The Senate

Standing Committee on Economics

Trade Practices Legislation Amendment Bill 2008 [Provisions]

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Chapter 1

Introduction

1.1 The Trade Practices Amendment Bill 2008 amends sections 46, 51 and 155 of the *Trade Practices Act 1974* (TPA). The provisions include clarifying a number of terms relating to predatory pricing and unconscionable conduct. The Minister for Competition Policy and Consumer Affairs, the Hon. Chris Bowen, has described the bill as 'the biggest TPA reform in over 20 years'.[1]

1.2 The bill was introduced into the Parliament on 26 June 2008, and the same day the Senate referred the bill to the Senate Standing Committee on Economics for report by 27 August 2008.

Conduct of the inquiry

1.3 The committee advertised the inquiry in the national press and invited written submissions by 21 July 2008. The committee received eight submissions to its inquiry which are listed at Appendix 1. They are available on the Committee's website; http://www.aph.gov.au/Senate/committee/economics_ctte/tpa_08/submissions/sublist.htm.

1.4 The committee held a public hearing on the bill in Melbourne on 5 August, in conjunction with its hearing on the Trade Practices (Creeping Acquisitions) Amendment Bill 2008. The witnesses are listed in Appendix 2.

1.5 The Committee thanks those who participated in the inquiry.

Structure of the report

1.6 The changes to section 46 relating to predatory pricing are discussed in Chapter 2. Other provisions are discussed in Chapter 3. .

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1 The Hon. Chris Bowen, 'The Government introduces into Parliament the biggest reform to the Trade Practices Act in over 20 years', *Press Release*, 26 June 2008.

Chapter 2

Predatory pricing

2.1 Predatory pricing refers to a firm deliberately selling at unsustainably low prices in an attempt to drive a competitor out of the market. Charging consistently lower prices than rivals because of lower costs from greater efficiency is ***not*** predatory pricing. Nor is a temporary cut in prices to clear excess stock.

2.2 Predatory pricing is addressed by section 46 of the TPA, although the term is not actually used in the legislation. The bill addresses three significant 'threshold tests' to which the courts may have regard in assessing whether a firm has engaged in predatory pricing. The first concerns the firm's degree of power in a market; the second relates to the meaning of the term 'take advantage'; and the third refers to a firm's capacity to recoup the losses it incurs from below-cost pricing. All these issues were dealt with in the March 2004 Senate Economics Committee inquiry into the effectiveness of the Trade Practices Act.[1] The bill is a response to some of the report's key recommendations.[2]

Predatory pricing and 'power in the market'

Background

2.3 In August 2007, the Senate Economics Committee recommended passing an amendment to the TPA on predatory pricing. New subsection 46(4A) allowed the courts to take into account 'a sustained period' of selling goods and services at a price 'less than the relevant cost to the corporation of supplying such goods and services' and the corporation's reasons for engaging in this practice. Section 46(4A) was passed into law.

2.4 In a dissenting report to the August 2007 Senate inquiry, Senator Barnaby Joyce proposed bolstering the Act's provisions on predatory pricing through the following amendment:

> A company that has substantial market share or substantial financial power must not supply or offer to supply goods or services for a sustained period at a price that is less than the relevant cost to the company of supplying such goods or services for the purpose of:
>
> (a) eliminating or substantially damaging a competitor of the company in that or any other market;

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1 The 2004 inquiry was chaired by a Labor Senator. The then Government Senators made a dissenting report.

2 The Explanatory Memorandum of the bill makes several references to the 2004 report.

> (b) preventing the entry of a person into that or any other market; or
>
> (c) deterring or preventing a person from engaging in competitive conduct in that or any other market.

2.5 This was known as the Birdsville amendment.[3] On 25 September 2007, this amendment (minus the reference to 'financial power') became law under new subsection 46(1AA) of the TPA.

2.6 While many commentators supported the Birdsville Amendment, there was concern in some quarters, both before and after it was passed, that the reference to 'relevant cost' was a significant departure to the familiar legal definition of 'below cost' pricing. It was also noted that the Birdsville Amendment was 'passed through in two weeks without public consultation'.[4]

'Market power' versus 'market share'

2.7 This bill amends subsection 46(1AA) to align it with the prohibition on the misuse of market power in subsection 46(1).[5] The reference in the Birdsville amendment (46(1AA) to 'a substantial share of a market' is changed to 'substantial degree of power in a market', consistent with subsection 46(1).

2.8 The Government argues that the present reference to 'share of a market' in section 46(1AA) 'has given rise to uncertainty and may reduce pro-competitive price competition in markets'.[6] The Minister explained:

> I have reached the view that having separate predatory pricing offences is, on balance a good thing…However, having strengthened the substantial degree of market power test, there is no need, in my view, to have a separate 'market share' test for predatory pricing. Having a new market share test creates considerable uncertainty in the market as to how it will be interpreted by the courts...Accordingly, we will legislate for the test of breaches of 46AA to be 'a substantial degree of market power'.[7]

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3 The final draft of the amendment was sent by Senator Joyce from the hotel in the western Queensland town of Birdsville. For a good overview of the Birdsville Amendment, see Freehills, 'The Birdsville Amendment: Getting back on track', November 2008, http://www.freehills.com.au/publications/publications_7040.asp

4 Michael Hodge, *Submission 4*, p. 4. Matthew Drummond, 'New Law may turn predators into prey', *Australian Financial Review*, 28 September 2007.

5 The term 'substantial market power' replaced 'dominance' in 1986, with the intention of lowering the threshold; Associate Professor Frank Zumbo, *Proof Committee Hansard*, 5 August 2008, p. 5.

6 The Hon. Chris Bowen, 'Second Reading Speech', *House of Representatives Hansard*, 26 June 2008.

7 The Hon. Chris Bowen, 'Reviewing the federal government's amendments to the Trade Practices Act 1974', *Keynote address to the 4th Annual Trade Practices and Corporate Compliance Summit*, The Grace Hotel, Sydney, 28 April 2008.

