Australian Competition & Consumer Commission

AUSTRALIAN COMPETITION AND CONSUMER COMMISSION

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY INTO THE EFFECTIVENESS OF THE *TRADE PRACTICES ACT 1974* IN PROTECTING SMALL BUSINESS

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EXECUTIVE SUMMARY

This submission outlines the Australian Competition and Consumer Commission's (ACCC) response to the terms of reference provided by the Senate Economics Reference Committee (Senate Committee) inquiry into the effectiveness of the *Trade Practices Act 1974* (the Act) in protecting small business.

The submission notes the ACCC's role in promoting competition and fair trading and in providing consumer protection. It then proceeds to address each of the Senate Committee's heads of reference specifically.

In developing this submission, the ACCC has drawn upon its national database of complaints and inquiries and its experience both in administering and enforcing the Act, particularly in light of recent judicial decisions bearing on the relevant provisions. It has also drawn upon its experience in assisting small business operators and their representative organisations to understand their rights and responsibilities under the Act.

In addition to providing its views on the degree to which various parts and provisions of the Act provide protection for small business, the ACCC has put forward a number of proposals for consideration by the Senate Committee. These proposals are summarised as follows:

In relation to the misuse of market power

The development of case law has provided increasing clarity as to the operation of s. 46. However, subsequent to the Dawson Committee completing its consultations with interested parties, several decisions of the Full Federal Court and the High Court, particularly the decision of the High Court in *Boral Besser Masonry Ltd (Now Boral Masonry Ltd) v ACCC*,[1] have raised issues as to the application and operation of s. 46. These recent decisions suggest that courts are not consistently applying s. 46 in accordance with the policy intention of Parliament.

These decisions have, to some degree, shifted the focus of s.46 to the 'market power' and 'take advantage' elements of the provision. The following proposals are directed largely to those issues.

1. It is desirable to provide immediate guidance to the courts and certainty to market participants as to the substantial market power element of s.46. The policy intention behind s.46 should be given effect by amending s.46 to clarify the following principles:

    - the threshold of 'a substantial degree of power in a market' is lower than the former threshold of substantial control;

[1] *Boral Besser Masonry Ltd (Now Boral Masonry Ltd) v ACCC* [2003] HCA 5

- the substantial market power threshold does not require a corporation to have an *absolute* freedom from constraint – it is sufficient if the corporation is not constrained to a *significant* extent by competitors or suppliers;
- more than one corporation can have a substantial degree of power in a market; and
- evidence of a corporation's behaviour in the market is relevant to a determination of substantial market power.

2. The ACCC takes the view that it would be appropriate to amend s.46 by providing further clarification as to the 'take advantage' element of the provision. Relevant amendments should clarify the following principles:

   (a) the 'take advantage' element should be applied by the courts consistently with the underlying policy and existing High Court authority – the relevant inquiries are:
   - whether the corporation would be likely to engage in the conduct in a competitive market;
   - whether the conduct of the corporation was materially facilitated by its substantial degree of power in the market; and
   - whether the conduct was otherwise in reliance upon or related to its substantial degree of power in the market.

   (b) an inquiry as to the business rationale for the relevant conduct may be a relevant circumstance, but is not critical, to determining whether a corporation has taken advantage of its substantial market power in any particular matter.

3. The ACCC takes the view that s.46 requires amendment to provide, in predatory pricing cases, that it is not necessary to find an expectation or likely ability to recoup losses in order to establish a contravention of s.46. Such an amendment would ensure that the application of s.46 is consistent with Parliament's stated intention.

4. The ACCC considers that it would be appropriate to amend s.46 to clarify that the provision applies to any use of substantial market power with a proscribed purpose, irrespective of whether the conduct takes place in the same market where the power exists.

There are also a number of legislative deficiencies relating to s.46 that cannot be resolved by further judicial development. These problems would benefit from immediate consideration of legislative amendments to promote the efficacy of s.46 and the Act in dealing with conduct that is damaging to the competitive process.

5. The ACCC takes the view that s.46 requires amendment to enable market power analysis to encompass the concept of coordinated interaction in the absence of an

explicit agreement. Misuse of coordinated market power can be as damaging to competition as unilateral misuse of market power.

6. The ACCC considers that it would be appropriate to amend the Act to extend the application of s.155 powers until substantive enforcement proceedings have commenced.

In relation to unconscionable conduct

7. It appears to be an arbitrary distinction to draw a difference in applicability of section 51AC based on whether the quantum of the transaction is above or below $3 million. The limit suggests that the legislation is intended to protect not merely small businesses but corporate consumers of a commercially significant size. The limitation therefore no longer appears to be warranted.

8. The ACCC recommends that the imposition or exploitation of an unfettered unilateral variation clause, by a businesses in a superior bargaining position, should be added to the list of factors that a court may have regard to when determining whether conduct is unconscionable within the meaning of s.51AC.

In relation to industry codes of conduct

9. The ACCC believes that a system of ACCC endorsed voluntary codes of conduct has the potential to provide effective industry codes of conduct that deliver real benefits to businesses and consumers with the least possible compliance costs placed on consumers or business.

   The role of the ACCC will be to assist industry groups in ensuring the success of their codes. The industry will need to demonstrate that its code is achieving its objectives before the ACCC will provide endorsement. Endorsement from the ACCC will be hard to obtain and easy to lose. The aim of such endorsement is to reassure businesses and consumers that the code participant they are dealing with operates in a fair, ethical and lawful manner.

In relation to other measures

10. The ACCC notes that the Commonwealth Government is developing a small business collective bargaining notification process based on recommendations of the Dawson review. The Government noted that it will be 'speedier and simpler for small business than existing processes' – that is, than the authorisation process.[2] The ACCC agrees that the proposal will streamline the process for small businesses seeking to apply for immunity for collective bargaining where those arrangements are considered to be in the net public benefit.

[2] Commonwealth Government response to the Review of the Competition Provisions of the Trade Practices Act 1974, p7.

The submission will now outline the context in which these proposals are made and the rationale on which they are based.

INTRODUCTION

In administering the competition and consumer protection provisions of the Trade Practices Act the ACCC has regard to the welfare of Australians through the promotion of competition and fair trading and provision for consumer protection.

This submission combines information from a variety of sources within the ACCC and its counterparts in the Organisation for Economic Cooperation and Development (OECD) to respond to the terms of reference outlined by the Senate Committee.

The purpose of competition policy and competition law is to promote and protect competition in the interests of consumers. Competition law is not about preserving competitors or protecting certain sectors of business from the rigours of competition.

Businesses that are able and motivated to take advantage of the competitive environment through innovation, improved efficiencies, keen pricing, quality service standards and other forms of vigorous competition will thrive. But businesses that are unable or unwilling to respond to the challenges of competition will languish and may ultimately fail.

It may be the case that to promote and nurture competition in a market, it is necessary to intervene to protect competitors or a class of competitors in that market from substantial damage or indeed elimination as a result of a course of behaviour by another competitor.

The difficult task is to distinguish between vigorous but lawful conduct that is likely to lead to significant benefits for consumers, and unlawful anti-competitive behaviour which may disadvantage consumers.

Whilst the competitive provisions of the Act are directed at promoting and protecting competition and not protecting individual firms, there are also provisions that act to protect smaller firms in their dealings with larger enterprises.

These provisions apply not to market conduct but instead to situations where a smaller firm is either a customer or supplier to a larger company. These provisions seek to establish a fair and equitable trading environment.

In enforcing these provisions, the ACCC very much has in mind the interests of small business and their ability to trade with larger firms in a fair, if sometimes robust, environment.

The unconscionable conduct provisions were introduced to redress the imbalance of bargaining power between small and large business. The provisions, and in particular s.51AC, are still relatively new and are the subject of a number of cases currently before the courts. Both s.51AC and Part IVB, which provides a framework for the prescription of industry codes of conduct, together with the Franchising Code of Conduct (the first mandatory code prescribed under Part IVB) took effect as of 1 July 1998. The ACCC

received funding from 1998 for four years to extend its small business education, information and enforcement activity at that time. This funding has now ceased.

Although the unconscionable conduct provisions do not have the backing of the pecuniary penalties which are attached to breaches of the misuse of market power provisions[3], they still remain an effective tool for small businesses. This is because many small businesses are not looking to penalise such conduct. Instead, what they seek is an opportunity to run their own business in a fair and competitive environment.

This submission will now address, in greater detail, each of the questions within the terms of reference of the Senate Committee.

[3] And other provisions of Part IV of the Act

1 MISUSE OF MARKET POWER

Part (1)(a) of the Senate Committee's terms of reference specifically asks:

whether section 46 of the Act deals effectively with abuses of market power by big businesses, and, if not, the implications of the inadequacy of section 46 for small businesses, consumers and the competitive process.

1.1 Introduction

This submission considers the original policy intention of section 46 of the Act as a basis for the Senate Committee to assess the efficacy of the provision. It then provides an overview of recent consideration and judicial application of the provision, before identifying possible inconsistencies between the original intention and the recent application of section 46.

1.2 Background

The misuse of market power provision plays a vital role in the policy framework and objectives of Part IV of the Act.

Section 46 prohibits a corporation that has a substantial degree of power in a market from taking advantage of that power for the purpose of:

- eliminating or substantially damaging a competitor
- preventing the entry of a person into that or any other market, or
- deterring or preventing a person from engaging in competitive conduct in that or any other market.

Broadly, the objective of s.46 is to prevent firms with substantial market power from engaging in illegitimate unilateral anti-competitive conduct. Section 46 is a necessary complement to other Part IV prohibitions against cartel arrangements and vertical restrictions in that it is directed to ensure that the effects of such arrangements cannot be achieved individually by a person in a position of substantial market power. As one commentator has noted:

> There is little point in proscribing the fixing of prices at anticompetitive levels or the limiting of production by agreement between competitors if the purpose of achieving like results by one in a monopoly position (and hence, often, their achievement) is not controlled.[4]

A consideration of the effectiveness of s.46 in dealing with abuses of market power must first identify the standard by which its effectiveness is measured – the policy goal of the provision.

[4] B Donald & J Heydon, *Trade Practices Law*, Vol. 1, 1978, p.205.

1.3 The Policy Intention Behind Section 46

The Act is a broad statute that regulates many aspects of trade and commerce within Australia. The breadth of the Act is reflected in the objects statement in s. 2:

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

The objective of Part IV has been described judicially. For example, in *Refrigerated Express Lines (Australasia) Pty Ltd v Australian Meat and Livestock Corporation*, Justice Deane said:

> The general purpose and scope of the Part can be described by saying that it contains provisions which proscribe and regulate agreements and conduct and which are aimed at procuring and maintaining competition in trade and commerce.[5]

Consistent with these objectives, s.46 is designed to address the situation where a corporation with substantial market power uses that power to damage a competitor or potential competitor and thereby damages the process of competition. While s.46 is focussed on market conduct directed at competitors or potential competitors, it is not about protecting those competitors as an end in itself. Although s.46 does provide a degree of protection to firms from abuses of market power, it is important not to confuse the protection of competition with the protection of individual competitors.

It is an inevitable part of competition that some firms will be damaged, while some firms will prosper. Other firms will be forced to close because they are not able to compete efficiently or effectively. This is a normal feature of a vigorous, competitive market and is an important part of achieving the most efficient use of the nation's resources. The misuse of market power provision is not intended to hamper vigorous and legitimate competitive conduct.

In his Second Reading Speech introducing the *Trade Practices Bill 1974*, Senator Lionel Murphy made the following observations about the original section 46:

> Monopolisation is defined in clause 46… The clause covers various forms of conduct by a monopolist against his competitors or would-be competitors…
>
> Clause 46 as now drafted makes it clear that it does not prevent normal competition by enterprises that are big by, for example, their taking advantage of economies of scale or making full use of such skills as they have; the provision will prohibit an enterprise which is in a position to control a market from taking advantage of its market power to eliminate or injure its competitors.
>
> The provision will not apply merely because a person who is in a position to control a market engages in conduct within one of the classes set out in the clause. It will be necessary for the application of the clause that, in engaging in such conduct, the person concerned in taking advantage of the power that he has by virtue of being in a position to control the market. For example a person in a position to control a market might use his power as a dominant purchaser of goods to cause a supplier of those goods to refuse to supply them to a competitor of the first

[5] (1980) ATPR 40-156.

> mentioned person – thereby excluding him from competing effectively. In such circumstances the dominant person has improperly taken advantage of his power.[6]

The Second Reading Speech for the *Trade Practices Revision Bill 1986* confirmed the original intentions of s.46 with the following observations about misuse of market power and the proposed amendments to s.46:

> A competitive economy requires an appropriate mix of efficient businesses, both large and small. Whilst large enterprises may frequently have advantages of economies of scale, there are many occasions when large size does not of itself mean greater efficiency. However, a large enterprise may be able to exercise enormous market power, either as buyer or seller, to the detriment of its competitors and the competitive process. Accordingly an effective provision controlling misuse of market power is most important to ensure that small businesses are given a measure of protection from the predatory actions of powerful competitors.[7]

The extrinsic materials at the time of both the introduction of s.46 and the 1986 amendments specifically identify small businesses as one category of competitors that may be particularly vulnerable to misuses of market power. Section 46 is designed to protect smaller and more vulnerable firms from the anti-competitive conduct of firms with substantial market power. Therefore, it is appropriate to prohibit conduct that is motivated by a purpose of eliminating or substantially damaging a competitor, preventing new entry by a potential competitor or deterring or preventing competitive conduct in a market.

This objective of protecting the competitive process has subsequently received wide judicial recognition, particularly in the three s.46 judgments delivered by the High Court.

In *Queensland Wire Industries v BHP*, Chief Justice Mason and Justice Wilson stated:

> [T]he object of s.46 is to protect the interests of consumers, the operation of the section being predicated on the assumption that competition is a means to that end.[8]

Justice Deane stated the object of s.46 somewhat more broadly:

> …the essential notions with which s.46 is concerned and the objective which the section is designed to achieve are economic and not moral ones. The notions are those of markets, market power, competitors in a market and competition. The objective is the protection and advancement of a competitive environment and competitive conduct…[9]

In *Melway Publishing v Robert Hicks*, Gleeson CJ, Gummow, Hayne and Callinan JJ stated:

> Section 46 aims to promote competition, not the private interests of particular persons or corporations.[10]

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[6] Senate Hansard. 30 July 1974.
[7] House of Representatives Hansard. 19 March 1986.
[8] (1989) 176 CLR 177 at 191.
[9] Ibid at 194.
[10] (2001) 205 CLR 1 at 13.

In *Boral*, the majority judgments reiterated the objective of s.46 to promote competition. Gleeson CJ and Callinan J referenced the earlier statements of the High Court and stated:

> 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.[11]

Justices Gaudron, Gummow and Hayne cited the above statement of Mason CJ and Wilson J from *QWI*[12]and made the following observation:

> The provisions of Pt IV are to be interpreted in accordance with the subject, scope and purpose of the legislation, in particular the object stated in s 2 of enhancing the welfare of Australians through the promotion of competition.
>
> The structure of Pt IV of the Act, does, despite the considerable textual differences, reflect three propositions found in the United States antitrust decisions. The first is that these laws are concerned with "the protection of *competition*, not *competitors*".[13] [emphasis in original. References omitted]
>
> …
>
> [T]he object of s 46 is not the protection of the economic well-being of competitors…[14]

Justice McHugh made the following observations about the intention of s.46:

> Section 2 of the Act declares that its object "is to enhance the welfare of Australians through the promotion of competition and fair trading and provision for consumer protection". The Parliament has determined that it is in the interests of consumers that firms be required to compete because competition results in lower prices, better goods and services and increased efficiency. …
>
> When a court applies the provisions of s 46 it must do so with the legislative object of the section in mind. While conduct must be examined by its effect on the competitive process, it is the flow-on result that is the key - the effect on consumers, not the effect on other competitors. Competition policy suggests that it is only when consumers will suffer as a result of the practices of a business firm that s 46 is likely to require courts to intervene and deal with the conduct of that firm.[15]

Accordingly, the High Court has placed particular emphasis on the objective of s.46 to protect the process of competition. However, it is notable that in contrast to the other provisions of Part IV, the terms of s.46 do not explicitly protect competition through the application of a substantial lessening of competition test. The form of the purpose test in s.46 differs from the purpose or effects test in sections 45 and 47. To establish a misuse of market power in contravention of the Act, there is no explicit requirement to prove that the conduct has harmed consumers or damaged competition generally.

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[11] [2003] HCA 5 at para 87
[12] ibid at para 164
[13] ibid at paras 159-160
[14] ibid at para 186
[15] ibid at paras 260-261

1.4 The Dawson Inquiry

In its submissions to the Dawson Committee, the ACCC proposed that the objective of protecting the process of competition would be enhanced by two amendments to improve the operation of s.46:

- The introduction of an 'effects test' to supplement the existing 'purpose' test, and
- Allowing faster action in certain cases, specifically by the introduction of cease and desist orders.

The arguments in favour of the inclusion of an effects test in s.46 and a power for cease and desist orders were set out in the ACCC's Submission to the Dawson Committee.[16]

The High Court handed down its decision in *Boral* after the terms of the Dawson Report were finalised in January 2003. The Dawson Committee subsequently reaffirmed its recommendations in respect of s.46 of the Act and the Treasurer released the Dawson Report and the Commonwealth Government's response in April 2003.

The views expressed by the Dawson Committee as to the policy of Part IV are consistent with the policy objective of s.46 discussed above:

> In a relatively small economy like Australia, the misuse of market power can be particularly detrimental to competition. The competition rules in Part IV of the Act seek to restrain conduct that tends to lessen competition… Where a corporation has acquired market power, the Act protects consumers and other businesses from its misuse.
> …
> Part IV seeks to prevent conduct that may lessen competition, not to protect less competitive businesses. The distinction is an important one. However, some of the submissions made to the Committee in support of changes to Part IV appear to conflate these two objectives.
> …
> [C]oncentrated markets should attract scrutiny to ensure that competition is maintained, but the purpose of the competition provisions of the Act is to promote and protect the competitive process rather than to protect individual competitors. The competition provisions should not be seen as a device to achieve social outcomes unrelated to the encouragement of competition. As a matter of policy those outcomes may be regarded as desirable, but the policy will not be competition policy. Nor should the competition provisions seek the preservation of particular businesses or of a particular class of business that is unable to withstand competitive forces or may fail for other reasons. Those are matters which may legitimately be the subject of an industry policy, but that is not a policy which is to be found in the competition provisions in Part IV of the Act.[17]

However, the Dawson Committee recommended that no amendments be made to s.46.

In relation to the proposal for cease and desist orders, the Dawson Committee recommended that the Act should not be amended to introduce a power to make cease and desist orders or to extend the powers of the ACCC under section 155 of the Act so that they apply after the commencement of judicial proceedings.

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[16] Australian Competition and Consumer Commission. *Submission to the Trade Practices Act Review. June 2002.* Chapter 3.
[17] Committee of Inquiry. *Review of the Competition Provisions of the Trade Practices Act.* January 2003. p29 and pp36-37

The decisions of the High Court in *Boral* and of the Full Federal Court in *Safeway* and *Universal/Warner* were handed down after the Dawson Committee had completed its consultations with interested parties. Those decisions have, to some degree, shifted the focus of s.46 to the 'market power' and 'take advantage' elements of the provision. The proposals in this submission are directed largely to the issues raised by those subsequent decisions.

1.5 Recent Judicial Decisions on s.46

Boral v ACCC

On 7 February 2003, the High Court of Australia handed down its first decision about below cost pricing under section 46 of the Act.[18] By a 6-1 majority, the High Court found that Boral Masonry Ltd did not breach the misuse of market power provisions of the Act as alleged by the ACCC. This decision overturned a unanimous decision of the Full Court of the Federal Court. The Court's decision was based on a finding that Boral Masonry Ltd did not have substantial market power.

ACCC v Safeway

On 30 June 2003, the Full Court of the Federal Court partially upheld the ACCC's appeal against the first instance decision of Justice Goldberg, who dismissed proceedings brought by the ACCC against Australian Safeway Stores Pty Limited.[19] The ACCC alleged that Safeway engaged in conduct in contravention of the price-fixing, misuse of market power and other provisions of the Act in the Victorian bread market. The majority of the Full Court found that on four of nine instances pleaded against Safeway the company had misused its market power as a wholesale purchaser of bread for an anticompetitive purpose.

The ACCC has sought special leave to appeal to the High Court in respect of the five instances that the Full Federal Court found Safeway had not engaged in misuse of market power. Safeway has also filed an application for special leave to appeal both the findings of misuse of market power and price fixing.

ACCC v Universal/Warner cases

In September 1999 the ACCC instituted proceedings against Warner Music and Universal Music. The ACCC alleged that the action taken by PolyGram, (since been taken over by Universal) and Warner preventing retailers from stocking parallel imports of CDs breached the exclusive dealing section of the Act; and breached the misuse of market power section 46 of the Act, by taking advantage of their market power to deter retailers from engaging in competitive conduct. At trial, the court found that Warner and

[18] *Boral Besser Masonry Ltd (now Boral Masonry Ltd) v ACCC* [2003] HCA 5 (7 February 2003)
[19] *ACCC v Safeway Stores Pty Ltd* [2003] FCAFC 149 (30 June 2003) on appeal. *ACCC v Australian Safeway Stores Pty Ltd* (No 2) (2002) ATPR 46-215 at trial.

Universal did engage in the alleged misuse of market power and exclusive dealing conduct.[20]

Universal and Warner appealed the trial decision as to liability and the ACCC appealed on penalty. The Full Federal Court handed down its judgment on 22 August 2003, upholding breaches of s.47 and increasing the penalties in respect of those contraventions. However, the Full Court found that neither PolyGram nor Warner had a substantial degree of power in the market and consequently there was no breach of s.46 of the Act. At the date of this submission none of the parties have sought special leave to appeal to the High Court.

It should be borne in mind that *Boral*, *Safeway* and *Universal/Warner* have significant factual differences. *Boral* was essentially a predatory conduct case, involving allegations of low pricing and capacity expansion, with the added dimension of an oligopolistic market structure. *Boral* provided the courts with the opportunity to clarify the application of s.46 to predatory conduct. *Safeway* by contrast, is a more traditional misuse of market power case involving the imposition of anti-competitive terms of trade or a refusal to deal. In addition, *Safeway* was in the vein of a monopsonist construction as opposed to a monopolist context. *Universal/Warner* deals with the intersection of intellectual property and misuse of market power, addressing the concept of 'temporary monopolies.'

The decision of the High Court in *Boral* raised several issues as to the application of s.46 that are considered below. The decision of the Full Federal Court in *Safeway* may, to a degree, have alleviated some of the initial concerns about the *Boral* decision. However, the Full Court decision remains subject to High Court appeal and has brought other issues about the application of s.46 into sharp relief. The Full Federal Court in *Universal/Warner* followed the High Court decision in *Boral* and held that on the relevant findings of fact, Polygram and Warner did not have a 'substantial degree of power in a market' at the time of the conduct. The Universal/Warner decision has not however, provided further clarification of some of the issues raised by *Boral*.

1.6 Section 46 cases on appeal

The ACCC has one other s.46 matter currently on appeal.

ACCC v Rural Press

In July 1999 the ACCC instituted proceedings against Rural Press and its subsidiary, Bridge Printing Office, alleging misuse of market power and an anticompetitive arrangement in breach of s.45 of the Act. On 23 March 2001 Justice Mansfield found that Rural Press and Bridge Printing had misused their substantial market power in contravention of s.46.[21]

[20] *ACCC v Universal Music Australia Pty Ltd and others/Warner Music Australia Pty Ltd and others* (2002) ATPR 41-855

[21] *ACCC v Rural Press Ltd* (2001) ATPR 41-804.

On appeal, the Full Federal Court decided that while an arrangement between Rural Press Limited, its subsidiary Bridge Printing Office Pty Ltd, and Waikerie Printing House Pty Ltd did not contain an exclusionary provision, it did have the purpose or effect of substantially lessening competition in the Murray Bridge market for regional newspapers in breach of section 45 of the Act. The court also decided that Rural Press and Bridge Printing did not misuse their market power in breach of section 46 of the Act.[22]

On 11 April 2003, the High Court granted special leave applications of both the ACCC and Rural Press, including on the s.46 aspects of the case. The High Court hearing took place on 13 August 2003 and judgment has been reserved.

1.7 Current section 46 proceedings

The ACCC currently has four other s.46 matters on foot.

ACCC v Qantas

In May 2002, the ACCC instituted proceedings against Qantas, alleging a misuse of market power by substantially increasing capacity and reducing fares on the Brisbane–Adelaide route in response to the entry of Virgin Blue Airlines Pty Ltd onto the route.

ACCC v Fila Sport

In September 2002, the ACCC instituted proceedings against Fila Sports Oceania Pty Ltd for the implementation of a selective distribution policy in relation to the supply of Fila's AFL licensed apparel to retailers, alleging contraventions of ss. 46 and 47.

ACCC v Eurong Beach Resort

The ACCC filed proceedings against Eurong Beach Resort Ltd and others, alleging predatory pricing and other conduct in contravention of the Act in September 2002.

ACCC v Baxter

The ACCC instituted legal proceedings against Baxter Healthcare Pty Ltd in November 2002, alleging contraventions of sections 46 and 47 of the Act. The ACCC has alleged that Baxter used its power in the relevant markets by structuring its contract terms so that a State was required to acquire all of the relevant products as a tied bundle of products if it wished to have the benefit of significantly discounted prices.

1.8 Issues to be addressed

The development of case law has provided increasing clarity as to the operation of s.46. However, the ACCC notes that several recent judicial decisions, particularly *Boral*, have raised issues as to the application and operation of s.46. It appears that s.46 is not being consistently applied in accordance with the policy intention of Parliament. A number of these issues require close monitoring as s.46 continues to be applied by the Federal Court and the High Court. The issues raised by *Boral* and other current matters require careful attention to ensure that s.46 deals appropriately with misuses of market power. Options

[22] *Rural Press Ltd v ACCC* (2002) ATPR 41-883.

for legislative reform should be considered to give effect to the policy intention underlying s.46 and to ensure that the section is applied consistently by the courts.

Market Power

It is possible that the recent decision of the High Court in *Boral* may result in a narrower application of s.46, by supporting a restrictive interpretation of the requirement for a corporation to hold a 'substantial degree of power in a market.' The *Boral* decision has caused the ACCC to discontinue some investigations because of several statements of the High Court in relation to the market power element of s.46.

In 1986, s.46 was amended by the *Trade Practices Revision Act 1986* and the heading of the section was changed from 'monopolisation' to 'misuse of market power.' Significantly, the accompanying Explanatory Memorandum (extracts set out at **Attachment A**) indicated that the application threshold was intended to be lowered – from substantial control to 'a substantial degree of power in a market.'[23] The Explanatory Memorandum makes it clear that the new threshold was not intended to require an absolute freedom or independence from competitive constraint, with the consequence that s.46 could apply to more than one firm in a market with significant freedom from competitive constraint.

