# WESFARMERS

# SUBMISSION TO TREASURY

# ON THE COMPETITION POLICY

# REVIEW FINAL REPORT

## Executive Summary

Wesfarmers welcomes the opportunity to contribute to the Treasury consultation process on the Final Report of the Competition Policy Review. Wesfarmers supports the Review's ambition to re-energise the microeconomic reform agenda and help restore Australia's position as an international leader in productivity and efficiency.

In particular, Wesfarmers supports the recommendations in the Final Report:

(a) to remove remaining restrictions on retail trading hours so as to provide consumers the right and convenience to shop where they choose at the time they wish;

(b) that competition policy considerations should be taken into account in assessing restrictions in planning and zoning rules; and

(c) to repeal the current price signalling provisions. The disclosure of information is crucial to the effective and competitive operation of markets and should only be restricted in very specific circumstances.

Wesfarmers and its businesses welcome policy reform that encourages competition, removes unnecessary regulation and intervention and creates an environment to promote innovation and enhance efficiency for the benefit of Australia and all Australians.

Wesfarmers is however, concerned that three recommendations in the Final Report fail to achieve the Panel's stated goals of establishing competition laws that are clear, predictable and reliable, making markets work in the long-term interests of consumers and encouraging innovation and entrepreneurship.

### Section 46

Wesfarmers continues to have serious concerns regarding the proposal to amend section 46 (misuse of market power).

The existing wording of section 46 makes it clear that having market power itself is not unlawful; it is the **misuse** of that market power for the proscribed purposes that is prohibited. It is submitted that this is a reasonable position as many companies achieve market power by enhancing efficiencies, competing effectively and driving innovation. The current law gives certainty to businesses, as a business will always be clear as to the purpose of its conduct.

However, the recommended amendments to section 46 would make *any* conduct by a company with market power unlawful if that conduct has the purpose, effect or likely effect of substantially lessening competition in a market, regardless of whether the conduct is innovative, drives efficiencies and brings lower prices and better service to consumers. Notably, exactly the same conduct by a competitor which does not have market power will not be prohibited. Despite the Panel's stated intentions, the focus of the law would shift therefore from the promotion of competition and the consumer's interests to protection of the competitor.

Further, the application and implementation of the amendments is fraught with difficulty and uncertainty. Businesses with market power make a multitude of decisions with proper competitive purposes daily, the actual effect (or even likely effect) of which are unknown and may be difficult to predict. Rather, the effect may only be judged in hindsight. Further no guidance is provided as to the relevant timeframe applied to assess the effect of such conduct. Wesfarmers' concern is that the recommendations in the Final Report in relation to section 46:

(a) will stifle risk taking, efficiencies and innovation by Australia's most successful companies due to the uncertainty surrounding assessment of the effect of a company's conduct even if it was for a legitimate and pro-competitive purpose;

(b) will create an "uneven playing field" between companies in the same industry as conduct that is acceptable by a company without market power is prohibited by a company with market power; and

(c) will provide a competitive advantage to foreign entrants in comparison to the established incumbent (who are often established Australian-owned companies) which may well result in profits flowing offshore.

At a time when Australia should be focussing on the need to promote and enhance innovation, efficiency and productivity, competition regulation that creates uncertainty and risks consequences as outlined above cannot be in the best interests of Australia or Australians (as consumers, employees, shareholders, superannuation holders and taxpayers).

Amendments to section 46 have been considered in 12 reviews and discussion papers since 1976. All of them recommended against the introduction of an "effects" test into section 46 with two exceptions: the Government's 1984 Green Paper – which invited discussion on a proposed effects test – and now the Harper Review. There is even less reason to adopt a different approach now, particularly in light of increasingly competitive global markets and technological transformations requiring Australian companies to adapt, operate and compete more efficiently in order to survive and succeed.

**Section 45**

The recommendation in the Final Report to include in section 45 a prohibition on "concerted practices" will create additional uncertainty and is unnecessary as truly anti-competitive disclosures of price and other information are likely to be caught by current laws (as recognised by the Panel itself).

If despite these reservations, section 45 is amended to include "concerted practices", it is vital that the resulting uncertainty be addressed by providing clear legislative definitions or regulations outlining what is considered to constitute "concerted practice".

**Section 47**

Wesfarmers does not support the removal of section 47 leaving all vertical supply restrictions to be assessed under section 45 as the section provides businesses with a useful guide as to the prohibited categories of conduct, acting as an aid to compliance. However, in Wesfarmers' view, the current section 47 should be simplified as it is overly complex and difficult to understand.

## 1 Introduction

In the 20 years since the Hilmer Review, the Australian and world economies have changed dramatically and are now more closely interconnected than ever before. These changes are highly likely to accelerate over the next 20 years, and Australia's competition policy, laws and institutions must be flexible and responsive to take full advantage of these developments. It is imperative that regulation not act as an impediment to productivity and efficiency.

Wesfarmers welcomes the Panel's recognition that new developments in technology are transforming, and will continue to transform, the way markets operate. Retail industries such as those in which Wesfarmers participates have been among the first to be exposed to these digital disruptions, providing previously unimaginable improvements to customer choice and convenience as well as supply chain management and logistics.

An increasing number of goods and services can now be purchased online at any time of the day or night, and delivered from anywhere in the world to Australian homes often long before the consumer would have found time to get to the shops. Developments in logistics also allow overseas operators to establish and scale up a physical presence with minimal advance preparation, investment and risk.

Competition policy must acknowledge the changes that have occurred and respond to changes yet to come. It should be flexible enough to review assumptions where they no longer serve Australia's needs.