2.9 Conceptually, 'market power' is more relevant to the ability to reduce competition in a market through engaging in predatory pricing.[8] It is possible in a readily 'contestable' market for a firm to have a large market share but little market power. The argument is that if a firm sets prices much above costs, it will quickly lead to new firms entering the industry and competing away the excess profits.[9]

2.10 A firm may also have market power and the ability to engage in predatory pricing despite a modest market share if it has 'deep pockets'. A large firm may have only recently entered a market and have a small market share but be able to cover losses in the new market easily from its profits elsewhere until it builds up a large share in the new market. The original Birdsville Amendment reflected this idea in its reference to 'financial power' but this was not incorporated in the legislated version.[10]

2.11 However, there are two reasons why despite this conceptual preference, it may be better to use a 'market share' test as an approximation to 'market power'. Firstly, it is much easier to measure 'market share' and therefore assess whether it is 'substantial'. This argument was put by the Fair Trading Coalition, an informal grouping of small business organisations; the National Association of Retail Grocers of Australia; and the Consumer Action Legal Centre.[11] It is also 'a better understood concept'.[12] It may also be a good proxy; 'if an entity does not have substantial market share, it is unlikely to have substantial market power'.[13]

2.12 Secondly, the High Court has adopted an interpretation of 'market power' (in the *Boral* case in 2003). It 'basically defined it as the ability to raise prices without losing business'.[14] Even monopolies face a downward-sloping demand curve for almost all products.[15] Monopolies therefore charge a higher price than would prevail

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8 This point is made by Ms Nicole Rich, Consumer Action Law Centre, *Proof Committee Hansard*, 5 August 2008, p. 42.

9 This argument was put by Mr Graham Maher, *Proof Committee Hansard*, 5 August 2008, p. 25 and Mr Ian Stewart, *Proof Committee Hansard*, 5 August 2008, p. 29.

10 Associate Professor Frank Zumbo, *Proof Committee Hansard*, 5 August 2008, p. 9.

11 Fair Trading Coalition, *Submission 3*; Mr Kenneth Henrick, NARGA, *Proof Committee Hansard*, 5 August 2008, p. 35; Ms Nicole Rich, Consumer Action Law Centre, *Proof Committee Hansard*, 5 August 2008, p. 43.

12 Associate Professor Frank Zumbo, *Proof Committee Hansard*, 5 August 2008, p. 3.

13 Associate Professor Frank Zumbo, *Proof Committee Hansard*, 5 August 2008, p. 3. He also mentioned that 'Canada recently issued some predatory-pricing guidelines whereby they see a threshold of 35 per cent or more as a central element of determining market power'; pp 5-6.

14 Associate Professor Frank Zumbo, *Proof Committee Hansard*, 5 August 2008, p. 2.

15 Perhaps a monopoly supplier of insulin would come close to being an exception.

in a competitive market.[16] They do not charge an infinite price. As a result of this interpretation, the ACCC has not taken any section 46 cases.[17]

2.13 The use of *market share* is the 'door that gets you into the court'.[18] It may be a somewhat wider door than *market power*. (Indeed the High Court's definition may have made *market power* a locked door, or perhaps a cat flap.) But it is only the door. Once inside the court, the case must be made that the motivation for pricing below cost is to reduce competition, rather than clearing excess stock or some other reason.

2.14 Proving predatory pricing is still a very difficult thing for a small business to do. As NARGA notes, one difficulty is assessing the costs of the alleged predator:

> whenever we have talked predatory pricing with the ACCC they have continually said to us: 'No, you don't even know whether it's predatory or not because you don't know what costs your competitors have. You may think the price is below their cost, but we don't think that is the case.'[19]

> it is impossible for a small business to know what a large business's relevant costs are. The only people with the power to investigate are the ACCC, and they do not. [20]

2.15 The desire to align the terms in different sections of part IV of the Act could be met by either changing section 46(1AA) to refer to 'market power' or changing other parts of section 46 to refer to 'market share'.[21]

2.16 An alternative means of getting around the interpretation of 'market power' by the High Court would be to embed a clear definition in the legislation.

2.17 The Law Council of Australia argues that section 46(1AA) should simply be repealed, on the grounds that sections 46(1) and 46(3) provide adequate statutory guidance for the courts to address anti-competitive pricing behaviour. In evidence to the committee, Mr Ian Stewart argued that there is now 'quite a developed body of law' in relation to section 46(1) and that at the High Court level, at least, the facts and the law have been correct.[22] Mr Stewart emphasised the distinction between below cost pricing which does not reflect the forces of market supply and demand, and the situation where a firm is setting prices below its costs because it is responding to the

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16 This proposition is demonstrated in any standard economics textbook. For example, see Paul Samuelson and William Nordhaus, *Economics*, p. 198.

17 Associate Professor Frank Zumbo, *Proof Committee Hansard*, 5 August 2008, p. 2.

18 Senator Barnaby Joyce, *Proof Committee Hansard*, 5 August 2008, many instances.

19 Mr van Rijswijk, National Association of Retail Grocers of Australia, *Proof Committee Hansard*, 5 August 2008, p. 35.

20 Mr Henrick, NARGA, *Proof Committee Hansard*, 5 August 2008, p. 36.

21 Associate Professor Frank Zumbo, *Proof Committee Hansard*, 5 August 2008, p. 6.

22 Mr Ian Stewart, *Proof Committee Hansard*, 5 August 2008, p. 28.

market. He argued that the *Boral* case—in which he acted as junior counsel for Boral—was an example of the latter situation.

2.18 The Law Council argued in its submission that section 46(1AA) fails to acknowledge that all firms cut prices to win sales from their competitors: 'the ability to cut prices…does not of itself indicate market power'. It gives the example of a highly competitive market suffering from excess industry capacity, with that excess supply causing market prices to fall below competitors' costs. It adds: 'Far from reflecting the existence or use of substantial market power, the below cost pricing may merely signify that no competitor has the ability to raise its prices above its costs'.[23] However, it is hard to see how this situation could lead to below-cost pricing being sustained for an extended period, rather than firms leaving the industry, and so it would not in practice form the basis for an action on the grounds of predatory pricing.

