Business Council of Australia

Submission to the
Senate Economic References Committee

Inquiry into whether the *Trade Practices Act 1974* adequately protects small businesses from anti-competitive or unfair conduct

29 August 2003

FOREWORD

The Business Council of Australia is pleased to provide this submission to the Senate Economic References Committee.

The Business Council recognises the important role that small business plays in the Australian economy. Equally, big business is a major contributor to the prosperity of many small businesses. The Business Council believes that the best way to ensure the continued growth and success of all business, including small business, is to maintain a buoyant and competitive Australian economy through strong competition and to ensure that small businesses have access to information and support services to assist them in their business activities.

This inquiry follows a number of reviews of the *Trade Practices Act*. These reviews and recent Court decisions have restated that the underlying objective of the *Trade Practices Act* is the promotion of competition, not the protection of individual competitors whether they be large competitors or small competitors. Competition regulation must create the right balance between:

1 promoting Australia's interests in becoming more internationally competitive; and

2 the need to protect strong competition in domestic markets.

There are dangers for Australia if this balance is not achieved. Ultimately, the result will be a less competitive Australian economy, resulting in fewer jobs, higher costs to Australian consumers and a potential acceleration of Australian companies preferring to invest overseas. This outcome would undermine the Hilmer Reforms and the implementation of the National Competition Policy which frees the Australian economy of legislation which inhibits competition. This has been regarded by the Organisation for Economic Co-operation and Development as one of the driving factors in microeconomic reform which has assisted Australia in maintaining a strong and robust economy in the face of a global economic downturn.

This inquiry, therefore, presents a valuable opportunity for the Senate Committee to assess what the *Trade Practices Act* is, in practice, able to achieve. While the Business Council believes it is important that the views of all sectors are canvassed and debated, the Business Council submits that the *Trade Practices Act*, which regulates competition across all businesses, may not be the most appropriate forum in which to address issues which relate purely to social or sector specific concerns. Accordingly, the Business Council believes it will be important that the Senate Committee takes into account, addresses and manages expectations where they go beyond the proper scope of the *Trade Practices Act* in promoting competition in Australia.

The Business Council of Australia is an association of chief executives of leading Australian corporations. It was established in 1983 to provide a forum for Australian business leaders to contribute directly to public policy debates to build a better and more prosperous Australian society. A list of companies comprising the Business Council is contained in the following pages.

The key role of the Business Council is to formulate and promote the views of Australian business. The Business Council is committed to achieving the changes required to improve Australia's competitiveness and to establish a strong and growing economy as the basis for a prosperous and fair society that meets the aspirations of the whole Australian community.

The Business Council has a particular responsibility to apply Australia's business experience and understanding to successfully resolving the challenges now facing Australia. In a global environment, Australia's future depends on achieving world class performance and competitiveness. On the basis of sound research and analysis, the Business Council seeks to play a key role with government, interest groups and the broader community to achieve performance and world class competitiveness.

I commend the Business Council's submission to the Senate Committee.

John Schubert
President

List of Member Companies of the Business Council of Australia

ABB Australia

ABN AMRO Australia

Accenture

ACI Packaging Group

Alcoa World Alumina Australia

Allens Arthur Robinson

Alumina Australia

Amcor

AMP

ANZ Banking Group

Australia Post

Australian Gas Light Company

Australian Stock Exchange

AWB

BHP Billiton

BHP Steel

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UBS

Visy Industries

Wesfarmers

Westpac Banking Corporation

WMC Resources

Woodside Petroleum

Woolworths

PROCESS AND ACKNOWLEDGEMENTS

The preparation of the Business Council's submission has involved:

(a) consultation with members and with a number of other business and other bodies;

(b) contributions from member companies through their CEOs and other representatives;

(c) external expert advice on certain aspects of the submission; and

(d) research and input by the Business Council's Secretariat.

The Business Council's work was directed by the Council's Regulatory Reform Task Force and the Council's Secretariat reporting to the Business Council's President and Board.

On behalf of the Business Council, we thank all those involved for their time and assistance.

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Executive summary

Introduction

The Business Council of Australia welcomes the opportunity to make a submission to the Senate Economic References Committee's ("**Committee**") inquiry into whether the *Trade Practices Act 1974 (Cth)* ("**TPA**") adequately protects small business from anti-competitive or unfair conduct.

The Business Council acknowledges the importance of small business to the Australian economy. The Australian economy needs small businesses to enter the market with new ideas and new methods, find new niches, challenge existing businesses and expand. Small business is also a major supplier of goods and services to bigger businesses. Equally, big business is a major contributor to the prosperity of many small businesses.

This inquiry, following a number of recent trade practices inquiries and reviews, presents a further opportunity to ensure that the TPA continues to keep pace with the interests of Australian consumers and businesses.

The Business Council

The Business Council represents 100 of Australia's largest corporations, which make a significant contribution to the Australian economy. In 2001/02, the Business Council's members earned revenue of $338 billion, equivalent to around half of Australia's economic output, and accounted for 31% of Australia's total export revenue. They employ nearly 1 million Australians, representing 10% of the workforce. These organisations are some of Australia's largest investors in research and development, and are responsible for a significant proportion of capital investment by the private sector.

Key themes of the Business Council's submission

The Business Council believes that the TPA, the underlying objective of which is to promote and protect the competitive process, serves the purpose of ensuring Australia's economy remains competitive through domestic markets that are increasingly dynamic, innovative and engaged with the world economy. The ultimate test of the TPA is whether it ensures competition between businesses is delivering long term benefits to consumers.

The 'well-being' of the Australian economy is fundamental to all Australian businesses, whether they be large or small. Competitive businesses are better positioned to meet the needs of Australian consumers, who have more choices and are better informed as new products, services and competitors constantly emerge.

Given that the overriding objective of the TPA is to foster the competitive process, which equips Australian businesses to meet the needs of their customers, the Business Council submits that, at this stage, there is no compelling evidence to justify specific legislative amendment to the TPA to protect small business from anti-competitive or unfair conduct. The Business Council believes that the legislative measures already in place provide all businesses, whether small or not, with adequate and effective protection from that type of conduct.

That said, the Business Council recognises the importance of the role that small businesses play in fostering the competitiveness of the Australian economy and the concerns that some small business groups have expressed.

The Business Council believes that where those concerns are warranted, they are better addressed in the form of other measures or initiatives (some of which are detailed below), rather than legislative amendments which could undermine the very architecture and purpose of the TPA. Accordingly, the Business Council encourages all governments to continue to assist small business with initiatives and programs that support small business, rather than legislative restrictions on competition by larger businesses.

In addition, the Business Council encourages and endorses initiatives which reduce the regulatory burden for small businesses, such as voluntary industry codes and the Australian Competition & Consumer Commission's ("**ACCC**") proposal to endorse those codes.

Key areas of submission

The Business Council's submission covers the context of the review and the competition and regulatory principles behind five key areas of the TPA. These five key areas correspond to the matters identified in the Committee's Terms of Reference, as follows:

- section 46;
- the unconscionable conduct provisions in Part IVA;
- industry codes in Part IVB;
- other measures to assist small business; and
- approaches adopted in other jurisdictions to protect small businesses.

Context of the review: healthy competition is a key to a healthy economy

A vital ingredient in a healthy Australian economy is the promotion and maintenance of healthy competition within that economy. The Australian economy continues to change, being driven by globalisation, liberalisation of trade and investment, and the evolution of new technologies. As these changes occur, so businesses must respond to the dynamics of the market-place. Businesses that are competitive at home will be businesses that can be competitive abroad.

The Business Council believes that the best way to ensure the continued growth and success of small business is to maintain a competitive Australian economy and, at the same time, to ensure that small businesses have access to information and support services to assist them in their business activities.

The cornerstone of the TPA is its objective of promoting competition, not competitors. All businesses, large and small, the Australian economy and, ultimately, Australian consumers will be harmed by measures that unnecessarily "blunt" the competitive process by protecting certain competitors from competition. The Business Council is concerned that some business interests may be turning to the TPA to provide them with protection from competition, in response to the dismantling of past protective policies such as restricted licensing and operating laws. These laws have often been removed to promote greater competition for the benefit of consumers and should not be replaced by changes to the TPA.

It is for this reason that the Business Council believes that any further measures to protect small business, by amending the TPA, should be approached with considerable caution.

To the extent that there is sufficient evidence to justify a change to the law, that change must, nonetheless, conform with the objective of the TPA and the long term economic interests of Australia.

The Business Council notes that Part IV of the TPA has only recently been subject to an intense and independent review, the *Review of the Competition Provisions of the Trade Practices Act*[1] ("**Dawson Committee**"). Extensive submissions were made to the Dawson Committee by a range of consumer and business groups. As a result, the Dawson Committee made a number of recommendations for changes to the TPA and the operation of the ACCC. It also rejected a number of other changes to the TPA.

As discussed in this submission, the Business Council's view is that apart from the Dawson Committee's recommendations, there is no compelling evidence to support further changes to the TPA at this time.

Section 46 of the TPA

The Business Council submits that section 46 of the TPA is dealing effectively with misuses of market power and at this time, a legislative amendment specifically to protect small business from anti-competitive or unfair conduct is not warranted. In particular:

- section 46 of the TPA must be viewed in the light of the object of the TPA, namely the protection of competition, not competitors;

- competition law should be sufficiently certain so that businesses, whether they be large or small, are able to understand the nature and scope of their obligations and are in a position to make business decisions with a clear understanding of conduct which may raise issues under the TPA. This is particularly the case for section 46, where the line between rigorous competition and anti-competitive conduct can be a fine one;

- while the law in this area is still developing, recent decisions of the High Court and the Full Court of the Federal Court have provided further clarification of the operation of section 46. These decisions demonstrate that the operation of the section is sufficiently clear and that the ACCC can succeed in prosecuting a contravention of the law;

- proposals to incorporate an effects test into section 46 would create undue uncertainty in the operation of the law and would risk catching pro-competitive conduct to the detriment of the competitive process and all competitors large and small. This view has been endorsed by several legislative reviews of the TPA, including the Dawson Committee's recent review;

- seeking to define market power by reference to market share alone, or market concentration thresholds, would run counter to accepted economic principles that market power is, in effect, the ability to act unconstrained in a market. While market share may be a relevant factor in determining the existence of market power, factors such as the height of barriers to entry and the constraints exerted by a corporation's competitors, suppliers and customers are equally important;

[1] January 2003.

- the proposal to codify section 46 would unduly restrict what is in essence an evolving economic concept; and
- a specific prohibition against predatory pricing could deter competition thereby damaging the competitive process and ultimately consumers.

This submission does not deal with previous calls for the introduction of cease and desist orders to assist in the enforcement of section 46, or a reversal of the onus of the proof in section 46, as these issues were subject to a detailed review and were ultimately rejected by the Dawson Committee. However, the Business Council would be happy to make submissions on these points if the Committee would find that helpful.

Unconscionable conduct

The Business Council supports the current unconscionable conduct provisions under the TPA which provide small business with effective protection from unconscionable or unfair conduct in business transactions.

Under Part IVA of the TPA, small businesses may have recourse to a number of key provisions. Section 51AC was recently enacted with the purpose of better protecting small business from unconscionable or unfair conduct.

Although the law is still developing, the early indications are that the section is achieving its purpose and the ACCC has been successful in a number of cases. In addition, there are 6 cases under section 51AC currently before the Courts, the outcome of which will clarify the scope of the section even further. Accordingly, the Business Council submits that it would be premature for the Committee to recommend an amendment to, or expansion of, Part IVA whilst section 51AC is bedded down. The Business Council believes that it is appropriate to allow the courts to continue to develop the relevant principles and allow precedent to be refined.

Further, to intervene at this formative stage would subject all businesses (large and small) to undue uncertainty in their commercial dealings. This uncertainty would be likely to have negative implications for the operation of the competitive markets, the Australian economy and consumers in general.

Industry codes

The Business Council submits that industry codes are generally an effective compliance tool. Industry codes encourage self-regulation by promoting best practice standards relevant to the industries in question and they typically lower compliance costs for business compared with intervention by regulatory agencies.

Part IVB helps promote better standards of business conduct in industries where self-regulation has failed and has been used effectively to regulate franchising operations.

The Business Council submits that the recent ACCC proposal to endorse industry codes is a good one. ACCC endorsement of industry codes should help to encourage a greater degree of compliance while having the potential to reduce compliance costs. The Business Council accepts the stated position of the ACCC that its endorsement will be "*hard to obtain and easy to lose*"[2].

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[2] "*ACCC to endorse high standard voluntary industry codes of conduct*", ACCC media release, 11 August 2003.

The Business Council particularly draws the Committee's attention to the Retail Grocery Industry Code of Conduct and notes that some of the concerns that sparked this inquiry have come from the retail grocery sector. The Business Council notes that this code is currently under review and a report is due on 1 December 2003. The Business Council submits that it would be appropriate to wait and see whether the report on the Retail Grocery Industry Code of Conduct addresses these concerns before assessing whether further legislative amendment is necessary.

Other measures to assist small business

The Business Council believes that the TPA already provides adequate and effective assistance to small business for dealing with anti-competitive or unfair conduct. The Business Council submits that the provisions that were enacted in the TPA as a result of the Reid[3] and Baird Committee[4] reports have not yet had an opportunity to be sufficiently tested. Further precedent and ACCC experience of enforcing these provisions is required before they can be reviewed properly. For this reason, the Business Council believes that further legislative amendment at this time is not warranted.

In addition, the Business Council submits that a proposal, supported by some sectors, to "cap" individual businesses' market shares would give rise to a number of practical and enforcement difficulties. Setting a market share cap would be, at best, an uncertain (if not arbitrary) exercise. Moreover, a market share cap would be likely to "blunt" the competitive processes by providing businesses with an incentive to maintain the *status quo* and a disincentive to pursue opportunities to become more efficient, innovative or productive which would usually allow a business to grow. Paradoxically, a market share cap could actually result in small businesses being "stranded" if, due to a market cap, they were denied the opportunity to sell their business to the highest bidder.

However, in order to further assist small business, the Business Council suggests, consistent with the recommendations of the Dawson Committee, that the ACCC consider issuing guidelines concerning its approach to Part IVA of the TPA. In addition, the Business Council notes that improvements to the collective bargaining approval process recommended by the Dawson Committee will address many small business concerns.

The Business Council also acknowledges and supports the assistance programmes Commonwealth, State and Local governments provide to small business.

Approaches in other jurisdictions

The Business Council notes the experience of competition regulation in OECD countries. The Business Council believes that drawing conclusions based on the experience of competition regulation of other countries with regard to the protection of small business should be undertaken with caution. In particular, the Business Council submits that regulation in these other jurisdictions has arisen due to historical, geographical and cultural reasons that are not necessarily applicable in Australia. Amendments to competition regulation should be in Australia's best interests and not merely to create uniformity with competition regimes in other jurisdictions.

[3] Report of the House of Representatives Standing Committee on Industry, Science and Technology, *Finding a Balance towards Fair Trading in Australia,* May 1997.

[4] Report of the Joint Select Committee on the Retailing Sector, *Fair Market or Market Failure,* August 1999.

1 Context of review

1.1 Key points

The Business Council submits that the Committee's review of the TPA should take account of Australia's changing economy, which is becoming more open, connected and integrated with the global economy. In this environment, Australian competition regulation should strive to:

- contribute to the productivity, efficiency and growth of the Australian economy; and
- minimise the risk of regulatory error. As the Australian economy becomes more exposed to international competition, so the cost of incorrect regulatory intervention becomes higher through inefficiencies, disincentives to invest and higher costs to consumers.

With this in mind, together with the Committee's Terms of Reference, the Business Council believes that now is not the time to make further changes to the TPA, given that:

- the Dawson Committee recently concluded that there is no need to make further changes to section 46. The recent decisions of the High Court and the Full Court of the Federal Court of Australia, which have been handed down subsequently, give further weight to this view;
- so far as specific small business provisions are concerned (Part IVA of the TPA), the Business Council believes that these provisions should continue to be enforced as they stand, in order to develop greater precedent, before determining whether they need further refinement;
- the amendments made to the TPA arising from the Baird Committee, including the extension of the powers of the ACCC to bring representative actions and the significant increase in the range of transactions covered by the unconscionable conduct provisions, have not yet been fully tested; and
- the recommendations of the Dawson Committee in response to small business concerns, including the improved processes for approving collective bargaining, have not yet been implemented.

Given these circumstances, the Business Council considers that there is not, at this time, sufficient evidence to support the view that the TPA does not adequately protect small business from anti-competitive or unfair conduct. Accordingly, the Business Council submits that the Committee should not recommend any legislative amendment to the TPA.

1.2 Importance of competition to the Australian economy

Australian businesses, irrespective of their size, have a particular interest in the TPA. Globalisation, liberalisation of trade and investment and the evolution of new technologies are driving change in the Australian economy. These changes have made Australia more interconnected with the rest of the world. New technologies have increased the ability of consumers to participate in the marketplace, giving them more

choices and making them better informed. These changes are forcing businesses to become more innovative, as the nature of markets changes more rapidly.

There are dangers for Australia if competition regulation fails to ensure productivity, efficiency and growth in an open, integrated Australian economy. The size of the Australian economy creates an acute dilemma for competition policy. Robust domestic competition is an important contributor to productivity and efficiency gains that benefit domestic consumers and businesses and underpin our international competitiveness. But if carried too far, competition regulation can, in small fragmented markets, deny businesses the economies of scale and scope needed to successfully compete and grow in increasingly global markets. The Business Council supports the view expressed by the then Chairman of the ACCC, Professor Fels, that:

> *"…in a small economy, some firms will be so small that they cannot achieve the benefits of large-scale production. From this perspective, if competition policy is pursued vigorously, it may inhibit the attainment of the economies of scale available in bigger countries"* [5].

The result of not achieving the right balance will be a less competitive Australian economy. Ultimately, the result will be fewer jobs and higher costs to Australian consumers.

