WA INDEPENDENT GROCERS ASSOCIATION (INC.)

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COMPETITION POLICY REVIEW: SUBMISSION

WA Independent Grocers Association (Inc.) (WAIGA) is the peak industry body for the independent grocery sector in WA. Our members include franchised Supa IGA and IGA stores, Supermarkets West stores and general grocery stores throughout the whole of Western Australia. The independent sector in WA has a combined turnover in excess of $2.5 billion employs 20,000 people and does over 1 million customer transactions a week.

WAIGA was a member of the National Association of Retail Grocers of Australia (NARGA) for over 30 years and John Cummings the president of WAIGA was a director of NARGA for 15 years and the Chairman of NARGA for eight years from 2003 to 2011.

WAIGA believes in a truly competitive environment for the retail sector in Australia and its first principle is that without competitors there is no competition.

We ask that the Review Panel recommend that section 49 which was repealed on the recommendation of the Hilmer Committee in its report, *National Competition Policy*, in 1993, be reinstated in the *Competition and Consumer Act 2010*. Australia needs now more than ever an effective prohibition on anti-competitive price discrimination.

We have been involved in advocating the position of the independent grocery sector and small business in general in Australia to government and reviews of the *Trade Practices Act 1974* and the more recent *Competition and Consumer Act 2010* in regard to the adequacy of these acts and the regulator in providing effective and fair competition between big business and small business. We believe in competition and recognise that competing businesses in agriculture, manufacturing and retail ultimately bring better outcomes for consumers in all Australia.

As a director and Chairman of NARGA I have put detailed submissions to the Baird Inquiry into the retail dominance of the chains, the Dawson review of The Trade Practices Act, the Senate Economics Reference Committee's *Inquiry into the effectiveness of the Trade Practices Act 1974 in protecting small business*, two Senate Economics Committee Inquiries into the Dairy Sector, a Senate Inquiry into the Banking Sector, and the ACCC's 2008 inquiry into the pricing of standard groceries, to name but a few.

The constant theme of our representations has been to have effective legislation and an effective regulator that deliver a fair and level playing field for all participants in the grocery sector including big business and small business, particularly for farmers, manufacturers and retailers.

In this submission we will not restate the size of the market or the dominance of the major chains in the grocery sector or others such as hardware, fuel, liquor etc. as these are well documented by the ACCC and in other submissions on the public record.

We would like the Review Panel to note that widely published figures on market share of the packaged grocery sector in Australia show unprecedented worldwide growth of the two major chains Coles and Woolworths in the last 40 years. Coles and Woolworths combined market share in 1975 was 35% to approximately 80% today. If one of the goals of the Trade Practices Act 1974 was to prevent such market dominance it obviously has not been successful. If competition law in Australia was to preserve and grow competition and if you agree with the premise that you need sustainable competitors to provide competition then neither the legislation nor the regulator have been able to achieve this in packaged groceries.

We put the deficiency down to three major things:

1 The repeal of s49,

2 The inability of s46 to deliver the intention of parliament to prohibit anti-competitive activity as a result of misuse of market power,

3 The lack of cases taken by the regulator to test s46, s45 or s51 in regard to the harm done to small business.

It is important to note that Hilmer's recommendation that the former s49 be repealed – accepted by the Keating Government - was based on the belief that any issues relating to anti-competitive price discrimination could be dealt with through s45 or s46. Earlier inquiries by Swanson (1976) and Blunt (1979) had recommended repeal of s49, largely on the basis that no cases had been brought to court, but the recommendations were rejected by the governments of the day. Indeed, it is clear that earlier regulators chose not to bring cases, ostensibly in the belief that cases should be brought by the disadvantaged parties. Such approaches failed to recognise that the limited financial resources of small businesses prevented them from bringing cases to court in the face of the much more substantial resources of big business competitors.

Critics have argued that while the original s49 prohibition was based mainly on the Robinson-Patman Act from the United States, that legislation has been ineffectual. However, such criticism cannot account for the fact that the Robinson-Patman Act has been a major factor in preventing the concentration of the US grocery market, for example, when compared to what has occurred in Australia. In the United States, Wal-Mart, the world's biggest retailer, and the second largest grocery retail chain, Kroger, jointly account for 20 per cent of the US grocery market. In Australia, Woolworths and Coles, with no effective impediment on anti-competitive price discrimination for the past 21 years, have joint market share of about 80 per cent.

The fact is, anti-competitive price discrimination is now rife in the grocery sector, to a far greater extent than it was prior to the repeal of s49. Former Senator Dee Margetts has pointed out both that the grocery price CPI exceeded general CPI and that the decline of the Franklins supermarket chain began shortly after the repeal of s49.*

Margetts, Dee, *National Competition Policy and the Retail Sector, Journal of Australian Political Economy,* No. 67, Winter 2011, Fig. 1, p. 83, Fig. 3, p. 85.

We now have in Australia the situation where anti-competitive price discrimination is occurring in a number of sectors and with independent grocers this is not only in the procurement of goods for sale but also other essential services.

In the case of electricity supply in WA, the chains appear to be able to pay from 30% to 40% less for electricity than their direct small business competitors. This also applies to other small business retailers in WA where it seems that the sellers of electricity work on the basis of 'charge whatever you can get away with' and use anti-competitive price discrimination to force their small businesses customers to pay higher prices than big business customers, beyond any differentials attributable to economies of scale. The effect of this is that small business retailers are subsidising through higher costs the supply of electricity to their big business competitors.

As an example in a small suburban shopping centre in Edgewater, Perth, there are two businesses side by side, each purchase their electricity from the same supplier, Alinta. One of the businesses is a small IGA store and the other an independent liquor store. For 31 days of supply of electricity 21/01/2014 to 20/02/2014 the liquor store was charged $2617.64 for consumption of 8489.94 KWH. If they paid the rate charged to the next door IGA they would have been charged $2110.85, a saving of $506.79 or showing the liquor stores pays 24% more for the electricity they use. The IGA for a similar period consumes 28,534.15 KWH.

The electricity to supply both outlets costs the supplier Alinta the same amount to purchase from the generator and is delivered down the same wires to each outlet with each business issued with a single monthly account by post that is calculated by the same metering method. This is a clear example of anti-competitive price discrimination as it is a 24% increase in a non- variable cost that the liquor store can never recoup and could be as high as 30% to 40% more than their closest competitor the Woolworths owned Dan Murphy Liquor is paying to chill its beer and wine to sell. At the same time the IGA may be paying 20% more for its electricity than its direct competitors Coles and Woolworths. We cannot find out the actual cost that Coles and Woolworths pay because no provider of electricity will tell us and neither will Coles or Woolworths.

If there was an effective prohibition on anti-competitive price discrimination in Australia and the ACCC acted on getting rid of such anti-competitive activity simply the electricity supplier could charge different prices to different customers if they could be justified by efficiency dividends. Currently they just charge smaller retail business customers extremely high prices to recoup margin that they give to the chains. It is worth noting that refrigeration and freezers either owned and operated by Coles, Woolworths or an independent draw power in the same profile and at the same time over a monthly invoice cycle, there are little if any economies of scale to the difference of supply.

In the case of milk, in WA the processor Harvey Fresh has the supply contract for house brand milk to Coles. Harvey Fresh process and manufacture 2ltr bottles of full cream milk on a daily basis under 4 different labels, Harvey Fresh, Ferguson Valley, South West and Coles. The Ferguson Valley and South West label are house brands that Harvey Fresh manufacture to sell to independent customers to enable them to retail 2ltr of milk at $1.99 the same as Coles.

The prices charged for the three house brand milks again have no justification but are a case of 'charge what you can to manage margins'. Harvey Fresh sell Ferguson Valley to an independent IGA, but not all IGA stores, for $1.70, South West to Farmer Jack stores at $1.75, these are not made available to Coles to whom we estimate they sell Coles milk to at $1.50 after all bundled terms and settlement discount. Harvey Fresh brand milk sells to independents in a range from $2.00 to $2.59.

Again under a prohibition of anti-competitive price discrimination Harvey Fresh could continue to sell these 4 products at different prices, but the differences would need to be justifiable.

In their submission to the 2011 Senate Inquiry into the Dairy Industry, Lion Dairy and Drinks (LD&D) stated that they could not make money out of the supply of house brand milk to either Coles or Woolworths at the contract price they charged. They said to make money out of their dairy division they had to sell milk at a higher price to smaller outlets to recoup the lost margin from the sale of house brand milk. From their admission they charge higher prices to independent customers than Coles and Woolworths on a range of dairy products they sell. This is a further example of the adverse impact of anti-competitive price discrimination in Australia. The ACCC has argued that, despite the domination of Coles and Woolworths and their use/misuse of market power, there is no case to be taken under s46. Ironically, this would support our view that the Australian grocery market is dysfunctional because of the absence of a specific prohibition on anti-competitive price discrimination and that such a prohibition should be reinstated.

