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TRADE PRACTICES REVIEW

ACCI SUBMISSION
TO THE
DAWSON COMMITTEE REVIEW
OF THE
TRADE PRACTICES ACT

JULY 2002

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BACKGROUND

The Australian Chamber of Commerce and Industry (ACCI) is the peak council of Australian business associations. ACCI's members are employer organisations in all States and Territories and all major sectors of Australian industry.

Through our membership, ACCI represents over 350,000 businesses nation-wide, including the top 100 companies, over 55,000 enterprises employing between 20-100 people, and over 280,000 enterprises employing less than 20 people. This makes ACCI the largest and most representative business organisation in Australia.

Membership of ACCI comprises State and Territory Chambers of Commerce and national employer and industry associations. Each ACCI member is a representative body for small employers or sole traders, as well as medium and large businesses.

PRELIMINARY REMARKS

A review of competition issues brings into focus a whole range of competing interests. Sometimes this is described as 'big business' issues conflicting with 'small business' issues. This can be too simplistic a notion. There is no doubt that there can be differing perspectives on issues depending of the size of a firm or whether firms are wholesalers, retailers, producers or middlemen. As Australia's peak business group representing a membership that range across all sections of the economy and all sizes of business, presents here what we believe is a considered view on behalf of our members both large and small.

We discuss a number of competition concerns raised by small business which affect the current functioning of our economy. We explore those issues, raised by our members, and make a number of recommendations that urge close examination by the Inquiry. Other issues of key concern for ACCI members have also been addressed. In particular we make recommendations regarding the governance arrangements for the Australian Competition and Consumer Commission (ACCC). Merger laws are discussed, as are other matters raised in public debate.

The recommendations put represent the overwhelming views of our constituent members. They have been overwhelmingly endorsed by both our Small Business Committee and Economic and Fiscal Policy Committee. Where one of our members does not support a

recommendation contained here they are at liberty to make their own submission to the inquiry.

RECOMMENDATIONS

Recommendation 1: No Major Change in TPA Needed

The Trade Practices Act is working well as it is presently structured. There should therefore be no major changes in the operational aspects of the Act. Where change will be needed is in the way the Act is administered by the Australian Competition and Consumer Commission.

Recommendation 2: Unconscionability

In relation to unconscionability, attention should be placed on reviewing the effect of s51AC on primacy of contract. Due consideration should also be given to whether the 'non-exhaustive list of matters' as introduced to s51AC needs broadening to encompass 'other' direct and non-direct matters. ACCI believes that the drawing down of s51AC within State and Territory legislative frameworks should be pursued in a nationally consistent fashion.

Recommendation 3: Representative Actions

In relation to representative actions, ACCI recommends that consideration be given to whether increased funding for the ACCC to undertake broadened representative actions, especially under s51AC, would deliver additional benefits for small business and consumers.

Recommendation 4: Price Discrimination

In relation to price discrimination, while not advocating a s49 be reinserted in the Act, it is appropriate that the Dawson Committee fully examine whether small business concerns about 'price from suppliers' is adequately addressed under the Act through the existing provisions, and whether those provisions operate, on balance, in the best interests of economic efficiency and the community.

Recommendation 5: Codes of Practice

In relation to codes of practice, Government should reinforce its position that prescribed or mandatory codes, enforced by the ACCC, are not necessary when industry self-regulatory schemes are

working effectively and efficiently. Furthermore, the ACCC should work with industry to develop voluntary codes where appropriate.

Recommendation 6: Corporate Governance and an ACCC Board

It is imperative stronger internal checks and balances be put in place to strengthen corporate governance within the ACCC. The model of such a Board would be an amalgam of the Board of Taxation and the Inspector General of Taxation. The characteristics of this Board would include the following:

- The Board would be comprised of individuals with an expertise in economics and law and would include persons drawn from the business community, including small business. It would also include individuals with an established reputation and understanding of the third strand of ACCC activity, which is consumer protection. There would be approximately 12 members of this Board with a non-executive chairman.

- The Board would have no statutory authority but management would be expected to seek Board approval for all important matters of policy and direction. Day-to-day management of the ACCC would be the responsibility of the Chief Executive Officer.

- The Board would be a forum to which complaints about the actions of the ACCC could be directed.

- Each year, the Board would provide a report to Parliament reviewing the operation of the ACCC over the previous year. The Board Report would outline where it had agreed with the management and where it had differed with it. It would put on record the major complaints that had been lodged against the ACCC.

It is imperative that the community generally maintain confidence in the actions of the ACCC, but also that the ACCC does not overstep its proper authority nor undermine the efficient operation of the economy. A properly constituted Board would be a critically important model for governance within public sector regulatory and enforcement agencies.

Recommendation 7: Media Code of Practice

A code of practice that limits the ACCC's use of media to a specific and constrained set of circumstances needs to be drawn up. Such a code of practice would include the following provisions:

- Prior to any decision by a court, no media statement should be released by the ACCC that states any more than that an investigation has commenced or proceedings have been initiated in regard to some specified breach of the Trade Practices Act.

- The aim of any such media release is to provide awareness of the provisions of the Act and to explain how the ACCC is interpreting the Act in this particular circumstance. The purpose of such a release would therefore be educative rather than punitive.

- No details of the specific breach should be discussed nor should a business under investigation be named until it is formally charged with a breach of the Act.

- When a business is charged with a breach of the Act, the media statement should simply state that the ACCC has completed an investigation into the named business and that it has decided to commence court proceedings. It should not use such a release to specify the evidence that it intends to present when the case goes before a court.

- If the business wishes to put out a media statement discussing either the investigation or the subsequent charges that have been brought against it, that should be its own prerogative. The ACCC should refrain from responding to such statements.

- Where there is a successful prosecution in a court of law, the ACCC may present, in a balanced and objective manner, details of its investigation and of the decision made by the court.

- Where a court decision has rejected the charges brought by the ACCC, the ACCC should refrain from commenting but it should acknowledge that the prosecution had failed and the reason for it. It may state in a subsequent media release that it intends to appeal the decision, but only when the formal appeal has been lodged with the courts.

Recommendation 8: Cease and Desist Orders

The Review should clearly and decisively reject calls for granting the power to issue cease and desist orders to the ACCC. There are already sufficient powers available through the injunction process. The ACCC should not be provided with such powers which are rightfully those of courts of law and not enforcement agencies.

