

Revised version

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## Australian Competition Law at the Crossroads

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**Author's Note:** This paper has been amended to include material put by the author to the Senate Economics Legislation Committee during its consideration of a Bill to amend s.46 of the *Competition and Consumer Act 2010* which proposed to give effect to the recommendations of the Competition and Consumer Act Review Panel. The Committee recommended enactment of the Bill. At the time of writing, the Bill has not been enacted.

### *Abstract*

*This paper examines the amendments recommended by the Competition and Consumer Act Review Panel, to section 46 of the Competition and Consumer Act 2010, and some associated provisions and suggests that, if enacted, they would allow corporations with substantial market power to prevent or deter entry; eliminate or damage smaller competitors; and prevent or deter them from engaging in competitive conduct; harming competition in the long-term,. They would stultify innovation, entrepreneurship and efficiency; and limit growth of the Australian economy. The recommendations are internally inconsistent and would put Australia at odds with leading developed economies. The long-term effect would be to increase inequality of incomes and wealth; encourage influence-peddling; and damage the integrity of the body politic.*

### **Executive Summary**

1. This paper analyses the effects of the Bill to amend s. 46 of the Competition and Consumer Act 2010, which seeks to give effect to the recommendations of the Competition and Consumer Act Review Panel in relation to the section. The key recommendation, to replace the provisions of s.46 1 (a) (b) and (c) with the test of *substantial lessening of competition*, is cause for considerable concern as that would permit a firm with substantial market power to:

- Prevent or deter entry as a prospective entrant has no market share, it would not substantially lessen competition;
- Prevent or deter competitive conduct by a firm without a substantial market share as that would not substantially lessen competition;

- Eliminate or damage a competitor without a substantial market share as that would not substantially lessen competition;

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2. A number of types of conduct aimed at individual competitors by a firm with substantial market power, which are generally not likely to have the *purpose, effect or likely effect of substantially lessening competition*, would be permitted, so long as the target is a prospective entrant or a competitor without a substantial market share, including:

- Refusals to deal;
- Price discrimination;
- Predatory pricing;
- Exclusionary conduct by foreclosure of access to customers or inputs e.g by tying; bundling; and margin price squeezing.

3. If enacted, the Bill would, in my view, have the following effects:

(a) permit powerful firms to prevent entry; eliminate competitors and deter competitive conduct, which is now prohibited;

(b) lead to greater concentration in markets; higher prices; and reduced quality and service;<sup>[1]</sup>

(d) transfer resources from the general population to large firms and their executives, thus increasing inequality of incomes and wealth, which in turn, reduces national economic growth, employment and living standards;

(e) allow the *non-recoupment defence*, now justifiably excluded, to be made, thus making it harder to prove a contravention;

(f) contrary to the Government's stated policy, stultify innovation, entrepreneurship and efficiency improvements; and reduce jobs and growth;

(g) put Australia out of step with leading Western economies on Misuse of Market Power prohibitions with the consequence of hampering international cooperation in competition law enforcement, particularly in relation to the Closer Economic Relations policy with New Zealand;

(h) create inconsistency in treatment of firms with substantial market power in some sectors regulated for access and pricing and other firms not so regulated;

(i) encourage the increasing concentration of markets and, thereby, tend to increase influence peddling to the detriment of the public interest.

4. There is no substantial issue of either:

(c) undue ambiguity about whether the current provisions prevent pro-competitive conduct; or

(d) whether the objective of competition law is to protect and preserve competition or protect individual competitors and I have suggested criteria for market efficiency as the touchstone.

5. If further clarity is needed (and a previous review has concluded that the provision is sufficiently clear), there are better ways than rewriting the provision.

6. There are existing arrangements for assessing and pursuing small business interests under the competition law, such as the Australian Competition and Consumer Commission (including its Small Business Commissioner); and the Small Business Ombudsman. The enactment of the Bill would limit the ability of those agencies to take appropriate action. It is surprising that they have not opposed the proposed amendments, but have supported them. Neither has the Council of Small Business Australia or the Australian Chamber of Commerce and Industry raised their voices in opposition to the Bill, which would harm their members.

7. The objectives of the Review Panel included *clarity* and *effectiveness* of the competition law. The objective of clarity appears to have been interpreted as *simplicity* and the objective of effectiveness has been overshadowed by the pursuit of simplicity and, as a result, implementation of its recommendations through the Bill would neuter the objectives of section 46.

8. Another significant problem with the enactment of the Bill is that by rewriting the existing provisions, the accumulated jurisprudence from decades of case law in Australia and overseas, would be lost and that would lead to extensive litigation to create a body of law which interprets the new provisions, but without the protection the current provisions afford.

9. Some parts of the Bill would improve the operation of section 46 and those should be retained, but others should be rejected. The Parliament should:

- (a) accept the recommendation to introduce the *effects* leg of the test of culpability;
- (b) accept the recommendation to replace the phrase *taking advantage* by the phrase *engage in conduct*;
- (c) reject the the recommendation to replace the current substantive prohibition in section 46 with the sole test of *substantial lessening of competition*;
- (d) reject the the recommendation to repeal amendments to the section made since 2007.

[1] Because of concerns about such effects of market concentration, the 1977 change in the merger test from the original 1974 test of *substantial lessening of competition* to that of *dominance*, was reversed about a decade later. Curiously, the 1977 amendment was *inconsistent with the Swanson Committee's recommendation on this point*. The Committee based its recommendations on its assessment of numerous submissions, a process which did not characterize the departure from its recommendations on the merger test.

## Introduction

1. Since the enactment of the *Trade Practices Act 1974*, now the *Competition and Consumer Act 2010*, Australia has been seen internationally as one of the leaders in competition and consumer law. This article is concerned with the changes to the misuse of market power prohibition of the Australian law in s.46 proposed by the *Competition and Consumer Act Review Panel*. The current substantive prohibition in section 46 reads as follows:

### 46 Misuse of Market Power

- (1) *A corporation that has a substantial degree of power in a market shall not take advantage of that power in that or any other market for the purpose of:*
  - (a) *eliminating or substantially damaging a competitor of the corporation or of a body corporate that is related to the corporation in that or any other market;*
  - (b) *preventing the entry of a person into that or any other market; or*
  - (c) *detering or preventing a person from engaging in competitive conduct in that or any other market.*
- 2. The Panel, set up by the Abbott Government, has recommended significant amendments to the section; and that has now been adopted as policy by the Turnbull

Government. An exposure draft of proposed legislation to implement the recommendations has been released.[2] The changes proposed are inconsistent with the recommendations of the Panel on certain other provisions; and have far-reaching deleterious long-term consequences for innovation; entrepreneurship; dynamism; economic efficiency; and growth, which would, in the long-term, increase economic inequality and harm the institutions of our democracy. The Prime Minister, The Hon. Malcolm Turnbull has repeatedly said that the proposed changes would prevent big businesses from harming small competitors. On the contrary, as this article argues, they would allow firms with substantial market power to engage in exclusionary and predatory conduct which harms their smaller competitors; conduct which is currently proscribed under the existing form of s.46.

## The Proposed Changes to s. 46

3. The amendments proposed would
  - (a) add a second leg of culpability to the *purpose* test by including the alternative of an *effects, or likely effects* test;
  - (b) replace the words '*take advantage*' with '*engage in conduct*' for the proscribed *purpose* (and after amendment, the *effect, or likely effect*);
  - (c) Insert a test of *substantial lessening of competition* as the only criterion of market outcome to assess the culpability of a firm with substantial market power;
  - (d) repeal the provisions in paragraphs (a); (b) and (c) of sub-section.46 (1) shown above, with which this article is primarily concerned;
  - (e) repeal the provisions in sub-sections 46 (1AA) and 46 (1AAA) which currently exclude consideration of the *recoupment argument* as a factor in defence of the impugned conduct in adjudicating culpability; and
  - (f) repeal of the explanatory provision in sub-section 46 (6A) which assists in the interpretation of the phrase 'taking advantage' in the current formulation of section 46.
4. The relevant recommendation by the Panel is:

### **Recommendation 30 - Misuse of market power**

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

To mitigate concerns about inadvertently capturing pro-competitive conduct, the legislation should direct the court, when determining whether conduct has the purpose, effect or likely effect, of substantially lessening competition in a market, to have regard to: the extent to which the conduct has the purpose, effect or likely effect of increasing competition in the market, including by enhancing efficiency, innovation, product quality or price competitiveness; and the extent to which the conduct has the purpose, effect or likely 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.

Such a re-framing would allow the provision to be simplified. Amendments introduced since 2007 would be unnecessary and could be repealed. These include specific provisions prohibiting predatory pricing, and amendments clarifying the meaning of 'take advantage' and how the causal link between the substantial degree of market power and anti-competitive purpose may be determined.

Authorisation should be available in relation to section 46, and the ACCC should issue guidelines regarding its approach to the provision.

5. A number of types of conduct aimed at individual competitors by a firm with substantial market power, which are generally not likely to have the *purpose, effect or likely effect of substantially lessening competition*, would be permitted, so long as the target is a prospective entrant or a competitor without a substantial market share, including:

- Refusals to deal;
- Price discrimination;
- Predatory pricing;
- Exclusionary conduct by foreclosure of access to customers or inputs e.g by tying; bundling; and margin price squeezing.

## **Broad analysis of effects of proposed amendments**

6. The addition of the *effects* leg is an improvement, as it is notoriously difficult to obtain evidence of *purpose* in a corporation where decisions are made by different 'minds'[3]; often not documented, or where relevant documentation is either inadvertently or deliberately[4] not retained.