The submission from LD&D clearly shows 'The Water Bed Effect' of their pricing policy caused by the supply of house brand milk to Coles and Woolworths at unprofitable prices. They cannot sell all of their milk at the same low price so in effect the other customers are subsidising the supply of house brand milk at low prices to Coles and Woolworths by paying more for the goods they buy from LD&D.

In NSW Metcash liquor, a wholesale supplier to the independent liquor industry nationally, found out the major brewery had agreed to supply Coles with cartons of packaged beer in pallet lots at a cheaper price if they picked up the beer from the Brewery warehouse. Metcash CEO Andrew Reitzer told the brewery that he would have their trucks also pick up pallet lots of packaged beer from the warehouse and asked if they would pass the same price on to them that they invoiced to Coles. The answer was that they could not afford to pass the discounted price on to all their customers as they needed to recoup the lost margin from larger customers. Mr Reitzer told me that he took this example of anti-competitive price discrimination to the then Chairman of the ACCC Graeme Samuel and one of the ACCC senior counsel who informed him there was nothing they could do to stop the practice.

While the ACCC argues that s46 does not give the commission the opportunity to act, the commission has put forward no recommendation on possible amendments to the Competition and Consumer Act which would allow the commission to ensure that anti-competitive price discrimination cease. Indeed, s46 was effectively gutted by the High Court decision in the Boral case in 1993 and minor amendments since then have not led to any significant cases being taken under that section in more than 20 years.

We are aware of many other cases of anti-competitive price discrimination and these not only include groceries that the sector buys for resale but also fruit and vegetables, meats and even

freight. There is a case where a transport company takes pallets of stock from Perth to Esperance with a delivery for Woolworths in the same truck as the independent, but the freight rate charged to Woolworths is half that of the independent.

There are two multi-outlet owners of independent supermarkets in WA who are forced to buy case goods groceries from the Metcash owned warehouse, and cannot buy these products to sell at the same price as the chains. They have set up a competing warehouse to buy direct from manufacturers to supply their businesses and other independents who may choose to buy from them. While they have been able to open accounts with a few manufacturers the major manufacturers will not open an account with them. The reason manufacturers give for not opening an account is that the retribution from Coles and Woolworths if they were to sell to them at competitive prices would irretrievably harm their business. These manufacturers already trade with Coles, Woolworths and Metcash competitors Costco, Aldi and Spar in other states, so why not in WA? Of course the new warehouse owners will comply with whatever quantity, order delivery time and payment that the manufacturers require to gain competitive prices if they open the account. This is obviously an impediment to competition in the grocery sector in WA. One could argue that at least in NSW and QLD you have the additional outlets of Aldi, Costco and Spar.

As one of the Terms of Reference of the review is to look at the impact of productivity in markets in relation to the *Competition and Consumer Act* these examples given above must take out some of the available margin denied to smaller grocery outlets from the chains' purchasing activity. As an example, how does the independent sector find savings in other areas for the running of refrigeration to compensate for the cheaper price that Coles and Woolworths pay for electricity? As we have stated the retailers in WA who choose to buy Ferguson Valley and South West milk are able to sell 2ltr of milk for the same price as Coles at $1.99. What price would those retailers sell milk for if they could access their house brand at the same cost as Coles? If Coles and Woolworths can obtain better buying prices than the independent by up to 20%, how much of that is lost productivity when it converts to retail prices charged?

Much is now being said of how a reduction in penalty rates on Sundays would improve productivity in Australia. A delivery of similar cost inputs including purchase of stock for either resale or added manufacturing or processing would improve productivity to a far greater degree. In an industry where a large business is able to receive a 10 or 20 per cent cost advantage while smaller competitors are still able to compete and survive, if the smaller competitors were to gain the same price it would have the dual effect of forcing prices down and the large business to increase productivity or lose market share to its more efficient smaller competitors who with lower input costs will have the ability to further increase their productivity and lower prices.

In the grocery retail market this is already happening where specialist retailers of fresh produce are able to deal directly with local producers, even if they are paying the local farmer a higher price than the chain generally pay farmers, and cut out the central warehouse and distribution costs the chains have. This enables them to offer a wider range and lower prices. The result of them being able to buy all they sell in the same quantities and price as Coles and Woolworths is obvious. We have many examples of this occurring in WA and can have the owners of those businesses give first hand examples to the Review.

Farmers, manufacturers and wholesalers in the grocery retail sector would also benefit through more certainty in pricing and knowing that the terms of the sale could not be altered at the whim of the major chains. This would have enabled LD&D not to be forced to recoup lost margin in the supply of house brand milk to Coles and Woolworths by raising prices of other dairy products to smaller retailers or reducing the price they paid for milk to the farmer as they declared in their evidence to the senate dairy inquiry.

National Competition Policy set up by the Keating government on the advice of the Hilmer Committee recognised the inefficiency of large organisations be they government or privately owned operating in a monopoly or duopoly. Smaller lean business will drive productivity in Australia, sourcing products from local growers and producers is the most efficient way to deliver fresher produce at better prices to consumers. The chains' model is to buy from one location and then transport by road all over Australia.

Below is the original s49.

SECTION 49 PRICE DISCRIMINATION

49(1) [Prohibited conduct]

A corporation shall not, in trade or commerce, discriminate between purchasers of goods of like grade and quality in relation to:

(a) the prices charged for goods;

(b) any discounts, allowances, rebates or credits given or allowed in relation to the supply of goods;

(c) the provision of services in respect of the goods; or

(d) the making of payments for services in respect of the goods;

if the discrimination is of such magnitude or is of such a recurring or systematic character that it has or is likely to have the effect of substantially lessening competition in a market for goods, being a market in which the corporation supplies, or those persons supply, goods.

49(2) [Certain price discrimination not prohibited]

Subsection (1) does not apply in relation to a discrimination if:

(a) the discrimination makes only reasonable allowance for differences in the cost or likely cost of manufacture, distribution, sale or delivery resulting from the differing places to which, methods by which or quantities in which the goods are supplied to the purchasers; or

(b) the discrimination is constituted by the doing of an act in good faith to meet a price or benefit offered by a competitor of the supplier.

49(3) [Onus of establishing subsection (1) does not apply]

In any proceeding for a contravention of subsection (1), the onus of establishing that the subsection does not apply in relation to a discrimination by reason of subsection (2) is on the party asserting that subsection (1) does not apply.

49(4) [Attempts to induce or to enter transaction to obtain benefit of prohibited conduct prohibited]

A person shall not, in trade or commerce:

(a) knowingly induce or attempt to induce a corporation to discriminate in a manner prohibited by subsection (1); or

(b) enter into any transaction that to his knowledge would result in his receiving the benefit of a discrimination that is prohibited by that subsection.

49(5) [Defence to prosecution under subsection (4)]

In any proceeding against a person for a contravention of subsection (4), it is a defence that if that person establishes that he reasonably believed that, by reason of subsection (2), the discrimination concerned was not prohibited by subsection (1).

Hilmer dismissed section 49 as being of no assistance to small business, but that was because the small businesses themselves were expected by the regulators to take the cases themselves. If we look at recent results of just Wesfarmers we note that 'other expenses' which include legal expenses were last year in excess of $3billion for that company. How could a small business in retail with total assets of between on average $1million to $5million even consider starting an action against the likes of Coles or Woolworths? What would happen when the total funds ran out?

Our suggestion is to reinstate the original s49, plus an effects test, plus a firm requirement that the ACCC investigate whenever an allegation of anti-competitive price discrimination is bought to its attention.

We have included the following separate papers and submissions as background.

Title: Current Issues in Australian Competition Policy ANTI-COMPETITIVE PRICE DISCRIMINATION. This was written by Ken Henrick CEO NARGA in February 2010.

Title: Current issues in Australian competition policy: anti-competitive price discrimination – international perspectives. This paper is on the Robinson-Patman Act, Treaty of Rome, UK Competition Act 1998 and Canada's Competition Act. This Discussion paper was written by Ken Henrick CEO and Gerard van Rijswijk, Senior Policy Adviser of NARGA in 2011 and later reproduced for Master Grocers Australia.

Title: Australian Competition Law. This was written by Ken Henrick CEO of NARGA in response to the Senate Economics References Committee Inquiry into the dairy industry in 2011.

John Cummings

President WAIGA

MASTER GROCERS AUSTRALIA

LIQUOR RETAILERS AUSTRALIA
Independent Liquor Outlets

Incorporating:

NARGA National Association of Retail Grocers of Australia

Current issues in Australian competition policy:
anti-competitive price discrimination - international perspectives

For many decades now, a specific prohibition on anti-competitive price discrimination has been regarded by competition regulators internationally as 'core to running a level playing field in business across the board' – for big companies as well as small companies. This contrasts with what Prof Hilmer suggested in his *National Competition Policy* report in Australia in 1993 - that it was specifically aimed at protecting small business.