2.19 The Law Council's submission noted that a corporation with substantial market power may need to price below its costs to meet the price of a competitor with a lower cost structure.[24] Mr Stewart told the committee:

> All firms cut their prices in order to win business from their competitors... Say you have two firms competing in a market, one of which has a lower cost structure than the other—for example, it might have more modern equipment and its cost of production might be lower than the other. In order for the second firm, with a higher cost structure, to meet the price of the first firm it might have to set its prices below its costs.[25]

2.20 It is not clear why any firm, let alone one with substantial market power, would 'need' or 'have to' make ongoing losses for an extended period rather than just leaving the market. Most cases where a firm chooses to continue operating at a loss for reasons other than a predatory pricing strategy are unlikely to lead to court cases. If it is running at a loss while it installs new equipment or restructures, this is likely to be only for a short period. If it is tolerating the loss because it believes the competitor cannot sustain the lower price, then it is more likely a victim than a perpetrator of predatory pricing, and it is unlikely to be taken to court. If it is just postponing a decision to leave a market in a vague hope that things will improve or out of loyalty to its staff and customers its rivals are more likely to just wait for its departure than start a court case.

2.21 There therefore seems to be little need to follow the Law Council's suggestion that a problem could be addressed by something analogous to the American approach:

> in the United States the Robinson-Patman Act has what I think is called the 'meeting the competition' defence, so that in the case of predatory pricing

23 Law Council of Australia, *Submission 8*, p. 5.

24 Law Council of Australia, *Submission 8.*

25 Mr Ian Stewart, Law Council, *Proof Committee Hansard*, 5 August 2008, pp 28, 32.

> allegations it is a defence if a corporation, in good faith, tries to meet the lower price of a competitor.[26]

2.22 The argument for moving from 'market share' to 'market power' would be stronger if it could be shown that 'market share' was leading to excessive numbers of successful prosecutions for predatory pricing.[27] But this has *not* been the case:

> the ACCC…recently said that they had 75 complaints so far under the Birdsville amendment and none of those represented a breach of the Birdsville amendment, clearly indicating to me that there are sufficient safeguards in the Birdsville amendment as currently drafted to ensure that it only targets predatory pricing and in no way undermines legitimate discounting practices.
>
> Coles gave evidence to the ACCC price inquiry where they said that their pricing behaviour had not changed as a result of the Birdsville amendment. So, if there was any suggestion that Coles had been frightened into not discounting as a result of the Birdsville amendment, that would have been the time for Coles to put their hand up—but they did not and they said that their pricing practices have not changed.[28]

Committee view

2.23 The committee believes that the term 'market share', as currently legislated in section 46(1AA) of the TPA, is a better defined and more readily measurable term than 'market power'. Moreover, it is concerned that the High Court's definition of 'market power' in the *Boral* ruling has set the threshold for predatory pricing cases far too high. The best evidence of this is that the ACCC has not brought a predatory pricing case before the High Court since the *Boral* ruling.

2.24 The committee believes that—regardless of whether there is or is not the potential for predatory pricing to occur in Australian markets—there should be a clear and straightforward threshold test for predatory pricing cases to reach the courts. The committee recognises that decisions of the High Court 'have, to some degree, shifted the focus of S46 to the 'market power' and 'take advantage' elements of the provisions.'[29] The committee recognises that the government has addressed the important 'take advantage' element in amendments to this Bill. However, if the government believes that section 46(1AA) should use the term 'market power' it is important that it seeks advice on the precise definition of 'market power'. The

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26 Mr Ian Stewart, Law Council of Australia, *Proof Committee Hansard*, 5 August 2008, p. 33.

27 As Treasury put it, 'Preventing a corporation or dissuading a person from discounting or otherwise providing a benefit to a consumer simply through an examination of their share in that market'; *Proof Committee Hansard*, 5 August 2008, p. 16.

28 Associate Professor Frank Zumbo, *Proof Committee Hansard*, 5 August 2008, p. 3.

29 ACCC, Submission to the Senate Economics References Committee inquiry into the effectiveness of the Trade Practices Act 1974 in protecting small business.

committee is concerned that deleting reference to the term 'market share' will give a green light for the courts to interpret 'market power' based on the *Boral* precedent.

Recommendation 1

2.25 The committee recommends the government reconsider the implications of changing 'market share' to 'market power' in section 46(1AA).

Predatory pricing and the meaning of 'take advantage'

2.26 The bill aims to clarify what is meant by the term 'take advantage'. For a corporation with substantial power to contravene section 46(1), it must 'take advantage' of that power for the purpose of:

> (a) eliminating or substantially damaging a competitor of the corporation or of a body corporate that is related to the corporation in that or any other market;
>
> (b) preventing the entry of a person into that or any other market; or
>
> (c) deterring or preventing a person from engaging in competitive conduct in that or any other market.[30]

2.27 There have been important test cases interpreting the meaning of 'take advantage' in the context of section 46. The High Court found in the *Melway* case that Melway had not taken advantage of its market power because the conduct in question was habitual and occurred before the company had obtained its market power. In its decision on *Safeway*, the Federal Court found that the rationale of the company's action matters. A company cannot contravene section 46(1) if it did not act with the intent of taking advantage of its market power. In the *Rural Press* case, the High Court emphasised the physical capacity of the company to take advantage of its market, as distinct from its rationale or intent. The key test was whether Rural Press could have acted in the same way if it did not have market power.[31]

2.28 The ACCC pointed out the absurdity of the High Court's judgement in the *Rural Press* case:

> What this test means is that so long as it *could* physically be possible for a firm to engage in the conduct in the absence of its having market power, it will be held not to have taken advantage of its market power, even though it

30 *Trade Practices Act 1974*.

31 Senate Economics References Committee, *The effectiveness of the Trade Practices Act 1974 in protecting small business*, pp. 12–14.

