SPEED AND STRACEY
LAWYERS

Committee Secretary
Senate Economics Committee
Department of the Senate
P.O. Box 6100
Parliament House
Canberra ACT 2600

Dear Sir,

Inquiry into the Trade Practices Amendment (Cartel Conduct and Other Measures) Bill 2008

Speed and Stracey has, for over 30 years, been advising on and involved in litigation concerning the operation and ambit of the existing sections 4D, 45 and 45A of the *Trade Practices Act 1974.* In March 2008 we made a detailed submission to Treasury in relation to the exposure draft of the current Bill before Parliament - relating to the proposed imposition of criminal sanctions and civil penalties for cartel conduct. We have now had the opportunity of reviewing the current Bill.

Whilst the Bill does address a number of the issues that we raised in our submission in March 2008 and by others in submissions lodged at that time, most notably the inclusion of anti-overlap provisions and the partial removal of an effects test, we remain concerned that the Bill defines cartel conduct too broadly such as to still catch innocuous every day commercial transactions. Further we are concerned that the Bill still fails to adequately distinguish between cartel conduct which attracts a civil penalty and that which attracts criminal sanctions.

Too Broad

By way of examples, in our opinion, the current Bill catches (or arguably catches) and subjects to serious criminal sanctions the following innocuous and insignificant every day commercial transactions:

1. Two doctors in a country town agreeing that they will restrict the services they provide – with one to work on Saturdays and the other on Sundays (rather than both being permanently on call).

2. A leading distributor of brand X product and the market leading retailer of that product agreeing to the price at which the distributor is to supply that product to the retailer - in circumstances where:

    a) it is likely that the effect of this agreement is to set a benchmark above which the price of that product will be maintained in the wholesale market generally including by that distributor to other retailers; and

b) but for the agreement on price, it is likely that the market leading retailer would itself have sought to set up or acquire, perhaps through a subsidiary, a distributor supplying that product to itself and others.

3. Two bakeries agreeing to one supplying croissants to the other– in circumstances where otherwise, but for the agreement reached, that other bakery would incur the capital cost of buying a bigger oven and produce its own croissants.

4. A franchisor allocating a specific geographic territory to a franchisee and agreeing not to itself open a franchise within that geographic territory nor allocate that territory to other franchisees in return for the franchisee agreeing not to operate outside its allocated geographic area.

5. A manufacturer and distributor allocating to a distributor a specific geographic territory (or customers) and agreeing not to itself distribute within that geographic territory (or to those customers) in return for the distributor agreeing only to distribute in that area.

6. Two competing coal miners entering into a joint venture to develop a coal mine. Pursuant to and in furtherance of this joint venture they establish management committees comprising representatives of each competitor to agree on the operational aspects of the joint-venture. The committee members subsequently agree to the prices for which the coal produced by the mine is to be sold.

In the attached schedule we detail why each of the above examples is caught or arguably caught by the proposed provisions under the current Bill and why none of the proposed defences/exemptions apply.

We do not consider that the above list is, nor is it intended to be, exhaustive of the various innocuous and insignificant every day commercial transactions that would still be caught or arguably would still be caught by the wide proposed cartel provisions contained in the current Bill.

Given the wide drafting of the Bill and the infinite variety of commercial transactions that may take place in the Australian economy we do not believe it is possible to, but rather believe it futile to attempt to, list each and every innocuous commercial transaction that would still be caught by the Bill in its current form.

The approach adopted in the Bill of defining the proposed offences broadly and then seeking to limit the ambit of those offences by including specific defences is, in our opinion, inappropriate given that the variety of commercial transactions that might be caught by the wide proposed provisions cannot adequately be foreseen and consequently sufficient specific defences cannot be adequately drafted in advance. Rather, in accordance with good legislative practice, we believe that the proposed definition of a cartel contained in the Bill should itself be more limited so as to only catch cartel/collusive conduct which is, by that definition, clearly and necessarily offensive.