Competition spurs businesses to produce goods and services that better satisfy the needs and desires of consumers and at lower prices. Firms engage in activities such as research and development, exploration, innovation and production efficiency in order to be able to offer better and cheaper goods and services.

The TPA is the Commonwealth Government's key legislative tool for promoting competition. It needs to be able to continue to meet the challenge.

1.3 Principles behind competition regulation

The Business Council submits that any change to the TPA should reflect a number of fundamental, underlying touchstones that are consistent with the objectives of the TPA. The fundamental objective underpinning the TPA is set out in section 2, which states that:

> *"The object of this Act is to enhance the welfare of Australians through the promotion of competition and fair trading and provisions for consumer protection."*

Recent statements by members of the High Court in the *Boral*[6] case acknowledge this purpose. Gleeson CJ and Callinan J held that:

> *"…the purpose of the Act is to promote competition, not to protect the private interests of particular persons or corporations. Competition damages competitors. If the damage is sufficiently serious competition may eliminate a competitor"*[7].

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5 Professor Allan Fels, "A Little Monopoly keeps the Economy Sound", *The Australian*, 2 February 2002, at 9.

6 *Boral Masonry Limited v ACCC* [2003] HCA 5 ("**Boral**").

7 [2003] HCA 5 at [87]. See also *Queensland Wire Industries Pty Ltd v Broken Hill Proprietary Limited (1989) 167 CLR 177* at *[191] ("**Queensland Wire**")* and *Melway Publishing Pty Ltd v Robert Hicks Pty Ltd (2001) 205 CLR 1 at 13 [17] ("**Melway**").*

"If the objective is achieved competitors will necessarily be damaged. If it is achieved to a sufficient extent, one or more of them may be eliminated. That is inherent in the competitive process. The purpose of the statute is to promote competition; and successful competition is bound to cause damage to some competitors"[8].

The Terms of Reference for this inquiry direct the Committee to consider "*whether the TPA adequately protects small business from anti-competitive or unfair conduct*". In so doing, the Business Council submits that the Committee should also consider a number of key principles which underpin competition regulation. These are:

- protecting competition, not competitors;
- equality before the law;
- certainty of the law, to enable all businesses to understand the nature and scope of their obligations and thereby to encourage compliance;
- proportionality of response;
- using existing powers first; and
- bedding down change.

More information on each of these principles is contained in **Appendix 1**.

1.4 Conclusion

All businesses have a particular interest in ensuring that the TPA operates effectively and efficiently and is able to contribute to the growth of an open, integrated Australian economy.

With this in mind, the Business Council believes that this inquiry presents the Committee with a valuable opportunity to assess what the TPA is, in practice, able to achieve. The Business Council acknowledges that some interest groups may have raised expectations that the TPA, as a legislative tool, is capable of dealing, and should deal, with small businesses' concerns on a sectoral basis. While this debate may touch upon a number of social issues, the Business Council believes that the TPA, the primary purpose of which is to regulate competition, is not be the most appropriate forum in which to address those concerns.

Accordingly, the Business Council believes it is important that the Committee takes this opportunity to appropriately take into account, address and manage those expectations where they are beyond the scope of the principles of the TPA. The BCA submits that the Committee should approach its review of the TPA with this key consideration, as well as the Terms of Reference, in mind.

1.5 Structure of submission

Against this background, the Business Council's submission focuses on the key areas identified in the Committee's Terms of Reference:

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8 [2003] HCA 5 at [122].

- section 46 of the TPA (**Section Two**);
- the unconscionable conduct provisions in Part IVA (**Section Three**);
- Part IVB and industry codes (**Section Four**);
- consideration of other measures to assist small business (**Section Five**); and
- whether approaches in other jurisdictions to protect small business are relevant to Australia (**Section Six**).

2 Section 46 of the TPA

2.1 Key points

The Business Council submits that section 46 of the TPA is dealing with misuses of market power as it was intended and a legislative amendment specifically to protect small business from anti-competitive or unfair conduct is not warranted at this time. In particular:

- section 46 of the TPA must be viewed in light of the object of the TPA, namely the protection of competition, not competitors;
- competition law should be sufficiently certain so that businesses, whether they be large or small, are able to understand the nature and scope of their obligations and are in a position to make business decisions with a clear understanding of the conduct which may give rise to issues under the TPA. This is particularly the case for section 46, where the line between vigorous competition and anti-competitive conduct can be a fine one;
- while the law in this area is still developing, recent decisions of the High Court and Full Court of the Federal Court have provided further clarification of the operation of section 46. These decisions demonstrate that the operation of the section is sufficiently clear and the ACCC can succeed in prosecuting a contravention of the law;
- proposals to incorporate an effects test into section 46 would create undue uncertainty in the operation of the law and would risk catching pro-competitive conduct, to the detriment of the competitive process and **all** competitors, large and small. This view has been endorsed by several legislative reviews of the TPA, including the Dawson Committee's recent review of the TPA;
- seeking to define market power by reference to market share alone would run counter to accepted economic principles that market power is, in effect, the ability to act unconstrained in a market. While market share may be a relevant factor in determining the existence of market power, factors such as the height of barriers to entry and the constraints exerted by a corporation's competitors, suppliers and customers are equally important;
- proposals to "codify" section 46 would unduly restrict what is, in essence, an evolving economic concept; and
- a specific prohibition against predatory pricing could deter competition, thereby damaging the competitive process and, ultimately, consumers.

2.2 Structure

This section of the submission:

- outlines the current state of the law and examines previous reviews of section 46, the majority of which concluded no significant amendment was necessary;
- examines recent cases under section 46, which demonstrate that while the law continues to crystallise, it does capture misuses of market power; and

- assesses whether proposals to reform section 46, put forward by small business and others, are warranted.

2.3 Current state of the law under section 46

The legislative prohibition

Section 46 of the TPA reads:

> *"A corporation that has a substantial degree of power in a market shall not take advantage of that power for the purpose of:*
>
> *(a) eliminating or substantially damaging a competitor of the corporation or of a body corporate that is related to the corporation in that or any other market;*
>
> *(b) preventing the entry of a person into that or any other market; or*
>
> *(c) deterring or preventing a person from engaging in competitive conduct in that or any other market."*

Possessing a substantial degree of market power is not, of itself, a contravention of section 46. Section 46 is directed at preventing corporations with a substantial degree of market power from engaging in conduct which has an anti-competitive purpose, which is open to it only (or predominantly) by virtue of the market power it enjoys. Accordingly, as noted in *Queensland Wire*, the object of section 46:

> "*… is to protect the interests of consumers, the operation of the section being predicated on the assumption that competition is a means to an end*"[9].

Importantly, section 46 does **not** regulate market structure. Rather, it is concerned with the behaviour between particular participants in a given economic market. It is not concerned with industrial policy, or the structure of particular industries.

[9] (1989) 167 CLR 177 at 191per Mason CJ and Wilson J.

In line with current judicial interpretation[10], conduct will only contravene section 46 if:

- a corporation has a ***substantial degree of power***. Section 46(3) provides a guide to the way in which market power is to be determined. It requires consideration to be given to the extent to which the conduct of the body corporate is or is not constrained by competitors, potential competitors, suppliers or purchasers[11];
- a corporation has ***taken advantage*** of its market power. In this context, "taken advantage of" means a corporation has "used" its power to engage in conduct in which it would not have engaged (in the "reality of the market") if it did not have substantial market power[12]. It does not require conduct which is predatory or morally blameworthy[13]; and
- the conduct satisfies ***one of three proscribed purposes***[14]. In this regard, section 4F(1)(b) provides that the purpose specified in section 46 need not be the only purpose to attract the operation of section 46. It need only be a "substantial" purpose. In addition, section 46(7) assists parties with proving the "purpose" element of subsection (1). It provides that a corporation may be considered to have taken advantage of its power for one of the proscribed anti-competitive purposes even though its purpose is ascertainable only by inference from the conduct of the corporation, or of any other person, or from other relevant circumstances.

Although not specifically outlined in the TPA, examples of the kind of conduct that may fall within the prohibition in section 46 include a refusal to supply, a refusal to deal, predatory pricing, price discrimination, leveraging, a price or supply squeeze and a misuse of buying power. Given the breadth of the prohibition, it is important to ensure that it only captures conduct that hinders competition, and does not prevent legitimate competitive behaviour.

2.4 Legislative reviews of section 46

There have been several major reviews of the TPA, including section 46, as well as a number of reviews by committees formed under the Senate or House of Representatives. Each of these reviews and their key findings is summarised in the table below, while a more detailed review of each is contained in **Appendix 2**.

Importantly, these reviews concluded that to amend section 46 significantly would subject the operation of the provision and, ultimately, businesses to an unacceptable degree of uncertainty in their day-to-day dealings. In particular, the proposal to incorporate an effects test into section 46 has been considered in nearly every major review of the TPA since its introduction. Without exception, the proposal has been rejected. Consistent concerns with an effects test for section 46 have been that:

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[10] See the decisions of the High Court in *Melway* and *Boral* and The Full Court of the Federal Court in *Universal Music Australia Pty Ltd v ACCC* [2003] FCAFC 193.

[11] See the *Boral* decision [2003] HCA 5 [121] per Gleeson CJ, Callinan J and [168] per Gudrow, Gummow and Hayne JJ.

[12] See the majority judgment in *Melway* (2001) 205 CLR 1 at 25 [55]

[13] *Melway* (2001) 205 CLR 1 at 17 [26].

[14] "Purpose" simply refers to an intention to achieve a particular result - *Queensland Wire* (1989) 167 CLR 177 at [214] per Toohey J; *Melway* (2001) 205 CLR 1 at 18-19 [31] per Gleeson CJ, Gummow, Hayne and Callinan JJ .

(a) it would not be able to satisfactorily distinguish between desirable and undesirable competitive activity, whereas the current test creates a fair balance between misuse of market power and aggressive competitive behaviour;

(b) only purposive misuses of market power, and not inadvertent conduct or efficiency-inspired conduct, should be at risk of contravening section 46;

(c) an effects test is likely to bring within its ambit much legitimate business conduct and so operate to stifle pro-competitive behaviour;

(d) it could inappropriately broaden the application of section 46 and render its application uncertain for businesses;

(e) it is not clear that the final result would differ from the existing interpretation of section 46, given that courts may develop a gloss on an effects test to ensure that it does not prohibit economically-efficient conduct; and

(f) any difficulties in proving a breach of section 46 in relation to purpose have been addressed by the facilitation of proof provision in section 46(7) of the TPA[15].

[15] M. Landrigan, et al, *An effects test under section 46 of the Trade Practices Act: identifying the real effects?* (2002) 9(3), Competition and Consumer Law Journal 258.

Review	Key finding
The Trade Practices Act Review Committee, 1976 (**“Swanson Committee”**)	Section 46 should only prohibit abuses by a monopolist that involve a proscribed purpose.
The Trade Practices Consultative Committee, 1979 (**“Blunt Committee”**)	Rejected an effects test because it would give section 46 too wide an application, bringing within its ambit much legitimate conduct.
Green paper on “*The Trade Practices Act Proposals for Change*”, 1984	Recommended that a lower threshold should apply and enabled the courts to infer a relevant purpose from the conduct of the corporation and any other relevant circumstances.
The House of Representatives Standing Committee on Legal and Constitutional Affairs, 1989 (**“Griffiths Committee”**)	Section 46 should be retained in its existing form because there was insufficient evidence to justify the introduction of an effects test.
The Trade Practices Commission’s Guidelines and Background Paper, 1990	Established guidelines for assessing whether a corporation had contravened section 46.
The Senate Standing Committee on Legal and Constitutional Affairs, 1991 (**“Cooney Committee”**)	An effects test might unduly broaden the scope of conduct captured by section 46 and challenge the competitive process itself.
The Independent Committee of Inquiry into Competition Policy in Australia, 1993 (**“Hilmer Committee”**)	Rejected the introduction of an effects test, saying that it would not adequately distinguish between socially detrimental and socially beneficial conduct.
The House of Representatives Standing Committee on Industry, Science and Technology, 1997 (**“Reid Committee”**)	Noted the effects test and the views of the Hilmer Committee, but did not recommend its introduction.
The Joint Select Committee, 1999 (**“Baird Committee”**)	Considered an amendment to section 46 could be to replace the “purpose test” with a test that states that once it is established that a corporation with a substantial degree of power in a market has used that market power, the onus of proof shifts to that corporation to prove that it did not use that power for a prohibited purpose. The committee was unconvinced that such a measure was appropriate at that stage.
The House of Representatives Standing Committee on Economics, Finance and Public Administration, 2001 (**“Hawker Committee”**)	Concluded that it preferred to await the outcome of further cases on section 46 before contemplating any change to the provision.
Senate Legal and Constitutional References Committee Inquiry into section 46 and s50 of the TPA, 2002	Deferred review of section 46 to the Dawson Committee.

Dawson Committee

Most recently, the Dawson Committee conducted a review of the competition provisions of the TPA and their administration. The report of the Dawson Committee was released by the Commonwealth Government on 16 April 2003. In relation to section 46, the Dawson Committee looked at the question of whether, as submitted by the ACCC and a number of other small business groups[16], the purpose test contained in the provision should be supplemented by an effects test. A key argument advanced by the ACCC for the proposed amendment was that section 46 had a limited application, due to the enforcement difficulties associated with proving the requisite purpose. The Dawson Committee recommended that no amendment should be made to section 46 based on the conclusion that:

- existing case law on section 46 does not substantiate the view that purpose is an unnecessarily onerous hurdle to prove;
- the addition of an effects test would increase the risk of regulatory error and render purpose ineffective as a means of distinguishing between pro-competitive and anti-competitive behaviour;
- overseas experience, insofar as it is of assistance, does not indicate that the introduction of an effects test would be appropriate; and
- cases presently before the courts provide an opportunity for the section to be further clarified and it would not be in the interests of consumers or competition to change the section at this stage.

In turn, the Commonwealth Government's response to the Dawson Committee's report acknowledged the extensive consideration given to possible amendments to section 46, by this and previous reviews, and agreed with the recommendation that no amendment should be made to section 46.

The Business Council endorses the Dawson Committee's findings and the views on which they were based.

2.5 Recent cases demonstrate that while section 46 continues to crystallise, the provision does capture misuses of market power

The Dawson Committee noted that there are a number of recently decided cases which have dealt with the interpretation of section 46 of the TPA and have provided further clarification of the scope and operation of the section.

The Business Council submits that these cases (some of which are summarised in **Appendix 3**) demonstrate that section 46, according to current judicial interpretation, is sufficiently clear at this time and is dealing with misuses of market power.

In particular, recent case law of the High Court and the Full Court of the Federal Court confirms that:

[16] See, for example, submissions made by the Council of Small Business Organisations of Australia Ltd (July 2002), the Fair Trading Coalition (July 2002) and the National Association of Retail Grocers of Australia ("**NARGA**") (July 2002).

- a corporation will contravene section 46 if is satisfies all three elements set out in the provision (see the *Boral* case, discussed below);

- market share is not the only determinant of market power. Depending on the competition dynamics in a given market, corporations may have a substantial degree of market power even with a relatively low market share; and

- a corporation having a substantial degree of market power takes advantage of that power when it engages in conduct which is only "materially facilitated" by the existence of that power.

Importantly, some of these cases are also being appealed, which will provide an opportunity for the section to be refined even further. The Business Council believes it would be premature for the Committee to recommend amendment to section 46 while the operation of the section continues to crystallise and while there is no clear evidence, at this stage, that the current section is flawed. To do so would subject businesses to an undesirable degree of uncertainty in their day-to-day conduct, whereas businesses should be able to reach decisions with a clear understanding of the nature and scope of their obligations.

***Boral Besser Masonry Ltd (now Boral Masonry Ltd) v ACCC*[17]**

- High Court decision - 2003

  Between April 1994 and October 1996, a Boral subsidiary ("**BBM**") sold a variety of building products including concrete masonry products ("**CMP**") at prices which, on some tenders, were substantially below its avoidable costs of production. This was at a time when the Victorian economy and the Melbourne building industry were in recession, there was excess capacity amongst producers of CMP in Melbourne, and there was growth in the popularity of competing products. The evidence demonstrated that customers were able to force the price of masonry products "down and down". BBM considered leaving the market but instead decided to stay, cut prices and increase efficiency. Accordingly, during this price war, BBM upgraded one of its plants, effectively doubling its capacity.

  A number of BBM's high level business plans and strategic documents revealed that these steps were taken to '*drive at least one competitor out of the market*', including a new, more efficient entrant to the market, C & M Brick (Bendigo) Pty Ltd ("**C&M**"). When one competitor, Rocla, withdrew from the market by the end of September 1995, BBM's Victorian Manager reported that '*part of BBM's strategic plan to reduce the number of masonry manufacturers in Victoria has been realised*'. The ACCC subsequently took action, alleging a contravention of section 46 of the TPA.

  At first instance, the Federal Court held that BBM did not have a substantial degree of market power but it did have one or more of the proscribed anti-competitive purposes. On appeal, the Full Court of the Federal Court held that BBM had contravened section 46. The Full Court of the Federal Court appeared to infer from the anti-competitive purpose that a company having such a purpose must have market power and would be using that power to achieve its purpose.

[17] (2003) 195 ALR 609.

On 7 February 2003, the High Court delivered judgment in BBM's appeal against the finding that it had misused its substantial power. The High Court found that BBM had not contravened section 46 when it engaged in a price war. The High Court found that while BBM participated in a price war with the purpose of eliminating competitors and achieving industry rationalisation, it did not have the requisite degree of market power to be in contravention of section 46.

- ACCC's response to decision

  The ACCC expressed disappointment with the High Court's decision, stating that the judgment raised questions as to the operation of section 46 in concentrated markets, with only a few major players[18].