> *would not on any rational commercial basis* have engaged in the conduct in the absence of market power.[32]

2.29 The 2004 Senate committee report supported the ACCC's view that the interpretation of the term 'take advantage' should be broadened from the Court's interpretation in the *Rural Press* case. It recommended that the Act should be amended to include a declaratory provision outlining the elements of the term 'take advantage'.[33] To this end, the report cited the ACCC's suggestions that in determining whether a corporation has taken advantage of its market power, the courts should consider whether:

(a) the conduct of the corporation is materially affected by its substantial degree of market power;

(b) the corporation engages in the conduct in reliance upon its substantial degree of market power;

(c) the corporation would be likely to engage in the conduct if it lacked a substantial degree of market power; or

(d) the conduct of the corporation is otherwise related to its substantial degree of market power.[34]

2.30 The bill incorporates these four non-exclusive factors, as new subsections 46(6A)(a–d), to provide a basis for the courts' consideration in determining whether a corporation has taken advantage of its substantial market power. The Explanatory Memorandum emphasises that the new provision enables the courts to consider whether the corporation could have engaged in the conduct in a competitive market and whether it *would* have been likely to do so.[35]

2.31 These provisions have been criticised in some submissions. The Law Council of Australia argues that the criteria in 46(6A)(a) and (c) are unnecessary, as they 'merely codify principles of law established by the several High Court decisions interpreting s 46'. The Business Council of Australia goes further, arguing that adding unnecessary prescription in the legislation poses a risk they would have 'unintended consequences and introduce uncertainty into how the law will be applied in practice'.[36]

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32 Senate Economics References Committee, *The effectiveness of the Trade Practices Act 1974 in protecting small business*, p. 13. The quotation comes from the ACCC's submission, p. 4.

33 Senate Economics References Committee, *The effectiveness of the Trade Practices Act 1974 in protecting small business*, p. xii.

34 Senate Economics References Committee, *The effectiveness of the Trade Practices Act 1974 in protecting small business*, p. 14.

35 The Hon. Chris Bowen, Second Reading Speech, *House of Representatives Hansard*, 26 June 2008.

36 Business Council of Australia, *Submission 7*, p. 4.

2.32 The Law Council argues that sections 46(6A)(b) and (d) should not be incorporated because they are:

> …unsound in principle, susceptible of differing interpretations, and likely to lead to uncertainty and error in the application of s 46(1).[37]

2.33 The Law Council also argues that the term 'reliance' in proposed subsection 46(6A)(b) had the potential to mislead the courts to consider the corporation's opinion as to whether it *believes* it is taking advantage of its market power, rather than the objective matter of whether it is using that power.

2.34 Both the Business Council of Australia and the Law Council argued that proposed subsection 46(6A)(d) will result in uncertainty and confusion and may penalise competitive activities.[38] The Business Council argued that the words 'otherwise related to' in proposed subsection 46(6A)(d) are much wider than the current judicial interpretation of the words of 'take advantage'. The result could be to 'dilute, or even eliminate, the current causal connection which is required between a corporation's market power and its purpose'.[39]

2.35 The Law Council's submission cited the High Court's ruling in the *Rural Press* case that the conduct of taking advantage of a thing is not identical with the conduct of protecting a thing. The Council's submission gave the example of a corporation which is a market leader with substantial market power developing a product which preserves its leadership and power in that market. By so doing, the corporation's conduct is related to its power in the market 'but the connection is not causal'. The Council cited and endorsed the judgement of Justice French in *Natwest Australia Bank v Boral Gerrad Strapping Systems Pty Ltd (1992)* that 'there must be a causal connection between the conduct alleged and the market power pleaded such that it can be said that the conduct is a use of that power'.[40]

2.36 Two lawyers appearing as witnesses questioned 46(6A)(d):

> I would, however, query subsection 46(6A)(d) of the proposed amendments—that is, the need for the remaining catch-all provision that exists there…whether it is going to lead to distraction from the other

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37 Law Council of Australia, *Submission 8*, p. 6.

38 Business Council of Australia, *Submission 7*, p. 3.

39 Business Council of Australia, *Submission 7*, p. 4. Minister Bowen has also emphasised the importance of maintaining 'a sufficient causal connection between the offending conduct and substantial market power'. The Hon. Chris Bowen, 'Reviewing the federal government's amendments to the Trade Practices Act 1974', *Keynote address to the 4th Annual Trade Practices and Corporate Compliance Summit*, The Grace Hotel, Sydney, 28 April 2008.

40 Law Council of Australia, *Submission 8*, p. 8.

> provisions which I think have root in some of the jurisprudence in the previous cases. [41]
>
> that is quite a dangerous proposal because it does not necessarily imply there has been a taking advantage of market power. We have given an example of a corporation with substantial market power which, in order to protect its market power, introduces a new and innovative product. That might be said to be related to its market power because it aims to protect it. However, it does not involve a taking advantage of market power.[42]

2.37 On the other hand, the Fair Trading Coalition was strongly supportive of the bill's section 46(6A) amendments, arguing that any suggestion that proposed subsections (c) and (d) be deleted 'would weaken a very necessary and welcome change to section 46'.[43] The Consumer Action Law Centre argued that given the past difficulty of proving that a company has taken advantage of its market power, it is appropriate for the Parliament to provide further guidance to the courts.[44]

2.38 There are other legal regimes that take a much stronger line than is envisaged in the bill. In some states in the United States, pricing below cost is regarded as 'prima facie evidence of predatory pricing'.[45]

Predatory pricing and 'recoupment'

Background

2.39 The matter of recoupment is another whether the law requires modification in response to the High Court making a ruling which frustrates the intent of the legislation by setting the barrier to prove predatory pricing unrealistically high. In February 2003, the High Court delivered its finding on the *Boral Besser Masonry v ACCC* case. The ACCC claimed that Boral was guilty of predatory pricing, highlighting that one of Boral's competitors had left the market as a result of its below-cost pricing. The High Court disagreed, arguing that Boral was not guilty of predatory pricing because it did not have the market power to recoup the losses it sustained when it dropped its prices. They made this ruling despite there being no reference in the TPA to recoupment.[46] Apparently the Court did not explain why it thought Boral was pricing consistently below cost if it would not gain from it in the longer run.

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41 Mr Graham Maher, *Proof Committee Hansard*, 5 August 2008, p. 21.