In our opinion the proposed offences could and should be drafted far more concisely than the current proposed provisions such as to catch offensive cartels such as the Visy and Amcor price fixing and market sharing cartel, and yet not catch conduct which is innocuous– without the need for the current extensive, yet deficient, list of defences and exemptions. Ideally this would involve a significant tightening of each element of what is required to constitute a "cartel provision".

We note that a key necessary attribute of the Visy/Amcor example (which makes it offensive) was the two parties, ostensibly competitors, conspiring with the intention of dishonestly obtaining a gain from third parties (suppliers and customers alike) – a conspiracy to defraud. An alternative, to

tightening each element of what is required to constitute a "cartel provision", might then be to require (in addition to that which is required in the current proposed provisions) the ACCC and crown prosecutor, in the context of criminal proceedings, to prove conduct that is dishonest and, in the context of civil proceedings, to prove conduct that is substantially anti-competitive. Certainly this would be more difficult for the ACCC and crown prosecutor to do than simply ticking each of the boxes of the current wide proposed provisions. That said, with the substantial existing investigative powers, capabilities and resources of the ACCC (which are to be substantially enhanced by the Bill to include phone tapping), we rhetorically ask:

1. Why should someone go to jail for cartel conduct (which given the above examples could be quite innocuous) unless the DPP is able to establish beyond reasonable doubt that person acted dishonestly for personal gain?

2. Why should someone be obliged to pay a significant civil penalty in respect of cartel conduct (which given the above examples could be quite innocuous) unless the ACCC is able to establish on the balance of probabilities that conduct had the purpose or effect of substantially lessened competition?

3. Why is the Australian business community not entitled to a presumption of innocence unless and until proven guilty of each of the elements of conduct which are necessary to make that conduct offensive?

ACCC discretion

A foreseeable consequence of the proposed provisions being drafted too widely is that the ACCC will be forced to exercise its own discretion to decide which conduct, that technically infringes the proposed provisions, does not warrant prosecution, which conduct is more serious and warrants the imposition of civil penalties and which conduct is very serious and warrants criminal prosecution. In our opinion, however, such a result is most unsatisfactory.

By leaving the ACCC such a wide discretion the laws enacted by Parliament will lack certainty and the capacity to guide commercial conduct - at least until the ACCC first "rules" retrospectively on types of conduct. As one competition commentator recently said:

> "*Something is needed to send up the red flag so people know what the rules of the game are, rather than just leaving it to the ACCC to say we will go civil or criminal* [or at all]".

There is a real risk, that pending the ACCC "ruling" on particular conduct, business people in Australia will take an overly conservative position (given the risk of conviction as well as jail time) and not engage in normal and worthwhile commercial conduct. This is of particular concern to Australians given the current commercial climate. Further, with the constant prospect of a change in personnel or attitude at the ACCC, past "rulings" will likely afford little comfort to the business community in any event.

The ACCC also ought not to be burdened with determining retrospectively on a case-by-case basis what conduct is permissible, what conduct bears a civil penalty and what conduct deserves criminal sanctions. Rather the Parliament, and not the ACCC, was popularly elected to determine these questions and to do so prospectively – such is the doctrine of the Rule of Law.

Further it cannot be assumed that the ACCC is, and at all times in the future will be, intuitively and objectively capable of determining on a case-by-case basis which conduct is offensive and which conduct is not and when to prosecute and when not to prosecute. For example in the past, in relation to medical practitioners rostering (example 1 above) - in applying the existing section 4D (which does not require proof of a substantial lessening competition) - the ACCC was heavily

criticised for *"making a mess of it in health"* by massively overreacting to *"relatively minor behaviour by doctors"* in reaching agreement between themselves as to a roster *"to get a night off"*. Dr Kerryn Phelps, then President of the Australian Medical Association, claimed that, by its heavy-handed approach, *"the ACCC has effectively put an end to after-hours anaesthesia services in the private sector in Australia, hindered the supply of VMO services to public hospitals, hindered the supply of rural GP medical services, and is in the process of significantly reducing the supply of rural obstetric services"*.

