Business Council of Australia

SUBMISSION

Submission to the Senate Economics Committee on the Competition and Consumer Amendment (Misuse of Market Power) Bill 2016

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Contents

The Business Council of Australia is a forum for the chief executives of Australia's largest companies to promote economic and social progress in the national interest.

About this submission

This is the Business Council of Australia's submission to the Senate Economics Legislation Committee on the Competition and Consumer Amendment (Misuse of Market Power) Bill 2016. The submission attaches an independent legal opinion prepared by Neil Young QC in June 2016.

The Bill implements changes to section 46 of the *Competition and Consumer Act 2010* that were recommended by the Competition Policy Review ('Harper Review'). It replaces the current section 46 with a test that adds an 'effects' alternative, removes the 'take advantage' element and refers to a 'substantial lessening of competition'. These changes were recommended "to improve its clarity, force and effectiveness"[1].

The Business Council disagrees with the changes and supports retention of the current section 46 for the reasons detailed in its past submissions and in Mr Young's opinion. The current law works as intended and is well understood, while the new law introduces considerable regulatory uncertainty, risks capturing pro-competitive behaviour and is misaligned with equivalent provisions in other countries.

Contrary to the government's intentions, the new law will be costly and disruptive for business and risks harming innovation and price discounting, thereby working against the interests of consumers. It will increase regulatory risk at a time of weak business investment and economic growth. If the provision is to proceed, it should be amended to send a clear signal to all businesses that competitive behaviour that is good for consumers will be unambiguously protected under Australian law.

Key recommendations

- The Committee should recommend rejection of the Bill unless it is amended to substantially reduce regulatory risk by:
  - specifically focussing the law on 'exclusionary conduct', which should be defined as unilateral conduct that interferes with the competitive process by preventing or deterring rivals or potential rivals from competing on their merits; and
  - protecting against the capture of conduct that has a legitimate commercial or business reason, or which advances the long-term interests of consumers.
    (These amendments are consistent with the ACCC's draft guidance materials.)
- The Committee should recommend a post-implementation review within two years of the commencement of any new provision. The review should assess the costs and benefits of the changes and identify whether any further legislative amendments are needed.
- The Committee should recommend that the ACCC provide six-monthly reports on complaints, investigations and authorisations activity under any new provision, to enable monitoring of the impacts of the Bill on costs and economic activity.
- The Committee should consider recommending a period of immunity from civil penalties and damages for conduct that has not previously been found to breach the new section.

1. Competition Policy Review, Final Report, March 2015, page 61

Submission on the Misuse of Market Power Bill

Assessment of the new provision

Healthy competition requires that businesses of all sizes are able to compete vigorously on merit, because this is in the best interests of consumers.

To support this, a well-designed 'misuse of market power' provision (section 46) must prevent companies with substantial market power from abusing that power to harm the competitive process (ie, by preventing or deterring rivals or potential rivals from competing on their merits), while also making it clear that legitimate competitive behaviour will not contravene the law.

The government has accepted the Harper Review's finding that the current section 46 needs to be 'strengthened' to make it more enforceable and to more effectively target and deter anti-competitive conduct. It has accepted the Review's recommended changes, even though no specific examples of conduct going unprosecuted under the current law have been presented to justify the changes.

The Business Council has consistently pointed out the flaws in the Harper Review's recommendation and opposed its introduction. However, now the Bill has been introduced it is important to get the wording right to avoid unintended consequences.

The new law is too broad and too ambiguous. It will potentially make illegal, and as a result will deter, competitive conduct by businesses with substantial market power that is good for consumers. It does not provide the clarity that is needed for businesses to compete vigorously, such as by price discounting or innovating.

The Business Council's submission attaches an independent legal opinion of the Harper Review's recommendations by Neil Young QC, one of Australia's most respected competition law barristers and a former judge on the Federal Court, prepared in June 2016. A summary is provided in Exhibit 1.

Mr Young finds that the new provison overreaches its proper role and there is a real risk of over-capture of competitive behaviour. He finds the provision is so broad as to be an outlier when compared to similar provisions in other countries, and concludes that it must be amended to address these problems.

Categories of competitive behaviour that are good for consumers but which could be illegal under the new law include lower prices, new product offerings and new store roll-outs.

Mr Young's opinion was provided to the government in our submission on the draft legislation in November. The government has since amended the draft legislation to limit the consideration of competition impacts to markets in which a company buys and sells products, rather than 'any market'. However the core problems relating to the breadth and the ambiguity of the new provision remain unaddressed.

Exhibit 1: Summary of legal opinion

Extracts from Neil Young QC's opinion on the Harper Review's recommended s 46

[Para 15] … There is some justification for the elimination of the "taking advantage" test… but, there are shortcomings in the way in which the Harper Committee seeks to substitute a so-called effects test for the current provision, which mean that the recommended section overreaches its proper role

[Para 16] Contrary to the view expressed by the Harper Committee the existing s46 is very much a mainstream provision when compared to its international analogues. It is the form of s46 proposed by the Harper Committee which is the outlier…

[Para 27] … the evidence seems to be overwhelming that the form of s46 proposed by the Harper Committee is an extreme outlier.

[Para 38] A very large number of companies in Australia will fall within the reach of the new s46. This is so because, in the Australian economy, the class of corporations that have a substantial degree of power in the market or markets in which they operate is a very wide one… The consequence is that, for the first time, many ordinary business decisions by those corporations will potentially fall within the reach of the new s46

[Para 59] … the message that emerges from this brief review of the authorities is that many uncertainties attend the application of the substantial lessening of competition test. Moreover its application is fact intensive and usually time consuming… The application of such a test to conduct engaged in by every corporation that falls within the wide reach of the new s46 is likely to be very disruptive to business.

[Page 65] In my view, the recommended s46 (2) is an empty vessel. It does no more than require the Court to have regard to two considerations which are in any event embraced within the concept of conduct that has an effect or likely effect of substantially lessening competition.

[Para 68] There is no suggestion in the case law applying the substantial lessening of competition test that it only applies to particular forms of conduct such as exclusionary conduct. To that extent, the arguments advanced by the ACCC are not consistent with the language of the proposed s46 or the case law that has expounded on the substantial lessening of competition test.

[Para 70] The logical flaws in the arguments advanced by the ACCC exposes a hole in the reasoning that underpins the Harper Committee's recommendation.

[Para 71] It is unclear how the revised s46 would be applied to unilateral conduct by large corporations, such as major supermarkets or hardware stores, which expand into smaller communities or markets in a way that is likely to lead to small businesses to exit that market. If the market is defined very narrowly, as the ACCC is prone to do, then the loss of small competitors on the major's entry could easily be treated as a substantial lessening of competition

[Para 73] The foregoing analysis demonstrates, in my view, that the risk of over-capture is real and imminent. It is unclear how those risks will be resolved.

[Para 74] Working from the premise that s46 is to be amended so as to include a prohibition on conduct that has the effect or likely effect of substantially lessening competition, there are in my view a number of improvements that could be made to the provision.

[Para 75] In my opinion, the following changes warrant serious consideration… a) … purpose and effect should be cumulative requirements… b)… the provision should be limited to any other market in which the corporation supplies or acquires goods and services… c)… it should be accompanied by a meaningful safeguard that confines the principal provision to anti-competitive or exclusionary conduct.

[Para 81] The changes I have proposed to s46 (1) are the minimum changes necessary to address the problems I have identified.

[Para 82] More broadly, my revised s46 is consistent with the ACCC's public assurances that the proposed s46 is not aimed, and should not be aimed, at anything other than exclusionary or anti-competitive conduct.

Chilling effects of the new law

Under the new law businesses with substantial market power could be liable for the unforeseen effects on competition resulting from any of their conduct. This will potentially deter innovation and price discounting as businesses are required to continually weigh up the risk of court action and large penalties when engaging in competitive behaviour.

Companies that contravene the provision could be fined up to 10 per cent of annual turnover. Individuals could face fines of up to $500,000. These costs are in addition to the legal and reputational costs from being investigated or taken to court.

A large number of companies across many sectors of the economy will be subject to the law, including smaller businesses in regional areas where markets can be more narrowly defined.

Addressing the problems in the Bill

There are two key problems with the provision that need to be addressed.

First, it is too broad, because ‘any conduct’ by a business with market power could be found to be illegal, not only anti-competitive ‘exclusionary conduct’, which the ACCC itself has consistently argued should be the only type of behaviour that is caught by the provision.

The Explanatory Memorandum argues against prescribing the conduct relevant to section 46, so as to be able to capture new forms of anti-competitive conduct in the future:

> […] it is not possible to prescribe specific forms of conduct which always will or will not contravene section 46. […] Rather than requiring a determination of whether conduct fits within detailed technical descriptions, the mandatory factors provide for a principled, holistic assessment of the conduct and its purpose, effect or likely effect in the particular circumstances of the market in question. This ensures that section 46 is flexible and may be applied to new forms of anti-competitive conduct as they arise. (Explanatory Memorandum, 1.29 and 1.30, page 10)

While there may not be a case for prescribing specific forms of conduct per se, there is a need for the provision to clearly focus on conduct that is ‘exclusionary’.

