The Senate

Economics Legislation Committee

Competition and Consumer Amendment (Misuse of Market Power) Bill 2014

February 2015

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Abbreviations

ACCC	Australian Competition and Consumer Commission
ANRA	Australian National Retail Association
CCA	*Competition and Consumer Act 2010* (Cth)
Dawson Report	*Review of the Competition Provisions of the Trade Practices Act*—2003 report of the Trade Practices Act Review Committee, chaired by Sir Daryl Dawson
Harper Review	Review of competition policy ongoing at the time of writing, chaired by Professor Ian Harper
Hilmer Report	*National Competition Policy*—1993 report of the Independent Committee of Inquiry into Competition Policy in Australia 1993, chaired by Professor Frederick Hilmer
Law Council	Competition and Consumer Committee of the Business Law Section of the Law Council of Australia

Chapter 1

Introduction

1.1 On 20 March 2014, the Senate referred the Competition and Consumer Amendment (Misuse of Market Power) Bill 2014 to the Economics Legislation Committee for inquiry and report by 24 June 2014.[1] The reporting date was subsequently extended on three occasions, first to 28 August 2014; then to 4 December 2014; and finally to 26 February 2015.

Conduct of the inquiry

1.2 The committee advertised the inquiry on its website and in *The Australian*. It also wrote to relevant stakeholders and interested parties inviting submissions by 30 June 2014. The committee received seven submissions, which are listed at Appendix 1.

1.3 The committee held a public hearing in Canberra on 2 October 2014. The names of the witnesses who gave evidence are at Appendix 2.

1.4 The committee thanks all of the individuals and organisations that contributed to this inquiry.

Consideration of the bill by the Scrutiny of Bills Committee

1.5 When examining a bill or draft bill, the committee takes into account any relevant comments published by the Senate Standing Committee for the Scrutiny of Bills. The Scrutiny of Bills Committee assesses legislative proposals against a set of accountability standards that focus on the effect of proposed legislation on individual rights, liberties and obligations, and on parliamentary propriety. The bill was considered by the Scrutiny of Bills Committee in its *Alert Digest No. 3 of 2014*. No comments were made on the bill.[2]

Structure of this report

1.6 This report comprises two chapters:

- The remaining sections of Chapter 1 provide an explanation of the proposed amendments and background information about the legislation the bill seeks to amend.

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1 *Journals of the Senate*, 2013–14, no. 22 (20 March 2014), pp. 663–64.

2 Senate Standing Committee for the Scrutiny of Bills, *Alert Digest No. 3 of 2014*, March 2014, p. 3.

- Chapter 2 examines the arguments for and against the proposed amendments. The committee's findings are outlined at the end of the report.

Overview of the bill

1.7 On 6 March 2014, Senator Nick Xenophon introduced this private senator's bill into the Senate. The bill proposes to amend the *Competition and Consumer Act 2010* (the CCA) to introduce a divestiture power where a corporation has misused its market power. Specifically, the bill would provide that where a corporation has been found to have contravened subsections 46(1) or 46(1AA) of the CCA, the court may make an order directing the corporation to reduce its power in, or share of, the market. The order would seek to secure the reduction in the corporation's power in, or share of, the market within two years.[3] The bill would provide that an application for divestiture may be made at any time within three years after the date on which the contravention occurred.[4]

1.8 As alternatives to the court making a divestiture order following a finding that subsections 46(1) or 46(1AA) of the CCA had been contravened, the bill would also enable the court:

- to accept an undertaking by the corporation to take particular action to reduce the corporation's power in, or share of, the market;[5] and
- if the court considers it appropriate, to make a divestiture order by consent of all parties regardless of whether the court has found that the corporation contravened subsections 46(1) or 46(1AA) of the CCA.[6]

1.9 The explanatory memorandum provides the following insight into the reasons behind the introduction of the bill:

> The provisions in this Bill are a response to the high concentration of many Australian retail markets, including grocery, fuel, liquor and hardware. There are significant concerns that the lack of competition in these markets is leading to higher prices for consumers and putting producers under increasing financial strain. The measures in this Bill would give the ACCC a further option in addressing these issues, as well as creating a new disincentive for corporations to abuse their market share.[7]

3 Schedule 1, item 1, proposed new subsections 80AD(1) and (2).

4 Schedule 1, item 1, proposed new subsection 80AD(3).

5 Schedule 1, item 1, proposed new subsection 80AD(5).

6 Schedule 1, item 1, proposed new subsection 80AD(4).

7 Explanatory Memorandum, p. 2.

1.10 In his second reading speech, Senator Xenophon noted that divestiture laws are in place in the United States.[8] A general divestiture power is also available in Canada, the European Union and the United Kingdom.

Section 46 of the Competition and Consumer Act

1.11 The overall object of the CCA is 'to enhance the welfare of Australians through the promotion of competition and fair trading and provision for consumer protection'.[9] In its submission, Treasury provided the following explanation of the benefits associated with competition:

> Competitive markets promote efficient production, delivering benefits for consumers through greater choice and lower prices. Over time, competitive pressures also drive innovation and investment in new technologies, and the development of new products that meet consumers' needs. This process of innovation is what drives economic growth and improvements in living standards in the long term.[10]

1.12 Anti-competitive behaviour is addressed in Part IV of the CCA. Restrictive trade practices that are prohibited include cartel conduct; anti-competitive price signalling in relation to certain prescribed goods and services; contracts, arrangements or understandings that restrict dealings or affect competition; the misuse of market power; exclusive dealing; resale price maintenance; and acquisitions that would result in a substantial lessening of competition. It is the misuse of market power prohibitions contained in section 46 of the CCA that are relevant to this bill. The following paragraphs outline the prohibitions contained in subsections 46(1) and 46(1AA) and the penalties that are currently available for contraventions of these prohibitions. As noted above, the bill seeks to introduce a divestiture power into the CCA that could be applied in relation to contraventions of subsections 46(1) and 46(1AA).[11]

Subsection 46(1)

1.13 Subsection 46(1) of the CCA is a long-established provision that prohibits the misuse of market power. The provision is based on a purpose test—that is, it relates to conduct engaged in by a corporation for a proscribed anti-competitive purpose (there are three proscribed purposes in subsection 46(1)). Subsection 46(1) reads as follows:

> A corporation that has a substantial degree of power in a market shall not take advantage of that power in that or any other market for the purpose of:

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8 Senator Xenophon, *Senate Hansard*, 6 March 2014, p. 1016.

9 *Competition and Consumer Act 2010*, s. 2.

10 Treasury, *Submission 4*, p. 5.

11 The CCA already includes a divestiture power as a remedy for mergers that contravene section 50 or 50A of the CCA or occurred under clearance or authorisation that was granted on false or misleading information. See *Competition and Consumer Act 2010*, ss. 81 and 81A.

(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.

1.14 A number of other subsections contain guidance for interpreting the concepts used in subsection 46(1). Other provisions in the CCA assist with the interpretation of 'market' and 'purpose'.[12]

Subsection 46(1AA)

1.15 Subsection 46(1AA), which is also known as the 'Birdsville Amendment', applies to corporations that have a substantial *share* of a market, as opposed to the prohibition in subsection 46(1) that refers to a substantial *degree of power* in a market. Subsection 46(1AA) prohibits corporations with substantial market share from supplying, or offering to supply, goods or services for a sustained period at a price that is less than their relevant cost. However, for the contravention to have taken place, the supply of goods or services must be for one of three proscribed anti-competitive purposes (the purposes are the same as those that apply to subsection 46(1)).

1.16 Market share is a relatively straightforward concept, defined by Treasury as 'a measure of the proportion of a market that is served by a single company'.[13] Market power, however, is a concept that takes into account a range of considerations that affect competition, such as barriers to entry. Market power has been interpreted by the High Court as being:

> …the ability of a firm to raise prices above the supply cost without rivals taking away customers in due time, supply cost being the minimum cost an efficient firm would incur in producing the product.[14]

1.17 Treasury described market power as an ability 'to behave persistently in a manner different from the behaviour that a competitive market would enforce on a firm'.[15]

Penalties

1.18 The pecuniary penalties available for each act or omission described in subsections 46(1) or 46(1AA) are the greatest of the following:

- $10 million;

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12 *Competition and Consumer Act 2010*, ss. 4E and 4F.

