The Senate Standing Committee on Economics

Inquiry into:

- **Provisions of the Trade Practices Legislation Amendment Bill (No.1) 2007, and**
- **Trade Practices Amendment (Predatory Pricing) Bill 2007**

National Farmers' Federation Submission

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1.0 Introduction

The National Farmers' Federation (NFF) welcomes the opportunity to make a submission to the Senate Standing Committee on Economics on its inquiry into:

- *Provisions of the Trade Practices Legislation Amendment Bill (No.1) 2007,* and
- *Trade Practices Amendment (Predatory Pricing) Bill 2007*

The NFF is the peak body representing Australian farmers at a national level.

The markets that farmers sell to are often concentrated, so that buyers can exercise market power by driving prices down or placing onerous contract requirements on farmers. The *Trade Practices Act 1974* (TPA) and the Australian Competition and Consumer Commission (ACCC) play a vital role in restraining the ability of firms to abuse their market power.[1]

To this end, the NFF has welcomed efforts to tighten Section 46 and 51AC of the TPA with a view to addressing some of the competition and contractual issues arising from market power imbalances. However, the NFF also recognizes that efficient and effective markets must also be allowed to operate without unnecessary constraints. Along these lines we believe a balance must be developed to ensure a clear distinction is made between the *misuse* of market power and the *use* of market power. As Graeme Samuel, ACCC Chairman recently stated:

> *"The Trade Practices Act (the Act) is not designed to protect small business from the rigours of normal, tough, competitive business. What it is designed to do is protect small business from unconscionable, harsh and oppressive conduct or misuse of power by big business."* [2]

The NFF is therefore concerned that proposals, such as those to introduce an effects test, could unintentionally find farmers in breach of section 46 simply by going about their business in a competitive manner.

2.0 Section 46 - Misuse of market power

The NFF firmly supports changes to the Trade Practices Act (TPA) through *Provisions of the Trade Practices Legislation Amendment Bill (No.1) 2007* to strengthen the TPA's powers in the area of 'Misuse of Market Power' through section 46.

Australia's farmers are proud of their strong record of productivity growth and recognise that they need a strong, competitive environment throughout the supply chain to effectively compete on domestic and international markets.

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[1] Under the Wheat Marketing Act 1989, permit conduct that would normally be an offence under the Trade Practices Act is exempt for the exports of Australian wheat. Section 51(1) of the Trade Practices Act provides that such conduct may be permitted if it is specifically authorised under this Act.

[2] National Small Business Summit 3 July 2007 – Graeme Samuel

Small businesses must be able to secure a fairer operating environment and allow authorities to more effectively combat predatory pricing tactics, which undermine their viability. The NFF believes that strengthening the 'Misuse of Market Power' provisions will ensure our competitive edge is maintained through retaining choice in the areas so vital to the Australian farm sector – including fuel distribution, retailing and transport suppliers. To this end, it is vital that situations such as that highlighted by the Boral case are not allowed to occur into the future[3]. On this point the NFF supports broadening the definition of what constitutes market power, which has been a vital element of *Provisions of the Trade Practices Legislation Amendment Bill (No.1) 2007*.

2.1 Proposal for an "Effects Test"

Currently the ACCC is able to take action under the TPA for misuse of market power where the *purpose* of a company's behaviour is considered damaging to a competitor; that is, the company *intended* the behaviour to be damaging. The NFF notes recent calls for the introduction of an effects test in section 46 (as well as retaining the purpose test) so that the ACCC could take action where the *effect* of a company's behaviour was anti-competitive.

The NFF believes that section 46 should provide a powerful deterrent against the abuse of market, to protect farmers and small business. However, the NFF does not believe that introducing an effects test into section 46 will provide additional protection. The NFF has the following concerns with the proposal to introduce an effects test:

2.1.1 Normal competition can damage competitors

In the marketplace in which farmers operate, a considerable number of actions by a company could be taken to have the effect of "substantially damaging" a competitor. Merely reducing price can be seen as damaging to a competitor. The High Court has stated: "competition by its very nature is deliberate and ruthless. Competitors jockey for sale, the more effective competitors injuring the less effective by taking sales away. Competitors almost always try to 'injure' each other. This competition has never been a tort"[4]. Any business that goes bankrupt could argue that its competitors' conduct drove it out of business.

For example, when Virgin Airlines entered the Australian market there was significant price discounting in air travel with the effect being that Ansett ceased operation. Under an effects test, the ACCC could say that Virgin Airlines was acting anti-competitively and in breach of the TPA when Ansett's demise could be due to a number of factors including bad management and uncontrolled costs.