It should also not be assumed that the ACCC will always make that decision, which would be unchecked by the judiciary, in a balanced and unbiased way, beyond corruption and without pre-judgment. In the past the ACCC has been heavily criticised at times for being overly zealous. For example in 2002 again Dr Kerryn Phelps, then President of the Australian Medical Association, savagely criticised the ACCC, in relation to doctor's rosters (again example 1 above), for engaging *"bovver boy antics"* and being *"a zealot who takes great pleasure in sneaking up behind medical practitioners and whalloping them with a big stick"*. In 2003 the Dawson Committee said the ACCC's use of the media was "*one of the issues most frequently raised with the Committee*". "*The common theme underlying these complaints was that the manner in which the ACCC released information and made comments to the media was neither balanced nor impartial and carried with it the danger that the Corporation or individual involved might be denied procedural fairness in proceedings yet to be determined. In short, the suggestion was the ACCC engaged in trial by media.*"

In the future, with a change in personnel or attitude, perhaps as a result of pressures to get "good press", to get "good results", to generate "wins" and to cut costs, it is inevitable that the ACCC's ability to justly and fairly make decisions - as to what conduct is inoffensive, what conduct justifies a civil penalty and what conduct deserves a criminal sanction - will be compromised. Rather than putting the ACCC in this impossible position of being the investigator, prosecutor and judge the Parliament should itself decide, and concisely prescribe, which conduct, of that which technically infringes the current proposed provisions, does not warrant prosecution, which conduct is more serious and warrants the imposition of civil penalties and which conduct is very serious and warrants criminal prosecution.

The ACCC's draft memorandum of understanding with the Commonwealth Director of Public Prosecutions (DPP) to the effect that it "*will not ordinarily refer relatively minor cartel conduct to the DPP for consideration for prosecution*" and that "*referral of possible serious cartel conduct will concentrate upon conduct of the type that can cause large-scale or serious economic harm*" is of no real comfort. First this is because the references to *"ordinarily"*, *"relatively minor"*, *"possible"*, *"that can cause"* etc are vague and do not confine the ACCC. Second the accused will have no right to judicial review of the ACCC's decision in this respect. Nor, for instance, will the accused be able to seek the assistance of a specialised ombudsman, like the Inspector-General of Taxation, responsible for overseeing the ACCC. In short nobody will be watching the watchdog.

If, for instance, the ACCC forms the erroneous belief, based on its own investigations (which are likely to be confidential and never disclosed to the affected party) that relevant business conduct, which in fact is innocuous, has some substantial effect on competition then companies and individuals are likely to be defending criminal proceedings without the opportunity of ever challenging the ACCC's assessment of the impact its conduct on competition. As the issue of whether or not the conduct was of such a serious nature as to cause large-scale or serious economic harm (ie substantially lessen competition) is not intended to be an element of the proposed offences (just a feature of the memorandum), under the proposed provisions it will then not be an issue which a judge or jury will ever have the opportunity of reviewing (except, and only perhaps, in relation to the length of jail term or severity of a penalty). So much for natural justice.

Whether corporations face the stigma of being found guilty of having committed a criminal offence and whether employees, senior managers and directors involved in the relevant conduct face very substantial civil penalties and jail terms should not be left to the whim of the ACCC nor to guidelines which are vague and in any event cannot be tested. Rather than abdicating its legislative responsibilities Parliament should itself determine (and legislatively prescribe in concise terms (and not by the current proposed wide terms) what conduct warrants the imposition of civil penalties and what conduct warrants criminal sanction.

Criminal vs Civil

The philosophical reason for imposing criminal sanctions in relation to cartel conduct is significantly different to the philosophical reason for introducing civil penalties. Criminal sanctions are imposed to redress morally reprehensible conduct - "hard-core cartel conduct" which involves suppliers, customers and the public being defrauded. Civil penalties are imposed to redress and prevent there being a substantial lessening of competition in the market – even if the conduct causing that lessening of competition is not morally reprehensible/dishonest.