However, the Business Council believes that the High Court's judgment does not preclude the successful enforcement of section 46 against corporations having a substantial degree of market power, which misuse that power for a proscribed purpose. Rather, the Business Council submits that the High Court's judgment reinforces the "traditional" view of section 46 and clarifies that each element (set out in paragraph 2.3 above) must be proved separately and sequentially. The High Court reversed the view of the Full Court of the Federal Court that having the purpose of defeating your competitor was enough to show market power.

In particular, the High Court's judgment confirms that a "*substantial degree of market power*" is an essential element of section 46 and this, in turn, will depend on the degree to which a business is constrained by its competitors, suppliers and customers. In this particular case, the High Court found that BBM did not have a "substantial degree of market power" for a number of reasons, including:

- barriers to entry in the market were relatively low;
- the customers of BBM were able to exercise countervailing power on BBM, C&M and the other players in the market; and
- there were numerous examples of BBM tendering unsuccessfully for contracts and winning contracts only after lowering initial bids in response to customer pressure.

The High Court found that evidence of the conduct of suppliers and customers demonstrated that the market was intensely competitive. In these circumstances, the High Court concluded that a company which has a substantial degree of market power may engage in vigorous price competition (even below cost) without necessarily using its market power. In effect, engaging in a price war is not a "taking advantage" of market power if those price cuts are driven by competitors or are something which a company without market power would undertake themselves.

If the High Court had dismissed BBM's appeal, the Business Council believes that Australian businesses would be subject to a high degree of uncertainty in their business dealings, particularly those operating in concentrated markets. Had *Boral* been decided differently, there would have been High Court precedent for analysing section 46 by beginning with an examination of the business' purpose in order to determine market power. According to this interpretation, a corporation which engaged in a vigorous

[18] *"High Court Decision Highlights Difficulties in Establishing Misuse of Market Power"* ACCC Media Release, 7 February 2003.

course of competitive conduct could risk contravening section 46 if a Court determined that it had a proscribed anti-competitive purpose and worked 'backwards' from that finding to determine, perhaps erroneously, that it had a substantial degree of market power. This uncertainty could deter businesses from engaging in vigorous competitive conduct, to the detriment of the competitive process.

However, by taking a traditional analysis of section 46, the High Court recognised that section 46 has three elements which should be addressed sequentially to determine whether the section has been contravened. The Business Council submits that this approach, which was followed by the Full Court of the Federal Court in *Universal Music*, is correct.

***Universal Music Australia Pty Ltd v ACCC*[19]**

- Full Court of the Federal Court's decision - 2003

  The Full Court of the Federal Court allowed the appeal against Hill J's decision that Universal Music Australia Pty Ltd ("**Universal**") and Warner Music Pty Ltd ("**Warner**") had contravened section 46 when they refused to supply stock to retailers who sold parallel imported compact discs. The Full Court held that in order to make out a contravention of section 46, a Court must consider as a threshold point whether the corporation has "a substantial degree of power in a market".

  Following the High Court's judgment in *Boral,* the Court held that determining whether a corporation has a substantial degree of power in a market requires attention to the whole of the evidence relating to the market and the conduct of its participants. It is not legitimate for a Court to base a finding of substantial market power simply upon incidents of abuse of power in that market. Almost all participants in a market have a degree of power, which may on occasions be abused.

  In this case, the relevant market was the market for wholesale recorded music in Australia. Universal and Warner had shares of 17.6% and 16% respectively of this market, which was characterised by low barriers to entry, a history of successful new entry and constraints exerted by the other major distributors and retailers. Accordingly, the Full Court concluded that the degree of power held by either Universal or Warner was not so significant as to warrant the description "substantial" within the meaning of section 46, as explained by the High Court in *Boral*.

- ACCC response to the decision[20]

  The ACCC stated that the decision further clarified the law regarding misuse of market power following *Boral* and the decision would send a strong message to those who would attempt to influence retailers against stocking parallel-imported CDs.

Accordingly, the Business Council submits that the High Court's judgment in *Boral,* which was followed by the Full Court of the Federal Court in *Universal Music,*

[19] [2003] FCAFC 193.

[20] "*Penalties more than doubled to over $2 million as Full Court upholds part of CDs decision*", ACCC Media Release, 22 August 2003.

demonstrates that section 46 is able to operate in a consistent manner. It is working, is able to be applied with sufficient certainty and captures a misuse of market power where, on the facts in question, a corporation satisfies each of the three elements set out in that provision. Indeed, the ability of section 46 to deal effectively with a misuse of market power in a concentrated industry is demonstrated by the Full Court of the Federal Court's decision in *Safeway*, in which Safeway was found to have contravened section 46. This is discussed below.

ACCC v Australian Safeway Stores Pty Ltd[21]

- Full Court of the Federal Court's decision - 2003

  Between 1994 and 1995, Safeway (in Victoria) imposed a condition on stocking bread made by manufacturers of Tiptop, Buttercup and Sunicrest brands ("**Plant Bakers**"). Some of the Plant Bakers supplied bread to independent retailers at a cheaper price than they were supplying it to Safeway. As a result of receiving cheaper bread, the independent retailers were able to undercut Safeway's retail price. Safeway threatened to cease stocking a Plant Baker's brands from the shelves of an individual Safeway store if the Plant Baker continued this conduct. The ACCC brought proceedings on the basis that Safeway had contravened section 46 of the TPA.

  On 30 June 2003, the Full Court of the Federal Court delivered judgment. The Court found that Safeway had misused its market power. There was no realistic possibility of a new entrant coming in the market to purchase the supplies that Safeway had boycotted. In addition, Safeway's state-wide operations created special barriers to entry.

  The Court held that Safeway had taken advantage of its power within the relevant market for a purpose proscribed by section 46 (1). The Court found that Safeway hoped to persuade the Plant Bakers to engage in anti-competitive conduct by dissuading them from supplying cheap generic bread to independent retailers. Safeway's activities were an indicator of substantial market power and Safeway had the ability to raise the cost of bread. One of its suppliers, Tip Top raised the price of bread it sold to the independent retailers. The Court held that market share was also a factor. Safeway purchased 20% of bread in Victoria - the largest individual purchaser of bread in the market. The excess capacity of the bakers meant that a reduction in purchases by Safeway could not be replaced by sales to another organisation.

  In reaching its decision, the Full Court of the Federal Court explicitly applied the High Court's decision in *Boral*.

- ACCC's response to decision

  The ACCC welcomed the Court's decision. It noted that in this judgment the Court appeared to place more emphasis on the actual conduct of Safeway rather than Safeway's stated policy. Since judgment, both the ACCC and Safeway have appealed to the High Court[22].

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[21] (2003) 198 ALR 657

[22] *"Bread Decision - Full Court holds Safeway Engaged in Price Fixing, Misused its Market Power in Some Instances"* ACCC Media Release, 30 June 2003

The Business Council submits that it is appropriate, and preferable, to allow the law to continue to develop and crystallise in this way, as opposed to recommending potentially premature amendments to section 46.

2.6 Suggested reforms to section 46 are not warranted

Prompted by perceived difficulties with the operation of section 46 in protecting small business from anti-competitive conduct, small business groups have suggested that section 46 of the TPA should be amended to take account of those particular interests. Proposals which have been suggested on a number of occasions includes a specific legislative prohibition on predatory pricing.

In its submissions to the Dawson Committee's review of the TPA, the ACCC also proposed that section 46 be amended to incorporate an effects test, arguing perceived enforcement difficulties and inconsistency of Australian law with overseas experience. This view has also been supported by a number of small business groups.

Specific legislative prohibition against predatory pricing

The Business Council is opposed to a specific legislative prohibition against predatory pricing, as the application of such a provision could undermine the fundamental objective of the TPA to enhance the welfare of Australians through the promotion of competition.

Experience in Canada

Advocates of a prohibition against predatory pricing have looked to section 50 of Canada's *Competition Act* in support of their proposal for reform. Section 50 of the *Competition Act* prohibits firms from:

> "*selling products at prices unreasonably low, having the effect or tendency of substantially lessening competition or eliminating a competitor or designed to have that effect*".

Setting aside the argument that consistency with overseas approaches is, in itself, a questionable basis for justifying a similar provision in Australia (see Section Six of this submission), experience in Canada suggests that enforcing a provision of this type may give rise to considerable difficulties. In particular, a recent Canadian parliamentary inquiry found that:

- the provision is rarely used by the regulator;
- predatory pricing is very difficult to prove (there have only been two contested cases); and
- most importantly, the provision (in its current form) offends against the overriding spirit of Canada's competition legislation, that is the protection of competition and not competitors[23].

The Canadian Standing Committee on Industry ("**Standing Committee**") noted that there was considerable debate among economists about what constituted predatory pricing. The Standing Committee found that a number of examples presented to it that might appear to

[23] *Interim Report on the Competition Act* - Report of the Standing Committee on Industry, 13 April 2000 - available at http://www.parl.gc.ca.

be predatory pricing, based on the definitions typically used, but which in fact were sensible commercial strategies that benefited consumers, including:

- airlines that offer super-cheap tickets on scheduled flights, to avoid having empty seats; and
- Amazon.com, which consistently prices below cost as an investment in future market share.

The Standing Committee concluded that often it can be "*extremely difficult to distinguish predatory pricing from aggressive price competition*"[24] and that "*economic theory, as a practical guide to enforcement of predatory pricing, leaves something to be desired*". An independent report[25] commissioned by the Standing Committee found that:

> *"Predatory pricing…is really by far the most difficult kind of anticompetitive behaviour for which to work out appropriate rules"*
>
> and
>
> *"…it's very difficult to use this provision as a reliable guide to distinguish aggressive competition that results in the reduction of prices from predatory pricing…in most circumstances it means you have to make a prediction about how the market's going to work."*

As a result, the Standing Committee recommended that the Canadian Government should repeal the predatory pricing provisions[26] of the *Competition Act,* and instead rely on the provision dealing with an abuse of a dominant position[27]. In effect, the Standing Committee recommended repealing the specific predatory pricing provision and relying on the Canadian equivalent of section 46 of the TPA. The Canadian Government has recently issued a discussion paper which deals, amongst other matters, with the reform of the predatory pricing provisions. It is expected that the outcome of the consultation process will be made known later this year.

Difficulties with proscribing predatory pricing

The findings of the Canadian Standing Committee confirm business fears that attempts to specifically proscribe predatory pricing introduce considerable uncertainty into competition law. This creates legal risks for businesses of all sizes and actively discourages businesses from engaging in robust price competition, to the detriment of consumers.

There is also a concern that some may be taking a simplistic approach to the concept of predatory pricing. One advocate of a specific provision on predatory pricing has dismissed business concerns about uncertainty by claiming that the:

> "… *distinction between price competition and predatory pricing is widely recognised. A fundamental element of predatory pricing is pricing below cost. In*

[24] *A plan to modernize Canada's competition regime* - Report of the Standing Committee on Industry, Science and Technology, April 2002 - available at http://www.parl.gc.ca.

[25] Report of J. Anthony VanDuzer and Gilles Paquet.

[26] Sections 50(1)(b) and 50(1)(c).

[27] Section 79 *Competition Act.*

our view, this represents a clear 'bright line' between legitimate and illegitimate conduct"[28].

In contrast, Professor Stephen Corones has stated:

"*There is a vast literature in the United States and Europe on the topic of predatory pricing and how one proves its existence. Predatory pricing is sometimes referred to as "below cost pricing" but courts and commentators disagree as to the appropriate measure of costs.* ***Fixed costs*** *are costs which remain constant despite changes in output…* ***Variable costs*** *are costs which vary with changes in output…* ***Total cost*** *is the sum of fixed and variable costs.* ***Average cost*** *is the total cost divided by output.* ***Marginal cost*** *is the addition to costs resulting from the production of an additional unit of output.* ***Average variable cost*** *is regarded as a substitute for marginal cost*". (emphasis added)[29]

The practical and conceptual difficulties associated with proscribing predatory pricing are illustrated by how the law surrounding predatory pricing has evolved in the United States. In the United States, an influential paper by Areeda and Turner[30] argued that pricing below average variable cost ("**AVC**") should be *per se* illegal ("**Areeda-Turner rule**"). Some commentators have noted that this approach appeared to be the basis of the ACCC's arguments in *Boral*.

However, looking simply at whether a corporation prices below AVC may be problematic. As discussed in *Boral*, there could be a number of reasons why a corporation might rationally, without an anti-competitive purpose, choose to price below AVC. For example, pricing below AVC could be the least costly (and most commercially) attractive option open to a corporation.

To take account of these practical difficulties, the law in the United States has developed beyond the Areeda-Turner rule and the Courts now require independent evidence that consumers will suffer. Accordingly, the Courts will look to some kind of recoupment to establish a strong likelihood of consumer harm.

This example, together with other extensive literature and analysis by economic and legal experts, seems to suggest that there is little certainty around what may constitute predatory pricing, let alone how to capture that in black letter law.

Legislative prohibition against predatory pricing could be likely to have adverse consequences for competition

Vigorous price competition can have real benefits for consumers (customers in the telecommunications sector being a recent example) and represents the very essence of competition. Competition is a ruthless process and firms will often try to damage each other in the competitive process by price cutting. This was recognised by the High Court in *Boral,* when it found that:

"*where the conduct that is alleged to contravene section 46 is price cutting, the objective will ordinarily be to take business away from competitors. If the*

[28] Senator Stephen Conway, "*BCA Dummy Spit on Predatory Pricing*", Media Statement, 20 June 2003.

[29] Corones, S G *Competition Law in Australia*, 1999, LBC Information Services, Sydney at p 345.

[30] P. Areeda and D. Turner *"Predatory Pricing and Related Practices under Section 2 of the Sherman Act"* 88 Harvard L. Rev 697 (1975).

objective is achieved, competitors will necessarily be damaged…. that is inherent in the competitive process".

Even if it were possible to arrive at a workable definition appropriate for Australia's economy, a prohibition against predatory pricing could actually stifle competition (and undermine the objective of the TPA) by deterring businesses from engaging in price competition for fear of contravening the prohibition. Predatory pricing provisions could even have the unintended consequence of encouraging price fixing or collusion as businesses may try to make arrangements so that they do not unintentionally undercut each other.

The Canadian Standing Committee also expressed concern that the predatory pricing provision "*offends the overriding spirit of the Competition Act, which is to preserve the process of competition and not competitors specifically*". The Committee found that the misplaced interpretation that competition law should protect competitors was compounded by a specific provision on predatory pricing. It quoted with approval the view of one academic that:

"… this section of the Act leads firms who have been unable to survive market competition into believing that they have a valid predatory pricing claim. It leads to cases which are frivolous from an economics point of view"[31].

The Business Council submits that section 46 in its current form is as well equipped as any provision could be to deal with the different types of conduct which may constitute a misuse of market power, including predatory pricing. The point at which competitive behaviour becomes anti-competitive is extremely difficult to define in the abstract and, accordingly, to express in a legislative provision.

The Business Council considers that section 46, as it currently stands, equips the courts to draw the distinction between vigorous pro-competitive conduct and unlawful anti-competitive conduct to arrive at commercially appropriate decisions, based on the realities and dynamics of the particular market. For example, in their joint judgment in *Boral*, Gleeson CJ and Callinan J stated that:

"*If one begins with the fact that a firm is a monopolist, or is in a controlling or dominant position in a market, then by hypothesis, such a firm has an ability to raise prices without fear of losing business. If such a firm reduces its prices, especially if it reduces them below variable cost, then it may be easy to attribute to the firm an anti-competitive objective, and to characterise its behaviour as predatory. But if one finds a firm that is operating in an intensely competitive environment, and a close examination of its pricing behaviour shows that it is responding to competitive pressure, then its conduct will bear a different character. That is the present case*"[32].

Similarly, Gaudron, Gummow and Hayne JJ quoted from the explanatory memorandum to the *Trade Practices Revision Act 1986* (Cth), which stated:

"*Kinds of conduct which in certain circumstances could be in breach of the provision would include… predatory pricing. These instances are indicative only and, in each case, it would be necessary to establish the requisite degree of*

[31] Op cit 24

[32] *Boral* [2003] HCA 5 at [129].

market power and that advantage had been taken of the power for one of the specified purposes"[33].

The High Court acknowledged that section 46 is capable of catching predatory pricing. Given the difficulties likely to arise out of a specific prohibition against predatory pricing, the Business Council submits that amending the TPA to incorporate a predatory pricing provision is unnecessary and would be likely to subject all Australian businesses, irrespective of their size, to uncertainty in their business dealings, while increasing the likelihood (and associated costs) of regulatory error.

An effects test in section 46

Incorporating an effects test into section 46 of the TPA has been suggested as a way of alleviating perceived difficulties in proving a contravention of section 46, or as providing a more appropriate way of distinguishing legitimate competitive conduct from anti-competitive conduct.

An effects test would encompass behaviour that, regardless of a legitimate purpose for the behaviour, has a substantially adverse impact on a competitor or competition.

The Business Council submits that the current provision is working appropriately and that change would create considerable and unnecessary uncertainty regarding the operation of the provision.

As noted in Section One of this submission, certainty of the law is an essential pre-requisite for high levels of compliance with the law and confidence in commercial dealings. Compliance with the TPA requires line and operational managers, as well as corporate counsel and legal advisers, to have a clear understanding of the decisions and conduct that are likely to contravene or raise issues under the TPA. This is particularly the case with section 46, where the line between robust competition and anti-competitive conduct can be a fine one.

From a legal perspective, in light of the level of pecuniary penalties which may be imposed on a corporation found to have contravened section 46 (that is, a financial penalty of up to $10 million per contravention for corporations and up to $500,000 per contravention for individuals[34]), corporations should be in a position to know, with some degree of certainty, what is lawful before engaging in a particular course of conduct.

