REVIEW OF THE COMPETITION PROVISIONS OF THE TRADE PRACTICES ACT 1974

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BY ALAN MORAN & JIM HOGGETT

Institute of
Public Affairs Ltd
Lvl 2, 410 Collins Street
Melbourne Vic 3000
Tel: (03) 9600 4744
Fax: (03) 9602 4989
Website: www.ipa.org.au

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1. GENERAL

The regulation of competition in Australia has become too intrusive and heavy handed.

The regulation of economic activity is the restriction of freedom to conduct private affairs. That such regulation is sometimes necessary should not cause us to ignore the principle of preserving and expanding that freedom wherever possible. State intervention in private matters ought always to be a last resort.

It is an unfortunate feature of regulation that it tends to grow by steps under the pressure of politics and there is no countervailing force which automatically dismantles it when it is no longer required. For example, Part IV is not the last word on competition regulation. There is other industry specific legislation that regulates competition such as the Broadcasting Act. The TPA also has provisions in Part IIIA and Parts XIB and XIC. The latter are used to virtually determine all key telecommunications prices and regulate many activities.

In addition, there is an automatic tendency for regulators to accumulate power by the exercise of an effective veto on transactions through information gathering processes or administrative delay. This will be reinforced by any propensity of the regulator to be heavy handed with the powers conferred. This has been the case with the regulation of competition, where the accumulation of powers and responsibilities conferred on the ACCC is now having a counter-productive effect on the efficient operations of the economy.

As with any body whose powers are wide ranging and subject to little constraint, the ACCC is abusing its position. This is most graphically seen in its stage-managed raids on oil company premises and the manufactured footage of ACCC officials poring over documents they allegedly seized. The activity itself falls well short of the standards of truthfulness and the avoidance of deception required by the Trade Practices Act which is the ACCC's governing legislation.

The ACCC has not gone without criticism from the courts. Thus, in passing judgement in *ESAA vs ACCC* on the question of power surges, the court found the Chairman of the ACCC was setting a poor example in truthfulness and inappropriately threatening those who opposed his views with civil and criminal proceedings[1].

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[1] The relevant comments of, the Judge, Justice Finn are:
"139 There are two matters to which it is necessary to draw attention. Both relate to the manner in which the ACCC conducted itself in its dispute with ESAA and the electricity suppliers. The first is simply a matter for comment. In his evidence Professor Fels indicated on a number of occasions that, in light of the issues that have achieved prominence in this proceeding, he would have been more careful in what he said in press releases and comments to the media. He took the view that in a media release it has to be "really simple". I do not wish to question the use of the media made by the ACCC in

All this is within a context of growing business regulation generally. The appropriateness of regulation and the burden it imposes on the business is rarely measured. It is a significant restraint on the flexibility and creativeness of the Australian economy.

We believe it is time to liberalise and that the competition provisions of the TPA are a good place to start. It follows that we do not think that it is a good time to make the provisions even more restrictive.

2. THE INTERNATIONAL DIMENSION

Competition policy should also take account of changes in the characteristics of the Australian economy.

The Australian economy has always been a trading nation, though our economy has not matched the openness of some equivalent sized economies in Europe and Asia. Through the early Post-War period, total imports and exports of goods and services were the equivalent of about 30 per cent of domestic production.

In the 1970s this ratio grew somewhat to about 35 percent but then stabilised in the 1980s before starting to climb again in the 1990s. This trend seems to have accelerated in the latter part of the 1990s and the ratio of traded goods and services to domestic production is now almost 43 per cent. We believe that this trend will continue because it is part of a global change and because Australian consumers have a strong propensity to travel and to purchase foreign goods.

Self evidently, there is also a much greater diversity in the goods and services traded. Rural and other primary exports have declined relatively and services trade has become more important. Flows of investment both to and from Australia have multiplied the points of contact with the major global and regional economies and the potential for new sources of supply.

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publicising its views. I would merely suggest that, as the agency responsible for policing s52 of the TP Act, it properly can be expected to set the example of care in its own representations to the public.

“140 Secondly, Professor Fels has not been reluctant to question in public forums the legal advice of those Queens Counsel who advised ESAA or its members. As I earlier noted, he characterised as "absurd" the view that Division 2 of Part V might not apply to the supply of electricity. And he has not been slow to raise the threat of civil and criminal proceedings under the TP Act against electricity suppliers who publicise or who might be minded to publicise views about the implied warranties that differ from the Commission's view. I refer by way of example to the ACCC's letter of 1 May 1997 which has been reproduced in part earlier in these reasons at [35].

“141 The stances so taken may constitute good public theatre. Whether they represent good public administration is another matter. There is a very real prospect that the view the ACCC has taken of Division 2 of Part V will be found to be incorrect. At the moment, as the ACCC's counsel in this proceeding properly acknowledges, whether and if so how the implied conditions apply to electricity supply contracts is a matter of debate about which there can be respectable opinions on both sides of the argument. To describe the opinions supporting one side of the debate as "absurd" borders on the mischievous.”