Wesfarmers supports the Panel's view that competition policy should:

- ensure markets work in the long-term interests of consumers;
- foster diversity, choice and responsiveness in government services;
- encourage innovation, entrepreneurship and the entry of new players;
- promote efficient investment in and use of infrastructure and natural resources;
- establish competition laws and regulations that are clear, predictable and reliable; and
- secure necessary standards of access and equity.

These are far-reaching goals and will be challenging to implement, requiring the cooperation of all levels of Australian government in what is likely to remain an unpredictable political environment. There is a danger that the reform process may be overtaken by sectional interests, and that difficult but important reforms will be sacrificed for ill-advised but more easily achievable changes.

Accordingly, while the present Treasury consultation process may be focused on recommended changes to the *Competition and Consumer Act 2010* (**CCA**) and issues relevant to small business, these issues must not be isolated from the broader program of essential microeconomic reform proposed by the Final Report.

## 2 Competition Policy

Wesfarmers welcomes and supports the Panel's findings and recommendations relating to competition policy to be implemented by Commonwealth, state, territory and local governments.

### 2.1 Key retail markets

Wesfarmers welcomes the analysis of the retail markets of grocery and fuel retailing. Wesfarmers agrees with the Panel's finding that:

> Australia's grocery market is concentrated, but not uniquely so. While concentration is relevant, it is not determinative of the level of competition in a market. A concentrated market with significant barriers to entry may be conducive to weak competition, but competition between supermarkets in Australia appears to have intensified in recent years following Wesfarmers' acquisition of Coles and the expansion of ALDI and Costco. Consequently, few concerns have been raised about prices charged to consumers by supermarkets.

Wesfarmers can attest that the supermarket sector is vigorously competitive and that competition has increased in recent years. Even the Final Report confirms that barriers to entry are not high and that prices to consumers have dropped in real terms due to intense competition and improved efficiencies.

While acknowledging the concerns of some market participants, the Final Report concludes that any concerns with the structure of these markets can be addressed by reducing regulatory impediments to competition and otherwise taking advantage of existing frameworks rather than by any sector-specific changes to competition law or policy. Wesfarmers agrees that "consumer preferences and choice should be the ultimate determinants of which businesses succeed and prosper in a market."

In relation to fuel retailing, the Final Report confirms previous ACCC findings that the industry is competitive and has benefited from the participation of supermarkets, that any concerns about supermarket shopper dockets are adequately addressed by the existing law, and that no substantial recommendations for change are appropriate to this sector.

However, changes proposed by the Final Report to the general competition law would have a particular impact on the grocery and fuel retailing industries. The loudest calls for an "effects" test in section 46 have come from smaller competitors to the major supermarket chains, and concerns with the law applying to information exchanges have arisen specifically in relation to petrol prices.

Although the Final Report's proposals are expressed to apply equally throughout the economy, in both their history and in their practical impact they are closely tied to the major supermarkets and fuel retailers. Since the Panel has so clearly found that these sectors are competitive and working well for consumers, Wesfarmers is concerned at the recommendations of the Final Report that could subject these industries to regulatory uncertainty and intervention to the ultimate detriment of consumers.

These concerns are further discussed in section 3 of this submission.

### 2.2 Retail trading hours

Wesfarmers strongly supports the Panel's recommendation for the removal of remaining restrictions on retail trading hours. It also notes the Panel's recommendation that, to the extent that jurisdictions choose to retain restrictions, these should be strictly limited to Christmas Day, Good Friday and the morning of Anzac Day, consistent with the best-practice model as currently operating in Victoria and Tasmania.

The patchwork of restrictions on retail trading within and between state and territory jurisdictions imposes significant compliance costs on business, adds to complexity, and denies consumers the right and convenience to shop where they choose at the time they wish. It is also inherently anti-

competitive, and ignores the changing dynamics of retail globally, given the freedom of consumers to purchase products online at any time.

Trading hour regulations prevent customers from shopping at a time best suited to their needs. They also limit the capacity for stores to manage their stocks effectively – particularly in the case of produce and other perishable goods – and to prepare to trade immediately after a closed day, since preparatory activities for a day's trading are most efficiently undertaken on the previous evening when the store has been otherwise open for trading that day.

Wesfarmers welcomes the extensive analysis of the impact on business, the economy and consumers of this incoherent and inconsistent regulatory framework in the 10 October 2014 report by the Productivity Commission, *Cost of Doing Business: Retail Trade*.

Wesfarmers notes in particular two key conclusions reached by the Productivity Commission:

- that governments at all levels can best provide support by encouraging an open, competitive and innovative retail sector "with the capacity to adjust quickly and efficiently to changes in technologies, the development of new goods and services and changes in consumer tastes and preferences";[1] and

- that "addressing deficiencies in the regulatory environment such as those related to trading hours and planning and zoning has the potential to lower retailers' costs over time, create a more competitive and sustainable sector, and ultimately benefit consumers through greater choice and affordability."[2]

Wesfarmers is pleased that the Productivity Commission has identified and acknowledged that restrictions on retail trading hours are increasingly out of step with changing patterns of work, leisure and shopping, and impose additional costs on retailers, the economy – and, ultimately, consumers – through forgone sales and higher operational and capital costs.

Wesfarmers also welcomes the Productivity Commission's rejection of factually unsupported commentary around the impact of trading hours liberalisation. As the Commission also points out, regional economies can lose out from a restrictive approach, with retailers and consumers suffering comparative disadvantage outside areas where trading hours are extended.