A purpose test requires specific evidence to be adduced of the purpose, or sufficient evidence of surrounding circumstances to allow an inference to be drawn about the purpose. By comparison, drawing conclusions about whether unilateral conduct is likely to have a prescribed effect on a competitor or competition requires a complex analysis of market definition and the forecasting of potential effects on competitors and competition. Accordingly, there is also likely to be a higher rate of regulatory error in applying an effects test than in applying a purpose test.

Protecting competition, not competitors

The ACCC has previously sought to introduce an "effects" test while retaining the three paragraphs of section 46(1). The test, therefore, becomes one of the effect of conduct

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[33] *Boral* [2003] HCA 5 at [165].

[34] Section 76 of the TPA. In addition, damages and injunctive remedies are available under sections 80 and 82 and remedial orders under section 87.

upon competitors and potential competitors in a market. This approach would entrench a view that section 46 is about the protection of specific competitors, rather than the protection of competition. This is inconsistent with judicial interpretation of the section, which focuses on the role of protecting the dynamic state of competition.

In the Business Council's view, there is a risk that if section 46 is cast to protect competitors, it will result in inefficient or less competitive players being protected from robust competition, resulting in a decrease in competition overall. Such a result is undesirable from the point of view of the overall efficiency of the Australian economy, and from the point of view of consumers.

The following hypothetical examples further illustrate how an effects test could result in unintended consequences:

- *Hypothetical – Conduct with the effect of preventing new entry*

  Pharmacorp is an ASX listed company and manufactures a range of pharmaceutical products. Pharmacorp has achieved a substantial degree of market power through its efficient operations, its use of innovative technology and research methods and its commitment to R&D. The market in which Pharmacorp operates is relatively mature and Pharmacorp has enjoyed a relatively high and stable market share for a number of years although there are two smaller rivals operating in the same market, one of which is Medico.

  Given Pharmacorp's mature market share and limited opportunities for growth, Pharmacorp decides to diversify its operations into a related market in order to achieve satisfactory returns for its shareholders. Accordingly, it dedicates significant amounts of expertise and commits substantial funds to the research and development of a revolutionary new treatment, Wonderdrug. Pharmacorp supports the launch of Wonderdrug with a vigorous marketing campaign and, thanks to its industry-wide brand recognition, the new product quickly achieves high levels of market penetration and becomes the leading treatment in its market.

  Unbeknown to Pharmacorp, one of its rivals, Medico, had also embarked upon research and development into a similar drug therapy. However, upon learning of Pharmacorp's product and witnessing its success in the market, Medico decides to abandon the development of its own competing product.

  Pharmacorp took advantage of or used its market power, particularly its brand recognition, to achieve a high level of market penetration ahead of its rivals. Pharmacorp did not develop its new product with the purpose of preventing any other person from entering the market or, for that matter, deterring or preventing a person from engaging in competitive conduct. Rather, Pharmacorp developed its product with a view to diversifying its operations and achieving satisfactory returns for its shareholders. No anti-competitive purpose could be inferred and all Pharmacorp's internal documents supported Pharmacorp's legitimate commercial rationale for developing and launching the product. Nevertheless, the degree of market penetration achieved and high market share by Pharmacorp's new product could only have been achieved by Pharmacorp using its market position, 'deep pockets' and its brand awareness amongst consumers.

  The ultimate *effect* of Pharmacorp's use of its market power has been to prevent a new player from entering the market, with the apparent effect of reducing competition whereas, in reality, Pharmacorp launched a new product and thereby

increased consumer choice. Nevertheless, pursuant to an effects test, proceedings could be brought against Pharmacorp for engaging in anti-competitive conduct.

- *Hypothetical – Conduct with the effect of damaging/eliminating a competitor*

  Fizz soft drinks are the second most popular soft drink in Australia. Fizz Limited supplies Fizz soft drinks to ACME convenience stores, whose major product lines are soft drinks and snack foods. However, ACME has not been displaying Fizz soft drinks according to Fizz's retail guidelines. ACME does not display Fizz promotional material appropriately, does not supply refrigerated Fizz as required and does not re-stock the shelves promptly with Fizz when they are empty.

  As a result, Fizz sales by ACME convenience stores are very poor compared to other channels of distribution. Fizz decides to terminate supply to ACME convenience stores and plans to rely on sales from nearby Fizz vending machines instead. The Fizz vending machines make Fizz a technical competitor of ACME convenience stores.

  ACME has been poorly managed for some time and as a result has been struggling to remain commercially viable. Due to its inability to sell the popular Fizz soft drinks, ACME stores lose further business and its losses force it to exit the market. ACME accuses Fizz Limited of misusing its market power by changing its distribution network to eliminate or substantially damage ACME convenience stores.

  Under the current section 46 test, Fizz Limited's purpose is not a prohibited one - it simply wanted to protect the value of its product and the integrity of its brand. However, under an effects test, Fizz Limited may have contravened section 46 as its conduct produced the *effect* of ACME going out of business, even though its purpose was commercially legitimate.

- *Hypothetical – Conduct with effect of deterring competitive conduct*

  Over the last 10 years, Cyber Limited has grown to become one of the largest manufacturers of software in Australia. Its success is a combination of strategic management, efficiency and innovation. Accordingly, its software is very popular with consumers and retail stores are very keen to stock Cyber Limited's products.

  As a result, Cyber Limited enjoys considerable bargaining power when it comes to retailers, and receives significantly better trading terms than most of its smaller rival manufacturers. Many retail stores reserve more shelf space for Cyber Limited's products and, due to high turnover, mark up the cost price by only 10% for Cyber Limited's products whereas other products receive a mark-up of 15%. Some of the major retailers allow considerable shop space to be taken up by Cyber Limited's promotional material and display computers, whereas other manufacturers are charged a fee for such an arrangement.

  This means that many of the smaller manufacturers find it more expensive and more difficult to compete with Cyber Limited. They accuse Cyber Limited of misusing its market power with the effect of deterring or preventing competitive conduct as they cannot obtain comparable shelf space.

  Under the current purpose test in section 46 of the TPA, it could be argued that Cyber Limited's conduct is intended to reduce its costs and to increase

efficiencies, which is pro-competitive and not intended to prevent competitive conduct. However, under an effects test, this pro-competitive purpose may become irrelevant if it can be shown that Cyber Limited's conduct had the *effect* of preventing other manufacturers from engaging in competitive conduct.

A "substantial lessening of competition" threshold

The Business Council submits that introducing an effects test limited by a threshold of "substantially lessening competition" does not address the principal concerns with an effects test.

While this approach would correctly focus section 46 on the protection of competition rather than the protection of competitors, it would not overcome the increased uncertainty an effects test introduces. In other parts of the TPA, such as the mergers test in section 50, determining whether a proposed action will substantially lessen competition can involve detailed economic analysis and market inquiries, highlighting that determining the competition impact of actions is a complex matter.

The argument also fails to appreciate that vigorously competitive **unilateral** conduct is, as the High Court has recognised, "*by its very nature ... ruthless*"[35]. In this light, section 46 needs to be able to distinguish actions of companies that create efficiency and increase welfare, even though their effect is damaging to competitors. For example, if one firm can take advantage of its market share to invest in new technology that enables that firm to cut prices substantially, then the effect might well be damaging to competitors. But customers, and the economy, may be much better off as a result of that investment. The TPA, therefore, uses the purpose test to ensure that welfare-enhancing conduct with the effect (but not the purpose) of harming competitors is not proscribed. The fact that a company fails and exits a market should not automatically lead to the conclusion that it has been the victim of misuse of market power by a larger competitor.

Moreover, the hypothetical examples demonstrate that conduct could be in contravention of a substantial lessening of competition effects test despite being unobjectionable and even socially desirable. They also show that, notwithstanding the requirement that a substantial degree of market power be taken advantage of, a firm could contravene a provision based on an effects test inadvertently.

It has been argued that these concerns can be overcome through allowing the authorisation or notification of conduct that may contravene an amended section 46. However, these arguments do not recognise the impracticality of requiring companies to seek the approval of the regulator before engaging in day-to-day competitive conduct and the extra costs that would be involved.

Replacing paragraphs 46(a), (b) and (c) with a "substantial lessening of competition" test is, therefore, **not** a compromise position that would remove or even significantly reduce the serious practical problems and uncertainty that would result from an "effects" test in section 46. This has been acknowledged by the then ACCC Chairman, Professor Fels, who noted that:

> "[An effects test] *is also likely to create greater uncertainty for business. That is compounded by the fact that section 46 in its present form, because it has a purpose test, is far less likely to catch unintended behaviour. In other words, a*

35 *Queensland Wire* (1988) 167 CLR 177 at 191.

firm may innocently be competing and unknowingly breaching a section 46 effects test"[36].

Market share and market power

The Business Council believes that market power should not be defined by reference to market share thresholds, or market concentration thresholds, alone.

A corporation which has market power has the ability to behave in a market in a manner not constrained by its competitors for a sustained period of time. This is sometimes described as the ability to "give less and charge more".

Section 46(3) of the TPA requires a Court, in assessing the market power of a corporation, to take into account the extent to which the corporation is constrained by the conduct of its competitors, potential competitors or by its suppliers or those to whom it supplies goods or services. In addition, the matters set out in section 46(3) are not exhaustive[37].

Accordingly, while market share may be relevant to showing market power, the height of barriers to entry and the countervailing power of competitors, customers and suppliers are all relevant factors which determine whether a corporation has market power[38]. A large market share does not necessarily equate the ability to act unconstrained in a market.

Recently decided cases demonstrate that defining market power solely by reference to market share is not the approach the Courts adopt. In *Boral,* the High Court held that BBM did not have a substantial degree of market power for a number of reasons, including relatively low barriers to entry and evidence which showed that BBM's customers exerted countervailing power on BBM and other players in the market (C&M's market share grew to 40% during the period of BBM's alleged contravention of section 46). In *Universal Music,* the Full Court of the Federal Court found that Universal and Warner did not have a substantial degree of market power because the other major distributors, importers and overseas exporters exerted competitive constraints, barriers to entry were not high and large retailers exercised countervailing power. However, in *Safeway*, the Full Court of the Federal Court found that Safeway **did** have a substantial degree of power (even though it only had about a 20% market share), given particular features of the relevant market, including high barriers to entry.

Importantly, in the 1960s, a market threshold test existed in Australia. In the *Trade Practices Act 1965,* the precursor to section 46 contained a threshold test of *"one-third by quantity or value of the goods (including imported goods) or services of that description that are supplied in Australia or in that part of Australia*"[39]. This test was abandoned because it had been found to be unworkable. In his second reading speech when introducing the 1974 Act, Attorney General Lionel Murphy said that[40]:

"*A monopolist for this purpose is a person who substantially controls a market. The application of this provision will be a matter for the Court. An arithmetical*

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[36] Australia, Joint Select Committee on the Retailing Sector, *Hansard*, 13 July 1999, at 1161.

[37] *TPC v Pioneer Concrete (Qld) Pty Ltd* (1994) ATPR 41-345.

[38] This was confirmed in the recent *Boral* case and the Full Court of the Federal Court's decision in *Universal Music* where it was said at [132] that "*In Boral, the High Court emphasised that [section 46(3)], which is mandatory in terms, is central to a determination about the existence of market power*".

[39] *Trade Practices Act* 1965 s 37(4)(b).

[40] Australia, Senate *Hansard*, 30 July 1974 at 544.

test such as one-third of the market - as in the existing legislation - is unsatisfactory. The certainty which it appears to give is illusory."

The test was abandoned because it did not work in an increasingly complex 1970s economy. The Business Council believes it will be even less helpful in today's dynamic economy with new innovative technology-based industries and, moreover, would run counter to the accepted economic principles (in other jurisdictions as well as Australia) that market power requires an absence of constraint.

In addition, seeking to determine market power by reference to market share alone would also run counter to the approach adopted by the ACCC in its own Merger Guidelines. When assessing a merger under section 50 of the TPA, the ACCC acknowledges that market share is only the starting point of its investigation and will also evaluate a number of other market conditions, including the height of barriers to entry and the existence of countervailing power.

2.7 Other proposals

An alternative proposal has been put forward to amend section 46(7) to make it explicit that the purpose of a corporation can be inferred from the effect of its conduct[41]. The Business Council understands that under the current section 46(7), which allows a court to infer purpose from the conduct of a corporation, or from other relevant circumstances, it is already open to a court to infer purpose from the effect of the conduct[42]. The Business Council does not, therefore, see the need to make any change but would not oppose it.

It has also been suggested that section 46 should be "codified", by enumerating the types of conduct that may contravene the section. However, the Business Council believes that codification may give rise to practical difficulties (such as arriving at a workable definition of economic concepts, like predatory pricing) and would run contrary to the intentions behind the TPA itself. The TPA provides a balance between legal and economic considerations and there are good reasons to avoid codification. As Attorney General Murphy observed[43]:

"Legislation of this kind is concerned with the economic considerations. There is a limit to the extent to which such considerations can be treated in legislation as legal concepts capable of being expressed with absolute precision. Such an approach leads to provisions which are complex in the extreme and give rise to more problems than they remove."

Rather, the Business Council submits that the current formulation of section 46, at this point in time, preserves a greater degree of flexibility and enables section 46 to deal with misuses of market power in a variety of ways.

2.8 Conclusion - there is insufficient evidence to suggest reform is necessary

The Senate Committee has been asked to consider whether the TPA adequately protects small businesses from anti-competitive or unfair conduct, with particular reference to whether section 46 deals effectively with abuses of market power by big businesses. If not, the Senate Inquiry has been asked to consider the implications of the inadequacy of section 46 for small businesses, consumers and the competitive process.

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[41] See, for example, the submission of the National Farmers' Federation (June 2002, p 18).

[42] See, for example, *Melway* (2001) 205 CLR 1 at 37-38 [94]

[43] Australia, Senate, *Hansard* 20 July 1974 at 542

The Business Council submits that section 46, in its current form (and according to current judicial interpretation, which affirms that the provision is concerned with protecting competition, and not competitors) is sufficiently clear and effectively 'polices' misuses of market power. Recent decisions handed down by the High Court and the Full Court of the Federal Court have clarified the scope of the provision, including the principles that:

- a corporation will contravene section 46 if it satisfies the three elements set out in the provision;
- market share is not the only determinant of market power and depending on the market in question, corporations having a relatively low share may have a "substantial degree of market power"; and
- a corporation takes advantage of its market power where it does something that is only "materially facilitated" by the existence of the power.

Therefore, it is clear that a corporation with a substantial degree of market power may compete in the same way as other corporations (large and small) but may not "go further" and misuse that power. These principles facilitate the enforcement of section 46, while enabling all corporations to engage in vigorous competition which benefits the Australian economy and Australian consumers. The various proposals for amending section 46 that have been put forward by certain sectors would upset this balance and by increasing uncertainty and regulatory risk, would have negative consequences for competition in Australia.

Accordingly, the Business Council considers that there is not sufficient evidence (particularly at a time when several important cases are being appealed) to justify the Committee recommending an amendment to the section. Rather, the Business Council submits that it would be prudent to await the outcome of those decisions before evaluating whether any refinement, by way of legislative amendment, is necessary. To the extent that certain sectors have raised substantive concerns, the Business Council believes that these may be dealt with more appropriately by industry codes of conduct. These are discussed in Section 4 of this submission.

3 The unconscionable conduct provisions in Part IVA

3.1 Key points

- The Business Council supports the current unconscionable conduct provisions under the TPA, which provide small business with effective protection from unconscionable or unfair conduct in business transactions.

- Under Part IVA of the TPA, small businesses may have recourse to two key provisions. Of these, section 51AC was recently enacted with the purpose of better protecting small business from unconscionable or unfair conduct.

- Although the law is without doubt still developing, the early indications, including cases won by the ACCC, are that the section is achieving its purpose. Accordingly, the Business Council submits that it would be premature for the Committee to recommend an amendment to, or expansion of, Part IVA while section 51AC is "bedded down". The Business Council believes it is appropriate to allow the courts to continue to develop the relevant principles and to allow precedent to be refined. To this end, the Business Council notes that there are 6 cases under section 51AC currently before the Courts, the outcome of which will clarify the scope of the section even further. The Business Council submits that it is also important to acknowledge that many complaints which may fall within the scope of section 51AC are resolved informally, without litigation.

- Rather, to intervene at this stage (for example, by recommending that section 51AC incorporates a test of "unfairness") would subject all businesses (large and small) to undue uncertainty in their commercial dealings. This uncertainty would be likely to have negative implications for the operation of competitive markets, the Australian economy and Australian consumers.

3.2 Structure

This section of the Business Council submission will examine:

- the protection offered to small business by Part IVA of the TPA; and

- recent cases on section 51AA and section 51AC, which demonstrate that Part IVA is well equipped to deliver successful results for small business.

3.3 The protection offered to small business by Part IVA of the TPA

The Business Council considers that Part IVA of the TPA already provides small business with effective protection from unconscionable or unfair conduct in business transactions. Under Part IVA, small businesses may have recourse to two key provisions, including section 51AC, which was recently enacted specifically to protect small business from unconscionable conduct. Each provision will now be considered in turn.

Section 51AA

Section 51AA prohibits corporations engaging in unconscionable conduct within the meaning of the "unwritten law". This prohibition does not apply to conduct which falls within sections 51AB or 51AC of the TPA.

Section 51AA was inserted by the *Trade Practices Legislation Amendment Act* 1992 ("**1992 Act**"). Following the report of the Reid Committee in 1997, the Government considered inserting a provision into the TPA prohibiting unfair conduct against small business. In arguing for the use of the word "unfair" rather than "unconscionable", the Reid Committee stated that the word "unfair" was intended to encompass the words "unconscionable", "harsh" and "oppressive"[44].

This proposal was not adopted. Parliament determined that the term "unfair" was too broad and indiscriminate. Rather, Parliament preferred the expression "unconscionable conduct" in order to build on the existing body of case law, an approach which had worked well in the context of the consumer protection provisions of the TPA.

