our costs of operating through what has been a significant investment of over \$5.5 billion in the past 5 years, in its efficiency enhancing technology in supply chain, logistics and store operations. These lower costs, have meant lower prices to our customers as well as providing our shareholders with an adequate return on their investment.

Also, as so called "predatory pricing" can be difficult to distinguish from strong and often vigorous competition, particularly in the Australian retail food industry, legislators and Courts need to be alert to ensuring that these amendments are not used to protect competitors from such price competition, on the basis that they are unable to compete as successfully as their rivals.

In relation to the proposed section 46(4A), Woolworths considers that the following issues should be considered by courts in interpreting its application:

- (a) the requirement of a "*sustained period*" must permit normal competitive activity including discounting, clearance sales and other stock clearance activities which is normal commercial behaviour and which is pro-consumer;

- (b) the requirement of "relevant cost" must permit businesses to strive to achieve operational and other efficiencies, resulting in lower costs, without being penalised by competitors who choose not to be as efficient or to operate at a competitive cost level; and
- (c) the requirement to demonstrate that normal competitive behaviour, unrelated to targeted anti-competitive conduct, should not be prohibited, in the interests of consumers.

Importantly, therefore, Woolworths believes that there should not be anything in any proposed amendments to section 46 of the TPA which prevents open and vigorous competitive behaviour for the benefit of the consumer.

Woolworths does not seek any further amendments to section 46 in relation to predatory pricing.

3. Trade Practices Amendment (Predatory Pricing) Bill 2007

Senator Fielding's proposed amendments

The Family First proposals are quite unclear in their scope and cut across the fundamental legislative proposition that the TPA should be of general application across all sectors of the Australian economy, and not be confined to certain sectors. Under these Amendments, Australian families and consumers would suffer as a result through higher prices and less attractive service levels as they protect some companies from being eliminated in a market even if the company is inefficient or offers poor service.

The amendments also have the potential to constrain competitive pricing by a wide range of businesses, including small operators.

The *Trade Practices Amendment (Predatory Pricing) Bill 2007* would be very damaging if enacted. The Bill would introduce an effect "*on competition*" test and an effect of "*eliminating competitors*" standard as a result of charging "*unreasonably low prices*", a concept which is undefined and unknown to the law or any regulator.

Compliance would be impossible and the result would be to discourage or prohibit many worthwhile and competitive practices which are to the benefit of the economy and consumers. The Bill would protect companies from being eliminated in a market, even if the company is inefficient or offers poor service. Consumers in the market should be able to decide who they wish to shop with, not the law.

Senator Fielding's proposed Amendments misunderstand what market power is about when it catches a company that possesses "*substantial financial power*". Market power, fundamentally, is the capacity to act free from the constraints of competition. It is well established that financial power does not equate to market power.

In addition, Senator Fielding's proposed amendments to the TPA are sector specific, which does not accord with the TPA being designed to be of general application across the economy. The suggestion of introducing special provisions for groceries, fuel and pharmacy markets is misconceived and there is no explanation as to why other less competitive sectors are not included.

There is no concept known in law or economics of selling something at "*an unreasonably low price*" and the Bill does not offer guidance for companies to comply with such a law. This Bill could make illegal a company's strategy to offer the "*lowest*" prices with a guarantee of beating their rivals.

CONCLUSION

Woolworths emphasises that there should not be any changes to section 46 of the TPA which prevent open and vigorous competitive behaviour for the benefit of consumers, since ultimately it is consumers' interests that the TPA is intended to preserve, rather than protecting one or other sections of the retail industry.

Moreover those proposals from Senator Fielding would render illegal far too many legitimate actions by Australian businesses, including low priced initiatives merely because they might have an adverse effect on a particular weak or inefficient competitor.

Dated : 9 July, 2007