7. The expression '*taking advantage*' has been held by the High Court in *Queensland Wire Industries vs The Broken Hill Proprietary Company Limited*[5] to broadly equate to the word '*use*' by its rejection of a *pejorative* interpretation of the

expression; or the necessity to show *hostile intent* in the impugned conduct; and stipulating that the entire sentence should be considered as a whole in its interpretation, rather than attempting to split it into its component phrases or words and then seeking to interpret them individually. However, the High Court in subsequent cases has arrived at a different conclusion on that point. In *Melway*[6] and in *Rural Press* ,[7], no ‘taking advantage’ was found and those two cases could be argued to have introduced considerable uncertainty into the meaning of the phrase, although the facts were different from *QWI*. Following the *Rural Press* case, the explanatory amendment in sub-section 46 (6A) was introduced.[8] The proposed change to replace the phrase ‘taking advantage’ with ‘engage in conduct’, on the one hand, could be argued to provide certainty, eliminating the possibility of any future change in interpretation by the High Court which waters down the effect of the prohibition, but, on the other hand, would be unnecessary if the provisions of sub-section 46 (6A) are not repealed and the present proscriptions in paragraphs 46 (1) (a), (b) and (c) are retained.

8. Any benefits of the changes identified above, however, would be overwhelmingly outweighed by the proposed repeal of the prohibitions in paragraphs 46 (1) (a), (b) and (c), which prohibit a corporation with substantial power in a market from using its power to prevent or deter entry; eliminate or damage a competitor; or prevent or deter a competitor from engaging in competitive conduct in the market in which the firm engaging in the conduct has the requisite power or in any other market. Instead, conduct would be subject to a single test - whether it has the purpose, effect or likely effect of ‘*substantially lessening competition*’, after taking account of any pro-competitive intent or effect. The repeal of sections 46 (1AA) and 46 (1AAA) which prevent consideration of the *recoupment* defence, discussed in detail later in this article, would make it much more difficult to prove a contravention.

## Overseas antecedents of s. 46

9. The provisions of s. 46 have their origin in section 2 of the *Anti-trust Act of 1890* in the United States, known eponymously as the *Sherman Act* after its sponsor in the US Senate[9], prohibiting a corporation from monopolising, or attempting to monopolise, a market, which provides as follows:

“2. *Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any person or persons to monopolize any part of the trade or commerce among the several States or with foreign nations, shall be deemed guilty of a misdemeanour*”.[10]

10. Indeed, the US provision prohibits *any* firm, not just a firm with substantial market power, from engaging in such conduct.[11]

11. A provision broadly similar to section 2 of the *Sherman Act* is to be found in *Article 86 of the Treaty of Rome*, prohibiting similar conduct by *dominant* firms in the European Union:

*“To the extent to which trade between any Member States may be affected thereby, action by one or more enterprises to take improper advantage of a dominant position within the Common Market or within a substantial part of it shall be deemed to be incompatible with the Common Market and shall hereby be prohibited. Such improper practices may, in particular, consist in: (a) the direct or indirect imposition of any inequitable purchase or selling prices or of any other inequitable trading conditions; (b) the limitation of production, markets or technical development to the prejudice of consumers; (c) the application to parties to transactions of unequal terms in respect of equivalent supplies, thereby placing them at a competitive disadvantage; or (d) the subjecting of the conclusion of a contract to the acceptance, by a party, of additional supplies which, either by their nature or according to commercial usage, have no connection with the subject of such contract.”*

12. Section 46 of the Australian legislation is the result of careful codification of the jurisprudence in the United States and Europe, applying the law in this area, as in other areas of the legislation, by adjusting the scope of the prohibition, particularly to avoid the problems experienced from judicial activism in the U.S. jurisdiction (discussed in detail later) and limiting the extent of its reach to reasonable boundaries.

## **Disharmony with international law**

13. The proposed amendments would, in effect, mean that Australia would not have a comparable anti-monopolisation prohibition to those in place in the US, E.U. and other leading western democratic economies and progressively being adopted by a number of developing countries. What that does for international co-operation between Australia and other countries in cross-border investigation and enforcement of competition law is unclear. [12]

14. Our close neighbour, New Zealand, with which we have pursued closer economic relations over many years, not least by comparable provisions in our respective competition laws, to allow for the consideration of *‘joint markets’*[13] encompassing both countries in certain circumstances, has a prohibition that more closely reflects our existing prohibition in s.46. Section 46A[14] is not proposed to be amended, presumably because it flows from the Closer Economic Relations agreement with New Zealand and any change would require bilateral



agreement. The definitions of ‘conduct’; ‘impact market’; ‘market power’; and ‘trans-Tasman market’; respectively convey both, an inclusive common market encompassing both national markets, as well as separate markets in each country. The lack of commonality with the proposed amended s.46 is likely to provide fertile ground for litigation as to whether a firm with the requisite power in the Australian market, but engaging in conduct which could affect a New Zealand player, should be judged under s46 or s46A.[15]

## Consequences for Competition, Innovation, Efficiency and Economic Growth

### Predatory or exclusionary conduct by powerful firms

15. The proposed replacement of the current prohibitions with one prohibiting conduct by a firm with substantial market power that had the *purpose* [and, after amendment, *the effect or likely effect*] of *substantially lessening competition* would be seriously deleterious for the economy, by leading to ossification of market structure; stultification of initiative; innovation; entrepreneurship; and dynamism; and long-term sclerosis of markets. The reasoning for that conclusion follows.

16. A *potential entrant* into a market, by definition, has *no market share*; and the *market share of a new entrant or small competitor would not be large enough* to necessarily lead to a conclusion that exclusionary or predatory conduct against any one of them lessens competition *substantially*. The argument may be made that section 4G equates *prevention or hindrance of competition* to a *lessening of competition* but that is not the same as saying that such conduct amounts to a *substantial* lessening of competition. Reliance on the *relatively short-term time frame of assessment of substantially lessening competition*[16], therefore, is fraught with significant risk to economic progress by stultifying the dynamism of markets that comes from new entry and competition from small competitors.

17. It is well known that small entrepreneurs can disrupt markets through innovation. Targeted by a firm with substantial market power, not only is the small firm vulnerable to the ‘deep pockets’ of the predator, but is ill-equipped to undertake long and expensive litigation to prove a *substantial lessening of competition* ('SLC'). Unlike the existing form of s.46, under which proving the existence of market power; and the fact of elimination or harm to the small competitor or prevention or deterrence of entry, constitute a substantially lower barrier to surmount in proving a contravention, the SLC test is fraught with difficulty and complexity for many reasons. In *TPC v TNT Management & Ors* (1985) 58 ALR 423, (1985) 6 FCR 1, a case which involved transport brokerage services, the

then *Trade Practices Commission* was unable to satisfy the Court that competition was substantially lessened. More generally, the following factors have proved significant challenges to the regulator in various cases where SLC has been the test:

- identifying the product/services relevant to the case;
- defining the geographic area of actual or potential competition;
- considering actual or possible level of imports (in the case of goods);
- examining what other products/services or geographic areas should be considered for potential consideration for inclusion in the relevant market in the event of a price increase by incumbents;
- quantifying the shares of participants and their current and potential competitive ability;
- assessing barriers to entry and expansion;
- estimating the likelihood, timing and scale of any new entry or expansion;
- predicting likely future evolution and characteristics of the market, such as trends and possible changes in the demand profile and supply options;
- considering probable or likely counterfactual scenarios in the context of various dynamic factors; and, in light of these matters,
- persuading a court that competition is *likely* to be substantially lessened in light of the above factors and other relevant ones.

The difficulties outlined above would discourage even a regulator or a firm with substantial resources from instituting proceedings, because they often last many years; require expert economic and legal advice and, overall pose substantial financial risk. To expect a small-business private litigant, with severely limited resources to undertake and prosecute such expensive and risky litigation, is unrealistic.

### **The ‘Recoupment’ defence in predatory pricing**

18. One of the ways in which firms with substantial market power damage individual competitors is to engage in *predatory pricing*. Much has been written on the subject of *predation and recoupment*. One view is that it is only when a firm cuts prices below average variable cost, and *recoups, or is able to recoup*, lost profits, should it be illegal. Recoupment is often linked with ‘*rationality*’. Both recoupment and rationality were considered at some length by the judges of the High Court of Australia in exonerating the appellant in *Boral BesserMasonry*, which argued, in effect, that, since it was unable to recoup losses from the alleged predatory conduct it would have been *irrational* to engage in such conduct.<sup>[17]</sup> Sub-sections 46 (1AA) and 46 (1AAA), which were enacted in 2007 and 2008 respectively, in effect, outlaw

sustained below-cost pricing and exclude consideration of the inability of a corporation to recoup losses from below-cost supply, in assessing a breach of s.46.[18]

19. The author takes the view, that the ‘recoupment’ defence, (more accurately a ‘non-recoupability defence’) is not generally relevant to predation and that there are strong arguments in favour of retaining sub-sections 46(1AA) and 46(1AAA) because:

(a) Impugned conduct is viewed by courts through a ‘retrospectroscope’, and, in the case of the High Court, usually many years after the events being adjudicated. Subjecting such conduct to complex tests of rationality, divorced from the pressures of real-time corporate decisionmaking in the heat of market pressures with 20/20 hindsight is of little use in establishing intent.