‘Exclusionary conduct’ should be defined in the provision as unilateral conduct that interferes with the competitive process by preventing or deterring rivals or potential rivals from competing on their merits. (Typically, this might include cases of predatory pricing, bundling, refusal to deal or price discrimination, depending on the circumstances; noting all of these examples can be dealt with now under the current section.)

Importantly, this would make it clear to a business engaging in conduct that is not ‘exclusionary’ that it is not at risk under the law and is free to compete on merit. By contrast, ‘any conduct’ by a business with substantial market power could be captured under the provision as drafted.

There would be no loss of flexibility in focusing the section, because exclusionary conduct in all its forms will always be the type of unilateral behaviour that is recognised by international jurisprudence and economics as damaging to competition. It is a future-proof

definition of behaviour that is relevant to the provision and which improves regulatory certainty for business.

Secondly, the new 'substantial lessening of competition' test will be difficult to apply to unilateral conduct and requires stronger safeguards to protect pro-competitive and pro-consumer behaviour.

The weighing up of mandatory pro-competition and anti-competition factors under the new test is deliberately designed to be ambiguous and provides very little guidance and no certainty for business decision-making. The Explanatory Memorandum demonstrates this:

> […] it is not possible to prescribe how any particular factor will be weighted in reaching a determination as to the overall purpose, effect or likely effect of conduct. How the factors are weighted will depend on the particular circumstances of the conduct.
>
> In particular circumstances, it is possible that one anti-competitive factor is so significant as to outweigh one or more pro-competitive factors. Similarly, one pro-competitive factor may be so significant as to outweigh one or more anti-competitive factors. In some circumstances, a factor which is not listed in subsection 46(2) may nevertheless be of significant weight. (1.37 and 1.38, page 11)

When businesses are making decisions to innovate, expand their business or reduce prices they will be required to go through this 'weighing of factors' process internally and second guess how a court might interpret their conduct under the legislation. It will be time–consuming and costly to apply. This will create uncertainty and cause risk-aversion in business, with consumers and the economy bearing the ultimate costs should vigorous competition be impeded.

In the words of Neil Young QC, the mandatory factors are an 'empty vessel'. A stronger defence for legitimate business conduct is required. A better approach would be to make it clear that legitimate business conduct that is pro-competitive and which advances the interests of consumers is at all times protected under competition law.

Amending the Bill

The Business Council's recommended amendments below retain the core elements but make clear the new provision is only concerned with 'exclusionary conduct' and provide a meaningful protection for conduct engaged in for legitimate business reasons (provided the conduct is not disproportionate to the achievement of that reason) or which has the effect of advancing the interests of consumers:

> (1) A corporation that has a substantial degree of power in a market must not engage in exclusionary conduct that has the purpose, or has or is likely to have the effect, of substantially lessening competition in that market or any other market in which the corporation supplies or acquires goods or services.
>
> (2) For the purposes of subsection (1), "exclusionary conduct" means unilateral conduct that interferes with the competitive process by preventing or deterring rivals or potential rivals from competing on their merits.
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> (3) For the purposes of subsection (1), conduct will not be considered to have the purpose, or to have or be likely to have the effect, of substantially lessening competition in any market where:

(a) the corporation has or had a legitimate commercial or business reason for engaging in the conduct, and the conduct was not unreasonable or disproportionate to the achievement of that legitimate commercial or business reason; or

(b) the conduct would be likely to have the effect of advancing the long-term interests of consumers.

These changes should not be controversial as they reflect the principles set out in the ACCC's draft guidance materials and are consistent with the government's policy objectives. They are needed to be included in the provision itself because the ACCC's guidance has no weight in law and provides business with insufficient certainty. The ACCC itself acknowledges its guidance materials will not bind the court. They will have no effect where business is the subject of litigation by private parties. The guidance could also easily be changed in future under different leadership of the ACCC.

Post-implementation

Immunity from civil penalties and damages

Given the uncertainty surrounding the new provision, consideration should be given to immunity from civil penalties or damages for conduct that has not previously been found to breach the new section.

A clear precedent for this approach can be found in the *Competition Act 1998* of South Africa. Section 8 of that Act prohibits a dominant firm from engaging in particular forms of exclusionary conduct, such as exclusive dealing, refusals to deal, tying or bundling, selling below marginal or average variable cost, or buying up scarce inputs. It also prohibits such a firm from engaging in any other exclusionary act, which it defines as an act that impedes or prevents a firm from entering into, or expanding within, a market.

In both cases there is a defence for conduct that has technological, efficiency or pro-competitive gains that outweigh any anti-competitive effect. However, in relation to the specific exclusionary acts the firm must prove these efficiencies, while in relation to the general prohibition the onus of proof is reversed and the other party must prove that the anti-competitive effect outweighs any efficiency gains.

Critically, in relation to the general prohibition there is no administrative penalty for a first-time contravention, only for a repeat offence. These differences are designed to compensate for the uncertainty that the open-ended and general prohibition of exclusionary conduct presents for business decision-making.[2]

As the current Bill is not even limited to exclusionary conduct, the additional uncertainty strengthens the argument that there should be no civil penalties or damages for conduct that has not previously been found to breach the new section 46. Other remedies such as injunctions and declarations would be available for all conduct.

[2] See Katharine Kemp, "Submission to the Competition Policy Review – The South African Example: A Legislated Effects-Based Test and Efficiency Defence for Misuse of Market Power", 29 May 2014.

Monitoring and review

In the absence of a full regulation impact statement (RIS), the government should commit to a post-implementation review within two years of the commencement of the provision. This would apply the government's rule for any regulatory change that is exempt from a RIS.

The explanatory memorandum says that a RIS is not required because "the independent Harper Review constituted a process and analysis equivalent to a Regulation impact statement".

It is difficult to accept that the Harper Review is equivalent to a proper RIS process. The Harper Review panel conceded there would be costs and risks associated with its proposal, but it failed to identify any pro-competitive or pro-consumer benefits.

The post-implementation review should assess post-implementation costs and benefits of the changes, including the impacts on innovation and pricing activity. The review should test whether actual compliance costs for business are consistent with the estimate in the RIS of $2.5 million a year, or $25 million over 10 years.

To support the post-implementation review the ACCC should be directed to report every six months on complaints and investigations and the application of its new authorisation process under any new provision.

The ACCC's authorisation process should include a fast-track process for conduct that, based on the ACCC guidelines, is not conduct that the legislation is intended to capture.

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IN THE MATTER OF THE FINAL REPORT OF THE COMPETITION POLICY REVIEW (HARPER REVIEW) AND THE RECOMMENDED FORM OF AN AMENDED S 46

OPINION

1. Recommendation 30 of the final report of the Competition Policy Review (**Harper Review**) published in March 2015 states:

> 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.

2. The Harper Review recommended that sub-sections (1) and (2) as set out below should be substituted for the existing s 46(1) of the *Competition and Consumer Act* 2010 (Cth) (**CCA**):

> (1) A corporation that has a substantial degree of power in a market shall not engage in conduct if the conduct has the purpose, or would have or be likely to have the effect, of substantially lessening competition in that or any other market.

(2) Without limiting the matters that may be taken into account for the purposes of subsection (1), in determining whether conduct has the purpose, or would have or be likely to have the effect, of substantially lessening competition in a market, the court must have regard to:

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

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

3. The Harper Review also recommended the retention of existing sub-sections (3), (3)(A), (3)(B), (3)(C), (3)(D) and (4) which expand on the concept of market power. Those provisions remain relevant, but they are to be re-numbered as sub-sections (3)-(8) of the recommended form of s 46.

4. The other sub-sections of the existing s 46(1) are to be deleted as they relate to abandoned aspects of the former sub-section (1), such as the concept of "taking advantage".

5. The Federal Government has announced that it proposes to implement recommendation 30. There is, however, a prospect that the Government may entertain submissions concerning the wording of the new section, and perhaps particularly the wording of sub-section (2) as recommended by the Harper Review.

6. On the assumption that the existing s 46 will be replaced by an "effects test" substantially in the form of sub-section (1) as recommended by the Harper Review, I have been asked to provide an opinion examining the strengths, weaknesses and problems of the proposed drafting of sub-sections (1) and (2) and canvassing ways of improving the draft.

Purpose of the recommended amendments

7. A useful starting point is to identify the purposes of the recommended amendments, as explained by the Harper Committee.