> A corporation having a 'substantial degree of market power' may have a lesser degree of market power than that of a corporation which 'would be, or be likely to be, in a position to … dominate a market' as provided in s.50 [as it was then]. 'Dominance connotes a greater degree of independence from the constraints of competition than is required by a 'substantial degree of market power.' Whatever the position in regard to 'dominance', more than one firm may have a 'substantial degree of power' in a particular market.[24]

The majority judgments in *Boral* contain several statements indicating an absolute freedom from constraint is required to establish a 'substantial degree of power' – effectively restoring the threshold to monopolists or near monopolists contrary to Parliament's intention behind the 1986 amendments.[25] Consistent with some statements of the majority in *Boral*, the dissenting judgment of Justice Emmett in the subsequent Full Federal Court *Safeway* appeal defines market power as 'the absence of constraint' and 'the advantage that flows from monopoly or near monopoly' in holding that Safeway did not have a substantial degree of power in the market. [26] (Relevant extracts from the cited judgments are set out at **Attachment B**.) By definition, more than one firm in a market cannot be a monopolist or near monopolist. Consequently, it appears that s.46 does not apply as broadly as was intended by Parliament.

However, the majority of the Full Federal Court in *Safeway* applied a threshold test for 'substantial degree of power' in a manner that appears consistent with the intention of the lower application threshold from the 1986 amendments.[27] Safeway and the ACCC are

[23] See paras 35, 37, 42 and 45.
[24] *Trade Practices Revision Bill 1986.* Explanatory Memorandum at para 45.
[25] See paras 121, 137, 146, 264, 287, 289 and 293. cf majority in *Melway* at para 43.
[26] See paras 457-458, 460-461.
[27] See paras 301-302.

both seeking special leave to appeal to the High Court on the findings of misuse of market power and consequently this issue may be specifically considered by the High Court in the near future. The Full Federal Court in *Universal/Warner* closely followed *Boral* and took the view that it was not necessary to deal with the difference between the pre-1986 market dominance threshold and substantial power in the market.[28]

Secondly, the High Court has previously applied two alternative definitions of market power. The majority judgments of the High Court in *Boral* gave primary emphasis to the ability of a firm to raise prices above supply cost as a test of market power.[29] However, the majority justices do not appear to give significant consideration to the alternative definition of market power as the ability to behave persistently in a manner different from that a competitive market would enforce.[30]

In the subsequent *Safeway* decision, the Full Court specifically approves the alternative approach to market power adopted by Dawson J in *QWI*; that market power may be manifested by market conduct other than raising prices.[31] This issue may also be the subject of further consideration and clarification by the High Court if special leave is granted in the *Safeway* case. The Full Federal Court in *Universal/Warner* found that it was not necessary to deal with the issue of whether pricing power alone is decisive of market power.[32]

It remains to be seen whether the High Court will confirm a possible narrower application of the market power element of s.46 in future cases. If special leave is granted, the *Safeway* case may allow the High Court to clarify the approach to market power adopted in *Boral*.

However, the ACCC takes the view that it is desirable to provide immediate guidance to the courts and certainty to market participants. The policy intention behind s.46 should be given effect by amending s.46 to clarify the following principles:

1. the threshold of 'a substantial degree of power in a market' is lower than the former threshold of substantial control;
2. the substantial market power threshold does not require a corporation to have an *absolute* freedom from constraint – it is sufficient if the corporation is not constrained to a *significant* extent by competitors or suppliers;
3. more than one corporation can have a substantial degree of power in a market;
4. evidence of a corporation's behaviour in the market is relevant to a determination of substantial market power.

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[28] *Universal Music Australia Pty Ltd v ACCC* [2003] FCAFC 193 at para 161

[29] See *QWI v BHP* (1989) 167 CLR 177 at 188 per Mason CJ and Wilson J applied in *Boral* at paras 100, 136, 194,199.

[30] see *QWI v BHP* (1989) 167 CLR 177 at 200 per Dawson J. Approved in *Melway* at 21 per Gleeson CJ, Gummow, Hayne and Callinan JJ. cf *Boral* at paras 30, 184 -186, 188, 194, 268, 312-314.

[31] See paras 299-300 per Heerey and Sackville JJ. See paras 455, 460 per Emmett J.

[32] [2003] FCAFC 193 at para 161

Take Advantage

In *QWI*, the High Court held that 'take advantage' does not require a hostile intent inquiry and that the expression simply means 'use.'[33] In *QWI*, the majority of the justices considered whether BHP would have been likely to engage in the relevant conduct if it lacked a substantial degree of market power. That approach was subsequently approved by the High Court in the *Melway* decision.[34] The *Boral* decision of the High Court does not provide any further clarification of the appropriate ways to apply the 'take advantage' element of s.46 as the 'market power' element was determinative of that case.[35]

In *obiter*, the *Melway* High Court also accepted that it was appropriate to consider whether the relevant conduct was 'materially facilitated' by the substantial market power of the corporation.[36] The 'materially facilitated' formulation of 'take advantage' has subsequently been applied by the majority of the Full Federal Court in *Safeway*.[37]

There appears to be some inconsistency in the way in which 'take advantage' is being applied by the Federal Court in s.46 cases that has the potential to create uncertainty in the application of the provision. The ACCC has appealed to the High Court in *Rural Press* on a number of issues including the Full Federal Court's application of the 'take advantage' element.[38]

The majority of the Full Federal Court in *Safeway* also found that the business rationale behind the particular conduct was 'critical' to the assessment of whether Safeway had taken advantage of its market power.[39] While the High Court has accepted that the business rationale of impugned conduct may be relevant to a finding that a corporation has taken advantage of its power,[40] there is a risk that the statement of the majority in *Safeway* may be relied upon to argue that a 'rational business conduct' defence has been introduced by a gloss on the 'take advantage' element.

The High Court may have the opportunity to further clarify the meaning and application of 'take advantage' in the *Rural Press* appeal and also in *Safeway*, if special leave is granted in respect of the s.46 conduct aspects of the case.

The ACCC takes the view that it would be appropriate to amend s.46 by providing further clarification as to the 'take advantage' element of the provision. Relevant amendments should clarify the following principles:

1. the 'take advantage' element should be applied by the courts consistently with the underlying policy and existing High Court authority – the relevant inquiries are:

[33] (1989) 176 CLR 177 see for example at 191.
[34] (2001) 205 CLR 1 at 21.
[35] Although see comments of Justice McHugh at para 279 that 'use' does not capture the full meaning of 'take advantage of'.
[36] (2001) 205 CLR 1 at 23.
[37] See para 333.
[38] See *Rural Press Ltd v ACCC* (2002) ATPR 41-883 paras 148-150.
[39] *ACCC v Safeway Stores Pty Ltd* [2003] FCAFC 149 (30 June 2003) at para 329.
[40] See statement of Heerey J, cited with approval by Gaudron, Gummow and Hayne JJ in *Boral* at para 170.

- whether the corporation would be likely to engage in the conduct in a competitive market;
- whether the conduct of the corporation was materially facilitated by its substantial degree of power in the market; or
- whether the conduct was otherwise in reliance upon or related to its substantial degree of power in the market.

2. an inquiry as to the business rationale for the relevant conduct may be a relevant circumstance, but is not critical, to determining whether a corporation has taken advantage of its substantial market power in any particular matter.

Predatory Pricing and the role of recoupment

It was the intention of Parliament that predatory pricing conduct, could in certain circumstances, breach s.46 of the Act.[41] The Full Federal Court has observed however, that 'predatory pricing' is not a statutory expression in Australia or in the United States. The majority judgment in *Eastern Express* stated:

> Caution is required in translating United States judgments, which place glosses upon the text of the United States antitrust laws, to the interpretation of the Australian law. Our law evinces a somewhat different approach to legislative drafting.[42]

Boral was the first opportunity for the High Court to specifically consider whether it is necessary to establish the possibility of 'recoupment' to prove that predatory pricing conduct contravenes s.46 of the Act.

'Recoupment' is a concept derived from economic analysis of predatory pricing conduct and has been applied in the United States context of antitrust jurisprudence. In *Brooke*,[43] the United States Supreme Court identified two elements to a predatory pricing claim:

(1) The plaintiff must establish that competitive injury resulting from a rival's low prices occurred as a result of prices being below an appropriate measure of its rival's costs; and
(2) The rival must have a 'dangerous probability'[44] of subsequent recoupment of lost profits.

As a result of the 1993 *Brooke* decision, it appears that the threshold for such claims has been set so high as to prevent subsequent predatory pricing cases from succeeding in the United States.

The European Court of Justice has subsequently rejected a requirement for recoupment to establish an abuse of dominant position infringing Article 82 of the EC Treaty. In the

[41] *Trade Practices Revision Bill 1986.* Explanatory Memorandum at para 53.
[42] *Eastern Express Pty Ltd v General Newspapers Pty Ltd* (1992) ATPR 41-167 at 40,306 per Lockhart and Gummow JJ.
[43] *Brooke Group Ltd v Brown & Williamson Tobacco Corp.* 509 US 209 (1993).
[44] Under s.2 of the *Sherman Act*.

Tetra Pak case, it was held that there was no requirement of proof that Tetra Pak had a realistic chance of recouping its losses.[45]

A requirement to establish an expectation of recoupment under s.36 of the New Zealand *Commerce Act* (the equivalent of s.46 of the *Trade Practices Act*) has also been rejected by the New Zealand Court of Appeal.[46]

The majority of the High Court in *Boral* did not expressly hold that recoupment is a necessary element of a predatory pricing claim under s.46. However, the majority judgments allow the possibility that s.46 will be interpreted to require the ability to recoup losses by pricing at supra-competitive levels. Specifically, one of the majority justices held that if a firm cannot recoup its losses by supra-competitive pricing it does not have market power and cannot take advantage of that power.[47]

The issue of what is required to establish unlawful predatory pricing remains contentious. It appears that any requirement of recoupment of losses to establish a contravention of s.46 would be contrary to Parliament's intention. The Explanatory Memorandum accompanying the 1986 amendments to s.46 stated:

> It is not the intention of s.46 that pricing, in order to be predatory, must fall below some particular cost. The prohibition in the section may be satisfied 'notwithstanding that it is not below marginal or average variable cost and does not result in a loss being incurred.'[48]

The ACCC takes the view that s.46 requires amendment to provide that in cases involving allegations of predatory pricing, a finding of expectation or likely ability to recoup losses is not required to establish a contravention of s.46. Such an amendment would ensure that the application of s.46 is consistent with Parliament's stated intention.

Leveraging market power – conduct in a second market

The concept of leveraging involves the use of market power in one market to give rise to market power in another market. The terms of s.46 explicitly proscribe the use of market power where the purpose is to exclude competitive conduct in the market where power is held, 'or any other market.' It is clear that s.46 will apply if a corporation *engages in conduct in the market where it holds substantial market power*, with the purpose of excluding competition in a second market.[49]

Until recently, it also appeared that a corporation with substantial power in one market could contravene s.46 through using that power *to engage in conduct in a second market* for one of the proscribed purposes. In *Victorian Egg Marketing Board*, the Federal Court found a prima facie case for a contravention of s.46 had been made out and granted an

[45] *Tetra Pak v European Commission* [1996] ECR 1 – 5951.
[46] *Carter Holt Harvey Building Products Group v The Commerce Commission* [2001] NZCA 298 at paras 29-30.
[47] See paras 278, 289 and 290 per McHugh J.
[48] *Trade Practices Revision Bill 1986.* Explanatory Memorandum at para54.
[49] See for example *QWI v BHP* (1989) 167 CLR 177

interlocutory injunction in circumstances where the Board had power in the Victorian egg market and used that power in the ACT egg market. The Full Federal Court dismissed an appeal from that decision and affirmed the grant of an interlocutory injunction.[50]

Chief Judge Bowen addressed the issues on the basis that the Board was in a position to substantially control the Victorian market but was not in a position to substantially control the ACT market. His Honour stated:

> The Board is taking advantage of its power in relation to the Victorian market by engaging in its price-cutting activities in the ACT.
>
> …
>
> It was argued that the Board could not contravene sec.46(1) unless the act of taking advantage was done in or in relation to the Victorian market. In my view however all that sec.46(1) requires is that there be a taking advantage of a power. The power in question is one in relation to a market which the corporation is in a position substantially to control. Properly construed the sub-section does not contain a further requirement that whatever it is that constitutes a "taking advantage", has also to be done in relation to that same market.[51]

The Full Federal Court in *Rural Press* has cast doubt on that construction and appears to have held that for there to be a taking advantage of power in a market, the relevant conduct must take place in the market where the power exists.[52] Such a limitation in the application of s.46 is not supported by the terms of the provision or the decision in *Victorian Egg*. However, in *Rural Press*, their Honours stated that 'the interlocutory nature of the [*Victorian Egg*] decision makes it of little value in resolving the present case.'[53]

If followed, the *Rural Press* decision may mean that s.46 no longer applies to situations where a corporation uses its market power from one market to engage in conduct in a second market as a means of leveraging. In other words, s.46 would have no application if a corporation with substantial market power uses that power to engage in conduct in a second market, even with the intention of increasing its power in the first market and/or damaging competition in the second market.

The High Court may consider the application of s.46 to leveraging conduct in the *Rural Press* appeal. However, the ACCC considers that it would be appropriate to amend s.46 in any event, to clarify that the provision applies to any use of substantial market power with a proscribed purpose, irrespective of the whether the relevant conduct takes place in the same market where the power exists.

1.9 Further deficiencies in relation to s.46

There are also a number of legislative deficiencies relating to s.46 that cannot be resolved by further judicial development. These problems would benefit from immediate

[50] *Victorian Egg Marketing Board v Parkwood Eggs Pty Ltd* (1978) ATPR 40-081.
[51] Ibid at 17,789. The comments reflect the terms of s.46 prior to the 1986 amendments that lowered the threshold from 'position substantially to control a market' to 'substantial degree of power in a market.'
[52] *Rural Press Ltd v ACCC* (2002) ATPR 41-883 paras 142 -148.
[53] Ibid at para 147.

consideration of legislative amendments to promote the efficacy of s.46 and the Act in dealing with conduct that is damaging to the competitive process.

Coordinated market power

Section 46 matters typically deal with allegations of the unilateral use of market power. Subsection 46(2) has the effect that the market power of related entities is to be considered jointly in assessing whether a corporation has a substantial degree of power in a market. However, it is not clear to what extent Australian jurisprudence recognizes the application of s.46 to the coordinated use of market power by unrelated firms.

The issue of coordinated market power was considered in *Dowling v Dalgety* and Justice Lockhart stated:

> A corporation charged with contravention of s.46 must itself have a substantial degree of market power. It cannot be liable under the section on the basis of a shared position of substantial market power with another unrelated corporation.
> …
> In my opinion, it is permissible, however, when considering the market power of a corporation, to have regard not only to its individual power but to additional power which it has through agreements, arrangements or understandings with others.
> …
> In short, a corporation may have power in a particular market gained through a variety of means and from a number of sources. Some of the power is held by the corporation through its own activities and some power is held because of its arrangements with others. Those arrangements must be taken into account when assessing the particular degree of power exercised by the individual corporation.[54]

Justice Lockhart did not have occasion to consider whether conscious parallelism or other forms of coordinated interaction would be sufficient to constitute 'agreements, arrangements of understandings' for the purpose of establishing whether an individual corporation has substantial market power.

In *Boral*, Chief Justice Gleeson and Justice Callinan observe that the ACCC's allegations appeared to suggest that there was collusion, or at least conscious parallelism, between BBM and Pioneer that would have allowed BBM to raise prices above competitive levels after a price war. However, that line was not pursued and at trial Justice Heerey 'rejected any hope or expectation of either collusion or conscious parallelism.'[55]

Nevertheless, the judgment of Chief Justice Gleeson and Justice Callinan suggests that where conscious parallelism or coordinated interaction can be established, it may be relevant to market power analysis:

[54] *Dowling v Dalgety Australia Ltd & Ors* (1992) ATPR 41-165. Cited with approval in *Eastern Express Pty Ltd v General Newspapers & Ors* (1992) ATPR 41-167 at 40,299 per Lockhart and Gummow JJ.
[55] para 92

> … it should be remembered that the ACCC originally endeavoured to make out a case involving at least conscious parallelism between BBM and Pioneer. That attempt failed. If it had succeeded, the case may have taken on a different complexion.[56]

An example of such coordinated interaction may be where a price war eliminates several competitors and the remaining firms are subsequently content to raise prices to supra competitive levels without further vigorous competition. In these circumstances, conscious parallelism in relation to pricing would effectively allow the remaining firms to jointly extract monopoly profits. If a corporation expects to be able to recoup its losses by supra competitive pricing made possible by conscious parallelism, this may assist a finding that the corporation possesses a substantial degree of market power.

Such coordinated interaction provides greater scope for misuse of market power than for a corporation on its own. The risks of coordinated market power are enhanced in highly concentrated oligopolistic markets, such as commonly exist in Australia.

In a concentrated market, there is a danger that the firms will find it easier to lessen competition by colluding. This collusion could be in the form of an explicit agreement, or take a more subtle form, which is known variously as tacit coordination, coordinated interaction or conscious parallelism. Firms may prefer to cooperate tacitly rather than explicitly because tacit agreements are more difficult to detect, and explicit agreements are subject to prosecution where tacit agreements are not.

The US Department of Justice and the US Federal Trade Commission have identified the possible nature and impacts of coordinated interaction:

> Firms coordinating their interactions need not reach complex terms concerning the allocation of the market output across firms or the level of the market prices but may, instead, follow simple terms such as a common price, fixed price differentials, stable market shares, or customer or territorial restrictions. Terms of coordination need not perfectly achieve the monopoly outcome in order to be harmful to consumers. Instead, the terms of coordination may be imperfect and incomplete – inasmuch as they omit some market participants, omit some dimensions of competition, omit some customers, yield elevated prices short of monopoly levels, or lapse into episodic price wars – and still result in significant competitive harm.[57]

Legislation in other jurisdictions gives explicit recognition to the ability of two or more corporations to exercise coordinated market power. It should be noted that these jurisdictions do not have the substantial market power threshold that applies under s.46.

The Canadian prohibition against abuse of dominant position is contained in s.79 of the *Competition Act.* The terms of the provision explicitly apply to 'one or more persons' who substantially control a market. Consequently, s.79 applies to the exercise of joint market power between unrelated firms where no single firm is dominant on its own. There is little judicial guidance as to what is required to establish joint dominance under s.79 in the absence of an explicit agreement. The Competition Bureau has indicated that for a joint dominance case, it would look for evidence of something more than conscious

[56] para 131
[57] US Department of Justice and the US Federal Trade Commission's 1992 *Horizontal Merger Guidelines*.

parallelism, such as coordinated behaviour to increase price or other conduct designed to inhibit intra-group rivalry.[58]

Article 82 of the EC Treaty, prohibiting abuse of dominant position, has also been interpreted to apply to positions of joint dominance held by two or more unrelated firms.[59]

If it is appropriate to prohibit the unilateral use of market power for a proscribed purpose, it is equally appropriate to prohibit the coordinated use of market power for a proscribed purpose. The ACCC takes the view that consideration should be given to amending s.46 to encompass the concept of coordinated market power in the absence of an explicit agreement, as contemplated by Gleeson CJ and Callinan J in *Boral*.

Enforcement issues – limitation on s.155 powers

The ACCC is concerned that its ability to address anti-competitive conduct quickly, by obtaining interim injunctions, is restricted by the limitation on the investigatory powers under s.155 of the Act.

Section 155 of the Act confers powers on the ACCC to obtain information, documents and evidence when investigating possible contraventions of the Act.

Section 155(1) provides that where the ACCC, the Chairperson or Deputy Chairperson has reason to believe that a person is capable of furnishing information, producing documents or giving evidence about a matter that constitutes, or may constitute a contravention of the Act, or is relevant to a decision under s. 93(3), a member of the ACCC may issue a notice requiring the person:

- to furnish information in writing within a specified time and in a specified manner (s. 155(1)(a))
- to produce documents specified in the Notice to the ACCC or to a person specified in the notice (s. 155(1)(b))
- to appear before the ACCC at a time and place specified in the notice to give evidence, either orally or in writing, and produce documents (s. 155(1)(c)).

Section 155(2) empowers a member of the ACCC to authorise in writing a staff member to enter premises and to inspect any documents in the possession of, or under the control of, a person the ACCC, the Chairperson or Deputy Chairperson has reason to believe has engaged, or is engaging, in conduct which constitutes or may constitute a breach of the Act and to make copies of or take extracts from those documents.

After the ACCC has commenced court proceedings, it is not able to issue a notice under s.155 of the Act, where the answer to the notice is relevant to those proceedings.[60]

[58] Canadian Competition Bureau. *Enforcement Guidelines on the Abuse of Dominance Provisions*. July 2001. p17

[59] see for example *Italian Flat Glass v Commission* [1992] 5 C.M.L.R. 302.

Consequently, if the ACCC seeks an interim injunction upon learning of anti-competitive conduct, its subsequent ability to fully investigate the matter is limited and the prospects for success in substantive proceedings are hindered. As noted at 1.4 above, the Dawson Committee considered and did not recommend an extension of s.155 powers so that they apply after the commencement of judicial proceedings.

The rationale for a limitation on s.155 powers is that the courts should maintain supervision of information disclosure and exchange between the parties to proceedings. The ACCC accepts that it would not be appropriate for it to have s.155 powers after the commencement of substantive proceedings for a contravention of the Act. However, the ACCC submits that it is not necessary to limit the application of s.155 powers at the interlocutory stage, prior to the commencement of substantive enforcement proceedings.

Parliament has seen fit to give the ACCC powers to compel parties to provide information where it has reason to believe such information may relate to a contravention of the Act. However, if the ACCC wishes to seek an urgent interim injunction to stop particularly egregious conduct while the matter can be fully investigated, it loses its powers to investigate under s.155.

The ACCC should have the ability to seek an interim injunction from the court, maintaining the status quo in a market, without limiting its ability to investigate and gather evidence of the substantive allegations. An extension of the powers under s.155 to the interlocutory stage would mean that the ACCC would be better placed to seek early intervention to protect targeted businesses, until judicial proceedings can be brought for alleged breaches of the Act. Early intervention to stop anti-competitive conduct would allow smaller businesses with limited resources to avoid bankruptcy before the ACCC can use its powers fully to investigate a matter and institute enforcement proceedings.

Similar issues arise not just in respect of misuses of market power, but also in relation to other breaches of the Act. Part IV matters usually require complex economic evidence and the demands of such cases mean that there can be considerable delays in enforcing breaches of the Act. The ACCC's recent experience is that the time between alleged breaches occurring and final court orders being handed down can be up to eight years. The ACCC considers that it would be appropriate to amend the Act to extend the application of s.155 powers until substantive enforcement proceedings have commenced.

1.10 Anti-competitive conduct by firms without substantial market power

The expression 'market power' describes a market in which competition is less than 'workable' or 'effective.' If a firm possesses market power it has the ability to some extent to increase its profits by giving less and charging more. Australian courts have also recognised that market power may be manifested through other practices designed to restrict competition.

[60] See *Brambles Holdings Pty Ltd v TPC* (1980) ATPR 40-179.

Market power has the potential to be detrimental to Australian society in many ways, including:

- Prices above competitive levels
- Reduced demand for goods or services resulting in a 'dead weight' loss
- Resources used to maintain or enhance market power instead of the production of goods and services desired by citizens.

It is not a contravention of the Act to hold market power or to seek to gain market power through superior economic performance. However, the key focus of Part IV is to restrict certain forms of behaviour which result in, or are likely to result in a situation of market power. Nevertheless, there is no provision under the Act that prohibits a corporation without substantial market power from engaging in illegitimate unilateral conduct to create or increase its market power.

Section 46 may, under certain circumstances, capture conduct that is designed to increase the market power of a firm by excluding rivals. However, if a firm engages in illegitimate unilateral conduct to reduce competition, but either does not have market power at the time of the conduct, or relies on some other form of power to engage in the conduct, it may not contravene the Act.

For example, section 46 does not capture predatory pricing conduct in circumstances where the predator does not have substantial market power *at the time* of the conduct in question. This possible 'gap' was specifically identified in several judgments of the High Court in *Boral*.[61]

Financial strength may enhance the ability of a corporation to persistently engage in conduct that seeks to exclude competition. Several statements of the High Court in *Boral* indicate that the financial resources of a corporation do not equate to market power.[62] Consequently, a corporation with 'deep pockets' that does not have substantial market power is not subject to the application of s.46. Such a 'gap' may enable corporations to engage in predatory pricing conduct with impunity, including targeting of particular businesses, without contravening the Act.

This 'gap' is a deficiency in the legislative framework and specific amendments would be required to address this issue. However, a new provision addressing illegitimate conduct designed to achieve market power would be a significant addition to Part IV of the Act.

[61] See paras 98, 163, 269 and 319. The Court referred to the paper Breyer, *Five Questions About Australian Anti-Trust Law – Part II* (1977) 51 Australian Law Journal 63 at 69.
[62] See paras 138, 317 and 364.

2 PART IVA – UNCONSCIONABLE CONDUCT

whether Part IVA of the Act deals effectively with unconscionable or unfair conduct in business transactions.

2.1 Introduction

As noted above, Part IVA of the Act contains provisions that act to protect smaller firms in their dealings with larger enterprises. These unconscionable conduct provisions were introduced to redress the imbalance of bargaining power between small and large business.

The provisions, and in particular s.51AC, are still relatively new and are the subject of a number of cases currently before the courts.

This submission will now address Part (1)(b) of the inquiry's terms of reference by considering Part IVA and its remedies generally before considering specific issues related to sections 51AA and 51AC specifically. This part of the submission will also outline a number of issues that are typically represented by small businesses as indicating unfair or unconscionable conduct and industry sectors in which small business complaints are common.

Part IVA of the *Trade Practices Act 1974* currently contains the following three provisions dealing with unconscionable conduct:

- s. 51AA which prohibits businesses dealing unconscionably with each other in all commercial situations, not just when buying or selling;
- s. 51AB which applies to transactions between businesses and consumers; and
- s. 51AC which specifically prohibits one business dealing unconscionably with another when supplying goods or services.

The content of the three sections indicates a clear aim to give broad protection for persons who are involved in activities with a corporation in trade or commerce. The sections not only prohibit engaging in *"conduct that is, in all the circumstances, unconscionable*" by reference to a non-exclusive broad list of factors suggesting a 'statutory unconscionable conduct' (sections 51AB and 51AC), but also "*conduct that is unconscionable within the meaning of the unwritten law, from time to time*" (section 51AA).

The scope of the protection afforded by Part IVA therefore becomes at least that which is statutorily proscribed, with additional protection which the common law from time to time recognises. This additional protection is indicated by the wording of subsection

51AA(2) which specifically excludes the common law applying through section 51AA if the conduct is prohibited by section 51AB or section 51AC, or to put it another way, the common law position is not applicable if the conduct is caught by sections 51AB or 51AC. From this it may be taken that, but for conduct prohibited by sections 51AB and 51AC, section 51AA would cover the field of "*conduct that is unconscionable*" under the Act.

Remedies available under part IVA

The equitable concept of 'unconscionable conduct' was originally used to set aside contracts where they had been procured unfairly. By making 'unconscionable conduct' a breach of the *Trade Practices Act*, a range of other remedies became available, such as

- injunctions restraining similar conduct in the future[63];
- where a person has suffered loss, the recovery of that loss[64];
- findings of fact[65];
- community service, probation or publicity orders[66]; and
- other remedial orders, such as declaring a contract void in whole or in part, varying the contract, or an order refusing to enforce a provision of the contract[67].

Pecuniary penalties are not available for breaches of Part IVA.

Unconscionable versus unfair conduct

While the provisions within Part IVA of the Act address 'unconscionable' conduct they do not proscribe conduct which is merely 'unfair' or 'hard bargaining'. The issue of unfair conduct will be addressed separately in this submission.