> [T]he evidence does not support the claim that deregulation of trading hours has a material effect on the structure of the retail sector and the viability of smaller retailers. By using the participation of small business in the market as a metric for competition, trading hours restrictions ignore the potential for more than offsetting gains in terms of the lower cost of doing business and increased consumer welfare in such an economically significant sector.[3]

The Productivity Commission's Research Report goes into considerable and persuasive detail in analysing the inconsistencies and costs of the remaining restrictions on trading hours, and provides ample support for the Panel's recommendation.

### 2.3 Planning and zoning

Wesfarmers welcomes the Panel's recommendation that competition policy considerations should be taken into account in assessing restrictions in planning and zoning rules, and agrees that planning systems can create barriers to entry, diversification and expansion in retail industries.

[1] Productivity Commission, Research Report into the Costs of Doing Business: Retail, October, 2014, p 24.

[2] At p 24

[3] At p10

Retail developers need a planning system that is consistent and transparent. Currently, the combination of multiple regimes and multiple state-based regulators means the planning system imposes significant compliance and time delay costs on retailers and developers who are trying to expand their services to meet customer demand.

Each State and Territory has its own system of zones, processes, timelines and appeal paths. Based on Wesfarmers' experience working across all States and Territories of Australia, the Northern Territory, Western Australia and South Australia planning systems are considered the most straightforward, with New South Wales and Queensland the most complex.

The current NSW development consent application system is inconsistent and legalistic. It is also heavily focused on process rather than outcomes with multiple approval processes. Overly prescriptive conditions are imposed frequently. However, we note that the NSW Government has completed a review of its strategic planning system in recent years and proposed a number of reforms which will hopefully be fully implemented.

The Queensland planning system too is complex and requires more detailed design work to be completed for applications than in other jurisdictions. In Queensland, our experience has been that planning approvals often go beyond just planning, and can include compliance issues associated with the actual construction. This adds unnecessary costs and delays in the initial approval process.

For example, the approval of a new store in Queensland had 148 conditions and 37 advisory notes attached, over and above the approved drawings which were added after our business representatives had participated in numerous meetings with council and changed the drawings to suit its requests.

As a comparison, a new store in WA, which was a similar size project, had only 34 conditions attached, And the planning and approval was completed in under half the time of the Queensland store with considerable cost savings.

In the future, there needs to be a transparent process in place that is evidence based and outcome focused to ensure greater consistency and certainty for retail developers.

Some examples of sensible reforms include:

- planning approvals being evaluated on technical merit in accordance with legislation. For example, in regional NSW, councillors entered into direct negotiations with a business influencing conditions such as car park requirements in conflict with the requirements of the State Road Authority;

- improved design and public amenity from the use of Design Review Panels in NSW and Victoria. We note that design review panels sometimes look at aspirational goals, which may not reflect existing parameters, zoning or site constraints. An example of this is where a council urban planner wrote that entries to the store car park were required in the side street, yet the council zone prohibited retail traffic using the side streets;

- development and application of a consistent National Planning Code similar to the National Construction Code. This would avoid site-specific conditions that councils may impose unilaterally;

- all State and Territory governments legislating to require councils to hold a compulsory pre-lodgement meeting for commercial developments, to ensure open communication concerning requirements, timing and approval processes;

- allowing applicants to liaise with Referral Authorities pre-lodging with councils, to reduce local government planning officer workloads and time delays for planning decisions;

- development and application of an Australian Standard for planning permit conditions to promote increased consistency. A common format and language guide would ensure all permits are written the same way and address the same issues. In addition, the recommendations or requirements of all Referral Authorities should be attached to the council's approved documents; and

- planning and zoning systems need to be reviewed and benchmarked regularly across Australia and internationally to ensure best-practice outcomes are delivered.

### 2.4 Liquor sales

The responsible consumption of alcohol is a lawful, socially acceptable activity. The majority of people who consume alcohol do so responsibly.

Wesfarmers is one of Australia's largest liquor operators with 853 stores and 90 hotels across Australia, employing more than 7,500 team members. Wesfarmers is committed to the responsible service, supply and promotion of alcohol, and fully supports the Panel's comments on the importance of reducing alcohol-related harm in the community.

As a national retailer, we assume considerable responsibilities when selling alcohol, given the problems that may arise from excessive and harmful consumption of alcohol by a minority in the community. Liquor licensing laws set out many of these responsibilities and are aimed at protecting individuals and the broader community from harm caused by alcohol abuse.

Wesfarmers has always worked with key stakeholders, including police, councils and local communities to address such issues and in many communities has voluntarily introduced measures, such as removing products from sale or tailoring trading hours, to assist communities with the effective management of alcohol-harm related measures.

Wesfarmers is supportive of harm minimisation measures that are targeted, evidence based and proportional, and which do not penalise the vast majority of customers who consume alcohol in a responsible manner and do not cause harm to themselves or those around them.

As was highlighted in the Productivity Commission's recent report:

> even when regulation is justified and imposes efficient compliance costs, when that regulation differs between and within jurisdictions, retailers operating in more than one jurisdiction incur added compliance costs from the complexity of multiple sets of differing regulation.[4]

Regulations differ by jurisdiction in a number of areas in the liquor sector, including where liquor can be sold, the sale of sundries in a licensed liquor store, responsible Service of Alcohol (RSA) certificates, and changing floor plans of licensed areas.