42 Mr Ian Stewart, Law Council of Australia, *Proof Committee Hansard*, 5 August 2008, p. 29.

43 Fair Trading Coalition, *Submission 3*, p. 1.

44 Consumer Action Law Centre, *Submission 5*, p. 3.

45 Mr Graham Maher, *Proof Committee Hansard*, 5 August 2008, p. 20.

46 Mr Scott Rogers, Treasury, *Proof Committee Hansard*, 5 August 2008, p. 12.

2.40 This decision meant that the ability to recoup losses incurred from below cost pricing is a necessary precondition to establish that a corporation has engaged in predatory pricing.[47] It would not be possible to establish whether a firm had actually recouped its losses until years after the anticompetitive conduct had occurred. Proving that future market conditions will allow a firm to recoup losses would be very difficult.

2.41 This problem was discussed by the Senate Economics References Committee in its March 2004 inquiry into the effectiveness of the TPA. The majority report recommended that the Act be amended to state 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.[48]

2.42 The then-government Senators disagreed with this recommendation. Their dissenting report stated:

> The issue of recoupment is important, in particular because it often provides the best test of whether price-cutting is a genuine exercise in competition or has a predatory intent. (A firm which is genuinely competing on price does not plan to recoup its foregone revenue from the elimination of its competitor; a firm which is engaged in a predatory pricing strategy almost invariably will.) Rather, Government Senators consider that recoupment should be one of the criteria to which the court may (and ordinarily will) have regard in determining whether price-lowering behaviour is predatory.[49]

2.43 The explanatory memorandum which accompanied the legislation enshrining the Birdsville amendment stated that 'recoupment no longer needed to be proved'.[50]

The bill's response

2.44 The Government believes that while the likelihood of recoupment may be an indicator of predatory pricing, proving it should not be an essential precondition to

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47 The Hon. Chris Bowen, Second Reading Speech, *House of Representatives Hansard*, 26 June 2008.

48 Senate Economics References Committee, *The effectiveness of the Trade Practices Act 1974 in protecting small business*, pgs. xiii and 19.

49 Senate Economics References Committee, *The effectiveness of the Trade Practices Act 1974 in protecting small business*, p. 87.

50 Senator Barnaby Joyce, *Proof Committee Hansard*, 5 August 2008, p. 43. See Amendment to Explanatory Memorandum, *Trade Practices Legislation Amendment Bill 2007*, p. 5.

establishing that predatory pricing is occurring.[51] The bill replaces subsection 46(1AB) and substitutes:

> A corporation may contravene subsection (1AA) even if the corporation cannot, and might not ever be able to, recoup losses incurred by supplying the goods or services at a price less than the relevant cost to the corporation of the supply.

2.45 This reasoning is applauded by the Fair Trading Coalition.

2.46 The Business Council of Australia, on the other hand, argues that the provision on recoupment is unnecessary because:

> …based on judicial decision-making, it is not currently necessary to prove that a business must be able to recoup its losses in order to show the firm has market power and has taken advantage of that power. Rather, recoupment has been one element that the courts have used in considering whether a firm has market power, and has taken advantage of that power.[52]

2.47 Similarly the Law Council argued:

> the existing law is that one does not need to establish recoupment but it may be relevant in a given case.[53]

2.48 These views seem clearly at odds with the High Court's ruling in the *Boral* case. They may be relying on the explanatory memorandum that set out that 'recoupment no longer needed to be proved'.[54] However, 'statements that are made in explanatory memoranda and so on are relevant to courts in interpreting legislation but are not necessarily conclusive. It obviously has more force if it is included in legislation'. [55]

2.49 Moreover, the Business Council suggested that by inserting the provision with specific reference to recoupment, 'the amendment arguably creates the impression that recoupment is not an important element in assessing conduct under section 46'.[56]

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51 The Hon. Chris Bowen, Second Reading Speech, *House of Representatives Hansard*, 26 June 2008.

52 Business Council of Australia, *Submission 7*, p. 5.

53 Mr Ian Stewart, Law Council of Australia, *Proof Committee Hansard*, 5 August 2008, p. 28.

54 Amendment to Explanatory Memorandum, *Trade Practices Legislation Amendment Bill 2007*, p. 5.

55 Ms Nicole Rich, Consumer Action Law Centre, *Proof Committee Hansard*, 5 August 2008, p. 43.

56 Business Council of Australia, *Submission 7*, p. 5.

Recommendation 2

2.50 The committee recommends the Senate support the provisions of the bill relating to the meaning of 'take advantage' and recoupment.

Chapter 3

Other provisions

Small business expertise

3.1 Schedule 3 of the bill amends the TPA and the *Australian Securities and Investments Commission Act 2001* to require that one of the ACCC's Deputy Chairpersons have knowledge of, or experience in, small business matters. Presently, the legal requirements include that:

- in appointing a member of the Commission, the Minister must consider whether the person has knowledge of, or experience in, small business matters (section 7(3b); and
- at least one member of the ACCC must be a person who has knowledge of, or experience in, consumer protection (section 7(4)).

3.2 The Post Office Agents Association Limited strongly supported the bill's new requirement. It noted that avoiding unconscionable conduct is 'not always achieved in the current framework…especially…in situations where the supervisory authorities appear to be under-resourced to "prevent" the action'.[1] It argued that the bill's new requirement on small business expertise for the ACCC should enhance the ability of the Commission to deal with current and emerging issues.

3.3 Professor Zumbo does not see it as a positive move:

> the appointment of a small business deputy chairman will add nothing to the current administration or enforcement of the Trade Practices Act on behalf of small business…there has been a small business commissioner since 1998. The concerns expressed by small business have grown during that time… The fact that that small business commissioner now will be upsized to a deputy will not change the fundamental problem with those key sections which prevent small business getting their cases heard… it does have the danger of acting to fracture the ACCC… the ACCC has one responsibility and one responsibility only, and that is to protect the consumer interest…Any other label or other labels are just a distraction from that paramount responsibility of commissioners to consumers.[2]

3.4 This objection could be over-stated:

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1 Post Office Agents Association Limited, *Submission 2*, p. 3.