Recommendation 9: Effects Test

The Review should clearly and decisively reject calls for the introduction of an effects test in Section 46. In terms of competition, it is purpose which is the appropriate criterion.

Recommendation 10: Criminal Sanctions

The Review should clearly and decisively reject calls for the inclusion of criminal investigation powers and penalties into Part VI for breaches of the restrictive trade practices elements of the Trade Practices Act. There is no proven need for such expanded powers on the part of the Commission, and/or that existing legal avenues are inadequate to deter and punish such conduct.

Recommendation 11: Authorisations and Notifications

There is considerable merit in reviewing, updating and republishing the ACCC's guidelines for authorisations and notifications. This task should be given high priority, and that, as far as possible, the objective of the guidelines should be to make the process as simple as possible, explain the process in plain English and minimise the need for expert legal advice.

Recommendation 12: Conduct of Investigation

Legislative amendments are needed to ensure more stringent thresholds on the powers of the ACCC to initiate searches for information, documents and evidence. It is proposed that an amendment to s155 of the Act be introduced requiring the Commission, where it has reasonable grounds to believe there is a contravention of the Act, to seek a warrant from the Federal Court of Australia.

Recommendation 13: Definition of a Market

The current approach taken to the definition of 'a market' in the Act, and related judicial authorities, is sound and appropriate. As such, there is no need, at this time, for any legislative amendments to s4E.

EXECUTIVE SUMMARY

The Structure of the Australian Chamber of Commerce and Industry and the Relevance of ACCI's Structure to this Inquiry

The Australian Chamber of Commerce and Industry is Australia's peak council of employers and as such represents businesses of all sizes in all industries and in all states. Of particular importance to this review is the fact that it represents firms of all sizes, and therefore this submission is a distillation of the views of small, medium and large sized firms. It thus takes into account the considered views of the entire business community.

It is also the view of the ACCI General Council that although there are problems in its administration, the Trade Practices Act is working well. It is providing an appropriate regulatory environment in which both large and small businesses are able to compete. The introduction of unconscionable conduct provisions into the Act has been an important and welcome addition. It is in this area where the greatest tensions between large and small business exist and it is important that this area is developed over time to ensure that market power is not mis-used to harm competition through which small business is damaged.

There are obvious tensions between small businesses and large, but when the issues were considered by the General Council of the Australian Chamber of Commerce and Industry, the conclusion reached was that the concerns with increased regulation of business through granting additional legislative authority to the ACCC were greater than any apparent advantage that might be gained by adding to the ACCC's powers.

Moreover, it was the agreed position of the ACCI General Council that there needed to be additional restraints placed on the actions of the ACCC. As discussed more fully below, the need for a board of review is a necessary addition to the governance of the ACCC and is a position accepted by ACCI.

The overwhelming majority of our member associations do accept this submission in total and where there is disagreement it is only in regard to some elements of this submission.

Balancing the Interests of Small and Large Business

The Trade Practices Act is in the first instance legislation designed to protect competition in Australia. It is based on the recognition that the only road to prosperity is through competitive processes

which ensure that quality goods and services are brought to market at the lowest prices consistent with profitable business outcomes.

But there is a second equally important strand in the Trade Practices Act closely related to the first which is the preservation of an appropriate balance between the interests of small business and the interests of large. The prevention of the mis-use of market power by firms which have substantial market power is a crucially important feature of the Act. We, however, note the importance of the consumer protection provisions of the Act but recognise that they are not under review at this time.

In terms of the provisions which are under review, the Act seeks to enhance community welfare not just through competition of itself but also through the preservation of a "fair trading" environment. There are many aspects to this fairness criterion, but amongst them is the need to ensure that firms with a substantial degree of market power are acting fairly with other smaller firms. Establishing the proper norms of business behaviour is crucial to the process of competition.

Amongst these norms is the recognition that firms with substantial market power have obligations to deal fairly with small business. The Trade Practices Act and the regulatory environment surrounding business need to be crafted in ways that preserve competition and ensure that small business is not unfairly disadvantaged by the actions of large business.

The ongoing interpretation of the Act through the courts is deepening our understanding of how the ACCC will oversight competitive forces and the balance between large business and small. The crucial matter is that the balance is properly struck but it is also an important consideration in this Review that there are ongoing legal decisions that deepen our understanding of what the law means in practice. There should be no haste taken in adding new legislation and constraints on business when it is still uncertain how the present provisions are being interpreted in the courts.

Authorisation

As the granting of an authorisation is in effect an exemption from the law, each application should be assessed on its merits, and reviewed after an appropriate period of time to determine what if any circumstances have changed that may warrant the continuation or revocation of the authorisation.

However, for small- to medium-sized firms, the process of reaching a determination can be costly, long and onerous. While the ACCC aims to issue final determinations in six months it is not unusual for the process to take much longer.

There is considerable merit in reviewing, updating and republishing the ACCC's guidelines for authorisations and notifications.

Administration of the Act

The Trade Practices Act is administered by the ACCC. Its role is to interpret the Act and prosecute where it believes that the provisions of the Act are being breached.

The Act provides a legal framework for economic processes. It therefore requires deep understanding of how market economies operate. In particular, it requires an understanding of the nature of competition within the operation of a dynamic, constantly changing economic structure. It requires an appreciation of the way in which businesses routinely put pressure on each other through improving the quality of their products and through finding technological and organisational efficiencies that allow them to lower the prices that they charge.

The administration of the Act thus requires a strong sense of how markets work and what ought to be expected during the normal dealings between competitive firms.

There however seems to be an inadequate understanding within the ACCC of what is to be expected when firms compete. The absence of such understanding of dynamic market processes leads to the initiation of expensive legal actions at the discretion of the ACCC which creates uncertainty within business.

The lack of transparency in the actions of the ACCC where wide discretion is given to the regulator to determine which actions it will pursue has led to a situation where businesses remain uncertain where boundaries are found.

The Use of the Media

The approach taken by the ACCC in controlling what it deems to be unacceptable behaviour goes beyond the normal behaviour of an enforcement agency. Its use of media has become a commonplace matter. The ACCC has, as an apparent matter of policy, chosen to hold the reputations of businesses to ransom as a means to enforce conformity with its own interpretations of trade practices law.