We support the Panel's view that there is no reason why liquor regulation should not be subject to regular review. We are particularly supportive of reviews that seek to promote uniformity in regulatory frameworks across jurisdictions. In the case of liquor licensing, it is vital that regulation is predicated upon the tenets of evidence-based harm minimisation – not on providing competitive advantage to one class of retailers over another.

Wesfarmers believes any changes to liquor licensing laws should be consistent with the Federal Government's commitment to reduce red tape and the regulatory burden on <u>all</u> business.

[4] Productivity Commission's Report into the Costs of Doing Business: Retail Trade Industry, 2014, pg 13

## 3 Competition law

Wesfarmers welcomes the Panel's principled approach to its review of the competition laws. It fully supports the key questions framed by the Panel in assessing whether these laws are fit for purpose:

- Does the law focus on enhancing consumer wellbeing over the long term?
- Does the law protect competition rather than protecting individual competitors?
- Does the law strike the right balance between prohibiting anti-competitive conduct and not interfering with efficiency, innovation and entrepreneurship?
- Is the law as clear, simple and predictable as it can be?

Wesfarmers supports the majority of the Final Report's recommendations and considers that they are consistent with the principles set out above. However, in some instances Wesfarmers is concerned that these principles are applied inconsistently or may not be achieved by the Panel's recommendations.

In this context it is important to consider the local, regional and global developments identified by the Panel as key incentives for this Review, in particular the increase in globalisation and the digital revolution. In these times of great change and innovation, it is useful for Australia to look to the other major competition law jurisdictions and decide whether it will follow the more interventionist European approach or the market-based approach of the United States.

US antitrust jurisprudence and enforcement appears to give greater recognition to the increasing transience of market power in industries affected by technology – which may soon extend to every industry – and the inevitability of new and innovative solutions that can quickly disrupt apparently unassailable monopolies. European jurisprudence appears to place less faith in markets to self-correct and is more concerned with the immediate impact on competitors. Indeed, it has often been claimed that the US protects competition while Europe protects competitors.

In Wesfarmers' view, Australia should look to the US for its antitrust law.

### 3.1 Price signalling and concerted practices

Wesfarmers supports the Final Report's recommendation that the current price signalling provisions be repealed. We agree that the disclosure of information is crucial to the effective operation of markets and should only be restricted in very specific circumstances.

However, Wesfarmers does not agree with the recommendation in the Final Report to include in section 45 a prohibition on "concerted practices" as, in Wesfarmers' view, this creates additional uncertainty and truly anti-competitive disclosures of price and other information will be caught by current laws. As noted by the Panel:

> Other provisions of the competition law are capable of addressing anti-competitive price signalling. For example, if the price signalling causes competitors to agree the level of their prices, the conduct will be prohibited as price fixing by the cartel provisions. If, on the other hand, the price signalling falls short of price fixing but has the effect of substantially lessening competition (by enabling competitors to co-ordinate their pricing decisions), the conduct will generally be prohibited by section 45.

In light of the Panel's doubts as to whether any change in the law is necessary, it is surprising that the Final Report recommends the expansion of section 45 to prohibit a person engaging in a concerted practice with one or more other persons that has the purpose, effect or likely effect of substantially lessening competition.

As the Panel recognises, the concept of a concerted practice is not familiar to Australian jurisprudence, though it is familiar in Europe. The Final Report includes a number of explanations of the concept:

> [A] concerted practice is a regular and deliberate activity undertaken by two or more firms.
>
> It would include the regular disclosure or exchange of price information between two firms, whether or not it is possible to show that the firms had reached an understanding about the disclosure or exchange…
>
> The word "concerted" means jointly arranged or carried out or co-ordinated. Hence, a concerted practice between market participants is a practice that is jointly arranged or carried out or co-ordinated between the participants.
>
> The expression "concerted practice with one or more other persons" conveys that the impugned practice is neither unilateral conduct nor mere parallel conduct by market participants (for example, suppliers selling products at the same price).

The complexity of these explanations must cast some doubt on the Panel's conclusion that:

> [T]he word "concerted" has a clear and practical meaning and no further definition is required for the purposes of a legal enactment.

In Wesfarmers' view, this recommendation fails to achieve the Panel's stated goals of establishing competition laws that are clear, predictable and reliable and making markets work in the long-term interests of consumers. Amendments should not be introduced which are likely to create confusion, uncertainty and unpredictability. This would be likely to result in increased compliance costs (and hence lower productivity and efficiency) and reduced pro-competitive disclosure of information.

As noted by the Panel, the concept of a "concerted practice" has been developed in Europe through European case law and European Commission Guidelines on Article 101 of the Treaty for the Functioning of the European Union (**TFEU**). The EC Guidelines state that:

> In line with the jurisprudence of the Court of Justice of the European Union, the concept of a concerted practice refers to a form of coordination between undertakings by which, without it having reached the stage where an agreement properly so-called has been concluded, practical cooperation between them is knowingly substituted for the risks of competition. If there is no agreement on information exchange, it will have to be assessed on a case-by-case basis whether a concerted practice can be found or whether, for example, the regular dissemination of information of a company is a truly unilateral action which does not fall within the scope of Article 101(1).[5]

"Truly unilateral conduct" would include responding to a competitor's conduct even where that results in similar or parallel conduct being adopted:

> It is necessary to bear in mind that, although Article 101 TFEU prohibits any form of collusion which distorts competition, it does not deprive economic operators of the right to adapt themselves intelligently to the existing and anticipated conduct of their competitors...
>
> Parallel conduct, of itself, will only be held to establish the existence of a concerted practice in a scenario where concertation constitutes the only plausible explanation for the parallel conduct.[6]

As set out in the EC Guidelines, a *purely* unilateral disclosure of information will not constitute a concerted practice, but where a disclosure involves reciprocity or acceptance it will not be purely

[5] At p 16.

