

Dissenting Report from Senator Xenophon

Introduction

1.1 The Trade Practices Amendment (Material Lessening of Competition – Richmond Amendment) Bill 2009 seeks to strengthen sections 50 (1) and 50 (2) of the *Trade Practices Act 1974* by tightening the test for proposed mergers or acquisitions, and to prevent ‘creeping acquisitions’.

1.2 The Bill was introduced in part in response to the case of small business owners, William and Samira Fares, who have owned and operated an independent United service station in the Adelaide suburb of West Richmond for the last twenty years.

1.3 In late 2009 the Fares were notified that supermarket giant, Woolworths, who currently shares 44 percent of the petrol market and 80 of the dry packaged goods market with its direct competitor, Coles, applied to lease the land adjacent to the Fares on Marion Road, and submitted plans for a service station to be built on this site.

1.4 The impact of this aggressive tactic, the Fares' believe, will result in them being priced out of business and forced to close.

"If a Woolworths site ends up being next door to us then I am pretty sure that within no time, three months, six months or whatever it might be, that our doors will close. That is what I believe because they can afford to go as low as they can."¹

1.5 The Trade Practices Amendment (Material Lessening of Competition – Richmond Amendment) Bill seeks to address instances such as these, where corporations who already hold a substantial share of a market would be prevented from acquiring shares or an asset (in this case, leasing land) that would have the effect of lessening competition in the market.

1.6 While the ACCC has an existing 'substantial lessening of competition' threshold which it has applied to merger and acquisition cases since 1993, under the current test and those put to the ACCC, around 97 percent of mergers and acquisitions are approved.

This leads some parties to argue that the test does not adequately protect small business operators from predatory acquisition strategies by big business.

¹ William Fares, Proof Committee Hansard, 09 April 2010, pg 2

Indeed, Woolworths, Coles and the major oil companies control 93 percent of the retail petrol market, leaving just 7 percent to be shared between independent operators.

1.7 All submissions and witnesses to the Inquiry agree that competition is vital to ensure a fair market, however the key focus has to be on the need for fair competition, not at the expense of small businesses that are not only crucial to Australia's economy as a whole, but which are essential to a competitive market so as to produce the best possible result for consumers.

The case study

1.8 William and Samira Fares have owned and operated the independent United service station on Marion Road in West Richmond for the last twenty years.

"It is a service station workshop ... We rely on the sales of petrol and what we do through the workshop to pay the rent, pay the workers and pay everything else."²

1.9 Both William's parents and Samira's parents owned service stations (in Victoria and in South Australia) and they both worked at their parents' businesses on weekends, in the same way their three children work with them today.

1.10 When the Fares bought the land, it was a closed site with the nearest service station located 1.5 kilometres away.

Senator XENOPHON—What sort of competition do you have in your area? In other words, how many other service stations are there within a small radius of your area?

Mr Fares—It is pretty fair competition, I believe. Each site is about 1.5 to two kilometres away. That was the understanding when you first purchase a service station when there was actual Fuel Board licensing where you could not reopen a service station or be within certain kilometres of another service station. That is the guarantee why we outlaid that sort of money.³

1.11 The concern of the Fares', and the foreseen risk to their business, is that Woolworths will be able to price its petrol and store products well below the Fares, thanks to its market power in these sectors.

In his statement tabled to the Committee, William Fares shared:

"My family and I rely on one income – selling fuel. Woolworths has many income streams – it could sell below cost for months in one retail space and not feel it because they can make up for it elsewhere. And while we do have loyal customers and the community knows us by name, if the service

² William Fares, Proof Committee Hansard, 09 April 2010, pg 2

³ William Fares, Proof Committee Hansard, 09 April 2010, pg 2

station next door is selling its fuel at 4 cents, 8 cents or 10 cents cheaper than us, then of course they're going to go there. And this is the problem. Woolworths is able to sell their fuel that low. Quite simply, the power that Woolworths has and the income it has will allow it to cut prices that I simply can't match."⁴

1.12 It is important to recognise that this case has the propensity to be replicated nationally.

Senator EGGLESTON—What do you see as the future of small family businesses like your own who are faced with competition from these companies like Woolworths who have such a large market share in Australia? What do you see as the future of small business?

Mr Fares—There will not be a future.⁵

Mr Fares also said in his statement:

"I understand Australia has around 1.5 million trading small to medium sized businesses. I am just one of them. But what's happening here could happen to any other small business owner, and that's a scary thought."⁶

The threat to competition

1.13 Under current laws, Woolworths can use its extensive market power to, firstly, buy fuel at lower than normal wholesale costs, and secondly offer fuel at prices which undercut the prices of independent petrol retailers like the Fares'.