The aggressive and calculated manner in which the ACCC uses the media in ways that must damage the reputation of firms must end. It causes damage to the reputation of individual firms and to the manner in which business in general is conducted. While not denying that there are breaches of the Act which occur, many of these are matters whose actual circumstances are untested through the courts and where the interpretation of the Act has not yet been clarified.

This is unacceptable. A code of practice that limits the ACCC's use of media to a specific and constrained set of circumstances needs to be drawn up. Such a code of practice would include the following provisions:

- Prior to any decision by a court, no media statement should be released by the ACCC that states any more than that an investigation has commenced or proceedings have been initiated in regard to some specified breach of the Trade Practices Act.

- The aim of any such media release is to provide awareness of the provisions of the Act and to explain how the ACCC is interpreting the Act in this particular circumstance. The purpose of such a release would therefore be educative rather than punitive.

- No details of the specific breach should be discussed nor should a business under investigation be named until it is formally charged with a breach of the Act.

- When a business is charged with a breach of the Act, the media statement should simply state that the ACCC has completed an investigation into the named business and that it has decided to commence court proceedings. It should not use such a release to specify the evidence that it intends to present when the case goes before a court.

- If the business wishes to put out a media statement discussing either the investigation or the subsequent charges that have been brought against it, that should be its own prerogative. The ACCC should refrain from responding to such statements.

- Upon gaining a conviction by a court of law, the ACCC may present details of its investigation and of the decision made by the court.

- Where a court decision has rejected the charges brought by the ACCC, the ACCC should refrain from commenting but it should acknowledge that the prosecution had failed. It may state in a subsequent media release that it intends to appeal the decision, but only when the formal appeal has been lodged with the courts.

Improving Corporate Governance at the ACCC

There is the need to improve corporate governance of the ACCC to ensure that its operations remain within the limits intended by the Government. The ACCC has few disciplines on its operation at present. It is able to initiate investigations and bring court action without reference to any external body. It is able to issue media releases and has cultivated a media profile that allows it to harm business reputations before any court decisions have been made.

It is therefore imperative stronger internal checks and balances the operation be put in place to strengthen corporate governance at the ACCC. The model of such a board would be an amalgam of the Board of Taxation and the Inspector General of Taxation. The characteristics of this Board would include the following:

- The Board would be comprised of individuals with an expertise in economics and law and would include persons drawn from the business community, including small business. It would also include individuals with an established reputation and understanding of the third strand of ACCC activity, which is consumer protection. There would be approximately 12 members of this Board with a non-executive chairman.

- The Board would have no statutory authority but management would be expected to seek Board approval for all important matters of policy and direction. Day-to-day management of the ACCC would be the responsibility of the Chief Executive Officer.

- The Board would, like the Inspector General of Taxation, also be a forum to which complaints about the actions of the ACCC could be directed.

- Each year, the Board would provide a report to Parliament reviewing the operation of the ACCC over the previous year. The Board Report would outline where it had agreed with the management and where it had differed with it. It would put on

record the major complaints that had been lodged against the ACCC.

It is imperative that the community generally maintain confidence in the actions of the ACCC, but also that the ACCC does not overstep its proper authority nor undermine the efficient operation of the economy. A properly constituted Board of Review would be a critically important model for governance within public sector regulatory and enforcement agencies.

Mergers and Acquisitions

In 1992, s50 of the Trade Practices Act was amended to prohibit mergers or acquisitions which have, or are likely to have, the effect of substantially lessening competition. Under s50, the substantial lessening of competition test for mergers is not opposed by the ACCI. The matters that must presently be taken into account are accurate indications of important issues for merger considerations and ACCI would recommend that none of the matters be removed from the section.

It is generally considered that some mergers and acquisitions could provide a benefit to the public. A merger that substantially lessens competition can still be allowed to continue under authorisation. If public benefits are deemed to outweigh the negative effects of reduced competition, then authorisation, with or without remedies, can be granted by the ACCC and the merger will still proceed.

Need for Judicial Restraint

There also need to be constraints placed on the ACCC in terms of what actions it can initiate on its own. There needs to be judicial review of actions taken by the ACCC and the actions that the ACCC can take in gathering information from businesses under s155.

The powers available to the ACCC to take action against a business need to be restricted. The raids on companies on the basis of anonymous letters to the ACCC demonstrates how inadequate the safeguards currently are. The ACCC should need to appear before a member of the Federal Court to lodge an application to commence a fact finding investigation.

The costs imposed on business by frivolous actions from the ACCC need redress. There should be consideration of the role of adjudicating costs against the ACCC where actions taken by the regulator have been deemed to have been frivolous and have led to

the need to provide information that is in the normal course of events costly to obtain.

The Need for a Measured Regulatory System

The issue of this review is not whether there ought to be regulation of the market but how to ensure that regulation does not damage the Australian economy. The strength of the Australian economy is due to the operation of the market. The existence of a system of private ownership within a legal structure that seeks to protect property rights are crucial to the preservation of our living standards and personal freedoms.

No legal system can operate without a proper regulatory body where there is proper investigation and prosecution for breaches of the law. But in dealing with competition policy, it must always be understood that the aim of each person in a market is to take business away from others.

It is because of this system of competitive market behaviour, where firms attempt to attract customers through providing better quality products, lower prices and innovative solutions to consumer demands that it can become extremely difficult to distinguish mis-use of market power from the normal operation of the market. The existence of market pressures on other firms is not evidence of the need for regulation.

In agreeing that in some circumstances some firms mis-use market power should not lead to the conclusion that the proper solution is even greater regulatory powers. The danger to business generally and to the economy overall of regulatory failure is large enough for there to be a measured response to regulation.

In this review, there are some who are arguing that there need to be even greater powers granted to the regulator. Indeed, the Australian Competition and Consumer Commission (the ACCC) is seeking a substantial increase in its powers as part of this review. In its own way it is unusual enough that the regulator would act in so political a manner as to lobby for increased powers and lodge a submission of 323 pages in support of such an increase. It is not a neutral observer in this review.

But irrespective of whether it is or is not appropriate for the ACCC to be lodging its own submission, the core question is whether the Australian economy is in danger of excessive regulation of markets. In the view of business, excessive regulation is a major problem faced by business and is one that needs to be addressed as part of this review.