Whilst such a prohibition, by levelling the playing field, does help small business it also helps competition in general by allowing a wider range of entities to compete on a fair basis thereby generating a better competitive environment.

Much of the approach taken by legislators worldwide in relation to a prohibition of anti-competitive price discrimination in competition law has its origins in the US Robinson-Patman Act of 1936. We have been fortunate in being able to acquire a copy of the first book[1] written in 1938 by Mr Wright Patman, a co-sponsor of the Act, to explain the Act, its purpose and its provisions.

The following comments are pertinent:

- Patman makes it clear that the purpose of the Act was not to interfere with sound business practices but to deal with the small minority 'bandit fringe'.

  'Essentially the present Act provides that when a man sells a product to two or more customers, he must not discriminate between them in such a way that one is given an unfair advantage over the other.' (Preface p. iv)

  It is clear that when such an advantage is given early in the supply chain, the disadvantaged party can never make up the difference brought about at that point and will be at a competitive disadvantage when on-selling his product to the final consumer. The end result is that the disadvantaged entity

[1] Patman W. *The Robinson-Patman Act, What you can and cannot do under this law,* The Ronald Press Company, New York, 1938

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has difficulty in surviving as a competitor and drops out of the market, reducing competition in that market.

- Patman goes on to explain:

> *'The soundness of the Act is now generally acclaimed by business. It adds the force of law to many of the principles in codes of ethics adopted voluntarily by industry groups over the last twenty years, and makes possible for the first time their enforcement against the recalcitrant minority with whom every industry is afflicted. It is not a 'reform bill' but rather a long step toward the arming of business with effective weapons against the relatively few outlaws who will not play fair.'(Ibid)*

The corollary to that statement is, of course, that companies who want to 'play fair' have nothing to fear from the re-introduction of a s 49-style prohibition.

- Patman quotes W H S Stevens from the Harvard School of Business:

> *'The danger to fair competition comes not primarily from the customary and relatively small open and published price differentials given by nearly all sellers, and taken advantage of by hundreds and thousands of distributors, but rather from the large differentials, open or secret, available only to a limited number of large mass buyers.' (Preface p. v)*

- In Chapter 1, *The purpose of the Act,* Patman details the long term effect of such pricing differentials:

> *'In time the industry as a whole found itself in troubles from which it could not extricate itself. The resulting difficulties spread to the raw material suppliers and reacted upon the earnings and purchasing power of the workers. For wages were cut, profits disappeared, weak producers soon gave way to the stronger, and monopolistic control became centralized in the hands of a few men. That is a true story, and the industry is one of our rather large industries, still in a few hands.' (Chapter 1, pp 4-5)*

We have seen this type of market concentration develop in our retail grocery sector – fed by the unrestrained pricing pressure that can be brought to bear by the large chains on their suppliers....."

We also have a copy of Senator Patman's second book[2], an update of the book quoted above. We include a series of quotes from this book that shows the philosophy and economic thought behind the US prohibition against anti-competitive price discrimination:

- *'In the concluding chapters of this volume reference is made to the strong support given to the Robinson-Patman Act by representatives of business at all levels. It has been made clear by representatives of business that the discriminatory practices against which the Robinson-Patman Act is directed are unsound practices. They are harmful to business enterprises endeavouring to maintain high ethical standards and are destructive of competition generally....'*[3]

- *In the course of its consideration of proposed legislation against price discrimination, Congress became quite well informed on the economic significance of price discrimination. It was found that price discrimination had become a weapon of sellers who held some degree of monopoly power. This power had been effectively employed by powerful sellers, with the effect of destroying competition and the tendency to create stronger monopolies.'*[4] (Same argument could be applied to powerful buyers.)

- *The conclusions of Congress regarding the economic significance of the practice of price discrimination were vividly recorded in the committee reports on the Bill that became the Clayton Act. In those reports, references were made to the price discrimination practices of the Standard Oil Co of New Jersey and the American Tobacco Co., and to the great market power that these multi-market operators had acquired and abused through the use of price discrimination, with the reult of destroying competition and creating monopolies.'*[5]

- *'The House Committee on the Judiciary, in reporting H.R.8442 (the Patman Bill) stated "....Discrimination in excess of sound economic differences between the customers concerned, in the treatment accorded them, involve generally an element of loss, whether only of the necessary minimum of profits or of actual costs,* ***that must be recouped from the business of customers not granted them."***[6] (Our emphasis – those other customers are placed at a competitive disadvantage)

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[2] Patman W.,Complete guide to the Robinson-Patman Act, Prentice Hall Inc, 1963
[3] Ibid Page vi
[4] Ibid Page 1
[5] Ibid Page 6
[6] Ibid Page 9

- *From the same House Report, "...The existing law* (without the prohibition) *has in practice been too restrictive in requiring a showing of general injury to competitive conditions in the line of commerce concerned, whereas the more immediately important concern is in injury to the competitor victimised by the discrimination.* ***Only through such injury can the larger, general injury result.*** *Through this broadening of the jurisdiction of the Act, a more effective suppression of such injuries is possible and the more effective protection of the public interest at the same time is achieved."*[7] (Our emphasis)
- *'In short, the effects on competition to be questioned are the long-range effects. Although it is obvious that consumers may temporarily enjoy lower prices in the areas where discrimination takes place, and the competition may appear active and vigorous, the question to be answered is whether the long-range effects will be a substantial disappearance of competitors and, presumably, a substantial lessening of competition.'*[8]

- *The Grocery Industry Group I Rules published by the Federal Trade Commission January 16, 1929 contained the following elaboration on the typical trade-practice conference prohibition of secret rebates and allowances:*

  "Rule I. Whereas it is essential in the interest of the trade and the consuming public that the production and distribution of grocery products be conducted in accordance with sound principles of economics and justice, in order to afford an equal opportunity to all manufacturers and merchants and to secure effective competition in serving the public: Be it Resolved, That (1) terms of sale shall be open and strictly adhered to; (2) secret rebates or secret concessions, or secret allowances of any kind are unfair methods of business; (3) price discrimination that is uneconomic or unjustly discriminatory is an unfair method of business."

  'Of course prior to 1936,all responsible functioners in the food industry tried to practice these fair rules of the game, but their high hopes and good intentions were frustrated by the incessant coercive influence of mass buyers in all the market places.'[9]

- *Among unfair business practices, price discrimination most directly denies to small business an equal opportunity to live and grow on the basis of efficiency.*

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[7] Ibid Page 9-10
[8] Ibid Page 59
[9] Ibid Pages 107-8

Such opportunity is the very essence of the competitive economic system which our antitrust laws seek to preserve, maintain and restore.

That small business has survived or even grown despite price discrimination is of no relevancy when offered as evidence that price discrimination is not destructive of small business. What is relevant, but what must remain unknown until price discrimination is eliminated, is how successful small business can be when their larger rivals cannot exercise their monopolistic power to grant and receive price discriminations. Small business is entitled to the opportunity of showing what it can do in absence of the crippling handicap of discriminatory prices. Continued enforcement of the Robinson-Patman Act will ensure that small business is granted that opportunity.'(From a report submitted by the Federal Trade Commission to the chairman of the Select Committee on Small Business, United States Senate, February 21,1952)[10]

- *'Price discrimination favouring preferred buyers presents a danger to the competitive enterprise system which is inconsistent with the policy of the price discrimination statute. Firms can abuse their superior market position and engage in discriminatory practices that eliminate small suppliers and small retailers from the competitive scene.' (conclusion of the House Committee on the Judiciary in 1956)*[11]

- *'In conclusion, it is clear that Members of Congress and other public officials are faced with the problems of weighing those arguments for and against the practice of price discrimination. Congress has done that in the past on the basis of an abundance of factual information and has found that the effects of price discrimination are substantially to lessen competition and to create monopolies. In other words, Congress has found the practice of price discrimination to be anti-competitive – and it has done so on each occasion when it studied the details of the factual information about the practice of price discrimination. These legislative findings have been made despite arguments by the advocates of price discrimination that it is a form of competition and that the Robinson Patman Act and other similar legislation are antidiscriminatory....'*[12]

The above quotes appear to have some resonance with our current competitive situation.