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[3] The High Court found that Boral Masonry Limited did not breach the misuse of market power provisions of the TPA based on a finding that Boral Masonry did not have substantial market power. While the High Court did not find that Boral Masonry had the necessary degree of market power to trigger the section, this finding was based on the widely defined market for walling and paving products generally as opposed to the market for concrete masonry products in Melbourne.

[4] Queensland Wire Industries Pty Ltd vs Broken Hill Pty Co Ltd (1989) 63 ALJR 181

Some of these actions actually improve competition in the long run. For example, cost reductions by one company leading to price reductions could hurt other companies in the market in the short-term, but increase pressure for industry-wide cost reductions that improve competition in the long-term. Therefore an effects test would create a great deal of uncertainty for many small businesses.

2.1.2 Small businesses can have market power

An effects test would mean that a corporation that has substantial market power would not be able to take advantage of that market power if it has the effect of damaging a competitor.

For example, a small farmer has sought to build a niche market through producing and marketing biodynamic beef. Strict quality assurance measures and improved technology have enabled this farmer to have substantial market power. As the major supplier of organic beef in the State, the farmer is able to secure a contract with the majority of butchers in the State to supply organic beef. Due to this contract, the butchers no longer purchase beef from two other suppliers of organic beef and both of these farmers go out of business. An effects test would mean that this farmer could be in breach of section 46 when the farmer was simply using long-term contracts to continue to expand and improve their product. Further, this farmer would need to constantly be mindful of actions that could affect other farmers. While the farmer could be confident about the reasons for engaging in a certain type of behaviour, the same confidence could not extend to the effect the behaviour would have on a competitor.

Further, many farmers sell through or to co-operatives or trading organisations which would have substantial market power. A reduction in the ability to actively compete by these players could adversely impact on the returns to farmers.

2.1.3 It is difficult to predict the effect of actions

It may be difficult for a business to predict the effect of its actions. For example, the conduct of a company could have the effect of preventing the entry, or causing the removal, of another business into a market, even though the company did not have this as a purpose when it was implementing its strategy. Other company activities could have had the effect of preventing entry of a second business, such as a downturn in the market. If that intervening event was not caused by the first company and was not foreseen at the time of implementing the company's strategy, it would be unfair for the ACCC to prosecute the company, because at the time of implementing its strategy, that effect was not contemplated.

2.1.4 Comparisons in Australian law and overseas

Various sections of Part IV have an effects test, except for section 46. However, there is an important difference between s46 and these other sections: the other sections have a test that prohibits actions that have the *effect* of causing a substantial lessening of *competition*, whereas s46 talks about conduct with the *purpose* of substantial damage to a *competitor*. In essence, the change in s46 from effects to purpose is balanced by a change from competition to competitor.

While a test of effect on competitors is proposed for s46, it has not been proposed for other sections in Part IV. Damage to a competitor would generally be easier to show than damage to

competition[5], while some conduct that damages a competitor could actually improve competition, as noted in 2.1.1.

While Part XIB of the TPA (specific to telecommunications) has an effects test, this rule is in place to address telecommunications-specific issues, is generally not relevant to other markets and appears unique to Australia[6]. The Government envisaged that these rules would only be transitional in nature and it was "intended that competition rules for telecommunications will eventually be aligned…with the general trade practices law"[7]. There is however an argument that the *process* applying to Part XIB is quicker and simpler and could be more widely applied in other sections of the TPA.

The Australian rules for misuse of market power are not comparable with those in the United States (US), European Union (EU) or Canada. In the US and EU, an effects test is not legislated and has only arisen through case law – in other words, policy makers have not explicitly made the decision to incorporate an effects test. Case law in the US indicates that intent (purpose) "may play an important role in divining the actual nature and effect of the alleged anticompetitive conduct"[8]. In the US and Canada, the definition of market power is based on market dominance, which is distinctly stronger than the Australian test of substantial market power. In Europe the rules are aimed largely or wholly at trade between EU countries and therefore are not comparable with rules for trade within a country. New Zealand has a similar test to the current Australian TPA[9].