Regulatory failure is a well-recognised problem. Regulation of business can lead to sub-optimal outcomes because firms are diverted from those activities that would lead to the greatest net benefit to the community and instead find that they are producing either a different array of products than would otherwise be the case, or they are so caught up in meeting the requests of regulators that their productivity is diminished.

Regulation is about process, not outcomes. The need for a fair trading environment means that certain kinds of unacceptable behaviours must be identified, made illegal and then, when discovered, punished. But the concern has become that there is an attempt to go beyond the identification of such unacceptable behaviours and classify hard competition as itself a mis-use of market power.

It must be incumbent on those who propose a strengthening of the Act to do all of the following:

- They must demonstrate that there are practices occurring that are either not properly identified in legislation or if in legislation are unable to be prosecuted under current legal constraints

- They must provide concrete examples of the kinds of behaviour that would be made illegal by these changes or if such practices are already illegal, they must provide concrete examples to show that there are mis-uses of market power that are taking place that cannot be constrained within the present legal structure. And the emphasis here is on concrete examples. There have been many abstract examples given of abuse of market power but what is needed are specific examples of how market power is being abused in particular circumstances.

- They must demonstrate that if the law were changed that normal competitive behaviours would not be brought into this regulatory structure. Although we do not believe this to be the case, regulatory failure may be unable to deal with some forms of market abuse at this time. But given the changes that are being sought by the ACCC and others, there are large dangers that many firms would be caught up in regulation if these changes were made.

- They must demonstrate how the changes in the law would remedy the alleged problems. It is one thing to believe one has identified a problem but it is quite another to show that the

remedy that is proposed will fix the problem even assuming it does not create additional problems in other spheres. Those advocating such change would need to show through concrete examples how the proposed remedies would be expected to work in practice.

Cease and desist orders and the effects test under section 46 of the Act are the two most important examples being presented to this review of new forms of regulatory powers. Both would allow the ACCC to act unilaterally in ambiguous market situations and interfere with the independent decision making apparatus of Australian firms.

Both would increase the range of the ACCC to act without legal constraints, or indeed any other constraints, to change behaviours that it believed were damaging competition. No courts would be involved in the first instance nor would any other review body need to be involved. These would represent a massive addition in the regulatory powers of the Commission which would without question allow it to intervene in far more market situations than at present.

The core question is whether the addition of such powers would enhance competition or damage it. In the view of business, such additional powers would damage the Australian economy by reducing the ability of firms to make decisions without the ongoing concern that the ACCC would involve itself in these decisions and would interfere with its ability to plan its own strategies.

Such increases in the power of a regulator can only diminish the ability of the economy to expand and innovate. Rather than fostering competition and economic growth, it will chill competition and diminish economic growth. It would be the reverse of the initial intention of the Trade Practices Act since it would lessen the ability of the economy to respond to changed market circumstance.

It is therefore essential that the Review take into account the likelihood of regulatory failure in assessing the demands for additional powers under the Act. Regulatory failure is potentially a much more serious problem. The potential for regulatory failure of any changes made should be a threshold test before any increased powers are placed into the Trade Practices Act.

Opposed to Cease and Desist Orders and the Effects Test in Section 46

The cease and desist orders and effects test are additional powers sought by the ACCC. The unrestricted powers this would give a regulator would allow it enormous ability to intervene in normal market behaviour and would restrict the ability of firms to compete. It is almost impossible to imagine where the use of such powers would have applied to the advantage of the economy in circumstances in any existing market situation.

If there have been contraventions of the Act they are seldom of the kind that requires an emergency resolution. The examples which have been publicised over recent months, such as the allegations of price fixing amongst petrol companies and the allegations of capacity dumping by Qantas, did not require the ACCC to intervene instantaneously to change market behaviour, nor should such restraint have been sought.

The direct intervention in markets to stop actions by competing firms based on nothing other than the judgement of the ACCC can only do harm. The effects test would have an even more chilling effect on markets as it would for all practical purposes outlaw competition itself and would leave it for the ACCC to determine whether different forms of market behaviour were acceptable.

Criminal Sanctions

The issue of whether criminal penalties should be introduced into the Trade Practices Act is really a question of which forms of penalties are more effective in preventing certain breaches. Price fixing, bid rigging and market sharing agreements are rightly illegal and are not defended by business. Indeed, it is other businesses which are often the entities harmed by such behaviours. At the present time, there are fines of $10 million for such breaches of the Act. The issue that has been raised is whether criminal sanctions are also needed to limit this form of illegal conduct.

There is little evidence that such problems exist in great numbers in Australia and the present penalty structure appears to provide sufficient protection against such practices. There are already great difficulties and risks in managing businesses in Australia without also adding the threats of jail for those who are accused of behaviours which contravene the Trade Practices Act.

POLICY CONTEXT FOR THE REVIEW

The terms of reference for the Inquiry into the Trade Practices Act (TPA) itself takes as its starting point the fundamental needs of the Australian economy. It assumes, and rightly assumes, that competition is of the utmost importance is ensuring that our standard of living is maintained and that economic growth continues at strong rates.

Competition is a metaphor for the efforts firms take to gain customers for their products. Businesses are commenced to produce goods and services whose costs are financed through revenues these firms receive. Businesses are thus, in a sense, islands of production in a world of buyers.

What makes the market economy as productive as it has become is that there are often a number of firms who are trying to sell the same or similar product to potentially the same buyers. It is the efforts taken by each firm to attract buyers to its own products rather than to those of another firm that cause the owners of all firms to make the efforts necessary to improve quality, lower price or bring new goods and services to the market.

The essence of this process is that firms try to take each other's customers. This is what is meant by 'competition'. And the reason that buyers are sought is so that firms can earn revenues higher than their costs of production. These profits are the return to entrepreneurial activity. They are the reward for success in providing buyers with the products they have sought in a better way than any of the other firms that have also sought to satisfy the same buyers.

It is the nature of this process that the more successful firms will be characterised by having provided better products to the market, where the only appropriate judges of what is 'better' are those who make the decisions on what to buy. Similarly, in a productive environment, it must be the firms themselves which make the decisions on what to produce, how to produce and what prices to charge for the finished products.

In respect of competition, there is a role for government but it is a necessarily limited one. The role for government is to ensure that the processes through which firms attract customers are conducted fairly. There are rules that have been developed in the past and which are undergoing continuous evolution as laws are changed which provide the detail of how each of the firms selling into the market are to behave. Most of these rules are of a negative kind, where firms are forbidden by law to act in particular ways because

certain of these actions are deemed to be unfair forms of competition.