13 Treasury, *Submission 4*, p. 6.

14 *Queensland Wire Industries Pty Ltd v Broken Hill Pty Co Ltd* (1989) 167 CLR 177 at 188.

15 Treasury, *Submission 4*, p. 6.

- if the court can determine the value of the benefit that the body corporate, and any body corporate related to the body corporate, have obtained directly or indirectly and that is reasonably attributable to the act or omission—three times the value of that benefit;
- if the court cannot determine the value of that benefit—ten per cent of the annual turnover of the body corporate during the period of 12 months ending at the end of the month in which the act or omission occurred.[16]

1.19 Section 82 of the CCA provides that actions for damages may be taken by a person who suffers loss or damage as a result of conduct that contravened subsection 46(1) or 46(1AA).[17] The ACCC may also seek to take representative action on behalf of persons who have suffered or are likely to suffer loss or damage as a result of a contravention.[18] Orders disqualifying a person from managing corporations may also be sought.[19]

Purpose of section 46

1.20 Commentary about section 46 generally emphasises that the prohibitions are intended to 'protect the competitive process in markets, rather than individual competitors'. Treasury stated that the provisions:

> …are not designed to produce or promote any particular market structure or composition. The role of section 46 is to distinguish between vigorous competitive activity (which is desirable) and economically inefficient, monopolistic practices that may harm the competitive process, which drives efficient outcomes and benefits to consumers.[20]

1.21 In a landmark case that considered section 46, the High Court made the following observation about the object of section 46 and the nature of competition among businesses:

> The object of section 46 is to protect the interests of consumers, the operation of the section being predicated on the assumption that competition is a means to that end.
>
> Competition by its very nature is deliberate and ruthless. Competitors jockey for sales, the more effective competitors injuring the less effective

16 *Competition and Consumer Act 2010*, s. 76(1A)(b). These penalties were increased in 2006 by the *Trade Practices Legislation Amendment Act (No. 1) 2006*. Prior to these amendments, the maximum penalty was fixed at $10 million.

17 Although subsections 46(1) and 46(1AA) are cited as they are relevant to this bill, section 82 actually applies to any contravention of a provision in Part IV or IVB of the CCA. The action must be taken within six years 'after the day on which the cause of action that relates to the conduct accrued'. *Competition and Consumer Act 2010*, s. 82.

18 *Competition and Consumer Act 2010*, s. 87(1B).

19 *Competition and Consumer Act 2010*, s. 86E.

20 Treasury, *Submission 4*, p. 5.

> by taking sales away. Competitors almost always try to 'injure' each other in this way. This competition has never been a tort…and these injuries are the inevitable consequence of the competition section 46 is designed to foster.[21]

1.22 A 2003 review of the CCA (then known as the *Trade Practices Act 1974*) emphasised that section 46 'is aimed against anti-competitive monopolistic practices, not competition, even aggressive competition':

> The distinction is sometimes a difficult one, but it is one that section 46 seeks to maintain and in doing so seeks to balance the risk of deterring efficient market conduct against the risk of allowing conduct that would damage competition and reduce efficiency.[22]

Consideration of a divestiture power by other inquiries

1.23 Proposals for the introduction of a general divestiture power have been considered during other reviews including, among others:[23]

- the 1993 Committee of Inquiry into a National Competition Policy, chaired by Professor Frederick Hilmer (the Hilmer Report);
- the 2003 report of the Trade Practices Act Review Committee, chaired by Sir Daryl Dawson (the Dawson Report); and
- various inquiries undertaken by the Senate Economics References Committee between 2004 and 2011, including inquiries into the effectiveness of the *Trade Practices Act 1974* in protecting small business (2004); competition and pricing in the Australian dairy industry (2010); competition in the Australian banking sector (2011); and the impacts of supermarket price decisions on the dairy industry (2011).

1.24 The findings of these reviews are discussed in Chapter 2 where relevant.

Harper Review (2014)

1.25 A comprehensive review of competition policy is currently underway. The review was announced by the government on 4 December 2013 and is being chaired by Professor Ian Harper. Among other things, the terms of reference direct the review panel to consider whether the CCA 'appropriately protects the competitive process and facilitates competition', including by:

- 'examining whether current legislative provisions are functioning as intended in light of actual experience and precedent'; and

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21 *Queensland Wire Industries Pty Ltd v Broken Hill Pty Co Ltd* (1989) 167 CLR 177 at 191; cited in Treasury, *Submission 4*, pp. 5–6.

22 Trade Practices Act Review Committee, *Review of the Competition Provisions of the Trade Practices Act*, 2003, p. 80.

23 For a more exhaustive list of inquiries that have considered divestiture, and a useful summary of each inquiry's findings, see Treasury, *Submission 4*, pp. 10–12.

- 'considering whether the misuse of market power provisions effectively prohibit anti-competitive conduct and are sufficient to: address the breadth of matters expected of them; capture all behaviours of concern; and support the growth of efficient businesses regardless of their size'.[24]

1.26 The issues paper released by the Harper Review noted that previous reviews have considered whether a general divestiture power should be introduced.[25] The issues paper invited submissions on the following question:

> Are the enforcement powers, penalties and remedies, including for private enforcement, effective in furthering the objectives of the CCA?
>
> The Panel is interested in whether there are other remedies or powers (for example, in overseas jurisdictions) that should be considered in the Australian context.[26]

1.27 The draft report released by the Harper Review in September 2014 is discussed in Chapter 2. The Harper Review is expected to provide its final report to the government by the end of March 2015.

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24 Competition Policy Review, 'Terms of Reference', http://competitionpolicyreview.gov.au/terms-of-reference (accessed 10 July 2014).

25 Competition Policy Review, *Issues Paper*, 14 April 2014, http://competitionpolicyreview.gov.au/files/2014/04/Competition_Policy_Review_Issues_Paper.pdf (accessed 10 July 2014), p. 40.

26 Competition Policy Review, *Issues Paper*, 14 April 2014, p. 41.

Chapter 2

Key issues

2.1 This chapter examines the evidence received by the committee regarding divestiture orders generally and the specific proposal contained in the bill. The committee's findings can be found at the end of this chapter.

Rationale for a general divestiture power

2.2 According to the explanatory memorandum, the provisions in the bill are a response to market concentration in many retail markets, including those for groceries, fuel, liquor and hardware.[1] Although the committee did not examine the dynamics of these particular markets or assess claims about the state of competition within them,[2] it is clear that there are several markets in Australia with a small number of large firms. Treasury's submission acknowledged that comparisons of Australian markets and those in other countries indicate some Australian markets are more concentrated than in some other advanced economies.[3] The Australian National Retailers' Association (ANRA) suggested that there are many markets in Australia with a small number of firms operating at scale, and that this may be a consequence of Australia's small population dispersed across a large geographic area.[4] In any case, Treasury submitted that 'highly concentrated markets are not always detrimental to consumer welfare':

> This is particularly the case to the extent that they reflect the ability of larger firms to deliver services at lower overall cost, for example due to economies of scale associated with sophisticated logistics networks, and these savings are passed through to consumers. A range of other factors affecting market concentration include consumer preferences for variety, technologies relevant to the market, and planning and zoning regulations. Changes in technology over time, for example facilitating the uptake of

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1 Explanatory Memorandum, p. 2.

2 Although the committee has not examined these markets, the explanatory memorandum and submissions to this inquiry commented on them. The explanatory memorandum stated: 'there are significant concerns that the lack of competition in these markets is leading to higher prices for consumers and putting producers under increasing financial strain'. ANRA strongly objected to this claim. It stated that the supermarket sector is 'one of the most studied sectors when it comes to competition policy and no substantive evidence has been provided to support the claims that there is a lack of competition in Australia or that there is market failure in the grocery supply-chain'. ANRA argued that intense competition has imposed downward pressure on food prices between 2009 and 2013. Further, ANRA argued that the expansion of the international chains Costco and ALDI 'points to an increasingly competitive market'. ANRA, *Submission 2*, p. 2. The committee makes no judgment on these competing claims.