The Government has reinforced the trend by reducing protective barriers against foreign goods and services, eliminating controls on inward and outward investment and dismantling moribund public sector monopolies.

A greater cultural openness and diversity has, of course, accompanied the growth in trade.

This tendency towards greater openness in the Australian economy does not imply full integration in the regional or global economy. Nor does it dispose of the threat of anti-competitive conduct. However it does widen the range and power of the countervailing forces to anti-competitive conduct. There would have been no serious competition in telecommunications without a very aggressive entry of very large foreign companies. The opportunities for cosy cartels in motor vehicle manufacture and textiles, and clothing and footwear, would be much more extensive without the lowering of tariffs.

Over the life of the TPA there has been a significant shift in the exposure of local producers to overseas competition.

3. WHAT TO CHANGE

Provisions in the Act

The two provisions of the TPA which are required to be changes, are Section 46 on misuse of market power and Section 50 on acquisitions.

Both of these sections are made quite restrictive by virtue of the definition of a "market". In practice, the ACCC and the courts have taken a view of what is a market that embraces quite tiny segments of our already small national market. Our national regulator has applied the full legal apparatus to numerous competition disputes in small local or industry segments of national markets.

The accumulation of precedent for the definition of market makes it difficult to redefine it in the Act to apply to the more significant cases of anti-competitive conduct that we think ought to be the work of a national regulator. We suggest that the Review consider whether anything could be done in this respect to make the provisions less onerous, but a more practical solution might be to restrict the attention of the regulator to those parties that are a threat to competition.

A return to the concept of market dominance is appropriate in both sections.

In Section 46, the reference could be to "A corporation that is dominant in a market" rather than one which has a substantial degree of power". In Section 50, the effect would have to be to "creating a position of dominance in a market" rather than "substantially lessening competition".

In this case the anti-competitive strictures would be confined to situations involving the exercise of power by a dominant firm or the creation of such a firm.

The term "substantial lessening of competition" is meant to exclude trivial anti-competitive effects but defining an excessive number of markets has led to the inclusion of substantial effects in trivial markets, which is much the same thing.

We would add that the prohibition on the exercise of power in a small market segment does not seem to warrant the intervention of the Government. Nor will the creation of a dominant firm of itself necessarily either reduce competition or remain a permanent state of affairs. Nevertheless, the proposed change would restrict the regulation more closely to the cases that matter.

We would also recommend that the "likely effect" test be removed from Section 50.

This formulation is vague, subjective and speculative. The section already invites the regulator and the courts into the area of assessing an uncertain, future competitive effect. The terms "would", "substantially" and "market" give the regulator and the courts plenty of scope to reject any significant anti-competitive acquisitions. "Likely effect" is a formulation that invites much wider and less certain speculation and allows much more scope for the acceptance of unsupported opinion. The tendency is magnified because the "effect" is indefinite as to future time.

Because it is the nature of many acquisitions that they must be accomplished with dispatch, the Section can easily create substantial delay, which quickly becomes effective prohibition. Removing this additional uncertainty in the application of the Section would create a more flexible and competitive market in business acquisitions.

Policing of anti-competitive behaviour by unions

Industrial relations and trade practices have traditionally been separated. Expression to the dividing line is given under section 45 of the Trade Practices Act. Section 45DD says that if conduct relates to employment matters, a person's activity is not deemed to fall under the illegal secondary boycotting provisions covered in sections 45D (substantial loss or damage), 45DA (substantial lessening of competition), and 45DB (boycotts affecting trade and commerce).

Section 45DD defines where boycotts are permitted. This turns on definitions of industrial action. In particular, it is a defence under section 45DD(7)(b) if the defendant proves that the dominant purpose "was to preserve or further a business carried on by him or her." It is unclear to us whether the defences severely limit the scope of the ACCC to take action against action that goes beyond strike activity into boycotts involving, for example, aggressive picketing to prevent goods entering or leaving premises. If they do, the defences should be removed.

The distinction between (legitimate) action in pursuit of an industrial relations campaign *for* the supply of labour, and (proscribed) action in the supply *of* goods and services, is becoming less clear. This is because of the growth in contracting. Those

workers who are engaged in activities under some form of contract, or are self employed, now account for 28 per cent of the private sector workforce, a far higher share of the private sector workforce than the 16 per cent that is unionised[2].

Yet boycott action to preserve employment is almost invariably at the expense of workers who wish to offer services to the supplier. As the latters' services are likely to be cheaper, allowing the boycotts will mean more expensive goods and services. Indeed, under section 275 of its Industrial Relations Act, the Queensland Government has given the Industrial Relations Commission the power to declare a contract for services as employment. This seems to trespass on contracts that were outside of the purview of the industrial relations courts. In doing so, it will reduce the flexibility within the economy and increase costs.