But what is of critical importance is to recognise that the way in which we provide for our material wellbeing is conducted through a process in which businesses compete with each other for customers. It is this competition that is critical to improving productivity. It is therefore the tension between the flexibility needed for businesses to adjust to changed economic circumstances and the regulatory requirements to ensure that competition is conducted fairly that is at the core of the TPA.

That is the proper context in which the review of the TPA must be viewed. Business strongly supports regulation that is designed to provide a proper framework within which markets are able to function. It supports regulations that prohibit anti-competitive behaviour by firms. And while such behaviour, given the millions of transactions that occur in the Australian economy everyday, occurs only rarely, business strongly supports measures that are taken to stop such behaviour taking place.

It is also recognised that anti-competitive behaviour is a concept that continues to evolve as new market structures emerge and better understanding of how markets work is developed. We live in an increasingly globalised economy, where the definition of a market can be vastly different from our understanding in the past. Computerisation has changed many of the ways in which business operates, as have the adoption of other technological advances. There are new products and services coming onto the market each day that make older products redundant and often unsaleable.

In such a world the very concept of anti-competitive behaviour needs very careful examination. New products can simply be expected to displace other, older products. New suppliers will enter markets in place of other suppliers. There will be demands made by firms on their suppliers or their agents that will create market tensions. These are inevitable and to be expected.

It is therefore crucially important that anti-competitive behaviour is not confused with actions that simply put market pressure on other firms, or which place the responsibility of the owners of businesses to read and understand contracts before they are signed.

Market based competition is designed so that firms are continuously confronted by other firms which seek to provide for the same market or which seek to attract consumer outlays. Each firm must therefore recognise that other firms may enter its market at any time

selling a better product at a lower price and that its own customers can be taken away by others.

Perhaps more importantly, it must be understood that firms deal with other firms and that in such circumstances each firm will have its own aims in involving itself within such a relationship. There are business relationships which occur where firms are suppliers to other firms and where firms thus buy from their suppliers. Firms are often franchises or act as agents for others under contractual arrangements. Businesses are often tenants of other businesses.

Such business relationships may occur between different firms only a single time or they may be developed over a much longer period. Such firms may be of the same size of may be vastly different in size. The dealings may be cordial or filled with frictions.

But what is essential is that in all cases the dealings between firms are conducted in an honest and fair manner, which in the overwhelming majority of cases they are. That in some circumstances businesses may act dishonestly or in an unfair and unconscionable manner is recognised by everyone in business. In other cases, we find that there are grey areas in which it is difficult to tell whether the actions taken by a firm are outside the limits of fair competition. And while unacceptable dealings are recognised as the exception, they nevertheless create the need for appropriate legislation, enforcement provisions, a means of adjudication and a properly measured penalty structure.

Pricing as an Example of Competitive Behaviour

Some forms of business behaviour have been recognised as unacceptable and have been made illegal. As a clear example, pricing of products is a routine matter for all firms in a market economy. Pricing is designed so that the costs of production are met and also so that one's own firm will make the sale rather than another.

In determining an appropriate price, an explicit part of a business's strategy is to take customers from other firms, the resulting competitive pressures being felt, often very strongly, by those other firms in the same market. Indeed, on some occasions firms will use various products as loss leaders and sell at or below cost price. In none of this is there a role for a regulator nor should such pricing decisions be made illegal. It is through this form of competition that consumers are best served by a market economy.

However, it is also possible that the pricing policy chosen by a firm possessing substantial market power has the direct intent of driving a competitor from the market with the hope of raising prices at a later date. Rather than it being the aim to attract customers, which is a legitimate commercial purpose, the aim is instead to cause a competing firm to close down altogether so that substantially higher prices can be charged. Such 'predatory pricing' is rightfully illegal.

A reduction in price can thus be, as it normally is, part of the legitimate activities of a firm, but can also be, in extraordinarily rare circumstances, an attempt to achieve an anti-competitive outcome by driving a competing firm from the market with the intent being to raise prices at a later date and increase profits.

Appropriate Balance of Power Between Competing Businesses

From the initial question of even how to define a 'market', to the further questions of where some vague line has been crossed by the actions taken by a large business that may have made its actions 'anti-competitive', the fact remains that firms of all sizes are either competing with each other, or buying and selling to each other, in a market environment. And by agreeing to trade through a market, the implicit assumption one has accepted is that other firms may produce better products at cheaper prices and therefore may take one's customers away.

There are without question certain problems that confront smaller businesses when dealing with competitors, buyers or suppliers which are significantly larger than themselves are. These are extremely important matters and need to be addressed with extreme care. There are clear examples where larger firms with greater market power and the ability to cross-subsidise a loss-making operation can put immense pressures on its smaller competitors.

It is for this reason that business does support the inclusion of protective provisions within the TPA which are designed specifically to protect smaller firms from the actions taken by larger firms with which they come into commercial contact.

The Act, through the recently introduced unconscionable conduct provisions, has made it clear that there are unacceptable practices in the dealings between large firms and smaller. These are provisions which are a necessary addition to the Act since they ensure that fair dealings remain the standard by which such commercial relationships are judged.

Moreover, there may be additional need for provisions which add to the powers within the TPA that increase the protection offered to smaller firms in dealing with firms with substantially greater market power. Where such unfair practices can be identified and a legislative remedy can be formulated in law, these should be added to the provisions of the Act.

What must be clearly understood is that business does not oppose the existence of the TPA, nor does it oppose sensible extensions of its current provisions. What business opposes is the application of the Act in ways which cause commercial harm with no offsetting public benefit. Making markets work more efficiently, and protecting small business from unfair competition from other firms with greater market power, are important. Such provisions are fully supported by business.

But the fact that larger firms are able to generate cost savings through larger economies of scale, or may be able to supply a market at a consistently lower price, do not justify the actions of a regulator. There is no role whatsoever for a regulator to involve itself in the market-based actions of firms.

It is important to encourage competition and this is the intent of the TPA. Consumers are benefited by competition, and this is just as true for businesses when they are seeking to source their supply as it is for final consumers.