It is important that businesses are able to contract with each other with sufficient certainty, free from the risk that their agreements will be unnecessarily scrutinised after the fact. The courts have observed that it is not their intention to be able to substitute their own judicial conscience for the hard-headed decisions of business people[68].

The unconscionable conduct provisions do, however, recognise that small businesses can find themselves in a position where they are subjected to unreasonable behaviour by another business in a superior commercial position. Where one business acts in bad faith, employs unfair tactics or attempts to unfairly extract benefits out of another business as a result of its size or bargaining power, parliament has seen fit to empower the courts to grant a range of relief.

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[63] Section 80
[64] section 82
[65] section 83
[66] section 86C
[67] section 87(2).
[68] *Austotel Pty Ltd v Franklins Selfserve Pty Ltd*(1989) 16 NSWLR 582 at 585, cited favourably in *ACCC v CG Berbatis* 2003 [HCA] 18 at 111.

2.2 Section 51AA

As noted above, Section 51AA inserted into the Act in 1993 proscribes conduct that is unconscionable within the meaning of the unwritten law, from time to time. The addition of the protection of the common law in section 51AA was intended to ensure that the protection given under Part IVA is not static but flexible.

Section 51AA specifically recognises the fluidity of the protection given by the use of the expression "*from time to time*". Thus the protection provided under the Part moves with changes in common law interpretation which allows any developments to be automatically included within section 51AA without the need to amend the Act. The common law may develop in an expansionary manner, or it may become refined and more limited.

In considering the application and scope of Section 51AA the following discussion therefore considers cases determined with reference to the common (or unwritten) law of unconscionable conduct as well as those determined with reference to 51AA.

Cases such as *Blomley v Ryan*[69] and *Amadio*[70] noted that a party alleging unconscionable conduct must have been in a position of special disadvantage, such as drunkenness, infirmity, illiteracy, or other cognitive disability, that prevented them from making a judgement as to what was in their best interest.

The courts have subsequently expanded upon the situations in which the doctrine may apply[71]. It has been observed that the traditional heads (of intervention against unconscionable behaviour) may be ready for some redefinition or [rationalisation][72].

The courts have so far indicated that they may be willing to grant relief under section 51AA where:

- The stronger party unfairly exploits the weaker party's disadvantage[73].

The stronger party relies on their legal rights to take advantage of the weaker party in a way that is harsh or oppressive[74].

The stronger party allows the weaker party to rely on an incorrect assumption, or fails to disclose an important fact[75].

One party benefits unfairly from the deal at the expense of the other party[76].

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[69] (1956) CLR 362
[70] *Commercial Bank of Australia Limited v Amadio* (1983) 151 CLR 447
[71] cf *Stern v McArthur* (1988) 165 CLR 489 at 526; '…fraud, mistake, accident or surprise… do not… exhaust the scope of unconscionable or unconscientious behaviour.'
[72] The High Court in *Berbatis* approved of this observation by French J's in *GPG (Australia Trading) Pty Ltd v GIO Australia Holdings Ltd* at 44.
[73] *Louth v Diprose* (1992) 175 CLR 621, *Bridewater v Leahy* (1998) 194 CLR 457
[74] *Legione v Hately* (1983) 152 CLR 406, *Stern v McArthur* (1988) 165 CLR 489
[75] *Talyor v Johnson*
[76] *Muchinski v Dodds* (1985) 160 CLR 583

The weaker party relies on a misrepresentation by the stronger party[77].

The weaker party is unable to understand the deal, due to lack of experience or professional advice[78].

Although the extrinsic materials, which have been used in the interpretation of 51AA, tend towards a confined approach to the application of the doctrine, the Full Federal Court in *Samton* approved of French J's approach to section 51AA, in which it was observed that

> '*neither the Explanatory Memorandum nor the Second Reading Speech can be treated as imposing qualifications which are not found in the words of s.51AA*'.

Can a corporation suffer a special disadvantage

There is also precedent to suggest that a *corporation itself* may, to some extent, suffer from a special disadvantage. An example of such a situation where this might arise was in *Commonwealth Bank v Ridout Nominees*[79];

> 'I am therefore prepared to find that each of these corporations was in a position of special disadvantage … for the purpose of the principles governing unconscientious use of superior bargaining power.'

Commercial experience

In *Samton*, both the trial judge and the Full Court considered the commercial experience of the complainant. Although the ACCC submitted that the legislation, by virtue of its place in the Trade Practices Act, specifically contemplated conduct that occurred 'in trade or commerce' and therefore the parties would be expected to have some degree of commercial experience, the Full Court considered that the agreement reached was the result of a combination of considered commercial judgement and the complainant's oversight in exercising the option in good time;

> '*At least in the case of the experienced business person there must, in our opinion, be something more than commercial vulnerability (however extreme) to elevate disadvantage into special disadvantage*.' (64)

Alternatively, in *Berbatis*, Kirby J, (dissenting) noted that the very inclusion of s51AA in the Trade Practices Act, contemplated that the equitable doctrine be applied to a wider range of situations (73). He also noted that it was not necessary for the will of the complainant to be overborne to establish unconscionability, and distinguished between duress and unconscionability on this basis. Importantly, Kirby J reasoned that equity should provide relief where the act of the weaker party, even if voluntary, was a result of his disadvantageous position and the other party unconscientiously taking advantage of that position. In this case, he considered that *but for* the situation of disadvantage created by the desire to sell the business the lessors would have been unable to impose the relevant condition.

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[77] *Waltons Stores (Interstate) Ltd v Maher* (1988) 14 CLR 387
[78] *Garcia v National Australia Bank Ltd* (1988) 194 CLR 395
[79] [1999] FCA 903 at 212

Commercially irrelevant

In *Berbatis* the High Court generally disapproved of the concept of extracting a 'commercially irrelevant' concession, noting for example that 'What is relevant to a commercial negotiation is whatever one party to the negotiation chooses to make relevant.[80]' and that there were no objective criteria by which the court might decide what was and was not commercial relevant[81].

Special disadvantage

In determining whether the situation faced by the tenants in the *Berbatis* case constituted one of special disadvantage the High Court recognised that the lessees were in a difficult bargaining position, due to the fact that they had no option to renew their lease and that their prospects of selling the business depended upon the cooperation of the lessors, which they were not obliged to give.

The court did not, however, consider that this disadvantage was sufficiently 'special' to grant relief[82]. Although Kirby J noted that this disadvantage could not be ameliorated by access to legal advice or representation, Callinan J considered it inappropriate to characterise the detriment that a tenant has by reason of the imminent expiration of a lease as a special disadvantage[83]. Gleeson CJ observed that a person is not in a position of relevant disadvantage simply because of an inequality of bargaining power, and that many, perhaps even most, contracts are made between parties of unequal power[84].

Situational disadvantage

It has been recognised that the concept of disadvantage may extend beyond an inherent or constitutional disadvantage (for example, some kind of infirmity or cognitive impairment) to a 'situational disadvantage'. *ACCC v Samton Holdings*[85] considered the term 'special disadvantage' at length. The court accepted the finding of the trial judge that the categories of special disadvantage are open, and may extend to 'situational disadvantage'. It was accepted that the complainants were in a position of serious disadvantage; 'they had very little bargaining power. As a practical matter, they were not in a position to make any decision other than to pay the price demanded by the respondents.' This position is the same as that adopted in such cases as *Murphy v Overton Investments Pty Ltd*[86].

[80] Per Gleeson CJ at 16
[81] at 51.
[82] see for example at 68.
[83] At 155, and later at 179.
[84] At 11.
[85] [2002] FCA 62 at 64
[86] [2001] FCA 500

Of whose making was the disadvantage?

The courts have generally distinguished between situations where the disadvantage was beyond the control of the plaintiff, and where it was of their own making[87]. Callinan J observed that some aspects of the disadvantage suffered by the complainants in *Berbatis* was of their own making, for example their taking of a lease without further option, their delay in seeking a fresh lease, their failure to enforce what they contended was a concluded agreement (absent the relevant clause). Similar observations were made by the Full Federal Court in *ACCC v Samton Holdings*[88], where it was noted that the situation that the complainant found himself in was a result of his own actions (at 58). That court also held

> *The fact that somebody is in a position of special weakness through their own fault because they have lost rights necessary to the operation of their business does not provide a basis upon which a claim for unconscionable conduct can be built because another party puts a premium on the acquisition of those rights.*

The approach taken by the courts, however, to applying these expanded notions to particular circumstances has been conservative.

In *ACCC v CG Berbatis Holdings*[89], the High Court approved of the distinction drawn by the Full Federal Court between parties adopting an opportunistic approach to strike a hard bargain and those who act unconscionably. The court noted that a party in an inferior bargaining position may not lack capacity to make a judgement about their own best

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[87] Callinan J observed that some aspects of the disadvantage suffered by the complainants was of their own making, for example their taking of a lease without further option, their delay in seeking a fresh lease, their failure to enforce what they contended was a concluded agreement (absent the relevant clause). Similar observations were made by the Full Court in Samton, where it was noted that the situation that the complainant found himself in was a result of his own actions (at 58). It also said '*The fact that somebody is in a position of special weakness because they have lost through their own fault rights necessary to the operation of their business does not provide a basis upon which a claim for unconscionable conduct can be built because another party puts a premium on the acquisition of those rights.*' (62)

[88] [2002] FCA 62. This case concerned a small business tenant that failed to exercise their option to renew a lease by the required date. The landlord required the tenant to pay $70,000 to secure the extension. The Court concluded that while the company had struck a hard bargain it fell short of being unconscionable within the meaning of 51AA. An appeal by the ACCC was dismissed after consideration of the term 'special disadvantage'. Generally, it observed that unfair conduct does not equal unconscionable conduct. Carr J, the trial judge, held that the conduct in this case 'fell short, but not far short' of being unconscionable.

[89] [2003] HCA 18 concerned a shopping centre landlord that required a tenant to discontinue legal proceedings in the state tenancy tribunal as a condition of granting a lease renewal. The ACCC formed the view that these tenants were at a special disadvantage when bargaining with the landlord because of their financial dependence on the lease negotiations. The trial judge found the conduct by the landlord to be unconscionable within the meaning of 51AA. The Full Federal Court subsequently overturned that decision, and the ACCC's appeal to the High Court was ultimately dismissed.

interest[90]. Gleeson CJ distinguished between unconscientiously exploiting another's diminished ability to protect his own interest (which is unconscionable), and taking advantage of a superior bargaining position[91].

In *ACCC v Samton Holdings Pty Ltd*[92] it was held at trial that, almost by definition, conduct which attracts equitable relief as unconscionable can be viewed as 'towards the extreme end' of the scale of unreasonable behaviour by one person towards another. On appeal, this reasoning was not disturbed, with the Full Court holding that 'what his honour (Carr J) did was to make plain that it is not enough to demonstrate that one person has acted unreasonably towards another in the circumstances…[93]'

2.3 Section 51AC

In its report[94]released in May 1997, the Reid Committee found small businesses to be vulnerable to unfair dealing and exploitation by more powerful firms, primarily because of the imbalance in bargaining power between small and large firms. It recognised that small businesses in both retail tenancy and franchising relationships may be susceptible to such conduct. The Committee determined that small businesses required improved legal protection and access to effective enforcement mechanisms.

The Committee recommended further legislative protection for small business against unfair business conduct[95]citing a number of factors that might remedy perceived deficiencies in the then existing law. The Government largely accepted the Committee's suggestions and in September 1997 announced that it would introduce legislation strengthening the protections available to small business. The subsequent *Trade Practices Amendment (Fair Trading) Act 1998*, amongst other things, inserted the new unconscionable conduct provision Section 51AC into the Trade Practices Act.

The reforms were designed to ensure that small business can confidently deal with large firms in the knowledge that the rules under which they are operating are fair, and that there will be proper redress available when those rules are broken. The stated objective

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[90] See also at 46, where it was noted that equity intervenes not necessarily because the complainant has been deprived of an independent judgement and voluntary will, but because the party has been unable to make a worthwhile judgement about what is in their own best interest. Callinan J considered 'It was a commercial choice with respect to which they had to make, and did make a judgement (namely, between pursuing litigation that had uncertain outcomes and risks, and accepting a lease which enabled them to effect the prompt sale of the business). He later observed it was not an unreasonable quid pro quo.

[91] Gleeson CJ considered the alternative situation, where the lessors could have refused outright to offer a lease renewal, which would have been far more harmful to the lessees. He also noted that all parties to the transaction were experienced business people (cf para 23) acting in their own interests.

[92] [2002] FCA 62

[93] At 52.

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

[95] Ibid, ch 6.

of the Government was to induce behavioural change and improve standards of commercial conduct.

Section 51AC was introduced by the *Trade Practices Amendment (Fair Trading) Act 1998* which was assented to on 22 April 1998 and took effect from 1 July 1998. It extends the prohibition against unconscionable conduct to prohibiting unconscionable conduct in relation to the supply or acquisition of goods or services in small business transactions (where the goods or services are supplied to or acquired from a corporation that is not a listed company, at a price no more than $3 million)[96].

It prohibits *"conduct that is, in all the circumstances, unconscionable"* and provides a list of factors that the Court may have regard to for the purpose of determining whether conduct is unconscionable. They include, but are not limited to:

- the relative bargaining strength of the parties;
- whether the stronger party imposed conditions that were not necessary to protect their legitimate business interest;
- the use of undue influence or pressure tactics;
- whether the weaker party could obtain supply on better terms elsewhere;
- whether the stronger party made adequate disclosure to the weaker party;
- the willingness of the stronger party to negotiate;
- the extent to which each party acted in good faith; and
- the requirements of any relevant industry code.

Given the wording of subsection 51AA(2) which provides that section 51AA does not apply to conduct which is prohibited by sections 51AB or 51AC, when considering a contravention of Part IVA the practical starting point is whether the conduct is prohibited by either of these statutory unconscionability provisions. In this regard, as noted above, section 51AB is limited to circumstances concerning the supply of domestic goods or services to consumers, and section 51AC is limited to the supply or acquisition of goods or services in small business transactions at a price no more than $3 million. Thus, if the conduct generally falls within these parameters then prima facie the applicable prohibition is likely to be contained within sections 51AB or 51AC, and section 51AA will not apply.

This conclusion is reinforced by a number of features. First, the list of factors in both provisions to which the Court may have regard in determining unconscionability is broad and not exclusive. Second, the use of the phrases "*in all the circumstances*" in both sections (which is not present in section 51AA), and '*without in any way limiting the matters to which the Court may have regard*", suggests that the legislature intended that the Courts not be confined to traditional equitable doctrines.

[96] The limit was originally $1 million and was increased to $3 million by the *Trade Practices Amendment Regulations (No 2) 2000*, No 164, which took effect on 1 July 2000.

This interpretation is supported by the Explanatory Memorandum to the Bill that became the *Trade Practices Amendment (Fair Trading) Act 1997* by which section 51AC was introduced. The intention to extend the application of section 51AC to conduct that would not be found to be unconscionable within the meaning of the unwritten law was made clear at pages 22-23 where it is stated:

> *Equity recognises unconscionable conduct, undue influence and economic duress as separate grounds for relief. It is envisaged that [section 51AC] would prohibit conduct of a kind already covered by these equitable remedies but would, in addition, extend to other conduct that is in all the circumstances, unconscionable.*

Further, the Second Reading speech stated:

> *This new provision will extend the common law doctrine of unconscionability expressed in the existing section 51AA of the Act. The bill uses the expression 'unconscionable conduct' in order to build on the existing body of case law ...*

There are also indications in the wording of the statute itself that indicate the intention for 51AC to prohibit unconscionable conduct beyond that which is covered under the common law, specifically the list of matter to which the Court may have regard in determining unconscionability is a broad and non-exhaustive one, as indicated by the phrase '*without in any way limiting the matters to which the Court may have regard*'; and the phrase 'in all the circumstances', which does not appear in s.51AA.

It is therefore clear that it was the intention of the legislature that section 51AC should extend the common law doctrine of unconscionability to protect the circumstances of supply of goods and services in small business transactions. The section is clearly not limited to the need to establish '*special disadvantage*' or '*special disability*' in the sense described in equity in the cases of *Blomley v Ryan* and *Commercial Bank of Australia v Amadio*, given the list of factors which may be considered in making a finding of unconscionability.

This interpretation has received recent support from a number of judges in the Federal Court. The Full Federal Court in *Hurley v McDonalds Australia Ltd* (2000), held that "*unconscionable*" in section 51AC carried the dictionary definition of actions "*showing no regard for conscience*" or that are "*irreconcilable with what is right or reasonable*". The Court also stated that for conduct to be judged as unconscionable "*serious misconduct or something clearly unfair or unreasonable"* must be demonstrated [at paragraphs 19-20].

In *ACCC v Berbatis Holdings Pty Ltd* French J concluded that there was no reason to suppose that the unconscionable conduct prohibited by section 51AC is limited by reference to "*specific equitable doctrines*", and pointed out that the factors to which the Court is required to have regard for the purpose of determining whether there has been a contravention "*include undue influence and duress and other issues falling outside the equitable doctrines to which reference has been made.*" [at 335]

The views of the Full Court in *Hurley* and of French J in *Berbatis* were cited by Sundberg J in *ACCC v Simply No-Knead (Franchising) Pty Ltd* where His Honour concluded:

> *... in my view "unconscionable" in s51AC is not limited to the cases of equitable or unwritten law unconscionability the subject of s51AA. The principal pointer to an enlarged notion of unconscionability in s51AC lies in the factors to which sub-s(3) permits the Court to have regard. Some of them describe conduct that goes beyond what would constitute unconscionability in equity. ... Further, it is to be remembered that the list of factors in sub-s (3) is not exhaustive. [at 265]*

In *Simply No-Knead,* Sundberg J also endorses the view that there is a distinction to be drawn at least between section 51AC and section 51AA and that the former is not restricted to common law notions of unconscionability whatever they may be. With respect it is submitted that this view is correct. It is also submitted that section 51AC has a broader interpretation of unconscionable conduct by virtue of a dictionary definition together with the specific criteria which may be considered in reaching a decision as to whether a matter is unconscionable, than is indicated in section 51AA. Thus, section 51AC should not be interpreted in a restrictive way.

The ACCC takes the view that "*conduct which is unconscionable in all the circumstances*" extends beyond traditional equitable notions of unconscionability to a broader 'statutory unconscionability'..

In connection with

In considering the extent of the applicability of s.51AC it is relevant to note the phrase "in connection with".

Wilcox J observed in *Our Town FM Pty Ltd v Australian Broadcasting Tribunal* (1987) 16 FCR 465 at 479:

> *The words "in connection with" have a wide connotation, requiring merely a relationship between one thing and another. They do not necessarily require a causal relationship between the two things…*

His Honour's approach to the meaning of the phrase was subsequently adopted by Sackville J in *Drayton v Martin* (1996) 67 FCR 1 at 32.

In *Burswood Management Ltd & Ors v Attorney-General (Cth) & Another* (1990) 94 ALR 220 the Full Federal Court stated:

> *The words "in connection with" are words of wide import; and the meaning to be attributed to them depends on their context and the purpose of the statute in which they appear."* [at 223]

The Full Court also cited with approval from the judgment of Davies J in *Hatfield v Health Insurance ACCC* (1987) 15 FCR 487 at 491 to the following effect:

> *Expressions such as "relating to", "in relation to", "in connection with" and "in respect of" are commonly found in legislation but invariably raise problems of statutory interpretation. They are terms which fluctuate in operation from statute to statute ... the terms may have a very wide operation but they do not usually carry the widest possible ambit, for they are*

subject to the context in which they are used, to the words with which they are associated and to the object or purpose of the statutory provision in which they appear.

Having regard to these judicial observations, the phrase "in connection with" as it appears in section 51AC, supports a wide interpretation by reason of its ordinary meaning as well as the beneficial nature of the objectives underpinning the sections, being to protect small business consumers from unconscionable conduct. The fact that the section also provides a non-exhaustive list of criteria to which the Court may have regard in deciding whether the conduct complained of is "unconscionable", also supports an expansive interpretation of the provision, which appears intended to catch a wide variety of transactions.

As between the parties to a transaction therefore, the phrase "in connection with" appears broad enough to catch all conduct associated with the transaction. This would be sufficient to include collateral or peripheral aspects of the transaction such as collateral contracts between the parties as well as forbearance to sue.[97] However an interesting issue arises as to whether the words are sufficient to include a related contract with a third party.

Drummond J in the case of *Begbie v State Bank of New South Wales* (1994) ATPR 41-288 considered the circumstance of a widow with some commercial knowledge, being tricked by a fraudster with whom she was infatuated, into mortgaging her property with a bank and guaranteeing to secure his debts. The widow sued the bank. The Judge decided that section 51AB did not apply but only by reason of the provisions of subsection 51AB(5) which limit its application to goods or services for personal, domestic or household use or consumption. The widow instead succeeded at common law on the basis of unconscionability as it was found that the bank knew about her vulnerable circumstances and took unfair advantage of her in obtaining the guarantee and mortgage.

This case therefore supports the proposition that if a third person (guarantor) enters into a guarantee contract with a credit supplier (eg a bank), which contract in turn is in connection with a contract between a debtor and credit supplier for goods and services, (e.g. a loan to purchase domestic items for household use) that the credit supplier could be caught by the provisions of section 51AB if it knew or ought to have known about the situation of vulnerability and took unfair advantage of it. It is to be noted that the contract of guarantee and mortgage would not by itself amount to a contract for the supply of goods or services.

The approach taken by Drummond J appears to differ with the approach taken by Lindgren J in *Monroe Topple & Associates Pty Ltd v The Institute of Chartered Accountants in Australia* (2001) FCA 1056. That case considered, inter alia, whether the respondent engaged in unconscionable conduct within the meaning of section 51AC in respect of an alleged restrictive dealing clause between candidates wishing to qualify for membership of the respondent and the respondent, whereby those candidates were

[97] Sneddon M, "Unfair conduct in taking guarantees and the role of independent advice" (1990) 13 UNSWLJ 302 at 333-334

obliged to purchase support materials from the respondent. The applicant, who was in the business of supplying support materials to candidates, claimed that such restrictive clauses infringed section 51AC in that the candidates were not informed about alternative suppliers, such as itself. Lindgren J pointed out (at paragraph 254 and following) in relation to section 51AC (although his observations would appear to apply equally to section 51AB) that subsection 51AC(3) contemplates that the only parties to be considered are a "supplier" and a "business consumer" and that:

> *... the matters to which the Court may have regard for the purpose of determining whether the supplier has engaged in unconscionable conduct in connection with the supply will all be matters operating as between it and a business consumer.*

Whilst Lindgren J also noted that the opening words of subsection 51AC(3) make it clear that the list is not intended to be exhaustive, his Honour observed

> *"effect can be given to this disclaimer by the courts having regard to other matters which similarly have an effect as between the supplier and the business consumer".*

Lindgren J went on to recount the history leading to the enactment of sections 51AB and 51AC, concluding *"clearly, the purpose or object of s51AC was to protect small business in their dealings with 'big business'"*. His Honour then observed:

> *Both the content internal to 51AC and the legislative history to which I have referred, teach that the expression "in connection with" in s 51AC requires that the conduct impugned "accompany", "go with" or "be involved in" the supply of the goods or services, and that it is not sufficient that, as alleged in the present case, such a supply be the occasion of unconscionable conduct of the supplier directed to an unrelated third party with which the supplier has no dealings at all* (paragraph 260).

It is to be noted that the factual circumstances being discussed by Lindgren J differed significantly from those before Drummond J. In the case of *Begbie,* the credit supplier knew of the circumstances of the third party and was dependent upon the guarantee contract between it and the third party for the purpose of the loan to the consumer. There was a clear interrelatedness of the contracts and the conduct. By contrast in the case of *Monroe Topple* there was no contract, connection or conduct between the applicant third party and the respondent. The only contract and conduct was a separate contract between the candidates and the respondent (being the potential supply contract) and the only possible connection with the applicant was a secondary effect of the applicant being unable to enter into similar contracts with candidates.

It is suggested that the broad interpretative assertions made by Lindgren J should be confined to the fact circumstances with which his Honour was dealing and that it is open to third parties with whom the supplier has had some direct dealings, or whom the supplier knows is likely to rely on its information or representations to be protected by these provisions.

A particular limitation on the applicability of section 51AC

Sub-section 51AC(10) provides as follows:

A reference in this section to the acquisition or possible acquisition of goods or services does not include a reference to the acquisition or possible acquisition of goods or services at a price in excess of $3,000,000 or such higher amount as is prescribed.

There are a number of business transactions where the total value of the transaction may not be known at the time that the conduct is taking place. One example of this is in the health insurance industry where the total value of a contract between a private health insurer and a hospital may not be known until the end of the financial year. The issue of the monetary threshold may also be relevant in the context of an ongoing supply agreement, such as a lease or insurance contract. It is still undecided if the $3 million threshold in 51AC applies to a periodic contract in total or the part delivery elements (purchase order) progressively made and paid for on delivery; is the transaction the entirety of the contract of supply or just the progressive delivery, say, each month eg spare parts - motor vehicles, computers etc and paid within 30 days as per standard terms of trade?

Apart from issues which may arise as to the characterisation of the contract and transaction, and whether it applies to each discrete transaction or whether it encompasses the whole of the transaction, it is suggested that the monetary restriction provided in sub-section 51AC(10) should be broadly and robustly interpreted so long as the interpretation is prima facie properly available.

It is also suggested that it appears to be an arbitrary distinction to draw a difference in applicability of section 51AC based on whether the quantum of the transaction is above or below $3 million. The limit suggests that the legislation is intended to protect not merely individual small businesses but corporate consumers of a commercially significant size. The limitation therefore no longer seems to be warranted.

Enforcement outcomes under s.51AC

The ACCC has resolved nine cases under s.51AC since the provision was inserted into the Act in July 1998. Of those matters, both *Simply No Knead* and *4WD Systems Pty Ltd and ors*[98] were resolved by fully contested court outcomes. The remaining seven are the result of consent orders, voluntary undertakings, or other settlement[99].

The most recent of these decisions under 51AC in *4WD Systems* confirmed that the word 'unconscionable' in 51AC is not limited to the meaning of the word at common law or at equity but found no contravention on the facts of the case.

[98] Selway J, Federal Court of Australia S170 of 2001 (unreported).

[99] For further details of those matters see Attachment C. The fact that seven of the nine 51AC matters pursued by the ACCC were not fully contested should be considered in the context of the model litigant policy, which requires the ACCC to consider offers of settlement or other administrative remedies where appropriate.

Examples of conduct declared to be in contravention of s.51AC

The ACCC has obtained declarations of unconscionable conduct in the Federal Court in a wide range of commercial situations. The specific circumstances have included:

- Blatant disregard of industry codes of conduct or other law[100];
- Unreasonably withholding information[101];
- Placing conditions on supply of essential franchising goods to franchisees, where those conditions were not necessary to protect the franchisor's legitimate business interests[102];
- Conduct that is inconsistent with the nature of the relationship of the parties, particularly in a franchising context[103];
- Threatening to withhold essential franchising supplies[104];
- Attempting to terminate a commercial agreement for contrived reasons[105];
- Conduct calculated to harm the smaller business, such as a franchisor competing with its franchisees[106];
- Failing to honour terms of a retail lease[107];
- Unreasonably refusing to transfer a retail lease[108];
- Unreasonably refusing to renew a lease[109] ;
- Failing to adequately disclose key changes to a lease, despite representing that the lease is unchanged, in circumstances where the changes cause significant detriment to the lessee[110];
- Granting an 'exclusive' dealership to one business, while at the same time negotiating with another business for a dealership that would impinge on that of the first business[111];
- Unreasonably refusing to supply a business with whom a dealership had been entered into[112];

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[100] Sundberg J made reference in *Simply No Knead* to the course of conduct engaged in by the franchisor over a period of time in relation to a number of franchisees that included *intimidation, blatant disregard of industry codes and other law, and lack of good faith*. Other matters where the disregard for industry codes have been declared to be unconscionable include *ACCC v Cheap as Chips Franchising Pty Ltd and Peter Hudousek*, FCA (VIC) no. V354 of 1999, *Half Price Shutters*, and *ACCC v Suffolke Parke Pty Ltd and Gregory Bradshaw* FCA (SA) no S159 of 2001.