8. The Harper Committee cited three main reasons for substituting a so-called "effects test" for the current provision that focuses on a misuse of market power for anti-competitive purposes. Those reasons were:

   (a) the sole focus on purpose in the existing s 46 does not usefully distinguish pro-competitive from anti-competitive conduct, and it is inconsistent with the overriding policy objective of the CCA to protect competition, and not individual competitors;[1]

   (b) the sole focus on purpose in the existing s 46 is out of step with international approaches;[2] and

   (c) in contrast, a test that is expressed in terms of the purpose, or effect or likely effect, of substantially lessening competition is consistent with other prohibitions in the CCA and it would have the advantage of allowing the Court to weigh the pro-competitive and anti-competitive impact of the conduct in question.[3]

9. The Harper Committee expanded on the dichotomy it perceived between an approach that focused on purpose and one that focused on effects by describing the rival arguments in the following terms:[4]

> Those seeking reform of the law most commonly propose that the prohibition should be revised or expanded to include an 'effects' test – that is, a firm with substantial market power would be prohibited from taking advantage of that power if the effect is to cause anti-competitive harm. Two main arguments are advanced for the inclusion of an effects test:
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> - As a matter of policy, competition law ought to be directed to the effect of commercial conduct on competition, not the purpose of the

[1] Harper Review at 9, 61 and 339.
[2] Harper Review at 9, 340 and Appendix B.
[3] Harper Review at 9, 61 and 340-341.
[4] Harper Review at 335.

conduct, because it is the anti-competitive effect of conduct that harms consumer welfare.

- As a matter of practicality, proving the purpose of commercial conduct is difficult because it involves a subjective enquiry, whereas, proving anti-competitive effect is less difficult because it involves an objective enquiry.

Those opposing reform are concerned that introducing an effects test would 'chill' competitive behaviour by firms in the market, which would be harmful to consumer welfare.

The debate around whether section 46 should be based solely on a 'purpose' test or should also (or alternatively) have an 'effects' test is one of the enduring controversies of competition policy in Australia.

10. It is worth pausing to consider the reasons advanced by the Harper Committee for their recommended changes to s 46, and the weak points of that reasoning. That discussion will be assisted if I discuss the elimination of the "take advantage" requirement from s 46(1), and then turn to the Harper Committee's reasons for substituting an effects test (starting with the second reason advanced by the Harper Committee – the international comparators).

Eliminating the "take advantage" requirement

11. The central purpose of the recommended amendments is to address difficulties that have attended the current form of s 46. Those difficulties arise from the requirement that conduct falling within s 46 must "take advantage" of the corporation's substantial market power.

12. In the opinion of the Harper Committee, the words "take advantage" pose a test that is not sufficiently clear and predictable in interpretation and application to distinguish between anti-competitive and pro-competitive conduct. Further, the Harper Committee considered that the test had given rise to substantial difficulties of interpretation, as revealed in decided cases such as *Queensland Wire Industries v BHP* (1989) 167 CLR 177, *Melway Publishing Pty Ltd v Robert Hicks Pty Ltd* (2001) 205 CLR 1, *Boral Besser Masonry Ltd v ACCC* (2003) 215 CLR 374, and *Rural Press Limited v ACCC* (2003) 216

CLR 53; and that those cases have had the effect of undermining confidence in the effectiveness of the law.[5] The Harper Committee also noted that these problems have not been overcome by the introduction of sub-section (6A) in 2008.[6]

13. It is correct, but perhaps surprising, that Australian courts have struggled with the proper interpretation and application of s 46. In other jurisdictions, courts have not experienced any particular difficulties in applying provisions that are couched in language such as "abuse ... of a dominant position" and "abusing" a position of substantial market power or a dominant position. The root of the problem in Australia may lie in the fact that the courts have departed from the ordinary meaning of the words "take advantage". As the Harper Committee pointed out, the ordinary meaning of those words is simply to use to one's advantage. On their face, the words would seem to mandate a factual inquiry into the genesis, circumstances, purpose and effects of the conduct in question. Instead of taking this course, the courts have been influenced by unhelpful economic notions, particularly what the Harper Committee describes as the supposed "economic premise" of the test that a firm with substantial market power should be permitted to engage in particular business conduct if firms without market power could also engage in that conduct.[7] The Harper Committee goes on to point out that this is a dubious premise because particular conduct might be competitively benign when undertaken by a firm without market power but competitively harmful when a firm has market power.

14. In my view, the supposed economic premise of the expression "take advantage" has led the courts to embark on a difficult and often arid inquiry into whether the same conduct could have been undertaken by a corporation that lacked substantial market power. Such an inquiry is unlikely to produce any useful answers. The perceived difficulties of the provision would surely have been less if Australian courts had applied the provision in accordance

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[5] Harper Review at 337-338.
[6] Harper Review, at 338.
[7] Harper Review at 338.

with the ordinary meaning of the language it used, so as to mandate an inquiry into the origins and circumstances of the conduct, and the effects that the corporation with substantial market power sought to achieve, or in fact achieved, by engaging in that conduct.

15. For the foregoing reasons, there is some justification for the elimination of the "taking advantage" test, as recommended by the Harper Committee, and the insertion of an effects test into s 46, so long as the new provision links purpose and effects in a way that has the practical result that the section is confined to conduct that amounts to an abuse of substantial market power. But, as discussed below, there are shortcomings in the way in which the Harper Committee seeks to substitute a so-called effects test for the current provision, which mean that the recommended section overreaches its proper role.

Overseas comparisons

16. Contrary to the view expressed by the Harper Committee,[8] the existing s 46 is very much a mainstream provision when compared to its international analogues. It is the form of s 46 proposed by the Harper Committee which is the outlier. Let me give a few examples.

17. In relation to Canada, the Harper Committee argues that the existing s 46 is inconsistent with s 79 of the Canadian Competition Act which it says "prohibits anti-competitive conduct by a dominant firm that has the effect or likely effect of substantially lessening competition".[9] This description of the Canadian Act is incomplete because it omits to mention that s 78(1) describes an anti-competitive act in purposive terms. It provides:

> 78(1) For the purposes of section 79, "anti-competitive act", without restricting the generality of the term, includes any of the following acts:
>
> (a) squeezing, by a vertically integrated supplier, of the margin available to an unintegrated customer who competes with the supplier, for the purpose of impeding or preventing the customer's entry into, or expansion in, a market;

[8] Harper Review at 9 and 340.
[9] Harper Review at 340.

(b) acquisition by a supplier of a customer who would otherwise be available to a competitor of the supplier, or acquisition by a customer of a supplier who would otherwise be available to a competitor of the customer, for the purpose of impeding or preventing the competitor's entry into, or eliminating the competitor from, a market;

(c) freight equalization on the plant of a competitor for the purpose of impeding or preventing the competitor's entry into, or eliminating the competitor from, a market;

(d) use of fighting brands introduced selectively on a temporary basis to discipline or eliminate a competitor;

(e) pre-emption of scarce facilities or resources required by a competitor for the operation of a business, with the object of withholding the facilities or resources from a market;

(f) buying up of products to prevent the erosion of existing price levels;

(g) adoption of product specifications that are incompatible with products produced by any other person and are designed to prevent his entry into, or to eliminate him from, a market;

(h) requiring or inducing a supplier to sell only or primarily to certain customers, or to refrain from selling to a competitor, with the object of preventing a competitor's entry into, or expansion in, a market; and

(i) selling articles at a price lower than the acquisition cost for the purpose of disciplining or eliminating a competitor.

18. Building upon s 78(1), s 79(1) provides:

> 79(1) Where, on application by the Commissioner, the Tribunal finds that
>
> (a) one or more persons substantially or completely control, throughout Canada or any area thereof, a class or species of business,

(b) that person or those persons have engaged in or are engaging in a practice of anti-competitive acts, and

(c) the practice has had, is having or is likely to have the effect of preventing or lessening competition substantially in a market,

the Tribunal may make an order prohibiting all or any of those persons from engaging in that practice.

19. Additionally, s 79(4) provides:

(4) In determining, for the purposes of subsection (1), whether a practice has had, is having or is likely to have the effect of preventing or lessening competition substantially in a market, the Tribunal shall consider whether the practice is a result of superior competitive performance.

20. The Enforcement Guidelines published by the Canada Competition Bureau state:[10]

> Section 78 of the Act enumerates a non-exhaustive list of acts that are deemed to be anti-competitive in applying section 79. The Federal Court of Appeal has stated that an anti-competitive act is defined by reference to its purpose, and the requisite anti-competitive purpose is an intended negative effect on a competitor that is predatory, exclusionary, or disciplinary.[11] However, the Federal Court of Appeal and Tribunal have acknowledged that paragraph 78(1)(f) is an exception to this standard in that it does not contain a reference to a purpose vis-à-vis a competitor. In any event, while many types of anti-competitive conduct may be intended to harm competitors, the Bureau considers that certain acts not specifically directed at competitors could still be considered to have an anti-competitive purpose.
>
> When assessing whether an act is anti-competitive, the purpose of an act may be proven directly by evidence of subjective intent, or inferred from the reasonably foreseeable consequences of the conduct. Although verbal or written statements of a firm's personnel may assist in

[10] At 10. Where the Guidelines describe s 78(1)(f) as not referring to a purpose vis a vis a competitor the emphasis is on the last words describing the target. The provision is still purposive in the wider sense that it describes a purpose of maintaining prices above a competitive level

[11] *Canada (Commissioner of Competition) v Canada Pipe Co* 2006 FCA 233 at para. 66.

> establishing subjective intent, evidence of subjective intent is neither strictly necessary nor completely determinative.[12] In most cases, the purpose of the act can be inferred from the circumstances, and persons are assumed to intend the reasonably foreseeable consequences of their acts.[13]
>
> An additional factor in the determination of whether an act is anti-competitive is whether it was in furtherance of a legitimate business objective. A business justification is not a defence to an allegation that a firm has engaged in anti-competitive conduct, but rather an alternative explanation for the overriding purpose of that conduct, if and as required, that a firm can put forward where the Bureau believes that purpose to be anti-competitive.