3 Treasury, *Submission 4*, p. 7.

4 Australian National Retailers' Association, *Submission 2*, p. 1.

> internet shopping, have in some sectors helped small retailers overcome diseconomies associated with their size and compete more effectively with larger incumbents.[5]

2.3 Treasury also noted that whether a market is highly concentrated is neither the only, nor necessarily the most useful, indicator of the state of competition in that market:

> When assessing the level of competition in a market, other factors besides market concentration are important, including the presence of barriers to entry or expansion, competition from imports, the level of countervailing power held by buyers, the nature of key competitors, and the availability of substitute products or services. The Productivity Commission noted in its 2011 review of Australia's retail industry that market concentration by itself provides little guidance on the extent of competition in the market, and barriers to entry and the extent of market contestability, it noted, are more important.[6]

2.4 Treasury's submission provided an overview of the arguments made to previous public inquiries in support of a divestiture power. According to Treasury, these include that such a power may provide:

- a structural remedy to conduct perceived to flow from the structure of a market, rather than attempting only to remedy the problematic conduct;
- a deterrent to firms from contravening section 46 that is potentially stronger than other remedies currently available; and
- a negotiation tool in the hands of regulators seeking non-judicial dispute resolution.[7]

2.5 The Competition and Consumer Committee of the Law Council of Australia's Business Law Section acknowledged the argument that a 'well-targeted divestiture order could eliminate market power with "one cut"…thus, so it would be said, reducing the regulatory task for the future'. However, it argued that the idea of a divestiture power, and the specific power proposed in the bill, create significant uncertainty and risks.[8]

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5 Treasury, *Submission 4*, p. 6.

6 Treasury, *Submission 4*, p. 6.

7 Treasury, *Submission 4*, p. 9.

8 Competition and Consumer Committee of the Business Law Section of the Law Council of Australia, *Submission 3*, p. 3.

2.6 The Australian Competition and Consumer Commission (ACCC), the independent statutory authority charged with administering the *Competition and Consumer Act 2010* (CCA), advised the committee that in its opinion the introduction of divestiture as a remedy for the misuse of market power would be 'unnecessary at this point of time' as the other remedies already available were adequate.[9] Mr Bruce Cooper, ACCC, informed the committee that the commission recognises that section 46 has deficiencies but they 'go to the law rather than the remedy'. He explained:

> I see the divestiture as a remedy. Once a court has found that a corporation has breached section 46, if a divestiture power were in place, that would be a remedy for that; whereas the ACCC, in its submission to Harper, identified a number of shortcomings in the law which make bringing the section 46 case more difficult in the first place. So it is focused on the law.[10]

2.7 Mr Ben Dolman, Treasury, suggested that a divestiture power 'could be seen as a stronger remedy than those currently available' and acknowledged that one of the arguments in favour of such a power was that 'it would provide a negotiating tool for the regulator'. He stated further, however:

> On the other hand, it is a very different remedy from the other remedies available. When we look at misuse of market power, the current remedies are around changing behaviour and changing the way that the company uses that power, whereas a divestiture power would seek to resolve the issue by changing the market power of the company. So it is a structural remedy designed to influence the structure of the industry rather than to change how that market power is used. That is very different to the way market power has been treated previously in Australia.[11]

2.8 The existence of divestiture powers in other jurisdictions including Canada, the European Union, the United Kingdom and the United States has itself led to calls for similar powers to be introduced in Australia.[12] However, others contend that these powers are not frequently utilised—the Law Council advised that the Canadian and European Union powers have never been used, and the United States power 'has been used only sparingly', with no order other than by consent made since the 1960s.[13]

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9 Mr Bruce Cooper, General Manager, Strategy, Intelligence, International and Advocacy Branch, ACCC, *Proof Committee Hansard*, 2 October 2014, p. 13.

10 *Proof Committee Hansard*, 2 October 2014, pp. 13 and 15.

11 *Proof Committee Hansard*, 2 October 2014, p. 14.

12 For example, this was the case during the inquiry into the dairy industry conducted by this committee in 2011. See Senate Economics References Committee, *The impacts of supermarket price decisions on the dairy industry: Final Report*, November 2011, pp. 107–109.

13 Law Council of Australia, *Submission 3*, p. 4.

2.9 From the evidence received during this inquiry, the committee has identified three categories of key issues relevant when considering a divestiture power for the misuse of market power. The following sections examine these categories in turn.

Key issue 1: How to divest the assets of an established company

2.10 Submissions referred to the difficulties or risks associated with the divestiture of a company's assets. For example, the Law Council argued that divestiture orders involve a serious risk that several less efficient businesses will be created and/or 'involve divesting a part of a business which cannot then be a competitive operation itself'.[14] The following paragraphs consider the uncertainty and risks that submitters argued may accompany the introduction of a divestiture power.

Identifying the assets to be divested

2.11 Proposed subsection 80AD(2) would allow the court to give directions for the 'purposes of securing, within two years of the order being made, a reduction in the corporation's power in, or share of, the market'.[15] Some submissions questioned how the court would make this order. Ms Caroline Coops, Chair of the Law Council of Australia's Competition and Consumer Committee, argued that the proposed subsection would 'have unpredictable consequences potentially creating less efficient businesses and increasing consumer cost'. Ms Coops provided the following reasoning:

> …in reality, business assets are rarely capable of easy dissection. For example, whilst individual grocery stores are easy to identify they need to access wholesale supply and are often reliant on internal distribution centres or external third-party distributors in order to operate efficiently. A major internal distribution centre for a large grocery operation cannot practically be cut in half to keep servicing stores that may be divested; and third-party wholesalers, who are not themselves in breach of the act or a party to the proceedings, cannot be forced to supply them. Brand loyalty, for example, could account for a large market share, but a dominant brand or trademark cannot effectively be shared by two businesses operating in the same market.[16]

2.12 The difficulty in identifying assets that could be divested has also been identified by other inquiries. For example, the 2003 report of the Trade Practices Act Review Committee (the Dawson Report), considered whether a divestiture power should be introduced as a remedy for the misuse of market power. It noted that:

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14 Law Council of Australia, *Submission 3*, p. 3.

15 Schedule 1, item 1, proposed subsection 80AD(2). However, the background discussion in the explanatory memorandum refers only to the reduction of market share. See Explanatory Memorandum, p. 1.

16 Ms Caroline Coops, Chair, Competition and Consumer Committee, Law Council of Australia, *Proof Committee Hansard*, 2 October 2014, p. 1.

> …given that ownership of assets is a passive state, it is difficult to know what the divestiture would be aimed at, whether it be the substantial lessening of competition or the degree of concentration in the market.[17]

2.13 As noted in Chapter 1, a divestiture power is available in the CCA as a remedy for acquisitions that would result in a substantial lessening of competition.[18] The Dawson Report observed that divestiture may be appropriate in this context because any contravention of the CCA would have occurred as a result of recent conduct that consists of the acquisition of identifiable shares or assets.[19] However, the report concluded that extending the remedy of divestiture in Australia to other forms of anti-competitive conduct, such as the misuse of market power, would be 'inappropriate…because there is no clear nexus between the assets to be divested and the contravening conduct'.[20] Treasury and the ACCC advised that this power is rarely used, with the most recent case dating from 1988.[21]

2.14 Courts in the United States have grappled with divestiture and the instances where its application may be appropriate. In *United States of America v Microsoft*, the United States Court of Appeal noted 'divestiture is a remedy that is imposed only with great caution, in part because its long-term efficacy is rarely certain'.[22] This case considered whether divestiture is an appropriate remedy for a unitary corporation. As the following extract of the court's judgment shows, however, divestiture orders in the United States have generally been a response to acquisitions:

> By and large, cases upon which plaintiffs rely in arguing for the split of Microsoft have involved the dissolution of entities formed by mergers and acquisitions. On the contrary, the Supreme Court has clarified that divestiture 'has traditionally been the remedy for Sherman Act violations whose heart is intercorporate combination and control,' du Pont, 366 U.S.

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17 Trade Practices Act Review Committee, *Review of the Competition Provisions of the Trade Practices Act*, 2003, pp. 162–63.

18 Mergers that contravene section 50 or 50A of the CCA or occurred under clearance or authorisation that was granted on false or misleading information. See *Competition and Consumer Act 2010*, ss. 81 and 81A.

19 Similarly, in its submission to this inquiry, Treasury noted that divestiture can be a 'natural solution' to a merger that resulted in a substantial lessening of competition, as 'the pre-merger structural state of the market is a state the court can return to via use of the remedy, though it is not always possible to "unscramble" a transaction post-acquisition'. Even so, Treasury noted in that context the power has been rarely used. Treasury, *Submission 4*, p. 8.