[101] *ACCC v Leelee Pty Ltd* (2000) ATPR 41-742

[102] *ACCC v Simply No Knead*

36 In Simply No Knead, Sundberg J remarked that SNK's conduct was '*unfair and unreasonable having regard to the franchisor/franchisee relationship, and oppressive*. (45). He went on to say 'This conduct was *calculated to damage the franchised businesses*, in the sense that SNK must have known it would damage them. It was inconsistent with a proper relationship between franchisor and franchisee, and demonstrated a *lack of good faith* on the part of SNK (46)'.

[104] *Simply No Knead*

[105] *Automasters Australia Pty Ltd v Bruness Pty Ltd & Anor* [2002] WASC 286

[106] *Simply No Knead*

[107] *ACCC v Leelee Pty Ltd*

[108] *ACCC v Leelee Pty Ltd*

[109] A*CCC v Suffolke Parke Pty Ltd and Gregory Bradshaw FCA (SA)* no S159 or 2001

[110] *ACCC v Avanti Investments Pty Ltd and Giuseppe Rocco Barbaro, FCA (SA*) no, S51 of 2001

[111] *ACCC v Daewoo Heavy Industries & Machinery Pty Ltd & Daewoo Australia Pty Ltd*

[112] *ACCC v Daewoo Heavy Industries & Machinery Pty Ltd & Daewoo Australia Pty Ltd*

- Conduct that is unfair, unreasonable, harsh or oppressive, intimidating, or wanting in good faith[113];
- Conduct that is capricious and unreasonable in circumstances where there was not a sufficient basis to terminate the contract [114];
- Making a call on a letter of credit, where a dispute has been effectively settled, as if the circumstances of the settlement had not occurred.[115]

2.4 Small business complaints alleging unconscionable or unfair conduct

The ACCC information centre receives a significant amount of direct contact with small business owners, managers and advisers (for detailed statistics, refer to Attachment D).

The complaints received by the ACCC cover a broad range of issues and conduct. While a number of small business complaints are considered closely by the ACCC to determine whether they evidence unconscionable conduct, many of the issues raised might be more properly characterised as being of a contractual nature or constitute what may be considered merely 'unfair' conduct and therefore unlikely to fall within the scope of the unconscionable conduct provisions.

The ACCC sometimes finds that a number of complaints about a particular form of conduct or from a particular sector can indicate systemic market concerns. In isolation, such issues may not warrant regulatory intervention, but when systemic complaints are identified the ACCC will consider a range of measures to resolve the issues. These measures may involve facilitating dialogue between the key stakeholders, encouraging industry participants to put a dispute resolution mechanism in place or facilitating the development of a framework for fair play such as an industry code of conduct to address the issues.

The ACCC notes the following systemic small business complaints, as well as industries in which they occur:

Exercise of legal rights in bad faith

The ACCC has received a number of complaints from small businesses alleging that large businesses will attempt to defeat legitimate small business claims exercising appeal rights until the smaller business exhausts its funds.

The ACCC has sought advice on whether or not such conduct could constitute 'unconscionable conduct'. The terms of s.51AC(5) are relevant in that they provide that

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[113] Sundberg J remarked, variously, in *Simply No Knead* that 'SNK's conduct in relation to the McKinnon franchisees was *unreasonable, unfair, harsh, oppressive and wanting in good faith* (44)'. He referred to the 'hostile and pugnacious manner in which Bates dealt with [the franchisees], and summarised the conduct as being 'an overwhelming case of unreasonable, unfair, bullying and thuggish behaviour'.

[114] *Automasters Australia Pty Ltd v Bruness Pty Ltd & Anor* [2002] WASC 286

[115] *Boral Formwork v Action Makers* [2003] NSWLR 713

a person does not engage in unconscionable conduct *by reason only* that the person institutes legal proceedings.

Where such allegations are made, clear evidence would be required that the larger party's decision to institute proceedings was based merely on a strategy to exhaust the smaller businesses resources rather than on the merits of the case before it is likely to constitute unconscionable conduct. Such evidence has not been provided in relation to such complaints received by the ACCC.

Slow payments

Many small businesses suffer liquidity problems because their larger trading partners delay settlement of accounts. Small businesses suffer embarrassment when they have to delay paying their own bills because of money outstanding.

Some business groups allege there is a deliberate strategy by big business to use money they owe to invest in the short term money market or in the business for short term purposes. The ACCC has not been provided with evidence to substantiate such allegations.

Of itself, slow payment would be unlikely to constitute unconscionable conduct within the meaning of Part IVA of the Act. Such a matter would ordinarily be viewed by the ACCC as a contractual matter to be resolved between the parties.

In some industries such as the motor vehicle body repair industry small businesses, who are not members of an insurer's repair network, have alleged that they do not receive payment on the same terms as those within the scheme. The Victorian Automobile Chamber of Commerce has surveyed a number of smash repairers on this issue.

While some repairers report that they suffer from unnecessarily delayed payments the ACCC has not been provided with any specific evidence to substantiate allegations of unfairness or unconscionable conduct. Evidentiary issues aside, the ACCC notes that larger businesses delaying payments to smaller businesses in circumstances that evidence bad faith, or other elements of section 51AC to which the courts may have regard, may risk contravening the Act.

Use of standard form contracts

The ACCC is aware that the use of standard form contracts is not uncommon in agreements such as those between primary producers and processors, newsagents and publishers and franchisors and franchisees; where one large business is contracting with a number of smaller businesses and wishes to promote a uniform distribution or supply system.

Although it acknowledges that the use of standard form contracts can be used to promote standards in commercial dealings and reduce transaction costs, the ACCC notes that in

some circumstances a larger party unreasonably refusing to negotiate on terms, when using such contracts, may risk contravening Section 51AC.

Unilateral variation clauses

A unilateral variation clause is one that allows terms or conditions of the agreement to be varied by one of the parties without further negotiation with or agreement by the other party such variation.

These clauses sometimes relate to fundamental aspects of the agreement. For example, in telecommunications contracts, a clause might regulate the amount of free downloads an internet user might be entitled to before additional charges are incurred. Sometimes the right of unilateral variation by the stronger party is a clear one, and confers discretion on the larger party to, for example, alter rates or terms of payment. Other agreements specify key terms such as royalty fees, allowances, marketing contributions and other payments, by reference to schedules which may be varied by one party.

Variation clauses that may only be exercised when triggered in circumstances agreed by both parties (a change in the law for example) can provide flexibility in an agreement that nonetheless retains some certainty for the parties. Variation clauses that are not referable to any external trigger or subject to further negotiation between parties, however, are of concern to the ACCC.

The ACCC's concerns relate first to the imposition of such unfettered clauses on parties with relatively lesser bargaining power and secondly to conduct by those seeking to unreasonably exploit such clauses.

On the first point, it is arguable that contract terms conferring such unfettered discretion on one party (invariably the party with relatively greater bargaining power) constitute a condition that is not reasonably necessary for the protection of the legitimate interests of that party. While the Court may currently have regard to such conditions when considering allegations of unconscionable conduct within the meaning of s.51AC the imposition of such a term is not *per se* unconscionable with the meaning of that provision.

On the second point (the unreasonable exploitation of such clauses) it is arguable that such conduct may be considered by the Court under s.51AC in circumstances where the party exercising its rights does so in bad faith. The mere exercise by the larger party of legal rights, conferred by such a clause, will not however constitute unconscionable conduct within the meaning of that provision. In the ACCC's view, however, there is little justification for such variations without reference to circumstances previously considered by both parties or further negotiation between the parties when unforeseen circumstances arise.

2.5 Industry sectors in which small business complaints commonly arise

Retail tenancy

Retail tenancy was identified as a key area of concern in the Reid Report, which went into some detail about the specific issues facing small business participants in the industry[116]. The ACCC has ongoing involvement with participants in the retail leasing industry. As a means of clarifying the issues involved, the ACCC engaged a consultant to prepare a report on the interaction of retail tenancy issues with part IVA of the Act. Late last year, the ACCC also facilitated industry discussion at a round table of key industry representatives, including landlords, tenants and small business organisations, as well as state retail tenancy officials.

A significant number of complaints received by the ACCC from retail tenants allege unconscionable conduct. The number of unconscionable conduct allegations received by the ACCC has increased steadily since 1999, the first full year of operation of s51AC. Approximately one third of all unconscionable conduct complaints received by the ACCC each year involve retail tenancy issues.

Where complaints to the ACCC have been specific they have dealt with the following:

- problems with, or at, lease re-renewal;
- negotiation of rent increases;
- discrimination between tenants that occupy similar premises for similar purposes;
- alleged anti-competitive behaviour by lessor;
- disputes over the interpretation of the conditions within the lease;
- problems arising from renovations to a shopping complex;
- misrepresentations regarding future earnings;
- not allowing the lessee to transfer the lease to a tenant of their choice;
- casual leasing; and
- restrictions placed on the business of existing tenants.

Allegations of unconscionable conduct associated with retail lease renewal are of particular concern. The ACCC remains active in investigating allegations which evidence unconscionable conduct and has sought judicial clarification of the law in relation to a number of these.

Importantly, State jurisdictions including New South Wales, Queensland and Victoria have drawn down versions of 51AC into their respective retail tenancy regimes. The ACCC understands that other States are considering similar reforms. By doing this, small businesses will have easier access to justice, often in a less expensive and quicker environment such as a tribunal.

[116] Finding a balance – towards fair trading in Australia, Report by the House of Representatives Standing Committee on Industry, Science and Technology, May 1997 – see generally ch 2.

The ACCC works closely with the various State based retail tenancy officials to refer concerns that are more appropriately resolved by the specific Retail Tenancy laws and dispute resolution mechanisms.

Primary production

Many issues arise in the primary production industries when a larger business imposes strict terms and conditions on growers. Many problems can be attributed to basic supply and demand, when there have been times of oversupply in the industry, the ACCC has received many complaints from primary producers. This is evidenced by recent concerns in the wine grape industry. Some processors have felt it necessary to vary the terms and conditions which they offered to growers because of a surplus supply of high quality wine grapes. Many growers felt that the changes to contracts, which some processors sought to impose on them without substantive negotiation, were unreasonable and perhaps unconscionable.

The ACCC has closely considered a number of allegations by wine grape growers that processors have unconscionably sought to vary contracts. In one case, the ACCC successfully encouraged a processor to revisit its initial proposal that gave rise to such concerns.

Motor body smash repair industry

Many issues between repairers and insurers arise as a product of various structural changes in the industry, changes in the market for insurance products, improvements in technology and training and improvements in efficiency and quality.

The ACCC has received a number of allegations by smash repairers and their representative organisations that some insurers have acted unconscionably in their dealings with the repairers. A number of these allegations are associated with the decision by some insurers to use only a select network of repairers to provide smash repair services. While some allegations may raise issues of fairness, the ACCC has not received sufficient evidence to establish unconscionable conduct in relation to these matters to date.

Due to the frequency and the variety of concerns raised, the ACCC canvassed the issues in the industry by convening a round table discussion involving a broad selection of participants within the industry. Issues raised during the meeting, and later in submissions, included:

- consumer choice and information and the possible application of the Consumer Insurance Code;
- lifetime guarantees on work performed and implications for repairers;
- payment terms and job pricing/hourly rates;
- repair parts;
- collective bargaining;
- industry rationalization;
- repair networks/accredited repairer schemes;

- industry and corporate codes of conduct; and
- The possible application of the Consumer Insurance Code.

While the issues do not evidence contraventions of unconscionable conduct, they do indicate ongoing concern by some repairers and their representative organisations that some insurers treat them unfairly[117]. As noted above, many concerns arise from repairers who feel they have been unfairly excluded from a given insurer's select network of repairers.

2.6 Recommendations for future consideration

The market in which businesses operate is a dynamic one; it is constantly evolving in terms of size, concentration, or broader structural change. These changes are brought about by a number of factors; new technology, consumer trends, and even the regulatory environment itself. It is important that any regulatory regime is sufficiently flexible to adapt to the market within which it purports to govern conduct. Subject to the above discussion, in the ACCC's view Part IVA of the Act generally provides just such a flexible mechanism to address individual examples of unconscionable conduct.

As noted above, however, the ACCC considers there is little commercial justification for the imposition or exploitation of unfettered unilateral variation clauses.

As noted above, one of the matters to which a court may have regard when considering whether conduct is unconscionable within the meaning of 51AC is whether, as a result of conduct by the larger party, the business consumer was required to comply with conditions that are not reasonably necessary for the protection of the legitimate interests of the larger party.

It is arguable that a term which provides one party with unfettered discretion, to vary the terms and conditions within a contract without further negotiation with or the specific agreement of the other party, is a condition that is not reasonably necessary for the protection of the legitimate interests of that party. As such, it is arguable that the very inclusion or imposition of such a term in a contract, by a party with greater bargaining power, could constitute unconscionable conduct within the meaning of 51AC.

This might be contrasted with a variation clause in which the discretion to vary terms and conditions is restricted and proportionate to circumstances where it is reasonably necessary to respond to external changes (eg. in a relevant law) to maintain the balance of risk and return that was originally struck by both parties. Such proportionate discretion can provide parties to a given contract with sufficient flexibility to maintain a robust contract (particularly in the longer term) in the face of external changes.

The ACCC recommends that the imposition or exploitation of such unfettered unilateral variation clauses be added to the list of factors to which the court may have regard under

[117] Further information on the ACCC's liaison with the motor body smash repair industry is contained in the August 2003 issues paper.

ss.51AC(3) and ss.51AC(4). Such addition would, on the one hand, provide greater certainty for small businesses contracting with larger businesses and also prevent those larger businesses from unfairly exploiting the advantage that such clauses offer.

Part IVB Industry Codes of Conduct

Part (1)(c) of the Senate Committee's terms of reference asks

Whether Part IVB of the Act operates effectively to promote better standards of business conduct, and, if not, what further use could be made of Part IVB of the Act in raising standards of business conduct through industry codes of conduct.

3.1 Introduction

Part IVB of the Act provides a framework by which the government can prescribe both mandatory and voluntary codes of conduct. The government issued guidelines on the prescription of such codes in 1999. This guideline notes that "…the Minister will only consider initiating a proposal for prescription of a Code of conduct if:

- The code would remedy an identified market failure or promote a social policy objective; and
- The code would be the most effective means for remedying that market failure or promoting that policy objective; and
- The benefits of the code to the community as a whole would outweigh any costs; and
- There are significant and irremediable deficiencies in any existing self-regulatory regime-for example, the code scheme has inadequate industry coverage or the code itself fails to address industry problems; and
- A systemic enforcement issue exists because there is a history of breaches of any voluntary industry codes; and
- A range of self regulatory options and 'light-handed' quasi regulatory options has been examined and demonstrated to be ineffective and
- There is a need for national application as State and Territory Fair Trading authorities in Australia also have the options of making codes mandatory in their own jurisdiction."[118]

Furthermore the government will only consider prescribing a code of conduct under the Act if the code is not underpinned in other Federal legislation.[119] Examples of this would be the Internet and the telecommunications industry. Both of these industries are underpinned by other legislation such as the *Broadcasting Services Act* and the *Telecommunications Act* 1997 both of which provide for the registration of and enforcement of industry codes by the Australian Communications Authority;[120]

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118 *Prescribed Codes of Conduct-Policy Guidelines on making industry codes of conduct enforceable under the Trade Practices Act 1974,* Hon Joe Hockey MP, Minister for Financial Services and Regulation, May 1999,piv.

119 Ibid 1, p7 examples of

120 Section 123 of the Broadcasting Services Act outlines the matters which these codes may cover. Sections 117-122 of the Telecommunications Act 1997 provide for the registration and enforcement of industry codes.

3.2 The framework

Section 51AE of the Act provides that:
Regulations may:

(a) prescribe an industry code, or specified provisions of an industry code, for the purposes of this Part
(b) declare the industry code to be a mandatory industry code or a voluntary industry code; and
(c) for a voluntary industry code, specify the method by which a corporation may be bound by the code and the method by which it ceases to be so bound (by reference to provisions of the code or otherwise).

In most instances the methods of being bound or unbound to an industry code are referenced in the code.

A code may be declared in whole or in part either voluntary or mandatory. The main distinguishing features between a prescribed voluntary industry code and a prescribed mandatory industry code are:

- A prescribed voluntary industry code is only binding on the members of the industry that agree to be bound by the code while a mandatory prescribed code is binding on all members of that industry and

- The ACCC's obligations of monitoring a prescribed mandatory industry code of conduct are envisaged to be greater than that of a prescribed voluntary code of conduct if not all industry stakeholders subscribe to the voluntary industry Code.

A mandatory industry code by its very nature implies a greater involvement by the ACCC to ensure total compliance with the code.

For example a mandatory prescribed industry code of conduct may also place a greater industry/ consumer education burden on the ACCC as opposed to a voluntary code regime that encourages this burden to be borne in full or at least shared by industry.

If the prescription of a code declares the industry code to be voluntary it must also specify by which method a corporation agrees to be bound by the code and the method by which it ceases to be bound by it. The method of binding a corporation that is a signatory to a voluntary code is might for example be achieved by signing a code register or by joining an association that administers the code. The method by which the corporation ceases to be bound might be given effect either by having the name removed from the register or ceasing membership of the association. The removal of a name from the registry of code signatories or the cessation of membership of an association may not always be voluntary, in some circumstances it may be a natural consequence to a breach of the code.

3.3 Timeframe for prescription of an industry code of conduct

It is difficult to determine the exact time it would take from the identification of a systemic problem in an industry to the time of implementing a prescribed code that addresses that systemic problem. The difficulty in determining an exact timeframe is in part due to the policy which requires that codes are only prescribed as a last resort after all other avenues have failed to remedy the systemic problem identified and partly to the varying nature of industries and systemic problems.

If the Franchising Code of Conduct can be used as an indicator of the time it takes from recognising that there is a systemic problem to the time of prescribing an actual code it may take some significant time. The chronology for the Franchising Code, the only prescribed industry code, is as follows:

- 1976 onwards-Unfair practices in franchising became the subject of comments in a serious of government reports.
- 1987-the federal government released an exposure draft of a franchising Agreement Bill which was abandoned the same year.
- 1991-the *Report of the Franchising Task Force to the Minister for Small Business and Customs* submitted to government.
- 1993-a voluntary Franchising Code of Practice was implemented along with the Franchising Code Council.
- 1996-the voluntary Franchising Code of Practice and the Franchising Code Council ceased operating.
- 1997-the Reid report recommended the legislative underpinning of a generic franchising code.
- 1998-the mandatory Franchising Code of Conduct became law.

3.4 The Franchising Code

As noted above, the Franchising Code of Conduct is the first mandatory industry code to have been prescribed under Part IVB of the Act. The Code provides, in the ACCC's view, substantial protection for franchisees.

The current disclosure regime under the Code, for example, requires the franchisor to disclose information deemed necessary in order for a prospective franchisee to make an informed decision prior to entering into a binding business agreement with the franchisor. The amount of information required to be disclosed under the Code is deemed to be the minimum amount required by the franchisee to make this informed decision.

Most franchisors now appear to offer the disclosure documents to prospective franchisees 14 days prior to entering the franchise agreement. A number of strong messages have been sent out by the ACCC on the possible consequences of a franchisor failing to comply with the disclosure requirements under the Code. Remedies in the event of failure to adequately disclose include a refund of money paid by the franchisee as well as rescission of the franchise agreement.

Feedback from franchisors indicates that the disclosure requirements have made the industry more transparent and act as a strong deterrent to some of the business practices, which cause dispute, and high rates of business failure. Franchisees have reported that the information provided by the franchisor allows them to make a more informed decision about the business they are about to enter and consequently greater chance of success.

The current dispute resolution mechanism as outlined in the Code has functioned successfully thus far with a large number of cases that complete the mediation process reaching a compromise.

3.5 Proposals for future consideration

ACCC endorsed Codes of Conduct

The ACCC believes that credible industry codes of conduct can deliver real benefits for consumers and small businesses in their dealings with bigger businesses. Effective industry codes can therefore result in increased compliance and reduced regulatory costs.

Effective voluntary codes, whether in the context of industry self regulation or co-regulation, carry substantial benefits for government, the regulator and industry. It is in the interests of all concerned to ensure that industry codes are developed, implemented, administered and maintained as an effective tool to achieve compliance with laws, best industry practice and maintaining effective competition. The ACCC also recognizes, however, that industry codes are sometimes unable to deliver in practice the outcomes they strive to achieve on paper. Such failures, as exemplified by the voluntary Franchising Code, do little to inspire small business confidence in self-regulatory approaches to industry concerns. Those who lack confidence in such measures will often call for the more prescriptive measure of a mandatory code of conduct.

In the ACCC's view, the benefits that might delivered by prescribing a mandatory code of conduct are accompanied with significant costs. These costs include the funds required for a regulatory agency to administer and enforce the code and to inform industry participants about their rights and obligations under the code. Additionally, those subject to the code must often consider substantial compliance costs. In contrast to this, the cost of administering a voluntary code of conduct can be considerably less.

Also, the processes associated with a mandatory code of conduct can result in a delay between identifying the need to amend a code (for example to address new industry practices) and actually making the amendment. Such delays can result in business meeting compliance costs for obligations that are no longer seen as necessary or, alternatively, in businesses continuing to engage in conduct that has been identified as a concern but has not been proscribed in law. Amendments to voluntary codes can, in contrast, be achieved relatively quickly and thus reduce these possible costs.

While the ACCC recognizes that there may be occasions when the additional costs associated with mandatory codes may be considered appropriate (such as in the

franchising sector), it also believes that greater effort can be put into ensuring that voluntary codes are credible and able to really deliver the benefits they purport to. The identified benefits of an effective industry code include but are not limited to effective dispute resolution regimes and a more transparent and an efficient industry that inspires confidence and industry growth.

Industry codes that fail to meet their objectives are deemed ineffective and if left unchecked are costly to industry[121] and the consumer and are likely to be counterproductive. If a code is not effective in delivering real benefits it will come under criticism by those whom the code purports to protect. In these circumstances, those businesses which incur compliance costs in meeting their obligations under an ineffective code are carrying unnecessary compliance burdens without any tangible benefits. Eventually, consumer and industry loss of confidence in ineffective codes will follow.

Currently, the ACCC is actively discussing codes issues with a number of industry groups - ranging from informal consultations, including working parties formed either to develop a code of practice or to review the effectiveness of a particular code. Continued requests from industry for assistance with code development demonstrate the ongoing interest by industry in the role of effective codes of conduct to address industry concerns.

The ACCC believes that a system of endorsing voluntary codes of conduct has the potential to provide effective industry codes of conduct that deliver real benefits to businesses and consumers with the least possible compliance cost placed on consumers or business.

The role of the ACCC will be to assist industry groups in ensuring the success of their codes. The industry will need to demonstrate that its code is achieving its objectives before the ACCC will provide endorsement.

Endorsement from the ACCC will be hard to obtain and easy to lose. The aim of such endorsement is to reassure businesses and consumers that the code participant they are dealing with operates in a fair, ethical and lawful manner.

However, if the ACCC assesses that an industry code is not achieving its objectives, it will recommend possible changes to that code to ensure all the essential criteria are met for an effective industry code. If the industry fails to adopt these recommendations, the ACCC will remove any endorsement.

It should also be noted that the proposed endorsement process should be distinguished from the existing prescription mechanism pursuant to s.51AE. The purpose of prescribing industry codes of conduct under the Act is to underpin or strengthen a voluntary industry code of conduct that has failed to meet its objectives. The effect of prescription is, of course, government regulation in a different form as the code becomes quasi-law. While there is a role for prescribed codes of conduct, as noted above, the

[121] The OECD estimated that Australian small and medium size businesses incurred compliance costs averaging $33,000 annually. *OECD 2002, Main Economic Indicators, OECD, Paris*.

proposed ACCC endorsement of voluntary codes should provide a credible and rigorous alternative to the more regulatory option.

The ACCC has recognised that for a code to be successful, numerous criteria must be met. These are not exhaustive but may include:

- Addressing specific consumer concerns
- Consultation with all stakeholders
- Clarity; Code administration
- Transparency
- Coverage
- Complaints handling
- In house compliance
- Sanctions for non compliance
- Independent review of complaints handling decisions
- Consumer awareness
- Industry awareness
- Data collection
- Monitoring
- Accountability
- Review of the Code, and
- Competitive implications and Performance indicators.

It is envisaged that increased interaction with industry will give the ACCC a greater understanding of the needs, constraints and challenges faced by a particular industry group. Moreover, it increases the prospect of industry groups formulating effective codes of conduct for self-regulation.

Information for small business on monitoring and reviewing codes of conduct

The ACCC considers there may be merit in the development of clear guidelines to assist small businesses and small business organisations in monitoring and reviewing the efficacy of voluntary codes. Such a guideline might provide the benefit of promoting effective and timely responses to consumer or industry concerns.

In the ACCC's view, it is important that self-regulatory or co-regulatory mechanisms such as industry codes of conduct can play an important role in addressing such concerns when such the small business or consumer stakeholders have confidence that such codes are genuinely capable of delivering the benefits they purport to offer.

4. OTHER MEASURES THAT MIGHT BE IMPLEMENTED

Whether there are any other measures that can be implemented to assist small businesses in more effectively dealing with anti-competitive or unfair conduct.

4.1 Small business collective bargaining notification

a small business collective negotiation notification process based on recommendations of the Dawson review. These recommendations were largely based on a proposal by the ACCC.

Under the proposed notification process:

- small businesses wishing to collectively negotiate would be able to obtain immunity from legal challenge under the *Trade Practices Act 1974* within a short statutory period of lodging a notification;
- the ACCC would only be able to revoke a notification if it was satisfied that the likely benefits to the public from the collective bargaining would not outweigh any public detriment;
- the process would be available for collective bargaining including associated collective boycotts;
- immunity from legal challenge would extend for three years;
- at least initially, notifications would only be able to be lodged for transactions valued at $3 million or less (the Minister would be able to vary this amount by regulation);
- third parties would be able to lodge collective bargaining notifications on behalf of a group of small businesses; and
- the notification fee would be set at an appropriately low level.

The Government, in agreeing to develop this notification process, noted that it will be 'speedier and simpler for small business than existing processes' – that is, than the authorisation process.[122] The ACCC agrees that the proposal will streamline the process for small businesses seeking to apply for immunity for collective bargaining where those arrangements are considered to be in the net public benefit.

[122] Commonwealth Government response to the Review of the Competition Provisions of the Trade Practices Act 1974, p7.

5. APPROACHES ADOPTED IN OTHER OECD ECONOMIES

Part (1)(e) of the Senate Committee's terms asks

Whether there are approaches adopted in Organisation for Economic Cooperation and Development (OECD) economies for dealing with the protection of small business as a part of competition law which could usefully be incorporated into Australian law.