21. The Guidelines go on to observe that s 78 describes various means by which a firm may engage in exclusionary conduct which is designed to make current and/or potential rivals less effective at disciplining the exercise of a firm's market power, to prevent them from entering the market, or to eliminate them from the market entirely.

22. Further, it is noteworthy that s 79 requires both an anti-competitive act that is identifiable by its anti-competitive, exclusionary or predatory purpose, and a demonstrated effect on competition. It is not sufficient in Canada that a particular practice has, or is likely to have, an adverse effect on competition.

23. In relation to the U.S., the Harper Committee said[14] that the prohibition on monopolisation or attempted monopolisation in s 2 of the Sherman Act depends on objective, not subjective, intent, which can be inferred from conduct and effect. This marks only a marginal difference from the existing s 46. Its purposive requirement has been described as stipulating for an operative subjective purpose, but the existence of that purpose is commonly, indeed ordinarily, inferred from conduct and effect. Moreover, it is not

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[12] *Ibid.* at para. 72-73.
[13] *Canada (Director of Investigation and Research, Competition Act) v. NutraSweet Co.* (1990), 32 C.P.R. (3d) 1 (Comp. Trib.), at 35.
[14] Harper Review at 340.

conclusively established simply because individuals give evidence of their subjective intentions.[15]

24. The more important difference is that the concepts of monopolisation and attempted monopolisation in s 2 of the Sherman Act require proof of conduct that amounts to a wilful acquisition or maintenance of such power so as to cause anti-trust injury. In effect, U.S. jurisprudence requires that monopoly power must be obtained or maintained by anti-competitive, exclusionary or predatory means, as distinct from its growth or development as a consequence of superior product, business acumen or historic accident.[16] This is a far cry from the form of s 46 proposed by the Harper Committee where a contravention can be established simply by pointing to an effect or likely effect of substantially lessening competition and without any need to prove a link between the possession of substantial market power and the assessed substantial lessening of competition.

25. In relation to the European Union, Article 102 of the TFEU states:

> Any abuse by one or more undertakings of a dominant position within the internal market or in a substantial part of it shall be prohibited as incompatible with the internal market in so far as it may affect trade between Member States.
>
> Such abuse may, in particular, consist in:
>
> (a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions;
>
> (b) limiting production, markets or technical development to the prejudice of consumers;

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[15] *Universal Music Australia Pty Ltd v ACCC* (2003) 131 FCR 529 at [256]; and *ASX Operations Pty Ltd v Pont Data Australia Pty Ltd* (1990) 27 FCR 460 at 482-3.

[16] *National Ass'n of Pharmaceutical Mfrs., Inc. v Ayerst Laboratories, Div. of/and American Home Products Corp.*, C.A.2 (N.Y.) 1988; *Shavrnoch v Clark Oil and Refining Corp.*, C.A.6 (Mich.) 1984, 726 F.2d 291; *Hunt-Wesson Foods, Inc. v Ragu Foods, Inc.*, C.A.9 (Cal.) 198, 627 F.2d 919, certiorari denied 101 S.Ct. 1369, 450 U.S. 921, 67 L.Ed.2d 348.; *Commercial Data Servers, Inc. v International Business Machines Corp.*, S.D.N.Y. 2003, 262 F.Supp.2d 50; *Picker Intern., Inc. v Leavitt*, D.Mass. 1994, 865 F.Supp. 951; *Marnell v United Parcel Service of America, Inc.*, N.D.Cal. 1966, 260 F.Supp. 391.

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

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

26. In its Final Report,[17] the Harper Committee said that because Article 102 is framed in terms of an "abuse ... of a dominant position", this allows regard to be had to matters such as the adverse effects of the conduct on competition. But neither the terms of Article 102, nor the European jurisprudence that applies it, can be assimilated to an effects test, contrary to what the Harper Committee asserts in Appendix B. Most importantly, the key feature of Article 102 is that the conduct in question must constitute an abuse of market power deriving from a dominant position. A substantially similar requirement lies at the core of the existing s 46 (albeit a lower threshold of substantial market power applies), but the Harper Committee's proposed amendments would remove it.

27. In its submissions to the Commonwealth Department of Treasury in February 2016 in relation to the amendment of s 46, the Business Council of Australia (**BCA**) referred to equivalent laws in many other jurisdictions. From the BCA's summary, it is plain that most countries have an abuse of market power provision that is broadly similar to the existing s 46. Countries in this category include Hong Kong, Singapore, Malaysia, Indonesia, China, South Korea, India and South Africa. The evidence seems to be overwhelming that the form of s 46 proposed by the Harper Committee is an extreme outlier.

Sole purpose

28. The Harper Committee's first reason for its recommendation depends on a flawed characterisation of s 46(1). While a proscribed purpose is one essential element of the provision, the other essential elements are equally important as

[17] At 340 and in Appendix B.

they demand proof of a causal link between the possession of substantial market power and conduct or practices that use or rely upon that market power for a proscribed purpose. The Harper Committee is also mistaken in suggesting that the proscribed purposes in s 46(1) are confined to a purpose of inflicting damage on individual competitors. That describes s 46(1)(a) but sub-sections (1)(a) and (b) refer, respectively, to purposes of preventing market entry and deterring or preventing a person from engaging in competitive conduct. Given the range of purposes it proscribes and the other necessary elements it contains, the existing s 46 is squarely aimed at misuses of market power.

29. There is also a flavour to the Harper Committee's comments that objective circumstances and anti-competitive effects are irrelevant to the application of the current s 46. That is not the case. In s 46, "purpose" refers to an intention to achieve a particular end, result or market effect. The relevant purpose need not be the only purpose, provided it is a substantial purpose: s 4F. As to proof of that purpose, it can be established by direct evidence or inference from all the circumstances, including the effect of the conduct on competition. The latter situation tends to represent the norm; in other words purpose will usually be inferred by the courts from all the circumstances, including in particular the nature of the conduct, the circumstances in which it occurred, and its likely effect on competitors and competition. Statements from individuals in the witness box as to their intentions or purpose will be tested closely and are treated with the utmost caution.[18] This approach of inferring purpose from all the circumstances is virtually indistinguishable from that adopted in Canada, as summarised in the enforcement guidelines published by the Competition Bureau of Canada.

The advantages of an effects test

30. The Harper Committee placed great weight on the fact that the current s 46(1) does not explicitly refer to anti-competitive effects. Although, as discussed

[18] *ASX Operations Pty Ltd v Pont Data Australia Pty Ltd (No 1)* (1990) 27 FCR 460; *Taprobane Tours Pty Ltd v Singapore Airlines Ltd* (1990) 96 ALR 405.

above, the effects of the conduct on competition are relevant in applying the current s 46, there is no requirement in the provision, as there is in the corresponding Canadian provision, articulating a specific requirement that the conduct have, or be likely to have, the effect of substantially lessening competition. If there were such a requirement, it would ensure that the Court weighs the pro-competitive and anti-competitive effects of the conduct in determining whether there had been a misuse of market power. Accordingly, there is in my view merit in adding a requirement that there must be an effect or likely effect of substantially lessening competition.

31. The Harper Committee's recommended provision does not secure such an outcome because it treats purpose and effect as alternative ways of establishing a contravention.

32. The fact that the recommended form of s 46 poses alternative requirements for purpose or effect, rather than cumulative requirements, is of particular significance, given the fact that the proposed s 46 contains no necessary link between the possession of substantial market power and the conduct that is alleged to have a purpose, effect or likely effect of substantially lessening competition in a market. This is brought home by the closing words of the proposed s 46(1). They have the effect that a corporation can contravene s 46(1) by engaging in conduct that has the purpose, effect or likely effect of substantially lessening competition in a second market, even though its own substantial power resides in a first market; and there is no need to show that the conduct in the second market amounted to a use of the substantial market power held in the first market. In contrast, the concluding words of s 46(1) are apposite in the current provision because there is a requirement that the conduct affecting the second market must amount to a taking advantage of substantial market power in the first market.

33. As for the proposition that the substitution of the substantial lessening of competition test will bring s 46 into line with provisions such as ss 45, 47 and 50, there is an important difference between s 46 and these other provisions. Section 46 is aimed at unilateral conduct by corporations possessing

substantial market power, whereas the other provisions are triggered when two or more corporations enter into a contract, arrangement or understanding, or where the conduct relates to a supply relationship that attracts the exclusive dealing provision in s 47, or where two or more corporations come together and agree to acquire or dispose of shares or assets in a manner that is caught by s 50. Hitherto, the premise of the *Consumer and Competition Act* has been that there is no need, and there are dangers, in applying a substantial lessening of competition test to unilateral business decisions.