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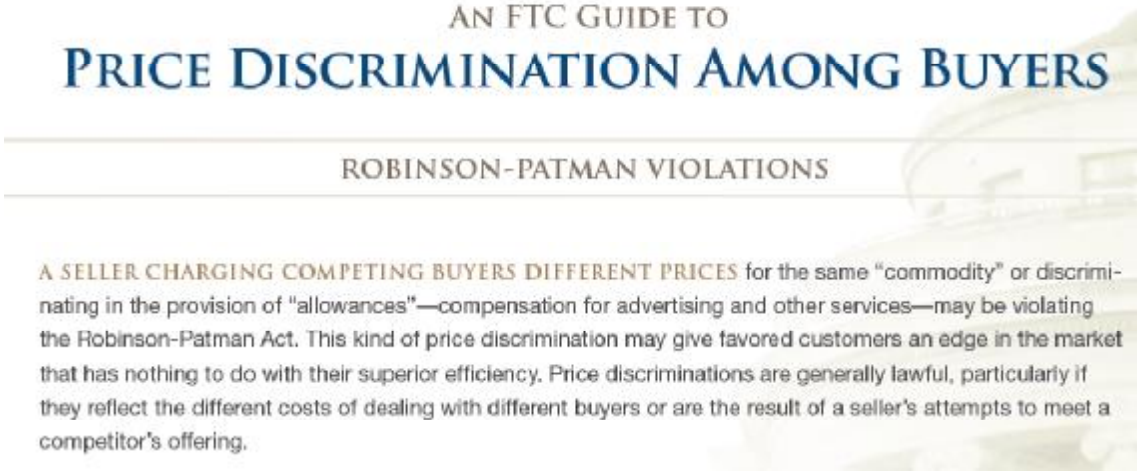
[10] Ibid Page 200
[11] ibid Page 206
[12] ibid Page 208

We note that the US is still enforcing the Robinson-Patman Act as shown by the following extract from the FTC Guide on anti-trust law. Note that the advice makes it clear that there are many forms of legal price discrimination, it is only discrimination of the anti-competitive type that is illegal.



AN FTC GUIDE TO

PRICE DISCRIMINATION AMONG BUYERS

ROBINSON-PATMAN VIOLATIONS

A SELLER CHARGING COMPETING BUYERS DIFFERENT PRICES for the same "commodity" or discriminating in the provision of "allowances"—compensation for advertising and other services—may be violating the Robinson-Patman Act. This kind of price discrimination may give favored customers an edge in the market that has nothing to do with their superior efficiency. Price discriminations are generally lawful, particularly if they reflect the different costs of dealing with different buyers or are the result of a seller's attempts to meet a competitor's offering.

The prohibition of anti-competitive discrimination was taken up by the Treaty of Rome in 1957 (and subsequent versions) which set up the Common Market and later the European Union – See Article 85 1.(d) below:

ARTICLE 85

1. The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decision by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market, and in particular those which:

(a) directly or indirectly fix purchase or selling prices or any other trading conditions;
(b) limit or control production, markets, technical development, or investment;
(c) share markets or sources of supply;
(d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
(e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

It has its parallel in UK competition law (Competition Act 1998):

The prohibition

2 Agreements etc. preventing, restricting or distorting competition.

(1) Subject to section 3, agreements between undertakings, decisions by associations of undertakings or concerted practices which—

(a) may affect trade within the United Kingdom, and

(b) have as their object or effect the prevention, restriction or distortion of competition within the United Kingdom,

are prohibited unless they are exempt in accordance with the provisions of this Part.

(2) Subsection (1) applies, in particular, to agreements, decisions or practices which—

(a) directly or indirectly fix purchase or selling prices or any other trading conditions;

(b) limit or control production, markets, technical development or investment;

(c) share markets or sources of supply;

(d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

(e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

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(b) limiting production, markets or technical development to the prejudice of consumers;

(c) applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

(d) making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of the contracts.

The above clauses dealing with anti-competitive agreements and with abuse of market power both make specific mention of anti-competitive price discrimination.

We do not see that parallel in the Australian *Competition and Consumer Act 2010,* since s 49, the section dealing with this form of anti-competitive conduct in the *Trade Practices Act 1974* was repealed in 1995 with the result that such anti-competitive conduct has flourished, while the regulator has never taken a single case against alleged anti-competitive price discrimination under either s45 or s46. Hilmer had argued in his 1993 *National Competition Policy* report that s49 was not needed because s45 and/or s46 would do the job. History has shown that under an indolent regulator, neither will do so. The parliament repealed s49 on Hilmer's flawed

recommendation but has never conceded that anti-competitive price discrimination was acceptable conduct.

Canada's *Competition Act* makes its purpose quite clear and does not shy away from support of SMEs as a means of maintaining a competitive market:

> **1.1** The purpose of this Act is to maintain and encourage competition in Canada in order to promote the efficiency and adaptability of the Canadian economy, in order to expand opportunities for Canadian participation in world markets while at the same time recognizing the role of foreign competition in Canada, in order to ensure that small and medium-sized enterprises have an equitable opportunity to participate in the Canadian economy and in order to provide consumers with competitive prices and product choices.

The Canadian act refers to anti-competitive price discrimination as follows:

> **Delivered pricing**
>
> **81 (1)** Where, on application by the Commissioner, the Tribunal finds that delivered pricing is engaged in by a major supplier of an article in a market or is widespread in a market with the result that a customer, or a person seeking to become a customer, is denied an advantage that would otherwise be available to him in the market, the Tribunal may make an order prohibiting all or any of such suppliers from engaging in delivered pricing.

> **Definition of *delivered pricing***
>
> **80 (1)** For the purposes of section 81, ***delivered pricing*** means the practice of refusing a customer, or a person seeking to become a customer, delivery of an article at any place in which the supplier engages in a practice of making delivery of the article to any other of the supplier's customers on the same trade terms that would be available to the first-mentioned customer if his place of business were located in that place.

We conclude from the above that anti-competitive price discrimination is a practice that is viewed as deleterious to competition by competition regulators generally as it is injurious to competition, not just competitors.

The fact that price discrimination hurts large businesses was made clear during evidence given to the Committee by dairy industry suppliers who were obviously being disadvantaged by the low prices that they themselves had agreed to.

We do not understand the opposition by some to the re-introduction of such a prohibition as, by definition, the ***only type of price discrimination that is prohibited by such a clause is one that is anti-competitive.*** In other words, companies that are behaving ethically and fairly have nothing to fear.

The current debate over milk pricing

Australia's *Competition and Consumer Act 2010* has sections 45 and 46 that deal with anti-competitive agreements and abuse of market power respectively. The question is whether anti-competitive price discrimination is seen as illegal under either s 45 (because it is based on an agreement that is anti-competitive) or under s 46 (because it is based on the abuse of market power – maybe even unconscious abuse[13] – i.e. abuse that results from the unconscious power due to sheer size.).

The problem here is that even if the answer to either question were 'yes' both Section 45 and 46 are relatively difficult to enforce, requiring evidence of a substantial effect on competition (which itself is undefined in the Act). Of course once the effect on competition emerges, the damage has already been done.

We do not know whether the behaviour of the major chains and their suppliers in the case of milk prices are in breach of either ss. 45 or 46 as no assessment of the relevant facts has been made public by the ACCC.

Investigation of the Coles changes to milk pricing was initiated under the previous Chairman of the ACCC and concentrated on the 'straw man' of predatory pricing and the validity of the Coles 'Down, Down' campaign - with the only conclusion in the public domain being the obvious one, that there had been no breach of the law in relation to predatory pricing or misrepresentation.

[13] The two major grocery chains represent such a large proportion of the market that a supplier cannot afford to lose the volume of business associated with either. The tendency is therefore to accommodate them in any way possible, even to the extent that doing business with them could incur a loss. The alternative would involve a greater impact on the business due to losses in economies of scale. Losses on the business dealings with the majors are compensated for by higher prices elsewhere, either for the same goods or for other goods the supplier provides to the sector generally.

We also know that all Coles did (followed by Woolworths) was to reduce the price of their private label milk from $2.07 per two litres to $1.99 per two litres. The evidence appears to be that, at the time, Coles' purchase price of milk had not changed.

The retail price drop was not great, but the subsequent promotion of that drop – including an initial claim that the decrease had been more substantial – has seen a significant shift from branded milk to private label milk and from smaller retailers (e.g. convenience stores and route trade) to the major chains, to the extent that the overall supplier profitability of milk sales has been affected. So obviously there has been an impact on the market and on competition.

The basic questions that have not been answered include:

- Is the low price the major chains pay for private label milk a result of their market power or its abuse?
- Is the agreement between the suppliers of private label milk and the major chains anti-competitive?
- Did the ACCC in its assessment of compliance with s 46 of the Act take note of s 46 (7)

(7) Without in any way limiting the manner in which the purpose of a person may be established for the purposes of any other provision of this Act, a corporation may be taken to have taken advantage of its power for a purpose referred to in subsection (1) notwithstanding that, after all the evidence has been considered, the existence of that purpose is ascertainable only by inference from the conduct of the corporation or of any other person or from other relevant circumstances.