[6] See OECD Roundtable, Unilateral Disclosure of Information with Anticompetitive Effects, 14 February 2014, at pp 3-4.

unilateral and may constitute a concerted practice. These considerations depend on the nature of the information, whether the disclosure is public or private, and how other firms appear to have responded to or distanced themselves from the disclosure.

It is uncertain whether Australian courts or the ACCC would reach similar conclusions or apply similar considerations in interpreting the prohibition on concerted practices recommended by the Panel.

If information disclosure or exchange is considered to be a concerted practice, it remains to consider its effect on competition. The EC Guidelines note:

> Information exchange is very often pro-competitive as it can lead to, for example, an intensification of competition or significant efficiency gains. However, in situations where the exchange of market information is liable to enable undertakings to be aware of market strategies of their competitors it may lead to restrictive effects on competition. The competitive outcome of information exchange depends on the characteristics of the market in which it takes place (such as concentration, transparency, stability, complexity etc.) as well as on the type of information that is exchanged, which may modify the relevant market environment towards one liable to coordination.[7]

The EC Guidelines go into useful detail about the market characteristics that are likely to make information exchanges problematic as well as the characteristics of the information to be exchanged: for example whether it is commercially sensitive, whether it is genuinely public data or not, whether it is available to all market participants, whether it is aggregated or individualised, how old it is and how frequently it is exchanged.

In Australia, in the absence of clear guidance on which factors will be taken into account, and how they may be weighted, it will be difficult for business to make decisions on the circumstances in which information exchanges, which in many instances increase transparency, competition and empower consumers, may be considered anticompetitive.

Article 101(3) also provides that an otherwise anti-competitive agreement or concerted practice that "contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit" will not be prohibited, subject to certain conditions.

In Australia, it is not clear whether or how these public benefit or efficiency considerations are to be taken into account in the "substantial lessening of competition" test or whether they can only be taken into account in an authorisation context.

If, despite the objections outlined above, a prohibition on concerted practices is added to section 45, it will be necessary to develop, through public consultation, a clear legislative definition addressing:

- when conduct will be considered a concerted practice;
- when information disclosures will be considered to substantially lessen competition; and
- whether and how efficiency gains and other public benefits will be taken into account.

Wesfarmers notes that prices in the supermarket industry are highly transparent, with national pricing for the majority of products easily discoverable from the major supermarket chains' online shopping services and weekly specials clearly announced and aggregated by several third-party websites for the benefit of customers. Because of this transparency, supermarkets are quick to match each other's price reductions, again benefiting all consumers. This responsive parallel conduct is the essence of competition and it is critical that any treatment of concerted practices is able to reliably distinguish competition and transparency from anti-competitive coordination.

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[7] At p 17.

### 3.2 Misuse of market power

Wesfarmers remains concerned at the Panel's proposal to replace section 46 with a new section that:

- adds an "effects" alternative to the current "purpose" test;
- removes the "take advantage" element; and
- replaces the enumerated categories of exclusionary conduct with a general "substantial lessening of competition" test.

The proposal to add an "effects" test to section 46 has been closely associated with the Review since it was first detailed by the Coalition, with specific reference to retail industries including those in which Wesfarmers operates.

Although the scope and ambition of the Competition Policy Review has greatly expanded since then, the intersection between retail markets, small business and an "effects" test for section 46 has remained a focus of the Review. It is disappointing that the Final Report has not been able to move beyond the origins of the Review in this area, given its findings that key retail markets are competitive and benefit consumers and the Review's desire to ensure entrepreneurship and innovation.

In Wesfarmers' view, the recommendation in the Final Report in relation to section 46 fails to achieve the Panel's stated goals of establishing competition laws that are clear, predictable and reliable and that make markets work in the long-term interests of consumers.

Amendments to section 46 have been considered in 12 reviews and discussion papers since 1976. All of them recommended against the introduction of an "effects" test into section 46 with two exceptions: the Government's 1984 Green Paper – which invited discussion on a proposed effects test – and now the Harper Review. In Wesfarmers' view, the recommended amendments to section 46 are unwarranted and undesirable for the following reasons.

#### (a) No case for change has been made

The Final Report does not argue that the current section 46 is failing to deter or capture any anti-competitive conduct that it should be deterring or capturing. Nor does it argue that any cases under the current section 46 have been decided wrongly or have allowed any competitive detriment or consumer harm to go unrestrained or unpunished.

#### (b) The "take advantage" element should be retained

The Final Report argues that the "take advantage" element is the primary concern with the current section 46, and that it is difficult for courts to interpret and apply. As evidence for this proposition it points out that, in a number of cases, trial and appellate courts have reached different views on whether particular conduct met the test.

The fact that judges reached different conclusions on the facts says little about the test – except that it is designed to make sometimes difficult judgments about whether a company's behaviour represents legitimate competition on the merits or anti-competitive conduct. Any proposed change to section 46 – and in particular the general test and broad directions proposed by the Final Report – would be subject to even greater judicial divergence and would significantly increase uncertainty compared to the current section.

The established interpretation of the "take advantage" test is that a firm will not take advantage of its market power if it would, or could profitably, have engaged in the same conduct without that market power. That test was again confirmed and applied without apparent difficulty in the recent *Pfizer* case.