Consistent with this, in our view the proposed criminal cartel provisions should be distinct from and drafted differently to the proposed civil cartel provisions - which, unlike the criminal provisions, will be tried before a judge alone and not a jury. While the two sets of provisions are likely to be the same in a number of respects the criminal offences should require proof of conduct that is, by the definition adopted in the proposed offence, clearly morally reprehensible/ dishonest and thus worthy of criminal sanction. The civil penalty provisions should instead require proof of conduct that is, by the definition adopted in the proposed provision, clearly and substantially anti-competitive.

By so distinguishing between the two sets of provisions the legislature will avoid the issues recently raised in the press concerning the risk of the ACCC using the threat of criminal sanctions to convince executives accused of involvement in illegal cartels to plead down to civil charges (whether guilty or not). Further, such a distinction, will render the willingness of the ACCC to try alleged cartel participants twice – bringing civil charges if a criminal trial fails- somewhat moot. It will not then be the case of the ACCC having the ability nor having the obligation, when it is unhappy with the umpire's decision, of having a second bite of the same cherry.

Summary

In our view the Bill should be amended to ensure that the proposed provisions do not catch innocuous and insignificant every day commercial transactions. Ideally this would be done through more concise drafting and a significant tightening of each element of what is required to constitute a "cartel provision" – with the result that the criminal sanctions are directed to addressing conduct that clearly is morally reprehensible/dishonest conduct and the civil penalties are directed to addressing conduct that substantially lessens competition. It is most unsatisfactory, by drafting the proposed offences too widely, to give by default the ACCC the retrospective discretion of determining what conduct is offensive and what is not and what should be prosecuted and what should not be prosecuted.

Dated: 20 January 2009

Speed and Stracey Lawyers Pty Ltd

SCHEDULE 1

Example 1

In our opinion, the current Bill catches (or arguably catches) and subjects to serious criminal sanctions and significant civil penalties:

> *Two doctors in incorporated practice in a country town agreeing that they will restrict the services they provide – with one to work on Saturdays and the other on Sundays (rather than both being permanently on call).*

This is because pursuant to the Bill: s44ZZRF – criminal,s44ZZRJ- civil and s44ZZRD

(1) A corporation commits an offence [contravenes this section] if:
  (a) the corporation makes a contract or arrangement, or arrives at an understanding; and
  (b) the contract, arrangement or understanding contains … a provision …[which]

(3) ….. has the purpose of directly or indirectly:
  (a) preventing, restricting or limiting: …
    (iii) the supply, or likely supply, of goods or services to persons or classes of persons by any or all of the parties to the contract, arrangement or understanding; …[and]

(4) …..at least 2 of the parties to the contract, arrangement or understanding:
  (a) are or are likely to be; or
  (b) but for any contract, arrangement or understanding, would be or would be likely to be;
 in competition with each other in relation to: …
  (h) …. —the supply of those goods or services; …

The proposed Bill will catch this example of the two doctors notwithstanding the note to the proposed sections that:

> Note 1: For example, subparagraph (3)(a)(iii) will not apply in relation to a roster for the supply of after-hours medical services if the roster does not prevent, restrict or limit the supply of services.

This is because, but for the contract, arrangement, or understanding, it is assumed the two medical practitioners would be on call seven days a week - leading to the conclusion that the contract arrangement or understanding (Saturday/Sunday roster) does indeed prevent, restrict or limit the supply of services by a one or both of those practitioners and has that very purpose.