20 Trade Practices Act Review Committee, *Review of the Competition Provisions of the Trade Practices Act*, 2003, p. 162.

21 *Trade Practices Commission v Australia Meat Holdings Pty Ltd* (1988) 83 ALR 299; cited in Treasury, *Submission 4*, p. 8. See also Mr Bruce Cooper, General Manager, Strategy, Intelligence, International and Advocacy Branch, ACCC, *Proof Committee Hansard*, 2 October 2014, p. 12.

22 *United States of America v Microsoft Corporation*, United States Court of Appeals, No. 00-5212, 28 June 2001, www.justice.gov/atr/cases/f257900/257941.htm (accessed 22 August 2014).

> at 329…and that '[c]omplete divestiture is particularly appropriate where asset or stock acquisitions violate the antitrust laws,' Ford Motor Co., 405 U.S. at 573…
>
> One apparent reason why courts have not ordered the dissolution of unitary companies is logistical difficulty. As the court explained in United States v. ALCOA, 91 F. Supp. 333, 416 (S.D.N.Y. 1950), a 'corporation, designed to operate effectively as a single entity, cannot readily be dismembered of parts of its various operations without a marked loss of efficiency.' A corporation that has expanded by acquiring its competitors often has pre-existing internal lines of division along which it may more easily be split than a corporation that has expanded from natural growth. Although time and corporate modifications and developments may eventually fade those lines, at least the identifiable entities pre-existed to create a template for such division as the court might later decree. With reference to those corporations that are not acquired by merger and acquisition, Judge Wyzanski accurately opined in United Shoe:
>
> *'United conducts all machine manufacture at one plant in Beverly, with one set of jigs and tools, one foundry, one laboratory for machinery problems, one managerial staff, and one [labour] force. It takes no Solomon to see that this organism cannot be cut into three equal and viable parts'*.[23]

2.15 During the committee's public hearing, another United States case was cited—the 1910 Standard Oil judgement that resulted in the divestiture of the oil companies within Standard Oil. Although the prosecution occurred 'under a section 46 equivalent', Mr William Reid, a member of the Law Council's Competition Committee, explained that the case is more applicable when considering anti-competitive mergers and acquisitions rather than the conduct of a unitary corporation:

> [A]s I understand the history of it, Standard Oil was an aggregation of many small oil companies and the court was really looking to disaggregate that which had been aggregated rather than to dissect an existing business which had grown organically.[24]

2.16 Similarly, the Law Council argued it would be difficult for the court to make a divestiture order in any of the section 46 cases the ACCC has previously taken.[25]

Outcomes following the divestiture process

2.17 One of the risks associated with a divestiture process is that divestiture necessarily involves some form of 'industry engineering'. The Law Council argued

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23 *United States of America v Microsoft Corporation*, United States Court of Appeals, No. 00-5212, 28 June 2001.

24 Mr William Reid, Member, Competition and Consumer Committee, Law Council of Australia, *Proof Committee Hansard*, 2 October 2014, p. 5.

25 Law Council of Australia, *Submission 3*, p. 4. These cases involved a steel manufacturer, a power distribution business, a street directory publisher and a rural newspaper publisher.

that this process would result in 'wider competitive impacts across the relevant market(s)'. In particular, the consequences of a divestiture power being applied to a market with more than one large firm were alluded to—the Law Council noted that other firms may potentially acquire substantial market power as a result of forced divestiture.[26] Indeed, the committee has previously heard that in the United States the divestiture power is a remedy for monopolisation.[27]

2.18 The previous section discussed some of the potential complications associated with the forced divestiture of a company's assets to meet a certain market power or market share threshold. However, the Law Council added that the drafting used in the bill 'introduces further uncertainty and complexity' to the general concept of what divestiture involves as the process envisaged by the bill is not clear. Proposed subsection 80AD(2) states that the court's directions must be 'for the purpose of securing' a reduction in market power or share', which the Law Council argued only indirectly provides for the divestiture of assets'. The Law Council wrote:

> How is one to tell whether a particular directed course of conduct for the corporation will have—let alone, assuredly achieve—the 'purpose of securing' the required reduction in (market) power or share?[28]

2.19 The Law Council speculated that the courts would approach this requirement by either:

- endeavouring to identify assets (physical, real or intangible) to be divested by the business, for the purpose of achieving a reduction in market power or share; or
- ordering that the corporation reduce its market share to a particular level.[29]

2.20 The first option presents the issues discussed in paragraphs 2.11–2.13. However, if the court followed the second option and left the divestiture to the corporation,[30] the Law Council questioned what the consequences of that would be:

> If [the corporation] is simply to withdraw from a market or to reduce its output, this is likely (by definition, given that the corporation has substantial market power) to result in, or to sustain, an increase in prices and/or reduced availability of the relevant product(s). These are not the usual objectives of effective competition regulation. If the corporation is to invite its competitors to win business it would otherwise pursue, the

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26 Law Council of Australia, *Submission 3*, p. 3.

27 Mr Brian Cassidy, Chief Executive Officer, ACCC, *Senate Economics References Committee Hansard*, Inquiry into competition in the Australian banking sector, 25 January 2011, p. 56.

28 Law Council of Australia, *Submission 3*, p. 5.

29 Law Council of Australia, *Submission 3*, p. 5.

30 Proposed subsection 80AD(5) would allow the court to accept an undertaking by the corporation to take particular action to reduce its market power or share as an alternative to a court order.

> corporation will contravene the cartel prohibitions. Ultimately also, reduced market share is a relative concept—to achieve it, the corporation's competitors, practically, must respond with increased output if demand remains constant.[31]

2.21 The Australian National Retailers' Association (ANRA) argued that a divestiture provision could not guarantee the business being divested would be purchased. It remarked that 'divestiture forces sales; it cannot compel purchases'.[32]

Implications for the courts and ACCC

2.22 Submissions questioned the role that the courts and the ACCC would be expected to perform under the proposed amendments. ANRA expressed two key concerns. First, ANRA emphasised that the courts and the ACCC 'have no experience in how to split up companies'. Second, ANRA argued that a range of factors in addition to competition need to be considered:

> Divestiture can result in significant economic harm through the loss of economies of scale and scope, which in turn could flow through to consumers in the form of higher prices. It can impose significant losses on investors, and jeopardise jobs and wage levels. There is a real risk that the outcomes of forced divestiture would be at the worst end of the scale for shareholders, employees, customers and communities.[33]

2.23 Ms Caroline Coops, Law Council of Australia, maintained that 'the way markets operate and the assets that businesses need to operate effectively can be complicated. Further:

> …it is difficult to predict in any given circumstance whether an order to divest an asset or a store will in fact give rise to a more pro-competitive environment than existed previously. We see it as quite difficult for a court to craft orders that have that effect or to supervise the ongoing outcomes of those orders so as to achieve the objective of the bill.[34]

2.24 Elaborating on this matter of supervision, the Law Council claimed that a divestiture order would involve the imposition of 'ongoing, supervising behavioural orders on the firm(s) involved' such as orders in relation to how the newly formed businesses may deal with one another and/or their former parent corporation.[35] Mr Joe Silver, a co-chair of the Law Institute of Victoria's Young Lawyers' Law Reform Committee, advised that his organisation is concerned the amendment proposed by the bill (i.e. the insertion of a subsection 80AD) 'invites the courts to take

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31 Law Council of Australia, *Submission 3*, pp. 5–6.

32 Australian National Retailers' Association, *Submission 2*, p. 3.

33 Australian National Retailers' Association, *Submission 2*, p. 4.

34 *Proof Committee Hansard*, 2 October 2014, p. 3.