2.1.5 An effects test could be used anti-competitively

Some businesses may take action under an effects test for tactical and anti-competitive reasons – in other words, in direct opposition to the intended reason for the legislative change. As noted above, it would simply be too easy to show an adverse effect on a competitor. While anyone can bring an action under section 46, not just the ACCC, this type of anti-competitive claim could be restricted if an effects test was limited to actions by the ACCC only. However, the NFF remains concerned that an effects test gives substantial additional powers to the ACCC thus increasing the risk of regulatory error[10].

2.1.6 Summary of NFF concerns with an effects test

Farmers have embraced technological advances in agriculture with enthusiasm and the uncertainty that an effects test would introduce into the market could reduce the incentive for farmers to continue to invest and explore more innovative ways of doing business.

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[5] Productivity Commission (2001), *Telecommunications Competition Regulation Report*, p179.
[6] Productivity Commission (2001), *Telecommunications Competition Regulation Report*, p165.
[7] Trade Practices Amendment (Telecommunications) Bill 1996 Explanatory Memorandum, p7.
[8] US v United States Gypsum Co 438 US 422 at 436, n 13 (1978)
[9] Productivity Commission (2001), *Telecommunications Competition Regulation Report*, p164.
[10] This includes taking action when it is not warranted, not taking action when it is warranted, and deterring firms from pro-competitive behaviour – see Productivity Commission, *Telecommunications Competition Regulation Report 2001*, p156.

The TPA is concerned with protecting competition and the NFF supports the promotion of open competition. However, an effects test may well be at the expense of competition. The NFF therefore does not support the proposals to introduce an effects test into the TPA.

3.0 Section 51AC – Unconscionable Conduct

The NFF welcomes efforts to widen the Unconscionable Conduct provisions within the TPA to send a strong message to large business that they cannot simply back-out of contractual obligations on a whim. The targeting of unfair unilateral variation clauses in particular will help to ensure reneging on contracts will come under heightened scrutiny.

Australian farmers have noted, and have become increasingly concerned about, players in the market trying to capitalise on the limited number of buyers within regional areas by including unfair clauses in their contracts with farmers. We need to see greater scrutiny on contract clauses allowing buyers to 'opt out' of their contractual obligations whenever they see fit, leaving farmers unjustly exposed.

Examples have been brought forward involving 'market disruption' contract clauses that unfairly and without reasonable notice, suspend the growers contracts. Other examples within the horticulture sector have involved clauses that require growers to agree to allow a trader acting as a merchant to unilaterally reject produce because of a change in market conditions after a merchant has taken delivery[11]. When such clauses are activated within a short timeframe of the harvest or in reference to perishable product, this can place the growers under considerable exposure, with few alternative buyers. The NFF refers to the Senate Rural and Regional Affairs and Transport References Committee report on *The operation of the wine-making industry* for more information on the impacts on agricultural businesses.[12]

The NFF recognizes that unilateral contract variation clauses will not be illegal in their own right under *Provisions of the Trade Practices Legislation Amendment Bill (No.1) 2007*. In isolation, each of these factors may not amount to unconscionable conduct. However, the proposed amendments do send a positive message allowing the courts to specifically consider unilateral contract variation clauses in determining whether the conduct is unconscionable. The NFF supports maintenance of the principle of 'freedom of contract' and believes that Government should be extremely cautious of interfering with this freedom by going further by outlawing unilateral contract variation clauses altogether.

The NFF also welcomes an increased transaction threshold from $3 million to $10 million as stipulated in the *Provisions of the Trade Practices Legislation Amendment Bill (No.1) 2007*. This recognizes that small businesses such as farmers often have high turnovers and low margins. In addition, as more rationalisation takes place within the agricultural processing sector (often the major customers for farmers), many farmers find themselves with an increasingly limited number of buyers of their produce within their region. Therefore, in a growing number of cases, farmers' complete turnover is being accounted for by their transactions with a single customer, increasing their potential exposure to the $3 million transaction threshold.

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[11] http://www.accc.gov.au/content/index.phtml/itemId/787979
[12] Senate Rural and Regional Affairs and Transport References Committee report on *The operation of the wine-making industry* October 2005

The NFF also recognises that industry itself has a clear role to play in mitigating situations that made lead to accusations of *misuse* of market power. A growing number of tools are available for small businesses to use in ensuring they obtain a fair deal. It is important that farmers are educated more effectively about the importance of the appropriate process of understanding, negotiating and protecting themselves when developing their contracts. We also hope that more farmers will utilize the Collective Bargaining Notification and Authorization processes at their disposal to help combat the market power imbalance issue. We hope that these will help to minimize occurrences of unconscionable action and relieve the need for involvement of the courts.

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