(b) Firms could engage in conduct which might not be regarded as *rational* because strategy may be formed by one or more people whose decisions may not be rational.[19] . The concept of decision-making not based entirely on rational criteria is known as “*bounded rationality*”. [20]

(c) While losses attributable to the conduct may not be recoverable, the powerful firm’s continued existence and preservation of most of its market share for a prolonged period, as a result of the conduct, means that predation, whether with or without the likelihood of recoupment, may be the *least bad* outcome in terms of its ongoing existence and profitability, rather than the possible drastic loss of market share, and even exit from the market, in the face of a disruptive, innovative and efficient potential or actual entrant, or such an existing smaller competitor, likely to grow rapidly in the absence of the impugned conduct by the incumbent.

(d) Even if profits foregone by predation are not recoverable in the short to medium term, the disciplining effect on firms considering entering the market is likely to *chill new entry and longer term competition from new entrants or existing smaller competitors*. Potential entrants would get the message very quickly that the powerful incumbent firm or firms would be prepared to dig deep into their deep pockets to fend off new threats to their strong market positions, whether they could recoup profits foregone or not (commonly described in the industrial organization literature as a *disciplining effect*). [21]

(e) A key consideration in the application of the recoupment test, if, indeed, it is appropriate to consider it (and the current law prevents that), is the proper assessment of

- (i) *pre-entry prices*;
- (ii) *post entry prices* and
- (iii) *post exit prices*.

(f) It is not appropriate to apply a test which, in effect, would find culpability only where the firm is able to *compensate itself* for losses due to *price reductions, even if they arise from erosion of its economic rents or losses arising from its own inefficiencies*, through the impugned conduct. Let's assume the following circumstances for the sake of illustrating the argument.

- The *pre-entry* price before a new entrant begins competing has a component consisting of economic rent and/or the costs of productive or dynamic inefficiency;
- such components are eroded by the entrant (where it is due to the latter's superior efficiency gained from innovation or business acumen[22]) leading to *lower post entry prices*;
- the entrant is eliminated from the market by the impugned firm pricing below its *average variable costs* (or, in the case of exclusionary conduct, by *foreclosing access to inputs or customers*); and
- *post-exit prices* do not return to *pre-entry prices* but do rise to cover the incumbent's average variable costs.

There would still not appear to be a case for consideration of non-recoupment of lost profits. The post entry price reductions would have been the result of superior efficiency of the new entrant, which have merely brought competitive prices to the market, which benefits customers (and, ultimately, consumers), who have previously had to pay the higher, supra-competitive, prices (above costs plus a reasonable return), not justifiable on efficiency criteria.

(f) While it may be argued that inability to raise post-exit prices to pre-entry levels indicates a lack of substantial market power, that is unlikely to be the case for the following reasons:

- customers having become aware of the level of economic rents or inefficiency costs prior to entry, are likely to be strongly motivated to negotiate more vigorously;[23] and
- the incumbent may be discouraged from immediately reverting to pre-entry prices for public relations reasons, but may still raise prices above costs over time.[24]

(g) There is a very significant *temporal aspect* to the relationship between action to eliminate a competitor or prevent or deter new entry; and failure to recoup (if recoupment is reinstated as a test). At the inception of predatory conduct, it may appear to the firm engaging in it that it is likely to be able to recoup profits foregone, but, over time, for a range of reasons, including changing market dynamics or its own

relative inefficiency, recoupment may not materialize. The change in circumstances does not change the *intent* to deter or eliminate, or the *effect* of deterring or eliminating a competitor or of preventing entry. Because *the condition of entry*[25] is key to competition; and the chilling effect of deterrence of entry and damage to individual competitors, together with the ‘falling of more dominoes’[26], will inevitably damage competition and the competitive process over a long time-frame, by increasing or maintaining concentration (the anti-competitive effects of highly concentrated markets is discussed further in this article), although short of a level of concentration that is considered to result in a substantial lessening of competition.

(h) Another key consideration for a powerful incumbent is the likely *stranding of its assets* if a new entrant with more efficient plant or superior business acumen, establishes itself and makes significant inroads into the incumbent’s market share. To protect its market share and deal with an existential threat without predation, the incumbent must *compete on the merits*[27], *i.e. on price, quality and service*. To do that, it would need to make substantial new investment to upgrade plant and equipment, (assuming such replacement plant is available to the incumbent or its supplier without any intellectual property barriers) to match the entrant's productive efficiency. More significantly, substantial write-down, or total write-off, of the incumbent’s existing plant and exit from the market is a distinct possibility, if it is unable to compete on the merits.

20. Hence, even without recoupment, ‘seeing off’ an interloper, which poses an existential threat to the incumbent, by predatory conduct would, from the perspective of long-term profitability and survival, be a much less risky strategy than competing on the merits and, is arguably, as *rational* as basing its decision on the possibility, or otherwise, of recoupment. Since the law did not exculpate a breach on grounds of rationality or non-recoupability of lost profits, it is perplexing that a majority of the High Court gave such weight to those factors as part of their reasons for exonerating the appellant in *Boral Besser Masonry*. The subsequent amendment to exclude non-recoupment as an exculpatory factor was obviously made as a result of that case. *Furthermore, the so-called 'bright line' test of average variable costs in assessing predatory pricing, much vaunted by US anti-trust practitioners, is not necessarily a line as bright for economic efficiency as claimed by its adherents*. The certainty claimed by them is illusory, because, for a range of reasons, the relevant purpose and/or effect of damaging/eliminating a competitor, or preventing/deterring a prospective one from entering, is capable of being established, even in circumstances where sales are made at higher than average variable costs, but below fully distributed costs. Some so-called economic ‘tests’ do not always fit commercial reality, or long term national efficiency objectives, and the law needs to allow for adequate consideration of the long term public benefit from long term national efficiency,

particularly from the dynamism that effective competition delivers throughout the economy, by preventing unacceptable behavioural barriers to entry. *It may well be time to revisit the High Court decision in Boral in an appropriate case.*

## **Claimed ambiguity in interpretation of section 46**

### **Pro-competitive vs Anti-competitive Conduct[28]**

21. Much has been made, over time, of the argument that it is difficult to distinguish between *pro-competitive* conduct from that which is aimed at *harming a competitor* and therefore, only conduct intended to, or having the effect of *substantially lessening competition* should be punished. That argument largely relies on a quote in the joint judgment of their Honours Mason C.J. and Wilson J. in the High Court of Australia judgment in *Queensland Wire Industries vs The Broken Hill Proprietary Company Ltd*[29]. The oft-quoted sentences are as follows:

*“Competition by its very nature is deliberate and ruthless. Competitors jockey for sales, the more effective competitors injuring the less effective by taking sales away. Competitors almost always try to “injure” each other in this way. This competition has never been a tort and these injuries are the inevitable consequence of the competition section 46 is designed to foster.[30]”*

22. The argument that that quote blurs the line between legitimate competition and illegal predation, amounts to sophistry, for the following reasons:

(a) Neither the ‘jockeying for sales’; ‘injury’; or any other term in that passage in any way condones predatory or exclusionary conduct by a firm with substantial market power and is consistent with positive internal efforts within a firm to gain sales by innovation, efficiency, strategic initiatives and superior business skill and acumen, thereby, having the *consequence* of ‘injuring’ competitors by decreasing their market share or limiting their growth. If it is argued that the passage does not, in terms, exclude predatory or exclusionary conduct, it should not be expected to do so, as the section explicitly proscribes such conduct by a firm with the requisite market power where it had the relevant purpose.

(b) The passage is merely commentary on the general nature of business, rather than approval of exclusionary or predatory conduct by a firm with substantial market power, which, in the case, was unanimously found to be a contravention.

(c) If the quote was intended to signal that those two justices believed that there should be no impediment to *‘no-holds barred’* competition, they would not have joined in the unanimous judgment of the Court, finding BHP culpable. To argue

otherwise, would be to suggest that they condoned a breach of s.46, clearly an absurd proposition. The only reasonable explanations which reconcile the quote with the two judges joining in the unanimous judgement of the Court; and the joint judgment of the other judges finding culpability is

- (i) the implicit precondition '*in the absence of section 46*'; or
- (ii) in the context of the particular joint judgment and the unanimous judgment of the full court, that such conduct is the ordinary behavior of most firms without market power, seeking to increase their market share, without suggesting that predatory or exclusionary conduct by firms with substantial market power is acceptable.

23. Hence, taking that quote literally, without regard to the other parts of the joint judgment, including the preceding sentence;<sup>[31]</sup> the totality of the other judgments; and the implications of the two justices joining in the unanimity of all the Justices in their judgements in finding BHP culpable; is a specious interpretation of the relevant sentences and of the outcome of the case, that amounts to sophistry.

24. It should present no difficulty to a Court, and no uncertainty to a firm with substantial market power, to differentiate

- internally focused conduct, on the one hand, which improves a firm's own innovativeness; management; productivity; marketing; product design or quality; service standards; and promotion of its offering; from
- conduct, on the other hand, which is specifically aimed at damaging a competitor's ability to gain sales by foreclosing markets or customers to them by exclusive dealing agreements; refusal to supply; or predatory pricing.