SMALL BUSINESS CONCERNS

Amendments to the TPA have increasingly focussed on the operation of the market from a small business perspective. This was particularly the case with amendments made in 1998 that implemented the Government's policy *New Deal: Fair Deal*, which was the Government's response to the *Finding a Balance: Towards Fair Trading in Australia (*Reid Parliamentary Inquiry)

While, ACCI firmly believes in the primacy of contract and the efficiency of markets, we acknowledge that there is a role for regulation where the market has failed to deliver. The Reid Report was right when it discussed the importance of finding a balance. There will always be business failures as a result of competition in the marketplace. Competition leading to businesses exiting the market in itself is not bad, but unconscionable behaviour in the pursuit of competition is not acceptable.

It is on that basis that ACCI supports the legislative policy initiatives arising from *New Deal: Fair Deal*. Quite simply, they have provided an excellent framework for making our markets fairer. These included provisions to:

- give small business genuine access to protections against unconscionable conduct (s51AC)

- allow industry designed codes of practice, in full or part, to be prescribed as mandatory or voluntary codes and enforced under the TPA (Part IVB)

- allow the ACCC to take representative actions against misuse of market power (s87(1B); and

- give small business interests equal importance to consumer interests when appointments are made to the ACCC (s7(3)(b).

Other non legislative initiatives arising from *New Deal: Fair Deal* which have contributed to a fairer market for small business which we support include:

- Stronger enforcement by the ACCC of small business fair trading rights through funding for test cases

- An education and awareness program on small business issues

- The establishment of a Small Business Unit with Small Business Managers in each state and territory

- Support for dispute resolution to provide small business with quicker, less costly and more efficient remedies than traditional court litigation

- Support for the extension of the Banking Industry Ombudsman Scheme to small business.

ACCI is particularly supportive of the activities of the ACCC in its education and awareness program for small business. The small business managers in each state and territory organise seminars and meetings to distribute information about the Act and to discuss small business concerns. The four Competing Fairly Forums that the ACCC has organised over the last two years have also been useful in reaching a wide range of rural and regional businesses through the Sky Channel Business Television Network in over 100 towns around Australia. ACCI and its Chamber network have been involved in all four of the forums.

We have also found the appointment of a Small Business Commissioner to the ACCC helpful for business generally and have worked well with the appointed person. The Small Business Consultative Forum which meets twice a year has also been a good mechanism to discuss issues.

Unconscionability

Reid Report

In May 1997, the report by the House of Representative Standing Committee on Industry, Science and Technology (Reid Report), found that:

- The equitable doctrines that have developed over time (in common law) that underpin 'unconscionability' and supported in s51AA of the TPA (ie s*51AA Unconscionable conduct within the meaning of the unwritten law of the State and Territories*) were deemed to be inappropriate – that is, 'the categories where relief has been granted are isolated and exceptional and the jurisdiction is confined within narrow limits' (note – the context is within trade or commerce transactions, not so much consumer transactions);

- The Committee found that a broader provision was required. Those not in favour of adopting a 'wider' definition of unconscionability argued that the existence of a harsh or oppressive conduct provision could be used to overturn or delay the action of contracts which would normally be

enforceable (ie the 'undue uncertainty' and 'freedom to contract' argument) and it would force courts to make 'value judgements'; and

- The committee recommended that the existing s51AA be repealed and a new provision proscribing unfair conduct in commercial transactions be introduced.

Reid Response

The Government, via its *Giving Small Business a Fair Go* ('New Deal: Fair Deal') statement, amended the TPA by introducing a specific small business section (similar to the already existing consumer protection provisions) and by creating a new part of the TPA which allowed prescription of industry and consumer developed codes of practice as either mandatory codes or voluntary codes with enforceable provisions. Hence, the provision s51AC Unconscionable Conduct in business transactions now exists. The Fair Trading Bill that encompassed these legislative changes was passed by Parliament and took effect on 1 July 1998.

The new s51AC effectively lists a number of factors (over and above the existing equitable doctrines) that the courts can consider in deciding whether conduct was 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.

ACCI's Position

In response to the Government's commitment to introduce s51AC, ACCI called for the government to ensure that that the Courts interpretation of 'unconscionable' would not extend beyond what is intended by the Government. ACCI called on the Government to issue a further explanatory memorandum re-iterating the importance of maintaining market forces and primacy of contract. Subsequent to these calls, ACCI learned that some lawyers were advising the larger businesses to avoid dealing with the smaller enterprises to avoid possible litigation under the new unconscionable laws. ACCI called on all parties to work towards building relationships.

In October 1998 and June 1999, the ACCC released two documents, 'A Guide to Unconscionable Conduct in Business Transactions' and 'Fair Game of Fair Go?' These documents were released in response to a demand to provide small business retailers with more information of their rights.

Baird Report

In August 1999, the report by the Joint Select Committee on the Retailing Sector (Baird Report), *Fair Market or Market Failure* found that:

- The new TPA s 51 was possibly limiting because it only applied to transactions of less than $1 million; and

- A 'gap' existed with respect to 'remedies' available to small business retailers in their dealings with big business.

In response to the Baird Report, the Government responding by stating that it believed the $1 million transactional limitation of s51AC of the TPA did deter some small businesses from accessing the unconscionable conduct provisions of the Act. The Committee recommended that the transactional limit be increased to $3 million. This change was later enacted.

Case Law since 1 July 1998

Since the introduction of the new unconscionability legislation on 1 July 1998, there have been a number of important cases heard in the Federal Court.

ACCC v Simply No Knead (Franchising) Pty Ltd [2002] FCA 1365 (22 September 2000) and *CG Berbatis Holdings Pty Ltd v ACCC [2001] FCA 757 (27 June 2001)*

In this case, Judge Sundberg found that 'unconscionable' in s 51 AC is not limited to cases of equitable or unwritten law as found in s 51 AA (ie the 'old' common law definition of 'unconscionability'). In effect, sub–section (3) permits 'an enlarged notion of unconscionability' than what would typically be applied in unconscionability in 'equity'.

His Honour in this case effectively allowed a broader definition of equity unconscionability (ie the 'old' common law equitable doctrine definition) to be applied in his determination, and in doing so, he effectively created a precedence for pursuant cases.