Retaining elements of s 46(1) – Substantial market power

34. The recommended provision retains the threshold test of "a substantial degree of market power" because the Harper Committee regarded it as appropriate and well understood.[19] It therefore remains the gateway to s 46 in the sense that it defines the class of corporations to whom the provision applies, but the proposed section requires no other nexus between the possession of a substantial degree of market power and the remaining elements of s 46(1). Specifically, there is no requirement in the new section that such power must be used in a way that is intended to bring about, or which is likely to bring about, a substantial lessening of competition. Nor is there any requirement that the possession of a substantial degree of market power must be connected with the corporation engaging in conduct that has the purpose, or effect or likely effect of substantially lessening competition.

35. When s 46 was initially enacted, it contained a more stringent threshold requirement that meant it only applied to corporations that had a dominant position in a market. The provision was re-drafted in 1986 so that the threshold was reduced to a substantial degree of market power. This occurred because of a concern that s 46 might only apply to corporations that held monopoly power or something akin to monopoly power.[20] It was further relaxed in 2007 and 2008 when sub-sections (3), (3A), (3B), (3C) and (3D) were added or amended to ensure that the phrase "a substantial degree of

[19] Harper Review at 61.
[20] *ACCC v Baxter Health Care Pty Ltd (No 2)* (2008) 170 FCR 16 at [378].

market power" was not construed too restrictively. For instance, sub-section (3C) provides that a body corporate may have a substantial degree of power in a market even though it does not substantially control the market or does not have absolute freedom from constraint by the conduct of competitors, or potential competitors or its suppliers or acquirers. Similarly sub-section (3D) provided that more than one corporation may have a substantial degree of power in a market.

36. The requirement for a substantial degree of market power is not an exacting one. The word "substantial" is a relative term and can have a range of meanings. In the context of s 46, it has been interpreted as referring to a degree of market power that is real, or of substance, or considerable, rather than trivial or minimal.[21] Thus, a substantial degree of market power is power that is, to an extent that warrants the description substantial, not constrained by competitors, potential competitors, suppliers or acquirers. Plainly, it can extend to companies whose degree of market power falls well short of monopoly power or a dominant level of market power.

37. What this background shows is that it was one thing to progressively relax the threshold of a substantial degree of market power in s 46 when the section was aimed at a taking advantage of market power for proscribed anti-competitive purposes. However, it is another thing to adopt the same threshold in a revised provision that is no longer aimed at the abuse of market power, and which will apply a substantial lessening of competition test to any conduct engaged by a corporation that happens to have a substantial degree of power in a market.

38. A very large number of companies in Australia will fall within the reach of the new s 46. This is so because, in the Australian economy, the class of corporations that have a substantial degree of power in the market or markets in which they operate is a very wide one. In fact, many Australian markets are so concentrated that all of the major players (which will often amount to less than, say, six or so) will have a degree of market power that qualifies as

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[21] *Dowling v Dalgetty Australia Limited* (1992) 34 FCR 109; *Eastern Express Pty Ltd v General Newspapers Pty Ltd* (1991) 30 FCR 385; and *Mark Lyons Pty Ltd v Bursill Sports Gear Pty Ltd* (1987) 75 ALR 581.

substantial. The consequence is that, for the first time, many ordinary business decisions by those corporations will potentially fall within the reach of the new s 46.

Introducing a Test of Substantial lessening competition

39. The Harper Committee considers that it is a significant advantage if the new s 46 adopts the same test of substantially lessening competition that is found in other provisions in Part IV of the Act. Accordingly the ingredients of that test warrant close examination.[22]

Substantial

40. It is fair to say that the judicial interpretation of the word "substantial" within the phrase "substantially lessening competition" has undergone an evolutionary process. The result of that process is that the meaning of the word substantial in the phrase "substantially lessening competition" differs significantly from the way in which the same phrase has been construed in the opening words of the existing s 46.

41. The earlier cases treated the word "substantial" as a primarily quantitative expression. Hence, substantial was construed as meaning "more than trivial or minimal", perhaps "considerably", and as importing "a greater rather than a lesser degree of lessening".[23]

42. Later cases, however, have placed greater emphasis on a qualitative assessment of the state of competition, compared to the future state of the market with and without the impugned conduct. The formula that the courts now commonly use to capture the qualitative dimension of the test is that the impact of the conduct must be "meaningful or relevant to the competitive

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[22] Those ingredients have been examined, very helpfully, in a recent article by Peter Armitage, "The Evolution of the 'Substantial lessening of competition' test – a review of case law", (2016) 44 ABLR 74.

[23] See, e.g., *Dandy Power Equipment Pty Ltd v Mercury Marine Pty Ltd* (1982) 64 FLR 238 at 260; *Singapore Airlines Pty Ltd v Taprobane Tours WA Pty Ltd* (1991) 33 FCR 158, 181; *Universal Music Australia Pty Ltd v ACCC* (2003) 131 FCR 529, [241]; and *Radio 2UE Sydney Pty Ltd v Stereo FM Pty Ltd* (1982) 62 FLR 437, 445.

process" to qualify as a substantial lessening of competition.[24] This formula springs from the decision of French J in *Stirling Harbour* and it was applied by French J in the *Australian Gas Light Co* case.[25] It received qualified approval from the High Court in *Rural Press v ACCC*[26] where the High Court used the formula while observing that it was unnecessary to reach a view with respect to the inconclusive debate about the proper construction of substantial. The High Court clearly accepted the qualitative dimension of the test for substantially lessening competition because it went on to say that the authorities "do not support the proposition that it would be sufficient for liability if the relevant effect was quantitatively more than insignificant or not insubstantial".[27]

43. The High Court's decision in *Rural Press* effectively endorsed the Full Court's view that a competitive impact may be substantial where it nips competition "in the bud". The High Court also described the entrant who was deterred as "a small but potentially significant competitor" that would have diluted the impact of the existing monopoly.[28] Both these matters suggest a qualitative assessment that does not always require a large impact on competition.[29]

44. In *Australian Gas Light Co*,[30] French J applied the meaningful or relevant test and in doing so he endorsed the observation by the Full Federal Court in *Universal*[31] that the lessening must be sufficiently serious to adversely affect the process of competition and that this would exclude a short term effect which would be readily corrected by market processes.

45. It would be going too far, however, to conclude that the test is purely qualitative. My own assessment of these cases corresponds to that expressed

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[24] See *Stirling Harbour Services Pty Ltd v Bunbury Port Authority* [2000] ATPR 41-752 at [113]; *Australian Gas Light Co v ACCC (No 3)* (2003) 137 FCR 317 at [351]; and *Rural Press Ltd v ACCC* (2003) 216 CLR 53 at 41.
[25] Supra.
[26] (2003) 216 CLR 53 (***Rural Press***).
[27] *Rural Press* at [41].
[28] *Rural Press* at [46].
[29] *Rural Pres Ltd v ACCC* (2002) 188 FCR 236 at [129]; and *Rural Press Ltd v ACCC* (2003) 216 CLR 53 at 46.
[30] (2003) 137 FCR 316.
[31] *Universal Music Australia Pty Ltd v ACCC* (2003) 131 FC.R at [242].

by Allsop J in *ACCC v Liquorland (Aust) Pty Ltd*[32] where his Honour said that "there is a layer of meaning of "considerable" to be added to the notion of being meaningful or relevant to the competitive process".

Likely

46. In most legal context, the word "likely" connotes a factual outcome that the Court assesses to be more probable than not. But that is not the meaning that the word bears in the context of a likely substantial lessening of competition. Rather, the courts have construed the word "likely" in that context as requiring only that there must be "a real chance" that the conduct, practice or acquisition in question will result in a substantial lessening of competition.[33]

47. In *Australian Gas Light Co v ACCC*, French J expanded on the meaning of the word "likely" in s 50:

> The meaning of "likely" reflecting a "real chance or possibility" does not encompass a mere possibility. The word can offer no quantitative guidance but requires a qualitative judgment about the effects of an acquisition or proposed acquisition. The judgment it requires must not set the bar so high as effectively to expose acquiring corporations to a finding of contravention simply on the basis of possibilities, however plausible they may seem, generated by economic theory alone. On the other hand it must not set the bar so low as effectively to allow all acquisitions to proceed save those with the most obvious, direct and dramatic effects upon competition. By the language it adopts and the function thereby cast upon the Court and the regulator in their consideration of acquisitions s 50 gives effect to a kind of competition risk management policy. The application of that policy, reflected in judgments about the application of the section, must operate in the real world. The assessment of the risk or real chance of a substantial lessening of competition cannot rest upon speculation or theory. To borrow the words of the Tribunal in the Howard Smith case, the Court is concerned with "commercial likelihoods relevant to the proposed

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[32] [2006] FCA 826 at [829]
[33] See, e.g., *ACCC v Metcash Trading Ltd* [2011] FCA 967 at [146]; and *Australian Gas Light Co v ACCC (No 3)* (2003) 137 FCR 317 at [320]-[348].