25. It was BHP's refusal to supply an input ('Y-bar') that was essential to the ability of a new entrant to produce star-picket fence posts, to compete with it, that led to the finding against it. A policy of most firms not aiming to exclude entry is to expand sales<sup>[32]</sup> and that would have led to increased revenue from the sales of Y-bar, to all comers, including the appellant, clearly a *merits-based approach*<sup>[33]</sup>. It was, by BHP's own admission, its objective of protecting its sales of fencing products from competition by Queensland Wire Industries, by refusing to supply it with the feedstock to make its own star picket fence posts, which, together with fencing wire it was marketing, which would have allowed it to supply the complete range of fencing products preferred by customers to buying them separately from different suppliers. That was judged to constitute exclusionary behaviour that contravened S

46. For the reasons above, therefore, it is puzzling that the oft-quoted passage in the joint judgment of Mason C.J. and Wilson J. in *QWI* was given such prominence by the majority of the High Court judges in *Boral Besser Masonry*.

26. The Hilmer Committee[34], on the point about possible amendment of s.46, said:

*“In addressing this challenge, the Committee starts from the position that there is already in place a regime which provides a basis for making the appropriate distinctions, that the regime is broadly consistent with approaches in comparable overseas jurisdictions, and that it has been sufficiently interpreted by the High Court to provide a reasonable degree of business certainty as to the limits of acceptable conduct. Moreover, none of the submissions presented to the Inquiry gave practical examples of any particular behaviour that was not proscribed by the current law and yet was clearly unacceptable. The Committee thus considers that proposals for alternative mechanisms for dealing with misuse of market power should offer a demonstrable improvement over the current regime to justify introducing further uncertainty in this difficult area” (emphasis mine).*

27. Robert Bork, an eminent industrial organization analyst and jurist in the U.S, proposed a sensible criterion to distinguish conduct that is predatory, exclusionary, or otherwise arguably harmful to competition or unjustifiably removes competitors, from pro-competitive conduct – the test of *output restriction*[35]. Put simply, conduct should be judged on whether it restricts total market output or not. If not, it should not be found to be illegal, but if it does restrict output, it should be judged illegal.

28. There would be very few instances of conduct that could not be judged on the basis of its short, medium or long-term effects on total output in the relevant market.

29. As for the uncertainty of the existing s.46 provisions, they are no more uncertain than the provisions of many laws, given the wealth of jurisprudence in a number of important international jurisdictions in this field of law.

### **Protecting Competition vs Protecting Competitors**

30. Another argument put forward by proponents of the amendments is that s. 46 creates ambiguity between protecting competition, which they argue is the *sole purpose of competition law*, and *protecting individual competitors*, which they argue, is not a proper objective. Applied slavishly, without discernment and analysis of the facts and circumstances of particular conduct, this argument too becomes a sophistry.

31. There is substantial jurisprudence in the US jurisdiction about *competition on the merits*[36], which allows firms, whether they possess substantial market power, or not, to pursue innovation, productive and management efficiency; and good business



strategy for the purpose of increasing their output and sales, even if at the expense of competitors, exemplified in *US vs Grinnell Corporation*, where the defendant was exculpated on the basis that its conduct represented *superior business acumen*[37]. That was also the governing principle in *Byars v Bluff City News*[38].

32. Clearly, competition law is not intended to permit powerful firms to damage or prevent the entry of, or eliminate or prevent *efficient* competitors from competing; nor to protect *inefficient* competitors from vigorous competition.

33. Obviously, there can be no business competition without competitors; just as there can be no sporting competition without competing teams or individuals. The logical outcome of the progressive elimination of individual competitors in markets can only be oligopoly; (not necessarily followed by duopoly or monopoly, because by those latter stages, no one would disagree that a substantial lessening of competition is the outcome). However, concentration approaching or reaching the level of oligopoly[39] which does not cross current concentration thresholds in the merger guidelines of the ACCC, is cause for concern because, absent ease of entry or import competition, a substantial lessening of competition in the long-term can be expected from the loss of market dynamism (the anti-competitive consequences of concentration are discussed further in this article).[40]

34. The dissenting judgment of His Honour Justice Michael Kirby in *Boral Besser Masonry*[41], deals with that argument effectively:

*“Secondly, the chief object of s 46 of the Act is the protection of the competitive process in order to further the welfare of consumers and the Australian public generally. As this Court has said, the provision is not aimed **merely or primarily** at protecting the interests of competitors. If the charging of low prices constitutes the alleged contravening conduct, it will usually be appropriate, as a threshold question, to ask **whether it would be possible for consumers to suffer harm as a result of such conduct.**”* [42] (emphasis mine).

35. The likely harm to consumers considered in Kirby J’s judgment needs to be assessed in a longer-term time frame than that of substantially lessening competition, exploring whether the progressive elimination of individual competitors and the prevention or deterrence of new entry is likely to lead to increased concentration and, therefore, higher prices, lower quality and deteriorating services.

36. Kirby J goes on to say:

*“The ultimate outcomes of exclusionary conduct will often be uncertain. They will depend upon too many imponderables. In some circumstances, after the event, the results may not coincide with the original expectations and objectives. Yet such conduct can, of itself, damage the interests of consumers. It can do so:*

- *by forcing the exit of equally or more efficient competitors; or .*
- *by increasing the concentration of the market and making it more conducive to anticompetitive practices and outcomes; or .*
- *by making the entry of new competitors into the market less attractive; or .*
- *by strengthening the predatory reputation of the corporation engaging in such conduct. Those were the reasons for the legislative prohibition of such conduct in s 46. The section should not be whittled away. Yet that, in my respectful view, is what the approach now taken by this Court will produce.” (emphasis mine)*

37. It is well recognized that *competition is only a means to an end, not an end in itself*. The only reasonable conclusion to be drawn, therefore, is that *consumer welfare is the objective of competition law*, and that is harmed by the exercise of market power, which excludes choice in the price, quantity or quality of goods or services by excluding or eliminating competitors.

38. Furthermore, there are other sections of the Act clearly aimed at protecting or enhancing the ability of individual competitors to survive, compete and grow in the market. For example, the current resale price maintenance provisions protect individual retailers from retribution for price cutting, although it is recognized that the amendments proposed would incorporate an SLC test to RPM. Similarly, the prohibition in sections 45, read with section 4D (acknowledging that the proposed amendments would repeal the prohibition on primary boycotts); and sections 45D; 45E; and 45EA; (which are not proposed to be repealed) are aimed at protecting individual competitors.<sup>[43]</sup>

## **Relevance of claimed ambiguity to International Competition**

39. Presumably, Australian firms look farther afield than Australian shores to expand their markets and have to comply with laws in place abroad. If Australian firms find the existing prohibition in Australia ambiguous, how would they find the comparable prohibitions in the US, EU and elsewhere clear enough to enter and compete in those jurisdictions?

## **Significance of Freedom to Enter Markets**

40. The freedom to enter markets and expand operations is key to their efficiency; national economic growth; increasing employment; and improved standards of living. Behaviour by powerful firms which heighten barriers to entry should be treated with the seriousness they deserve.

41. In *re: QCMA*[44], the Trade Practices Tribunal, in a seminal decision examining the factors which influenced competition, wrote:

*'Of these, the most important is [2], the condition of entry.'*

42. It is generally accepted that barriers to entry, created or heightened, either collectively by competitors or by individual firms with substantial market power, harm competition and dynamic efficiency[45] but, as outlined above, the effect in most cases would not be to *substantially* lessen competition, the *only test* that would be applicable post-amendment.

43. Protected from the spur of actual or threatened entry, incumbents, insulated from the impetus of new entry, or able to dispose of troublesome small competitors, become lazy and lose their edge. Consequently, markets become ossified, complacency leads to lack of innovation, entrepreneurship and efficiency. The search for new markets, whether at home or abroad, new methods of production, new marketing strategies and new approaches to management, become unnecessary with the profits from the domestic market guaranteed by the progressive exclusion of competitors or deterrence of entry, so long as it does not *substantially lessen competition*. Attempting to compete abroad, without honing competitiveness at home, is unlikely to be successful.

## **Static vs Dynamic Factors in Assessing Competition Effects**

44. The exclusive reliance on the substantial lessening of competition test in s.46 would focus entirely on what is largely a *snapshot* of the effect of conduct on *existing competition*, ignoring the significance of the deterrence or elimination of *potential competition* that could be provided by new entrants and long-term dynamism that is essential for increasing employment; improving standards of living and sustained national economic growth,.

45. *Potential competition* has long been a significant factor in the jurisprudence of competition law in the US and the E.U and now of other nations developing competition law.

Australia would be at odds with international standards in this area if the recommendations of the Panel are adopted. It is not just a matter of keeping up with international trends for its own sake. The significance of preserving and protecting the ability of new competitors to enter and grow in markets has incalculably important implications for dynamism, innovation and growth in the national economy, as recognized in *re: Queensland Co-operative Milling Association*[46]. It was *potential competition* that was the primary focus in *Queensland Wire Industries v The Broken Hill Proprietary Company Limited* and it appears to have been ignored in the CCA

Panel recommendations. *If the amendments are passed, the High Court Judgement in QWI would, in effect, be nullified*[47], with the curious results examined below.