Further, there is evidence to suggest that the courts since this determination have readily applied the 'broadened' factors that should be taken into consideration when determining whether a 'business to business' action was unconscionable. Ultimately, it would appear that the Courts have been able to give 'new meaning' to unconscionability (ie as intended by the government to reduce the adverse affects on small business) and s 51 AC has become an effective statute (ie in terms of protecting small business).

Further, in *ACCC v Berbatis Holdings Pty Ltd* (2000) Judge French examined at length the ambit of the unwritten law of unconscionability. His Honour said there was no reason to suppose that the unconscionable conduct prohibited by s51AB and s51AC 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.'

These two cases have demonstrated a willingness of the courts to adopt the list of matters that were introduced as part of the *Fair Trading Bill.*

Monroe Topple & Associates Pty Ltd v The Institute of Chartered Accountants in Australia [2001] FCA 1056 (6 August 2001)

In this case, The Institute of Chartered Accountants (ICAA) changed the training requirements that persons seeking admission to their membership must satisfy. It had done so for the purpose of maintaining or raising the standards of its members. The changes had the effect of disappointing the expectations of those who had developed businesses from the selling of Professional Year (PY)

support services (ie of the kind that Monroe Topple [MTA] did) but, and as Judge Lindgren noted, it fell short of unconscionable conduct.

MTA was effectively a third party to the actions of ICAA. That is, MTA was seeking a claim of unconscionability as a 'third party' as a result of the transaction/s that commonly occurred between the 'consumer (of the similar training products that both ICAA and MTA produced) and the ITAA. Judge Lindgren found that the purpose of s51AC was to protect small businesses in their dealings with 'big business', and thus the expression of 'in connection within s51AC requires that the conduct impugned 'company' 'go with' or 'be involved in' the supply of the goods or services.

The precedence in this case is that s51AC cannot be enacted in favour of third parties in a business unconscionability case.

Matters of Issue - Unconscionability

The possible adverse effect of s 51 AC on primacy of contract needs exploring. This should be part of the review. Little case evidence to support or deny evidence to the contrary exists. Although it is generally accepted that the assumptions underlying the doctrine of contract – that contracts are always based on the mutual agreement of fully informed individuals and they arise out of free choice – no longer hold, it would be important to gather evidence to ascertain whether the new laws have had the effect of 'eroding' the validity of contracts (to protect against incidences when normally enforceable contracts could be overturned or delayed placing undue pressure on the 'other' party).

Section 51AC appears to be working well, with a number of respondents being successfully prosecuted for 'business to business' unconscionability. Further, the courts have successfully incorporated into their decision making the non-exhaustive list of matters to which the Court has been authorised to have regard for the purpose of determining whether a corporation has contravened the provision. The question though is whether the list of matters needs to be widened.

There may be a need to broaden the 'net' of s 51 AC to ensure that it protects those third parties that, due to the peculiarities of their market structure or circumstances, cannot be protected from unconscionability as their dealings were not of a 'direct' nature.

There is finally a need to ensure that the laws have not resulted in a 'shying away' affect. That is, big business makes a conscious decision not to interact with small business to protect against costly litigation.

Amendments to the TPA proclaimed on 1 October 2001 provided the States with the opportunity to draw down on s51AC so as to include the provision within their own retail legislation. To date, NSW, QLD and VIC have adopted the provisions without delay, the legislation in WA and NT is expected to be introduced in the latter part of 2002, the recent SA election has delayed the introduction of the legislation and the TAS government are seeking a re-wording to the provision. The ACCC is encouraged to work closely with those governments to ensure that the new provisions are introduced promptly and in a uniform fashion (ie in an attempt to reduce inconsistencies between jurisdictions). Inconsistencies in legislation, especially in retail tenancy, is an issue, and uniform legislation should be encouraged. Codes of practice (see below) may counteract this issue.

The ACCC should be applauded for its efforts to make small businesses aware of their legislative rights in relation to this issue. Apart from the numerous publications produced on the issue, there is a dedicated ACCC Infocentre and recently the establishment of Small Business Managers and Regional Outreach Officers in each state and territory.

The good 'corporate citizen' concept should be reinforced. That is, society is increasingly demanding a greater demonstration of ethical behaviour amongst the business community. There is evidence to suggest that society is beginning to give preference to those organisations that are able to demonstrate 'triple bottom line' outcomes for example. The social element of sustainability does encompass elements of sound corporate governance. There needs to be a perpetuation of the ideal that big businesses will be 'penalised' by consumers if they engage in poor corporate governance – for example, unconscionable conduct (prevention being better than a cure).

Recommendation

In relation to unconscionability, attention should be placed on reviewing the effect of s51AC on primacy of contract. Due consideration should also be given to whether the 'non-exhaustive list of matters' as introduced to s51AC needs broadening to encompass 'other' direct and non-direct matters. ACCI believes that the drawing down of s51AC within State and Territory legislative frameworks should be pursued in a nationally consistent fashion.

Representative Actions

Following the 1999 Baird Report, the Government enacted legislation that gave the ACCC the power to undertake representative actions and to seek damages on behalf of third parties under Part IV of the Act. Further, the Hon Joe Hockey MP, Minister for Small Business and Tourism, in May of this year introduced the *Trade Practices Amendment (Small Business Protection) Bill 2002* which proposes to amend section 87 of the Act.

This legislation would effectively enable the ACCC to bring representative actions in respect of breaches of sections 45D and 45E. The effect of this change would be to enable the ACCC to seek orders from the Federal Court on behalf of one or more persons who have suffered, or are likely to suffer, loss or damage by conduct of another person where the conduct engaged is in contravention of sections 45D or 45E. ACCI supports the introduction of this legislation and a possible widening of the representative action provisions to encompass other sections in the Act.

ACCI believes that the ability of the ACCC to take representative action against a party considered to be in contravention of the Act is an important feature as it effectively protects and empowers small businesses as well as contributing to the development of important case law that otherwise may never occur.

Recommendation

In relation to representative actions, ACCI recommends that consideration be given to whether increased funding for the ACCC to undertake broadened representative actions, especially under s51AC, would deliver additional benefits for small business and consumers.

Price Discrimination

An issue that the Dawson Committee may wish to examine is the question of price discrimination. Price discrimination is regulated under Part IV of the Act in that it .may be grounds for contravention under sections 45, 46 and 47. However, a specific section on price discrimination (s49) was repealed in 1995 on the recommendation of the Hilmer Review on National Competition Policy.