Parliament did, however, provide for specific remedies for a contravention of unconscionable conduct provisions and in this respect broadened the common law doctrine of unconscionability.

The net effect is that section 51AA precludes large business taking action for reasons other than legitimate commercial interests. The rights of small businesses therefore mirror those of consumers.

Section 51AC

Section 51AC prohibits a corporation from engaging in unconscionable conduct in business transactions involving the supply to or acquisition from a person, other than a listed company, of goods or services of under $3 million.

Section 51AC provides small business with broader legal protection against unconscionable conduct than section 51AA. Under section 51AC, a court may take into account a wide range of circumstances when determining whether a business has been subjected to unconscionable conduct, which goes beyond the interpretation of "unconscionability" in section 51AA. The court may consider:

- the parties relative commercial strengths;
- whether undue influence was exerted;
- whether the contract exceeded what was reasonably necessary for the legitimate interest of the larger business;
- the requirements of any applicable industry code; and
- whether there was evidence of disclosure, good faith and willingness to negotiate.

Remedies under Part IVA

The ACCC, the Australian Securities & Investments Commission (in relation to unconscionable conduct in the financial services industry) or individuals can bring proceedings under Part IVA seeking injunctions, damages or other remedial orders under Part VI of the TPA.

[44] The Reid Committee at 180 [6.72].

3.4 Recent cases on sections 51AA and 51AC demonstrate that Part IVA offers effective protection to small business

Introduction

Recent cases on sections 51AA and 51AC demonstrate that Part IVA of the TPA is well equipped to offer small business effective protection from unconscionable or unfair conduct in their business dealings.

According to current judicial interpretation, section 51AA protects small business from conduct which falls within the scope of the common law doctrine of unconscionability[45].

In addition, cases brought under section 51AC indicate that this provision affords small business more extensive protection from unconscionable and unfair conduct than that available under section 51AA, the common law, or equity[46].

Section 51AA cases

ACCC v CG Berbatis Holdings Pty Limited[47] *("**Berbatis**")*

In *Berbatis*, the ACCC took action under section 51AA on behalf of Mr and Mrs Roberts, the lessees of a fish and chip shop, who wanted to renew their lease in a small shopping centre. There was no obligation on the lessor to renew the lease. The Roberts were keen to renew as they wanted to sell their business and assign the lease to a new purchaser. The value of their business without a new lease was small. The Roberts found a purchaser who signed an offer to purchase, subject to a lease being assigned to his satisfaction. The Roberts had earlier commenced an action with other tenants against the owners of the shopping centre on the ground that they had been overcharged levies.

In negotiating the deed of assignment, the lessors required the inclusion of a clause whereby the Roberts would consent to the dismissal of any current legal proceedings against the owners. In 1998, the ACCC instituted proceedings against Berbatis, alleging that the imposition by them of conditions requiring withdrawal by the Roberts of their participation in pending legal proceedings, as a condition of the grant of a new lease, contravened section 51AA of the TPA.

At first instance, French J found for the ACCC, declaring the condition to be unconscionable. On appeal, the Full Court of the Federal Court reversed his Honour's findings and found that there was no special disadvantage when a lessee (without an option to renew) wished to obtain a fresh lease with the effect that the landlord took advantage of the situation to obtain a business advantage.

The ACCC appealed this decision to the High Court. The High Court delivered judgment on 9 April 2003 and held that uneven bargaining power, on its own, was not caught by section 51AA.

The High Court found that "unconscionable conduct" has a technical meaning developed by judges over time. This technical meaning does not reflect its "*ordinary or natural meaning in general usage*"[48]. Rather, the term refers to "*various grounds of equitable*

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[45] *ACCC v CG Berbatis Holdings Pty Ltd* (2003) 197 ALR 153

[46] *ACCC v Simply No-Knead (Franchising) Pty Ltd* [2000] FCA 1365

[47] (2003) 197 ALR 153

[48] (2003) 197 ALR 153 at [38]

intervention to refuse enforcement of or to set aside transactions which offend equity and good conscience"[49].

The Explanatory Memorandum makes clear that section 51AA has a specific meaning outlined in a series of cases. In those cases, as in *Berbatis*, the form of unconscionability under consideration was "*the knowing exploitation by one party of the special disadvantage of another*"**.** The High Court also found that in this case, no "special disadvantage" existed, only uneven bargaining power.

A "special disadvantage" refers to a "*disabling condition or circumstance … which seriously affects the ability of the innocent party to make a judgment as to his own best interests*"[50]. The characteristics of disadvantage may include, but are not limited to:

- poverty or need of any kind;
- sickness or infirmity of body or mind;
- age;
- sex;
- drunkenness;
- illiteracy or lack of education, or ignorance;
- lack of assistance or explanation where assistance or explanation is necessary; and
- inexperience.

When might a person not be in situation of "special disadvantage"?

The High Court applied the facts of this case and indicated a series of criteria which do not indicate special disadvantage:

- uneven bargaining power, on its own;
- an inability to get one's own way;
- the disadvantaged party being a business person who had their own financial interests;
- the presence of legal advice;
- a rational decision; and
- an ability to judge or protect the financial interests of the "disadvantaged" party.

Proper scope of section 51AA

It has been suggested that the decision of the High Court in *Berbatis* has rendered Part IVA ineffective in protecting small business from unconscionable or unfair conduct. However, the Business Council submits that this is not the case. In the Business

[49] (2003) 197 ALR 153 at [42]

[50] (2003) 197 ALR 153 at [12]

Council's view, the High Court in *Berbatis* confirmed that section 51AA provides small businesses with protection from conduct which falls within the scope of the unwritten law.

Moreover, the Business Council notes that section 51AA was never intended to apply to all cases of unconscionable conduct. This was acknowledged by Parliament and section 51AC was enacted to provide small business with extended protection against unconscionable or unfair conduct. Indeed, following the High Court's decision in *Berbatis*, the then chairman of the ACCC, Professor Fels, stated:

> "*While this matter was taken under previously existing provisions of the Act, a new provision, section 51AC, which came into effect from 1 July 1998, provides an improved level of legal protection for small businesses. It does not rely simply upon the 'unwritten law'. Section 51AC mirrors for small businesses the rights previously enjoyed by consumers and incorporates a range of additional matters that the Court can consider in order to ensure that small businesses are protected from unconscionable conduct in their dealings with large businesses*" [51].

Section 51AC cases – the section works

The Business Council submits that the experience to date with cases under section 51AC demonstrates that the provision is well equipped to provide small business with protection from unconscionable or unfair conduct.

The case law under this section is in the early stages of development. Nonetheless, current judicial interpretation indicates that the list of factors a Court may take into account when determining whether a business has engaged in unconscionable conduct results in broader protection than under the common law, equity or section 51AA[52].

An overview of successful cases brought by the ACCC is at **Appendix 4.** In summary, these cases demonstrate that there may be a contravention of section 51AC where:

- conduct is "*unreasonable, unfair, harsh, oppressive and wanting in good faith*"[53];
- the business engaging in unconscionable conduct is exercising contractual rights[54]; and
- the business engaging in unconscionable conduct fails to comply with an industry code[55].

These cases have resulted in the award of a range of remedies, including compensation, injunctions and court-enforceable undertakings. In addition, it is important to remember that many small business complaints which might fall within the scope of section 51AC are resolved informally.

The Business Council submits that in light of experience at this formative stage, it would be premature for the Committee to recommend an amendment to, or extension of, Part IVA. The Business Council understands that the ACCC currently has 6 cases under

[51] Allan Fells, "High Court Dismisses ACCC Appeal in Unconscionable Conduct", Media Release, MR66/03 10 April 2003.

[52] *ACCC v Simply No-Knead*, supra, at [31] (Sunberg J).

[53] *ACCC v Simply No-Knead*, supra.

[54] *ACCC v LeeLee Pty Ltd* [1999] FCA 1121.

[55] *ACCC v Cheap as Chips Franchising Pty Ltd.*

section 51AC before the Courts[56], the outcomes of which are likely to crystallise even further the scope of this provision. As noted in Section One of this submission, there is a legitimate need to allow the effect of recent changes to be felt before further amendments are considered.

To intervene prematurely would, most likely, subject all businesses (large and small) to unnecessary and potentially destabilising levels of uncertainty in their day-to-day commercial dealings. This, in the Business Council's view, would be likely to have a detrimental effect on the ability of all businesses to conclude business transactions, with consequential adverse implications for the healthy operation of competitive markets, the Australia economy and, ultimately, Australian consumers.

In particular, the Business Council submits amending the section to incorporate a test of "unfairness" would give rise to potentially detrimental consequences for all businesses.

As indicated above, when the Reid Committee initially considered the unconscionable conduct provisions, it recommended an "unfair" conduct provision but this was rejected by Parliament. The same concerns about "unfair" conduct that applied when the Reid Committee was considering such a provision still apply today. That is, the definition of what is "unfair" is too subjective and indiscriminate and would create enormous uncertainty for all businesses. Rather, the concept of unconscionable conduct in section 51AC, as interpreted by the Courts, provides small business with protection from conduct which may be described as "unfair".

3.5 Conclusion - no need for reform

The Business Council submits that Part IVA of the TPA deals effectively with unconscionable or unfair conduct in business transactions, particularly since the enactment of section 51AC which provides small business with extensive and effective protection in their business dealings.

While the Business Council acknowledges that the law is still in its formative stages, the Business Council submits that it would be inappropriate for intervention at this time while precedent is being continually developed and refined.

Accordingly, the Business Council submits that there is no compelling case at this time for the Committee to recommend legislative amendments to Part IVA.

[56] ACCC Report for 2002-2003 - *ACCC v Oceana Commercial Pty Ltd; ACCC v Westfield Shopping Centre Management Co (Qld) Pty Ltd; ACCC v Arnolds Ribs and Pizza; ACCC v Chaste Corporation Pty Ltd and Mr Peter Foster; ACCC v Kwik Fix International Pty Ltd; ACCC v Global Pre Paid Communications.*

4 Part IVB and industry codes

4.1 Key points

The Committee has been directed to consider whether Part IVB of the TPA operates effectively to promote better standards of business conduct and, if not, what further use could be made of Part IVB in raising standards of business conduct through industry codes of conduct. Against this background, the Business Council submits that:

- industry codes are, generally, an effective compliance tool. Industry codes encourage self-regulation by promoting "best practice" standards relevant to the industry in question and they typically lower compliance costs for business, compared with intervention by regulatory agencies;
- the ACCC's recent proposal to endorse voluntary industry codes is a good one. This proposal should encourage a greater degree of co-regulation, while having the potential to reduce compliance costs; and
- Part IVB, which has the effect of making an industry code law, provides a useful way of promoting better standards of business conduct in industries where self-regulation is inadequate and has been used effectively to regulate franchising operations. For example, the Federal Court recently held that a 4WD franchisor had contravened the Franchising Code of Conduct and issued injunctions against the corporations in question, restraining them for three years from entering into franchising arrangements without giving any prospective franchisee detailed information as to the quality of goods that will be supplied and the delivery time of those goods. The ACCC noted that:

  > *"The judgment sends another clear message to the franchise industry that franchisors have an obligation to deal fairly and honestly with their franchisees"*[57].

4.2 Structure

This part of the Business Council's submission will examine:

- the benefits of self-regulation for all businesses;
- the background to Part IVB and the legislative framework;
- the Franchising Code of Conduct, the only code prescribed under Part IVB to date; and
- the important role played by voluntary codes in promoting better standards of business conduct.

4.3 Benefits of self-regulation for all businesses

Businesses, large and small, have a commercial interest in negotiating the standards that apply to them, as those standards are likely to be tailored to the requirements of the relevant industry and the challenges that industry faces. Self-regulation enables businesses to strive towards industry "best practice" and in so doing, businesses typically

[57] *Federal Court finds 4WD Franchisor Misled Franchisees* - ACCC media release, 15 August 2003.

incur lower transaction and compliance costs than standards devised by government agencies[58].

The Chairman of the ACCC, Graeme Samuel, recently observed:

> "*Effective codes result in increased compliance and reduced regulatory costs. In contrast, ineffective codes not only fail to provide real benefits to business, but may put business at a clear competitive disadvantage by adding compliance burdens on business without providing clear benefits to either business or consumers*.
>
> *Effective voluntary codes whether in the context of industry self regulation or co-regulation carry substantial benefits for government, the regulator, the industry and the consumer. It is in the interests of all concerned to ensure that voluntary industry codes are developed, implemented, administered and maintained as an effective tool to achieve compliance with laws, best industry practice and maintaining consumer sovereignty. Effective codes have the potential to significantly reduce levels of complaints to the Commission as the industry deals with and satisfactorily resolves its own disputes*" [59].

The Business Council submits that industry codes are more likely to achieve effective self-regulation where there is consensus amongst stakeholders as to the scope of the code and the likely costs of compliance. Where this is achieved, mandatory or voluntary codes can provide an effective way of balancing the interests of big and small business.

4.4 Legislative framework of Part IVB

Introduction

Part IVB provides for industry codes to be prescribed and enforced under the TPA. Part IVB was enacted as a result of concerns that self-regulation was failing in the franchising, retail grocery and service station industries[60].

In its submission to the Reid Committee (which examined the Franchising Code of Conduct and the OilCode), the ACCC took the view that ideally, industry codes should operate on a voluntary basis but where this was unsuccessful, some other means, either one that makes it commercially attractive, or more coercive, should be used. Some small business groups argued that legislative-backing would be required if industry self-regulation were to be successful.

The legislative framework

In response, the Government enacted Part IVB[61] of the TPA. Sections 51AD and 51AE provide that industry codes of conduct may be prescribed in regulations and enforced by the ACCC or by right of private action. Contravention of a prescribed code may result in

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[58] *Telecommunications Competition Regulation Inquiry Report* at 450; see also *Policy Guidelines on making industry codes of conduct enforceable under the Trade Practices Act 1974* - Minister for Financial Services and Regulation, May 1999.

[59] Graeme Samuel, "The Big Issues and the Big Ideas" Speech to the Australian Industry Group National Industry Forum 11 August 2003.

[60] A review of the *Franchising Code of Conduct* in 1994 found that the standard of conduct provisions had not been effective in addressing serious franchise disputes. Similarly, the Reid Committee concluded that the Franchising Code and the Oilcode were ineffective.

[61] *Trade Practices Amendment (Fair Trading Act) 1998* and *Trade Practices Amendment (No.1) 2000.*

a range of sanctions under the TPA, including injunctions, damages, requirements to give an undertaking to the ACCC and orders to disclose information or publish corrective advertising.

Regulations may declare a code to be mandatory or voluntary. Mandatory codes bind all industry participants. Voluntary codes only bind those participants who have formally subscribed to the them.

Policy considerations

Importantly, when launching its policy guidelines on the making of industry codes of conduct[62] ("**Policy Guidelines**"), the Government expressly noted that:

- industry should continue to regulate itself, allowing consumers to reject suppliers which fail to comply with high standards of customer service and product quality; but

- where industry is unable to maintain the appropriate standards through self-regulatory means, and where there is severe market failure, the Government would look to prescribe industry codes and subject them to the TPA.

Accordingly, the legislation was underpinned by the expectation that Part IVB should only be used as a "last resort" and voluntary codes of conduct should be the preferred method of regulation.

Process

This expectation is reflected in the process by which a code may be prescribed under Part IVB. The Policy Guidelines indicate that formal proposals for the prescription of codes may be initiated at all levels of business and from within various Ministerial portfolios to underpin important industry self-regulation schemes, where that is necessary to make them operate effectively. However, this may only occur if:

- the code would remedy an ***identified market failure*** or promote a ***social policy objective***;

- the code would be the ***most effective means for remedying market failure*** or ***achieving that policy objective***;

- the ***benefits of the code to the community as a whole*** would outweigh any costs;

- there are ***significant and irremediable deficiencies*** in any existing self-regulatory regime;

- a ***significant enforcement issue*** exists due to a history of contraventions of voluntary codes; and

- ***self-regulation*** and 'light-handed' quasi-regulatory options have been examined and are ***considered to be ineffective***.

[62] *Prescribed Codes of Conduct - Policy Guidelines on Making Industry Codes of Conduct Enforceable under the Trade Practices Act 1974* - May 1999.

In addition, the Policy Guidelines indicate that it will not be appropriate to prescribe a code of conduct under the TPA in circumstances where a code is underpinned, and enforceable, under other legislation[63].

Given that a prescribed code of conduct would be likely to impose significant compliance costs on business, a formal process of public consultation (which includes consumer and business representatives) is undertaken and a Regulation Impact Statement is published before any code is prescribed.

4.5 Franchising Code of Conduct

The first and only code prescribed under the TPA to date is the Franchising Code of Conduct ("**Franchising Code**"). This code was prescribed and made mandatory because of the serious social and economic costs of problems identified in the franchising sector, together with the failure of existing regulatory mechanisms to resolve difficulties in this sector. The Franchising Code aims to prevent franchisors from abusing the power inherent in the franchising relationship.

Franchising Australia's 1999 survey found that about a quarter of franchisors felt that the Franchising Code had a positive effect on their franchise system, while about a quarter felt that the Franchising Code had had a negative effect. About 48% of franchisors felt that the Franchising Code had not had any effect on their system.

Nevertheless, the Franchise Council of Australia ("**FCA**"), which is the primary industry body, has raised a number of concerns with the Franchising Code. While the FCA supports the need for a code, the FCA has noted that the Franchising Code has had a number of unintended consequences for the industry and may be affecting the sector's growth[64].

In particular, concerns have been raised in relation to the cost and administrative burden of complying with the Franchising Code's disclosure requirements. 23% of franchisors surveyed saw the Franchising Code as "*bureaucratic, too detailed or inflexible*" and the cost of compliance was seen by some franchisors as detrimental to their business. For franchisors involved in master franchising or mobile service delivery, the cost of compliance was especially high.