35 Law Council of Australia, *Submission 3*, p. 4.

an overly interventionist role both in the marketplace, and more problematically in the management of certain corporations'. Mr Silver continued:

> In all likelihood, the courts will have similar concerns regarding section 80AD, as despite concerning competition (rather than management), it too anticipates becoming involved in the day-to-day management of businesses, and not insubstantial ones at that, particularly because it would involve the effective creation of new businesses. While perhaps not as involved as 'unbaking' a cake (separating it back into its ingredients), it is not simply about reversing how the corporation actually built its market share. It is about reshaping the market. That will occur regardless of what resources the ACCC can make available. For a divestment to be equitable and viable, comprehensive modelling is needed for any new entities proposed, as well as an understanding of how the existing market structure, and how the realignment, would impact upon it. Analysis of how it would affect the complying entity, as well as other stakeholders in the supply chain, would also be needed.[36]

2.25 In addition to the challenges that the court would likely face in developing feasible divestiture orders, there are also possible implications for the court process. Treasury noted that the report of the 1993 inquiry into competition policy (Hilmer Report) concluded divestiture would affect the court process by involving the courts 'in a process with inevitable political implications' that was 'more appropriate for decision by governments than by the courts'.[37] At the committee's public hearing, a representative of the Law Council's Competition Committee similarly argued that, in his personal view, although he was not against divestiture in principle, such a decision should be made by the Parliament rather than by the judiciary.[38]

2.26 If the bill were passed, the ability of the court to consider in a timely manner both the questions before it regarding section 46 and then, in the event of a contravention being found, any divestiture proposals that may follow was also queried. Treasury noted that the Hilmer Report believed a divestiture process 'may be administratively expensive and lack timeliness, particularly as companies accused of misuse of market power may be expected to defend allegations and appeal decisions vigorously'.[39] It is evident that section 46 cases are already likely to be considered over a prolonged period of time—a witness from the ACCC advised that litigation generally takes 'several years' to reach the judgment stage. As a specific example, the witness noted that in the ACCC's current section 46 litigation against

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36 Mr Joel Silver, *Submission 1*, pp. 4–5

37 Independent Committee of Inquiry into Competition Policy in Australia, *National Competition Policy*, 1993, p. 164; cited in Treasury, *Submission 4*, p. 9.

38 Mr William Reid, *Proof Committee Hansard*, 2 October 2014, p. 5.

39 Treasury, *Submission 4*, p. 9.

Cement Australia,[40] the conduct occurred in 2003 with the final court hearing expected in December 2014.[41] Similarly, Mr Silver of the Law Institute of Victoria's Young Lawyers' Law Reform Committee noted that although the proposal is 'no doubt intended as an extraordinary measure', if enacted and pursued it 'would represent a drain on limited court resources'.[42] The United States experience appears to support this reasoning; the Law Council provided the following example indicating that even in instances where a divestiture order was made by consent the process was not straightforward:

> In the 1980s, AT&T was broken up into the 'Baby Bells' by consent decree, to end long-running litigation with the US government. However, then followed years of litigation (over 900 petitions) in relation to the 'line of business' restrictions in the consent decree.[43]

Other potential adverse economic consequences

2.27 The Dawson Report suggested that making a corporation with market power susceptible to forced divestiture would 'create an uncertain business environment'.[44] Treasury also cited relevant findings of the Hilmer Report that highlighted potential broader economic consequences. They included that divestiture may 'involve reshaping an entire industry with consequent disruption to all who deal with it' and eliminate economies of scale, with the smaller firms constructed by the courts 'less efficient and perhaps not even economically viable, detracting from economy-wide productivity'.[45]

2.28 ANRA argued that 'artificial and arbitrary limits' on market share in the grocery sector would 'most likely mean ownership would be taken up by new entrants from overseas, with profits going offshore'.[46] ANRA suggested, however, that this reasoning may not apply to regional areas, and that these areas could be disadvantaged if a divestiture order was made in relation to the grocery sector. Depending on the nature of the divestiture order, ANRA argued that 'smaller regional stores would probably be sold first, and would be more unlikely to be purchased by any new entrants'. According to ANRA, this is because the operation of regional stores involves higher transport costs and lower turnover, and does not appear to otherwise

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40 *Australian Competition and Consumer Commission v Cement Australia Pty Ltd* [2014] FCA 148.

41 Mr Bruce Cooper, General Manager, Strategy, Intelligence, International and Advocacy Branch, ACCC, *Proof Committee Hansard*, 2 October 2014, p. 12.

42 Mr Joel Silver, *Submission 1*, p. 4.

43 Law Council of Australia, *Submission 3*, p. 4.

44 Trade Practices Act Review Committee, *Review of the Competition Provisions of the Trade Practices Act*, 2003, pp. 162–63.

45 Independent Committee of Inquiry into Competition Policy in Australia, *National Competition Policy*, 1993, p. 164; cited in Treasury, *Submission 4*, p. 9.

46 Australian National Retailers' Association, *Submission 2*, p. 3.

fit into the strategies of the two large international operators Aldi and Costco, which are focused on large population centres.[47]

Key issue 2: Would a divestiture power be a justified and proportionate response to a contravention?

2.29 It is clear that divestiture would be a serious penalty. Treasury stated that if a divestiture power was introduced into the current CCA 'it would likely be perceived as sitting at the high end of this framework of remedies, being a more severe penalty than most pecuniary penalties, compensation orders or injunctions'.[48]

2.30 It is useful to consider whether the current penalties are inadequate. The current penalties were outlined in Chapter 1 (see paragraphs 1.18–1.19). ANRA noted that these penalties were significant, and suggested there 'is no demonstrated evidence that Australian courts have had insufficient remedies available to address misuse of market power'. Further, ANRA argued that a divestiture power 'would not be consistent with the concept of a proportional penalty being imposed for breaches of competition law'.[49]

2.31 Another suggestion was that a divestiture power could be considered arbitrary. Treasury noted that this is one of the arguments commonly made against a divestiture power as the effects of a divestiture order are 'unrelated to the nature of the contravention'.[50] The Law Council argued that 'in the absence of a clear and direct nexus between the contravention and the assets to be divested', there would be a risk the divestiture would not appropriately address the conduct which led to the contravention.[51] ANRA also noted that the bill does not detail or limit the extent of divestiture that the court could order.[52]

2.32 The potential repercussions for individuals not directly involved in the contravention were noted. ANRA argued that divestiture 'unambiguously destroys shareholder wealth' and could affect 'millions of Australians [who], through superannuation funds, have investments in prominent and successful Australian-owned companies'. ANRA also suggested that divestiture would have implications for employees. It cited the the grocery sector, maintaining that disruption to employment 'would be significant and severe if major supermarkets were forced to close stores to reduce their market share'. ANRA argued this was possible because:

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47 Australian National Retailers' Association, *Submission 2*, p. 3.

48 Treasury, *Submission 4*, p. 8.

49 Australian National Retailers' Association, *Submission 2*, pp. 2–3.

50 Treasury, *Submission 4*, p. 9.

51 Law Council of Australia, *Submission 3*, p. 4.

52 Australian National Retailers' Association, *Submission 2*, p. 3.

> There is no guarantee the business model of any new entrants to the sector would replicate the jobs currently provided by the major supermarkets, or that existing retail outlets would necessarily be bought up.[53]

Key issue 3: Are the proposed amendments the best remedy to perceived market issues?

2.33 In his second reading speech, Senator Xenophon drew attention to the fact that that the grocery retail sector was one of the sectors noted in the explanatory memorandum. Submissions also referred to the grocery retail sector. For example, SPAR Australia, a grocery wholesaler supplying independent retailers, contended that the grocery market is not operating effectively. SPAR argued that small businesses are one of the biggest employers and wealth creators in Australia, yet 'in the retail sector they are becoming increasingly extinct, with anti-competitive, market abuse behaviour a key driver of their extinction'.[54] SPAR concluded:

> Coles and Woolworths continue to dominate the retail sector and Metcash continues to dominate the wholesale independent sector, with the ultimate loser being the Australian consumer with small independent family owned business being collateral damage along the way.[55]

2.34 ANRA expressed an opposing view. It rejected concerns about the current state of the grocery sector and suggested recent inquiries that have considered the sector have found competition 'is vibrant and vigorous'.[56]

2.35 A potential benefit of a divestiture power for the misuse of market power is that corporations with substantial market power (or share) may be deterred from engaging in misconduct due to the risk of the serious penalty of mandatory divestiture being imposed. Nevertheless, those who consider that the competition law has not prevented abuses of market power from occurring, were unconvinced that the proposed amendments contained in the bill would assist. This is because the proposed amendments only address the penalties available for a contravention of section 46; any difficulties associated with the investigation and successful pursuit of a section 46 case remain.

2.36 Indeed, the one submission the committee received in support of the bill, from SPAR Australia, observed that while it considers providing the courts with an additional remedy would be 'a good thing', the amendments 'would appear to be

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53 Australian National Retailers' Association, *Submission 2*, p. 3.