> merger". The word "likely" has to be at a level which is commercially relevant or meaningful as must be the assessment of the substantial lessening of competition under consideration.[34]

His Honour also said that this approach applies across Part IV whenever there is a reference to a likely substantial lessening of competition.[35]

Framework for assessing a substantial lessening of competition

48. It is now well established by judicial decisions under Part IV that the question whether conduct has the effect or likely effect of substantially lessening competition must be assessed by considering the future state of the market with and without the impugned conduct.[36]

49. This counter factual analysis does not exclude reference to the present state of competition to illuminate the future state of the market, but it does mean that it would be an error to confine attention to the present state of the market. It is also clear that the future counter factual cannot be a purely hypothetical one. In *Metcash*, Emmett J held at trial that the ACCC must demonstrate that, absent the acquisition, it was more probable than not that the counter factual situation would occur.[37] On appeal, Buchanan J agreed with this aspect of the trial decision, but the other two appellate Judges (Yates and Finn JJ) treated the counter factual as merely an aid to detect the existence and extent of changes in the process of competition.[38]

50. Next, there is the question of what categories of evidence or market factors are likely to assume importance in applying the counter factual analysis. This is another area where the views of the courts and the Australian Competition Tribunal have undergone something of an evolution. The classical starting point has been the list of structural factors that Professor Maureen Brunt

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[34] *Australian Gas Light Company v Australian Competition and Consumer Commission* (2003) 137 FCR 31 AAT [348]
[35] *Australian Gas Light Co v ACCC (No 3)* (2003) 137 FCR 317 at 347
[36] *Stirling Harbour Services Pty Ltd v Bunbury Port Authority* [2000] ATPR 41-752 at [113]; Australian Gas Light Co v ACCC (No 3) at [352]; and ACCC v Metcash Trading Ltd (2011) 198 FCR 297 at [148]; and *Re Chime Communications Pty Ltd (No 2)* (2009) 234 FLR 210 at [14] (a decision of the Australian Competition Tribunal).
[37] *ACCC v Metcash Trading Ltd* (2011) FCA 967 at [146].
[38] *ACCC v Metcash Trading Ltd* [2011] 198 FCR 297 at [90] per Buchanan J and [228] and [230] per Yates and Finn JJ.

identified in *QCMA*. Those factors included the height of barriers to entry, the level of market concentration, the character of vertical relationships (which would capture any countervailing power held by customers and suppliers, and the nature and extent of vertical integration) and the dynamic characteristics of the market. A number of those factors are replicated in s 50(3). It follows that those factors are relevant throughout s 46 wherever the substantial lessening test is used.[39]

51. It has often been said that the most important of these factors is the height of barriers to entry.[40]

52. However, recent Tribunal cases have laid much greater emphasis on behavioural rather than structural factors when applying the substantial lessening of competition test.[41]

53. Although the courts have not gone as far as the Competition Tribunal, in *Boral Besser Masonry Ltd v ACCC* (2001) 106 FCR 328 at [225] and [341]-[342] both Merkel and Finkelstein JJ took strategic, and not just structural, barriers to entry into account. On appeal to the High Court, only McHugh J endorsed this approach.[42]

54. The shift towards behavioural factors may have particular bearing on the question whether a substantial lessening of competition can be discerned from the fact that the conduct has led, or is likely to lead, to the exit of one or more competitors. In *Chime*, the Tribunal said that the level of competition cannot be measured simply by the number of firms in the market, their market shares and the market concentration. In *Re Telstra Corporation (No 3)* the Tribunal said that it was important not to confuse the objective of promoting

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[39] Armitage, supra, at 92.
[40] See, e.g., *Queensland Wire Industries Pty Ltd v Broken Hill Pty Co Ltd* (1989) 167 CLR 177; and *Melway Publishing Pty Ltd v Robert Hicks Pty Ltd* (2001) 205 CLR 1 at [67].
[41] See *Re Qantas Airways Ltd* [2004] AComp.T 9 at [304], [400], [420] and [438]; *Re Chime Communications Pty Ltd (No 2)* (2009) 234 FLR 210 at [29], [48] and [53]; *In the Matter of Fortescue Metals Group* [2010] AComp.T 2 at [1050] – [1051]; and *Re AGL Energy Ltd* [2014] AComp.T 1 at [369]
[42] *Boral Besser Masonry Ltd v ACCC* (2003) 215 CLR at [295] and [313]; see also Greenwood J in *ACCC v Cement Australia Pty Ltd* [2013] FCA 909 at [980].

competition with the outcome of ensuring the greatest number of competitors.[43]

55. In his text, Heydon observes that the exit of many small firms may not affect the quality of the competition process because it may leave the market as competitive as previously.[44]

56. Notwithstanding these authorities, there are cases where the impact of conduct on a particular competitor proved decisive in applying the substantial lessening test. *Rural Press* was one such case. Other cases of that kind include *Mark Lyons*, and *O'Brien Glass*. In *Boral*, McHugh J drew attention to the signaling effects of conduct on particular competitors or potential entrants into the market.[45] In a similar fashion, Hill J in *Universal Music Australia Pty Ltd v ACCC* (2003) 131 FCR 529 drew attention to the impact of exclusive dealing conduct on other retailers.[46]

57. Practitioners commonly experience situations where the ACCC expresses the view in the course of its merger clearance process that a reduction in the number of corporations from say, four to three, is highly likely to have the effect of substantially lessening completion. The explanation may be that the ACCC considers that the acquisition falls within the scope of s 50(3)(h) and would result in the removal of a vigorous and effective competitor.[47] But of course, even very small competitors might satisfy this description if the market is defined very narrowly in product and geographic terms.

58. One question that arises in the context of the proposed new s 46 is whether its incorporation of a substantial lessening of competition test creates uncertainty as to whether s 46 might apply to conduct by a corporation holding substantial market power where that conduct results in the exit of competitors from the market. It may be, for instance, that competitors in a narrowly defined regional market cannot match it with a more powerful corporation that enters

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[43] *Re Telstra Corporation (No 3)* [2007] AComp.T 3 at [98]-[99]; see also the explanatory memorandum relating to the introduction of s 50(3) at page 6 in 1992.
[44] Heydon, Trade Practices Law, at s 30.230.
[45] *Boral*, supra, 215 CLR 374 at [313].
[46] *ACCC v Universal Music Australia Pty Ltd* (2001) 115 FCR 442 at [464]-[465]; and in the Full Court, 131 FCR 529 at [243]-[244].
[47] See the ACCC Merger Guidelines at 49.

the regional market because of its size and economies of scale. It would be an odd result if those facts alone were enough to expose such a corporation to the risk of contravening s 46 in its revised form. Yet the ACCC's approach to merger cases affords little confidence that such situations will be treated as falling outside the reach of the proposed s 46.

59. In conclusion, the message that emerges from this brief review of the authorities is that many uncertainties attend the application of the substantial lessening of competition test. Moreover, its application is fact intensive and usually time consuming. This is evident in the fact that the ACCC analysis of the test in the context of merger cases normally takes many months to complete and may involve narrow market definitions which tend to magnify the consequences of the impugned conduct. The application of such a test to conduct engaged in by every corporation that falls within the wide reach of the new s 46 is likely to be very disruptive to business.

60. In its February 2016 submission to the Treasury in relation to the proposed revision of s 46, the BCA made the following submissions:

> The Business Council has argued against applying the SLC test to unilateral behaviour in section 46. The SLC test is difficult and expensive to apply and does not provide a clear guide to business about the likely effects of its actions.
>
> Market definition, in particular, is frequently contested, and there is concern about the tendency of the ACCC to define markets narrowly and in some cases artificially, which risks capturing more, rather than less, business conduct.
>
> The risks, time and costs associated with the ACCC's application of the SLC test, which can take many months, many experts and millions of dollars to contest, is itself a significant deterrent to competitive behaviour.
>
> In addition, to manage regulatory compliance and risk management, firms will need to start conducting their own internal SLC tests when innovating. These will need to be consistent with court interpretations of what constitutes a substantial lessening of competition.

61. In my view, the uncertainties and vagueness of the substantial lessening of competition test, as explained in the authorities, lends support to the BCA's submissions.

Over-capture

62. The Harper Committee acknowledged in its Final Report that its proposed s 46 posed a significant risk of over-capture.[48]

63. The Committee initially proposed a defence providing that the prohibition in s 46 would not apply if the conduct in question would be both a rational business decision by a corporation that did not have a substantial degree of power in the market, and likely to have the effect of advancing the long term interests of consumers. It is unclear why these conditions were expressed cumulatively rather than in the alternative.[49] Be that as it may, in its Final Report, the Harper Committee said that the risk of inadvertently capturing pro-competitive conduct in the re-drafting of the provision was better addressed by a further sub-section to the following effect:

> 46(2) Without limiting the matters that may be taken into account for the purposes of subsection (1), in determining whether conduct has the purpose, or would have or be likely to have the effect, of substantially lessening competition in a market, the court must have regard to:
>
> (a) the extent to which the conduct has the purpose, or would have or be likely to have the effect, of increasing competition in the market including by enhancing efficiency, innovation, product quality or price competitiveness in the market; and
>
> (b) the extent to which the conduct has the purpose, or would have or be likely to have the effect, of lessening competition in the market including by preventing, restricting or deterring the potential for competitive conduct in the market or new entry into the market.

[48] Harper Review at 61 and 342-345.
[49] Harper Review at 342.