The Franchising Policy Council ("**FPC**") reviewed the Franchising Code in May 2000 and noted the strong support from most franchising industry operators for continuing with the Franchising Code. On the issue of compliance costs, the evidence presented to the FPC revealed that estimated costs vary widely. The FPC found:

> *"Moderate to low costs may reflect that some franchisors were already operating with fairly sophisticated practices and documentation that did not require any significant change to meet the compliance requirements. The impression gained during the review was that the low value service franchise sector encountered the most difficulty and costs in adjusting for compliance"*[65].

[63] For example, the *Telecommunications Act 1997* provides for the registration and enforcement of industry codes of conduct by the Australian Communications Authority and States and Territories have mandated various industry codes of conduct under Fair Trading legislation.

[64] Report of the FPC, *Review of the Franchising Code of Conduct,* May 2000 at 67

[65] Ibid at 43

In addition, the FPC noted that seeking advice on complying with the Franchising Code could give rise to professional costs, but concluded that:

> "*the Code will continue to consolidate high ethical standards in the franchising industry and that the costs and administrative burdens incurred so far will pay healthy dividends in the future*"[66].

In addition, a significant number of franchisors claim that the Franchising Code is a positive influence on the sector. 36% of respondents thought that the Franchising Code would restrict substandard operators, while about 26% felt that the Franchising Code would improve the franchising sector's reputation and confidence. The Government has also received similar comments from individual franchisors, and has broadly received strong statements of support for the Franchising Code from a franchisee body, the Motor Trades Association of Australia ("**MTAA**")[67], notwithstanding a number of concerns relating to alternative dispute resolution procedures.

4.6 The important role played by voluntary codes in promoting better standards of business conduct

It is important to remember that Part IVB of the TPA is, by design, only intended to regulate industries where self-regulation is failing or where there is a demonstrated need to achieve a particular social objective. Indeed, the Government's stated policy is that self-regulation is preferable and the option to prescribe codes under Part IVB will be rarely used[68], with effective voluntary codes of conduct being the preferred method of regulation.

Accordingly, the Business Council submits that when considering the effectiveness of Part IVB, it is equally important to acknowledge the role that voluntary codes of conduct play in promoting better standards of business conduct. These include the OilCode, the Retail Grocery Industry Code and the Film Distribution and Exhibition Code.

- *OilCode*

The first OilCode was established in 1989. It contained principles for agreements and provision for alternative dispute resolution between oil companies and resellers.

While disputes arising from the termination and assignment of agreements, tenure, supply and performance criteria were able to be addressed under the OilCode, disputes arising from general pricing matters were not. This caused the MTAA to withdraw from the OilCode in 1996. Although the Government has sought to revive the OilCode, this has not yet occurred, apparently due to stakeholders being unable to resolve major issues.

In March 2003, the Government outlined its intention to revoke the Sites and Franchise Acts in favour of a mandatory Petroleum Industry Oilcode ("**PI Oilcode**"). The PI Oilcode would apply to all market participants. It aims to provide companies with greater flexibility in determining the most efficient arrangement for marketing their products. The PI Oilcode would also revise tenure provisions and apply to a range of agreements not currently covered by the Franchising Code. The PI Oilcode also proposes improved transparency of petrol prices at the terminal gate, a simpler dispute resolution procedure and minimum standards for petrol re-selling arrangements.

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[66] Ibid

[67] Report of the FPC page 67.

[68] Policy Guidelines, page iv.

The Government issued a press release on 7 May 2003, stating that the changes to the PI Oilcode would ensure that all customers are better informed about terminal gate prices and have the option of buying petroleum products at terminal gate-based prices. Negotiations are continuing to finalise the PI Oilcode with major stakeholders.

- *Retail Grocery Industry Code of Conduct*

The Retail Grocery Industry Code of Conduct ("**Retail Code**") was implemented in response to the recommendations of the Baird Committee. Although the Baird Committee recommended a mandatory code, the Government decided to support a voluntary code, which came into effect on 13 September 2000. At the same time, a Retail Grocery Industry Ombudsman was appointed to mediate industry disputes and the Retail Grocery Industry Code of Conduct Committee commenced overseeing the Retail Code.

The Retail Code is a set of voluntary guidelines promoting fair and equitable trading practices in the retail grocery industry and simple dispute resolution mechanisms. It addresses standards and specifications for produce, product labelling, packaging and preparation, contracts and voluntary notification of retail business acquisitions. A number of organisations and businesses have committed to promoting the Retail Code and their own internal dispute resolution procedures[69].

The Retail Code is currently under review and a report is due on 1 December 2003.

- *Film Distribution and Exhibition Code*

The Film Distribution and Exhibition Code of Conduct was implemented to address the imbalance of bargaining power that exists between small film exhibitors and the large film distributors. It provides objective benchmarks for access to films and terms and conditions such access will be granted on.

- *Other codes*

From time to time the ACCC has provided feedback and advice to industries who are engaged in formulating codes of conduct. The ACCC Report for 2002-2003 states that the ACCC has provided technical assistance with 5 developing industry codes, the review of 2 industry codes as well as continued technical assistance to 10 other industry and consumer codes. These include:

  - the Internet Industry Association's codes of practice especially the ISP Code of Conduct;
  - the Fruit Juice Industry Code of Conduct;
  - the Australian Pharmaceutical Manufacturers Association Code;
  - a code for marketing of IVF services;
  - the Jewellery and Timepiece Industry Code of Conduct; and

[69] Australian Chamber of Fruit and Vegetable Industries Limited, Australian Food and Grocery Council, Australian Retailers Association, Coles Myer Limited, National Association of Retail Grocers of Australia, National Farmers' Federation, Queensland Retail Traders and Shopkeepers Association, Retailers Association of Queensland Limited and Woolworths Limited.

- various telecommunications codes through the Australian Communications Industry Forum[70].

4.7 ACCC proposal to endorse industry codes.

On 11 August 2003, the ACCC announced a proposal to endorse voluntary industry codes. This process is different from the existing processes under Part IVB of the TPA. As the ACCC Chairman observed:

> "*The effect of prescription is, of course, government regulation in a different form as the code becomes quasi-law*"[71].

The Business Council supports a system of ACCC endorsed voluntary codes of conduct, as this confirms that good consumer and competitive outcomes can be achieved without necessarily relying on "heavy-handed" regulation. It also confirms that the majority of businesses operate within the law and do adhere to the principle of self-regulation.

The ACCC has indicated that before it will endorse a code, it will need to be satisfied that it fulfils the ACCC's non-exhaustive criteria, which include matters such as consultation with stakeholders, transparency and coverage of the proposed code, provision for complaints handling and sanctions and whether the code will address consumer concerns.

The Business Council looks forward to further development of the ACCC's proposal.

4.8 Conclusion - no evidence to support an amendment to Part IVB

The Business Council endorses the Government's view[72] that competitive market forces deliver greater choice and benefits to consumers and self-regulation should be preferred over intervention by regulatory agencies.

The Business Council considers that industry codes are, generally, an effective compliance tool. Industry codes encourage self-regulation by promoting "best practices" relevant to the industry in question. Given that industry codes usually require a significant consultation between stakeholders and consensus within the industry before they can be finalised, this typically ensures greater ownership and greater compliance than may be the case with other forms of regulation. In addition, industry codes typically reduce compliance costs for businesses and increase confidence in the integrity of the industry in question.

Nevertheless, the Business Council acknowledges that the success of an industry code will ultimately depend on a high level of awareness of the code through educational programmes and promotion of the code among industry participants. In addition, an industry code is only likely to be effective if there are sufficient incentives for relevant stakeholders to "sign up" to the principles set out in the code and there are sufficient sanctions to deter and punish any deviation from the code.

That said, the Business Council's view is that an industry code should only be prescribed under Part IVB of the TPA when there is market failure or a demonstrated need to achieve

[70] Other examples of codes which have received ACCC support or assistance include the Automotive Body Repair Code; the Cinema Code; the Car Hire Code; The Horse Industry Council; the Model Direct Marketing Code; the Retail Tenancy Code; the Tourism Code and the Therapeutic Goods And Code.

[71] Samuel op. cit. 59

[72] *Codes of Conduct Policy Framework*, March 1998, released by the Hon Warren Truss MP.

a particular social objective. The Business Council submits that such circumstances will rarely arise. Accordingly, the Business Council submits that because there is currently only one prescribed industry code does **not** mean that Part IVB is ineffective in promoting better standards of business conduct. Rather, the Business Council submits that the current system of industry self-regulation, supported by a regulatory power to intervene when necessary, is working well.

Accordingly, the Business Council submits that there is no evidence to support an amendment to Part IVB of the TPA. In any event, the Business Council submits that it would be prudent for the Committee to await the outcome of the review of the Retail Code before making recommendations on whether particular sector-specific codes are needed.

5 Other measures to assist small business

5.1 Key points

- The Business Council recognises that small businesses are extremely important to the Australian economy. The economy needs small businesses to enter the market with new ideas and new methods, find new niches, challenge existing businesses and expand.
- The Business Council believes that the best way to ensure the continued growth and success of small business is to maintain a buoyant and competitive Australian economy and that small businesses have access to information and support services to assist them in their business activities.
- The Business Council believes that the TPA already provides adequate and effective assistance to small business for dealing with anti-competitive or unfair conduct. The Business Council submits that provisions that were enacted as a result of the Reid and Baird Committee inquiries have not yet had an opportunity to be sufficiently tested. Further precedent and ACCC experience in enforcing these provisions is required before these provisions can, properly, be reviewed. For these reasons, the Business Council believes that further legislative amendment, at this time, is not warranted.
- In particular, proposals to "cap" the market share of individual businesses would give rise to a number of practical and enforcement difficulties. Setting a market share cap would, at best, be an uncertain (if not arbitrary) exercise. Moreover, a market share cap would be likely to "blunt" the processes of competition by providing businesses with an incentive to maintain the *status quo* and a disincentive to pursue opportunities to become more efficient, innovative or productive which would usually allow a business to grow. This, ultimately, would have a detrimental impact on the Australian economy and Australian consumers and, paradoxically, could result in an individual proprietor being "stranded" if, due to a market cap, that person was denied the opportunity of selling his or her business to the highest bidder.
- However, in order to further assist small business, the Business Council suggests, consistent with the recommendations of the Dawson Committee, that the ACCC consider issuing guidelines concerning its approach to Part IVA of the TPA.
- The amendments made to the TPA arising from the Baird Committee, including the extension of the powers of the ACCC to bring representative actions and the significant increase in the range of transactions covered by the unconscionable conduct provisions, have not yet been fully tested.
- In addition, the recommendations of the Dawson Committee in response to small business concerns, including the improved processes for approving collective bargaining, have not yet been implemented.
- The Business Council also acknowledges and supports the assistance programmes that Commonwealth, State and Local Governments provide to small business, many of which may assist small business with dealing more effectively with anti-competitive or unfair conduct.

5.2 Structure

This section of the submission focuses on:

- balancing the needs of small business with the objectives of the TPA;
- the adequacy of current provisions of the TPA in assisting small business in dealing with anti-competitive or unfair conduct; and
- additional assistance available for small business in this regard.

5.3 Balancing the needs of small business with the objectives of the Trade Practices Act.

The Business Council acknowledges the vital role that small business plays in the Australian economy. Around 30% of Australia's economic activity is generated by the small business sector. 3.3 million Australians are employed in 1.1 million small businesses. There were (net) 47,000 new small businesses in 2000 - 2001 and in the last 20 years, the number of small businesses has grown by 3.5% per annum[73].

The Business Council believes the best way to ensure the continued growth and success of small business is to maintain the healthy operation of a competitive economy in Australia. Underpinning the operation of the Australian economy is the principle that competition regulation should promote and protect the competitive process and not individual competitors. This principle is enshrined in section 2 of the TPA, and was recently confirmed by members of the High Court in *Boral*[74].

Specific protection for small business may conflict with the competitive process and is likely to damage the economy as a whole, to the detriment of all businesses (large and small) and the economic welfare of Australians. Accordingly, the Business Council believes that any changes to the TPA which are designed to assist small business should be in accordance with the objectives of the TPA.

5.4 Adequacy of current provisions of the TPA in assisting small business

The Senate Committee is the third Parliamentary inquiry since 1996 into the protection of small business under the TPA. The two previous inquiries[75] ushered in a number of significant reforms, such as:

- a voluntary code of conduct for the retail grocery sector and the Retail Grocery Industry Ombudsman to ensure fair competition in the grocery industry;
- a Franchising Code of Conduct - the only prescribed code under the TPA - which provides for greater transparency in franchising negotiations;
- the creation of an unconscionable conduct provision for small business (section 51AC, discussed in Section Three of this submission); and
- amending the definition of a 'market' in section 50(6) of the TPA to include a substantial market in a region of Australia when assessing a merger.

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73 *Annual Review of Small Business* 2002-2003 Office of Small Business, Canberra.

74 [2003] HCA 5 at [87] see also *Queensland Wire at [191] and Melway at 13 [17].*

75 The Reid Committee and the Baird Committee.

In particular, as a result of the changes to the TPA arising out of the Baird Committee enquiry (given effect by the *Trade Practices Amendment Act (No 1) 2001*), the ACCC stated that:

> "*… it is now in a better position to assist small business after changes to the Trade Practices Act… the new legislation fills in gaps in the protection already given to small business with unconscionable conduct provisions passed in 1998*"[76].

Collective bargaining proposal

In addition, the Dawson Committee made substantial recommendations concerning collective bargaining for small business which will address many small business concerns.

The Dawson Committee recommended that a notification process should be introduced, along the lines of the exclusive dealing notification process in section 93 of the TPA, for collective bargaining by small business dealing with large business. A transaction value threshold of $3 million would apply.

The Commonwealth Government accepted those recommendations and stated that it would develop a notification process for collective bargaining by small business, which would be speedier, simpler and less costly than the current authorisation process. The Commonwealth Government went on to say that the process:

> *"…will aim to provide an appropriate balance of power where small businesses are competing or dealing with businesses that have substantial market power"*[77].

The Business Council notes that the vast majority of small business organisations appear to have welcomed these proposals and recognise the benefits that they will bring to their members[78].

Equally, the Business Council has accepted these proposals and submits that they present an effective way of rebalancing the relationship between small and large business. Care needs to be taken with these proposals, however, as collective bargaining and collective boycotts will generally be anti-competitive and not in the interests of consumers. The proposals raise a number of legal complications that will need to be resolved before they can be implemented.

Market cap proposal

The Business Council understands that some sectors support a proposal to cap individual businesses' market shares, thereby preventing them from engaging in strategic conduct or acquisitions that would otherwise enable them to grow their market share.

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[76] ACCC Media Release, "*Greater Support for Small Business*", 12 July 2001.

[77] Commonwealth Government response to the review of the Competition provisions of the TPA, 16 April 2003.

[78] Small business support for collective negotiation reforms, Joe Hockey, 30 July 2003 - See also for example ACCI, Media Release, 16 April 2003 *"ACCI supports the thrust of the major recommendation affecting small business which is the introduction of a notification process to allow collective bargaining by small businesses dealing with large businesses"*; Australian Hotels Association, Media Release, 16 April 2003, *"Dawson Recommendation Big Win for Small Business"*; National Farmers' Federation, Media Release, 16 April 2003 *"NFF was particularly pleased that the Government had accepted the Review's recommendations to facilitate farmers' ability to collectively negotiate"*.

The Business Council is not aware of any major Western jurisdiction implementing a market cap for individual businesses. The Business Council submits that imposing a market share cap on individual participants would be fraught with difficulty and would, most likely, stultify competition in the particular market or sector in question. In particular:

- in the vast majority of industries, determining market share is not an exact science and market share figures may differ widely according to the empirical data and the methodology used. For this reason, it would be extremely difficult to arrive at an accurate, reliable market share figure which could constitute a basis for a cap;

- similarly, arriving at an appropriate market cap for individual businesses would be, at best, an uncertain (if not an arbitrary) exercise. As noted in Section One of this submission, Australia's economy is changing and is becoming more open, connected and integrated with the global economy. The practical consequence of this is a changing competitive landscape in most, if not all, sectors. To impose a market cap on individual participants would not reflect the dynamic and often complex nature of competition and the competitive process;

- even if it were possible to delineate markets and then calculate market share on a consistent, accurate and reliable basis, such a proposal would impose an obligation on businesses (and the ACCC) to monitor their market shares. This would, most likely, be a burdensome, costly and time-consuming exercise, which would absorb a proportion of businesses' resources and detract from their day-to-day business dealings;

- setting aside these practical difficulties of arriving at and enforcing such a proposal, a market share cap would be likely to have a detrimental impact on competition in Australia. Knowing that their market share would be capped at a certain level, businesses would have no incentive to find ways of becoming more efficient, innovative or productive, all of which would usually contribute to businesses' growth. Instead, businesses would have an incentive to maintain the *status quo*, rather than pursuing opportunities for growth and risking a contravention of the law. In this way, the purpose would actually stultify competition to the detriment of the Australian economy and Australian consumers; and

- paradoxically, a market share cap could result in small businesses being "stranded" if, due to a market share cap, they were denied the opportunity to sell their business to the highest bidder

5.5 Additional assistance available for small business

State legislative regimes

In addition to the protection and assistance offered by Part IVA of the TPA, the Business Council notes that small businesses are also assisted in dealing more effectively with anti-competitive or unfair conduct by industry codes (see Section 6) and by other State legislation. Small business retailers, in particular, are protected from unconscionable conduct under State retail tenancy legislation. Victorian small businesses also have the benefit of a legislative regime, including the *Fair Trading Act 1999* (Vic) and the *Small Business Commissioner Act 2003* (Vic).

Other States also have similar regimes.

ACCC specialist assistance for small business

In recent years, the ACCC has been an active advocate for small business. It established a small business advisory group to better appreciate the needs of the sector. Unlike other business sectors, small business has a dedicated commissioner within the ACCC.

