



PHILIP MORRIS LIMITED

SUBMISSION TO THE PRODUCTIVITY COMMISSION

ON THE

REVIEW OF THE *PRICES SURVEILLANCE ACT 1983*

APRIL 2000



EXECUTIVE SUMMARY

Philip Morris Limited (PML) would like to support the Productivity Commission on its timely review of the *Prices Surveillance Act 1983* (the Act).

It is PML's view that price surveillance may be an appropriate form of consumer protection where a competitive industry does not exist. In PML's experience, companies operating in a competitive industry, are unlikely to possess market power capable of being exercised to the detriment of consumers. Rather, surveillance imposes high costs of compliance without improving consumer benefits.

PML therefore believes that the objective of consumer protection should be clearly stated within the Act and that the powers of surveillance only be applied when a competition test has not been passed.

PML believes that the introduction of a competition test will ensure that the objective of the Act is achieved in an efficient manner.

BACKGROUND INFORMATION

In Australia, PML is one of two manufacturers in the tobacco industry. Between 1984 and 1996 PML was a declared manufacturer under the Act and thus subject to prices surveillance. In 1996 PML was de-declared as it was found that the tobacco industry in Australia was operating in a competitive environment.

We draw on our experience of prices surveillance under the Act for 12 years as a basis for our submission.



PRICES SURVEILLANCE APPROPRIATE

Prices surveillance is appropriate where there is a lack of competition in a market in order to protect consumers from abuses of market power. Any form of prices surveillance should be transparent, based on a clearly defined set of criteria and include appropriate levels of accountability for both the regulator and the regulated. The continued need for surveillance should be subject to review at frequent intervals.

PRICES SURVEILLANCE IS WASTEFUL WHEN APPLIED TO COMPETITIVE INDUSTRIES

During the period PML was declared, PML incurred \$1.4 million in compliance costs, its competitors no doubt incurred similar costs, and the Prices Surveillance Authority (PSA) and the Australian Competition and Consumer Commission (ACCC) must also have incurred costs surveying tobacco prices without improving benefits to tobacco consumers.

Throughout this period, the prices PML charged were considerably lower than the approved prices set by the PSA. By 1996 the in-market price of a packet of cigarettes was approximately 10% less than the prices approved by the PSA.

From 1984 through 1996, competitive price discounting, (through retailers to the public at PML's cost) provided consumers with a cumulative benefit of \$417 million, when compared to the approved PSA prices.

Accordingly we consider that prices surveillance is costly and unnecessary when competition exists.



CLEARLY STATED OBJECTIVE OF THE ACT

PML believes the Act should have a clearly stated objective.

The Act's objective should be to establish a transparent, accountable mechanism to oversee prices of organisations that may possess market power in non competitive markets to ensure that market power is not used to the detriment of consumers.

COMPETITION TEST

If the Act's purpose is to protect consumers from uncompetitive behaviour by persons or companies with market power, there should be a test within the Act that must be passed before a product or industry will come under prices surveillance.

Under the Act the task of determining which organisations should be requested to undergo prices surveillance rests with the Designated Minister (Section 21). We submit that the Act should provide the statutory guidance as to which organisations should be subject to prices oversight.

PML believes that part of that statutory guidance should be a competition test similar to that proposed in the Industry Commission Submission to the PSA, ("What future for price surveillance", AGPS, Canberra, September 1994).

The Industry Commission considered that prices surveillance should be confined to situations where four criteria are satisfied, namely where a single firm:

- Has greater than two thirds of the market; and
- Has no major rival; and
- Faces sporadic or trivial imports (less than 10 per cent); and
- Is sheltered by substantial barriers to entry.



Such a firm would be deemed to be operating in a non-competitive market and would therefore be in a position of market power with the potential opportunity to abuse that power. In such a situation, prices surveillance would be appropriate.

IN CONCLUSION

PML advocates the incorporation of a competition test.