54 SPAR Australia, *Submission 5*, p. [4].

55 SPAR Australia, *Submission 5*, p. [2].

56 Australian National Retailers' Association, *Submission 2*, p. 1.

potentially meaningless given the enforcement actions taken by the ACCC under section 46 have been minimal'.[57] SPAR explained that between 1974 and 2012, the ACCC had only prosecuted 18 cases alleging a contravention of section 46 and was only successful in 11 of these cases. SPAR concluded:[58]

> …either the law is deficient in regards to section 46, or the ACCC is deficient in not seeking to litigate more cases under 46.[59]

2.37 Accordingly, SPAR encouraged the committee to consider 'the issue of the failure of section 46 to prevent ongoing market abuse practices in the Australian marketplace'.[60] Similarly, the chief executive officer of Master Grocers Australia and Liquor Retailers Australia, Mr Jos de Bruin, described section 46 as 'inadequate'. Mr de Bruin also argued that specific provisions targeting anti-competitive price discrimination should be reintroduced, in an amended form.[61]

2.38 The effectiveness of section 46 is a debate already occurring elsewhere as part of the current Harper Review. In its submission to the Harper Review's issues paper, the ACCC called for amendments to subsection 46(1) to ensure the prohibition 'is effective in prohibiting anti-competitive conduct by firms with substantial market power'. The ACCC endorsed the insertion of an 'effects' test to complement the 'purpose' test, as well as amendments to overcome limitations with the application of the 'take advantage' concept.[62]

The Harper Review's September 2014 draft report

2.39 The Harper Review's draft report was released on 22 September 2014. In this draft report, the review panel did not express support for a divestiture power for contraventions of section 46; rather it concluded that the existing range of remedies is sufficient. The following comments were made:

> While reducing the size of a firm may limit its ability to misuse its market power, divestiture is likely to have broader impacts on the general efficiency of the firm. Such changes could also have negative flow-on

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57 SPAR Australia, *Submission 5*, p. [6].

58 SPAR Australia, *Submission 5*, p. [6]. Private enforcement of section 46 is available and has occurred in a number of cases.

59 SPAR Australia, *Submission 5*, p. [6].

60 SPAR Australia, *Submission 5*, p. [7].

61 Mr Jos de Bruin, Chief Executive Officer, Master Grocers Australia and Liquor Retailers Australia, *Proof Committee Hansard*, 2 October 2014, p. 9.

62 It is envisaged an effects test would capture conduct that had the effect or likely effect of substantially lessening competition, but could not be shown to have been for one of the three proscribed purposes. See ACCC, Submission to the Competition Policy Review, June 2014, http://competitionpolicyreview.gov.au/files/2014/06/ACCC.pdf (accessed 20 August 2014), pp. 76–80. See also *Proof Committee Hansard*, 2 October 2014, p. 13.

> effects to consumer welfare. It is also possible that divested parts of a business might be unviable.
>
> The Panel considers that the existing range of remedies is sufficient to deter a firm from misusing its market power and to protect and compensate companies that have been harmed by such unlawful conduct.[63]

2.40 The Harper Review is, however, considering whether the current misuse of market power prohibitions are adequate. The review's draft report indicated support for the insertion of an effects test in section 46 subject to a defence that the action 'would be a rational business decision or strategy by a corporation that did not have a substantial degree of power in the market' and 'the effect or likely effect of the conduct is to benefit the long-term interests of consumers'.[64]

2.41 The Harper Review panel's final report to the government is expected to be finalised by the end of March 2015.

Committee view

2.42 Australian consumers benefit when the competitive process in markets functions well and practices that harm competition are addressed. The committee understands that some parts of the community are concerned about the market power or share certain firms have in the markets in which they operate. The committee also understands that some consider the competition law is not effectively deterring or addressing misuses of market power. Indeed, the ACCC was of the view that there were deficiencies in section 46.[65]

2.43 Even so, the committee does not consider a convincing case has been made for the introduction of a divestiture power as a remedy for the misuse of market power. Evidence has not demonstrated that the potential advantages of such a power would outweigh the likely disadvantages. In particular, the evidence received by the committee was compelling in questioning the courts' ability to 'fix' perceived problems with a market by ordering that certain assets of a large, complex and unified business organisation be divested. The committee is concerned that court-ordered divestiture would risk significant disruption and economic damage, with unpredictable consequences for competition.

2.44 In the committee's view, the evidence available suggests that the debate about section 46 should be focused on whether the prohibitions contained in it are effective, not whether further penalties need to be available. The committee notes this is the approach that appears to have been taken by the current independent review of

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63 Competition Policy Review, *Draft Report*, http://competitionpolicyreview.gov.au/files/2014/09/Competition-policy-review-draft-report.pdf (accessed 22 September 2014), p. 211.

64 Competition Policy Review, *Draft Report*, http://competitionpolicyreview.gov.au/files/2014/09/Competition-policy-review-draft-report.pdf (accessed 22 September 2014), p. 44.

65 *Proof Committee Hansard*, 2 October 2014, pp. 13 and 15.

competition policy being chaired by Professor Ian Harper. The Harper Review provides an opportunity for a thorough and holistic examination of competition policy, and the committee awaits the Harper Review's final report with great interest.

Recommendation 1

2.45 The committee recommends that the Senate not pass the bill.

Senator Sean Edwards
Chair

Dissenting Report by Senator Nick Xenophon

Competition laws – the butter knife needs to be replaced with a sword of Damocles

1.1 Australia's competition policy is in need of urgent repair. The fact that we can find ourselves in a position where two retailers control approximately 75 percent of the grocery market clearly demonstrates that the remedies available under the *Competition and Consumer Act 2010* (CCA) do little to deter anti-competitive behaviour. The Competition and Consumer Amendment (Misuse of Market Power) Bill 2014 aims to give the courts the power to order the divestiture of a corporation where that corporation has misused its market power. The effect of this bill would be a powerful disincentive for corporations to abuse their market power.[1]

1.2 It is therefore incredibly disappointing the committee recommended this bill not be passed. While the majority report analysed the effect of the bill and the practical consequences of a divestiture power, the committee failed to examine the state of competition in Australia's retail markets. By not examining why and how a handful of corporations have been able to establish such wide reaching control over our retail markets, we are leaving ourselves vulnerable to higher prices and less variety in goods and services in the long run.

Australia's retail sector

1.3 The current state of the Australian retail sector was described by the Master Grocers Association in its submission to the inquiry:

> The retail ownership landscape in Australia has changed dramatically over the past 30 years. Small businesses, particularly independent retailers, have been faced with the ever increasing threat and challenge of two giant supermarkets, Coles and Woolworths, growing at an unabated pace, using their ever increasing market power and dominance to crowd out existing retailers and to block out new competition. Nowhere else in the world is there such a hyper – concentration of two massive supermarket retailers![2]

1.4 MGA's submission continued:

> It is highly questionable that the growth of Coles and Woolworths is simply due to the allegedly greater expertise, business acumen and skills they exercise in the market place. It is the effect of oversaturation of areas with numerous stores that results in the crowding out of their competitors where

1 Explanatory Memorandum, p. 2.

2 Master Grocers Australia, *Submission 6*, p. 5.

> in most circumstances there is ample room for the larger and smaller stores to compete on a level playing field.[3]

1.5 Australian competition policy is failing to keep pace with the increasing presence of anti-competitive behaviour and the serious consequences that flow on from this, both for consumers and businesses alike.

The case for reform

1.6 A well-known example of the market power of the 'big 2' supermarkets was the milk price war in 2011 when Coles announced it was selling Coles brand regular and low fat milk for $1 a litre. Woolworths followed suit immediately, also cutting the price of its home brand milk. Other retailers cut prices soon after.