The ACCC publishes eight small business specific guides including "Small Business and the Trade Practices Act: A Practical Guide for Australian Small Businesses". The ACCC also produces a range of videos relating to matters relevant to small business, many broadcast through regional television networks.

Commonwealth Government's assistance for small business

The Commonwealth Government also provides a series of services for small business. A summary of some of these are listed in **Appendix 5**. They include a wide and varied range of services, a number of which may assist small business in dealing more effectively with anti-competitive or unfair conduct.

5.6 Conclusion - no evidence to suggest that additional measures are justified to protect small business from anti-competitive conduct

The Business Council recognises the extremely important role small business plays in the Australian economy. In that context, the Business Council submits that small business already receives effective assistance and protection from a variety of sources, ranging from the TPA to initiatives introduced by the Commonwealth and State Governments.

Given that some of the assistance afforded by the TPA, particularly Part IVA, is relatively new, the Business Council considers that these provisions should continue to be enforced as they stand, in order to develop greater precedent, before determining whether they need further expansion or refinement. Moreover, the recommendations of the Dawson Committee that will benefit small business are yet to be implemented.

Accordingly, the Business Council advocates a prudent approach of waiting to see whether the legislative provisions already in place, or which will be introduced pursuant to the Dawson Committee's recommendations, will suffice in assisting small business in more effectively dealing with anti-competitive or unfair conduct.

6 Approaches in other jurisdictions to protect small business

6.1 Key points

- The Business Council notes the experience of competition regulation in Organisation for Economic Co-operation and Development ("**OECD**") countries and the approaches adopted in those jurisdictions.
- Nevertheless, the Business Council believes that drawing conclusions, based on the experience of competition regulation in other countries with regard to the protection of small business, should be undertaken with caution.
- In particular, the Business Council submits that regulation in other countries has arisen due to historical, geographical and cultural reasons that are not necessarily applicable in Australia.
- Amendments to competition regulation should be in Australia's best interests and not merely to create uniformity with competition regimes in other jurisdictions.

6.2 Structure

This section of the submission examines a number of the approaches adopted in OECD economies for dealing with the protection of small business, as a part of competition regulation, and addresses whether any of these approaches could usefully be incorporated into Australian law.

6.3 Comparison with approaches adopted in OECD jurisdictions

United States

The key federal antitrust laws in the United States are:

- ***section 2 of the Sherman Act*** which prohibits monopolisation, attempted monopolisation and conspiracies to monopolise; and
- ***The Robinson-Patman Act*** which prohibits price discrimination.

Monopolies and the abuse of market power

Under section 2 of the *Sherman Act*, it is illegal to "*monopolise, or attempt to monopolise, any part of the trade or commerce among the several states, or with foreign nations*". In effect, section 2 prohibits unilateral monopolisation as well as combinations or contracts in the pursuit of a monopoly. The offence of monopolisation comprises:

- the possession of monopoly power; and
- a course of conduct to acquire, use or preserve this power.

Importantly, the possession of monopoly power is not, by itself, unlawful. Rather, section 2 is aimed at capturing the deliberate acquisition or retention of monopoly power through anti-competitive or predatory activities, such as refusing to deal with other firms.

The Robinson-Patman Act - price discrimination

The *Robinson-Patman Act* is enforced by both the Federal Government and private parties (through bringing a civil action) and is the principal federal antitrust statute governing price discrimination, promotional payments and allowances and other conduct relating to the equal (or unequal) treatment of purchasers in the sale of commodities.

In general terms, the *Robinson-Patman Act* prohibits the sale of commodities of like grade and quality at different prices to competing customers, where the price differential may adversely affect competition. A seller or buyer may defend such a price differential on the ground that it was necessary to meet a competitor's price, that there was a cost-based justification for the lower price, that market conditions changed between the time of the two sales or that the lower price effectively was made available to all competing purchasers.

From a practical perspective, litigation under the *Robinson-Patman Act* typically focuses on whether the price differential in question adversely affected competition. However, it has been suggested that the legislation has been little used and for that reason, its repeal has been widely recommended[79].

Canada

Canadian competition law is governed by a single federal statute, the *Competition Act*. The Act applies to all aspects of anti-competitive conduct, including the abuse of a dominant position.

Monopolies and the abuse of market power

Similar to the position in other OECD jurisdictions, a monopoly is not, in itself, illegal. However, under the Canadian *Competition Act*, the abuse of a dominant position is illegal if that abuse results in a substantial lessening of competition. Although the existence of a monopoly is not a prerequisite, a relatively high market share is needed to allow the dominant firm to substantially dictate market conditions and exclude competitors.

The *Competition Act* includes a non-exhaustive list of conduct that may constitute an abuse of a dominant position, such as:

- a vertically integrated supplier charging more advantageous prices to its own retailing divisions;
- selling at prices lower than the acquisition cost;
- inducing a supplier to refrain from selling to competitors; and
- pre-empting 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.

Predatory pricing

As well as potentially constituting an abuse of a dominant position, under Canadian legislation, predatory pricing may also constitute a criminal offence. Predatory pricing

[79] Baird Committee report, at 111 [7.35].

occurs when a firm employs a "*policy*" of charging "*unreasonably low*" prices with the object or effect of "*substantially lessening competition or eliminating a competitor*".

However, there have been few prosecutions since this provision was enacted[80] and recent enforcement guidelines suggest a cautious approach, indicating that:

> "*most investigations will be terminated at the preliminary stage unless there are circumstances suggesting that predatory conduct could be rational and effective…..even where* [those] *conditions exist, only pricing below average variable cost raises a presumption of predation*".

Concerns with the Canadian predatory pricing provision were discussed in Section Two of this submission.

Price discrimination

In addition, Canadian legislation provides for a criminal offence of price discrimination when a seller knowingly engages in a "practice" of granting one customer preferential discounts or concessions not "available" to its competitors on transactions involving a "like quality and quantity" of goods. Proof of injury to competition is not an element of the offence; the law is designed to promote equity between competitors rather than economic efficiency. However, enforcement guidelines indicate that a more restrained approach will be taken to various elements of the offence in order to enable firms to develop flexible pricing policies.

European Union

Abuse of a dominant position

Article 82 of the EC Treaty prohibits an abuse, by one or more undertakings, of a dominant position with the common market, or a substantial part of it insofar as it may affect trade between Member States.

Article 82 then sets out a non-exhaustive list of conduct which may constitute an abuse of a dominant position, including:

- directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions;
- limiting production, markets or technical development to the prejudice of consumers;
- applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage; and
- making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their very nature or according to commercial usage, have no connection with the subject of such contracts.

Therefore, an abuse of a dominant position may include activities such as discriminatory pricing, excessive pricing, fidelity discounts, refusal to supply and refusal to give access to essential facilities.

[80] The only reported conviction is *R. v Hoffman-La Roche* (1980), 28 O.R. (2d) 164 (H.C.J.).

Collective trading arrangements

Joint selling or joint purchasing of goods would usually contravene Article 81 of the EC Treaty, which prohibits agreements and concerted practices between undertakings, which may affect trade between Member States, and which have as their object or effect the prevention, restriction or distortion of competition within the common market. However, an agreement which would otherwise contravene Article 81 may be exempted from the operation of that provision under Article 81(3) where that agreement contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not:

- impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives; and
- afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

Pursuant to Article 81(3) of the EC Treaty, the European Commission has recognised in certain circumstances the necessity of collective arrangements to protect the interests of small producers. Similarly, decisions of the European Courts have supported collective selling arrangements between small businesses in circumstances where there are a large number of small producers of products which are inherently exposed to the possibility of market failure[81].

Other initiatives to assist small business

The European Charter for Small Enterprises ("**Charter**") was adopted by the Feira Council in June 2001. It calls upon Member States to take a range of actions to support small business in a number of ways, including "*better legislation and regulation*". The Charter also provides for monitoring and evaluating progress on Charter issues, including the publication of periodic reports. Importantly, the principles underpinning the Charter recognise that the position of small business in the European Union can be improved by action to stimulate entrepreneurship, to evaluate existing measures and **when necessary**, to make those measures small-business friendly.

The Charter has resulted in Member States implementing legislative measures across a range of issues, including education and training for entrepreneurship, cheaper and faster start up, 'better' legislation and regulation and availability of skills.

United Kingdom

The *Competition Act 1998* has brought UK domestic competition law into line with Article 82 of the EC Treaty. In addition, the UK regulator, the Office of Fair Trading, has issued guidelines on what may constitute an abuse of a dominant position, recognising that particular problems can arise in specific industries, such as exclusive distribution agreements, selective distribution agreements, third line forcing, full line forcing and quantity forcing (where a retailer is required to purchase a minimum quantity of a product).

[81] See, for example, Cases T-70 & 71/92 *Florimex and VGB v Commission* [1997] ECR II-693 concerning the auction sales of flowers.

6.4 Application to Australia

Comparisons with other jurisdictions

A number of submissions to the Dawson Committee looked to approaches adopted in other OECD jurisdictions and argued that it would be appropriate to adopt similar approaches in Australian law. Members of the Dawson Committee also travelled overseas to investigate the legislation and practices applied in other countries.

Are such comparisons legitimate?

Attempts to bring Australian competition law into line with OECD jurisdictions are usually based on a perceived need for uniformity with competition regimes in other jurisdictions. The Business Council submits that this is a weak basis, without further justification, for the adoption of similar measures in Australia.

For example, looking at section 46 of the TPA, it is a fair comment that the relevant provisions of US, EU and UK law do appear to place an emphasis on the particular effects of conduct. However, a simple comparison of the wording of legislation cannot support the inclusion of similar legislation in Australia, given that overseas legislation may be based on a particular policy objective relevant to that jurisdiction or, alternatively, the legislation may be interpreted in a manner specific to the jurisdiction in question.

For example, there is an argument that the standard which is applied in section 2 of the *Sherman Act* in practice is significantly narrower than that contemplated by the TPA. Under section 2 of the *Sherman Act*, the prohibition will only come into effect when it can be shown that unilateral conduct threatens actual monopolisation, as opposed to conduct which has the effect or likely effect of leading to one or more specified outcomes.

Similarly, in the European Union, the relevant legislative provision (Article 82 of the EC Treaty) is governed by principles relating to enhancing European Community industry and the institution of a system ensuring that the internal market does not become distorted.

Against this background, the Dawson Committee acknowledged that international comparisons also may give rise to difficulties and concluded, in relation to the proposed changes to section 46 of the TPA, that:

> "*there is no real counterpart to section 46 in other countries and comparison is difficult and unhelpful*".

A similar observation may also apply to calls from small business groups, such as the National Association of Retail Grocers of Australia ("**NARGA**"), for the enactment of a specific provision prohibiting predatory pricing, similar to the position in Canada. The flaws in that provision have been discussed in Section Two of this submission.

It is important to remember that the Baird Committee considered overseas approaches dealing with small businesses competing in the retail sector. The Baird Committee noted that as market structures differ from jurisdiction to jurisdiction for historical, geographic and cultural reasons, measures implemented overseas should be approached with caution. In particular, the Baird Committee specifically noted the ACCC's warning that:

"There is a danger in comparing concentration in the Australian retail grocery sector and its treatment by competition authorities with that experienced in equivalent sectors overseas"[82].

The Baird Committee concluded that protectionist measures for small business would not be appropriate, but recommended measures that it believed would enhance competitive processes.

6.5 Conclusion - no evidence to suggest that approaches adopted in other jurisdictions are relevant to the needs of Australian businesses

The Business Council submits that when looking to experience overseas of balancing the interests of particular sectors with overall competition policy, the overriding consideration should be whether there is evidence to suggest the measure in question is appropriate to Australia. In particular, the Australian economy differs in many respects from the economics of other jurisdictions. For example, the legal framework of European Union is underpinned by the operation of a single market between a number of sovereign states. In addition, the Australian economy is significantly smaller than that of the United States and Australia's other major trading partners. While Australia is similar in size to Canada, its legislative provisions which may protect small business from anti-competitive and unfair conduct- such as the prohibition against predatory pricing - have been criticised, most importantly, as being out of step with economic principles. Unlike Australia, Canada also lies adjacent to a much larger developed economy, which may affect Canadian policy and legislation.

The overriding consideration, therefore, is that while other jurisdictions' practices may appear helpful, care should be taken to ensure the measure in question is relevant to, and justified for, the efficient operation of the Australian economy.

[82] Baird Committee report, paragraph 7.7

Appendix 1 - Principles of competition regulation

This Appendix examines the touchstones of competition regulation, which were discussed in Section One of this submission.

1 Protecting competition not competitors

The Business Council believes, and the High Court has recently confirmed in the *Boral* decision, that the TPA is concerned with protecting the dynamic process of competition. This does not equate with the protection of specific competitors or classes of competitors.

The Business Council acknowledges that parts of the TPA are concerned directly with the protection of specific interests, especially those of consumers and small businesses. Section 51AC, for example, provides considerable protection to the small business sector.

The Business Council is concerned that legislative amendments to the TPA which seek specifically to protect small business may have the effect of protecting or insulating some players **from** competition. Consumers should not have to pay a premium to protect certain businesses. Where consumers see value in particular businesses, they can reflect that in their purchasing decisions.

The argument that the competition provisions of the TPA should be modified to protect small business has been run before. In its report, the Reid Committee stated that[83]:

> *"…section 46 of the Trade Practices Act does not address many of the problems small businesses encounter in dealing with powerful suppliers and competitors…it is not appropriate to attempt to protect small businesses through the competition provisions of the Trade Practices Act – which are designed to engender strong competition".*

To overcome the perceived limitations of section 46, the Reid Committee recommended strengthening the unconscionability provisions in Part IVA, with the result that section 51AC came into effect in July 1998. Section 51AC was, therefore, a direct result of the need to address unconscionable business transactions, while ensuring section 46 remained focused on protecting vigorous competition, not particular competitors.

It has been suggested that the TPA should be viewed as social legislation. This argument is often put as a justification for the TPA being used as a tool for protecting small competitors from the competitive processes. For example, during the Senate Inquiry into amendments to sections 46 and 50 of the TPA, Senator Andrew Murray stated[84]:

> *"…small business has a value in itself over and above an economic value. Whilst you may get numbers of small businesses which are inefficient, have higher prices than the majors et cetera, their existence as a component of society, as generators of activity in their communities and as the focus of community activity is worthwhile supporting in itself."*

[83] The Reid Committee at 135 [4.67].

[84] Australia, Senate Legal and Constitutional References Committee, *Hansard* 17 April 2002 at 39.

The Business Council considers that while these concerns may touch on legitimate social issues, any social dimension for Part IV of the TPA must be limited to the public policy position that strong and vigorous competition is beneficial to the long-term interests of consumers and the economy. The TPA is a powerful tool but its fundamental objective, as set out in section 2, should not be forgotten.

2 Equality before the law

In the Business Council's view, it is a fundamental principle of our legal system that all businesses and all individuals should be treated equally before the law. In particular, successful competitors should not be artificially constrained from competing fairly in the market place. Even where special provisions are considered appropriate to deal with, for example, the misuse of market power, these provisions should relate to the relevant characteristic of the firm, such as its market power, not to the size of the firm *per se*.

In discussions of 'inequality of bargaining power' there is a tendency to confuse size with power. From a competition perspective, what matters in dealings with a corporation is not its size but whether it is facing effective competition and whether it has "market power".

If the seller is in a competitive market, even a small buyer can be in an advantageous bargaining position. Before Ansett collapsed, for example, and even today, a consumer whose travel dates were flexible could obtain very low fares from the airlines, even though the sellers are billion dollar corporations.

On the other hand, when competition is weak, even a small supplier can reap monopoly rents, as can be seen in the prices of many goods and services in small country towns.

This point is relevant to proposals to amend section 51AC to proscribe, as *per se* offences, the unilateral variation of contracts, termination of contracts without just cause or due process, or the presentation of 'take it or leave it' contracts[85]. Proponents of this amendment argue that such conduct "*typically is made possible because of the market power held by large corporations*"[86] and "*only occurs because one party to a commercial transaction has much greater market power than the other*"[87]. As noted above, however, market power is not the same as corporate size, nor is it unique to large corporations. If prohibitions such as these were to be adopted, they would need to apply to all contractual dealings, regardless of whether the contractual parties were large corporations, small businesses or individual consumers. The issues such prohibitions raise for the certainty of the law are also discussed below.

3 Certainty of the law

Competition law should be sufficiently certain, such that businesses are able to understand the nature and scope of their obligations. In this way, businesses are able to comply with the competition provisions. Accordingly, the focus of competition regulation should be on clarity and compliance, rather than on prosecution and deterrence[88]. While prosecutions play a role in encouraging compliance, it is difficult for companies to comply with the TPA if its requirements are uncertain. Uncertainty can lead to

[85] Fair Trading Coalition, Submission to the Dawson Committee (July 2002, at 42); Council of Small Business Organisations of Australia, Submission to the Dawson Committee (July 2002, at 17).

[86] Fair Trading Coalition, Submission to the Review Inquiry (July 2002, at 42).

[87] Ibid at 43.

[88] For further discussion on this point, see PricewaterhouseCoopers, Submission to the Dawson Committee (July 2002).

unnecessary and excessive compliance costs. Where laws are certain and the requirements are clear, higher levels of compliance can be expected.

In considering proposed reforms to the TPA, regard should be had to whether these would enhance or detract from the certainty of the operation of the law.

4 Proportionality of response

There are significant dangers in both under-regulating and over-regulating. Due to globalisation, liberalisation of trade and investment and the evolution of new technologies, competition regulation is becoming more difficult and the costs of regulatory error are growing.

In light of this, it is essential that regulatory responses, in both legislative and administrative terms, are in proportion to the specific issues being addressed. Another approach to this is to ask whether the benefits of a proposed regulatory solution outweigh the costs. These issues often arise where regulatory solutions are proposed for very specific issues, often involving only a few companies or one part of the economy, but the new regulation imposes costs across all companies or sectors of the economy.