## **"Essential Facilities" Legislation and Internal Inconsistency of Panel Recommendations**

46. It is instructive that the *QWI* decision, followed by the Hilmer inquiry, which considered s.46 and, on the basis of the High Court jurisprudence, recommended no change to it, led to the *National Competition Policy* reforms requiring third party access to *essential facilities*, reflected in the enactment of Parts IIIAA, IIIA; and XIC of the legislation[48]. If the law is now to be amended to remove that obligation from firms with substantial market power not caught by those parts of the legislation, there appears to be little rationale for the preservation of those parts of the legislation, as that would mean that only powerful competitors *in some markets*, such as telecommunications, electricity, gas, water, ports, rail, roads, airports, would continue to be obliged to behave in a manner that powerful competitors *in other markets* would not be required to so behave. *In this context, the following draft recommendations in two of the dot-point recommendations (reproduced below), in Recommendation 1 of the CCA Review Panel on s 46 represent discriminatory treatment of some market sectors, as they advocate (a) structural separation and privatisation; (b) bringing Government enterprises within the purview of the Competition and Consumer Act 2010; but (c) presumably continued regulation for supply of infrastructure services.*

*Governments should separate remaining public monopolies from competitive service elements, and also separate contestable elements into smaller independent business activities.*

*Government business activities that compete with private provision, whether for profit or not for profit, should comply with competitive neutrality principles to ensure they do not enjoy a net competitive advantage simply as a result of government ownership.*

47. Such restructure is not recommended in relation to firms with substantial market power not covered by the access and pricing provisions of the law and, as a result of the proposed amendments, would not be required to provide inputs to third parties.

48. Yet a third dot point, within the same recommendation advocates:

*A right to third party access to significant bottleneck infrastructure should be granted where it would promote a material increase in competition in dependent markets and would promote the public interest.*

49. The third dot-point recommendation above is reinforced by *Recommendation 19* (reproduced in full below); and in the relevant part of *Recommendation 20* (shown below):

## **Recommendation 19 - Electricity and gas**

*State and territory governments should finalise the energy reform agenda, including through: application of the National Energy Retail Law with minimal derogation by all National Electricity Market jurisdictions; deregulation of both electricity and gas retail prices; and*

*the transfer of responsibility for reliability standards to a national framework administered by the proposed Access and Pricing Regulator (see [Recommendation 50](#)) and the Australian Energy Market Commission (AEMC).*

*The Panel supports moves to include Western Australia and the Northern Territory in the National Electricity Market, noting that this does not require physical connection.*

*The Australian Government should undertake a detailed review of competition in the gas sector.*

## **Recommendation 20 - Water**

*Where water regulation is made national, the responsible body should be the proposed national*

*Access and Pricing Regulator (see [Recommendation 50](#)) or a suitably accredited state body.*

50. It is unnecessary to reproduce *Recommendations 42 and 50*, which recommend the continuation of regulation under Parts IIIAA; IIIA; and XIC despite removal of such obligations on powerful firms in market sectors not falling within those Parts, to supply under s.46 as the point about inconsistency has already been adequately made.

## **Further Internal Inconsistencies in Panel Recommendations**

51. It is interesting that the Panel recommends the repeal of the prohibition on exclusionary provisions in *Recommendation 28*, which deals with one type of boycott (primary boycotts), but recommends the retention of s 45D (*Recommendation 36*) and the strengthening of sections 45E and 45EA (*Recommendation 37*) which relate to another type of boycott (secondary boycotts). That dichotomy of approach is puzzling to say the least.

## **‘National Champions’ Argument**

52. The proposals to amend s 46 represent the ‘national champions’ argument in a new garb. The Chair of the Panel, in an interview on ABC television, suggested the

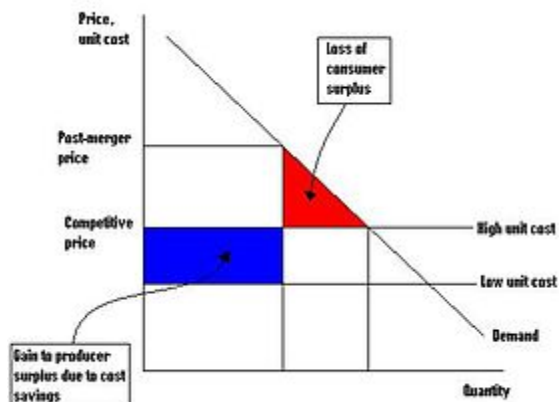
need for Australian firms to 'bulk up'[49] to compete in a globalised world. Perhaps that view has permeated the deliberations of the members of the Panel and led to the recommendations that would have the effect of trying to create 'national champions' if legislated.

53. The *National Champions* argument has been generally rejected by policymakers following the publication of *The Competitive Advantage of Nations*[50]. In a more Australian vein, the then *Trade Practice Commission* likened the national champions argument to the abolition of what was then the Sheffield Shield cricket competition to improve the chances of the national cricket side.

## Redistributive effect of market power

54. Professor Oliver Williamson's Trade-off Model (reproduced below) illustrates the effect of the creation or enhancement of market power through mergers. It is relevant to note that a firm with substantial market power can enhance its market power by conduct of a kind that is currently proscribed by s 46, but would be legally possible if the recommendations of the Panel are legislated, by eliminating small competitors and increasing concentration, close to the level where competition is substantially lessened, but where that test is not breached.

### Williamson Trade-off Model[51]



The model shows that the efficiencies from scale are appropriated by the monopolist which has the power and incentive to raise prices, thus imposing a 'deadweight loss' of surplus on consumers. While the model demonstrates the consequences of 'monopoly' power, the re-distributive effect of transfer of benefits from consumers to producers in concentrated markets applies, as a consequence of collective market power and tacit co-ordinated conduct that does not contravene the prohibitions against overt agreements on prices or other anti-competitive behavior, as discussed below.

## **Unilateral exercise of market power and concentration**

55. Although mergers and acquisitions are the more usual pathways to increasing concentration of markets, a permissive regime against the unilateral exercise of market power, as recommended by the Panel, would result in increasing concentration of markets, over time, arising from the ‘domino effect’, short of substantially lessening of competition. There is a considerable body of literature on the relationship between structure, conduct and performance which shows that concentrated markets lead to anti-competitive conduct and poor economic performance. [52]

56. The following are some decisions by the ACCC to approve mergers and acquisitions which have arguably increased concentration to the level where considerable harm to the public has resulted.

- Acquisition by the Commonwealth Bank of Australia of BankWest.
- Acquisition by Westpac of St. George.
- Combination of the Australian Stock Exchange and the Sydney Futures Exchange to create the Australian Securities Exchange.

57. In the cases of the bank acquisitions, a highly concentrated banking market has emerged, the consequences of which are being felt. The financial advice scandals; the insurance scandals; allegations of interest rate rigging; high fees and charges; high forex margins; poor business decisions e.g. NAB’s disastrous foray into the United Kingdom, can be attributed to lack of competition and the pressures it creates for consumer responsiveness and management efficiency. The ability of the big four banks to gouge customers and operate inefficiently without the market consequences one would expect; together with high levels of executive remuneration (although not limited to banks) have led to consumer outrage. Consumers have suffered and, shareholders could pay the price in the longer term as a result of the public backlash which could lead to greater regulation which would impose higher costs and reduce profits. The ACCC, however, is not the sole arbiter of bank mergers. The Commonwealth Treasurer also has the power, and the responsibility, to clear, or block, such mergers in the public interest. Both regulators receive submissions on issues, including what the proponents argue are emergency factors, but discernment is needed in the evaluation of temporary exigencies, such as the Global Financial Crisis, which may justify time-limited accommodatory arrangements, but not acquisitions, which by their very nature, change market structure permanently. During the GFC, Bendigo Bank; Bank of Queensland; and many building societies and credit unions, much smaller than St. George and BankWest, survived without the necessity of being acquired by one of the Big Four, giving the lie to such claims of international financial exigency. In addition, the Government’s loan guarantee for borrowings by deposit taking financial institutions was a big factor ensuring liquidity and solvency to meet

prudential standards and maintain public confidence, so the necessity of acquiring BankWest and St. George, by the Commonwealth Bank and Westpac respectively, is highly questionable. Furthermore, there are viable alternatives to mergers in circumstances of international emergency conditions affecting borrowing capacity and problematic confidence in solvency of financial institutions. Many competitors in a range of industries during World War II, in many jurisdictions, including the United States of America, and Canada, were allowed to collaborate for the duration of such exigency. Perhaps history is a better teacher than regulators, and others, give it credit for. The combination of substantially increased concentration in banking markets, caused by the above acquisitions, as well as the loan guarantee terms, imposed by the Government on financial institutions, that discriminated in favour of the Big Four vis-a-vis their smaller competitors, has

- accelerated the agglomeration of banking services with other financial services such as financial advice and wealth management, resulting in their becoming financial behemoths;
- led to significant anti-competitive consequences in all those markets, to the detriment of performance in the financial sector generally; and
- caused acute harm to consumers.

58. The ASX/SFE combination, which was once previously rejected by the Commission, was subsequently allowed. Arguably, the poor competition outcome has led the Treasurer to try to introduce competition by structurally separating the settlement function.

## **Societal implications of market power and redistributive effects**

59. Quite apart from the direct effects of market power on prices and consumer welfare, there are two deeper socio-economic implications – effects on inequality of wealth and incomes; and the risk of subordination of the bureaucracy and the body politic as discussed below.

60. Reduced output; higher prices, and declining quality of goods and services arising from exclusionary or predatory conduct, reduce the value of disposable incomes of consumers while increasing producer profits. Consequently, such conduct leads to a redistribution of income from the population at large, including the ordinary citizen and the very poor, to the few, being shareholders and executives of producers. Left unchecked, the inequality between the ‘haves’ and the ‘have nots’ would grow. The economic literature shows the connection between lack of competition; increasing inequality of incomes and wealth; reduced economic growth; and risk of harm to democracy. [53]



61. Experience has shown that the more powerful individual firms or industries are, the greater their propensity to influence governments, sometimes by improper means. While attempts to suborn the political and administrative processes will always be with us for a variety of reasons, the transfer of economic resources from the general population to the hands of a few enterprises/industries which, if allowed to gain or enhance their market power, by preventing, eliminating or damaging entry and individual competitors, facilitates such conduct.