By contrast, the ACCC has rarely ventured into areas that industrial relations practitioners might claim as within their preserve. Yet, as illustrated by industrial action and boycotts by unions supporting their preferred scheme for funding workers entitlements (Manusafe) and resisting the use of contractors for maintenance, these actions are damaging both to the economy as a whole and to particular supplyers and customers. The boycott measures are designed to prevent firms from selecting the inputs into their production processes that they consider to be least costly.

The ACCC should be energised to pursue trade practices contraventions involving union activity and, if necessary, changes to the Act should be introduced to facilitate this.

Administrative arrangements

We are conscious that the powers and responsibilities of the ACCC are far more comprehensive than those of its counterparts in the US and UK.

A critical issue in assessing mergers is the definition of the proposed merged businesses' markets. This entails examining a wide variety of complex issues including the product, functional, time and geographic dimensions of the market. In addressing the time dimension, the ACCC must consider complex issues such as technological, and supply and demand changes. All this must be done rapidly in view of the urgency of merger proposals that have a time-limited banking dimension, and other constraints.

The case for regulating monopoly rests on the ability of the monopolist to raise price above the levels that would prevail in a competitive market. There is a social loss as a result, because the net cost of the production foregone is less than the net value consumers place on it.

But determining when this is taking place presents difficult issues in economic analysis. Estimating marginal cost is one; the necessity to charge above it to cover fixed costs, and accommodate joint costs, comprise a raft of others. In addition, the actual market place is seldom in a static state, and major opportunities for profit are

[2] See http://www.ipa.org.au/pubs/workreform/numbers.html

constantly presenting themselves. These opportunities drive entrepreneurial activity, and in themselves represent situations where prices are considerably above marginal costs.

Regulatory measures to forestall price increases in markets may also detract from efficiency. Where two firms are engaged in cut-throat competition, the outcome will often be that one is driven out of business or exits the particular market segment. A merger of two such firms can avoid this outcome and restore normal profits in a less socially wasteful manner.

Accordingly, it is incorrect to oppose a rationalisation of two business entities on the grounds that this might bring increased prices. If lower prices are merely the result of a continued existence of surplus labour and capital forcibly retained within a production facility, improved resource allocation can be brought about by their shift to other activities.

There is a further reason why measures to prevent mergers may be unwise. This turns on "principal/agent" problems in modern firms, where the owners are not the managers. Such a divorce can lead to conditions outlined by Berle and Means[3] 70 years ago (and accounts for Adam Smith's hostility to the joint stock company). Professional managers may prefer the quiet life or fail to pursue the opportunities for efficiency with the same zeal of those whose stake is the residual income of the firm, its profits. Under such circumstances, the firm becomes vulnerable to takeover, either because its share price falls or because rivals spot an opportunity to use the assets more efficiently. Takeovers are a major discipline on firms' managements, not least because they make the incumbents vulnerable to early dismissal. Hence, inhibiting takeovers can foster inefficiency.

These matters call for economics expertise which is outside the ACCC's core skills. The absence of this has contributed to some poor decisions that the ACCC has made.

One example of these concerns the merger between Westpac and the Bank of Melbourne. In its examination of the proposed merger, the ACCC addressed six features of the banking market: deposits, home loans, personal loans, small business banking, credit cards, and transaction accounts. Each of these market segments was addressed from the ACCC perspective of whether the segment was a state or national market.

In terms of overall matters, the existence of four major banks and a great number of smaller entities competing in the various segments should have been assurance enough of continued robust competitive conditions, as the Bank of Melbourne's market share was less than 2%. However, in different segments, especially on a State basis, that share would be much more significant.

By considering the market as State based, ACCC managed to define two of the six segments as crossing its threshold. Thus, although the two entities each only had 9%

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[3] Berle, A., and Means, G., *The Modern Corporation and Private Property*, MacMillan, New York, 1932.

of the Victorian deposit market, this was sufficient to cause "concern". Similarly, although the merged entity had only 20% of the Victorian transaction accounts, "concern" was again triggered.

Yet the markets for financial services were progressively being integrated. Banks, building societies, and other financial intermediaries were increasingly "poaching" on territory that was previously protected. These developments have continued with increased competition from food stores with EFTPOS and other financial services, the Post Office, and direct dealings in savings and deposits over the internet.

Rather than seeking to graft a new economics layer onto the ACCC's legal skills, we recommend a divestment of some of the ACCC's present powers so that initial proposals for mergers are filtered through an alternative body. The Commonwealth's prime adviser on micro-economic matters, the Productivity Commission, would seem to be best capable of taking on that role.

Although primarily an advisory body, the PC already has some regulatory functions[4].