5.1 Introduction

The following discussion considers information provided by a number of the ACCC's counterparts within the OECD. As a general introduction to this information, the ACCC recommends caution when considering the extent to which provisions in one country might be considered by another's laws; both the legislative, judicial and administrative frameworks and the economic structures of various markets within the respective countries may have some impact on the application of such provisions.

Many OECD countries distinguish between the promotion of competitive markets on the one hand and the mere protection of competitors on the other. A number of countries explicitly recognise the importance of small businesses in promoting competition.

A number of OECD countries have provisions that are substantially similar to those in Australian competition law, (for example the prohibition on price maintenance under the Canadian Competition Act, which is similar to the resale price maintenance provisions of the Australian Trade Practices Act). This submission focuses on those approaches to pro-competitive small business protection which differ significantly with, or are not currently addressed in, Australian competition regulation.

5.2 Recognition of small businesses by OECD competition regulations

The purpose of the Australian Trade Practices Act is to 'enhance the welfare of Australians through the promotion of competition and fair trading and provision for consumer protection. This purpose does not specifically refer to small or medium sized businesses in the marketplace.

Various OECD competition regimes do contain specific references to small businesses in their competition regime. For example, section 1.1 of the Canadian Competition Act states:

> 'The purpose of this Act is to maintain and encourage competition in Canada in order to promote the efficiency and adaptability of the Canadian economy, in order to expand opportunities for Canadian participation in world markets while at the same time recognizing the role of foreign competition in Canada*, in order to ensure that small and medium-sized enterprises have an equitable opportunity to participate in the Canadian economy and in order to provide consumers with competitive prices and product choices* (emphasis added).'

While only five of the respondents (France, Germany, Belgium, Korea and Japan) have competition laws that specifically exempt small businesses from bans on anticompetitive agreements, four others (Denmark, Austria, Hungary and Poland) include turnover and/or market share thresholds for exemption from these prohibitions that effectively give exemption to small businesses. Turkey is considering the inclusion of such exemptions in its laws.

Apart from Japan, the countries that specifically allow anticompetitive agreements between small businesses require that the agreement's purpose be to improve the competitiveness of the small businesses involved (see below at 4.8).

Japan and Korea have subcontract laws, which aim to prohibit unfair conduct by contractors towards subcontractors. Subcontractors tend to be smaller businesses than contractors.

5.3 Price discrimination

Price discrimination essentially involves selling the same product to different consumers for different prices, where the differences in price do not reflect the differences to the supplier in the cost of serving those customers.

Until 1995, the prohibition on price discrimination was found in s.49 of the Trade Practices Act. It essentially prohibited a corporation from discriminating between purchasers of goods of like grade and quality in relation to

- the prices charged for the goods;
- any discounts or rebates given in relation to the goods;
- the provision of services in respect of the goods; or
- the making of payments for services provided in respect of those goods where the discrimination is of such magnitude or is of such a recurring or systematic character that it has or is likely to have the effect of substantially lessening competition in the market for goods.

A number of defences[123] were included in the section, specifically

- Where the discrimination makes reasonable allowance for differences in manufacturing costs, distribution, sales or delivery resulting from the differences in places, methods of delivery, or quantities in which the goods are supplied to the purchasers; or
- The discrimination is done for the purpose of meeting competition
- Sub -section (5) contained a further defence, essentially that of reasonable and honest mistake, in circumstances where a person establishes that they 'reasonably believed, by reason of sub-section (2), the discrimination concerned was not prohibited by sub-section (1).

[123] Sub section (3) provided that the onus of proof lay on the party seeking to rely on the defence.

Over the years, views on the relative benefits of price discrimination prohibition in Australia have varied. In its report to the Minister for Business and Consumer Affairs made in August 1976, the Swanson Committee recommended the repeal of the section[124]:

> "The Committee considers that in the Australian context the conduct of a large buyer who is endeavouring to secure price cutting in his favour, whether it be discriminatory or not, may be more procompetitive than anti-competitive. Indeed such price cuts as a large buyer is able to obtain can trigger off competition from rival suppliers or can trigger off competition in a market where other forces are unlikely to produce active competition.
>
> As discussed above, the prohibition on price discrimination in section 49 has, in our view, operated substantially to limit price flexibility. The Committee believes that in the Australian context, section 49 has produced such price inflexibility that the detriment to the economy as a whole from the operation of the section outweighs assistance which small business may have derived from it. It is price flexibility which is at the very heart of competitive behaviour. The Committee thus recommends that section 49 should be repealed."

Some minor amendments to s.49 were introduced the following year. Amongst other things the Minister in charge of the Bill (Senator Durack) said:

> "The Bill does not accept the recommendation of the Swanson Committee that section 49 - the section which prohibits anti-competitive price discrimination - should be abolished.
>
> The Government has decided that section 49 should be retained - in the interests of assisting the competitive position of small businesses. The Government recognises, however, that difficulties with the interpretation of section 49 will remain. Accordingly, over the next few months, the Government will be looking at the operation of the section to determine whether there is any way in which those difficulties can be removed while still preserving the benefits of the section."

The prohibition on price discrimination in Australia under section 49 of the Trade Practices Act was repealed by the Competition Policy Reform Act 1995[125].

United States

The major federal statutes governing restrictive trade practices law in the US are the *Sherman Act 1890*, the *Clayton Act 1914*, and the *Federal Trade Commission Act 1914*.

In 1936 s.2 of the Clayton Act was amended by the Robinson-Patman Act to make price discrimination a felony if it may substantially lessen competition or tends to create a monopoly, or injures, destroys or prevents competition with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them.

A seller charging competing buyers different prices for the same "commodity" or discriminating in the provision of "allowances" -- compensation for advertising and other

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[124] Its views appear in Chapter 7 (pp. 43-46). The concluding paragraphs of the chapter were (pp. 45- 46).
[125](No. 88 of 1995). Like it's counterpart in the US Robinson-Patman Act, section 49 was criticised for promoting price rigidity and for hindering rather than helping competition. The Swanson, Blunt and HIlmer committees all recommended the repeal of the section. The repeal of the bill relegated any potential price discrimination regulation to sections 46 and 45.

services -- may risk contravening the Robinson-Patman Act. This kind of price discrimination may hurt competition by giving favoured customers an edge in the market that has nothing to do with the superior efficiency of those customers. However, price discriminations generally are lawful, particularly if they reflect the different costs of dealing with different buyers[126] or result from a seller's attempts to meet a competitor's prices or services[127]. A further defence concerns a response to changing conditions[128]. The onus of establishing any of these defences is on the party charged with price discrimination.

Price discrimination also might be used as a predatory pricing tactic -- setting prices below cost to certain customers -- to harm competition at the supplier's level. Antitrust authorities use the same standards applied to predatory pricing claims under the Sherman Act and the FTC Act to evaluate allegations of price discrimination used for this purpose.

Section 2(a) of the Robinson-Patman Act prohibits price discrimination where the effect of the discrimination has a reasonable possibility of substantially injuring competition[129]. This may occur in the context of dealings between the discrimination seller and its rival (primary line injury) or in the market in which the favoured and disfavoured customers compete (secondary line injury).

For the purposes of section 2(a) the Supreme Court has interpreted discrimination to mean 'merely a price difference'[130]. Delivered pricing systems, whereby some customers paid more than their actual costs of delivery and some paid less, were condemned in a number of early cases, however more recent authority has allowed various delivered pricing systems so long as they were available to all customers on a non-discriminatory basis. In finding discrimination, only reasonably contemporaneous sales may be compared[131].

Other requirements to establish price discrimination under the US laws include the requirement that the goods be of like grade and quality, that there be at least two different purchasers, and that the conduct relate to commodities (tangible objects as opposed to services)[132].

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[126] Known as the 'cost justification defence', which permits price differentials that 'make only due allowance for difference sin the cost of manufacture, sale or delivery resulting from the differing methods or quantities in which the goods are sold or delivered'.
[127] Cf Standard Oil Co v FTC 340 US 231, 251 (1951).
[128] Section 2(a) includes a defence for price differences resulting from a response to changing conditions affecting the market for or marketability of the goods concerned.
[129] FTC v Anheuser-Busch, Inc. 363 US 536 (1960)
[130] FTC v Anheuser-Busch Inc, cited above. For the purposes of determining a difference, the actual net prices are compared. The net price, in turn, takes into account all discounts, rebates, surcharges, and other factors that affect price to determine, as a question of fact, whether there was a price difference.
[131] What is reasonably contemporaneous is a question of fact determined by overall market conditions and the particular terms of sale.
[132] See generally Antitrust law developments (4th) vol 1, ABA section of antitrust law USA 1997

Price discrimination generally litigated in terms of secondary line injury. In *McCormick & Co*[133]., the largest supplier of spice and seasoning products in the US agreed to consent orders intended to address its alleged practice of giving discounts to favoured grocery store chains, conditional on their agreement to devote all or most of their shelf space to the McCormick line of products. The order required McCormick to cease and desist from discriminating in the net price charged to competing purchasers where the effect of the discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce or to injure, destroy or prevent competition.

A presumption of injury to competition

In arriving at their decision, the majority noted the Supreme Court decision in *FTC v Morton Salt Co*[134], in which it was held that injury to competition at the retailer level could be inferred where substantial and durable price discrimination exists between competing purchasers who operate in a market with low profit margins and keen competition. The majority also rejected the argument that the discriminating discounts were granted in the midst of, and possibly because of a price war, stating that the limits on discriminatory pricing – including the rile that a seller can meet but not exceed prices offered by a competitor – are not suspended during price wars.

In *Allied Sales & Service Co v Global Industrial Technologies Inc*[135], the standard set down in *Morton Salt* was interpreted to mean that injury to competition is established prima facie by proof of substantial price discrimination between competing purchasers over time.

Further, plaintiffs need not demonstrate that competition has, in fact, been adversely affected. The Act requires only a 'reasonable possibility' or 'probability' of substantial competitive injury[136].

Canada

The primary legislation governing restrictive trade practices in Canada is the federal Competition Act. It applies to most businesses and contains criminal as well as civil provisions. The general prohibition on price discrimination is found in s.51(1)(a) of the Competition Act. It makes price discrimination a criminal offence in some circumstances. Of particular note is the requirement for an anti-competitive effect, or an intent to eliminate a competitor.

> 50. (1) Every one engaged in a business who
>
> (*a*) is a party or privy to, or assists in, any sale that discriminates to his knowledge, directly or indirectly, against competitors of a purchaser of articles from him in that any discount, rebate, allowance, price concession or other advantage is granted to the purchaser over and above any discount, rebate, allowance, price concession or other advantage that, at the time

[133] *Decision and Order, Dkt no*. C-3939, 2000 WL 521741 (FTC Apr. 27 2000)
[134] 334 US 37 (1948)
[135] 2000 WL 726216 (SD Ala May 1, 2000)
[136] *Falls City Indust. V Vanco Beverage Inc* 460 US 428, 435 (1983).

the articles are sold to the purchaser, is available to the competitors in respect of a sale of articles of like quality and quantity,

(*b*) engages in a policy of selling products in any area of Canada at prices lower than those exacted by him elsewhere in Canada, having the effect or tendency of substantially lessening competition or eliminating a competitor in that part of Canada, or designed to have that effect, or

(c) engages in a policy of 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, is guilty of an indictable offence and liable to imprisonment for a term not exceeding two years.

(2) It is not an offence under paragraph (1)(*a*) to be a party or privy to, or assist in, any sale mentioned therein unless the discount, rebate, allowance, price concession or other advantage was granted as part of a practice of discriminating as described in that paragraph.

The instances of complaints concerning price discrimination in Canada are consistent with those of Australia, in that they are most prevalent in the grocery and petroleum retailing markets.

5.4 Predatory pricing

In most circumstances, low prices are considered beneficial. In fact, cutting prices to increase business is often a key aspect of competition. A business cannot usually increase its own market share without appropriating market share from one or more other businesses.

Predatory pricing occurs when a firm temporarily lowers its prices for the purpose of deterring market entry by new competitors, to drive out existing competitors, or to deter existing competitors from engaging in competitive conduct.

Other competition regimes within the OECD do, either though legislative or case law development, recognise predatory pricing as a distinct kind of anti-competitive conduct.

United States

The US Federal Trade Commission website notes that:

Because the antitrust laws encourage competition that leads to low prices, courts and antitrust authorities challenge predatory activities only when they will lead to higher prices. While the FTC has not found predatory pricing violations in recent years, it examines potential violations very carefully and maintains a close watch for other kinds of tactics -- like raising competitors' costs -- that may disadvantage rivals[137].

[137] Cited on US FTC website.

Spectrum Sports, Inc. v McQuillan[138] set out the elements of attempted monopolisation under section 2 of the Sherman Act; specifically, they are i) specific intent to monopolise, ii) anticompetitive or predatory conduct, and iii) a dangerous probability of achieving monopoly power.

State based regimes

It is important to note that a number of US states have unfair sales laws that differ significantly from federal laws; for example, some contain express prohibitions against selling below cost. There is also some variation in the approach taken by the various courts as to whether evidence of intent will be required to establish a breach, and if so the degree to which intent must be proven.

Canada

Predatory pricing is addressed in section 50(1)(c) of the Competition Act, and provides that

> 50. (1) Every one engaged in a business who
>
> (*c*) engages in a policy of 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, is guilty of an indictable offence and liable to imprisonment for a term not exceeding two years.

5.5 Misuse of market power

Although competition law in many jurisdictions proscribes the misuse of market power in a way that is anti-competitive, the means by which they do this, and the remedies available once a breach has been established, vary significantly.

The legislation and interpretation of the Australian prohibitions on misuse of market power have been discussed in detail above. What follows is an examination of the approach in other jurisdictions to the prevention of larger businesses from abusing their market position.

European Union

Article 82 of the EC Treaty prohibits abuse of dominant position in so far as it may affect trade between member states. The article is intended to regulate dominance and to prevent firms with significant market power from 'abusing' competitors and consumers. Any abuse of a dominant position is prohibited.

In the Hoffman-La Roche case, the conventional formulation of 'abuse' is expressed as:

> …an objective concept relating to the behaviour of an undertaking in a dominant position which is such as to influence the structure of a market where, as the result of the very presence of the undertaking in question, the degree of competition is weakened and which, through recourse to methods different from those which condition normal competition in

[138] 113 S. Ct. 884, 890-91

> products or services on the basis of the transactions of commercial operators, has the effect of hindering the maintenance of the degree of competition still existing in the market or the growth of that competition[139].

In recent years, the European Union has interpreted dominance as including collective dominance—a standard similar to that of a substantial degree of market power.

United States

Section 2 of the Sherman Act declares it a crime to 'monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce' among the states or with foreign countries.
Monopolization is the 'wilful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident.' (*United States v. Grinnell Corp.* 384 US 563, 570–71 (1966).)

Canada

Section 79 of the Canadian Competition Act proscribes the abuse of dominant position. The Canadian Act also directs the tribunal to consider whether the conduct is a result of superior competitive performance[140], and contains exemptions regarding intellectual property[141].

Abuse of dominant position

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

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[139] *Hoffman-La Roche* Case 85/76 [1979] ECR 461; 3 CMLR 211

[140] 79 (4) provides (4) In determining, for the purposes of subsection (1), whether a practice has had, is having or is likely to have the effect of preventing or lessening competition substantially in a market, the Tribunal shall consider whether the practice is a result of superior competitive performance.

[141] 79(5) provides that 'for the purpose of this section, an act engaged in pursuant only to the exercise of any right or enjoyment of any interest derived under the *Copyright Act*, *Industrial Design Act*, *Integrated Circuit Topography Act*, *Patent Act*, *Trade-marks Act* or any other Act of Parliament pertaining to intellectual or industrial property is not an anti-competitive act.'

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

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

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

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

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

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

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

(*j*) acts or conduct of a person operating a domestic service, as defined in subsection 55(1) of the *Canada Transportation Act*, that are specified under paragraph (2)(*a*); and

(*k*) the denial by a person operating a domestic service, as defined in subsection 55(1) of the *Canada Transportation Act*, of access on reasonable commercial terms to facilities or services that are essential to the operation in a market of an air service, as defined in that subsection, or refusal by such a person to supply such facilities or services on such terms.

On December 2, 2002 the Canadian Competition Bureau issued an Interpretation Bulletin on 'Abuse of Dominance in the Canadian Grocery Sector' that outlines how the Bureau 'addresses allegations that a dominant firm or group of firms, in the grocery sector is harming competition through the abuse of market power'.[142[1]]The Bulletin indicates, amongst other things, the Bureau's approach to assessing market share in the sector and notes that 'in contested cases heard to date by the Tribunal, the market shares of the dominant firms were 87% or higher'.[143[2]]

Prohibition where abuse of dominant position

79. (1) Where, on application by the commissioner, the Tribunal finds that

(*a*) one or more persons substantially or completely control, throughout Canada or any area thereof, a class or species of business,

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142[1] See *The Abuse of Dominance Provisions (Sections 78 and 79of the Competition Act) as applied to the Canadian Grocery Sector*, November 2002, at http://strategis.is.gc.ca
143[2] ibid at p.6."

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

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

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

Japan

In Japan, ss. 3 and 2(5) of the Antimonopoly Act prohibit 'private monopolisation'. Private monopolisation refers to overtly exclusionary or controlling conduct that causes substantial restraint of competition that is contrary to the public interest. The provisions have almost never been used. More often the JFTC has taken action against abusive tactics and exclusionary practices by treating them as unfair practices, probably because the standards of proof are less demanding. The separate provision about 'monopolistic situations' (s. 8–4) empowers the JFTC to break up monopolies without regard to whether they have engaged in monopolising practices.

New Zealand

Section 36 of the *New Zealand Commerce Act 1986* is modelled on the current section 46 of the Trade Practices Act. The prohibition on unilateral anti-competitive behaviour prevents a person from taking advantage of a substantial degree of market power for the purpose of restricting entry to any market, preventing or deterring competition or eliminating anyone from a market.

Austria

The Federal Competition Authority of Austria notes that Article 34 of the Austrian Cartel Act 1988 defines an undertaking (firm/business) as market dominating when exposed to insignificant or no competition, or is in a very superior market position compared to other competitors. Market dominance is defined as 30% or more market share, or at least 5% market share when only one or two competitors, or at least 5% market share when four largest competitors have at least 80% combined market share.

Turkey

Article 6 of the Law on the Protection of Competition 1994 prohibits Abuse of dominant position. Abusive practices include:

- Impeding the activities of competitors;
- Discriminating between purchasers;
- Resale price maintenance;
- Practices aiming to distort competition by means of their dominance; and
- Restriction of production, marketing or technical development.

5.6 Refusal to deal

While Australian competition law does not make specific reference to refusal to deal, it has, in certain circumstances, found a refusal to be in contravention of the TPA. A refusal to deal may constitute a misuse of market power[144], or unconscionable conduct[145]. Similarly, where the refusal is the result of an illegal anti-competitive agreement, exclusive dealing arrangements, or an attempt to enforce resale price maintenance, it will also be illegal.

Canada

Section 75 of the Canadian Competition Act specifically addresses conduct that constitutes a refusal to deal:

> 75. (1) Where, on application by the Commissioner or a person granted leave under section 103.1, the Tribunal finds that
>
> (*a*) a person is substantially affected in his business or is precluded from carrying on business due to his inability to obtain adequate supplies of a product anywhere in a market on usual trade terms,
>
> (*b*) the person referred to in paragraph (*a*) is unable to obtain adequate supplies of the product because of insufficient competition among suppliers of the product in the market,
>
> (*c*) the person referred to in paragraph (*a*) is willing and able to meet the usual trade terms of the supplier or suppliers of the product,
>
> (*d*) the product is in ample supply, and
>
> (*e*) the refusal to deal is having or is likely to have an adverse effect on competition in a market,
>
> the Tribunal may order that one or more suppliers of the product in the market accept the person as a customer within a specified time on usual trade terms unless, within the specified time, in the case of an article, any customs duties on the article are removed, reduced or remitted and the effect of the removal, reduction or remission is to place the person on an equal footing with other persons who are able to obtain adequate supplies of the article in Canada.

5.7 Unconscionable conduct

The current Australian law on unconscionable conduct as it pertains to Part IVA of the TPA is discussed in detail above. A number of other OECD countries that recognise a doctrine of unconscionability have approaches that differ in a number of ways.

United States

Unconscionability in contractual terms – 'substantive' and 'procedural' unconscionability

[144] *Queensland Wire Industries v BHP*
[145] cf *ACCC v Simply No Knead, ACCC v Suffolke Parke*

The starting point for examining unconscionable conduct in the United States is *Williams v Walker-Thomas Furniture*[146], in which it was noted

> 'Whether a meaningful choice is present in a particular case can only be determined by consideration of all the circumstances surrounding the transaction. In many cases the meaningfulness of choice is negated by a gross inequality of bargaining power. The manner in which the contract was entered is also relevant to this consideration.'

It was further noted that

> 'In determining reasonableness or fairness, the primary concern must be with the terms of the contract considered in light of the circumstances existing when the contract was made. The test is not simple, nor can it be mechanically applied. The terms are to be considered "in the light of the general commercial background and the commercial needs of the particular trade or case."'

The court also approved of *Henningsen v Bloomfield Motors*, in which it was held that 'a one sided bargain is itself evidence of the inequality of the bargaining parties.'

Further, it cited favourably *Daley v People's Building, Loan & Savings Ass'n*[147], where the court observed that its reluctance to interfere with people's right to contract as they choose only went so far as it is understood 'we are speaking of parties standing in an equal position where neither has any oppressive advantage or power.'

Craig Comb and Roberta Toher v. PayPal Inc. and Jeffrey Resnick v. PayPal Inc. C-02-1227 JF (PVT) in the United States District Court for the Northern District of California[148] ("the PayPal Case") provides a detailed exposition on situations in which contractual terms will *of themselves* be considered unconscionable;

> "Unconscionability has both procedural and substantive components. The procedural component is satisfied by the existence of unequal bargaining positions and hidden terms common in the context of adhesion contracts. The substantive component is satisfied by overly harsh or one-sided results that "shock the conscience." The two elements operate on a sliding scale such that the more significant one is, the less significant the other need be. A claim of unconscionability cannot be determined merely by examining the face of the contract; there must be an inquiry into the circumstances under which the contract was executed, its purpose and effect."

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[146] 121 US APP DC 315. This case dealt with a term of a contract on a hire purchase agreement that purported to allow the store, in the event of default of a payment, to repossess *all* the items previously purchased by the same purchaser. The furniture store sought and obtained enforcement of the term of the contract, however the appellate court refused to enforce the term.

[147] 178 Mass. 13, 59 NE (1901)

[148] This case involved 'click-wrap' agreements, whereby users of an online payment service entered into an agreement by clicking on a box at the bottom of an application page, stating that they had read and agreed to the user agreement. A link was provided to the user agreement, but did not need to be opened for the application to be processed. The agreement consisted of twenty-five pages, and included terms that conferred upon Paypal a unilateral right to vary the user agreement without notice. It also provided that Paypal may, at its discretion, restrict accounts and withhold funds pending the outcome of its own investigation into any dispute. Further, the agreement prohibited users from consolidating claims, and required that arbitration be carried out in a specified county in California. Paypal sought to enforce the arbitration clause, however this motion was denied on the grounds that the contract was unconscionable and therefore arbitration could not be compelled.

The court went into further detail regarding procedural and substantive unconscionability:

> 'A contract or clause is procedurally unconscionable if it is a contract of adhesion. A contract of adhesion, in turn, is a standardized contract, which, imposed and drafted by the party of superior bargaining strength, relegates to the subscribing party only the opportunity to adhere to the contract or reject it[149]….
>
> Substantive unconscionability has been found in many cases based upon arbitration provisions requiring arbitration of the weaker party's claims but permitting a choice of forums for the weaker party.'

In this particular case, the court found that 'Paypal's unilateral and apparently unfettered right to revise the User Agreement did bear on the question of whether the User agreement is substantively unconscionable.'

Further, the court found that the clause in the agreement prohibiting the consolidation of claims was unconscionable. The court cited the decision of the California Court of Appeal in *Szetela v Discover Bank, 97 Cal. App. 4th at 1094;*

> As is this case here (the Paypal Case), the arbitration agreement at issue in Szetela categorically prohibited individual customers from joining or consolidating claims in arbitration. The court determined that a large credit card company could not enforce the prohibition with respect to consumer claims against it because in practice most claims likely would involve consumers seeking the return of small amounts of money, and any remedy obtained by the few consumers who would not be dissuaded from pursuing their rights would pertain only to those consumers without collateral estoppel effect. *Id. at 1101.* The court concluded that such circumstances raise "the potential for millions of customers to be overcharged small amounts without an effective method of redress. . . ."

In particular, the court considered that the requirement to attend mediation in a specified county in California was unconscionable[150].

[149] In relation to adhesion contracts, the court cited *Flores v Transamerica Homefirst, Inc* 93 Cal. App. 4th 846, 853, 113 cal. Rptr 2d 276 (2001) and Armendariz v Foundation Health Psychcare Serv. 24 Cal. 4th 83, 113 (2000)

[150] This should be contrasted, however, with the decision in Bruce G Forrest v Verizon Communications Inc and Verizon Internet Services Inc, in which it was held that a forum selction clause located on page 13 of a clickwrap agreement was enforceable.

5.8 Application of competition law to small business

A number of jurisdictions within the OECD directly or indirectly ameliorate the application of competition law to the activities of small businesses. The approaches taken in different jurisdictions vary greatly. In some countries, small businesses below a certain turnover threshold have a general immunity from the competition provisions for certain purposes or for certain conduct. Other countries include a notification requirement.

The main examples are:

- legislated exemptions that directly benefit small business, for example the UK's Small Agreements and Conduct of Minor Significance Regulations and some US state government exemptions for collective bargaining agreements between medical professionals;
- exemptions granted by the competition agency, for example the EC block exemption for horizontal agreements and the ACCC's power to grant authorisation;
- safe harbours established by enforcement guidelines of competition agencies, for example the EC's *de minimis* Notice and the US *Antitrust Guidelines for Collaborations Among Competitors;*
- court based interpretation of the law, for example application by US courts of the rule of reason; and
- legislated exemptions for agriculture and primary producers.

The following is an outline of the application of competition law to small businesses in countries including NZ, Canada, the US, the EU and the UK. It is common for one jurisdiction's competition law to incorporate a number of features.

However, apart from the Australian and NZ authorisation processes, in most cases these approaches offer little or no comfort for price fixing as part of a collective bargaining strategy by small business.

In the UK and the EU where prohibitions on anti-competitive agreements can be declared inapplicable by the competition authority if an agreement meets certain cumulative criteria. Under the EC and UK competition rules, a party will not qualify for an exemption unless they can establish that the agreement leads to improvements in the production or distribution of goods, or the promotion of technical or economic progress and consumers will gain 'a fair share' of the benefits of the efficiency gain.

The UK, the EU and the US each have a system of 'safe harbours' within which agreements are presumed by agencies not to raise competition concerns. However these safe harbours are generally not available for agreements which fix price and they offer little assistance to small business collective bargaining on price.

New Zealand

New Zealand's *Commerce Act 1986* applies to both small and large businesses. Although the Act allows for the creation of statutory exceptions to the restrictive trade practices provisions, generally NZ small businesses that wish to engage in collective bargaining activities (including agreements on price) must seek authorisation from the Commerce Commission on the grounds that the conduct will lead to a net public benefit.