1.7 More recently Woolworths has begun selling its home brand bread for 85 cents a loaf. This move will has already put great pressure on independent bakers and supermarkets who cannot compete with bread being sold at what appears to be below the cost of production. The impact of selling bread for 85 cents per loaf on the retail industry was explained by Mr Jos de Bruin, Chief Executive Officer of Master Grocers Australia, during the committee's public hearing on 2 October 2014:

> **Mr de Bruin:** … we believe that (anticompetitive price discrimination) is a misuse of market power. It creates what we call a 'waterbed effect': the cheaper the chains buy a product for, the higher the price it is for anyone else to buy. Call it whatever you wish, whatever technical term they use around trading terms—'promotional buys', 'scan deals', 'volume', 'settlement discounts'—it does not matter: there is a strict net cost that they arrive at and ultimately it is the smaller people that pay here.
>
> **Senator XENOPHON:** Just further to that, a practical example is the issue of the 85c bread. I have spoken to a number of your members. I spoke to the Asplands up in Townsville who have been speaking about this nationally. You cannot buy bread, even some of your bigger members do not get bread, anywhere within cooee of 85c. There is the fear that, whatever the big bakeries are providing the bread at, if it is 85c, it does have a waterbed effect in for Coles and/or Woolies to get it that cheap means that other retailers in the supply chain have to pay more? Is that what you are saying?
>
> **Mr de Bruin:** I cannot tell you how many phone calls, emails, texts I have had about bread in the last week. It was absolutely in override last week. Clearly our members around Australia see this behaviour as predatory—predatory because there is a sense that Woolworths and Coles are not losing a cent. They claim they may be and if they are they are cross subsidising it with additional margins in store. Our members have said, 'Yes, well, they will make a decision in their own right whether they match it or not.' But when they match it they will be losing a minimum of 35c a loaf and in volume terms in grocery terms that is a massive amount of margin that

3 Master Grocers Australia, *Submission 6*, p. 8.

> comes out of their business that will affect employment and will affect their business in ways that Woolworths and Coles would not understand. The consumer does seek cheap bread out there. I am not sure that the consumer actually sees what the ramifications of that cheap bread may be in the medium to long term. But, as I said before, we do view it as predatory. It may be legal but we believe it is immoral.[4]

1.8 SPAR Australia Ltd in its submission to this inquiry confirmed concerns regarding the level and concentration of market power in Australia's retail industry:

> The issue of misuse of market power is one that SPAR has first-hand experience of in terms of suffering commercially from market power abuse and seeing first-hand the total incapacity of the current legislative and regulatory framework to address it.
>
> It is interesting to note that since the 2008 Grocery Inquiry conducted by the ACCC and its examination of the retail grocery market and the power of the two supermarket chains Coles and Woolworths and the power of Metcash as a wholesale provider to the independent sector, not much if anything has changed.
>
> Coles and Woolworths continue to dominate the retail sector and Metcash continues to dominate the wholesale independent sector, with the ultimate loser being the Australian consumer with small independent family owned business being collateral damage along the way.[5]

1.9 SPAR's submission also pointed out the unmistakable truth: sections 46(1) and 46(1AA) of the CCA do not go far enough to prevent anti-competitive conduct. Section 46 prohibits the misuse of market power, stating:

> (1) A corporation that has a substantial degree of power in a market shall not take advantage of that power in that or any other market 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.

1.10 Section 46(1AA) on the other hand prohibits a corporation that has a substantial market share from supplying or offering to supply 'goods or services for a sustained period at a price that is less than the relevant cost to the corporation of supplying such goods or services' for the same purposes as those listed in section 46(1).

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4 Mr Jos de Bruin, CEO, Master Grocers Australia, *Proof Committee Hansard*, pp. 9–10.

5 SPAR Australia Ltd, *Submission 5*, p. 3.

1.11 The Harper Review has already identified the limits of requiring proof of the purpose of damaging a competitor and the 'effects test' would be a much needed reform. The draft report released by the Harper Review explains the arguments in favour of an 'effects test':

> As a matter of policy, competition law ought to be directed to the effect of commercial conduct on competition, not the purpose of the conduct, but it is the anti-competitive effect of the conduct that harms consumer welfare; and
>
> As a matter of practicality, there can be difficulties in proving the purpose of commercial conduct because it involves a subjective enquiry, whereas proving anti-competitive effect is less difficult because it involves an objective enquiry.[6]

1.12 The draft report also makes the following proposition in relation to reforming section 46:

> The Panel proposes that the primary prohibition in section 46 be re-framed to prohibit a corporation that has a substantial degree of power in a market from engaging in conduct if the proposed conduct has the purpose, or would have or be likely to have the effect, of substantially lessening competition in that or any other market.[7]

1.13 In that context, this amendment would be even more effective if an effects test was implemented. To date, even where anti-competitive conduct has been identified, prosecutions by ACCC have been few and far between with only 18 cases brought in the past 38 years. Successful prosecutions are even fewer and further between, with the courts siding with the ACCC in only 11 of the 18 cases.[8]

1.14 While enforcement of these provisions is an issue, one must also question whether the penalties currently available under the CCA are sufficient to deter anti-competitive conduct. Many submitters to this inquiry quite rightly pointed out that divestiture of a corporation is not a straightforward matter and that it would have large scale ramifications on the business operations of a corporation. Ms Caroline Coops of the Law Council of Australia explained to the committee:

> …business assets are rarely capable of easy dissection. For example, whilst individual grocery stores are easy to identify they need to access wholesale supply and are often reliant on internal distribution centres or external third-party distributors in order to operate efficiently. A major internal

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6 Competition Policy Review, *Draft Report*, September 2014, http://competitionpolicyreview.gov.au/files/2014/09/Competition-policy-review-draft-report.pdf (accessed 25 February 2015), p. 206.

7 Ibid, p. 210.

8 Ibid, p. 210.

> distribution centre for a large grocery operation cannot practically be cut in half to keep servicing stores that may be divested.[9]

1.15 However, the threat of divestiture would act like the sword of Damocles in that a corporation would be even more wary of abusing its market power with a potential divestiture sanction. Given the state of our grocery sector in Australia (as well as other sectors with high concentrations of market power), the penalties available under the CCA are acting as more of a butter knife than a sword. They are more of an inconvenience or nuisance and do little to discourage large corporations from abusing their market power.

1.16 The fact that similar divestiture powers exist overseas in the United States, Canada, the European Union and the United Kingdom demonstrates other jurisdictions take addressing anti-competitive behaviour seriously. It is true that to date these powers have only been exercised by consent in the US and have not been exercised at all in the EU and Canada. However, I do not accept that this means these powers are not useful as demonstrated in my discussion with Mr William Reid from the Law Council of Australia during the committee's public hearing:

> **Senator XENOPHON:** …In the EU and Canada these laws have been in place for a number of years but have not been used. I do not know whether you have had the opportunity to do research on this but do you consider that simply having such a law on the statute books would act as a sword of Damocles? When a large corporation is managing risk, would it think not only could it cop a fine but the court, if it is so minded, could order a divestiture which would be incredibly painful and messy for the corporation?
>
> **Mr Reid:** I am not aware of research that has been done in relation to that. In Europe, of course, there is a different situation from our own in that the regulator imposes the penalty and makes the initial decision in relation to a contravention. The regulator has never done that. In that context, one might assume that businesses in Europe do not seriously consider it a threat in relation to dealing with the regulator, its track record having been never to have imposed this sanction. Perhaps there is more uncertainty in our system. Where a court is invested with this power and has it at its disposal, that may remain a more credible threat for business into the future than would be the case otherwise.[10]

1.17 There is an increasing groundswell of public opinion including from the small and medium business sector to see meaningful reform in the area of Australia's competition policy. A divestiture power should be an integral element of such a reform package. Whilst I acknowledge there are some concerns about this bill, I believe it is necessary for it to be passed in order to protect the long term interests of

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9 Ms Caroline Coops, Chair, Competition and Consumer Committee, Law Council of Australia, *Proof Committee Hansard,* p. 1.

10 Mr William Reid, Member, Competition and Consumer Committee, Law Council of Australia, *Proof Committee Hansard,* p. 4.

Australian consumers and small businesses. This bill, if passed, will irrevocably change the corporate culture of some large corporations for the better.

Recommendation

1.18 That the bill be passed.

Senator Nick Xenophon
Independent Senator for South Australia

Additional Comments by Senator Canavan

1.1 The committee notes concerns within the community about the misuse of market power by large corporations and the limitations in existing competition law in effectively deterring or addressing such behaviour (2.42). I wish to add my voice to these concerns. The important role that competition plays in promoting productivity and innovation in the Australian economy means that ensuring Australia has a strong and effective competition laws should remain an ongoing focus for policymakers.

1.2 In my view, competition in Australian markets would be strengthened through including divestiture as a potential remedy for a breach of section 46 of the *Competition and Consumer Act 2010*. This change is required because:

- the existing penalties are not sufficient to deter serious breaches of competition laws;
- claims that its introduction would introduce undue business certainty do not stack up against the extensive overseas experience of divestiture penalties; and
- a divestiture remedy would only be used in cases of serious misconduct and it was a practical remedy given the nature of the markets under consideration.