62. The following comments by E.G.Nadeau[54]: express the nature of the risk:

*“Concentrated economic power means that a relatively small number of corporations and individuals make decisions that affect our entire economy and society. Included in this economic decision-making power is the ability to manipulate parts of the market and, in some cases, bring about financial crises that reverberate throughout the entire society.”* and

*“This essay has argued throughout that too much decision-making is concentrated in the hands of large corporations and the wealthy. This manifests itself in too little regulation, which paves the way for self-serving economic abuses that negatively affect the large majority of us. It is built into an electoral and lobbying process that allows those with money to have undue influence on the political system, tilting it to meet their needs and effectively subverting the democratic process. It skews our tax system, so that income and wealth become more concentrated, which besides unfairly taxing the rest of us now is leading toward a less and less tractable deficit crisis in the years ahead.”*

63. The power of big business to influence politicians and bureaucrats is well known. The mining lobby’s successful efforts to stave off the ‘mining tax’ proposed by the Gillard Government is an example. Overseas, examples abound of big business corrupting the body politic. Many public servants have been the object of ministerial pressure, including me, despite not being a decision-maker, but only an adviser. Should we increase the likelihood of such behavior by encouraging further concentration of markets?

## **Proposal for Authorisation of intended s. 46 conduct**

64. As for the proposal to include a provision for authorization, there are two, equally arguable, approaches to it. On the one hand, it appears illogical that conduct traditionally described as 'monopolisation' or 'attempts to monopolise' (in Australia, 'misuse of market power') by very powerful players should be authorized when such conduct has long been perceived in the US to be so pernicious as to merit such powerful sanctions as divestiture and break-up of large, powerful corporations and trusts.[55] On the other hand, the amendments, if passed, only address the intent, or effect, of substantially lessening market competition (as other prohibitions also

prohibit), and, therefore, should be capable of authorisation. Furthermore, even under the existing provisions, there could be some conduct by firms with substantial market power that could be seen as either pro-competitive because of their efficiency-enhancing effects when assessed in all dimensions i.e. productive, allocative and dynamic; or as giving rise to other preponderant public benefits, such as consumer-protection benefits. On balance, adopting the *precautionary principle* of avoiding a blanket ban on conduct that could be seen to be nett positive, the authorization proposal is supported, without the changes proposed to s.46, with which this article takes objection.[56]

## **Effect of reported ACCC position to not pursue 'harm to individual competitors' matters**

65. A matter of considerable concern is the reported statement by the Chairman of the ACCC[57] that it would not pursue conduct aimed at individual competitors but only pursue conduct involving a substantial lessening of competition. Since the amendments proposed have not yet been enacted, it must be concluded that the reported new ACCC policy on enforcement of s.46 applies under the current provisions, as the new provisions would make that position legislatively binding.

66. If the report is accurate, the adoption of that position by the ACCC is highly regrettable for the following reasons.

- As this article argues, conduct aimed at eliminating individual competitors or having the effect of preventing their entry or competitive conduct, inevitably harms dynamic competition; certainly in the longer term and, for reasons articulated above, no bright line can be drawn between conduct harming individual competitors and conduct harming market competition.
- The ACCC would not be enforcing the law as it stands.
- Presumably, because it would be enforcing the current proscription only where the additional criterion of 'substantially lessening competition', not stipulated in law, but one which it has imposed on itself, is met, the ACCC would be pursuing an element of unilateral conduct that the law, as it stands, does not proscribe.
- Victims of conduct currently proscribed would not be likely to pursue their cause in the courts, as they would typically be much smaller than the alleged culprit and, therefore, unable to match the latter in terms of funding the 'fire-power' of highly knowledgeable and expensive lawyers and economists, required in such litigation.
- If the public agency charged with enforcing the law fails to do so, there would be no avenue for the public enforcement of the law, unless the Minister chooses to do so, a highly unlikely prospect.

## **Implications for small business**

61. Small business is the key driver of employment; a significant source of innovation; and an opportunity for individuals who choose to create their own enterprise. Competition law has posed a challenge for policy-makers in reconciling the objective of efficiency from large scale and the legitimate interests of small business in claiming protection from predatory or exclusionary conduct by large and powerful firms, which threatens the ability of small firms to compete on their merits. As this paper shows, there need be no tension between the objectives of efficiency and opportunity to enter markets and compete on the merits. The ACCC; its designated Small Business Commissioner; the Small Business and Family Enterprise Ombudsman; and relevant policy-making departments; all have a role to play in ensuring the protection of small business from illegal conduct. It is surprising, therefore, that no objection has been expressed, by those charged with that responsibility, against these proposed amendments, rather, support has been expressed for the amendment proposals. Neither has the Council of Small Business Australia or the Australian Chamber of Commerce and Industry raised their voices in opposition to the Bill, which would harm their members and that is inexplicable except by assumption that neither the office-holders nor members are aware of the implications of the proposed amendments on their businesses. Nevertheless, if enacted, the amendments would limit their ability to fulfill their responsibilities to protect the legitimate interests of small business.

## **Simplifying the Law**

62. A theme in the Panel report and recommendations is the objective of *simplification of the law*[58]. In doing so, little regard appears to have been had to the tortuous evolutionary process of the law in other jurisdictions, particularly the U.S. There is a significant amount of legislation and judicial interpretative doctrines which has guided the development of the law there. Jurisdictions more recently adopting competition law have had regard to the principles of U.S. law and jurisprudence. While the E.U has relatively simple black letter law, the administrative process e.g. block exemptions, regulations, directives and economic analysis in litigated cases, clearly have had regard to the U.S. law and jurisprudence and to profound consideration of sophisticated analyses of the economic effects of unilateral exclusionary or predatory conduct, as it has evolved. Hence it is apposite to visit the U.S. law and jurisprudence to examine the claim of a need for simplification of the law in Australia.

## **Complexity of the Law in the United States**

## Legislation

63. There have been the following pieces of *legislation* which took many decades to evolve in the United States.

(a) *Anti-trust Act 1890*, known as the *Sherman Act*, after its sponsor, U.S. Senator John Sherman of Ohio,[59] prohibited agreements in restraint of trade; and monopolization, or attempts thereat. (26 Stat. 209, 15 U.S.C. §§ 1–7):

(b) *The Anti-trust Act 1914 (known as the 'Clayton Act')* amended the *Sherman Act* to cover acquisitions of stock[60] (*Pub.L. 63–212, 38 Stat. 730, enacted October 15, 1914, codified at 15 U.S.C. §§ 12–27, 29 U.S.C. §§ 52–53*),

(c) *Antitrust Procedures and Penalties Act, 1914* (known as the '*Tunney Act*'); 15 U.S.C. § 16(b)

(d) *The Federal Trade Commission Act 1914*; created the Federal Trade Commission (*15 U.S. Code § 41*)

(e) *Capper-Volstead Act 1922*: granted certain agricultural cooperatives limited immunity from the antitrust laws, permitting their members jointly to process, prepare for market, handle, and market their commodities; (7 USC 291-292)

(f) *Robinson-Patman Act 1936*: Prohibited anti-competitive practices by producers, especially price discrimination (*Pub. L. No. 74-692, 49 Stat. 1526 (codified at 15 U.S.C. § 13)*) (g) *Celler-Kefauver Act 1950*: extended the application of the *Clayton Act* to acquisitions of assets (*64 Stat. 1225*)'

(h) *Anti-Trust Improvement Act 1976* known as the '*Hart-Scott-Rodino Act*' which amended the *Clayton Act* to require pre-merger notification of certain categories of mergers: (15 U.S.C. § 18a)

(i) *Foreign Trade Anti-trust Improvement Acts of 1982 and 1986* aimed at protecting U.S corporations engaging in trade in countries without legislation comparable to U.S. anti-trust law : (15 U.S. Code § 6a).[61]

## Judicial activism

64. *Judicial activism* in the form of 'doctrines', which became necessary because of legislative vacuum or ambiguity, introduced by Courts in judgments, is extensive. The 'simple' U.S. legislation has led to decades of litigation on the exact

scope and meaning of the anti-trust laws, a consequence foreseen by the U.S. Senate, according to the literature describing the legislative history of the *Sherman Act*, but accepted by the legislature in light of its confidence in the ability of the judiciary to properly interpret the law. The U.S. judiciary, however, is known to be interventionist, unlike the Australian judiciary, which eschews judicial activism. The long, complex and contorted formulation of various anti-trust principles by the judiciary on the law as it is now understood in the U.S. is a powerful argument in favour of reasonably prescriptive legislation rather than *simple* legislation which proves *vague* and leaves courts to decide on the ambit of the law. Examples of such judicial activism is to be found in the various doctrines, and rules (not only in court judgments but also by bureaucratic rule-making) in the U.S, which add to complexity as follows:

(a) *Rule of reason vs per se* – changing judicial views on the standard by which particular conduct should be adjudged, led to a pendulumatic oscillation between a *per se* or *rule of reason* test for some types of conduct. Some verticals were first ruled *per se*, then dealt with under the *rule of reason* test. [62] Geographical restraints were also subject to similar changes in the test. Ultimately, generally agreed *per se* tests were applied to boycotts [63]; resale price maintenance; price fixing and ‘tie-ins’ (third line forcing).