Under the NZ authorisation process, the primary focus is on efficiency gains—the Commerce Commission assesses both benefits and detriments and the focus has increasingly been on economic efficiency.[151] The Commerce Act specifically requires the Commerce Commission, when it determines the extent to which conduct will result in a public benefit, to have regard to any efficiencies that will result from the conduct. Other than an application currently before it involving proposed collective negotiations by pharmacists[152], the ACCC understands that the Commerce Commission has not adjudicated in recent years on any applications relating to small business collective bargaining.

European Union

The EU competition rules do not contain an explicit small business exemption. However, the European Court of Justice found that agreements between competitors that do not have an appreciable effect on competition or on intra-community trade are not caught by the prohibition on agreements that have the object or effect of preventing, restricting or distorting competition.

The European Commission (EC) considers that conduct will not appreciably restrict competition if the aggregate market share of parties to an agreement is no greater than 10 per cent when the parties are actual or potential competitors, or 15 per cent when they are not.[153] The market share threshold drops to 5 per cent when competition is restricted by the cumulative effects of parallel networks of similar agreements established by several manufacturers or dealers. However, these 'safe harbours' do not apply to agreements which, among other things fix prices, limit output or sales or allocate markets or customers.

The prohibition on agreements that may prevent, restrict or distort competition can be declared inapplicable if an agreement or practice meets the following criteria:

- contributes to improving the production or distribution of goods or to promoting technical or economic progress; and
- allows consumers a fair share of the resulting benefit; and

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151 NZ Commerce Commission, *The Pharmacy Guild of New Zealand (Inc)* Draft Determination at p. 50.

152 ibid. On 26 April 2002, the Commerce Commission issued a draft determination proposing to deny authorisation to these arrangements.

153 *Commission Notice on agreements of minor importance which do not appreciably restrict competition under Article 81(1) of the Treaty establishing the European Community (de miminis),* European Commission, 2001/C, at 368–07.

- does not impose unnecessary restrictions on the parties involved; and
- does not afford those parties the possibility of eliminating competition in respect of a substantial part of the products in question.

As well as the power to provide parties with exemptions for individual agreements, the EC also has limited power to declare that the prohibition does not apply to certain limited categories of agreements. For example, for horizontal agreements the EC has issued block exemption regulations for research and development (R&D) and specialisation agreements. However these do not exempt the parties if their combined market share exceeds 25 per cent (for R&D) and 20 per cent (for specialisation agreements). They also do not apply to agreements that aim to fix price or limit output or sales.

United Kingdom

The UK's *Competition Act 1998* applies to all businesses, whatever their size. Other than price fixing or market sharing, the Director-General of Fair Trading does not regard an agreement as having the requisite appreciable effect on competition if the parties' combined market share does not exceed 25 per cent.[154]

In addition, regulations made under the Act provide limited immunity from financial penalties only for 'small agreements' entered into by parties with combined worldwide turnover of less than £20 million, and 'conduct of minor significance' (which may involve an abuse of a dominant position) by a party with combined worldwide turnover of less than £50 million. The immunity under these regulations is not available for price fixing agreements. Nor does it protect businesses involved from any Office of Fair Trading investigations, or any other consequences that may arise from an infringement of the Competition Act.

Competing businesses that wish to collectively agree on price (or engage in conduct that is likely to appreciably prevent, restrict or distort competition) risk contravening the Competition Act unless they obtain an individual or block exemption. The grounds for such an exemption are the same as those applying under EC law.

United States

The Sherman Act outlaws 'every contract, combination … or conspiracy, in restraint of trade'. The US Supreme Court found that a reasonable interpretation of this provision is that it only prohibits arrangements that injuriously restrain trade and it does not prohibit arrangements which, although restraining trade, do so in a way that promotes competition, for example through the efficient self regulation of trade.

Under US law, price fixing agreements can be declared per se unlawful without requiring a detailed assessment of actual market power. The US Federal Trade ACCC (FTC) has expressed the view that stand-alone 'joint negotiation of price terms by non-integrated

[154] See the UK Office of Fair Trading's publication, *The Chapter 1 Prohibition.*

competing' small businesses would amount to an agreement not to compete on price, and would be per se unlawful.[155]

However, where the negotiations on price are reasonably related to 'an efficiency-enhancing integration of economic activity'[156] and are reasonably necessary to achieve the pro-competitive benefits of the integration, an arrangement will fall for consideration under the rule of reason. The FTC considers also that 'mere coordination of decisions on price, output, customers, territories, and the like' is not considered integration and cost savings without integration are insufficient to avoid the per se prohibition.[157] US courts have been prepared to condemn naked price agreements or boycotts by small business even where the participants may not have a particularly large market share.[158]

The FTC and US Department of Justice issued *Antitrust Guidelines for Collaborations Among Competitors*, which provide a safe harbour for competitor collaborations as a matter of enforcement policy. Under the guidelines, neither agency will ordinarily challenge a collaboration where the market shares of the collaboration and its participants collectively account for no more than 20 per cent of each relevant market. These safe harbours do not apply for price fixing or other per se conduct, and so they are unlikely to provide a safe harbour for small business collective bargaining on price.

The US *Small and Medium-Size Business Act 1958* allows exemptions for 'certain narrowly-defined agreements between small "independently owned and operated" firms which are not dominant in their sphere of activity'.[159] However, these exemptions, which have almost never been used, only appear to cover joint R&D agreements and those that in the President's opinion contribute to national defence.

A small number of US states have passed (or introduced) laws enabling medical professionals to collectively negotiate and in some cases require health care providers to negotiate in good faith with medical professionals. For example, since September 1999 Texas legislation has allowed competing doctors to jointly negotiate with health benefit plans where the likely benefits outweigh the likely disadvantages of a reduction in competition. When fees are being negotiated, the Texas Attorney-General is required to determine whether the health plan has substantial market power.

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155 See, for example, the FTC's Advisory Opinion provided to MedSouth Inc.

156 See the FTC and US Department of Justice's *Antitrust Guidelines for Collaborations Among Competitors* (April 2000), p. 8.

157 ibid.

158 For a discussion of this issue, see for example, *FTC v Superior Court Trial Lawyers Association (1990)* 493 US 411.

159 'Exemption for horizontal co-operation agreements for small and medium-sized enterprises (SME) from general cartel ban', background note in *General Cartel Bans: Criteria for Exemption for Small and Medium-Sized Enterprises,* Organisation for Economic Cooperation and Development (OECD) Roundtables on Competition Policy, series no. 10, p. 14. Also see 'Aide Memoire of the Discussion', p. 55.

Canada

Canada's competition laws apply to all sectors of the Canadian economy, except where specific exemptions exist (under the Competition Act or other legislation). The Competition Act contains no specific exemption for small businesses and accordingly many arrangements between small businesses, particularly on price, are considered under the prohibition against conspiracies.[160] First, this prohibition involves a consideration of whether the parties to the agreement have market power (that is, the ability to unilaterally affect industry pricing) and second, whether their behaviour is likely to be injurious to competition. While price fixing is generally viewed as injurious to competition, arrangements between small businesses which together do not have power in the relevant market do not contravene the Act.

5.9 Collective bargaining in agriculture

The application of competition law to the activities of primary agricultural producers varies considerably. While the EC and the UK approaches are influenced by the competing objectives of the formation of the EU, the US retains traditional protections for agricultural cooperatives and marketing organisations (while devolving more limited anti-trust responsibility to a specialised agency). New Zealand, Australia and Canada have favoured more universal application of competition law. However, by allowing primary producers to seek authorisation for collective bargaining, Australia and NZ have the flexibility to permit anti-competitive conduct where the broader public interest benefit is considered to outweigh the detriment to competition.

The application of competition law to collective bargaining in rural agricultural industries also varies among key overseas jurisdictions.

Although there is scope for statutory exemptions to be made under the NZ Commerce Act, the ACCC understands that there are few NZ regulations exempting arrangements in particular industries. However, following the amalgamation of numerous dairy cooperatives to form one national dairy processor, the NZ Government passed specific legislation giving the Commerce Commission powers to regulate the national dairy processor's operations.

The EC competition rules apply to production and trade in agricultural products. However, a regulation exempts from the rules agreements that form an integral part of a national public market authority or are necessary to meet common agricultural policy objectives (including productivity, efficiency and reasonable prices for consumers).

In particular, arrangements of farmers or farmers' associations in one state—for the production or sale of agricultural products or the use of joint facilities for storage, treatment or processing—are exempt, if they do not fix prices, exclude competition or jeopardise common agricultural policy objectives. To ensure compliance with EC competition rules concerning agriculture, the UK Competition Act excludes certain

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160 'Canada: Criteria for Exemption For Small and Medium-Sized Enterprises From General Cartel Bans', *General Cartel Bans: Criteria for Exemption for Small and Medium-Sized Enterprises,* p. 31.

agreements from the prohibition on anti-competitive agreements, to the extent that they relate to the production of or trade in an agricultural product.

Agriculture is one of a few US industries that are to various degrees exempted from general anti-trust laws. These exemptions are in a number of US statutes, including the Capper-Volstead Agricultural Producers' Associations Act, which allows persons engaged in the production of agricultural products to act together for the purpose of 'collectively processing, preparing for market, handling and marketing' products. However, this exemption is not absolute and the Secretary for Agriculture is authorised to act against cooperatives that monopolise or restrain trade to such an extent that the price of an agricultural product is 'unduly enhanced'.

Canadian competition law applies to rural industries, but not to arrangements and legitimate collective bargaining activities (including agreement on price) between 'fishermen' and persons engaged in buying or processing fish.

Belgium

The Belgian Act on the Protection of Economic Competition, coordinated on 1 July 1999. Chapter 2, s 1, art 2 allows exemption from prohibition for:

- any agreement or category of agreements between undertakings;
- any decision or category of decision by associations of undertakings; or
- any concerted practice or category or concerted practices,

that:

- Allow SMEs to increase their competitiveness in the particular market or international market; and
- Provide users with a fair share of profit that results,

without:

- Imposing on the undertakings concerned any restriction that is not indispensable for these objectives; or
- Giving such undertakings the opportunity to eliminate competition for a substantial part of the products concerned.

Under Chapter 2, s 1, art 5, there is no notification obligation for SMEs in order to obtain exemption from restrictive competitive provisions, as the Competition Council can exempt a competitive practice from the day the practice came into force.

The Competition Council can decide that the restrictive practice is forbidden, but cannot impose a fine unless the SME continues the practice.

Due to some uncertainty with the Act for the judge and parties, many SMEs notify of their anticompetitive practices to gain exemption anyway.

Germany

Section 4 of the Act against Restraints of Competition relates to Cartels of Small or Medium-Sized Enterprises (SMEs).

Agreements and decisions to rationalise economic activities via cooperation other than through specialisation cartels, may be exempted so long as there is no substantial impairment of competition, and it improves SME competitiveness.

The prohibition on cartels does not apply to joint purchasing agreements, so long as they do not compel participants to purchase from that source, and providing that the impairment of competition and improvement of SME competitiveness criteria are met.

Section 22 - Prohibition of Recommendations

Recommendations in order to circumvent the Act are prohibited, as are recommendations to maintain minimum or maximum prices with purchasers.

However SMEs are exempt when recommendations are made exclusively by SME trade and industry associations to their members, provided such recommendations are to improve competitiveness in relation to large businesses, and are declared to be non-binding and no pressure is applied to enforce them.

The Cartel Authority (i.e. the Bundeskartellamt) can declare these recommendations impermissible if they no longer meet exemption conditions.

Japan

Japanese law has

- exemptions for small business from prohibitions on anticompetitive agreements,
- prohibitions on the abuse of market power, and
- subcontract laws.

Section 22 of the Antimonopoly Act exempts cooperatives from the prohibition on unreasonable restraint of trade provisions on condition that:

- they are formed according to other laws;
- unfair trade practices were not used;
- competition is not substantially restrained;
- the purpose of the cooperative is mutual aid for small businesses or consumers;
- entry and withdrawal is voluntary;
- each member has equal voting rights; and
- limits on the distribution of profits among members (if applicable) is set out in law, Cabinet Ordinance or the articles of an association.

Act Against Delay in Payment of Subcontract Proceeds, Etc. to Subcontractors

Korea

MRFTA Article 19.(2).6 Allows improper concerted acts if they strengthen the competitiveness of SMEs where there is no other means for the small businesses to compete with large companies.

5.9.1 Approaches based on market thresholds

Rather than having a requirement to specifically gain an exemption, either through a specific process or by notification, a number of OECD countries contain broad exemptions for businesses meeting certain criteria.

In Austria, for example, article 16 of the Cartel Act 1988 defines minor cartels as those that at the time of formation have less than 5% of entire domestic market and less than 25% of relevant domestic local submarket.

Germany's federal cartel office, the Bundeskartellamt (BKA) committed not to apply the prohibition to SMEs with combined market share of less than 5%; and BKA can also simply choose not to oppose some anticompetitive agreements. About half the unopposed agreements are between SMEs.

In Hungary, the prohibition on restrictive agreements does not apply to those which have less than 10% market share, with the exception of some hardcore agreements.

Turkey is currently working on a "Communique on De Minimis" to exempt small businesses from Article 4's prohibition on agreements, concerted practices and decisions restricting competition. The threshold for exemption will be 10% of market share for horizontal agreements and 15% for vertical agreements.

ATTACHMENT A

Extracts from the Extrinsic Materials accompanying the 1986 Amendments to Section 46.

(emphasis added)

1986

PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

TRADE PRACTICES REVISION BILL 1986

EXPLANATORY MEMORANDUM

(Circulated by authority of the Attorney- General, the Honourable Lionel Bowen, M.P.)

TRADE PRACTICES REVISION BILL 1986

OUTLINE

The purpose of this Bill is to amend the Trade Practices Act 1974. The principal amendments are designed to effect significant improvements to the restrictive trade practices provisions (Part IV) and the consumer protection provisions (Part V) of the Act. The other amendments contained in the Bill form two broad categories-amendments of a technical character necessary to close loopholes, and amendments bringing up to date provisions relating to the administration and functioning of the Trade Practices Commission and the Trade Practices Tribunal.

2. Prior to the 1983 general election the ALP opposition released a business regulation paper in which it outlined, amongst other things, proposals to amend the Trade Practices Act. The Prices and Incomes Accord also highlights the need to amend certain sections of the Trade Practices Act. In February 1984, following a departmental review of the operation of the Act, the Government released a Green Paper entitled The Trade Practices Act: Proposals for Change. When releasing the paper the Government emphasised that the paper was intended as a catalyst for public discussion and that the proposals did not represent a final Government position. 120 submissions were received on all aspects of the proposals which were reassessed in the light of these submissions. Green Paper proposals have been significantly modified as a result of that reassessment.

3. The most significant amendment of Part IV is in cl.17 (misuse of market power). **It will lower the threshold of s.46, to apply the provision to those corporations which have a substantial degree of market power** and improve the effectiveness of s.46 in other respects. A new provision (s.50A) will extend the application of the act to mergers and acquisitions which occur outside Australia but which have anti-competitive effects in Australia.

Clause 17: Misuse of market power

35. **The amendments to s.46 are designed to lower the threshold test for determining whether the section is applicable to the conduct of a corporation.** The amendments also address the mode of proof. The new marginal note 'misuse of market power' is a more accurate characterisation of conduct of the kind to which s.46 is directed than 'monopolisation' as used in the Act now.

36. The amendment to sub-s.46(1), substituting the words 'a corporation that has a substantial degree of power in a market shall not take advantage of that power for the purpose of' is a composite provision. It should therefore, in the final analysis, be construed as a single provision even if particular words or expressions need to be looked at separately in the first instance.

Threshold test

37. The test of whether a corporation has 'a substantial degree of power in a market' is substituted for the previous test of a corporation 'being in a position substantially to control a market'. **The new test is intended to provide a lower threshold for the operation of s.46. The section may be invoked in relation to a corporation that has a lesser degree of market power than is required under the present provision.**

38. The expression 'power' is synonymous with 'market power' (see new sub-s.46(4)).

39. 'Market power' is a recognised economic concept which has been subject to considerable analysis in economic literature.

40. The use of the word 'degree' in the expression 'degree of power in a market' reflects the fact that 'market power' is a relative concept. All participants in a market possess a degree of market power which may range from negligible to very great.

41. The word "substantial" is used in several different contexts in the Act, and its meaning may change according to the context. Thus in Tillmanns Butcheries Pty Ltd v The Australasian Meat Industry Employees' Union and Ors (1979) ATPR 40-138 at page 18,500, in the context of 'substantial loss or damage', Deane J. preferred a meaning for 'substantial' of 'real or of substance as distinct from ephemeral or nominal' to the alternative 'large or weighty'. However, in the context of s.46, 'substantial' is intended to signify 'large or weighty' or 'considerable, solid or big' (Palser v Grinling [1948] A.C. 291 at page 317).

42. The word imports 'a greater rather than less' degree of power, per Smithers J. in Dandy Power Equipment Pty Ltd & Anor b Mercury Marine Pty Ltd (1982) ATPR 40-315 at p.43, 888. At the same time, **'substantial' in this context is not intended to require the high degree of market power connoted by the reference in existing s.46(1) to being in a position substantially to control a market, or by the reference in existing s.46(3) to the power to determine the prices of a substantial part of the goods in a market.**

43. New sub-s.(3) provides a guide to the way in which 'market power' is to be determined. It requires that consideration be given to the extent to which the conduct of a firm is or is not constrained by competition on the part of other participants in the market, potential entrants to the market, suppliers or purchasers.

44. The circumstances which give rise to absence of competitive constraint upon a corporation are diverse. They are not confined to size or market share in relation to competitors, or to those matters combined with technical knowledge, raw materials or capital. Other matters such as easier access to supplies or government controls on the market are relevant if they bear upon the extent to which the corporation can act without

being constrained by competition. Thus market power can be derived from statutory limitations on competition (e.g. through the creation of statutory monopolies) in the same way as any other constraints on competition can affect the operation of the market.

45. **A corporation having a 'substantial degree of market power' may have a lesser degree of market power than that of a corporation which 'would be, or be likely to be, in a position to … dominate a market' as provided in s.50. 'Dominance' connotes a greater degree of independence from the constraints of competition than is required by a 'substantial degree of market power'. Whatever the position in regard to 'dominance', more than one firm may have a 'substantial degree of power' in a particular market.**

46. In Europemballage and Continental Can v. Commission /1973/ CMLR 199; United Brands v. Commission /1978/ 1 CMLR 429 and Hoffman La Roche v. Commission /1979/ 3 CMLR 211 the court had to determine the degree of market power in order to decide the question of dominance. Although the test of dominance is higher than that applying in the case of a substantial degree of market power, these cases adopt a similar approach to that envisaged by new sub-section 46(3) for the purpose of determining the degree of market power.

Prohibited conduct

47. A corporation having the requisite degree of market power is not prohibited from engaging in any conduct directed to one or another of the objectives set out in paras.46(1)(a), (b) and (c). Such a prohibition would unduly inhibit competitive activity in the market-place. The section is not directed at size as such, nor at competitive behaviour as such. What is prohibited, rather, is the misuse by a corporation of its market power.

48. A corporation which satisfies the threshold test by reason of its market power is not permitted by s.46(1) to take advantage of that power for the purpose of one or other of the objectives set out in paras. (a), (b) and (c). Those paragraphs describe various ways in which competition may be impaired in a market.

49. The term take advantage in this context indicates that the corporation is able, by reason of its market power, to engage more readily or effectively in conduct directed to one or other of the objectives in paragraphs (a), (b) and (c). It is better able, by reason of its market power, to engage in that conduct. Its market power gives it leverage which it is able to exploit and this power is deployed so as to 'take advantage of' the relative weakness of other participants or potential participants in the market. Whether this is so in a particular case is a matter to be inferred from all the circumstances.

50. Likewise, the reference to purpose in this context indicates that the conduct of the corporation, by which it takes advantage of its market power, must be directed to impairing competition in a market in one of the ways set out in paras. (a), (b) and (c).

51. Sub-s.(7) makes it clear that whether a corporation has taken advantage of its power for a particular purpose is a matter which may be ascertained by inference from conduct or other relevant circumstances. While explicit statements if proved may establish the necessary purpose, direct evidence of that kind is not essential. The court may draw the necessary inference from conduct or other circumstances without the need for direct evidence. The ability to draw such an inference does not of course change the onus of proof. Proof of particular conduct or other circumstances may however give rise to a need for the other party to adduce evidence in order to rebut an inference which might otherwise be drawn. This amendment does not, by inference, limit the ways in which purpose may be proved in relation to other sections of the Act containing a purposive element.

52. By virtue of s.4F(b), it is sufficient if a requisite purpose (i.e. directed to s.46(1)(a), (b) or (c)) is one among other purposes of the corporation provided that the requisite purpose was a substantial one. In this context, 'substantial' is intended to signify a purpose which has substance or significance - as distinct from one which is ephemeral or nominal - rather than a purpose which is large, weighty or big.

53. **Kinds of conduct which in certain circumstances could be in breach of the provision would include inducing price discrimination, refusal to supply and predatory pricing.** These instances are indicative only and, in each case, it would be necessary to establish the requisite degree of market power and that advantage had been taken of the power for one of the specified purposes.

54. In regard to predatory pricing, in Victorian Egg Marketing Board v. Parkwood Eggs Pty Ltd (1978) ATPR 40-081, Bowen C.J. left open the question 'whether in the ordinary course a monopolist can engage in predatory price cutting only if the price is below some particular cost, and not where the price set, although it may deter competitors, is one which merely does not maximise the monopolist's profit' (at p.17,789). **It is not the intention of s.46 that pricing, in order to be predatory, must fall below some particular cost. The prohibition in the section may be satisfied 'notwithstanding that it is not below marginal or average variable cost and does not result in a loss being incurred'** (at p.17, 789). Certainly, though, where a corporation with the requisite market power is, in the absence of countervailing evidence that its pricing was not aimed at destroying actual or potential competition, selling at below average variable cost there may be grounds for inferring that it is taking advantage of its power for a proscribed purpose.

55. On the other hand, a corporation which is able to price its goods very competitively by reason, for example, of economies of scale or the acquisition of new efficient production facilities, would not be inhibited from so doing by reason of the fact that it enjoys a substantial degree of market power. By reflecting in its pricing policy its efficiency it would not, without more, be taking advantage of its market power notwithstanding any effect of its pricing on its competitors.

……

HOUSE OF REPRESENTATIVES. Hansard. 19 March 1986. extracts from pp 1624-1627.

TRADE PRACTICES REVISION BILL 1986

Bill presented by Mr Lionel Bowen, and read a first time.

Second Reading

Mr LIONEL BOWEN (Kingsford-Smith Attorney-General) 5.08) – I move:

That the Bill be now read a second time.

This Bill is to strengthen and improve the working of the Trade Practices Act 1974 in significant respects. It provides for the amendment of key provisions directed at restrictive trade practices in order to increase their effectiveness. It includes important new provisions to extend the protection afforded to consumers by the Act. The Bill also clarifies the intended meaning of a number of provisions and effects other changes for which experience with the legislation has shown a need.

Misuse of Market Power

A competitive economy requires an appropriate mix of efficient businesses, both large and small. Whilst large enterprises may frequently have advantages of economies of scale, there are many occasions when large size does not of itself mean greater efficiency. However, a large enterprise may be able to exercise enormous market power, either as buyer or seller, to the detriment of its competitors and the competitive process. Accordingly an effective provision controlling misuse of market power is most important to ensure that small businesses are given a measure of protection from the predatory actions of powerful competitors. Unfortunately, section 46 as presently drafted has proved of quite limited effectiveness in achieving that result, principally because the section applies only to monopolists or those with overwhelming market dominance. Even in those cases, it has been extremely difficult for a plaintiff to establish the requisite predatory purpose on the part of the defendant corporation.

The amendments proposed in clause 17 address these two problems and are designed to make section 46 much more effective. **The test for the application of the section is to be reduced from that of a corporation being in a position substantially to control a market to a test of whether a corporation has substantial degree of market power. As well as monopolists, section 46 will now apply to major participants in an oligopolistic market and in some cases, to a leading firm in a less concentrated market.** The amendment will also make it clear that the court can infer the requisite predatory purpose from the conduct of the corporation or from the surrounding

circumstances. Section 46 in its proposed from, which will be described as misuse of market power rather than monopolisation, is not aimed at size or at competitive behaviour as such of strong businesses. What is being aimed at is the misuse by a business of its market power. **Examples of misuse of market power may include in certain circumstances, predatory pricing or refusal to supply.**

Price Discrimination

I should mention that the Bill does not propose amendments to section 49, which deals with price discrimination. The Government has concluded that amendments of the kind which were canvassed in the Green Paper could have unintended and undesirable effects in particular leading to price rigidity. However, predatory price discrimination can be merely one manifestation of misuse of market power. The strengthening of section 46, and its more effective application to powerful buyers, will extend the potential application of that provision to predatory price discrimination.

ATTACHMENT B

Relevant extracts from cited s.46 judgments

(some references omitted, emphasis added)

Queensland Wire Industries Pty. Ltd. v. The Broken Hill Proprietary Company Limited & Anor. (1989) 167 CLR 177

Per Mason CJ and Wilson J

After the market has been delimited, the question is whether the defendant has "a substantial degree of power" within that market. **Market power can be defined as the ability of a firm to raise prices above the supply cost without rivals taking away customers in due time, supply cost being the minimum cost an efficient firm would incur in producing the product**: see Fuller, "Article 86 EEC: Economic Analysis of the Existence of a Dominant Position", (1979) 4 *European Law Review* 423 at p. 428. Section 46(3), which was added in 1986 by the *Trade Practices Revision Act,* provides that in determining the degree of market power a court should consider "the extent to which the conduct of [the defendant] in that market is constrained by the conduct of ... competitors, or potential competitors ...".[at 188]

…

The question is simply **whether a firm with a substantial degree of market power has used that power for a purpose proscribed in the section**, thereby undermining competition, and the addition of a hostile intent inquiry would be superfluous and confusing. [at 191]

Per Dawson J

In truth, the need to define the relevant market arises only because the extent of market power cannot be assessed otherwise than by reference to a market. **The term "market power" is ordinarily taken to be a reference to the power to raise price by restricting output in a sustainable manner.** See Landes and Posner, "Market Power in Antitrust Cases", (1981) 94 *Harvard Law Review* 937 at p. 937; Sullivan, *Antitrust* (1977), at p. 30; Areeda and Turner, *Antitrust Law* (1978), vol. II, at p. 322; Easterbrook, "The Limits of Antitrust", (1984) 63 *Texas Law Review* 1 at p. 20; Fuller, "Article 86 EEC: Economic Analysis of the Existence of a Dominant Position", (1979) 4 *European Law Reports* 423 at p. 428. **But market power has aspects other than influence upon the market price. It may be manifested by practices directed at excluding competition such as exclusive dealing, tying arrangements, predatory pricing or refusal to deal.** See *Standard Oil Co. v. United States (1911) 221 U.S. 1 at pp. 55-59*; *United States v. E.I. Du Pont De Nemours & Co. (1956) 351 U.S. 377 at pp. 389, 391-392*; 54 *Am Jur* 2d, Monopolies, §35. **The ability to engage persistently in**

these practices may be as indicative of market power as the ability to influence prices. Thus Kaysen and Turner define market power as follows:

> "A firm possesses market power when it can behave persistently in a manner different from the behaviour that a competitive market would enforce on a firm facing otherwise similar cost and demand conditions."

