

CHAPTER 7

EFFECTIVENESS OF TRADE PRACTICES LAW

How does trade practices law apply to ASX?

7.1 This Chapter focuses on the elements of Part IV of the *Trade Practices Act 1974* (TPA) which deal with anti-competitive behaviour. The majority of evidence in relation to this aspect of the terms of reference supports the current approach to applying the trade practices law to the ASX.

7.2 The Australian Competition and Consumer Commission is the independent government body which is responsible for ensuring compliance with Part IV of the TPA. The ACCC has jurisdiction to apply the sections of Part IV of the Act across all sectors of the Australian economy, including the ASX. The TPA is applied through a series of authorisations and court enforceable undertakings, examples of which are discussed later in this Chapter.

7.3 Part IV of the TPA prohibits the following anti-competitive behaviour:

- anti-competitive agreements and exclusionary provisions, including primary or secondary boycotts (section 45);
- misuse of market power (section 46);
- exclusive dealing (section 47);
- resale price maintenance (sections 48, 96-100); and
- mergers which would have the effect or likely effect of substantially lessening competition in a substantial market (sections 50, 50A).¹

7.4 The purpose of Part IV in relation to the structure of the ASX is to deliver a market place which avoids monopolies and maintains competition, where practical. Monopolies are recognised as being detrimental to consumers because they can lead to higher prices, reduce innovation and deliver sub-standard services.² In addition, the application of Part IV encourages fair competition which in turn is aimed at generating lower transaction costs.

Exceptions and authorisations

7.5 In its submission, the ACCC outlined numerous examples of the role Part IV has played in ensuring a competitive stock exchange. It has achieved this by applying a flexible system of authorisations and court enforceable undertakings in relation to

¹ ACCC, Submission No. 7, p. 2.

² ACCC, Submission No. 7, p. 3.

anti-competitive behaviour. Anti-competitive conduct which leads to possible breaches of the TPA can be exempted by the ACCC from legal proceedings. This is achieved by the application of an authorisation under section 88 of the TPA.³ The Committee notes that rulings made by the ACCC are appealable via the Australian Competition Tribunal. This tribunal is an independent body headed by a judge of the Federal Court who is assisted by two lay persons such as an economist and a business person.⁴

7.6 The ACCC has applied this system to the ASX since the introduction of the TPA in 1974. The ACCC has made rulings in a variety of areas including acquisitions, proposed changes to the ASX listing rules and the introduction of new technologies such as the SEATS and CHES systems.

7.7 When considering applications which seek to pursue actions that may breach Part IV of the TPA, the ACCC applies a public benefit test. The test requires that the applicant show that the results of the proposed activity, if approved, would lead to a public benefit outweighing the anti-competitive detriment.⁵

7.8 The concept of public benefit is determined, amongst other factors, as including such benefits as economic development and fostering business efficiency which improves international competitiveness.⁶

7.9 The 1992 decision in relation to SEATS is an example of the ACCC sanctioning an application which would lead to anti-competitive behaviour, on the grounds of a public benefit.

7.10 SEATS is a computer-screen based system which removes the need for floor trading. The SEATS system offers added efficiency and security for people trading in the market. The benefits gained by the use of SEATS contributes to the ASX becoming more competitive in the international market. The ACCC held that such advantages outweighed the possible breach of the TPA.

7.11 However, before approving the implementation of SEATS the ACCC required the ASX to agree to two points. Firstly, the ASX is required to supply market information to persons on reasonable commercial terms. Secondly, any restrictions in relation to intellectual property only apply in respect of where the law currently applies and to the extent necessary to protect the property.

7.12 By contrast, a notable example of an ACCC refusal of authorisation for an application from the ASX was in relation to the 1999 ASX bid for the Sydney Futures

³ ACCC, Submission No. 7, p. 4.

⁴ ACCC, Submission No. 7, p. 5.

⁵ ACCC, Submission No. 7, p. 29.

⁶ Miller's Annotated Trade Practices Act 2000/21st Edition, Russell V Miller, LBC, Sydney, 2000, p. 637.

Exchange (SFE). In this case the ACCC decided not to grant permission for the purchase.