The Panel expresses concern that this interpretation may not recognise that conduct engaged in by a firm with market power may have a greater impact than the same conduct engaged in by a firm without market power, and that:

> Business conduct should not be immunised merely because it is often undertaken by firms without market power. Conduct such as exclusive dealing, loss-leader pricing and cross-subsidisation may all be undertaken by firms without market power without raising competition concerns, while the same conduct undertaken by a firm with market power might raise competition concerns.

However, the fact that conduct by a firm with market power may have a greater impact than the same conduct by a firm without market power does not justify the removal of the "take advantage" or "misuse" element of the provision. This element of the provision creates a crucial causal connection between the market power and the conduct under consideration. It does not operate to immunise categories of conduct on the basis that they are also undertaken by firms without market power, but involves a consideration of the market power and the relationship of that market power to the relevant conduct.

The existing wording of section 46 makes it clear that having market power itself is not the issue; it is the **misuse** of that market power for a proscribed purpose that is inappropriate.

Companies with substantial market power are already examined with particular scrutiny (firms without market power do not fall under section 46 at all), but that does not mean that firms with substantial market power should be restrained from engaging in conduct that has no connection to their market power. There is no evidence of widespread misapplication of the existing test.

### (c) The "purpose" test is essential and appropriate

The Final Report describes the debate over purpose and effect "unproductive" and argues that it "tends to obscure a more significant issue":

> Presently, the purpose test in section 46 focuses on harm to individual competitors – conduct will be prohibited if it has the purpose of eliminating or substantially damaging a **competitor**, preventing the entry of a **person** into a market, or deterring or preventing a **person** from engaging in competitive conduct.
>
> Ordinarily, competition law is not concerned with harm to individual competitors.

Wesfarmers agrees that competition law should not be concerned with harm to individual competitors. But section 46 is not concerned with harm to individual competitors. It is concerned with protecting the competitive process by preventing the **misuse** of market power for a predatory or exclusionary purpose.

As the Federal Court noted in the *Eastern Express* case:[8]

> Part IV of the Act is designed to promote competition, and the role of Section 46 is to maintain competitive markets by restraining misuses of market power that will produce a non-competitive market.

To suggest that section 46 is intended or likely to protect individual competitors is to ignore decades of clear and consistent interpretation and application by both courts and regulators. In fact, the proposed amendments to section 46 increase the focus on competitors, by prohibiting conduct by some competitors but permitting other competitors to engage in the identical conduct. ,

[8] *Eastern Express Pty Limited v General Newspapers Pty Limited* (1992) ATPR ¶41-167

### (d) Section 46 is not out of step internationally

The Final Report also argues that the focus of section 46 is inconsistent with comparable provisions in international jurisprudence, but the examples it gives are not convincing.

In relation to the **United States,** the Final Report cites the American Bar Association's opinion that:

> Modern U.S. decisions hold that it is not subjective intent but objective intent that is relevant, and that intent can be inferred from conduct and effect. The focus of the U.S. courts is on evidence of monopoly power and proof of exclusionary conduct.

Not only does the ABA acknowledge that intent – that is, purpose – remains an essential element in the United States, but it continues:

> Similarly, in Australia it appears that "purpose" is considered broadly under an objective—not a subjective—standard… it seems clear that Australian courts can and do consider the totality of the circumstances in determining whether a corporation possesses the requisite anticompetitive purpose, including analysing the nature of the conduct and its likely effect.

That is, the submission concludes that the current Australian position is closely aligned to that of the United States.

Similarly, in relation to **Canada** the Final Report notes that:

> [S]ection 79 of the Competition Act prohibits anti-competitive conduct by a dominant firm that has the effect or likely effect of substantially lessening competition.

However, "anti-competitive conduct" is defined in the Act to include a number of acts with particular purposes directed against actual or potential competitors. As the Federal Court of Appeal has confirmed: [9]

> First, an anti-competitive act is identified by reference to its purpose. Second, the requisite purpose is an intended predatory, exclusionary or disciplinary negative effect on a competitor.

The key difference between the Canadian law and the section 46 is that the Canadian law requires not only an anti-competitive purpose but *also* an effect of substantially lessening competition. In Wesfarmers' view, this is an appropriate use of that test.

Finally, in relation to **Europe**, the actual position in practice is, in Wesfarmers' view, much closer to the current Australian position than reflected in the Final Report. European law refers to an "abuse" of a dominant position – that is a dominant position is not itself anti-competitive, but, as the European Commission explains, if the company *exploits this position to eliminate competition,* it is considered to have abused it.[10]

Although early European decisions have been interpreted to query the need for a causal connection between the dominant position and the conduct in question,[11] more recent cases have confirmed that the law "presupposes a link between the dominant position and the alleged abusive conduct".[12]

This principle is also expressed in the European defence of objective justification in the form of legitimate business conduct or efficiency gains, which operates to exempt conduct that has no connection with market power. Similar to the "take advantage" element in the existing section 46, and

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9 *Canada (Commissioner of Competition) v. Canada Pipe Co* (2006) FCA 233.

10 European Commission website at http://ec.europa.eu/competition/consumers/abuse_en.html

11 eg *Europemballage Corporation and Continental Can Company v Commission,* Case 6/72 R [1972] ECR 215.

12 eg *Tetra Pak International SA v Commission,* Case C-333/94 [1996] ECR I-5951; *Konkurrensverket v TeliaSonera AB*, Case C-52/09 [2011] ECR I-00527

inherent in the concept of "misuse", there must be a causal or facilitating relationship between market power and the conduct in question.

The Panel's proposal for section 46 would be broader and more interventionist than that of Europe or indeed of any antitrust jurisdiction.