2 Associate Professor Frank Zumbo, *Proof Committee Hansard*, 5 August 2008, p. 4.

> this is not a label. There is no small business commissioner… What is being asked for is someone who has experience in that area. They may have experience in other areas [as well].[3]

3.5 The Consumer Action Law Centre are supportive of the bill requiring an ACCC commissioner with expertise in small business, but think the appointment of a commissioner with consumer experience should be similarly enshrined, rather than remaining a matter of convention.[4]

3.6 The importance of the measure should not be over-emphasised:

> the commission operates as a board. It is not as though the small business commissioner gets to make all the decisions that come before the commission about small business issues.[5]

Committee view

3.7 The requirement that an ACCC deputy chair have small business expertise will probably not make an enormous difference to the operations of the ACCC. But it is a useful signal to the ACCC, the small business sector and the general community that the parliament acknowledges the role of small businesses in keeping markets competitive and that trade practices legislation has an important role in preventing large businesses unfairly reducing competition in markets at their expense.

Repealing the thresholds for unconscionable conduct

3.8 The bill repeals the price thresholds that currently limit the protection afforded by section 51AC against unconscionable conduct. Section 51AC was introduced in 1998 to establish legal remedies for smaller businesses when they are subjected to unconscionable conduct. The factors that may constitute 'unconscionable conduct' are listed under sections 51AC(3)—relating to suppliers—and 51AC(4)—relating to acquirers. These factors include any relative imbalance in bargaining power and the ability of the smaller business to understand the terms of the transaction.[6]

3.9 The redress available to small businesses under section 51AC is limited by subsections 51AC(1) and 51AC(2), which excludes publicly listed companies, and subsections 51AC(9) and 51AC(10), which excludes dealings in excess of

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3 Senator Doug Cameron, *Proof Committee Hansard*, 5 August 2008, p. 11.

4 Ms Catriona Lowe, Consumer Action Law Centre, *Proof Committee Hansard*, 5 August 2008, p. 41.

5 Ms Catriona Lowe, Consumer Action Law Centre, *Proof Committee Hansard*, 5 August 2008, p. 48.

6 *Explanatory Memorandum*, p. 8.

$10 million.[7] Consistent with the recommendation of the 2004 Senate inquiry, the bill repeals subsections 51AC(9) and 51AC(10) and section 12CC of the ASIC Act. At the time, the ACCC argued that these subsections were not necessary as the courts already have regard to the relative strengths of the bargaining positions of the companies under subsection 51AC(3)(a).[8] The government argues that the reform will enhance the protection afforded by section 51AC 'by focusing the prohibition on the wrongdoing involved, rather than monetary thresholds'.[9]

3.10 Professor Zumbo did not oppose the measure, but saw its use as being part of a broader reform process:

> unless you change the substantive meaning or the substantive flaws in 51AC as they currently exist—that is, a lack of definition of unconscionable conduct in the section itself—removing the cap will not be of any practical assistance.[10]

Jurisdiction – Federal Magistrates Court

3.11 The bill confers jurisdiction on the Federal Magistrates Court in matters arising under section 46. The goal is 'to provide a simpler and more accessible alternative to litigation in the superior courts'.[11]

3.12 This idea appealed in some ways to one expert witness:

> Part of what is attractive about the Federal Magistrates Court is that its approach is, on the whole, conciliatory. It looks to use mediation in other sorts of processes,…[12]

3.13 However, he was cautious about some aspects of it:

> you should think about resourcing, how that is going to fit within the jurisdiction and who is going to handle it. Maybe you need dedicated judges with a particular background in these issues… I think that court is specifically suited to matters currently within its jurisdiction. [13]

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7 This threshold was increased from $3 million to $10 million last year (Trade Practices Legislation Amendment Bill (No. 1) 2007).

8 Senate Economics References Committee, *The effectiveness of the Trade Practices Act 1974 in protecting small business*, p. xv.

9 The Hon. Chris Bowen, Second Reading Speech, *House of Representatives Hansard*, 26 June 2008.

10 Associate Professor Frank Zumbo, *Proof Committee Hansard*, 5 August 2008, p. 3.

11 *Explanatory Memorandum*, p. 17.

12 Mr Graham Maher, *Proof Committee Hansard*, 5 August 2008, p. 26.

13 Mr Graham Maher, *Proof Committee Hansard*, 5 August 2008, p. 26.

3.14 Professor Zumbo did not believe this change would be of much benefit given the other problems he raised:

> access to the Federal Magistrates Court will deliver nothing of practical benefit because you just will not be able to bring section 46 cases; they are too difficult, given the very narrow interpretation given by the High Court to those two concepts of market power and take advantage.[14]

3.15 Another lawyer warned:

> …section 46 cases usually go on appeal. This reflects the complexity of the law. So, if one starts off at the Federal Magistrates Court, there is going to be one extra layer of appeals to be dealt with. That is going to increase costs and delay.[15]

Committee view

3.16 It is hard to know beforehand how many cases will be able to be satisfactorily resolved in the Federal Magistrates Court without needing referral to the High Court. However, the committee believes measures with the potential to reduce the cost of parties seeking justice are worth at least trying.

ACCC's information gathering powers

3.17 The bill clarifies the timeframe under which the ACCC's powers to require the production of documents under section 155 can be exercised. It provides that the ACCC can exercise these powers until it commences proceedings or the close of pleadings.

3.18 One lawyer appearing as a witness raised some concerns, suggesting that:

> it be made clear in the relevant provisions of the bill that nothing therein is intended to derogate from a court's power to control the procedures before it so that the court is aware that there is no conflict and the court is aware of its power to be able to ask the ACCC or direct the ACCC to expedite its investigations[16]

3.19 Other witnesses expressed no concerns about the provisions.

Recommendation 3

3.20 The committee recommends that the Senate support the provisions of the bill relating to requiring one of the ACCC deputy chairs to have small business expertise, repeal of the threshold for unconscionable conduct, extending jurisdiction to the Federal Magistrates Court and clarifying the ACCC's information gathering powers.

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14 Associate Professor Frank Zumbo, *Proof Committee Hansard*, 5 August 2008, p. 3.