Example 2

In our opinion, the current Bill also catches (or arguably catches) and subjects to serious criminal sanctions and significant civil penalties:

> *A leading distributor of brand X product and the market leading retailer of that product agreeing to the price at which the distributor is to supply that product to the retailer - in circumstances where:*

- *it is likely that the effect of this agreement is to set a benchmark above which the price of that product will be maintained in the wholesale market generally including by that distributor to other retailers; and*

- *but for the agreement on price, it is likely that the market leading retailer would itself have sought to set up or acquire, perhaps through a subsidiary, a distributor supplying that product to itself and others.*

This is because pursuant to the Bill: s44ZZRF – criminal,s44ZZRJ- civil and s44ZZRD

(1) A corporation commits an offence [contravenes this section] if:
  (a) the corporation makes a contract or arrangement, or arrives at an understanding; and
  (b) the contract, arrangement or understanding contains a ...provision [which]

(2) .... has or is likely to have the effect, of directly or indirectly:
  (a) fixing, controlling or maintaining; or
  (b) providing for the fixing, controlling or maintaining of;
 the price for....
  (c) goods ... supplied, or likely to be supplied, by any or all of the parties to the contract, arrangement or understanding; or
  (d) goods .... acquired, or likely to be acquired, by any or all of the parties to the contract, arrangement or understanding; .... [and]

(4) ... at least 2 of the parties to the contract, arrangement or understanding:
  (a) are or are likely to be; or
  (b) but for any contract, arrangement or understanding, would be or would be likely to be;
 in competition with each other in relation to:
  (c) if paragraph (2)(c) ... applies in relation to a supply, or likely supply, of goods or services—the supply of those goods or services; or
  (d) if paragraph (2)(d) ... applies in relation to an acquisition, or likely acquisition, of goods or services—the acquisition of those goods or services; ....

The proposed provisions catch this example because they contain an "effects test". This is notwithstanding that such price leadership may be pro-competitive rather than anti-competitive – and certainly is not sinister. The additional requirement for a criminal offence, that the corporation has "knowledge or belief" in the purpose or likely effect of the relevant provision provides little comfort as the leading distributor and leading retailer may well be aware that the prices they negotiate are likely to set the industry benchmark. Such knowledge should not expose them to potential jail time.

Example 3

In our opinion, the current Bill also catches (or arguably catches) and subjects to serious criminal sanctions and significant civil penalties:

Two bakeries agreeing to one supplying croissants to the other– in circumstances where otherwise, but for the agreement reached, that other bakery would incur the capital cost of buying a bigger oven and produce its own croissants.

This is because pursuant to the Bill: s44ZZRF – criminal,s44ZZRJ- civil and s44ZZRD

(1) A corporation commits an offence [contravenes this section] if:
  (a) the corporation makes a contract or arrangement, or arrives at an understanding; and
  (b) the contract, arrangement or understanding contains ... a provision ...[which]

(3) .... has the purpose of directly or indirectly:
  (a) preventing, restricting or limiting:

(i) the production, or likely production, of goods by any or all of the parties to the contract, arrangement or understanding; .... [and]

(4) .... at least 2 of the parties to the contract, arrangement or understanding:

(a) are or are likely to be; or

(b) but for any contract, arrangement or understanding, would be or would be likely to be;

in competition with each other in relation to: ...

(f) .... —the production of those goods; ...

In terms of the proposed civil penalty provision it would not even matter whether the supplying baker knew about the needs of its competitors for a bigger oven. As the Full Federal Court said in *ASX Operations Pty Ltd v Pont Data Australia Pty Ltd* (1990) 27 FCR 460 the purpose of a provision can be offensive where only one of the alleged parties subjectively has that purpose. So long as one party has the relevant purpose and pursuant to section 4F of the Act that purpose was "a substantial purpose" then both parties may be liable.

The proposed criminal cartel provisions do require the supplying baker to have "knowledge or belief" of the other party's purpose. In this example, however, knowledge or belief of such an innocuous purposes should not result in substantial penalties nor jail time for either party.

Examples 4 & 5

In our opinion, the current Bill also catches (or arguably catches) and subjects to serious criminal sanctions and significant civil penalties:

A franchisor allocating a specific geographic territory to a franchisee and agreeing not to itself open a franchise within that geographic territory nor allocate that territory to other franchisees in return for the franchisee agreeing not to operate outside its allocated geographic area.