### (e) The "substantial lessening of competition" test is not appropriate

The Final Report argues that the "standard test" of the CCA asks whether conduct "has the purpose, or has or would be likely to have the effect, of substantially lessening competition." Although the Panel's recommendations, if implemented, would go some way towards establishing that test as a standard, there remain a wide range of tests throughout the CCA. For example:

- sections 45 (anti-competitive agreements) and 47 (exclusive dealing) require a purpose, effect or likely effect of substantially lessening competition;
- section 50 (mergers) requires an effect or likely effect of substantially lessening competition;
- Division 1 (cartels) requires a purpose, effect or likely effect of fixing prices, a purpose of restricting output, a purpose of market-sharing or a purpose of bid-rigging;
- Division 1A (price signalling) requires a private disclosure to competitors outside the ordinary course of business or a public disclosure for the purpose of substantially lessening competition;
- sections 45D, and 45DA (secondary boycotts) require a purpose **and** likely effect of causing substantial loss or damage to a person, or a purpose **and** effect of substantially lessening competition, respectively.

The key difference between the "effect of substantially lessening competition" provisions and section 46 is that only section 46 deals with the unilateral conduct of a single firm acting alone. The Dawson Review recognised the significance of this distinction:

> [T]hose other provisions are, as is noted above, concerned with conduct involving competitive relationships between two or more corporations, whereas section 46 is concerned with unilateral anti-competitive behaviour on the part of a corporation with a substantial degree of market power.
>
> It is the behaviour which gives rise to the prohibition rather than its effect although, of course, the ultimate object of the section is to protect and advance a competitive environment and the competitive process rather than to protect individual competitors. The section pursues that object by restraining the misuse of market power. Misuse occurs when a corporation takes advantage of the power for a proscribed purpose, regardless of the actual effect of the conduct, whether it be the achievement of a proscribed purpose or the substantial lessening of competition.

On this last issue, it has been suggested that previous rejections of "effects" tests for section 46 have only considered adding an "effects" alternative to the existing section, and have not considered a test that looks for a purpose, effect or likely effect of substantially lessening competition. In fact the test proposed by the Final Report has been considered and explicitly rejected many times:

- the **Dawson Review** (2003) considered that a "substantial lessening of competition" test for section 46 would be worse than simply adding "or effect or likely effect" and that "*since the effect of legitimate competitive activities may result in the lessening of competition in a market, the section, as amended, would be likely to catch pro-competitive as well as anti-competitive conduct*".

- the **Hilmer Review** (1993) considered that a "substantial lessening of competition" test in section 46 "*does not address the central issue of how to distinguish between socially detrimental and socially beneficial conduct.*"

- the **Cooney Review** (1991) considered a "substantial lessening of competition" test for section 46 but considered that "purpose is an essential element of the contravention" and that an effects test would "*force corporations to evaluate the potential effect of their every action on their competitors and potential competitors*".

- the **Griffiths Review** (1989) considered proposals to replace section 46 with "*a provision which prohibits a corporation with a substantial degree of power in a market from engaging in conduct which has the purpose or has or is likely to have the effect of lessening competition in any market*" but found that no change to the law was necessary.

It is common internationally to have quite different tests for unilateral conduct and arrangements between market participants. Articles 101 and 102 of the Treaty for the Functioning of the European Union maintain this distinction, as do Sections 1 and 2 of the US Sherman Act. Applying the same test to unilateral and multilateral conduct in Australia would be arbitrary at best.

### (f) The proposed court directions will not protect legitimate commercial conduct

The Final Report recognises the need to distinguish between competition on the merits and harmful anti-competitive conduct and proposes to assist in this distinction by directing the court to take into account:

- the extent to which the conduct has the purpose, or would have or be likely to have the effect, of increasing competition in the market including by enhancing efficiency, innovation, product quality or price competitiveness in the market; and

- the extent to which the conduct has the purpose, or would have or be likely to have the effect, of lessening competition in the market including by preventing, restricting or deterring the potential for competitive conduct in the market or new entry into the market.

It is not clear that this provision adds any clarity. As Stephen King and Graeme Samuel note:

> The proposed legislative guidance will not help the courts. Rather it just restates obvious principles. If actions are pro-competitive then they are not anti-competitive.

Nor will this guidance help business to understand or predict whether its conduct may be considered to have the purpose or effect of substantially lessening competition. In fact, it attempts to clarify one competition test by adding two more competition tests, compounding the confusion and the likelihood of error.

Wesfarmers is concerned that efficiency and innovation may only be relevant to the competition test where they affect the competitive structure of a market, such as by allowing smaller businesses to compete more effectively against a larger incumbent. It is not clear whether an efficiency gain or significant product or service innovation by a large incumbent – the kind of business likely to be subject to the new section 46 – would be seen as increasing competition for the purposes of such a test.

By contrast, it seems much clearer that preventing, restricting or deterring the potential for competitive conduct in the market or new entry into the market will be considered a *lessening* of competition. The result of this asymmetry would be that conduct that made it more difficult for competitors to remain in or enter a market would usually be considered a lessening of competition, while the efficiencies that resulted in those circumstances might not be taken into account as an increase in competition.

Even if both were taken into account, it is difficult to predict how they would be weighed against each other. It is particularly unclear how a *purpose* of enhancing efficiency would be weighed against an *effect* of preventing new entry (or vice versa) in assessing whether conduct has the *purpose or effect* of substantially lessening competition. What seems clear is that requiring the court to take these factors into account is a long way from the defence of a legitimate business purpose provided in overseas jurisdictions and effectively replicated in the current “take advantage” element.