The benefits of a specific prohibition on anti-competitive price discrimination are many.

Such a prohibition:

- Makes it clear to business that this type of behaviour is clearly illegal – without the need to parse the intricacies of Sections 45 and 46. (It is for that reason that other jurisdictions include this specific prohibition.)

- The evidence for a prosecution (or injunction) is relatively easy to obtain – the parties need to be able to justify any pricing differential and an outside affected party can lodge a complaint.

- Both parties, the supplier and the purchaser, are liable under law, enhancing likelihood of compliance.

- Suppliers will have a mechanism that can be used to negate unrealistic pricing demands from larger customers – demands which, if acceded to will

either damage their viability or require them to increase prices to other customers.

The final question then is whether the reintroduction of a prohibition on anti-competitive price discrimination will help the dairy industry (and other sectors in a similar position).

Another way of addressing this question is to ask how, under current law, a supplier can resist the pressure from the major chains for lower prices without risking the relationship and potentially losing the sales involved? Note here that we have seen in the case of the dairy sector that private label milk prices are so low as to be unprofitable and to have an impact on prices charged to others.

It is our contention that, armed with a prohibition on anti-competitive price discrimination, the dairy sector is better able to resist unrealistic pricing pressures. This may mean higher priced private label milk (unless the major chains are prepared to reduce their own margins), but could mean lower prices for dairy products generally and a more competitive grocery market in the longer term.

21 October 2011

NARGA National Association of Retail Grocers of Australia

Current Issues in Australian Competition Policy

ANTI-COMPETITIVE PRICE DISCRIMINATION

Other OECD countries have legal prohibitions against anti-competitive price discrimination - where a company sells identical product to different customers at different prices. Australia does not.

Such laws *do not prohibit* lower prices based on economies of scale, but require that the seller should be able to demonstrate genuine economies of scale proportionate to the discounts. [Nevertheless, wholesalers and retailers typically order in standard quantities per order, such as by pallet or truck load, even if competitor A might order twice as much as competitor B over the course of a year. Economies of scale do not necessarily arise in that context.]

Until 1993, Australia had a prohibition against anti-competitive price discrimination, s49 of the *Trade Practices Act*. Section 49 was repealed by the Keating government on the recommendation of the Hilmer Committee.

Hilmer argued that s49 was unnecessary because s46 (misuse of market power) was available to protect against such conduct. Section 46 was subsequently found to be seriously deficient in the High Court's decision in the *Boral Besser Masonry v. ACCC* case and has effectively been gutted. The ACCC admits that prosecuting s46 cases is now difficult. Small business has thus been deprived of the protections both s.46 and s.49.

In other jurisdictions, where anti-competitive price discrimination occurs, both buyer and seller are liable. A prohibition on anti-competitive price discrimination is thus a protection for a weaker party which is being intimidated by a stronger party to engage in anti-competitive price discrimination.

In the United States, the relevant legislation is the *Robinson-Patman Act.* Section 2(a) of the Robinson-Patman Act[1] says:

> *That it shall be unlawful for any person engaged in commerce, in the course of such commerce, either directly or indirectly, to discriminate in price between different purchasers of commodities of like grade and quality...where the effect of such discrimination may be substantially to lessen competition or*

.../2

[1] Ibid., p. 11

tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit or such discrimination or with customers of either of them.

Former Congressman Wright Patman, one of the co-authors of the Act, made the point that once anti-competitive price discrimination has occurred, the competitor who has suffered the discrimination is unlikely to be able to remain competitive in relation to that product or service, even if he accepts a lower profit margin.

Patman summarised the issue thus:

If we had to provide a single statement as to the economic tests of an objectionable price discrimination, we would have to say that it is a discrimination that has a substantial tendency to divide the market shares in ways different from the division that would take place if efficiency were the sole determinant of this question.[2]

Anti-competitive price discrimination may arise in a number of ways. In the Australian grocery market it is likely to be in the form of demands from a supermarket chain to a supplier to accept a lower price for a product than the price at which he sells that product to his competitor(s) or to provide equivalent benefits through bundled terms, such that the supermarket chain effectively enjoys a pricing advantage at that point in the supply chain. From that point on, the competitive advantage is unlikely to be eroded and the consequences for smaller competitors can be dire.

Until repealed, s49 read in part:

49(1) [Prohibited Conduct] *A corporation shall not, in trade or commerce, discriminate between purchasers of goods of like grade and quality in relation to:*

(a) The prices charged for goods
(b) Any discounts, allowances, rebates or credits given or allowed in relation to the supply of goods;
(c) The provision of services in respect of the goods; or
(d) The making of payments for services provided in respect of the goods;

If the discrimination is of such magnitude or is of such a recurring or systematic character that it has or is likely to have the effect of substantially lessening competition in a market for goods, being a market in which the corporation supplies, or those persons supply, goods....

The rest of the section provided limited exemptions and defences.

.../3

The former s49, we note, relied on a "substantial lessening of competition" test which has clearly failed in relation to other issues, such as creeping acquisitions. We do not suggest the reintroduction of s49 as it formerly stood.

[2] ibid., p. 54.

Simpler and more direct legislation applies in the United Kingdom. The UK *Competition Act 1998,* Chapter 1, s2(2)(d) prohibits agreements, etc., which "apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage". We think a "competitive disadvantage" test would be preferable, but there may be other options also.

The Hilmer committee's report said that:

> *... price discrimination can be anti-competitive where it enables a firm to entrench its position of market power by creating strong buyer-seller ties and thus raising barriers to the entry of new competitors. Extreme forms of price discrimination can amount to predatory pricing.*[3]

Indeed, it sets the scene for predatory pricing of a type not caught by the current predatory pricing provisions of the *Trade Practices Act* - the "Birdsville amendment" - but which is recognised in the literature as "above cost predation".

In the Australian context, the beneficiary of anti-competitive price discrimination - a buyer with sufficient market power to extract a discriminatory price advantage from a supplier - has the capacity to lower prices (using the extra margin gained from the price discrimination) to a level its competitors are unable to match, without actually having to sell "below relevant cost" (that is, at a loss) which the Act prohibits if it is conducted for a "sustained period of time" for the purpose of injuring or eliminating a competitor or preventing the entry of a new competitor.

Clearly, Hilmer's committee did not consider the duopsonistic circumstances of today's retail grocery sector. From the year the Hilmer report was published, 1993, until now, Woolworths and Coles have increased their joint market share from about 50 per cent to just under 80 per cent. That circumstance puts it outside any experience of market behaviour available to Hilmer and his committee at that time and it is now at a level which they could not have contemplated.

Despite National Competition Policy, in 2008 the ACCC found the retail grocery industry to be only "workably competitive" (a term which has no status in competition law literature) and that Coles and Woolworths had a lack of incentives to compete strongly on price.[4]

.../4

An industry sector is either competitive in the way it operates, or it is not. In a competitive market, sellers will compete to improve products and supply them at the lowest possible cost.

A perfectly competitive market is one in which profits are high enough to pay costs and deliver net profits just high enough to persuade investors that their funds are not better off in a savings account or some other investment.

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[3] *National Competition Policy,* Report by the Independent Committee of Inquiry, August 1993, pp. 74-75

[4] ACCC grocery inquiry report, p. xvi

Clearly, the ability of Woolworths, for example, to deliver double digit profit *increases*, as it has done in recent years, is a function of the hyper-concentration of the Australian grocery market and the disproportionate market power which derives from that concentration.

The assumptions of the Hilmer committee and more recently the ACCC inquiry into the grocery retailing sector are based on academic theories of competition which assume "normal" competition, but which largely do not apply in some industry sectors in Australia because of the hyper-concentration of markets. When markets are hyper-concentrated, competition theory doesn't work. As the law is based on competition theory - that is, on functioning competitive markets - and at least some markets are not functioning as competitively as they should, the legislation needs to be amended to take account of that.

For example, the Act could be amended specifically to deal with competition in hyper-concentrated markets. Indeed, partly as a result of National Competition Policy, there are now a number of industry sectors - banking, telecommunications, air transport, petroleum, grocery retailing - which are concentrated to the point where market-sharing, rather than competition, seems to be the predominant feature.

We believe the reintroduction of a prohibition against anti-competitive price discrimination would go a long way towards returning the Australian food and grocery market to a more competitive context.

National Association of Retail Grocers of Australia
February 2010

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AUSTRALIAN COMPETITION LAW

Introduction

This discussion paper follows on from the recently completed Senate Economics References Committee Inquiry into the dairy industry and draws on Chapter 7 of the final report of that committee: '*The impacts of supermarket price decisions on the dairy industry'*, issued in November 2011 (the Report).