A manufacturer and distributor allocating to a distributor a specific geographic territory (or customers) and agreeing not to itself distribute within that geographic territory (or to those customers) in return for the distributor agreeing only to distribute in that area.

This is because pursuant to the Bill: s44ZZRF – criminal,s44ZZRJ- civil and s44ZZRD

(1) A corporation commits an offence [contravenes this section] if:

(a) the corporation makes a contract or arrangement, or arrives at an understanding; and

(b) the contract, arrangement or understanding contains ... a provision ...[which]

(3) .... has the purpose of directly or indirectly:

(b) allocating between any or all of the parties to the contract, arrangement or understanding:

(i) the persons or classes of persons who have acquired, or who are likely to acquire, goods or services from any or all of the parties to the contract, arrangement or understanding; or

(ii) the persons or classes of persons who have supplied, or who are likely to supply, goods or services to any or all of the parties to the contract, arrangement or understanding; or

(iii) the geographical areas in which goods or services are supplied, or likely to be supplied, by any or all of the parties to the contract, arrangement or understanding; or

(iv) the geographical areas in which goods or services are acquired, or likely to be acquired, by any or all of the parties to the contract, arrangement or understanding; ..[and]

(4) .... at least 2 of the parties to the contract, arrangement or understanding:

(a) are or are likely to be; or

(b) but for any contract, arrangement or understanding, would be or would be likely to be;

in competition with each other in relation to:

(c) if paragraph … (3)(b) applies in relation to a supply, or likely supply, of goods or services—the supply of those goods or services; or

(d) if paragraph … (3)(b) applies in relation to an acquisition, or likely acquisition, of goods or services—the acquisition of those goods or services; …

In relation to the fourth example arguably the franchisee (being an acquirer of the franchisor's services) will be protected by the new anti-overlap provision(section 44ZRS) in relation to the restriction imposed on the franchisor not to supply its services to competing franchisees in a particular place (s47(4)). It, however, will not be protected, particularly given the words in the defence "in so far as", in relation to the restriction on the franchisor not to itself operate a franchise in the area. Nor do the anti-overlap provisions protect the franchisor since the supply of its services on the condition the franchisee sticks to its designated area and not compete outside that area is not a condition restricting "resupply" of goods of services but the supply of good or services. That is to say that the later restriction on the franchisee would not otherwise constitute a contravention of section 47 and therefore would not be covered by the proposed section 44ZRS defence.

Similar problems exist with the fifth example.

The difficulties with the existing anti-overlap provisions, which are now mirrored in the Bill, became evident in the much criticised case of *Visy Paper Pty Ltd v ACCC* (2003) 201 ALR 414 wherein it was found, depending on how one characterised the same conduct, it was or was not protected by those anti-overlap provisions.

As Professor Pengilley said, in an article he published in relation to that case, "*sadly, however for Visy a perusal of the 14 subsections, 40 sub-subsections and 10 subsections of subsections of statutory verbiage which make up s47 fails to reveal any provision in that section covering acquisitions of goods or services on the condition that the supplier will not acquire goods or services from another person.*"

Example 6

In our opinion, the current Bill also catches (or arguably catches) and subjects to serious criminal sanctions and significant civil penalties:

Two competing coal miners entering into a joint venture to develop a coal mine. Pursuant to and in furtherance of this joint venture they establish management committees comprising representatives of each competitor to agree on the operational aspects of the joint-venture. The committee members subsequently agree to the prices for which the coal produced by the mine is to be sold.

This is because the proposed joint venture defence only applies to a "contract" containing a cartel provision and not arrangements or understandings containing cartel provisions. In this example it is arguable that the conduct of competitors acting jointly in a committee to set their joint venture's own prices does not involve the making or giving effect to a cartel provision in a "contract" rather it involves the making or giving effect to a cartel provision of an arrangement or understanding.

Note: The definition of a joint venture in section 4 J is arguably not wide enough, in any event, to cover a joint-venture undertaken through a trust structure rather than through a company or by a partnership.