15 Mr Ian Stewart, *Proof Committee Hansard*, 5 August 2008, p. 29.

16 Mr G Maher, *Proof Committee Hansard*, 5 August 2008, p. 21.

Senator Annette Hurley
Chair

Coalition Senators' Dissenting Report[1]

The Federal Government's proposals to amend Section 46 in relation to predatory pricing takes small business back to the former complexities and improbabilities of having to prove the market power test. The market power test was given an onerous interpretation by the High Court in the Boral Decision in 2003. Small businesses seeking to take legal action for predatory pricing under the market power test have been required to satisfy the High Court market power test before they could even argue that the behaviour by the big business was anti-competitive. If the small business could not prove market power then they could not have any remedy under law against predatory pricing. Reliance on the market power test would be a retrograde step as is clearly exemplified in the evidence delivered to the Senate Inquiry which showed under the market power test the ACCC has not commenced any new court prosecutions under s 46 since the Boral Case in 2003.

> …if a small business feels that it has been the subject of predatory pricing or predatory conduct of any sort they are effectively looking down the barrel of a 10-year case appealed all the way to the High Court and a cost of $1 million or more —God knows how much. That is just an impossibility for a small business. The only recourse that a small business has is if the ACCC will take up a case and prosecute it. There has been a clear reluctance on the part of the ACCC to do that…[2]

In contrast, the market share test as stated in Section 46(1AA), generally known as the Birdsville Amendment, gives Australians, especially those in small business, access to an effective legal remedy against predatory pricing. Predatory pricing is anti competitive as it removes efficient competitors from the market and with a reduction in competition comes inflation leading to higher interest rates and a general disfunctionality in the economy.

So often it is put that proving substantial market share is all that one has to do to win a case on predatory pricing but the evidence stands for itself in that over 75 cases have been taken to the ACCC, under the Birdsville Amendment, involving a complaint against an entity with substantial market share but this has not been held to be a breach of the law as the other hurdles in the Birdsville amendment had not been satisfied.

Far more needs to be proved to win a case of predatory pricing under the Birdsville Amendment than just having substantial market share. There are sufficient safeguards in the Birdsville Amendment that have ensured that it has not dampened legitimate competition in any way. Accordingly, the Birdsville Amendment strikes an appropriate balance in preventing predatory pricing while in no way undermining legitimate competition. In summary, there is no evidence that the Birdsville Amendment is undermining competition in any way. Rather, there is ample evidence from the ACCC alone that there are sufficient safeguards in the Birdsville Amendment.

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1 Senator Alan Eggleston (Deputy Chair), Senator Barnaby Joyce and Senator David Bushby

2 Mr Kenneth Michael Henrick, Chief Executive Officer, National Association of Retail Grocers of Australia, *Proof Committee Hansard*, 5th August, 2008.

In this environment, the Federal Government has failed to make out a case for amending the Birdsville Amendment. Instead, the Government is proposing to undermine the effectiveness of the Birdsville Amendment by reintroducing the very onerous market power test.

> The government's…proposed amendments are what can be described as procedural changes and do not deal with the underlying substantive weaknesses or gaps in key sections of the Trade Practices Act dealing with abuses of market power and unconscionable conduct by large and powerful entities.[3]

In addition, the Government is proposing adding a further hurdle; the Take Advantage Test. The Take Advantage Test will add extra complexities to the process of proving predatory pricing which will be to the detriment of small business. The additional hurdle of the Take Advantage Test is unnecessary given the already sufficient safeguards in the Birdsville Amendment. Clearly, the Federal Government's proposal to insert the Take Advantage Test as an additional hurdle is yet another form of excluding small business from recourse to the courts against anti competitive actions such as predatory pricing.

The Government has put forward the argument that having both a market power and a market share test leads to uncertainty yet has stated that having separate predatory pricing offences, is on balance a good thing.

> I have reached the view that having separate predatory pricing offences is, on balance a good thing…However, having strengthened the substantial degree of market power test, there is no need, in my view, to have a separate 'market share' test for predatory pricing. Having a new market share test creates considerable uncertainty in the market as to how it will be interpreted by the courts. Accordingly; we will legislate for the test of breaches of 46AA to be 'a substantial degree of market power'.[4]

The Federal Government's assertion that market share tests lead to uncertainty fails to recognise that the ACCC will, when assessing predatory pricing claims, closely review the market share of the entity allegedly engaging in the predatory pricing. Market share is a well understood concept and can be easily defined by reference to the relevant market. While market share depends on the market definition, it is clear that once we define the relevant market we can determine the market shares of each entity and determine if that market share is substantial. The word “substantial” is a generally understood term which has long been used throughout the competition law sections of the *Trade Practices Act*.

The Federal Government's further assertion that having both market share and market power tests in s 46 means that there is a “dual track” process under s 46 fails to acknowledge that other competition law sections of the *Trade Practices Act* also contain a “dual track” process. Having two different tests within s 46 is not a valid criticism and a dual track approach is totally consistent with the approach taken in other competition law sections of the *Trade Practices Act*.

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3 Associate Professor Frank Zumbo, *Proof Committee Hansard*, 5 August 2008.

4 The Hon Chris Bowen MP, Keynote Address to the 4th Annual Trade Practices and Corporate Compliance Summit, 28th April, 2008.

If there is a concern that the substantial market share test should be discarded as it is not used elsewhere in the *Trade Practices Act*, one would presume that the most effective way to deal with this lack of use elsewhere would be to expand the use of the market share test to other sections of the act and remove the market power test altogether. In fact, the real concern is with the narrow ambit of the market power test and the fact that not one witness through out the whole enquiry was able to provide any conclusive evidence that the market power test would fully capture all forms of predatory pricing.