(Kaysen and Turner, *Antitrust Policy* (1959), at p. 75) [at 200]

Melway Publishing Pty Ltd v Robert Hicks Pty Ltd (2001) 205 CLR 1

Per Gleeson CJ, Gummow, Hayne and Callinan JJ

41. In *Queensland Wire*, Dawson J said:

> "The term 'market power' is ordinarily taken to be a reference to the power to raise price by restricting output in a sustainable manner ... But market power has aspects other than influence upon the market price. It may be manifested by practices directed at excluding competition such as exclusive dealing, tying arrangements, predatory pricing or refusal to deal ... The ability to engage persistently in these practices may be as indicative of market power as the ability to influence prices."

42. His Honour then went on to quote the authors Kaysen and Turner, who wrote:

> "A firm possesses market power when it can behave persistently in a manner different from the behavior that a competitive market would enforce on a firm facing otherwise similar cost and demand conditions."

43. **The notion of market power as the capacity to act in a manner unconstrained by the conduct of competitors is reflected in the terms of s 46(3). Such capacity may be absolute or relative. Market power may or may not be total; what is required for the purposes of s 46 is that it be substantial.** There has been no attempt in this Court to challenge the finding that Melway's market power is substantial.

44. The focal point of debate was whether, even accepting the purpose for which it was found to have been done, Melway's refusal to supply the respondent was a taking advantage of that power for the proscribed purpose. Consistently with the approach of the Court in *Queensland Wire*, much of the argument was directed to a consideration of **how Melway would have been likely to behave, if it had lacked the power it had**. Section 46 of the Act requires, not merely the co-existence of market power, conduct, and proscribed purpose, but a connection such that the firm whose conduct is in question can be said to be taking advantage of its power.

51. Dawson J's conclusion that BHP's refusal to supply QWI with Y-bar was made possible only by the absence of competitive conditions does not exclude the possibility that, **in a given case, it may be proper to conclude that a firm is taking advantage of market power where it does something that is materially facilitated by the existence of the power, even though it may not have been absolutely impossible without the power.** To that extent, one may accept the submission made on behalf of the ACCC, intervening in the present case, that s 46 would be contravened if the market power which a corporation had made it easier for the corporation to act for the proscribed purpose than otherwise would be the case.

Boral Besser Masonry Ltd (Now Boral Masonry Ltd) v ACCC [2003] HCA 5

Per Gleeson CJ and Callinan J

30. The Full Court did not disagree with any of those primary findings, but added a qualification to the proposition that barriers to entry were low. Finkelstein J, while acknowledging that structural barriers were low, observed that "the strategic behaviour of incumbent firms" may be a deterrent to new entrants. He then pointed to the pricing behaviour of the firms in the market, and postulated that a firm might set out to cultivate a reputation for predatory behaviour as a method of deterring entry. However, even if one were to accept the potential significance of such a "strategic barrier to entry", it needs to be kept in mind that the period in question saw a substantial and successful entrant to the market.

92. In asserting that BBM illegally took advantage of its alleged market power, the ACCC appeared to suggest, amongst other things, that there was collusion, or at least conscious parallelism, between BBM and Pioneer. In its pleading it referred to "an ability for Boral/BBM to communicate with Pioneer by market signals". Heerey J recorded that, at the beginning of the hearing, senior counsel for the ACCC disavowed any suggestion of collusion between BBM and Pioneer, but in final address contended that BBM "believed that once the market had been [rationalised] by the removal of two or three competitors during the price war, Pioneer would not prevent prices then rising to profitable levels". Heerey J was prepared to accept that BBM hoped and expected that, at the end of the price war, it could operate at a profitable level, but he rejected any hope or expectation of either collusion or conscious parallelism; and he found that, throughout the relevant period, the competition between both firms was "ferocious and relentless". Those findings were not challenged on appeal.

98. Fundamental to the case, and strongly contested, is the proposition that, **at the time of the conduct in question**, BBM had a substantial degree of power in a market, and that the conduct complained of constituted a taking advantage of that power.

100. The reference in that passage to "a firm's ability to 'give less and charge more'" is an expression of the central idea involved in the concept of market power. An aspect of the explanation of the concept of a market to which it will be necessary to return is the need to pay attention to the demand side as well as to the supply side.

121. **The essence of power is absence of constraint. Market power in a supplier is absence of constraint from the conduct of competitors or customers.** This is reflected in the terms of s 46(3). Matters of degree are involved, but when a question of the degree of market power enjoyed by a supplier arises, the statute directs attention to the extent to which the conduct of the firm is constrained by the conduct of its competitors or its customers. The main aspect of the conduct of BBM in question in the present case was its pricing behaviour. Therefore, the Federal Court was required by the statute to have regard to the extent to which BBM's pricing behaviour was constrained by the conduct of other CMP suppliers, or by purchasers of CMP. The reasoning of Heerey J followed that statutory direction.

131. In this connection, it should be remembered that the ACCC originally endeavoured to make out a case involving at least conscious parallelism between BBM and Pioneer. That attempt failed. If it had succeeded, the case may have taken on a different complexion.

Market power

136. In *Queensland Wire*, Mason CJ and Wilson J defined market power as the ability of a firm to raise prices above supply cost without rivals taking away customers in due time, supply cost being the minimum cost an efficient firm would incur in producing the product. Each side in the present case called an economist as a witness. They both defined or described the market power of a supplier in terms of its ability to raise prices above supply cost without losing business to another supplier. Pricing may not be the only aspect of market behaviour that manifests power. Other aspects may be the capacity to withhold supply; or to decide the terms and conditions, apart from price, upon which supply will take place. But **pricing is ordinarily regarded as the critical test**; and it is pricing behaviour that is the relevant conduct in the present case.

137. **Power, that is, the capacity to act without constraint**, may result from a variety of circumstances. A large market share may, or may not, give power. The presence or absence of barriers to entry into a market will ordinarily be vital. Vertical integration may be a factor.

138. **Financial strength is not market power, although if a firm has market power, its financial resources might be part of the explanation of that power.** The financial ability to survive a price war is not market power, or a manifestation of characteristics that give market power, if, when the price war is over, the market is still highly competitive. **Power in a supplier ordinarily means the ability to put prices up, not down.** But if a market is not competitive, and a firm puts prices down, seeking to eliminate a potential rival, in the expectation that it will thereafter be in a position to raise prices without competitive constraint, its ability to act in that manner may reflect the

existence of market power. An example of such conduct is *Compagnie Maritime Belge Transports SA v Commission of the European Communities* in which a liner conference, whose members were collectively in a dominant market position, used fighting ships and offered selective price reductions to force an entrant out of business. Ordinarily, where the members of a shipping conference agree between themselves not to engage in price competition, their agreement not to compete on prices will be a source of market power. If an outsider enters the trade, and they make the outsider a target, their conference agreement means they need not fear price competition from each other. Shippers cannot play them off against one another. They may then take advantage of the market power that results from their agreement to force the outsider from the trade, knowing that they can withdraw their offers of reduced prices when the outsider leaves, because the market will then be uncompetitive.

146. Further, there is an ambiguity in the concept of exclusionary conduct, which is of particular significance in a case such as the present. Paragraphs 11, 16 and 17 of the Statement of Claim are referred to above. The conduct on the part of BBM identified in par 11(a), and said in pars 16 and 17 to amount to a taking advantage of its market power, was pricing below cost. As the case was framed, the contravening conduct was price-cutting. If the manner in which BBM set its prices was an exercise of market power, the relevant kind of **power lay in its supposed ability to set prices free from constraint** resulting from the conduct of its competitors or its customers.

Per Gaudron, Gummow and Hayne JJ

163. Until its repeal in 1995, s 49 of the Act (inspired by the Robinson-Patman Act) may have proscribed predatory pricing when practised along with discrimination in pricing by the charging of two or more prices for the same product. So also s 46. It will be recalled that, as first enacted in 1974, s 46(1) spoke of a corporation that was in a position "substantially to control a market". Speaking of the provision in that form, Professor Breyer (as Justice Breyer then was) wrote:

> "Section 46 apparently prohibits predatory pricing, whether or not accompanied by price differences, when it prohibits a firm from taking 'advantage of the power' that it derives from being 'in a position substantially to control a market for goods or services' in order 'to eliminate ... a competitor'. This prohibition would apply when the predator already possesses significant market power. As a practical matter, also, this prohibition, together with that of s 49, may prove sufficient to stop almost all instances of predatory conduct. **Nonetheless, it should be noted that the Act does not prohibit predatory pricing when carried out by a firm with a comparatively small share of the market into which it is entering -- a firm that may have large financial resources behind it. If such a firm engages in predatory pricing before it obtains control of the market, but then ceases its practice once it succeeds, it may remain free of s 46.** As long as it charges only one price at any one time, it will remain outside s 49."

The reference to firms with large financial resources has a significance for this litigation to which it will be necessary to return.

170. What is involved in the sufficiency of the connection between the market power and the conduct complained of, expressed in the notion of taking advantage, was considered in *Melway*. In the present case, Heerey J observed:

> "**If the impugned conduct has a business rationale, that is a factor pointing against any finding that conduct constitutes a taking advantage of market power.** If a firm with no substantial degree of market power would engage in certain conduct as a matter of commercial judgment, it would ordinarily follow that a firm with market power which engages in the same conduct is not taking advantage of its power."

184. In any event, as s 46 is framed and has been interpreted in this Court, what is required first is an assessment of whether the firm in question possessed a substantial degree of market power, having regard to considerations such as those referred to by Heerey J and, if so, then asking whether the firm has taken advantage of that power for a proscribed purpose and in that way abused the power.

185. Merkel J reasoned substantially in similar fashion to Finkelstein J. His Honour referred to various matters which he said were "closely related to or form part of BBM's exclusionary conduct" and said that, when they were considered cumulatively, it was clear that to a significant extent BBM was able to behave independently of competition and of the competitive forces in the market. He added:

> "Each of the elements of BBM's exclusionary conduct demonstrate[s] that during the relevant period it persistently behaved in a manner that was significantly different from the behaviour that a competitive market would *enforce* on a firm facing otherwise similar cost and demand conditions. The factors to which I have referred indicate that during the relevant period BBM's market power was substantial."

186. This concentration upon the significance of exclusionary conduct tended to colour the result with notions of disapproval of competitive behaviour which was seen as unfair. But, as has been pointed out, the object of s 46 is not the protection of the economic well-being of competitors; if the behaviour which excludes or damages rivals is low pricing, it is customers who stand to benefit.

188. Both Merkel J and Finkelstein J relied upon the statement by Dawson J in *Queensland Wire*:

> "[M]arket power has aspects other than influence upon the market price. It may be manifested by practices directed at excluding competition such as exclusive dealing, tying arrangements, predatory pricing or refusal to deal ... The ability to engage persistently in these practices may be as indicative of market power as the ability to influence prices."

Some indication of what Dawson J had in mind may be seen in his reference to the observation by the Trade Practices Tribunal in *Re Queensland Co-operative Milling Association Ltd*:

> "In our view effective competition requires both that prices should be flexible, reflecting the forces of demand and supply, and that there should be independent rivalry in all dimensions of the price-product-service packages offered to consumers and customers."

In any event, Dawson J concluded the passage in question by setting out the text of s 46(3) with its reference to constraint by the conduct of competitors, suppliers or customers. What was said by Dawson J does not supply any adequate foundation for the approach taken in this case in the Full Court.

194. At the evidentiary level, the matters relied upon were not probative of the conclusion derived from them. They lacked the necessary rational probative value referred to in *Smith v The Queen*. The persistence of its pricing conduct demonstrates that BBM had access to sufficient financial resources to enable it to persist in setting its prices at the levels it did for as long as it did. It may also suggest that the alternatives of continuing to produce but not sell CMP in the Melbourne market, or to cease production of some or all of the CMP lines, were alternatives that were seen as being even less palatable than sustaining losses in the amount and for the time which BBM did. Neither producing without selling, nor ceasing production, is cost free. But to appreciate these considerations does not found any conclusion as to the existence of a substantial degree of market power. Further, to reason, as a matter of permissible statutory construction, from purpose to existence of substantial market power, is to invert the reasoning process which, consistently with the object of the provisions in s 46, is mandated by the decisions in *Queensland Wire* and *Melway*.

Per McHugh J

199. In my opinion, BBM did not have a substantial degree of power in the relevant market -- the sale of concrete masonry products -- because **it was not able to raise prices to supra-competitive levels without its rivals taking away customers**. **Nor was it in a position to recover the losses it made by pricing below relevant cost when and if the price- cutting finished. Accordingly, irrespective of the purpose of its pricing, it did not have a substantial degree of market power of which it could take advantage.**

264. The case brought by the ACCC must fail unless the evidence established that BBM had a substantial degree of power in the market for concrete masonry products. **A firm, in the position of BBM, possesses market power when it has the ability to sustain a pricing policy or the terms on which it supplies its product without regard to market forces of supply or demand.**

268. The ACCC contended that BBM had a substantial degree of market power because of its ability to engage in "predatory pricing" and that the nature of the market allowed it to take advantage of that market power. Central to the argument is the claim that BBM

"persistently sold important parts of its [concrete masonry products] range at prices that were below avoidable cost". Underlying the claim of the ACCC is the proposition that "predatory pricing" is itself a manifestation of market power, a proposition that gains support from a *dictum* in the judgment of Dawson J in *Queensland Wire*. But what is "predatory pricing"? Dawson J did not explain it. All that he said was that market power may be evidenced by a firm's capacity to engage in "predatory pricing". Is it pricing below some level of costs such as marginal cost or average variable cost? If so, how does it fit into the terms of s 46? How is "predatory pricing" distinguished from ruthless price-cutting that is the hallmark of the competitive market? Even a firm with a substantial degree of market power "has no general duty to help its competitors, whether by holding a price umbrella over their heads or by otherwise pulling its competitive punches". If "predatory pricing" can be defined in legal or economic terms, is its existence conclusive evidence of market power and the taking advantage of market power within the meaning of s 46 of the Act?

269. As I have indicated, neither s 46 nor any other provision of the Act defines or even uses the term "predatory pricing". And the terms and structure of s 46 suggest that it is not well suited for dealing with claims of "predatory pricing". In the context of a "predatory pricing" claim, s 46 seems under- and may be over-inclusive. **Conduct that is predatory in economic terms and anti-competitive may not be captured by s 46 simply because the predator does not have substantial market power when it sets out on its course to deter or injure competitors.** That may be because until it achieves its object it has no substantial degree of market power. Or it may be that it is a firm in a cyclical industry which has had, but does not have a substantial degree of market power at the time of the predatory conduct. In cyclical industries such as construction and building materials, firms may have no substantial degree of market power at the bottom of the economic cycle when competition is fierce and margins slender. As demand increases, however, some firms may acquire a substantial degree of market power. Section 46 is ill drawn to deal with claims of predatory pricing under these conditions. …

271. The difficulty of applying s 46 to a claim of "predatory pricing" is seen in the ACCC's rejection of BBM's contention that to determine substantial market power the test is the traditional one: "is the firm able to produce less and charge more?'' The ACCC conceded that this test "may be unobjectionable as a matter of theory". But the ACCC argued that in a case "involving price cutting below avoidable cost coupled with capacity expansions, the test for which [BBM] contends has no practical utility". This comes close to conceding that the term "market power" in s 46 cannot always capture "predatory pricing" if the traditional tests for determining market power are used.

278. Courts in the United States and the United Kingdom Office of Fair Trading regard the concept of recoupment as a fundamental element of a successful "predatory pricing" claim. Sound economic reasoning justifies the policy of the Office of Fair Trading and the United States jurisprudence. As Lockhart and Gummow JJ warned in *Eastern Express Pty Ltd v General Newspapers Pty Ltd*, however, care must be taken in translating the United States decisions on "predatory pricing" into s 46 at the expense of

an independent examination of the terms of the Act. **Nevertheless, to require recoupment as a necessary element of a "predatory pricing" claim fits in with the terms of s 46.** Although s 46 does not use the term "predatory pricing", two of its key components are "a substantial degree of [market] power" and a taking "advantage of that power". **A firm does not possess "substantial market power" if it does not have the power to recoup all or a substantial part of the losses caused by price-cutting by later charging supra-competitive prices.** If it cannot successfully raise prices to supra-competitive levels after deterring or damaging or attempting to deter or damage competitors by price-cutting, the conclusion is irresistible that it did not have substantial market power at the time it engaged in the price-cutting. As Mr Geoff Edwards has argued, "it is a contortion to find that a firm possesses substantial market power if the firm cannot use that power to obtain economic profits".

279. **Nor if a firm has substantial market power can it be said that it "take[s] advantage of that power" if it has no intention of recouping its losses**. In *Queensland Wire*, this Court held that "take advantage of" market power did not require proof of a hostile intent or use of that power. The Court equated "take advantage" with "use". **But the term "use" does not capture the full meaning of "take advantage of"**, as the later decision in *Melway* shows. There must be a causal connection between the "market power" and the conduct alleged to have breached s 46. Moreover, that conduct must have given the firm with market power some advantage that it would not have had in the absence of its substantial degree of market power. *Melway* could not have been decided as it was unless these propositions were correct.

287. The views of Merkel and Finkelstein JJ also seem to be based on a misunderstanding of what is meant by a substantial degree of market power. **Firms only have a substantial degree of market power when they can persistently act in a way over a reasonable time period unconstrained by the market's forces of supply and demand. Firms that do not have "the power to raise price above cost without losing so many sales as to make the price rise unsustainable" do not have market power. Cutting prices is not evidence of market power.** Any firm can do that. Market power is an economic concept and should be given its ordinary meaning. As Professors Krattenmaker, Lande and Salop point out:

> **"When economists use the terms 'market power' or 'monopoly power,' they usually mean the ability to price at a supracompetitive level."**

289. To require the prospect of recoupment in a "predatory pricing" claim does not limit the application of s 46 to conduct engaged in solely by monopolists rather than by firms having a substantial degree of market power, as Merkel and Finkelstein JJ thought. The United States jurisprudence and economic literature speaks of recoupment in the sense of the ability of a firm to extract monopoly rent out of the market because of its ability to gain a monopoly through the removal of competition. But this is not the only way of looking at the concept of recoupment. Recoupment involves the capacity of a firm to price in a manner inconsistent with what a competitive market would dictate in order, at a minimum, to make good the losses sustained during a price war. Although a firm may

seek not only to recoup its losses but also to earn monopoly profits, at a minimum a clearing of the losses would be required to make the conduct rational. The greater the degree of recoupment that a firm can achieve, the greater is its market power. **But a firm that is unable to recoup any of its losses has no market power.** It is the capacity to give less and/ or charge more or to act in a manner unconstrained by competitors that enables the price-cutter to recoup all or part of its losses by earning supra-competitive profits. A firm does not have to be a monopolist to have this capacity.

290. Merkel J also referred to the fact that the 1986 amendments to the Act lowered the s 46 threshold from a firm in a position "substantially to control a market" to a firm that has "a substantial degree of power in a market". He said that a firm with only a substantial degree of market power is unlikely to ever have the capacity to recoup its losses unless it was a monopolist, rendering the amendments nugatory. His Honour thought that the use of a recoupment test put a gloss on the section. Again, with great respect, his Honour's view appears to be founded on an erroneous view of market power. Section 46 is not breached unless a firm has a substantial degree of market power and takes advantage of that power. **As I have indicated a firm that cannot recoup its losses by supra-competitive pricing simply does not have market power and cannot take advantage of that power.** Heerey J placed no gloss on s 46 when he applied the United States cases on recoupment. Rather his Honour gave legal content and effect to the terms used by the legislature.

293. The concept of "market power" in s 46 shows that the section is not concerned with a one-second snapshot of economic activity. Market power can only be determined by examining what a firm is capable of doing over a reasonable time period. **Whether a firm has market power -- whether it has the ability to act unconstrained by competition, whether it can raise prices above competitive levels --** requires an examination of the existing structure and the likely structure of the market if competitors are removed or prices rise to supra- competitive levels. Such an analysis requires an examination of the business structure and practices of the alleged offender and its competitors, their market shares and the barriers to entry (if any) into the market. In *Queensland Wire*, Mason CJ and Wilson J said:

> "A large market share may well be evidence of market power ... but the ease with which competitors would be able to enter the market must also be considered. It is only when for some reason it is not rational or possible for new entrants to participate in the market that a firm can have market power ... There must be barriers to entry. ... Barriers to entry may be legal barriers -- patent rights, exclusive government licences and tariffs for example. Barriers to entry may also be a result of large 'economies of scale'."

Dawson J said:

> "The existence of barriers to entry may be conclusive in determining the relevant market and the degree of market power in it. In the context of s 46, the existence of significant barriers to entry into a market carries with it market power on the part of those operating within the market. Market power follows as a natural

> consequence of barriers to entry ... There is, of course, vigorous debate in economic circles about what constitutes a barrier to entry into a market. There are those who would and those who would not accept that the high cost of entry constitutes a barrier. ... However, it is less important to arrive at a precise meaning than to recognize the assistance given by the identification of conditions, in the nature of barriers to entry, for the purpose of defining the relevant market, measuring the extent of market power and determining whether that power has been exercised."

312. Nevertheless, Merkel and Finkelstein JJ were correct in saying that a market may have strategic barriers to entry as well as structural barriers to entry. Structural barriers can be assessed objectively by looking to the existence of intellectual property, capital investment, the availability of labour and materials, the nature of technology and similar matters. Strategic barriers to entry include matters such as economies of scale, pricing policies and the expansion of plant to generate excess capacity. The existence of strategic barriers can only be assessed by what is likely to happen in the particular market. While it may be difficult to draw the line between factors that merely make entry difficult because of a firm's superior efficiency and size and those that are properly considered strategic barriers to entry, it is necessary to do so. A failure to make such a distinction leads to a result inconsistent with the consumer oriented policy of s 46. If all matters that make entry difficult are considered barriers to entry, firms are likely to be regarded as having substantial market power when they do not have it. Consequently, they are more likely to be found to be in breach of the Act. Efficiency itself will be a burden on firms and will make it easier to find them guilty of breaches of the Act.

313. In assessing strategic barriers to entry, it is necessary to distinguish between the usual practices or conduct of the incumbent firms that act as a barrier and conduct in the circumstances of a period of economic depression or extremely vigorous competition. The Full Court looked to the conduct of BBM when the market was depressed, there was an excess of supply in the market and the major players were all competing for their survival. In such circumstances, it is unattractive for any potential entrant to enter at that point in time. However, unattractiveness to enter at a particular point of time is different from entrenched practices that act as true barriers to entry regardless of what is occurring in the market. Furthermore, the problem of viewing low prices as a significant barrier to entry is that a firm which prices low, below its costs, as in this case, will eventually seek or need to raise those prices -- a firm will not go on indefinitely suffering losses. If prices are raised to supra-competitive levels, other firms will see the incumbent making profits and enter the market, provided there are not other barriers to entry, as the only disincentive from entering the market has been removed. Pricing below cost is by its nature generally so transitory that by itself it usually cannot be considered a barrier to entry. It is true that BBM cut its prices and that in some circumstances price-cutting may constitute a signal to potential competitors that entry into the market is not worthwhile -- that is to say, the price-cutting may constitute a strategic barrier to entry. However, if pricing below cost is to be considered a strategic barrier to entry through its signalling effect, information asymmetries in the market would need to be considered. Signalling is effective when rivals are not aware of each other's cost structures and are led to believe a

rival can produce more efficiently at a lower price. Under those conditions, the signal informs a potential entrant that it should stay out of the market.

314. As I have indicated, the Full Court did not disagree with Heerey J's finding that the structural barriers to entry were low. And this was not a market in which the evidence showed that the strategic barriers, if they existed at all, were high. The evidence concerning major projects indicated that invariably BBM reduced its prices in response to requests -- or demands -- from the buyers to beat the prices tendered by its competitors. Once BBM determined to stay in the market, it was entirely rational for it to adopt the strategy of bettering its competitors' prices for as long as it could, as Heerey J found. All that a potential entrant would see from BBM's conduct was a firm that was prepared to match or better its rivals' prices at a time when the capacity for supply exceeded demand. A potential competitor would be reading a lot into this conduct to conclude that BBM was prepared to engage at any time in below cost pricing. Moreover, such a strategy could only be effective if BBM's "predatory pricing" was below the competitive costs of an efficient producer. The Act encourages competition because it benefits consumers. Competitive cost cutting cannot be regarded as a strategic barrier to entry and proof of substantial market power. But in any event, here the evidence showed that BBM had no substantial market power. That being so, whether the barriers to entry were high or low is a matter of no importance: BBM simply did not have substantial market power when it engaged in "predatory pricing".

317. Finkelstein J also said that BBM's ability to sustain the trading losses arising from its pricing policy was the result of it being part of a vertically integrated group and was indicative of market power. Similarly, Merkel J referred to the ability to engage in low pricing as indicative of market power. As Gleeson CJ and Callinan J point out in their joint judgment, **financial strength is not equivalent to market power, although financial resources may go to explaining the reason for a firm's power**. In his Second Reading Speech, explaining the amendments to s 46, the Attorney-General said that, while the threshold was reduced to substantial market power, the section as amended is not aimed at size or at competitive behaviour as such of *strong* businesses. Given the competitive nature of the market, the fact that BBM was part of a financially strong vertically integrated group has no relevance.

319. The findings of Heerey J make it plain that, while Pioneer remained in the market, the market would remain competitive. Without a finding that the removal of other players -- particularly C&M -- would lead to a non- competitive market allowing BBM to charge supra-competitive prices, the claim against BBM had to fail. It would fail because it would show that BBM had no substantial degree of market power leading to the conclusion that **it had none when it engaged in price-cutting**. Even if the removal of other players would lead to a non-competitive market, the ACCC's case faced the difficulty of establishing that BBM **had substantial market power *at the time* that it engaged in its price-cutting**. As I have already indicated, one of the difficulties in forcing a "predatory pricing" claim into the straightjacket of s 46 is that its terms may fail to catch conduct that ultimately has anti- competitive consequences.

Per Kirby J

364. I accept that **having access to financial resources is not the same as having "a substantial degree of power in a market"**. Nevertheless, the link between the two concepts cannot, and should not, be overlooked. In some circumstances, financial power can indeed be an indicator of the ability of a corporation to set supra-competitive prices in the past and to maintain in the future conduct with strategic objectives, the pursuit of which would otherwise be ruinous. It follows that access to financial power is by no means irrelevant to the possession by a corporation of a substantial degree of power in a given market. In a particular case, of which this was one, access to financial resources may be a marker for the existence of a substantial degree of power in the market as that expression is used in s 46 of the Act.

ACCC v Australian Safeway Stores Pty Limited [2003] FCAFC 149

Per Heerey and Sackville JJ.

299. In *Queensland Wire*, Mason CJ and Wilson J defined (at ATPR 50,009; CLR 188) market power as the ability of a firm to raise prices above the supply cost without rivals taking away customers in due time. Dawson J, however, adopted (at ATPR 50,015; CLR 200) a rather broader approach:

> "The term 'market power' is ordinarily taken to be a reference to the power to raise price by restricting output in a sustainable manner ... But market power has aspects other than influence upon the market price. It may be manifested by practices directed at excluding competition such as exclusive dealing, tying arrangements, predatory pricing or refusal to deal ... The ability to engage persistently in these practices may be as indicative of market power as the ability to influence prices. Thus Kaysen and Turner define market power as follows:
>
> 'A firm possesses market power when it can behave persistently in a manner different from the behaviour that a competitive market would enforce on a firm facing otherwise similar cost and demand conditions.' (Kaysen and Turner, *Antitrust Policy* (1959), p 75)."
>
> [Some citations omitted.]