Further, the proposed court directions are unclear as to the outcome if conduct reduces competition in one market, but increases it in another. The proposed court directions appear to contemplate only considering benefit and detriments in a single market (by use of the term “the market”) and does not contemplate different effects in different markets.

**(g) The change would act as a deterrent to innovation and efficiency.**

If the amendments to section 46 recommended in the Final Report are implemented, businesses that may be considered to have market power will need to think twice before engaging in any conduct that is intended to increase efficiency and benefit consumers, but which may make it more difficult for smaller competitors to compete. This caution and delay will have costs to business and consumers, particularly in the increasingly dynamic market conditions faced by the retail industry among many others.

The proposed amendments do not take into account that a multitude of decisions to enhance efficiencies and lower costs are made daily in the operations of a large business where it is impossible to know the effect or likely effect of that decision in any one or more of the many markets that the decision may impact. Further, it is arguable that this illustrates how the provisions may be manipulated to stifle competition, price efficiencies and value to the consumer. For example, if a business decides that it will diminish the number of its suppliers from three to two in a particular goods market, and that market is already concentrated, the affected supplier may complain that the decision has substantially lessened competition.

The competitive business may therefore be deterred from keeping its prices low, finding efficiencies that enable it to drive prices lower, offering quality and service or innovating to develop new products and services, which is all conduct that has the lawful purpose of improving business performance and outcomes for consumers, employees and shareholders. Equally, such conduct may later be judged as having the effect or likely effect of substantially lessening competition in a market.

In Wesfarmers’ view, the proposed amendments to section 46 will result in a lessening of innovation and risk taking by Australia’s most successful companies by creating uncertainty as to whether conduct may be found to have the effect or likely effect of substantially lessening competition even if it was for a legitimate (i.e. not anti-competitive) purpose.

The actual effect (or even likely effect) of conduct is often difficult to predict, and easy to judge in hindsight. There is a real and significant risk that well-intentioned conduct will be judged at a later point to have had an unacceptable outcome or effect, even if it could not be predicted. Businesses may be unwilling to take on the financial and operational risks of investment and innovation if the regulatory outcome is uncertain.

A legislative amendment that would require a court (or the ACCC through an authorisation process) -- to consider the extent to which unilateral conduct is likely to increase competition, including by enhancing efficiency, innovation, product quality or price competitiveness in a market (or multiple markets), before it can be confirmed to be lawful will inevitably result in a reduction in desirable and pro-competitive investments and innovations.

As Stephen King and Graeme Samuel note:

> This will drown the commercial activity of big business in a sea of uncertainty. One can only wonder how a committee that on one hand recommends pro-competitive reforms to commerce

> can then proceed to urge a significant intrusive constraint on the commercial activities of big business. The only winners will be the lawyers and economists who will need to sit at the right hand of business CEOs to guide them on the legality of every significant transaction and the ACCC, which will need a big budget increase to deal with the mass of authorisation applications.

Wesfarmers does not agree that there will be a mass of authorisation applications, as few businesses can afford to wait the six months of the authorisation process before they respond to changes in competitive dynamics or consumer preferences. But we agree that the new section would impose a significant and intrusive constraint on commercial activities and on competition.

The Panel suggests the new test will be worth any costs that may arise due to transitional uncertainty:

> The Panel's proposed reform to section 46 is an important change, which will (like all regulatory change) involve some transitional costs, as firms become familiar with the prohibition and as the courts develop jurisprudence on its application. In the Panel's view, the change is justified as transitional costs should not be excessive and will be outweighed by the benefits.

Although Wesfarmers believes that transitional costs would be significant and protracted, the proposal involves more fundamental costs and uncertainties that would persist no matter how familiar firms may become with the prohibition or how extensive the courts' jurisprudence may grow.

#### (h) Concluding comments on proposed amendments to section 46

There is inherent uncertainty in the shift in focus from a specific predatory purpose to an effect or likely effect on competition. And there is an inherent cost in subjecting the commercial conduct of the most efficient competitors to investigation and substantial penalty on the basis of their unintended consequences.

The Panel has not established that there is any need for change or that the proposed amendments to section 46 will deliver any benefits over the current section. The Panel has failed to recognise or appreciate the significant costs of the proposal and the risk it would present to vigorous competition in Australia. The practical difficulties with implementation and execution of the proposed law on the multitudes of decisions made on a daily basis within large businesses will also stifle innovation and efficiencies in business.

The proposal to replace section 46 would have a profound impact on the competitive landscape to the disadvantage of Australia and all Australians, and it should not be adopted.

### 3.3 Vertical supply restrictions

Wesfarmers is of the view that vertical supply restrictions should be excluded from section 45 (just as they are excluded from the cartel provisions) and assessed exclusively under a simplified version of section 47. Wesfarmers does not support the removal of section 47 as the section provides businesses with a useful guide as to the prohibited categories of conduct, acting as an aid to compliance. However, the current section 47 should be simplified as it is overly complex and difficult to understand. In Wesfarmers' view, a substantial lessening of competition test should apply to all limbs of section 47 (including third line forcing).

### Further contact

We will be pleased to further engage the Review panel directly on the issues raised here, particularly as they relate to the detail of potential impacts on individual Wesfarmers businesses. Should you wish to clarify any particular issue raised in our submission, please contact Wesfarmers' Executive General Manager Corporate Affairs, Alan Carpenter acarpenter@wesfarmers.com.au (08) 9327 4267.