5 Using existing powers first

The Business Council submits that before new powers are added to the TPA, or existing powers are amended, the scope of existing powers to address concerns should be fully explored, particularly when those powers are relatively new and the relevant principles are still being developed by the Courts. Constantly changing the law creates uncertainty and confusion and does not allow the full impact of existing legislative requirements to be developed and tested.

6 Bedding down change

Related to the need to explore the potential of existing powers before amending existing ones or introducing new ones, is the need to allow the effect of recent changes to be felt before further changes are made.

When changes are made to legislation, there can be a significant lag before the effect of these changes is felt "on the ground". For example, there have been recent changes to the TPA to address many of the issues raised by some small business groups. These changes resulted from the inquiry of the Reid Committee and were given effect by the *Trade Practices Amendment Act (No 1) 2001*. These amendments expand considerably the options and protection available to small business and consumers under the TPA and it is likely to take some time before the scope and effectiveness of these provisions can be properly assessed.

8 Conclusion

The Business Council believes that the above principles should be used to test the appropriateness of proposals to amend or extend the TPA. The Business Council is of the view that many of the proposals that have been put forward do not meet these principles. It is for this reason that the same proposals have been repeatedly rejected by past inquiries.

Appendix 2 - Reviews of section 46 of the TPA

This Appendix outlines the broad history of reviews of the TPA, prior to the Dawsom Committee, as discussed in Section Two of this submission.

1 The Swanson Committee

The Trade Practices Act Review Committee (the **"Swanson Committee")** undertook a review of the TPA, including section 46, in 1976. It recommended two minor alterations to the language of section 46 which were subsequently implemented by the *Trade Practices Amendment Act 1977*. These changes were:

- The substitution of the words "for the purpose of" for the word "to" in subs (1); and,
- The insertion of a new subs (5) which provides:

  "Without extending by implication the meaning of sub-section (1), a corporation shall not be taken to contravene that sub-section by reason only that it acquires plant or equipment."

In the eyes of the Swanson Committee, the objective of these minor amendments was to make two things clear: first, that only a *purpose* to monopolise is required and not proof that the monopolistic purpose has been achieved; and secondly that monopolisation does not occur by reason only of investment in new plant and equipment (the test of section 46 at the time was one of monopolisation, rather than of substantial market power, as is the current provision).

2 The Blunt Committee

In 1979, the Trade Practices Consultative Committee (the **"Blunt Committee")** recommended some major alterations to the language of section 46 which were subsequently implemented by the *Trade Practices Revision Act 1986*. The Blunt Committee felt that the threshold condition of requiring corporations to be in a position "*substantially to control a market*" was too restrictive. Accordingly, it recommended that these words be replaced by a new threshold test that would only require a corporation to have a substantial degree of market power to come within the ambit of the section.

This recommendation was, however, made conditional upon retention of the test of purpose. The Trade Practices Commission **("TPC")** in its submission to the Blunt Committee had argued against the purpose test because of problems of proof. The Blunt Committee rejected this submission by saying:

> *"we are concerned that removing the purpose element altogether could give the provision a very wide application and bring within its ambit much legitimate business conduct. It is also a fundamental aim that competitive conduct should not be outlawed ... there is a need to place some limit on the application of the section. It is only purposive misuse of market power and not inadvertent conduct or efficiency inspired conduct that should be at risk… Accordingly, we*

recommend that the purpose element should remain because we consider it is fundamental to a provision dealing with misuse of market power"[89].

3 Green Paper on "The Trade Practices Act Proposals for Change"

The 1984 Green Paper, "*The Trade Practices Act Proposals for Change*", questioned the effectiveness of section 46 on the basis that the requirement of "*substantial control*" of a market was so onerous that it applied to only a few powerful corporations. This led to legislative change in 1986, when section 46 was amended to lower the threshold, requiring a corporation to have only a "*substantial degree*" of power in a market. At the same time, the heading of the section was changed from "*Monopolisation*" to "*Misuse of market power*".

The 1986 amendments to the TPA made some other significant changes to the previous "monopolisation" provision. These changes were:

(a) in determining market power the court shall have regard to the extent to which the conduct of the relevant body corporate and that of any related bodies corporate is constrained by competitors or potential competitors or persons supplied by the body corporate or from whom it acquires goods or services (section 46(3));

(b) *"Power"* be interpreted as *"market power"*, so that the substantial degree of power which must be held before the section applies refers to power possessed by the corporation by reason of its presence in the relevant market (section 46(4)); and

(c) the purpose element was retained, however, the courts were expressly permitted to conclude that conduct had been engaged in for a proscribed purpose not only from direct evidence but also *"by inference from the conduct of the corporation or any other person or from other relevant circumstances"* (section 46(7)). Furthermore, section 84 (conduct by directors, servants or agents deemed to be that of a body corporate) was amended so that the *"state of mind"* of a body corporate may be ascertained by the state of mind of a director, servant or agent of the body corporate acting within the scope of that person's actual or apparent authority (section 84(1)).

4 The Griffiths Committee

The Griffiths Committee tabled its report in Parliament in 1989. Among its recommendations were that section 46 be retained in its existing form because there was insufficient evidence to justify the introduction of an effects test.

5 Trade Practices Commission Guidelines and Background Paper

In 1990, in response to the Griffiths Committee's concerns, the TPC issued guidelines and a background paper outlining the general considerations it would take into account in determining whether there was a misuse of market power. These were whether the conduct:

[89] At paragraph 9.21 and 9.22

- adversely affects the competitive process;
- adversely affects consumers or users of the goods or services (in terms of price, quality, availability, choice or convenience);
- raises barriers to entry or hinders market growth; and
- can be justified on the grounds that there is a legitimate business reason for it.

Furthermore, the Guidelines and Paper set out a ten step process that the TPC would follow in assessing whether a corporation had engaged in conduct in contravention of section 46.

6 The Cooney Committee

In 1991, the Senate Standing Committee on Legal and Constitutional Affairs (the **"Cooney Committee")** recommended that section 46 be amended to emphasise that the policy objective of the section is the protection of the competitive process rather than individual competitors. It concluded that an effects test might unduly broaden the scope of conduct captured by section 46 and challenge the competitive process itself. The Committee also rejected divestiture as an appropriate remedy, recommending instead that serious and persistent misuse of market power should be dealt with by increasing monetary penalties.

7 The Hilmer Committee

The Independent Committee of Inquiry into Competition Policy in Australia (the **"Hilmer Committee")** also considered whether to extend the prohibition in section 46 to conduct which has adverse "effects" on competition. It also examined a proposal to include a rebuttable presumption of intent in certain circumstances.

The Hilmer Committee concluded that section 46, as it stood, struck a fair balance between misuse of market power and aggressive competitive behaviour. It rejected the introduction of an effects test, saying that it would not adequately distinguish between socially detrimental and socially beneficial conduct.

7 The Reid Committee

In 1997, the House of Representatives Standing Committee on Industry, Science and Technology (the **"Reid Committee")** reported on an inquiry into the retail sector. It recommended an amendment to section 46 to provide that once it has been established that a corporation with a substantial degree of market power has used that market power, the onus of proof shifts to that corporation to prove it did not use that power for a prohibited purpose (as prescribed). The Reid Committee noted the effects test and the views of the Hilmer Committee but did not recommend its introduction.

8 The Baird Committee

In 1999, the Joint Select Committee (the **"Baird Committee")** investigated Australia's retailing sector in response to concerns of small and independent retailers about the pressures placed on them by a number of retail chains who were said to hold a substantial

degree of power in the market. The committee made some observations relevant to section 46 and devoted time to examining the merits of replacing the current "purpose" test with a "reverse onus of proof test". The committee stated that a possible amendment to section 46 could be to replace the current "purpose test" with a test that states that once it is established that a corporation with a substantial degree of power in a market has used that market power, the onus of proof shifts to that corporation to prove that it did not use that power for a prohibited purpose.

9 The Hawker Committee

In 2001, the House of Representatives Standing Committee on Economics, Finance and Public Administration **(**the **"Hawker Committee")** again considered the proposal to move to an effects test in section 46. It noted that there was significant opposition to an effects test and that it had been rejected by five inquiries since 1989. The Hawker Committee concluded that it preferred to await the outcome of further cases on section 46 before contemplating any change to the provision.

10 Senate Legal and Constitutional References Committee Inquiry into section 46 and section 50 of the TPA

This inquiry, in 2002, looked into the question of whether the TPA should be amended to reverse the onus of proof under section 46 in actions brought by the ACCC, where it could first be shown that the corporation had a substantial degree of market power and had taken advantage of that market power. The Committee generally deferred its consideration of this question pending the outcome of the Dawson Inquiry.

Appendix 3 - Recent cases on section 46

This Appendix outlines a number of key decisions concerning section 46 of the TPA, which are dealt with in Section Two of this submission.

1 Melway Publishing Pty Ltd v Robert Hicks Pty Ltd t/as Auto Fashions Australia[90]

- High Court decision - 2001

  Melway, the publisher of street directories, was found not to have contravened section 46 when it cancelled the distributorship of a company that distributed its Melbourne street directory and appointed another distributor. Melway was found to have the requisite degree of market power, and the evidence of its employees suggested that it had the requisite anti-competitive purpose. The case against Melway failed because the High Court found that Melway's actions did not amount to a use of its market power, not because the requisite purpose could not be shown.

- ACCC response to decision

  The ACCC welcomed this decision, stating that even though the Court found that Melway did not breach section 46, it clarified critical aspects of section 46. In particular, the ACCC noted that section 46 may be contravened where the conduct in question is materially facilitated by a firm's substantial degree of market power.

  Moreover, the then Chairman of the ACCC, Professor Fels, stated that such a decision provided assistance to small businesses by demonstrating that the Court will protect their legitimate interests, the competitive process and consumers from abuses of large and powerful market participants[91].

2 Rural Press v ACCC[92]

- Full Court of the Federal Court decision - 2002

  This was a decision concerning actions of the Rural Press (owners of *The Murray Valley Standard*) in pressuring Waikerie Printing (owner of *The River News*) to stay out of its territory. Following telephone calls, discussions, correspondence and threats by Rural Press to commence publishing a rival newspaper in direct competition with *The River News*, Waikerie Printing agreed to revert to its prime circulation area, which stopped 40km north of the Rural Press territory.

  Mansfield J at first instance had found that Rural Press had misused its market power. On appeal, Rural Press accepted that it had a substantial degree of power in the market and so the Full Court of the Federal Court considered whether their conduct amounted to a misuse of that power.

[90] (2001) 205 CLR 1.

[91] "*High Court confirms and enhances current approach to 'misuse of market power'*" ACCC Media Release, 16 March 2001.

[92] [2002] FCAFC 213.

The Full Court of the Federal Court found that Rural Press had the proscribed purpose of preventing Waikerie Printing from competing in the market, but the critical question was whether it had taken advantage of its market power. Following the *Melway* decision, the Court held that, even in a perfectly competitive market, Rural Press could have threatened to enter or actually enter the market in which Waikerie Printing competed. On this basis, the Court found that Rural Press was utilising something other than market power in making those threats. The Court noted that the issue of whether financial resources are relevant to the existence of market power is debateable. It went on to state that while the existence of resources in this case may have been either the ultimate cause or result of market power, Rural Press' use of those resources was not "taking advantage of" market power.

- ACCC's response to decision

  While the ACCC was disappointed that the Court did not accept that Rural Press took advantage of its market power in its dealings with Waikerie Printing, it welcomed the Court's finding that Rural Press had entered into an arrangement with another company which contravened section 45. The ACCC was also pleased that the Court accepted the submissions on penalties[93].

The High Court has heard the ACCC's appeal against the decision of the Full Court of the Federal Court's decision. Judgment has been reserved.

[93] *"ACCC and Rural Press"* ACCC Media Release, 18 July 2002.

Appendix 4 - Recent cases under section 51AC of the TPA

This Appendix outlines recent cases discussed in Section Three of this submission.

1 ACCC v Simply No-Knead (Franchising) Pty Ltd[94]

Simply No-Knead was the owner of a business that supplied training and materials for the making of bleach and related domestic products. From 1989 to 1999, Simply No-Knead franchised its business. In June 1999, the ACCC commenced proceedings on behalf of the franchisees seeking relief that included a declaration that Simply No-Knead had engaged in conduct in contravention of section 51AC(1).

The Federal Court delivered its judgment in 2000, holding that Simply No-Knead's conduct was "unreasonable, unfair, harsh oppressive and wanting in good faith".[95] The Court's clear reference to "unfair" and "unreasonable" behaviour suggests that section 51AC's scope is considerably broader than section 51AA's "unwritten law" notions. The decision also challenges any concerns that Part IVA is too narrowly expressed as the Court further stated that it is aided but not controlled by the factors listed in section 51AC(3).

ACCC reaction[96]

The ACCC said that the Court's decision in *Simply No-Knead* made it clear that while the meaning of 'unconscionable' conduct in section 51AA will be limited to the meaning it has in equity or unwritten law, 'unconscionable' conduct for the purposes of section 51AB and section 51AC has a broader or expanded meaning. For example, it is not necessary for a person wanting to establish a contravention of section 51AB or 51AC to show that the weaker party was in a position of special disadvantage and that the stronger party took unfair advantage of this.

The acceptance by the Court of this broader meaning of unconscionable conduct in section 51AB and 51AC will help the ACCC better protect the interests of small businesses from excesses in conduct by businesses with market power.

2 ACCC v Leelee Pty Ltd[97]

Leelee Pty Ltd ("**Leelee**") was the landlord of the Adelaide International Food Plaza and its business included leasing food stalls to various food stall operators. From 1991 to 1999, the Choongs were proprietors of the "Blessing Noddle Bar", a food stall space leased out from Leelee. In 1999 the Choongs complained to the ACCC about the conduct of Leelee. Following an investigation, the ACCC alleged that Leelee had engaged in unconscionable conduct toward the Choongs in breach of section 51AC.

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[94] (2000) 104 FCR 245

[95] See also www.accc.gov.au/speeches/2001/fels_business_centre_23_2_01.htm and John Martin, "Commercial Unconscionability and the TPA" (15 November 2001) at www.accc.gov.au.

[96] *"Federal Court finds Franchisor's Conduct Unreasonable, Unfair, Bullying and Thuggish"* ACCC Media Release, 25 September 2000.

[97] (2000) ATPR 41-472

In 2000, the Federal Court granted declarations and injunctions against Leelee, holding that the fact that Leelee may have been exercising contractual rights was not necessarily a circumstance which precludes a finding of unconscionable conduct in the circumstances.

ACCC reaction[98]

Following the decision the then Chairman of the ACCC, Professor Fels, issued a media release stating:

> "*This case is the first step in creating law in this particularly difficult area… I welcome the Court's acknowledgment that this conduct was in breach of the unconscionable conduct provisions of the Act*".

3 ACCC v Cheap as Chips Franchising Pty Ltd

One factor that the courts will consider in examining matters under 51AC is failure to comply with an industry code. Cheap as Chips, a chemical cleaning company, terminated a franchise without following the procedures contained in the Franchising Code. The Federal Court handed down its decision in 2001, declaring that the franchisor's director attempted to contravene the Code by trying to prevent a franchisee from associating with other franchisees for lawful purposes and was also knowingly concerned with other contraventions of the TPA. Cheap as Chips was restrained from engaging in similar conduct and was ordered to provide its franchisees with reasonable access to its records; to notify all current franchisees about the outcome of the legal proceedings; to pay compensation, interest and the ACCC's legal costs; and to implement a trade practices compliance program.

ACCC reaction[99]

Following the decision, the ACCC issued a media release stating:

> "*This is another win for small businesses and franchisees and another step in creating law in this particularly difficult area. In other recent cases the courts have held that unreasonable, unfair, bullying and thuggish behaviour by a franchisor can contravene the unconscionable conduct prohibitions in the Act… The prohibitions on unconscionable conduct in Part IVA of the Act will continue to be one of the ACCC's enforcement priorities*."

[98] *"Court declares landlord's conduct unconscionable"* ACCC Media Release, 25 June 2000.

[99] *"Franchisees awarded $82,000 compensation for unconscionable conduct"* ACCC Media Release, 16 March 2001.

Appendix 5 - Measures to assist small business

This Appendix outlines other measures which assist small business, which are discussed in Section Five of this submission.

1 Commonwealth Government's measures

- The Business Entry Point gives information on government obligations and compliance for small business;
- Area Consultative Committees give information on policies and programs of assistance to the business;
- Info Access Network gives information on Commonwealth Parliamentary and Government information;
- State and Territory small business advisory services offer a range of assistance services and information;
- Australian Securities and Investments Commission website provides information on corporations law compliance;
- the ACCC provides information on the Franchising Code of Conduct;
- the Grocery Industry Ombudsman provides information on the Retail Grocery Code of Conduct;
- the ACCC small business unit assists with any concerns or enquiries about trade practices and fair trading matters;
- the Commonwealth Purchasing and Disposals Gazette provides information on tendering and supplying to the Government;
- the Industry Capability Network helps businesses source competitive local supplies, ensuring that Australian companies have a full, fair and reasonable opportunity to supply goods and services to a project that may otherwise be sourced from overseas; and
- Austrade has a number of schemes including an Export Development Market Scheme, a New Export Development Program, Export Access Program and TradeStart facilitates exports.

2 Office of Small Business

The Office of Small Business which is located within the Department of Industry, Tourism and Resources publishes its "*Annual Review of Small Business*". In its most recent review it outlined a number issues, including the following which relate to assistance provided to small business in dealing with anti-competitive and unfair conduct:

- the healthy state of the economy providing an environment for small business to grow;
- the recent deliberations of the Small Business Consultative Committee;
- meetings of the Small Business Ministerial Council;
- the ACCC's role in assisting small business;
- the Retail Grocery Industry Code of Conduct review; and
- developments in franchising.