This passage was cited with approval by the joint judgment in *Melway Publishing*, at 21, per Gleeson CJ, Gummow, Hayne and Callinan JJ. See, too, *Eastern Express Pty Ltd v General Newspapers Pty Ltd (1992) ATPR ¶41-167 at 40,299-40,300; 35 FCR 43*, at 62, where Lockhart and Gummow JJ observed that market power is concerned with power which enables a corporation to behave independently of competition and of the competitive forces in a relevant market.

300. In the case of a buyer, such as Safeway in the Wholesale Market, market power might be evidenced by a firm's ability to extract favourable prices from suppliers. (While it might be thought that such an exercise of market power works to the ultimate benefit of consumers in the form of lower prices, it is by no means the case: RD Blair and JL Harrison, "Antitrust Policy and Monopsony" (1990-1991) 76 *Cornell L Rev* 297, at 303-306.) But as the primary Judge pointed out, there are ways in which a purchaser in a market can act unconstrained by competition, otherwise than by influencing the output of or prices charged by suppliers. A purchaser's market power may be demonstrated by its ability to secure more favourable terms of trade than those available to other purchasers in the same market. His Honour cited the evidence of Professor Williams who defined monopsony power as (at 238 [1025])

> "buyer's ability to extract terms more favourable to itself than it could extract in a competitive market."

See, too, RD Blair and JL Harrison, above, at 320-321.

301. The essence of market power is, as Gleeson CJ and Callinan J said in *Boral Besser*, at 632 [121], the absence of constraint. In the case of a purchaser of goods in a market, such as Safeway, s 46(3) of the Act directs attention to the extent to which the purchaser's conduct is constrained by its competitors and potential competitors, or by its suppliers and customers. **Of course, market power need not be total**. Section 46(1) of the Act applies where a corporation has a ***substantial degree of power*** in a market. **It is therefore not necessary for a purchaser to be a monopsonist (a single buyer of a product or service) in order to have a substantial degree of market power**: *Melway Publishing*, at 21, per Gleeson CJ, Gummow, Hayne and Callinan JJ. Matters of degree are involved. In assessing the extent of a firm's market power, it is not only the matters referred to in s 46(3) that are relevant. Other relevant matters include the number of competitors, their strength and size, the height of barriers to entry and the stability or volatility of demand: *Boral Besser*, at 643 [168], per Gaudron, Gummow and Hayne JJ.

302. Section 46(1) took its present form in 1986. The *Trade Practices Revision Act 1986* (Cth), s 46(1) substituted the test of "a substantial degree of power in a market" for the previous test of a corporation "being in a position substantially to control a market". According to the Explanatory Memorandum accompanying the *Trade Practices Revision Bill 1986* the amendment was "designed to lower the threshold test for determining whether the section is applicable to the conduct of a corporation" (par 35). The Attorney-General, in the second reading speech, expressed much the same view:

> "As well as monopolists, section 46 will now apply to major participants in an oligopolistic market and in some cases, to a leading firm in a less concentrated market."

The argument in the present case proceeded on the basis that the amended version of s 46(1) is intended to lower the threshold test. In any event, **it is clear that s 46(1) of the Act is not concerned only with a pure monopsony or a near monopsony**.

329. In our view, this analysis ignores the question of ***why*** Safeway engaged in the impugned conduct. This is not the same question as to whether one or more of the statutorily proscribed purposes existed. Before reaching that point it is necessary to look at not only what the firm did, but why the firm did it. That is why **a business rationale for the conduct, independent of the question of market power, is relevant**: *Melway Publishing*, at 13-14 [17]-[19], 18-19 [31], 20 [38], 26 [62], per Gleeson CJ, Gummow, Hayne and Callinan JJ; *Boral Besser*, at 643-644 [170]-[171], per Gaudron, Gummow and Hayne JJ; D Robertson, "The Primacy of 'Purpose' in Competition Law -- Part 1" (2001) 9 *CCLJ* 101, at 115, 121. Another example is *Queensland Wire* itself. The bare fact of BHP refusing supply to Queensland Wire would have taken on a different complexion if, for example, the reason for that refusal was genuine concern for the latter's creditworthiness. And again, as in *Boral Besser*, the bare fact of pricing below cost may be attributable to a firm having no market power but simply wanting to stay in business. Alternatively, it may be the firm has market power and expects it can drive competitors out of the market and then recoup its costs by obtaining supra-competitive prices: see at 643 [171], per Gaudron, Gummow and Hayne JJ. **The rationale for the conduct is critical.**

333. Section 46(1) of the Act is not confined to a case where a corporation succeeds in achieving an anti-competitive object. Its terms are satisfied when a corporation that has a substantial degree of power in a market takes advantage of that power for one of the proscribed purposes. **In determining whether a corporation has taken advantage of its market power it is enough that the corporation's conduct has been "materially facilitated" by the existence of its power.** In each of the four instances with which we are concerned Safeway deleted all or most of the plant baker's products from one of its supermarkets. Its reason for doing so was to induce the plant baker to cease supplying discounted bread to an independent retailer in competition with a Safeway supermarket. As we have explained, there would have been no purpose in Safeway acting in this manner in a competitive market. On the contrary, had Safeway done so it would have inflicted economic harm on itself for no gain. **Safeway's conduct in the four instances was therefore materially facilitated by the existence of its market power even though that same conduct would not have been "absolutely impossible" without that power.**

Per Emmett J.

455. Market power of a seller exists when a firm can behave persistently in a manner different from the behaviour that a competitive market would enforce on a firm facing otherwise similar cost and demand conditions: *Queensland Wire* (at 200); *Melway Publishing Pty Ltd v Robert Hicks Pty Ltd (2001) ATPR ¶ 41-805; 205 CLR 1 at 21*. Monopsony power may therefore be defined as the ability of a purchaser to obtain a market price lower than would otherwise be obtained in a competitive market, or to obtain more favourable terms of trade in the market than would otherwise be obtained in a competitive market.

457. **The essence of market power is absence of constraint. Market power in a supplier is absence of constraint from the conduct of competitors or customers.** When a question of the degree of market power enjoyed by a supplier arises, the Act

directs attention to the extent to which the conduct of the firm is constrained by the conduct of its competitors or its customers: *Boral Besser* (at 632[121]). So much is reflected in the terms of s 46(3) of the Act. Section 46(3) relevantly provides that, in determining, for the purposes of s 46(1), the degree of power that a body corporate has in a market, the Court must have regard to the extent to which the conduct of the body corporate is constrained by the conduct of:

• competitors, or potential competitors of the body corporate in that market; or
• persons from whom the body corporate acquires goods in that market.

458. In the context of s 46, the existence of significant barriers to entry into a market carries with it market power on the part of those already operating within the market. Market power follows as a natural consequence of barriers to entry, which are also a pre-requisite to the establishment and maintenance of a monopoly. The identification of barriers to entry helps both to define the relevant market and to establish the existence of market power: *Queensland Wire* (at 201). **The existence of barriers to entry will therefore be a prerequisite to the establishment and maintenance of monopsony or near monopsony.**

460. The term "market power" in relation to a supplier is ordinarily taken to be a reference to the power to raise prices by restricting output in a sustainable manner. However, market power has aspects other than influence upon the market price. It may be manifested by practices directed at excluding competition, such as exclusive dealing, tying arrangements, predatory pricing or refusal to deal. The ***ability*** to engage persistently in such practices may be as indicative of market power as the ***ability*** to influence prices. A firm may be said to possess market power when it can behave persistently in a manner different from the behaviour that a competitive market would enforce on the firm facing otherwise similar cost and demand conditions. **Market power may therefore be said to be the advantage that flows from monopoly or near monopoly.** Section 46(3) of the Act gives effect to that notion: see *Queensland Wire* (at ATPR 50,014; CLR 200-201).

461. Similarly, **market power on the part of a buyer may be regarded as the advantage that flows from monopsony or near monopsony. Also, exclusive dealing or refusing to deal might also be a manifestation of monopsony power**. That is to say, the ability to engage in such conduct persistently, without a loss of supply, may be indicative of market power if it can be shown that such conduct would have a different consequence if engaged in in a "competitive market".

Universal Music Australia Pty Ltd v ACCC [2003] FCAFC 193

Per Wilcox, French and Gyles JJ

161. In our opinion, it is not necessary in these cases to grapple with the difference between market dominance (the test before the 1986 amendments) and substantial power

in the market (the current test) (c.f. McHugh J in *Bora*l at paras 285, 286 and 289-90, *Australian Competition & Consumer Commission v Australian Safeway Stores Pty Limited* [2003] FCAFC 149 at para 301). Nor is it necessary to deal with ACCC's argument that pricing power alone is not decisive.

Rural Press Ltd v Australian Competition & Consumer Commission [2002] FCAFC 213

Per Whitlam, Sackville and Gyles JJ

148. In any event, there is a significant distinction between the facts in the present case and those in *Victorian Egg Marketing Board v Parkwood Eggs*. In the latter, the manner in which the Board acquired ownership of eggs in Victoria was regarded as an important element in its control of the Victorian market. It regulated prices in Victoria and was not required to maximise profit. Bowen CJ considered that it had been established, at least on a *prima facie* basis, that the manner in which the Board controlled the Victorian market enabled it to engage in price cutting in the Australian Capital Territory: see at 303-304. In other words, but for the Board's dominance of the Victorian market and its unusual powers to control that market, it could not have engaged in price cutting in the Territory. **In the present case, Rural Press and Bridge Printing could have threatened credibly to enter the Riverland market and, indeed, actually entered that market regardless of whether they had a substantial degree of market power in the Murray Bridge newspaper market.**

149. The matter can be analysed by considering the question which the primary judge posed, (at [128]; 42,741):

"... whether, even without the substantial market power ..., Rural Press and Bridge **might have been able to act** in the same way."

That this is the correct question is suggested by the majority judgment in *Melway Publishing v Hicks*. In any event, the ACCC did not dispute that the question was the appropriate one to ask.

150. In our opinion, the answer is plainly yes. Rural Press and Bridge Printing had ample financial and physical resources to make the credible threat that was made, regardless of the market power they held in the small Murray Bridge newspaper market. They may have been motivated by a desire to maintain that market power in making the threat, but they were not taking advantage of that market power in so doing. Even if there had been a perfectly competitive market in the Murray Bridge newspaper market, **Rural Press and Bridge Printing could have threatened to launch (and could have actually launched) a foray into the Riverland market. Had there been a perfectly competitive market in the Murray Bridge newspaper market, they may have lacked the motivation to make the threat, but they could have acted in precisely the same**

way. There is no finding that Rural Press and Bridge Printing could not have continued to service fully the Murray Bridge newspaper market in addition to the Riverland area. On the contrary, the findings rather assume that there was spare capacity. [emphasis added]

Summary of unconscionable conduct cases

SECTION 51AA

ACCC V CG Berbatis Holdings Pty Ltd [2003] HCA 18
The ACCC alleged that the landlord of Farrington Fayre shopping centre implemented a strategy in 1996 and early 1997 where they refused to grant renewals, variations or extensions of leases to three tenants unless those tenants withdrew from legal proceedings before the WA Commercial Tenancy Tribunal.

The ACCC formed the view that these tenants were at a special disadvantage when bargaining with the landlord because of their financial dependence on the lease negotiations.

In September 2000 the Court found the conduct by the landlord was unconscionable within the meaning of 51AA. The landlord appealed and the ACCC launched a cross-appeal. On 27 June 2001 the Full Federal Court upheld the appeal by the owners and dismissed the ACCC's cross appeal. The ACCC was subsequently granted leave to appeal the decision to the High Court, however this appeal was dismissed.

ACCC v Samton Holdings Pty Ltd [2002] FCA 62
A small business tenant failed to exercise their option to renew a lease by a required date. The ACCC alleged that the landlords were aware that the tenant wished to continue trading in the long term before the option expired. Following the failure to exercise the option on time, the tenant was required to pay $70,000 to secure the extension.

On 29 November 2000 the Court concluded that while the company had struck a hard bargain it fell short of being unconscionable within the meaning of 51AA. The Court dismissed the ACCC's application against the company and the six landlords.

An appeal by the ACCC was dismissed on 6 February 2002, after consideration of the term 'special disadvantage'.

National Australia Bank
The ACCC alleged NAB sought and enforced a personal guarantee for $200,000 to cover loans to Mrs Ashton's husband's business, using the couple's Mt Nelson, Hobart home as security, and then withheld $7,760 over and above the home mortgage amount, realised after the home was sold.

The guarantee was obtained from Mrs Ashton in June 1998 as security for a business loan to a company of which Mr Mark Ashton was a director. The ACCC alleged that at the time Mr Ashton was seriously incapacitated. Mrs Ashton executed the guarantee in her own name and in her husband's name, exercising a power of attorney. She was not a director or shareholder of the company.

The ACCC alleged that when NAB sought Mrs Ashton's guarantee, it did not explain the nature or effect of the guarantee, or advise her that she should obtain independent legal advice. The ACCC also alleged that NAB knew the company was in serious financial difficulty but did not inform Mrs Ashton. A year later, NAB demanded payment of the company's debts to the bank secured by the guarantee. The ACCC alleged that enforcement of the guarantee resulted in the sale of the Ashton's family home and NAB required the entire sale proceeds to be paid to the bank.

After the ACCC instituted the proceedings NAB annulled the guarantee signed by Mrs Ashton and refunded to the couple with interest the excess money taken from the proceeds of the sale of the Ashton's family home under the guarantee which amounted to $7,760. The ACCC and NAB engaged in mediation which resulted in agreement on orders to be sought from the Court. As part of the settlement NAB consented to pay $28,500 to the Ashtons for damages, the claim for which included emotional stress, caused to them by NAB's conduct, and consented to pay the ACCC's taxed legal costs.

SECTION 51AC

***ACCC v Simply No Knead (Franchising) Pty Ltd* [2000] FCA 1365**
This case dealt with disputes that developed between a franchisor, Simply No Knead (SNK), and some of its small business franchisees.

SNK refused to consider complaints unless received by mail and would not agree to joint meetings with the franchisees. SNK also placed unreasonable conditions on the meetings, and threatened to withhold essential business supplies unless the franchisees complied with certain conditions. These conditions included:

- requiring franchisees to purchase full boxes of a product, which may have taken several years to sell, despite telling the franchisees they could purchase half boxes;
- demanding the surrender of diaries containing details of customers;
- requiring franchisees to pay for brochures and other advertising that did not include their store's details.

SNK also competed directly with the franchisees, contrary to the terms of the franchise agreement, harming their businesses.

For these reasons, in September 2000 the court declared SNK had breached section 51AC of the Trade Practices Act. The court also declared that SNK had contravened the Franchising Code of Conduct (in breach of section 51AD) by withholding disclosure documents from each franchisee unless they gave their written consent to renew the agreement. It also declared that Cameron Bates, the Managing Director of SNK, was a person involved in the contraventions of section 51AC and 51AD by SNK.

Cheap as Chips
The court will also consider failure to comply with a relevant industry code when it examines unconscionable conduct cases under s. 51AC. In an example of such a case,

the court found Cheap as Chips, a chemical cleaning franchise, had terminated a franchise without following the procedures in the Franchising Code of Conduct.

On 14 March 2001 the Federal Court declared that Cheap as Chips had contravened the Code by, amongst other things, failing to negotiate with franchisees. This factor was relevant to a finding that Cheap as Chips had also engaged in unconscionable conduct in contravention of section 51AC of the Trade Practices Act.

Cheap as Chips was restrained from engaging in similar conduct and was ordered to give franchisees reasonable access to records, notify all current franchisees about the outcome of the proceedings, pay compensation, interest and a contribution towards the ACCC's legal costs. The Court also noted that Cheap as Chips provided an undertaking to the ACCC pursuant to section 87B, to implement a trade practices compliance program.

Half Price Shutters
Australian Industries Group (AIG) operated a company called Half Price Shutters in Perth. AIG was ordered to compensate three small business owners $77 594 after the court declared it had engaged in unconscionable conduct, breached the Franchising Code of Conduct and made false representations regarding the profitability of the business.

In addition to compensating the small businesses, AIG were restrained from engaging in similar conduct in the future, required to institute a trade practices compliance training program and pay the ACCC's costs.

Leelee
Leelee was a retail landlord operating a food court. In dealings with one of its tenants Leelee withheld crucial information about changes to the rental charged under the lease.. It also failed to honour existing terms of the lease, which conferred exclusive entitlements on the tenant in relation to the range and price of food sold by the tenant, and refused to consider the grant of a fresh lease to a prospective purchaser of the tenant's business.

The court declared that the landlord had acted unconscionably, and granted injunctions restraining Leelee and its director, Mr Ong from engaging in similar behaviour in the future.

Suffolke Parke
Suffolke Parke Pty Ltd was a master franchisee for The Cheesecake Shop. It leased premises to a franchisee, which operated a Cheesecake Shop business from the premises. Part of the leased premises was a separate shop that the franchisee had been permitted to sublet on previous occasions.

Following disputes between the parties over franchising matters, the franchisor refused to allow the franchisee to sublet the shop again. This refusal was allegedly in reprisal for complaints arising from Cheesecake Shop franchisees concerning the franchisor's conduct as a director of the master franchisee for SA.

When the franchisee sought mediation under the Franchising Code of Conduct, the franchisor refused to attend.

The court declared that Suffolke Parke and its director had acted unconscionably toward its tenant and that the company had breached the Franchising Code of Conduct by refusing to attend mediation.

The court ordered Suffolke Parke Pty Ltd and its director to compensate the franchisee, pay the ACCC's costs and implement a trade practices compliance training program.

This retail tenancy dispute was unrelated to The Cheesecake Shop national franchise.

Avanti

In 1994 Avanti Investments leased land to farmers in South Australia. The original lease agreements had no limitation on the water available from a bore on the land. However, subsequent agreements significantly reduced the amount of water available, despite Avanti claiming that the agreements were unchanged.

Avanti sold a large proportion of the water allocated to the bore, which resulted in the farmers incurring excess water charges. Avanti then demanded payment from the farmers, many of whom lacked formal education, English language skills or commercial experience, totalling more than $67 000 for excess water use.

The Federal Court declared that Avanti had engaged in misleading and deceptive conduct, had made false representations in relation to land, and had engaged in unconscionable conduct under s. 51AC.

The court granted injunctions restraining Avanti from demanding payment for excess water, and requiring them to indemnify the farmers for any excess water charges until their leases expired. Avanti and its then director were also required to pay the ACCC's costs.

Medibank Private
Medibank Private gave court enforceable undertakings to the ACCC following an investigation of its conduct in relation to an independent specialist psychiatric hospital located in Brisbane.

The conduct related to a Hospital Purchaser Provider Agreement (HPPA). HPPA's are agreements between private health funds and private hospitals whereby hospitals agree to provide services to members of health funds at agreed rates of contribution from the funds.

The Australian Private Hospitals Association complained to the ACCC about a clause in the HPPA with Toowong that would have allowed Medibank Private to vary the terms of a HPPA without the hospital's consent.

The ACCC believed the conduct may have been unconscionable due to the apparent disparity of bargaining power, the fact that Medibank Private did not discuss the reasons for the clause or negotiate on it for some time, and that Toowong had the impression that the clause was standard and should not be of concern. Further, the ACCC considered that the clause was not reasonably necessary to protect Medibank Private's commercial interests.

Medibank Private agreed not to use such a clause in future HPPA's with any hospital, reimburse Toowong's costs incurred that resulted from their dealings regarding the clause, contribute towards the ACCC's investigation costs, and review its trade practices compliance programs.

Daewoo
Daewoo entered into an agreement with one company, Porter Crane, on the basis that it would be the exclusive dealer in Queensland for certain heavy machinery for the term of the agreement. The agreement was also entered into on the basis that it included an option to renew, and that it would be ongoing and long term.

Daewoo did not, however, intend to appoint Porter Crane as its exclusive Queensland dealer but in fact intended to appoint a national dealer whose territory would include Queensland. Daewoo did not inform Porter Crane of this before contracting.

Daewoo subsequently appointed Construction Equipment Australia (CEA) as its Queensland dealer and gave effect to this agreement, to the detriment of Porter Crane, by:

- Refusing to supply Porter Crane with machines, and instead supplying CEA;
- Supplying machines to CEA at lower prices than it supplied Porter Crane;
- Referring all sales leads to CEA instead of Porter Crane;
- Relying on the strict wording of the agreement with Porter Crane to refuse to extend or renew its agreement.

The court declared that Daewoo had engaged in unconscionable, misleading and deceptive conduct and granted injunctions preventing similar conduct in the future. The court ordered Daewoo and its director to undergo trade practices compliance training in the event that they resume trading in Australia.

Small business complaints and inquiries

	1999	2000	2001	2002	q1 2003
Complaints from a small business (i.e. search by field "is the caller a small business")	4081	7552	5425	7295	1771
Inquiries from a small business (i.e. search by field "is the caller a small business")	1557	14213	3198	2209	726
Total complaints and inquiries from a small business	5638	21765	8623	9504	2497
Small business complaints/inquiries as % of total received by ACCC	26%	16.4%	17.4%	19.2%	19.6%

Franchising

	1999	2000	2001	2002	q1 2003
Complaints from franchisees (search by 'is the business a franchise?'	1046	3029	815	951	238
Inquiries from franchisees (search by 'is the business a franchise?'	404	2065	485	514	114
Total franchising complaints and inquiries	1450	5094	1300	1465	352

Commercial unconscionable conduct

	1999	2000	2001	2002	q1 2003
Commercial unconscionable conduct complaints and inquiries (s51AA, AC and AD)	1008	1079	1122	1062	207

Small business complaints - years by conduct

1999

	Complaints	Inquiries	Total
Restrictive trade practices	1424	184	1608

Unconscionable conduct/franchising	572	184	756
Misleading conduct/representations	1205	217	1422
GST	284	569	853
miscellaneous	569	403	999

2000

	Complaints	**Inquiries**	**Total**
Restrictive trade practices	1275	171	1446
Unconscionable conduct/franchising	568	77	645
Misleading conduct/representations	1498	199	1697
GST	3164	13357	16521
miscellaneous	1047	409	1456

2001

	Complaints	**Inquiries**	**Total**
Restrictive trade practices	1213	421	1634
Unconscionable conduct/franchising	436	185	621
Misleading conduct/representations	2171	646	2817
GST	732	1028	1760
miscellaneous	873	918	1791

2002

	Complaints	**Inquiries**	**Total**
Restrictive trade practices	1844	205	2049
Unconscionable conduct/franchising	511	60	571
Misleading conduct/representations	3529	398	3927
GST	179	152	331
miscellaneous	1233	1394	2627

2003 (first quarter)

	Complaints	**Inquiries**	**Total**
Restrictive trade practices	500	52	552
Unconscionable conduct/franchising	103	23	126
Misleading conduct/representations	847	141	988
GST	29	14	43
miscellaneous	298	498	796

Attachment E

ACCC response to market issues

Industry liaison

The ACCC's primary means of securing compliance is to inform businesses of their rights and obligations under the TPA so that they can implement measures to ensure their business complies, and so that they can respond effectively if their rights have been compromised. Where problems connected with the TPA do arise, the ACCC will usually emphasise mediation as the first and best option. However, in cases where such resolution is not possible, it may be necessary to take legal action.

Such problems are often relatively isolated and are best dealt with on an individual basis; they are generally not indicative of a broader market failure. However, in some cases where problems appear to be systemic or representative of wider industry concerns, the ACCC will take a more broadly based approach to addressing these problems.

Retail Tenancy

The ACCC has received significant numbers of retail tenancy complaints, involving such issues lease re-renewal, rent negotiations, anti-competitive behaviour by landlords, misrepresentations, and casual leasing. One possible reason for these complaints is the relative lack of prominence and awareness of the existence of state retail tenancy agencies.

In 2001 the ACCC engaged Eileen Webb, a senior lecturer at the University of Western Australia with expertise in trade practices law and retail tenancy, to prepare a paper on the impact of retail tenancy issues and State laws on the TPA and the role of the ACCC.

The issues raised in the paper formed the basis for a 'round table' discussion convened by the ACCC. The meeting presented an opportunity for a number of key industry participants to raise a number of matters, and discuss the potential for a nationally consistent approach to addressing these issues.

In addition to those matters above, the interaction of retail tenancy issues with the Trade Practices Act, current state regulations and perceived advantages and disadvantages of the various types of Code options were discussed. Further detail of complaints received in relation to retail tenancy is at Attachment D.

Motor body repair industry

The ACCC has from time to time investigated alleged breaches of the *Trade Practices Act 1974 (the TPA)* in the motor body/smash repair industry. Due to the frequency and the variety of concerns raised, the ACCC decided to canvass the issues in the industry by convening a discussion involving a broad selection of participants within the industry.

The aim of these 'round table' discussions was to identify and examine the impact of certain issues in the industry. Many issues between repairers and insurers arise as a product of various structural changes in the industry, changes in the market for insurance products, improvements in technology and training and improvements in efficiency and quality.

Information and education

The ACCC Small Business, Rural and Regional Unit is primarily concerned to inform small businesses of their rights and obligations under the Trade Practices Act so they can respond effectively if they have been subjected to any misleading, anti-competitive, or unconscionable conduct.

The ACCC Small Business, Rural and Regional Program

The Small Business Unit, now known as the Small Business, Rural and Regional Program, was set up and permanently staffed in September 1996. Its objectives are to coordinate:

enforcement of the Trade Practices Act in relation to small business issues;
education of small business about rights and obligations under the Act; and
promotion of small business aspects of ACCC activities.

The ACCC has an important role in improving market conduct, enhancing competition and promoting fair trade. It achieves this through both education and, when necessary, enforcement.

Small Business Managers, appointed in each ACCC office, keep in regular contact with industry associations, Business Enterprise Centres, ethnic associations, local government and other relevant bodies through mailouts, articles in association newsletters and trade magazines and radio interviews. This work is supplemented by the ACCC Regional Network of supporters.

Quarterly Ministerial Report

The Small Business, Rural and Regional Unit conducts ongoing analysis of small business and franchising industry complaints and inquiries. This analysis has enabled the identification of trends where they have emerged, and also contributes to the quarterly report to the Small Business Minister.

ACCC publications

The ACCC has produced a number of guides for business specifically dealing with unconscionable conduct or industry codes. These include:

- News for business – commercial unconscionable conduct (Sept 2002)
- Unconscionable conduct brochure series (September 2001)
- Fair game or fair go? Avoiding and dealing with a hard bargain (June 1999)
- Guide to unconscionable conduct in business transactions (October 1998)
- The Franchisees guide (Nov 2001)
- The Franchising compliance manual (Jan 2002)

ACCC Videos

- Fair Game or Fair Go: Unconscionable Conduct in Business - March 2001 ($10)
- Competing Fairly Forum: Unconscionable Conduct in Business - May 2001 ($10)

The ACCC has also produced a number of more general guides to the Act that deal with unconscionable conduct, such as

- The Best & Fairest compliance training package (September 2002)
- Small Business and the Trade Practices Act (May 2002)
- ACCC Infolink (monthly)
- ACCC Briefing (quarterly newsletter)
- Retail Flash (bi-annual)

The ACCC also regularly convenes the Competing Fairly Forum (CUFF) which presents a panel of experts to present a number of topical trade practices issues.

External materials

The ACCC also places articles in a number of targeted industry publications, including Retail News, Retail Industry Gazette, and editorial content in various newspapers.