64. Compared to the originally proposed defence, this safeguard does not contain any carve out for conduct that reflects a rational business decision by a corporation that did not have a substantial degree of power in the market. Nor does it contain anything that would limit the application of the new s 46 to conduct that both "substantially harms competition and that has no economic justification", contrary to the observation by the Harper Committee at [61].

65. In my view, the recommended s 46(2) is an empty vessel. It does no more than require the Court to have regard to two considerations which are in any event embraced within the concept of conduct that has an effect or likely effect of substantially lessening competition. Take the first factor in sub-section (2)(a). It is obvious that the Court will necessarily have regard to the extent to which the conduct has the purpose, effect or likely effect of increasing competition in the market when it applies sub-section (1). The position is not altered by referring, non-exhaustively, to several ways in which that might be done, viz., enhancements to efficiency, innovation, product quality or price competitiveness. Similarly, paragraph (b) merely re-states the necessary effect of sub-section (1), and the non-exhaustive references to several ways in which competition might be lessened adds nothing by way of safeguard.

66. The risk of over-capture can be illustrated in various ways, as the Business Council of Australia did in its February 2016 submission to the Treasury. The BCA's illustrations include the following:

    (a) *Delays and narrow market definitions:* The experience of BCA member companies is that the ACCC's application of the substantial lessening of competition test under other sections of the Act can take many months and regularly involves very narrow market definitions. Many examples can be given. For instance, Bluescope's recent merger applications took between 10 and 34 weeks and one involved a lengthy investigation by the ACCC into a narrow market definition affecting the provision of only 230 tonnes of steel. The ACCC's recent

investigations into the Asciano merger applications have taken many many months.

In merger clearance applications, the ACCC's application of the test has highlighted two major problems with the proposed new s 46. First, the narrow and unpredictable approach to defining markets at a very local level means a broad range of current and prospective business activities, including small businesses operating in smaller markets, fall within the scope of s 46 and their normal activities risk investigation and potential allegations of contravention. Secondly, the time and substantial cost to business involved in such inquiries or investigations will slow down decision making, put companies at a commercial disadvantage, and deter pro-competitive activity.

(b) *Small businesses:* The proposed change to s 46 will capture small businesses with market power operating in narrowly defined markets based on geography or the definition of the product on offer. The risk can be illustrated by reference to the hardware segment of the market.

> Former Woolworths Chairman, Mr John Dahlsen, has reportedly called for changes to the section 46 laws because hardware stores such as those owned by his company JC Dahlsen are finding it difficult to compete with new Bunnings stores ('Former Woolworths Chairman John Dahlsen attacks Bunnings', SMH, 12 August 2015). Dahlsen cites the case of three stores where his company 'had to sell those stores because Bunnings informed us they were entering those three markets'. Dahlsen also says, 'Bunnings is now entering very small markets which five years ago it wouldn't have contemplated, and it's having a dramatic effect on the small retailer – many small independent hardware merchants are failing'. ACCC Chair Rod Sims is quoted as saying that: 'Yes, there are some concerns with Bunning's share and it's an area of interest but so are many other areas'. Bunnings succeeds when consumers choose to switch from existing retailers to take advantage of the low prices and extensive range that a new Bunnings sore offers. This is the nature of competition and is good

for the consumer. If, as is suggested by the article, the proposed changes to section 46 could be used by existing retailers to stymie competition from new entrants (i.e. to prevent new Bunnings stores), it could deprive consumers in those areas of the benefits that are available to consumers in other parts of Australia where Bunnings already operates.

(c) *Supermarket home brands:* The major supermarket operators have introduced home brands which have had the effect of lowering prices and introducing more competition with other brands on supermarket shelves as the ACCC found in its 2008 food and grocery inquiry.

Major supermarkets have recently expanded their home brand range, to appeal to price sensitive customers and respond to competition from new entrants. If they expand the offer of home brands further, the effects on suppliers of branded products may put the supermarkets at risk of prosecution under the proposed section 46. The supermarkets may be deemed to have market power due to their market share and access to customers and supplies that its competitors do not have. There may be an effect of lessening of competition in the retail markets due to potential competitors not entering the market; or existing competitors potentially exiting the market.

(d) State-based pricing:

Under a policy called 'state-based pricing', the major supermarkets offer the same, low prices on goods like milk, meat, bread and other groceries to regional consumers as they offer to consumers in the city. Almost all stores within a state set the same price, even in regional areas where it costs more to transport and supply the goods. The policy helps to ease cost-of-living pressures in parts of the country where disposable incomes may on average be lower than in the cities. Under the proposed section 46, local grocers unable to match the low prices on those products could argue the effect is a 'substantial lessening of competition' (i.e. from grocers closing down, or choosing not to enter the market, because they cannot compete). To avoid this risk, the major supermarkets would

> have to consider abandoning state-based pricing and charge regional consumers higher prices for milk, meat, bread and groceries.

67. The ACCC has argued in various places, both by submissions to the Harper Committee and in public statements, that the proposed effects test in s 46 poses no risk to legitimate business conduct. The following is a sample of statements made by the ACCC:

(a) Competition on the merits will not be affected

> "Companies that want to compete on their merits have nothing to fear. Only those who wish to exclude their competitors and damage the competitive process will need to re-examine their conduct."[50]
>
> "I have heard concerns from many leaders in the business community about an effect of SLC test. It seems to me those concerns are based on a misunderstanding.
>
> Some business leaders have said that, for example, when they innovate, actively compete on price or enter a new geographic market, and the result is that they succeed and most others fail, they fear their outcomes will have the effect of SLC.
>
> This confuses the outcome with how you get there. To be held to have substantially lessened competition you have to do something anti-competitive; pro-competitive behaviour, whatever the outcome, cannot be held to SLC.
>
> As we have said, the ACCC sees anti-competitive behaviour as essentially exclusionary; it must affect the process of competition itself. New innovation, aggressive discounting (provided it is not below cost for a sustained period), and new market entry, are all pro-competitive and, in our view, cannot have the effect of SLC.

[50] "ACCC Chairman Rod Simms: 'Nothing to fear' from effects test", *AFR*, 17 March 2016.

To repeat, to SLC there must first be behaviour that could be seen as anticompetitive. There cannot be an SLC through competition on its merits."[51]

(b) Vertical arrangements with suppliers will not be affected

"The matter we have with Coles and the suppliers has got nothing to do with the misuse of market power, because they're not competitors, so there's just no issue there. The supplier case is not a competition case, it's got nothing to do with misuse of market power, it would be completely unaffected by the change I'm proposing.[52]

"Where the farmers are supplying a product and competing with the supermarkets who have a home brand in that product, that may be helpful... But if the issue is just a supplier relation, then it can't help them with an effects test".[53]

(c) State-based pricing will probably not be affected

"Craig Emerson has concerns that statewide uniform pricing could be subject to challenge under the Harper substantial lessening of competition test. The only circumstances where this could be the case is where the company is pricing all or most of its products below its own costs in a local market for a sustained period."[54]

"If there was predatory pricing involved, such as for example pricing below cost, there's laws there now to deal with that, 46 doesn't change that. Most importantly, let's say you price nappies at a low price. How is that going to substantially lessen competition in any market. How's that going to have an effect on retailing in in country towns. I mean it's just an extraordinarily strange proposition if I do say so myself... If

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[51] Rod Sims speech, "Bringing more economic perspectives to competition policy & law", RBB Economics Conference, Sydney, 7 November 2014.
[52] Extended interview with Rod Sims, *The Business*, ABC TV, 6 April 2014.
[53] "Competition watchdog ACCC head Rod Sims denies claims an 'effects test' would be 'economically dangerous'", *ABC Rural*, 19 August 2014.
[54] Rod Sims, "Why the change to Harper Competition Review law will help boost competition", *AFR*, 4 August 2015.

you out-compete your competition and put them out of business, that cannot possibly trigger section 46."[55]

(d) Opening a new retail store cannot breach the new section

"I am often told that when a supermarket opens in a new geographic area, that the existing shops will be substantially damaged. I am then asked: what is the ACCC going to do about it? Of course, there is no SLC in this case, although there may be harm to individual competitors in the market."[56]

"I find it very hard to see how the [Australian National Retail Association] could think that bringing a new store into a new market could have a purpose or effect of substantially lessening competition... Introducing a new business into a market doesn't substantially lessen competition, it adds to competition. I think the law on that is very clear."[57]

(e) The law will be limited to exclusionary conduct

"The ACCC wants to ensure competition is on its merits by dealing with exclusionary behaviour, when a business takes steps to prevent competitors entering a market."[58]

"Some argue that if a company outperforms its rivals and drives them out of business then this can lead to a substantial lessening of competition. This is not so. You cannot substantially lessen competition by outperforming your rivals, only by excluding them from competing on their own merits."[59]

68. There is no suggestion in the case law applying the substantial lessening of competition test that it only applies to particular forms of conduct such as

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[55] Extended interview with Rod Sims, *The Business*, ABC TV, 24 March 2016.
[56] Rod Sims speech, "Bringing more economic perspectives to competition policy & law", RBB Economics Conference, Sydney, 7 November 2014.
[57] "ACCC boss Rod Sims rejects supermarket claims effects test will hurt shoppers", *Sydney Morning Herald*, 27 April 2015.
[58] Rod Sims, "Enhancing Competition Policy", Law Council of Australia, Competition & Consumer Committee AGM, 12 September 2014.
[59] Rod Sims, "Why the change to Harper Competition Review law will help boost competition", *AFR*, 4 August 2015.

exclusionary conduct. To that extent, the arguments advanced by the ACCC are not consistent with the language of the proposed s 46 or the case law that has expounded on the substantial lessening of competition test.