(b) *The Essential Facilities Doctrine* [64] – obligation on owner of essential facilities to provide access to competitors, reflected in Parts IIIAA; IIIA; and XIC of the CCA.

(c) *Legitimate Business Purpose Doctrine* [65] appears to have been interpreted by Australia’s High Court as ‘rational business decision’ in *Boral Besser Masonry*.

(d) *State Action immunity doctrine* [66] - reflecting ‘*Shield of the Crown*’ in Australia.

(e) *Noerr-Pennington Doctrine* [67] - right to petition government and invoke legal rights,

(f) *Sham exception to Noerr-Pennington* - misuse of entitlement for anti-competitive purposes. [68]

(g) *Efficiency defense* – The U.S. jurisprudence requires efficiency to be taken into account in assessments of anti-trust cases.

(h) Export exemptions and bureaucratic exemptions for import cartels.[69]

(i) *Incipency doctrine* in cases under section 7 of the *Clayton Act*.[70]

65. Instead of such uncertainty, a reasonably level of codification is distinctly superior. It is clear that the law could be simplified in a drafting sense to remove unnecessary verbiage in the RPM section and the cartel provisions much of which may have their origin in constitutional considerations that are now probably irrelevant. *There is no justification, however, in emasculating s.46 in the pursuit of simplicity.*

66. The perceptive comments by Senator John Sherman are at least as relevant today as when they were made:

*“If we will not endure a king as a political power, we should not endure a king over the production, transportation, and sale of any of the necessities of life.*

## **Conclusion**

67. Australians have long held and cherished a firm belief in the principle of *A Fair Go* in all fields of endeavour. To allow smaller businesses to become carrion to predatory conduct by large and powerful firms is a betrayal of that principle.

68. The consequences of legislating the proposed amendments for national economic efficiency, innovation, entrepreneurship, employment, international competitiveness, living standards and economic growth would be highly deleterious in an environment of growing intensity of international competition.

## **Recommendations**

69. The Bill should be rejected by the Parliament on the basis of their effects on the long term dynamism of the economy. The reported position taken by the ACCC in relation to its enforcement of s.46, as the regulator charged by the Parliament to enforce the law, should also be closely examined by a Parliamentary committee.

70. The Parliament should:

(a) accept the recommendation to introduce the *effects* leg of the test of culpability;

(b) accept the recommendation to replace the phrase *taking advantage* by the phrase *engage in conduct*;

(c) reject the the recommendation to replace the current substantive prohibition in section 46 with the sole test of *substantial lessening of competition*;

(d) reject the the recommendation to repeal amendments to the section made since 2007.

## End Notes

- [1] The author worked for 25 years in the *Australian Competition and Consumer Commission* and its predecessor, the *Trade Practices Commission*, in all their areas of responsibility. Since leaving the Commission, he has advised the *Department of Communications, Information Technology and the Arts* (as it then was); and Governments and competition authorities in *Fiji* and *Papua New Guinea* on competition and structural reform over many years.
- [2] [https://consult.treasury.gov.au/market-and-competition-policy-division/ed\\_competition\\_law\\_amendments](https://consult.treasury.gov.au/market-and-competition-policy-division/ed_competition_law_amendments)
- [3] See *Barton v Westpac Banking Corporation (1983) FLR 101; 50 ALR 397; ATPR 40-407*
- [4] See the *document retention policy* of tobacco companies which, under the guise of *preserving* relevant documents, led to the *destruction of 'old' documents*: <http://www.theage.com.au/news/National/Tobacco-bodystrash-tactics/2005/02/10/1107890345799.html>
- [5] *Queensland Wire Industries Pty Ltd v Broken Hill Proprietary Company Ltd & Anor (1989) 167 CLR 177; 63 ALJR 181; 83 ALR 577; ATPR 40-925* See also, *National Competition Policy Review*; August 1993; ISBN 0 644 [Hilmer Committee] which recommended no change to s. 46. T
- [6] *Melway Publishing Pty Ltd v Robert Hicks Pty Ltd (2001) 205 CLR 1 at 21 [44], 27 [67]* per Gleeson CJ, Gummow, Hayne and Callinan JJ.
- [7] *Rural Press Limited v ACCC [2003] HCA 75.*
- [8] Act 116 of 2008, section 3 and schedule 1 item 5.
- [9] Senator John Sherman of Ohio.
- [10] This provision also outlaws *combinations and conspiracies to monopolise or attempts to do so*, which the Australian legislation does not, although such co-ordinated conduct is caught by s.45, which prohibits contracts, arrangements or understandings which restrict dealings or substantially lessen competition. . The principle of *joint dominance* in the European jurisdiction, is more closely aligned with the Australian approach, which envisages more than one firm possessing substantial market power.
- [11] . It is not suggested that the extremely wide U.S. provision be adopted in Australia.
- [12] Difficulties in co-operation may be created by substantive differences between the relevant prohibition in the Australian law and the law of another country as it is a usual requirement of co-operation provisions that there be substantive similarity of the relevant prohibition.
- [13] Section 5 (1A), inserted by Section 6 of Act No. 70 of 1990, extends application of s.46A to conduct by NZ Crown Corporations; bodies corporate carrying on business in New Zealand; or persons ordinarily resident in New Zealand; and removal of *Shield of the Crown* immunity by section 46B, from sections 36A, 98H and 99A of the *Commerce Act 1986* of New Zealand. Mirror legislation in the N.Z. legislation reciprocates these provisions.
- [14] Inserted by Act 70 of 1990, s 8.
- [15] For example, a firm with substantial market power in Australia, *capable* of competing in the NZ market, may engage in exclusionary or predatory conduct in relation to a firm operating in New Zealand firm. The principles of market definition include *potential competition*. Would the conduct be judged under s46 or 46A?

- [16] It is recognized that the test does look at likely effects but in a relatively short term context. Even in mergers, where forward-looking concepts are involved, the time-frame for analysis is one to two years, which is very short-term, when long-term market dynamics from structure and conduct are involved, as they shape the economy, in behavioural terms, for generations to come e.g. innovation and entrepreneurship.
- [17] *Boral Besser Masonry v The Australian Competition and Consumer Commission* [2003] HCA 5; (2003) CLR 374; 77 ALJR 623; 195 ALR; ATPR.41-167. See particularly, the judgment of McHugh J.
- [18] The recommendation to repeal sections 46 1A and 46 1 AA, which were introduced following *Boral*, brings back into the frame the whole recoupment argument, which those provisions were intended to avoid.
- [19] Many corporate decisions, such as to engage in corrupt or illegal conduct, can be regarded as *irrational* because the risk of detection is high and financial and reputational consequences are severe; but they are regularly made. The dominating motive may be corporate profit maximization and resulting remuneration benefits for executives, a rational motivation for the human perpetrators.
- [20] For a discussion of *bounded rationality*, see: Simon, H.A., 1957, *Models of Man*, New York, Wiley & Sons; and *What is Bounded Rationality?* SFB Discussion Paper B-454 prepared for the Dahlem Conference 1999 by REINHARD SELTEN May 1999.
- [21] Referred to by His Honour Mr Justice Kirby in *Boral Besser Masonry op cit*.
- [22] “*superior skill foresight and industry*” in *United States v Grinnell Corp* 384 US 563 at 577 (1966)
- [23] Whereas pre-entry, *information asymmetry* disadvantaged customers, the effects of new entry is likely to have negated that.
- [24] There may be a temporary hiatus in price maximization due to reputational concerns and, after that, economic rents may be re-commenced to be reaped by the incumbent(s).
- [25] See *Re: Queensland Cooperative Milling Association and Defiance Milling Corporation Limited and Barnes Milling Limited* (1976) 25 FLR 169; 8 ALR 481; 1 ATPR 40-012; discussed in greater detail later in this article.
- [26] With the elimination of a competitor, it becomes easier for the incumbent to prevent entry or eliminate others due to increasing returns to scale and the chilling effect.
- [27] The concept of *competition on the merits* is discussed further in this article.
- [28] Justices Gummow, Gaudron and Hayne in *Boral Besser Masonry*, quoted *Brown Shoe Co v United States* 370 US 294 at 320 (1962); *Brooke Group Ltd v Brown & Williamson Tobacco Corp* 509 US 209 at 224 (1993) in support of the proposition that the law was aimed at protecting competition rather than competitors.
- [29] *United States v Grinnell Corp* 384 US 563 at 577 (1966)
- [30] *Queensland Wire Industries v Broken Hill Pty Ltd* (1989) 167 CLR 177 at p. 191 (‘*QWI*’) quoted in *ACCC Draft Framework for Misuse of Market Power Guidelines; September 2016*;. Interpreted in the majority judgment in *Boral Besser Masonry* as “*Competition damages competitors. If the damage is sufficiently serious, competition may eliminate a competitor.*” Cited also in Treasury Discussion Paper: ***Options to strengthen the misuse of market power law; December 2015***
- [31] “ *the object of s.46 is to protect the interests of consumers the operation of the section being predicated on the assumption that competition is a means to that end.*” The significance of this sentence is that the effect on a competitor needs to be considered in the analytical frame of prices, quantity and quality of goods or services that will ultimately be available to customers and, consequently, consumers.
- [32] Unless, of course, creditworthiness or other legitimate purposes suggest refusal to supply is the most sensible approach.
- [33] See ‘*competition on the merits*’ Discussed later in this article.



- [34] *National Competition Policy Review Report*; August 1993; ISBN 0 644
- [35] *The Anti-trust Paradox – a system at war with itself*. Simon & Schuster, 1993; ISBN 0029044561 9780029044568.