One argument that is raised is that the Trade Practices Act is there to protect competition and not competitors. It stands to reason that you will not have competition without competitors and the more efficient and vigorous competitors you have, the stronger the competition. Predatory Pricing and other like actions remove competitors so as to reduce competition. They remove the competitors that are competitive, or are likely to be competitive, which means that they remove from the market the potential for the consumer to get a better price. The destruction of competition is not good for consumers and therefore we need the retention of the Birdsville Amendment in its current form as this is essential to the preservation of competition. It is the role of Government to make sure a competitive environment exists. A corporation with substantial market share should not be allowed to reduce competition to the detriment of consumers. The Government's proposed undermining of Section 46(1AA) only serves the interests of those corporations with substantial market share as these corporations will be given the green light to engage in predatory pricing by the Government's proposal to replace the current market share test in the Birdsville Amendment with the new and extremely onerous hurdles of the Market Power and Take Advantage tests.

In the representations from the law council it was made clear and apparent that, to the best of their knowledge, they had not represented a plaintiff in bringing a successful s 46 case under the Market Power Test but they had been quite successful in their representations on behalf of defendants that have escaped prosecution under s 46. We see this as clear evidence of the inadequacies of the Market Power Test under s 46 as it stood. Now the Government is proposing to take us back to a point where there will be no s 46 cases taken to Court. It seems paradoxical that the Government would say that they are concerned about competition and prices and in the same breath be moving amendments to the Birdsville Amendment to make the situation worse.

Take Advantage

The take advantage amendments proposed by the Government are merely a codification of the case law on the interpretation of take advantage. The opposition does agree that the Rural Press Case requires that the current onerous interpretation of the Take Advantage Test should be relaxed. However, we believe that the Government's proposed amendments on take advantage will not make it easier to take s 46 cases. Under the present court interpretation of take advantage, the ACCC needs to prove that the corporation is engaging in conduct that is unique to the market power held by the corporation. If the corporation can engage in the same conduct with or without market power, then the corporation is not taking advantage of its market power according to the High Court. So for instance, since selling below cost may be an action that one could undertake whether one had market power or not, such conduct would not represent a taking advantage and therefore the entity would not be in breach of s 46.
In short the Corporation with market power had to have done something they wouldn't have otherwise done in order to be deemed to have taken advantage of their market power. The Government's position once more is flawed as it relies on the market power and take advantage tests. Since proving a substantial degree of market power and a taking advantage

has been proved to be near impossible, the Govt position means that the ACCC and small business will not be able to take s 46 cases to court unde the Government's proposals.

> We already know from price surveys that, if a major chain store has no local competition, as is the case in some areas of Sydney or Melbourne, their prices are relatively higher than the same store in areas where there is competition. In answering your question about whether prices go up in the absence of competition, certainly, yes.[5]

Removing the monetary ceiling to bringing cases under s 51AC

The removal of the monetary ceiling will not assist small businesses in bringing unconscionable conduct cases under s 51AC. The Courts have interpreted the concept of unconscionable conduct in such an onerous manner that there have been very few successful cases under s 51AC. The fundamental problem with s 51AC is that it currently lacks a statutory definition of what is unconscionable conduct. Unless the fundamental problem with s 51AC is dealt with, the removal of the monetary ceiling will be of no practical benefit to small businesses.

The appointment of an ACCC Deputy Chairperson with responsibility for small business

The appointment of an ACCC Deputy Chairperson with responsibility for small business will be of no practical benefit to small businesses unless the Deputy Chairperson is given new powers to assist small business. We have seen the failure of the Petrol Commissioner because the appointee was not given new powers and this serves as a reminder that appointments to the ACCC must be given new powers if they are to be effective.

Access to the Federal Magistrates Court

Allowing access to the Federal Magistrates Court for cases under s 46 will be of no practical benefit to small businesses unless the Birdsville Amendment is retained and small businesses are given financial assistance to bring s 46 cases. Consideration should be given to the establishment of a Small Business Advocate that can help small businesses bring s 46 cases in the Federal Magistrates Court.

Recommendation 1

Section 46 (1AA) be left as is.

Recommendation 2

A statutory definition of unconscionable conduct be in inserted 51(AC);

Recommendation 3

A new statutory duty of good faith be inserted into the Trade Practices Act;

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5 Mr Kenneth Michael Henrick, *Proof Committee Hansard,* 5 August 2008.

Recommendation 4

ACCC Small Business Deputy Chair be given adequate funding and powers to take section 46 and 51(AC) cases on behalf of small business;

Recommendation 5

A small business advocate be established to help small business to take action under s46 and s51(AC) in the Federal Magistrates court; and

Recommendation 6

Divestiture powers be inserted into the Trade Practices Act.

Senator Alan Eggleston
Deputy Chair
LP

Senator Barnaby Joyce
LNP

Senator David Bushby
LP

APPENDIX 1

Submissions Received

Submission Number	Submitter
1	Mr Garth Campbell
2	Post Office Agents Association Ltd (POAAL) National Office
3	Fair Trading Coalition (FTC)
4	Mr Michael Hodge
5	Consumer Action Law Centre (CALC)
6	National Association of Retail Grocers Australia (NARGA)
7	Business Council of Australia (BCA)
8	Law Council of Australia

Additional Information

- Received on 19 August 2008 from Mr Scott Rogers, Senior Adviser, Competition Policy Framework Unit, Competition and Consumer Policy Division, Department of the Treasury. Answers to Questions taken on Notice on 5 August 2008.

APPENDIX 2

Public Hearing and Witnesses

MELBOURNE, TUESDAY, 5 AUGUST 2008

- BOWD, Mr Matthew, Analyst,
  Competition Policy Framework Unit, Competition and Consumer Policy Division, Treasury
- HENRICK, Mr Kenneth Michael, Chief Executive Officer,
  National Association of Retail Grocers of Australia
- LOWE, Ms Catriona, Co-Chief Executive Officer,
  Consumer Action Law Centre
- MAHER, Mr Graham, Partner,
  Addisons Lawyers
- RICH, Ms Nicole, Director, Policy and Campaigns,
  Consumer Action Law Centre
- ROGERS, Mr Scott, Senior Advisor,
  Competition Policy Framework Unit, Competition and Consumer Policy Division, Treasury
- STEWART, Mr Ian Barton, Member,
  Trade Practices Committee, Law Council of Australia
- van RIJSWIJK, Mr Gerard Anthony, Senior Policy Officer,
  National Association of Retail Grocers of Australia
- ZUMBO, Associate Professor Frank