69. Further, the arguments advanced by the ACCC are largely if not entirely question-begging for the reasons explained by Rachel Trindade, Alexandra Merrett and Rhonda Smith:

> The ACCC Chairman captured a popular sentiment in his speech to the RBB Economics Conference in November this year when he dismissed criticism of the use of the SLC test in section 46, saying:
>
> > To be held to have substantially lessened competition you have to do something anti-competitive; pro-competitive behaviour, whatever the outcome, cannot be held to SLC …
> >
> > > To repeat, to SLC there must first be behaviour that could be seen as anti-competitive. There cannot be an SLC through competition on its merits.
>
> Many people appear to agree with this general approach, but it's actually putting the cart before the horse …
>
> One simply cannot determine whether something is anticompetitive (or conversely "competition on the merits") without doing a proper competition analysis. The result of the competition analysis is what allows you to attach the label "anti-competitive" – in other words, conduct that substantially lessens competition in a market is anti-competitive. You can't start by characterising conduct as anti-competitive and then work backwards – that's exactly the type of error of reasoning our High Court has warned against.[60]

As a result, if the substantially lessening competition test were to become the only operative element of section 46,aside from the threshold requirement of substantial market power, a business would need to consider the effect of all of its conduct on competition in its immediate market and any related market.

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[60] Rachel Trindade, Alexandra Merrett and Rhonda Smith, *The state of competition*, Issue 21, December 2014.

70. The logical flaws in the arguments advanced by the ACCC exposes a hole in the reasoning that underpins the Harper Committee's recommendation. As Peter Armitage has pointed out in his article, "The evolution of the 'substantial lessening of competition' test – a review of case law"[61]:

> The inclusion of the "substantial lessening of competition" standard in the prohibition on unilateral conduct of firms which possess substantial market power would require further development and articulation of it. Questions such as the following would need to be addressed by the courts:
>
> - Would conduct which intentionally injures rivals but which results in increased efficiency contravene the standard?
> - Would conduct which raised strategic barriers to entry contravene the standard?
> - How enduring would the impact on competition need to be?
>
> Answers to such questions will emerge in due course but the current case law provides no clear guidance. The inclusion of the "substantial lessening of competition" standard in the prohibition on misuse of substantial market power will inevitably create a period of considerable uncertainty for many firms and for the ACCC. If the evolution of the case law concerning the current prohibition is any guide, that period of uncertainty would be in the order of 20 years.

71. It is unclear how the revised s 46 would be applied to unilateral conduct by large corporations, such as the major supermarkets or hardware stores, which expand into smaller communities or markets in a way that is likely to lead smaller businesses to exit that market. If the market is defined very narrowly, as the ACCC is prone to do, then the loss of small competitors on the major's entry could easily be treated as a substantial lessening of competition.

72. In this regard, I note that proponents of the effects test have argued that the section needs to be revised so as to protect small businesses from fierce competition from larger rivals. Likewise, they have argued that it is necessary

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to protect small suppliers from their powerful customers, particularly the major supermarkets. These objectives may be reflected in the extrinsic materials that support the enactment of the proposed s 46, and that would exacerbate the risk of over-capture. In those circumstances, there must be a real risk that the loss of small competitors consequent on a large corporation's entry into a local market will attract s 46. This may be the result despite the fact that there is something counter-intuitive in the proposition that conduct that makes it likely that certain competitors will leave the market can be treated as conduct that is likely to substantially lessen competition, given that competition is a ruthless process, and the exit of firms expresses the very nature of competition.

73. The foregoing analysis demonstrates, in my view, that the risk of over-capture is real and imminent. It is unclear how those risks will be resolved. Perhaps the most that can be said is that courts called upon to interpret and apply the proposed s 46 will have to grapple with issues such as:

(a) to what extent does vigorous competitive conduct that results in a reduction in rivalry in a market, perhaps a very narrowly defined market, fall within the scope of the provision.

(b) whether the provision will extend to conduct in relation to suppliers or customers, such as conduct by a large corporation in demanding low prices from suppliers that has led, or is likely to lead, to increased concentration in the suppliers' segment of the market or under investment in that upstream segment of the market.

(c) whether the extrinsic materials and the objectives of the amending Act will allow the provision to be read down so that it only applies to certain forms of exclusionary conduct, and if so how that conduct might be described or defined.

Potential improvements to the provision

74. Working from the premise that s 46 is to be amended so as to include a prohibition on conduct that has the effect or likely effect of substantially

lessening competition, there are in my view a number of improvements that could be made to the provision.

75. In my opinion, the following changes warrant serious consideration:

(a) Purpose and effect: Consistently with the approach in Canada, purpose and effect should be cumulative requirements. It ought not be possible to breach s 46 simply by reason of the fact that conduct by a corporation which happens to have a substantial degree of power in a market has the effect or likely effect of substantially lessening competition in that market.

(b) Any other market: These words give the proposed provision too wide an operation. Without the words, the provision will apply to conduct in any market in which the corporation has a substantial degree of power and engages in conduct that falls within the provision. At the very least, the provision should be limited to any other market in which the corporation supplies or acquires goods or services.

(c) A safeguard provision: If there is to be a widely expressed prohibition on conduct that has the purpose and effect or likely effect of substantially lessening competition in a market, it should be accompanied by a meaningful safeguard that confines the principal provision to anti-competitive or exclusionary conduct. This is the approach adopted in Canada.

76. These changes could be implemented by revising the proposed s 46 so that it provides:

> *(1) A corporation that has a substantial degree of power in a market shall not engage in conduct if the conduct has an exclusionary purpose, and has, or would have or be likely to have the effect of substantially lessening competition in that market or in any other market in which the corporation supplies or acquires goods or services.*

(2) For the purposes of sub-section (1) conduct will have an exclusionary purpose if it:

(a) has the purpose of preventing, restricting or deterring anyone from engaging in competitive conduct in the market or in any other market in which the corporation supplies or acquires goods or services;

(b) has the purpose of preventing, restricting or limiting the supply of goods or services to, or the acquisition of goods or services from particular persons or classes of persons generally or from particular persons or classes of persons in particular circumstances or on particular conditions; or

(c) has the purpose of eliminating or substantially damaging a competitor; or

(d) has the purpose of preventing, restricting or deterring new entry into the market.

(3) In determining whether conduct has an exclusionary purpose, and has, or would have, or be likely to have the effect of substantially lessening competition in a market, the court must have regard to whether the conduct, or its effect or likely effect on competition:

(a) was a result of superior competitive performance;

(b) would be a result of a rational business decision by a corporation that did not have a substantial degree of power in the market; or

(c) would be likely to have the effect of advancing the long-term interests of consumers.

77. My sub-section (2) incorporates language that is currently used in s 46(1)(a), (b) and (c) and in s 4D. In my view, it is preferable to express the provision in this way rather than listing types of anti-competitive conduct as s 78(1) of the Canadian Act does.

78. The advantage of defining the requisite purpose as an exclusionary purpose in this way is that it ensures that the new provision targets misuses of market power much more directly and specifically than the provision formulated by the Harper Committee.

79. I have considered whether it would be possible to retain s 46(1) in the form recommended by the Harper Committee, while building all of the changes I consider necessary into sub-sections (2) and (3) of a new s 46. In my opinion, that course would be neither feasible nor desirable. First, it would result in two different purpose requirements – a purpose of substantially lessening competition in sub-section (1) which would need to be overridden by a more restrictive definition of purpose in sub-section (2). I doubt that any Parliamentary draftsperson would entertain such a structure. Secondly, it would not address the fact that s 46(1) expresses purpose and effect as alternative bases for a contravention of s 46. Consequently, even if a new sub-section (2) narrowed the purpose requirement to an exclusionary purpose, it would not address the fact that conduct would contravene s 46(1) if there were a real chance that it would substantially lessen competition. Thirdly, it would not address the inappropriate width of the concluding words "any other market" in sub-section (1).

80. My revised sub-section (3) is based on s 79(4) of the Canadian Act and elements of the defence originally proposed by the Harper Committee when it recommended changes to s 46.

81. The changes I have proposed to s 46(1) are the minimum changes necessary to address the problems I have identified.

82. More broadly, my revised s 46 is consistent with the ACCC's public assurances that the proposed s 46 is not aimed, and should not be aimed, at anything other than exclusionary or anti-competitive conduct.

83. Taken together, the changes I have put forward would, in my opinion, ensure that the new s 46 targets serious anti-competitive conduct while avoiding the problems, uncertainties and economic inefficiencies of a provision that overreaches its proper function within the Act of addressing the competitive harm that can be caused by misuses of market power.

10 June 2016

NEIL J YOUNG

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