7.13 The ACCC determined that the bid would substantially reduce competition and so breach section 50 of the TPA. In evidence to the Committee the ACCC elaborated on this matter:

Again, I think it was expressed pretty strongly in our decision on SFE-ASX that we considered the risk to innovation, development of new products, pricing for users and so forth. We really saw those as being at risk - the whole development - as the SFE and ASX...We always have a concern with monopolies if there is no external discipline or import discipline.⁷

7.14 On the day of the ACCC's decision, the ASX withdrew its offer for the SFE.⁸

7.15 As an alternative to either accepting or rejecting applications outright, the ACCC may exercise a third option, namely to seek and accept enforceable undertakings from entities under section 87B of the TPA. Such undertakings create court enforceable agreements in relation to arrangements into which entities enter. The use of 87B allows some manoeuvring amongst the parties and the ACCC when considering a proposal.

7.16 In relation to the ASX, the joint venture between the ASX and Perpetual Registrars Australia forming ASX Perpetual Registrars made use of the 87B provisions by creating an agreement which aimed to ensure the separation of the commercial and regulatory functions of the ASX. The agreement also ensured that the ASX would not discriminate between parties utilising the ASX's CHESS system.⁹

7.17 The ability of the ACCC to apply enforceable undertakings offers an element of flexibility to the management of the trade practices law in regard to the ASX. The Committee notes that this facility allows the ACCC to maintain competition in the majority of the proposals put to it.

Effects on competition

7.18 The ASX has made a number of submissions in the past proposing the removal of the ASX from ACCC jurisdiction in favour of regulation under the Corporations Law.¹⁰ However, the Committee notes the important function the ACCC has performed, in terms of maintaining competition, with specific reference to the ASX.

⁷ Evidence, p. 91.

⁸ ACCC, Submission No. 7, p. 20.

⁹ Evidence, p. 92.

¹⁰ ACCC, Submission No. 7, p. 3.

7.19 For example, the Australian Associated Stock Exchanges (AASE) has sought, in the past to introduce conditions on trading and entry as a broker into the ASX. The ACCC ruled that such conditions would be substantially anti-competitive and did not have the requisite public benefit.

7.20 In the current environment, the Committee considers that the role which the ACCC performs has taken on an even greater importance. The evolution of the ASX into a 'for profit' organisation has attracted criticisms in relation to trade practices issues, such as the potential for the ASX to misuse its market power.

7.21 Some of the fears relating to possible anti-competitive behaviour were expressed by Mr Chamberlain, a senior executive with Computershare:

ASX's moves to vertically integrate its practical monopolies into areas where there has traditionally been competition, such as share registration and information distribution, are likely to have the effect of significantly reducing competition in those markets, with inevitable costs to consumers and reductions in levels of service and innovation.¹¹

7.22 In its submission, Computershare pointed out the advantages the ASX has in the marketplace. Such advantages include the tendency for buyers of equity shares to gravitate to the market that has the most sellers and vice versa. The result is that the majority of market participants in equity shares direct their business to the largest market, the ASX.

7.23 Another example of ASX's advantage is its monopoly ownership of the CHESSE system. Computershare pointed out that, currently, the CHESSE system is the only electronic method authorised to transfer the legal title of shares of a company formed under the Corporations Law.¹² Although, under the FSR Act, other bodies may apply for a licence to operate a clearing and settlement (CS) facility, no applications have been received to date.¹³ Computershare claimed that it is commercially impracticable to establish a competing CS facility due to the head start the ASX has enjoyed to this point:

[I]n a situation where ASX dominates trading in equities in Australia it is not possible as a practical matter for a competing clearing and settlement service to be offered. This is because clearance and settlement of any market transaction needs both parties to the transaction to participate in the same system. Otherwise, the system cannot match the purchaser's payment with the delivery of securities by the seller.¹⁴

¹¹ Evidence, p. 52.

¹² Computershare, Submission No. 4, p. 9.

¹³ *Financial Services Reform Act 2001*, s824A - s824C.

¹⁴ Computershare, Submission No. 4, p. 9.

7.24 The ASX did not agree that it was able to misuse its position in the market for its own commercial advantage, pointing out that the TPA prevents this:

Legislative sanctions are available for misuse of position. ASX cannot take advantage of its market power for the purpose of eliminating or substantially damaging a competitor in any market, preventing new entrants to any market. To do so would constitute a breach of section 46 of the Trade Practices Act.¹⁵

Global competition issues

7.25 The changing global market places pressure on small markets such as the ASX. The Committee acknowledges that this issue is best dealt with by the application of new technology, more efficient practices and market depth. In addition to this, the ASX has also expanded its traditional core services. Such expansion is squarely aimed at staying in touch with international trends, as more exchanges become 'for profit' organisations.

7.26 The development of additional services and products through vertical integration also reflects the ASX's desire to maximise profits. The development of a larger, deeper market leads to a more stable environment, which in turn creates a more attractive investment environment.