[36] *Brooke Group*, 509 U.S. at 223 (“As a general rule, the exclusionary effect of prices above a relevant measure of cost either reflects the lower cost structure of the alleged predator, and so represents competition on the merits, or is beyond the practical ability of a judicial tribunal to control without courting intolerable risks of chilling legitimate price cutting”).

A useful discussion of this concept is to be found in *OECD Roundtables: Competition on the Merits; 2005. DAF/COMP(2005)27; 30 March 2006*: “The profit sacrifice test states that conduct should be considered unlawful when it involves a profit sacrifice that would be irrational if the conduct did not have a tendency to eliminate or reduce competition. The no economic sense test states that conduct should be unlawful if it would make no economic sense without a tendency to eliminate or lessen competition. The equally efficient firm test states that conduct should be unlawful if it would be likely to exclude a rival that is at least as efficient as the dominant firm is. Consumer welfare balancing tests determine whether conduct should be unlawful by requiring decision-makers to weigh the positive and negative effects that the conduct has on consumer welfare.” These tests are conceptually similar to that proposed by Bork under his output restriction test.

[37] *United States v Grinnell Corp*; 384 U.S. 563 (1966).

[38] *Byars v Bluff City News Company Incorporated*; 609 F.2d 843 (6<sup>th</sup> Cir. 1980)

[39] See: Edwards, *The Perennial Problem of Predatory Pricing*, (2002) 30 Australian Business Law Review 170 at 181 fn 56 (original emphasis). “[F]irms with less than the pricing discretion of a pure monopolist can also achieve prices well above competitive levels, and even if not a pure monopoly, any firm with a substantial degree of market power certainly would have such an ability.”

[40] <https://www.accc.gov.au/system/files/Merger%20guidelines.pdf>. Also, <https://www.justice.gov/atr/horizontal-merger-guidelines-08192010>. These have changed. Previously, competition authorities not only considered Herfindahl Hershman Index measures, but also CR4 and CR1 measures for co-ordinated and unilateral market power assessments: However, HHI has the advantage of measuring *changes in concentration (Delta)* which may be more meaningful.

[41] Op cit.

[42] *Boral Besser Masonry* op cit.

[43] It is recognized that the Panel recommendations include repeal of the prohibition of exclusionary provisions in section 4D.

[44] *In re: Queensland Cooperative Milling Association and Defiance Milling Corporation Limited and Barnes Milling Limited* (1976) 25 FLR 169; 8 ALR 481; 1 ATPR 40-012. In considering barriers to entry, barriers to exit need to be considered as well. See *U.S. Department of Justice Horizontal Merger Guidelines*, op cit.

[45] Ultimately, allocative efficiency as well.

[46] Op Cit.

[47] The appellant, Queensland Wire Industries, in effect, had virtually no market share in the supply of star pickets (apart from a trial shipment from Korea). Hence no substantial lessening of competition could be concluded. *Its potential market share also could not be definitively quantified as substantial*.

[48] Refusal of access to (a) essential facilities has long been considered in the U.S. jurisdiction to contravene Section 2 of the Sherman Act e.g. *United States v. Terminal Railroad Ass'n* 224 U.S. 383 (1912); *Otter Tail Power Co. v.*

*United States* 410 U.S. 366 (1973) and (b) refusal to supply an essential physical input as well: *U.S. v. Corn Products Refining Co. et al.*, 234 Fed. 964 (1916).

[49] 22nd September 2015

[50] Professor Michael Porter, then of Harvard University; ISBN 978-0-333-73642-5

[51] *Williamson, O.E. (1968). "Economies as an antitrust defense: The welfare tradeoffs". American Economic Review* 58, 407–426.

[52] With the first competitor eliminated, the incumbent would be emboldened to repeat its conduct and small competitors are likely to be intimidated into exit rather than vigorously competing ('disciplining effect') and the incumbent may, with elimination of successive competitors, enjoy increased scale economies which strengthen its position and encourage similar conduct. Sherman s.2 which outlaws 'attempts to monopolise', addresses this problem and s.46, in effect, does so also in the provisions proposed to be repealed.

[53] Nobel Laureate Professor Joseph Stiglitz: *The Price of Inequality: How today's Divided Society Endangers Our Future*, New York: WW Norton, 2012. Harvard Law Review: Volume 129, Number 5 - March 2016: INEQUALITY AND ECONOMIC GROWTH; [www8.gsb.columbia.edu/](http://www8.gsb.columbia.edu/) and Thomas Piketty: *Capital in the Twenty First Century*; translated by Arthur Goldhammer; Belknap/Harvard University Press • 2014.

[54] *The Cooperative Solution*; ISBN 978-1478298267.

[55] For example, *U.S v American Telephone and Telegraph Modification of Final Judgment*; 552 F. Supp. 131 (D. D.C. 1982); *Standard Oil Co. of New Jersey v. United States*, 221 U.S. 1 (1911)

[56] See Professor Stephen King's article: <https://theconversation.com/changes-to-competition-laws-mayhurt-consumers-56364>.

[57] Read by the author in the Fairfax press, who has sought date of publication and is awaiting response from Fairfax. Mr Rod Sims, Chairman of the Commission, is also reported in the *AFR* as describing the proposed amendments as 'unambiguously good' – date awaited from Fairfax. ACCC did not provide details on the basis that it does not comment on reports. A further request has been made to the ACCC to establish whether it has formulated a policy of not pursuing s.46 matters that it considers only affect individual competitors but do not substantially lessen competition; and whether Mr Sims has publicly described the proposals as 'unambiguously good'.

[58] *Competition Policy Review Draft Report*; September 2014. © Commonwealth of Australia 2014 ISBN 978-1-925220-08-7. In its draft report, an objective of the competition law was stated to be: "...clear, predictable and reliable". No objection is taken to that objective but effectiveness of the law in preserving longterm competition should not be sacrificed for clarity, predictability and reliability exclusively. Another stated objective of the Panel: "encourages innovation, entrepreneurship and the entry of new players;" which in this author's view, it works against, by damaging freedom of entry. The latter objective is far more important than the former. At page 38, the report asks: "Is the law as simple as it can be consistent with its purpose?" It concludes: "The competition law provisions of the CCA would benefit from simplification, while retaining their underlying policy intent." For the reasons in this article, the author submits the simplification exercise, described in the report fails this test.

See also, discussion of simplification in: <https://theconversation.com/harper-makes-case-for-competition-overhaulexperts-react-39582>.

[59] It is commonly thought that the *Sherman Act*, was the first 'anti-trust' law, however, the U.S. *Interstate Commerce Act of 1887*, prohibited joint rate setting; inside rebates; price discrimination; and division of traffic aimed at road hauliers, , was, arguably, the first law regulating anti-competitive conduct.

[60] i.e. shares

- [61] The proposed amendments could trigger the operation of this legislation, exculpating U.S. corporations from anti-competitive conduct in Australia.
- [62] *Per se v Rule of Reason*: With respect to non-price vertical restraints, *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1978), overruled *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365 (1967). See Robert Bork, *Vertical Restraints: Schwinn Overruled, 1977 SUP. CT. REV. 171 (celebrating the Sylvania decision)*.
- [63] The current prohibition of exclusionary provisions in the CCA
- [64] *United States v. Terminal Railroad Ass'n* 224 U.S. 383 (1912); *Otter Tail Power Co. v. United States* 410 U.S. 366 (1973)
- [65] See *Byars v Bluff City News* op cit.
- [66] COMMENT: THE STATE ACTION EXEMPTION IN ANTITRUST: FROM PARKER V. BROWN TO CANTOR V. DETROIT EDISON CO. <http://scholarship.law.duke.edu/cgi/viewcontent.cgi?article=2635&context=dlj>
- [67] Private entities are immune from liability under the antitrust laws for attempts to influence the passage or enforcement of laws, even if the laws they advocate for would have anticompetitive effects: *Eastern R. Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127 (U.S. 1961) and *United Mine Workers v. Pennington*, 381 U.S. 657 (U.S. 1965)
- [68] “The Sham exception to the *Noerr-Pennington Doctrine*”; Christine M Spitzer; *Hastings Law Quarterly*; 11:329: “When the underlying goal of such petitioning is to interfere directly with a competitor, and the right to petition is merely a means to that end, then the First Amendment will not shield the petitioner from liability under the Sherman Act.” In Australia, ACCC brought action against a supermarket, for routinely objecting in liquor licensing process against private, individual applicants and succeeded.
- [69] For example, for importers fixing the acquisition price of petroleum imports- see Antony Sampson’s *The Seven Sisters: The Great Oil Companies and The World They Shaped* which describes how the U.S. Department of Justice gave a Business Review Letter to the U.S. oil companies to form a buying cartel, from which, the author considers, the middle east oil producers learned well to subsequently form the selling cartel, Oil Producing and Exporting Countries (OPEC).
- [70] Op cit. U.S. jurisprudence has not only considered and ruled against firms where actual market power existed, but where, despite no actual monopoly, or restraint, or substantial lessening of competition was found to have been intended, or to have occurred, but also where, in the long term, the possibility of any of those outcomes was *incipient* from the conduct. *Incipieny doctrine* under section 7 of Clayton Act: see *United States v. E. I. du Pont de Nemours & Co.* 353; U.S. 586 (1957). See also: Nicola Giocoli: *Predatory Pricing in Antitrust Law and Economics: A Historical Perspective*

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