1.3 Of particular importance is ensuring regulators have a sufficient range of tools, with appropriate powers to investigate and, where appropriate, penalise and remedy situations where competition is damaged. Of relevance are the cases brought by the Australian Competition and Consumer Commission (ACCC) last year against Coles which exposed the serious nature of the misconduct that has been taking place in Australia's retail sector. The Federal Court judgement concluded that Coles gravely misused its bargaining power. It found Coles demanded payments from suppliers to which it was not entitled by threatening to harm their business and withheld money from suppliers it had no right to withhold. The Court concluded that 'Coles' practices, demands and threats were deliberate, orchestrated and relentless.'[1]

1.4 The penalty given to Coles of $10 million, the maximum allowable under the existing arrangements, was insufficient. In particular, Federal Court judge Justice Gordon stated that the penalties should have been higher in part to provide an 'important element of deterrence' to others, noting:

> I don’t regard these penalties at the top end for these proceedings at all … This conduct could have attracted considerably higher penalties. You are

1 ACCC, *Court finds Coles engaged in unconscionable conduct and orders Coles to pay $10 million penalties*, 22 December 2014, Media Release.

> dealing with a company worth $22 billion on one side and the smallest supplier worth less than 0.1 per cent of that on the other.[2]

1.5 The Coles example does not, of course, provide prima facie justification for the introduction of a divestiture power in Australian competition policy laws. For one, this case involved a breach of unconscionable conduct provisions (section 20 of the Australian Consumer Law) not the misuse of market power provisions (section 46) that Senator Xenophon's bill deals with. Nonetheless, the brazen misconduct revealed in this case highlighted the need for stronger deterrents to broader issues of anti-competitive conduct covered by the *Competition and Consumer Act 2010*.

1.6 Further, the gravity of the revelations made by the ACCC in this case raises the question as to whether the existing competition policy framework may need to be augmented either now, or in the future, so that it can respond effectively and in a manner proportionate to the significance of the infringement. The importance of regulators having a sufficient range of enforcement tools to be able to respond to compliance breaches in a proportionate way was highlighted by the Productivity Commission in a recent study.[3]

1.7 A major reason provided to this inquiry for opposition to the introduction of divestiture powers are the potential loss to economic efficiencies, in particular economies of scale, that deliver positive outcomes to consumers as well as increasing the overall productivity of the economy. This is an important point. But it does not, of itself, rule out the use of a divestiture mechanism in some instances.

1.8 Clearly any use of divestiture powers would be an extraordinary measure and would only be appropriate in the most serious circumstances and for industries with particular market structures. This is borne out by the international experience highlighted in the committee's report. The use of such powers in jurisdictions where they exist, such as the United States, highlights that, notwithstanding the deterrent effect, they are in practice not often used. And when they are, real world economic imperatives mean they are used for industries that have a high degree of vertical integration. These include telecommunications, electricity and energy markets with clear points of division within businesses.

1.9 Another point to note is that the trigger for the consideration that a misuse of market power has occurred, under section 46, explicitly rules out behaviour by a firm — even one with substantial market power — that in the normal course of events would reasonably be undertaken to improve its efficiency of operations. Hence, beneficial activities undertaken to exploit economies of scale to reduce business costs, such as consolidation etc., would be unaffected by a divestiture provision. A business

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2 Mitchell and Durkin, *Coles to settle unconscionable conduct cases with ACCC*, Financial Review, 15 December 2014.

3 Productivity Commission, *Regulator Engagement with Small Business*, Research Report, 2013.

acting in a manner consistent with competitive behaviour would not breach section 46 and therefore would not be liable to a penalty of divestiture under this amendment.

1.10 More broadly, the possible adverse impact of divestiture provisions in terms of impacts on economic efficiency, such as reductions in economies of scale, logistical difficulties in divesting particular businesses, including the potential unviability of divested parts of a business, disruption to a firm or industry's activities, as well as the impacts on investment due to regulator risk and uncertainty need to be considered against the costs to economic activity and efficiency that are already occurring due to misuse of market power.

1.11 A point that cannot be overstated is that competition is the driving force for economic growth, dynamism and innovation in any economy. The very existence of competition laws recognises this fact. Hence, a substantial weakening of competition invariably extracts a heavy price on an economy, on consumers, businesses and workers. To take one example, the potential dampening role played on the investment plans of small firms or potential new market entrants by the actions of an incumbent with extensive market power must also be considered. Firm entry and exit is an important factor in economic efficiency over time.

1.12 Analysis by the Productivity Commission confirms that productivity growth 'arises from many small, everyday improvements within organisations to improve the quality of products, service customers better, and reduce costs.'[4] The Commission highlighted three policy 'planks' for driving and stimulating innovation — incentives, flexibility and capabilities. In emphasising the crucial role of competition as providing the first of these planks, the Chairman of the Commission Gary Banks observed:

> International evidence suggests that it is market competition, rather than government assistance, that is the main driver of innovation and its diffusion throughout an economy.[5]

1.13 As always, the question of when the employment and use of pro-competition policies and instruments is appropriate hinges on the likely balance of costs and benefits in particular circumstances. These are empirical questions. And, as such, consideration of whether a divestiture power is appropriate cannot be ruled out on grounds of the potential adverse impact on economic efficiency per se. Any arguments would need to be argued based on evidence rather than asserted.

1.14 Further, some of the arguments used against divestment on practical grounds, such as the concerns raised by the Law Council about the lack of certainty about what could be achieved, are not in themselves reasons to rule out divestment as a possible policy tool. All policy actions have degrees of risk and the potential for unintended

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4 Productivity Commission, *Annual Report 2007–08*, 2008.

5 Productivity Commission, *The Productivity Challenge and Innovation,* Media Release, 31 October 2008.

consequences. Many are highly complex and involve substantial risks that must be managed.

1.15 That there are many logistical and practical issues associated with implementation of divestiture powers is not in dispute. As the committee report has highlighted, identifying the assets to be divested and monitoring outcomes following the divestiture process will not be easy. But as with other aspects areas of competition policy, these are issues that would need to be worked out over time through the courts and mediation processes.

1.16 On balance, I believe that the *Competition and Consumer Act 2010* should be amended to include a divestiture remedy for breaches of the misuse of market power provisions. Nonetheless, the bill as drafted by Senator Xenophon should be amended to take into account the issues raised during this inquiry about its impact on business certainty. In particular, the bill should be amended to ensure that the remedy would only be used for serious and repeated breaches of section 46 and that a Court applying the remedy would consider the efficiency and competitiveness of any business entities formed following a divestment notice.

Senator Matthew Canavan
Nationals Senator for Queensland

APPENDIX 1

Submissions received

Submission Number	Submitter
1	Mr Joel Silver
2	Australian National Retailers Association
3	Law Council of Australia
4	The Treasury
5	SPAR Australia Limited
6	Master Grocers Australia
7	South Australian Independent Retailers
8	Mr Angelos Kenos

Tabled documents

- Opening statement tabled by the Law Council of Australia at a public hearing held in Canberra on 2 October 2014.

Answers to questions on notice

- From a public hearing held in Canberra on 2 October 2014, received from the Australian Competition and Consumer Commission on 3 November 2014.
- From a public hearing held in Canberra on 2 October 2014, received from the Treasury on 3 November 2014.

APPENDIX 2

Public hearing and witnesses

CANBERRA, 2 OCTOBER 2014

COOPER, Mr Bruce, General Manager, Strategy, Intelligence, International and Advocacy Branch, Australian Competition and Consumer Commission

COOPS, Ms Caroline, Chair, Competition and Consumer Committee, Law Council of Australia

de BRUIN, Mr Jos, Chief Executive Officer, Master Grocers Australia, Liquor Retailers Australia

DOLMAN, Mr Ben, Acting General Manager, Small Business, Competition and Consumer Policy Division, The Treasury

HEYS, Mr Nicholas, Deputy General Manager, Compliance and Enforcement Policy Implementation and Coordination, Australian Competition and Consumer Commission

MEZGAILIS, Mr Oskar, Analyst, Small Business, Competition and Consumer Policy Division, The Treasury

REID, Mr William (Bill), Member, Competition and Consumer Committee, Law Council of Australia