Senator XENOPHON—Is it the case that as an independent operator sometimes the petrol that is being sold at Coles and Woolworths is actually lower than the wholesale price you can get it at. Is that your understanding?

Mr Fares—It is a fact. The fuel that they buy is way under. Every week we are actually losing money to compete when they drop down to that level. For instance, our buying price yesterday was \$1.22 and we were selling it at \$1.19, so we were losing 3c a litre just to compete because Woolworths was \$1.18. If you do not do that then no-one comes in, so there is a bit of competition when you look at it in that circumstance.⁷

1.14 Further, Woolworths could operate its service station at a loss for a period of time, knowing that once the Fares are out of business, they can once again raise prices.

As the Law Council of Australia pointed out in its submission to the Committee,

⁴ William Fares, Statement tabled to the Committee, 09 April 2010

⁵ William Fares, Proof Committee Hansard, 09 April 2010, pg 2

⁶ William Fares, Statement tabled to the Committee, 09 April 2010

⁷ William Fares, Proof Committee Hansard, 09 April 2010, pg 2

"[Woolworths]' motivation is undoubtedly to make money. It is very likely that they will see that by entering and cutting prices, they are going to eliminate some of the local people."⁸

1.15 The Retail Traders Association of Western Australia shared this concern in its submission to the Committee:

The Association is aware that small business has [also] expressed concern that acquiring corporations may engage in anti-competitive behaviours. Such behaviour could utilise market power to a level impossible to compete with, causing smaller competitors either to close or sell to the larger corporation. Larger corporations are often able to cross-subsidise and achieve far better pricing within a market through their volume purchasing.⁹

1.16 The State Retailers Association of South Australia argues that:

"... the over-riding problem really is that Woolworths and Coles now dominate to the point that no government is brave enough to say "enough is enough!" You're market share (80% +/-) has reached the point where the oligopoly so created is in fact anti-competitive, anti small business and not in the best interests of Australian consumers."¹⁰

1.17 And, as the National Association of Retail Grocers of Australia argues in its submission to the inquiry:

"The importance of national market concentration cannot be overstated, as the non-majors have to survive and compete in the remaining space. Any further shrinkage of that space has major ramifications for the independent sector at both wholesale and retail levels."¹¹

1.18 Furthermore, Associate Professor Frank Zumbo, competition law expert from the University of New South Wales, argues that:

"Risks to competition and consumers arise because mergers and acquisitions lead to a reduction in competitors and, in turn, lead to less competitive behaviour amongst the remaining players or to less incentive to do so or to innovate. This reduction in the intensity of competition is detrimental to consumers, as any "efficiencies" or to reduced costs achieved

⁸ Dr Phillip Williams – Law Council of Australia, Proof Committee Hansard, 09 April 2010, pg 16

⁹ Retail Traders Association of Western Australia, Submission 4, pg 1

¹⁰ State Retailers Association of South Australia, Submission 8, pg 1

¹¹ National Association of Retail Grocers of Australia, Submission 7, pg 3

by a merger are much less likely to be passed on to consumers and much more likely to be pocketed by the merged firm."¹²

The current test

1.19 The current substantial lessening of competition test under the Trade Practices Act does not appear to appropriately take into account the extensive market strength a corporation may hold, which enables it to dominate at a local market level, such as in the case of Woolworths.

1.20 Australia has some of the most highly concentrated markets in the world.¹³ Supermarket giants, Woolworths and Coles, currently share 44 percent of the petrol market and 80 of the dry packaged grocery goods market, nationally.

This market power by its sheer volume enables Woolworths and Coles to operate and target competitors on a local level.

1.21 In these cases, the ACCC applies the substantial lessening of competition test to determine if a proposed merger or acquisition will have the effect of lessening competition in a market.

However, it can be argued that, with around 97 percent of proposed mergers and acquisitions being approved, it would seem that the threshold included in the test is far too onerous and high.

1.22 While a number of submissions and witnesses to the inquiry highlighted that the substantial lessening of competition test applied in Australia is in line with international competition law, it is important that this is held in context.

Contrary to other nations, Australia does not have powers, such as divestiture powers, which balance out this test and ensure fair competition in markets.

"If we are going to talk about international comparisons, we are missing one very vital tool in the competition toolbox, and that is we do not have a general divestiture power."

...