This chapter discusses the adequacy of competition law in Australia and in particular the sections of the Competition and Consumer Act 2010 (the Act) dealing with abuse of market power. Anti-competitive price discrimination and predatory pricing are discussed in some detail.

This paper uses the outline provided by this chapter as a framework for comment on the Act.

Some general comments are appropriate:

- The Inquiry provided an interesting case study into the workings of the Act and the inability of the Act to address the question of excessive market power

- The paucity of case law relating to Part IV of the Act and in particular S46 is of concern.

- The failure to amend S46 following the Boral decision to ensure ongoing effectiveness

- The reluctance to take action under the previous S49 when it was in place – only one case ever went to court and it was privately prosecuted.

- The emphasis on theoretical constructs that have little relevance to business realities.

The objective of Competition Law

It is generally agreed that the purpose of competition law is to enhance consumer welfare through the promotion of competition. One way the Act

does this is to prohibit anti-competitive conduct the purpose being, as described in the Treasury submission:

> The Part IV provisions are principally concerned with protecting the competitive process, not individual competitors. They are not designed to protect competitors from rigorous competitive behaviour, nor to force businesses to compete.[1]

Some questions arise:

- At what point does 'rigorous competition' become anti-competitive behavior and how does the Act or the regulator distinguish between the two?

- How can the competitive process be protected without competitors?

- Why have S46 dealing with abuses of market power if every instance of abuse is described as 'vigorous competition'?

Economic theory as well competition law administration in other jurisdictions recognizes the difficulties posed by highly concentrated markets. However Australia's approach appears to be based on 'contestability theory' which suggests that highly concentrated markets can still be competitive provided some possibility of an external challenge exists.

This theoretical approach has resulted in little action being taken against growing levels of concentration in many markets or against the resulting abuses within those markets.

The dividing line between competition and abuse of market power needs to be better defined.

In the absence of case law, guidance should be provided by the ACCC or by parliament.

The dairy industry case

The Report outlines the ACCC review of the milk pricing practices of the major chains and confirms that the ACCC's analysis of these practices were not in breach of the predatory pricing provisions of the Act.

However, evidence provided to the Committee by Lion dairy and drinks confirmed that they were losing money on sales of private label milk. to the major chains. In other words, the major chains were able to negotiate prices that were so low as to be below the cost of production, the outcome being that prices paid by other customers for milk (and presumably other dairy products) would have to be higher in order for the companies to remain viable.

And this was not seen as anti-competitive?

Whilst the ACCC has clearly addressed the predatory pricing aspect of the Act in this case – and made it clear that its analysis showed that the behaviour failed at the first hurdle, the 'purpose' test – it did not examine whether the behaviour was in breach of S46 (misuse of power) or whether the agreements reached between the processors and the major chains were in breach of S45 (contracts, agreements or understandings that restrict dealings or affect competition) which has an 'effects' test – in spite of the fact that the market for drinking milk is distorted by these agreements to an extent where competitors to the major chains are placed at a competitive disadvantage.

Anti-competitive price discrimination

Much has been written about price discrimination both before the repeal of S49 and more recently. Much of the commentary is ill-informed,confusing pro-competitive price differentiation with anti-competitive price discrimination or suggesting that a prohibition of the latter would impact pro-competitive activity. This has not been the experience in other jurisdictions.

An example of such confusion is contained in Ch7 where the concerns expressed in the Dawson Report:

> Their complaint was that independent wholesalers (who sell wholesale to independent retailers) are not able to obtain goods at prices comparable to those charged by suppliers to the two major chains, notwithstanding that their central distribution warehouses are, in comparison with the facilities of the major chains, of comparable size and capable of like performance. They submitted that this constituted a failure on the part of suppliers to provide 'like terms for like customers' at this level of the grocery distribution chain, namely, the central warehouse level. This meant, they said, that the independent retailers were such that there could be no fair competition between them and the major chains at the retail level, only the later being able to reflect the benefit of lower wholesale prices in their retail prices.[17]

were downplayed by reference to evidence given by the ACCC to a Senate Estimates hearing which confirmed that different pricing for different pack formats were not an example of price discrimination:

> Senator XENOPHON—Is it price discrimination to be selling branded milk and generic milk, or the home brand milk, for different prices when in effect it is the same product?
>
> Mr Markham—I think that is the case for most private labels and branded products anyway. Branded products carry a marketing component, a brand value, which has always put them at a higher price than a private label. So, no, I do not believe so.[19]

The issue for independents is rather whether their supplier has access to the same terms of trade as the majors for the same branded (or private label) offering. Only then can they compete with the major chains.

Although S49 was repealed in 1995 following the recommendations of the Hilmer report, attempts at repeal were made as early as 1976 shortly after the Trade Practices Act 1974 came into effect and had persisted since.

Hilmer's rationale for the repeal of S49 consisted in part of a belief that the Act should not protect any particular part of society, suggesting that it was there primarily to protect small business:

> The prohibition against price discrimination prevents the sale of like goods to different persons at different prices, where such discrimination substantially lessens competition. The provision is contrary to the objective of economic efficiency and has not been of assistance to small businesses. The Committee does not believe that it is the role of the competitive conduct rules to protect any particular sector of society, and does not believe that the competition rules should be used to achieve objectives contrary to economic efficiency.[7]

This interpretation of the purpose of such a provision does not allow for the fact that all entities are protected from this type of anti-competitive behavior – behavior that can equally impact large companies.

We note here that anti-competitive price discrimination prohibitions exist in most other jurisdictions and is part of the Lisbon Treaty that underpins the European Union.

Hilmer's other contention was that provision was unnecessary as S45 and S46 take care of such behavior. This view contrasts with the views of regulators in other jurisdictions. It was, however, the view expressed by the ACCC:

> … observed that anticompetitive price discrimination almost invariably involves a firm with market power. You have to have market power to make it stick. Alternatively, a group of suppliers has to get together and agree on the price discrimination; otherwise, it just does not work. The point the committee made was that if it is a use of market power then that is what section 46 is about. If it is a group of suppliers getting together and deciding on the anticompetitive price discrimination, then that is what section 45 is about. Basically, the Hilmer committee said that they did not see a role for section 49, because the conduct in question was already covered by sections 45 and 46.[11]

It is a little like saying that in traffic law you do not need a rule prohibiting drivers from crossing double lines because that behaviour is covered by provisions relating to dangerous driving.

The reason why other jurisdictions make specific reference to anti-competitive practices such as price discrimination is because such practices are destructive of competition and offences against general misuse of market power clauses are more difficult to prosecute.

TWhile the ACCC purported to investigate possible predatory pricing, in its submission to the Inquiry did not address possible breaches of S45 and/or S46 by the behaviour of the major chains and dairy processors.

Also the major difference between the previous S49 and the current S46 is that the former was based on an 'effects' test whereas in the latter a 'purpose' needs to be proven.

The Report goes on to question the effectiveness of S49 given that when it was in place '*it was invoked in legal proceedings in very few instances'.* In fact it was only invoked once – and that was in a private case which was successful.

The Parliament has been critical of the ACCC and its predecessors for failure to take cases. In the case of S49 not one case was taken by the regulator for the 21 years that it was on the statute books.

To use this fact as an excuse for its repeal would create an interesting precedent – one that suggests we should repeal laws not used to prosecute cases, when in fact the law exists as a framework to control appropriate behaviour.

The Report goes on to list the limitations of S49, again quoting Hilmer:

> It is not clear what degree of similarity is required for goods to be regarded as being "of like grade and quality"; it is not clear what might constitute a "reasonable" allowance for differences in cost; and it is not clear whether, when meeting a competitor's price, the goods must bear the same degree of similarity to the competitor's goods as is required by the phrase "of like grade and quality". The cost defence does not necessarily correspond with those factors which firms would monitor or consider significant.[25]

Firstly, the quote relates to meeting the price of a competitor (one of the defences against a breach of S49), it does not demonstrate a difficulty that a single supplier would have in pricing the same goods to two different customers. Secondly, other jurisdictions appear to have been able to work out which price differentials were due to cost differences and which were anti-competitive.

The ACCC is then quoted as suggesting that '*...you ended up with a fairly small set of pricing behaviours which potentially would have fallen under that section for consideration.'*

True – those behaviours that have an anti-competitive effect!

We note here that the wording of the former S49 may need to be revisited in order to better reflect its purpose in the current regulatory environment.

In evidence to the Committee the ACCC indicated that '*these types of provisions have been repealed in a number of countries in recent years'.*

The only country that has repealed such a provision is Canada which however has another clause in its legislation with similar impact:

DELIVERED PRICING

Definition of *delivered pricing*

80 (1) For the purposes of section 81, ***delivered pricing*** means the practice of refusing a customer, or a person seeking to become a customer, delivery of an article at any place in which the supplier engages in a practice of making delivery of the article to any other of the supplier's customers on the same trade terms that would be available to the first-mentioned customer if his place of business were located in that place.