7.27 Increasingly vertical integration and the expansion of commercial activity by an already strong organisation like ASX does have the potential to reduce competition. However, some witnesses to this inquiry expressed the view that strengthening the local operator's ability to compete on a global market is more important than ensuring a competitive market.

7.28 For example, the Chartered Secretaries of Australia expressed their disappointment with the rejection by the ACCC of the ASX takeover of the SFE. They argued that the SFE takeover would have been an efficient and effective way to add depth to the market, which would have helped better to position Australia in the international context.¹⁶

7.29 In a similar vein, the ASX argued that it operates in an environment of global competition,¹⁷ and that an isolationist application of the TPA is out of step in that context. In response, however, the ACCC noted that, as part of the public benefit test, it does factor in the international perspective.¹⁸

¹⁵ ASX, Submission No. 2B, p. 4.

¹⁶ Chartered Secretaries of Australia Limited, Submission No. 6, p. 3.

¹⁷ ASX, Submission No. 2B, p. 21.

¹⁸ Evidence, p. 94.

Cross subsidisation and the TPA

7.30 The Committee received some evidence arguing that there is a potential for the ASX to derive an unfair competitive advantage by using profits generated through its market supervision role to cross subsidise less profitable activities. Computershare argued in its submission that the only viable solution would be for the ASX to 'ring fence' its regulatory and monopoly infrastructure businesses from its commercial activities. Senator Conroy explored this potential problem during a public hearing at which the ACCC gave evidence:

The argument is that there is a cross-subsidy taking place of the monopoly profits that are being generated in the regulatory function and then used to subsidise a commercial business against, say, Computershare or some other companies...Unless they are segregating their business so that they have no capacity to pass the money backwards and forwards, it is not possible to prove that they are not because you just have to assume that they are.¹⁹

7.31 The ACCC gave evidence that this could potentially constitute a breach of section 46 of the TPA. Mr Davey, Director of Mergers and Asset Sales explained:

I think that particular conduct of leveraging of market power from one market into another would certainly raise issues under section 46 of the Trades Practices Act, which prohibits misuse of market power. There are mechanisms under the law to deal with these types of problems.²⁰

7.32 The Committee is aware that the ACCC investigated the relationship between Bridge DFS and ASX, which holds 15 per cent equity in Bridge DFS, following a complaint made against the ASX in regard to a possible breach of section 46 of the TPA along these lines.²¹ The complaint alleged that the accounting procedures used by Bridge DFS were inappropriate when calculating the fees owed to the ASX for the provision of real-time share market data. However, the ACCC found that the complaint could not be substantiated.

Conclusions

7.33 The Committee notes that the ASX's motivation for expanding its range of services relates to it being a relatively minor player in terms of international financial markets. The small size of the ASX in those terms places pressure on it to continually stay relevant and competitive internationally. The success of such a strategy is assisted by flexibility in trade practices law which allow certain concessions in respect of the TPA.

7.34 This flexibility was reflected in the 1986 application made to the ACCC in relation to the restructuring of stock exchanges to form the ASX.

¹⁹ Evidence, p. 88.

²⁰ Evidence, p. 89.

²¹ Additional information supplied by the ACCC.

7.35 In dealing with this application the ACCC considered advantages such as the efficiency of the market and the added security to investors of the creation of a larger market with more depth.²² These advantages were considered to outweigh any anti-competitive results.

7.36 The Committee considers that the needs of the ASX to continue with a global perspective will be ongoing. For this reason, the TPA will have to be applied with a view to international trends. However, the development of ASX's ability to compete globally will always have to be carefully balanced against the need to maintain competition in Australian financial markets. The past benefits of maintaining competitive pressures in this sector are clear.

7.37 The Committee finds that the application of the trade practices law is addressing the needs of the ASX in a manner which offers flexibility via its system of authorisations, section 87B undertakings and the appeals system. These tools offer flexibility while also maintaining a competitive environment, with the final arbiter in any situation regarding the TPA being the courts.

7.38 The Committee also notes that in the majority of submissions and evidence received, the adequacy of trade practices law in ensuring a competitive stock exchange market was not questioned. However, the Committee is mindful that as the ASX expands its activities into other commercial areas, it is causing concern to some of its competitors. The ASX is aware of these concerns. The Committee believes that moves to increase the transparency of the supervisory framework – including the establishment of the ASXSR – and the continued application of the Trade Practices Act to the ASX will assist in addressing those concerns.

Senator the Hon Brian Gibson
Acting Chairman

²² ACCC, Submission No. 7, p. 8.