"If we are going to talk about international comparisons, we need to be consistent. If the United States has a divestiture power we should have one, too. If the United Kingdom has a divestiture power, then we should have one, too."¹⁴

¹² Associate Professor Frank Zumbo, Submission 14, pg 2

¹³ Associate Professor Frank Zumbo, Submission 14, pg 4

¹⁴ Associate Professor Frank Zumbo, Proof Committee Hansard, pg 24

The case for replacing 'substantial' with 'material'

1.23 Under the proposed Richmond Amendment, a new test would be applied to prohibit any acquisition or merger that will have the effect, or is likely to have the effect, of 'materially' lessening competition in a market.

1.24 This would enable a more balanced test and a broader range of factors to be considered, such as local markets and national market power.

1.25 The material lessening of competition test would assess the reduction in consumer choice as a result of a merger or acquisition, whereas the substantial lessening of competition test effectively only focuses on pricing power.

1.26 Associate Professor Frank Zumbo states in his submission:

"A material lessening of competition test would focus attention on whether or not the merger or acquisition would lead to a reduction in the number of efficient competitors in the marketplace and whether such a reduction would reduce the diversity or range of goods or services available to consumers. A material lessening of competition would also look to see whether the merger or acquisition would allow or facilitate "price coordination" behaviour between the market players remaining following the merger or acquisition."¹⁵

Creeping acquisitions

1.27 Throughout this inquiry, creeping acquisitions was an issue keenly debated. This Amendment seeks to limit creeping acquisitions, where large corporations are currently able to acquire assets in a piecemeal manner.

1.28 The Law Council of Australia shares this concern in its submission.

...each individual acquisition may be unlikely to substantially lessen competition but there may nevertheless be a concern that, in aggregate, the combined effect of these acquisitions is to strengthen the acquirer's market position to the detriment of competition and consumers in the market.¹⁶

1.29 Indeed, while individually, these acquisitions may not be seen to substantially lessen competition, over time they may result in a larger market share and a reduction in competition.

1.30 In practice, a corporation under existing laws would ordinarily need to already hold substantial market power before it would be prevented from acquiring assets that, or would be likely to, further enhance that corporation's market power.

¹⁵ Associate Professor Frank Zumbo, Submission 14, pg 9

¹⁶ Law Council of Australia, Submission 2, pg 4

This effectively means that a corporation must have a monopoly, or near monopoly, of a market before it is prohibited under existing laws.

The most recent Federal Government proposals on creeping acquisitions will not change this and consequently, the gaps in the existing law will remain. The Richmond Amendment proposes to fill those gaps.

Conclusion

1.31 There is no question that competition is important and indeed crucial, and this sentiment is recognised by William Fares.

Mr Fares—Competition is good for any business. It depends on what the competition is. When you have equal competition with someone at your level then it is good for everyone, but when we are talking about Woolworths or a big chain like that then that is not competition; it is really them against one person. It is not fair competition, not at all.¹⁷

1.32 The State Retailers Association of South Australia points out that this Amendment indicates a broader issue.

While the amendment focuses on creeping acquisitions, this is but one part of a much bigger problem – market domination to the point where, in order to achieve the growth expected of them, Woolworths and Coles must, in fact, destroy the investment of others.¹⁸

During the hearing, Mr John Brownsea, Executive Director of the State Retailers Association of South Australia, further argued:

Mr Brownsea—In the case of Woolworths, clearly the problem is their undoubted ability to be an absolute predator. I do not think the real problem is their coming next door and selling petrol, because the service station next door could probably live with that; but the rest of it they cannot live with. That is the problem. They front a fairly small community in behind them because the airport is further in and that is the end of their drawing area. It is a busy road that they are on and that limits their ability. They have been lucky up until now perhaps that competition in terms of petrol sales is a fair way away from them; and that is another reason probably for their survival. But they are one of an absolute declining number of privately owned service stations. And this is a planned process; there is no doubt about it. There are those who want to see these private individuals wiped out because, once you have the market, you have the ability to change the pricing structure. People will have to pay because they will have no choice, in actual fact.¹⁹

¹⁷ William Fares, Proof Committee Hansard, 09 April 2010, pg 3

¹⁸ State Retailers Association of South Australia, Submission 8, pg 2

¹⁹ Mr John Brownsea – State Retailers Association of South Australia, Proof Committee Hansard, 09 April 2010, pg 45

1.33 The Trade Practices Amendment (Material Lessening of Competition – Richmond Amendment) Bill 2009 seeks to 'level the playing field', and give small businesses, like the independent petrol station owned by the Fares, the protection they need from aggressive and arguably anti-competitive strategies of larger and more powerful corporations such as Woolworths.

1.34 Small businesses are essential to the competitive process and are critical to keeping big business honest, so that consumers get the best possible deal.

Recommendation 1

1.35 That the Bill be passed following minor amendments developed in consultation with stakeholders, in relation to concerns raised during the inquiry.

Nick Xenophon

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