Definition of *trade terms*

(2) For the purposes of subsection (1), the expression ***trade terms*** means terms in respect of payment, units of purchase and reasonable technical and servicing requirements.

R.S., 1985, c. 19 (2nd Supp.), s. 45.

Delivered pricing

81 (1) Where, on application by the Commissioner, the Tribunal finds that delivered pricing is engaged in by a major supplier of an article in a market or is widespread in a market with the result that a customer, or a person seeking to become a customer, is denied an advantage that would otherwise be available to him in the market, the Tribunal may make an order prohibiting all or any of such suppliers from engaging in delivered pricing.

What we note about this approach is that it addressed the question of supply to a business, leaving retailer organization to (positively) discriminate in pricing to be competitive. We also note that the provision takes care of geographic differences.

The ACCC's evidence then refers to the situation in the UK where subsection 18(1) if the Competition Act 1998 includes, among other things that are an abuse of a dominant position, the '*application of dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage'.* Abuse is illegal if '*it may affect trade in the United Kingdom'.*

The Report concludes that '*A key part of this provision is that it requires the abuse of a dominant position – in the absence of this there is no general provision in the UK which prohibits discriminatory pricing.' (a paper by P. Whelan and P Marsden presented to the American Bar Association Antitrust Teleseminar series in 2006 was referenced).*

The implication here is that the UK approach based as it appears to be on the concept of market power, is not that different to our reliance on S46.

However, this is not the case:

- The ACCC evidence and the referenced paper are incorrect. The UK Act does contain a general prohibition as section 2 of that Act shows:

  2 Agreements etc. preventing, restricting or distorting competition.

  (1)Subject to section 3, agreements between undertakings, decisions by associations of undertakings or concerted practices which—

  (a)may affect trade within the United Kingdom, and

  (b)have as their object or effect the prevention, restriction or distortion of competition within the United Kingdom, are prohibited unless they are exempt in accordance with the provisions of this Part.

  (2)Subsection (1) applies, in particular, to agreements, decisions or practices which—

  (a)directly or indirectly fix purchase or selling prices or any other trading conditions;

  (b)limit or control production, markets, technical development or investment;

  (c)share markets or sources of supply;

  (d)apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

  (e)make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

Note that this section contains BOTH a 'purpose' and an 'effects' test.

- Note that the clause is contained in the parts of the Competition Act 1998 that could be considered the equivalent of S45 and S46 of Australia's Competition and Consumer Act.

- Note that both sections 2 and 18 contain the same non-exhaustive list of prohibited behaviours showing that the UK does not see the specific prohibitions as detracting from the thrust of the legislation.

The ACCC is again quoted in relation to US laws suggesting the enforcement approach:

> … has been to use the Robinson-Patman Act less and to now take action against price discrimination under the broader competition law framework (e.g. § 2 of the Sherman Act 1890), and only where the practices involved can be considered to be an attempt to monopolise. The ACCC considers that this is similar to the existing situation in Australia.[37]

We note the following:

- The Robinson-Patman Act prohibiting anti-competitive price discrimination has been in place since 1936, so there has been an opportunity for a cultural shift in business behaviour where it is quite clear to companies operating in the US what the rules of business are. This reduces the need for intervention by the regulator.

- There has been an increase in the number of private cases being taken, spurred on by the 'triple damages' rule where a private case that succeeds is awarded triple the amount of damage proven.

The Report's section dealing with the possible effect of the reintroduction of a price discrimination clause is erroneous, demonstrating again a lack of understanding of how anti-competitive price discrimination provisions work in

practice.

7.37 There appears to be two areas where price discrimination issues may be relevant to the dairy industry and the grocery sector generally. The first issue is the wholesale prices within the supply chain, including pricing differences between generic and branded milk and the price of milk offered by processors to different customers. The second is the different retail prices of generic and branded milk, although they are essentially the same product. An anti-competitive outcome may occur as a result of milk processors charging smaller retailers a higher price for their branded milk, to offset the lower wholesale price they receive for selling generic milk to Coles and Woolworths. The Chairman of NARGA expressed his frustration at this:

> … I have to admit that it does get up my nose that every day I figure out that I am actually subsidising Fonterra to sell house brand milk to Coles by the price they charge me for their branded milk and other products.[39]

The previous S49 would not have made it illegal to charge a different price for generic and branded milk at the wholesale level. However it would have required the supply of a private label brand to competitors of the major chains on similar terms, putting them in a position to compete.

This requirement would have meant that processors would have to take into account the need to supply additional volumes of milk at prices similar to those demanded by the chains, probably resulting in a decision not to offer such a large discount on private label milk.

Whilst current consumers of these products would then be paying more for milk than they do now (presuming the major chains would not forego more margin), the benefit of lower priced milk would be spread more widely through competitor outlets, and presumably the differential between private label and branded milk would be much less (as is the case in the UK), resulting in a lower level of erosion of branded product market share.

The second claim that '*the different retail prices of generic and branded milk'* may be relevant is also incorrect. Different brands of the same or similar product co-exist on grocery shelves in jurisdictions that have an ant-competitive price discrimination prohibition in place.

Again the ACCC is quoted to show that different terms of trade apply to larger customers:

> Generally speaking, larger customers will be supplied on more favourable terms (i.e. more generous rebates and discounts). For example, in its public submission Fonterra stated that it achieves lower unit costs, predominantly linked to volume, when selling to large customers. Fonterra states that additional benefits in dealing with larger customers include consistent purchasing patterns which enable manufacturing efficiencies. Fonterra stated that if a smaller wholesaler or retailer was to purchase the same volume as a larger customer, in general, they may be able to achieve similar discounts from Fonterra to the larger customer.[41]

Such differences in terms are not illegal in jurisdictions applying price discrimination rules. All the supplier needs to be able to show is that there are cost advantages associated with supplying the larger volumes and that these wholly or in part are passed on to the customer through the terms of trade.

What the prohibition does, however, is to prevent the reduction in price beyond the benefits of efficiencies associated with larger volumes – i.e. benefits that accrue to the buyer simple because of their market power, the result of which is an unwarranted decrease in price for the major chain and the need to increase prices to the chains' competitors, putting them at a competitive disadvantage.

In short, an anti-competitive pricing provision provides a framework for fair pricing and addresses the power imbalance between the supplier and the major chains.

This would be of significant assistance to the dairy industry.

The re-enactment of such a provision would also assist other markets currently under pressure from high levels of market concentration. Petrol and liquor come to mind.

Lastly we need to address the furphy that consumers would suffer should the provision be re-introduced as suggested by the ACCC:

> Mr Cassidy—… before the Coles action we already had quite a discrepancy in the price of branded versus home-brand milk. Indeed, that was shown in the report of this committee in, I think, table 3.4 [of *Milking it for all it's worth*]. The gap was about 60c or 70c a litre. What Coles has done, followed by others, might have widened that gap by 10c or 12c a litre. You then get the question: if it would have applied to the Coles behaviour, what would then be the case in relation to home-brand milk and branded milk more generally? Would that section result in the cost of home-brand milk increasing by 60c or 70c a litre, back to being equal to branded milk?

Firstly, Coles reduced the price of their cheapest milk by only 4.5c per litre and, according to available information were still making a profit at that price.

The existence of an anti-competitive price discrimination clause would require the processor to set a price for private label milk to the major chains that ensured he was also able to provide on equivalent terms to the chains' competitors (i.e. delivered in similar quantities to similar outlets.) This may have resulted in their setting a slightly higher price, but would have resulted in lower priced milk being more generally available.

The Law Council's comment in the report lacks understanding and validity:

> Such a law will more likely be harmful, since it would raise the cost to retailers of offering a discount on any product, because this would be required to be offered more widely than would otherwise have been the case. Such a law is likely to have the effect of increasing prices for consumer goods and staples generally, in all categories where generics or other forms of product differentiation are used, to the detriment of consumers and the economy.[45]

What we see in the case where a price discrimination clause exists is the spreading of the low price benefit and an increase in competitive tension as retailers competing with the major chains are in a better position to compete.

<u>Predatory pricing and market power</u>

We again see in this section several estimates of the market share of major chains, including an estimate by the Productivity Commission:

> 7.45 A recent draft report issued by the Productivity Commission estimated Woolworths' market share in 2009–10 to be 38 per cent, followed by Coles at 26 per cent, Metcash at 19 per cent, ALDI with three per cent and Franklins at one per cent.[47]

Apart from the fact that the combined shares only add up to 87%, the assessment is derived from evidence given by Woolworths.