The proposed change would need some coordination between the agencies, but no more so than is presently required within the ACCC between its initial filtering personnel and those that subsequently are required to develop legal approaches and liaise with legal advisers and officials in other agencies in order to actuate the initial advice.

There are several options as to the extent of the shift of responsibilities, the proposal would entail. The first is simply to allocate the determination of the market definition to the Productivity Commission. This would have the merits of providing to the Productivity Commission a range of work in which they are most expert.

Giving the function to the PC would allow some dedicated personnel to be assembled and to develop real expertise on the matter. It would also be possible for the resources to define in advance certain markets, targeting those that are more likely to see takeover activity, or where the notion of what constitutes a market is more controversial. All this would tend to improve the information base of business and give greater certainty in allowing firms to develop corporate strategies.

It is probably unwise to leave the definition of the market as a stand-alone task for the Productivity Commission. Market definition, and whether or not a particular company is "dominant", or the merger would result in substantial lessening of competition, particular companies and the market within which they operate are closely linked. This was clearly understood by the High Court which determined in the original *Queensland Wire* case:

In identifying the relevant market, it must be borne in mind that the object is to discover the degree of the defendant's market power. Defining the market and evaluating the degree of power in that market are part of the same process, and it is

[4] These include a role in safeguards investigations under the WTO and investigating competitive neutrality complaints.

for the sake of simplicity of analysis that the two are separated. (Mason C.J. and Wilson J., *Queensland Wire* case at 50,008)[5];

It follows that it would be preferable to adopt a second option. This would allocate all these market definition functions to the one agency, the Productivity Commission. This would avoid the excessive concentration of power within the ACCC that is presently evident, while locating the function within the Commonwealth agency that has the greatest expertise on the matter.

3. WHAT NOT TO CHANGE

There have been a number of proposals to "strengthen" the TPA. We think that the following ought to be rejected.

We disagree that there should be a reversal of the onus of proof as to the misuse of market power. Reversal of the onus of proof breaches a fundamental principle of law that a respondent has the presumption of innocence. That the change would make convictions easier is an argument against it rather than for it. Competition law is not a special case, such as protection of national security, that justifies abandonment of such an important protection of the citizen.

Likewise, **we would argue against an "effect" clause in Section 46** which would augment the existing "purpose" test. Elimination of competitors, prevention of entry into a market etc., are an everyday event in the markets that constitute the Australian economy. They are part of the normal, indeed essential, ebb and flow that creates and distributes our national income. They are not, per se, crimes. Their simple occurrence, as an effect of competition itself, should not be grounds for action without there being a damaging purpose behind them.

Nor would we support the granting of additional powers of divestiture to the ACCC or the courts. The existing powers are an adequate threat and response to those involved in breaches of Section 50. We think that divestiture is far too blunt an instrument to be used for breaches of Section 46. Matching of the punishment and the offence would be impossible in most cases.

Finally, **we believe that the imposition of jail sentences for breach of any of the provisions of Part IV would be wrong.** Proof of anti-competitive behaviour is a difficult and often complex matter. Proof of the gravity of the offence is even more difficult.

The degree of gain from breaches can sometimes be roughly estimated and a commensurate financial penalty applied. This is a better approach to punishment. Similarly, divestiture may reverse an unacceptable transaction and penalise the offender, though it will rarely restore the pre-existing status. Actions for damages also provide an avenue that can result in recompense and penalty at the same time.

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[5] quoted in *Merger Guidelines: Draft for Comment*, TPC 1992, p. 23.

The degree of harm suffered from anti-competitive behaviour is much more difficult to estimate and the imposition of a jail sentence would be much more open to doubt and criticism. We think the original decision not to permit criminal proceedings for contraventions of Part IV was sound.

4. CONCLUDING COMMENTS

We would add as a final comment that there appears to be a strain of thinking in some of the proposals for change that equates big business automatically with anti-competitive practices. We think that this sort of prejudice, while popular with the more excitable sections of the media, is unfair to that majority of large businesses operating in Australia that seek to observe the laws scrupulously. By definition, big business is likely to have more market power but that does not constitute a case for demonising them.

The Australian economy has made impressive gains in terms of labour productivity and efficiency over the past ten years. Many of these gains stem from the replacement of state monopolies in utilities with large and small competitive, and in many cases privately owned, businesses. These successes do not counsel a new range of measures against the activity of businesses and their leaders. The "sore thumbs" emanate from activity by radical union elements that are seeking to prevent more efficient labour relations and embarking on measures that would be blatantly illegal and subject to the most vigorous prosecution if employed by business firms.

Unfortunately, the Chairman of the ACCC has taken a position that is actively stoking animosity towards big business in the light of criticisms being made of ACCC excesses. We would see the ACCC's activities better diverted into combating restraint of trade by union monopolies rather than focusing on business behaviour.