Market share in the retail grocery market has here and elsewhere been traditionally measured through shares of packaged grocery sales (the market for packaged groceries). These show the following picture:

Fig 30. Growth in Market Share of Woolworths & Coles (1975-2009)

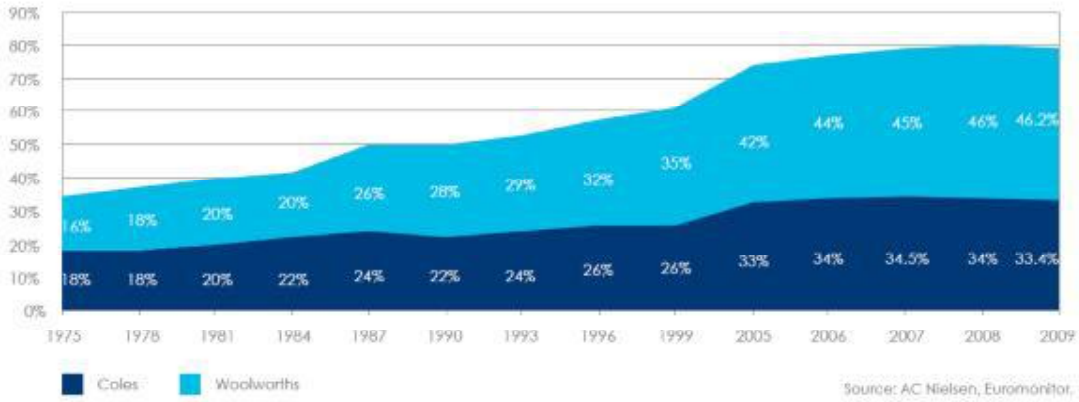

Fig 28. 2009 Turnover by supermarkets players (incl. Liquor sales)

	Turnover ($ billion)		Cumul		Market share	
	Incl. Liquor sales	excl. Liquor sales	Incl. Liquor sales	excl. Liquor sales	Incl. Liquor sales	excl. Liquor sales
Woolworths	$32.8	$27.6	$32.8	$27.6	47.4 %	45.6 %
Coles	$22.5	$20.1	$55.3	$47.7	32.7 %	33.2 %
IGA retail	$8.2	$7.7	$63.5	$55.4	11.9 %	12.7 %
FoodWorks	$1.7	$1.6	$65.2	$57.0	2.5 %	2.6 %
Franklins	$0.9	$0.9	$66.1	$57.9	1.3 %	1.4 %
Aldi	$2.3	$2.3	$68.4	$60.2	3.3 %	3.8 %
Spar	$0.4	$0.4	$68.8	$60.6	0.6 %	0.7 %
Total	$68.8	$60.6				

Sources: Company reports 2009, Euromonitor and other publications.. Convenience & forecourts retailers and specialist grocery retailers are excluded.

We note in the above table how the market share position changes depending on whether or not liquor is included.

It has become the trend in recent years to provide different estimates of market share by adding to the basic measure a range of other categories – categories which stores have more recently started to offer – and/or to add other providers of food to the definition of the 'market' – e.g. greengrocers, butchers, bakers and even fast food outlets and restaurants. These are clearly not supermarkets or considered to be 'grocery' outlets.

Market concentration is an important factor when considering market power in the context of S46. However the Treasury evidence tried to suggest that the recent entry of ALDI and Costco somehow dented the power of the majors:

> Mr Archer—Our submission points to a range of factors that are relevant to the consideration of the degree of competition in a particular market. That does include, but not exclusively, the degree of market share that participants have, but it also includes other factors, importantly barriers to entry that might exist in that market. We have seen in the retail sector Aldi introducing competition into the retailing sector and there is the prospect of other companies, such as Costco, coming in—they are in Melbourne.[48]

We note here that the UK Competition Commission's review of the grocery market categorized ALDI (and similar chains) as Limited Assorted Discount Stores (LADS) and excluded them from consideration as part of a market made up of full service supermarket outlets, suggesting their impact on competition, however defined, is limited.

Treasury also suggested that S46 was sufficient to control pricing behaviour:

> Concerns that the current conduct of supermarkets amounts to anti-competitive conduct would, if proven, appear capable of being dealt with under the existing prohibitions of the CCA, particularly section 46, which deals with the misuse of market power.[49]

We do not believe that the sale of low priced milk by the major chains was anti-competitive conduct, however the ability to sell milk at such a low price was a result of their market power unfettered by any aspect of the Act or how it is administered.

However, in the case of the dairy industry, no assessment appears to have been undertaken of the behaviour of the processors and the major chains in the context of sections of the Act other than that part of S46 dealing with predatory pricing.

While the ACCC assessed compliance on the predatory pricing issue, it needs to be pointed out that, in general, the absence of an anti-competitive price discrimination clause makes a predatory pricing case more difficult to prove.

This is because the major chain can command a price from a supplier so low that it is able to undercut a competitor without selling below relevant cost. So even if purpose could be proven, the behaviour would not be illegal.

Where an anti-competitive price discrimination clause exists, the difference in price offered to a major chain and its competitor would be less, more than likely requiring below cost selling in order for predatory behaviour to occur.

Prices set below cost can be assumed to be predatory as there is no other economic rationale for such behaviour.

We note here that S46(1) is qualified by S46(7), which states that purpose may be inferred.

> (7) Without in any way limiting the manner in which the purpose of a person may be established for the purposes of any other provision of this Act, a corporation may be taken to have taken advantage of its power for a purpose referred to in subsection (1) notwithstanding that, after all the evidence has been considered, the existence of that purpose is ascertainable only by inference from the conduct of the corporation or of any other person or from other relevant circumstances.

The section dealing with predatory pricing does not appear to benefit from this clause and therefore requires a higher test.

Section 46(1AA) is also relevant to the behaviour of processors, although this has not been assessed by the ACCC:

> (1AAA) If a corporation supplies goods or services for a sustained period at a price that is less than the relevant cost to the corporation of supplying the goods or services, the corporation may contravene subsection (1) even if the corporation cannot, and might not ever be able to, recoup losses incurred by supplying the goods or services.

Note here that the hurdle again is the 'purpose' test, whereas some other jurisdictions include an 'effects' test for predatory behaviour.

The effectiveness of Section 46

In its submission to the Dawson Committee inquiry the ACCC argued that the object of the general competition provisions of the CCA (then the Trade Practices Act) were to:

> … prohibit various types of conduct that are likely to maintain or enhance market power other than by competitive means.[53]

and expressed a number of concerns:

> … if the law does not even prohibit large firms with substantial market power from taking advantage of it with the effect of damaging competition—by virtue of such actions as an anti-competitive refusal to supply, anticompetitive predatory behaviour, anti-competitive leveraging of market power in one market to damage competition in another market—the law is not only deficient as a matter of economic policy, but deficient in relation to the above objectives.[54]

and:

> The reason for the distinction between s. 46 and the other Part IV prohibitions is not obvious. The policy objective of s. 46 is fundamentally the same as the other prohibitions in Part IV—that is, the prohibition of specified conduct that will damage competition. As well, Australia's prohibition on misuse of market power is inconsistent with similar prohibitions in the United Kingdom, Europe and the United States. The Commission believes the distinction between s. 46 and the other Part IV provisions should be removed. However, this does not suggest that the purpose test in s. 46 is inappropriate. As in ss. 45 and 47 a purpose test is an important element of s. 46 where it can be proved.[55]

We would agree with these comments and suggest that the effectiveness of the Act would be enhanced by the inclusion of an effects test in S46 and the inclusion of a series of prohibitions of specific anti-competitive behaviours as has been found necessary by other jurisdictions, particularly given the outcome of the Boral case.

Is it working?

The objective of the Act is as follows:

The object of this Act is to enhance the welfare of Australians through the promotion of competition and fair trading and provision for consumer protection.

The term 'competition', in the economic sense, is not defined by the Act leaving open the possibility of interpreting competition in accordance with any economic theory, whether or not such a theory is valid or applicable.

However, the primary purpose of enhancing community welfare is clear.

The question is whether the current Act is achieving that purpose.

Does the Act and the way it is administered result in more competitive markets, and how is this measured?

It is our view that the current Act lacks the ability to address market power associated with market concentration and, as a result, the trend towards higher levels of concentration continues unabated.

While higher levels of concentration in a market can, in the early stages, enhance economic efficiency – the benefits of which can be passed on to the consumer, too high a level of concentration leads to reduced efficiency and lower levels of innovation as smaller more innovative entities are squeezed out of the market.

They also allow the dominant players to simply share the market without genuine competition and hold on to higher margins, to the detriment of consumers.

We suggest that the Act needs to be amended to give the regulator more power to address the downside of market concentration and that a specific prohibition against anti-competitive price discrimination, whether as a stand-alone section or as part of an amended S46, should be part of any amendment.