The old s49 stated:

> *Section 49(1) prohibited a corporation from discriminating between buyers of goods of like grade and equality in relation to:*
>
> *(1) the price of goods;*
>
> *(2) any discounts, allowances, rebates or credits given or allowed in relation to the goods;*
>
> *(3) the provision of services in relation to the goods; or*
>
> *(4) the making of payments in relation to services;*
>
> *if the discrimination was of such magnitude, or such a recurring or systematic character, that it had or was likely to have the effect of substantially lessening competition in the market in which the goods were supplied.*

Essentially, the prohibition against price discrimination prevented the sale of like goods to different persons at different prices, where such discrimination substantially lessens competition.

The Hilmer Committee argued that s49 was contrary to the objective of economic efficiency and had not been of assistance to small business. The Committee also believed that it is not 'the role of the competitive conduct rules to protect any particular sector of society, nor that the competition rules should be used to achieve objectives contrary to economic efficiency.'[1]

Further the Hilmer Committee argued that 'competition policy should not be distorted to provide special protection to any interest group, including small business, particularly where this is potentially to the detriment of the welfare of the community as a whole…. In any event, it seems clear that small businesses have not achieved any significant benefit from the presence of Section 49.'[2]

Matters of Issue – Price Discrimination

There is a legitimate concern that a prohibition on price discrimination may discourage pro-competitive conduct. As quoted in the Hilmer Report: 'If prices must be equal, suppliers will be

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1 National Competition Policy Review, *National Competition Policy: Report by the Independent Inquiry (Hilmer Report)* (AGPS, August 1993), p. 74

2 Hilmer Report, pp 79-80

prevented from granting discounts to purchasers with large requirements such as grocery chains in the absence of a cost justification. The public generally will be denied the lower retail price the purchaser with large requirements would have been able to offer its customers, and prices may tend to go up to the level of the corner store rather than down to the level of the chain store.[3]

The Swanston Review in 1976 also recommended the removal of s49 as it believed that it has produced such price inflexibility that the detriment to the economy as a whole outweighed any assistance which small business may have derived from it. However, it is worth noting that the structure of Australian industry, and in particular the retailing industry, has changed significantly in the intervening period.

Recommendation

In relation to price discrimination, while, ACCI is not advocating a Section 49 be reinserted in the Act, we believe that it is appropriate that the Dawson Committee fully examine whether small business concerns about 'price from suppliers' is adequately addressed under the Act through the existing provisions, and whether those provisions operate, on balance, in the best interests of economic efficiency and the community.

Authorisations and Notifications in Respect of Restrictive Trade Practices

The TPA, at Part VII, allows the ACCC to provide authorisations and accept notifications for certain types of conduct which would otherwise be in breach of the TPA. The relevant provisions of the Act concern the powers of the Commission to grant authorisations (s88), and the procedures to be followed for granting and administering authorisations (ss89-91C).

Conduct covered by Part VII includes: contracts, arrangements or understandings which contain an exclusionary provision, or which substantially lessen competition; price fixing involving goods and services; exclusive dealing; resale price maintenance; and, mergers.

The essential elements of Part VII are that it permits corporations to enter into, and/or give effect to, commercial arrangements, such as contracts, or engage in conduct that is anti-competitive and likely to be in breach of the Act where the ACCC determines there are

[3] Hilmer Report, p78

public benefits outweighing the anti-competitive detriment (s88 and s90).

Authorisation must be *ex ante*, not *ex post* (s88(12)), is not available for misuse of market power, and may have conditions attached. The ACCC also has the power to grant interim authorisation to enable conduct that would otherwise be deemed anti-competitive while a final determination is made. Interim authorisation is only granted where the arrangement can be reversed if an application is ultimately unsuccessful.

Further, authorisation only applies to potential anti-competitive conduct under Part VII other than exclusive dealing arrangements, which is covered by the notification provisions of Part VII, Division 2 (s93 for the offence; and ss93A and 95 for administration matters).

While authorisation requires the express consent of the Commission for the conduct concerned, by contrast notification can be regarded as a 'no objection by the Commission' approach.

As the granting of an authorisation is in effect an exemption from the law, ACCI considers that each application should be assessed on its merits, and reviewed after an appropriate period of time to determine what if any circumstances have changed that may warrant the continuation or revocation of the authorisation.

However, for small to medium sized firms, the process of reaching a determination can be costly, long and onerous. While the ACCC aims to issue final determinations in six months it is not unusual for the process to take much longer.

For small to medium sized enterprises, the costs borne by applicants for authorisation are not insignificant. An application fee of $7,500 per authorisation is charged, regardless of the circumstances of the applicant. The Commission does not have the discretionary power to waive the application fee. In addition, SME applicants may not have the resources to engage legal counsel to assist them with their application, or provide advice on the process – particularly if a determination is challenged by a competitor. Indeed, the Chamber contends that the threshold for objecting to a determination may be too low if it is not a requirement for the objection to be argued and substantiated.

There is merit in examining whether the authorisations process can be streamlined, at least for some classes of authorisation, to assist small to medium sized firms minimise the cost and time involved in securing a final determination.

In addition, there is considerable merit in reviewing, updating and republishing the ACCC's guidelines for authorisations and notifications. ACCI recommends that this task be given high priority, and that, as far as possible, the objective of the guidelines be to make the process as simple as possible, explain the process in plain English and minimise the need for expert legal advice. As a matter of principle, it is inappropriate for public servants to be empowered to approve exemptions from the law.

In the current context, the process of granting authorisations empowers the ACCC to act as 'policeman, prosecutor and judge' for exemptions from the TPA but, as part of the process, still provides for reassessment of an application for authorisation initially by the Australian Competition Tribunal and ultimately by the Federal Court.

Codes of Practice

The Government, in its *New Deal: Fair Deal* statement amended the TPA by creating a new part of the TPA which allowed prescription of industry and consumer developed codes of practice as either mandatory codes or voluntary codes with enforceable provisions.

Underpinning this amendment was the introduction of a *Prescribed Codes of Conduct* which sets the policy guidelines on making codes of conduct enforceable under the TPA. Consistent with ACCI's position, the Government is of the view that prescribed or mandatory codes, enforced by the ACCC, are not necessary when industry self-regulatory schemes are working effectively and efficiently.

To date, only one mandatory code of conduct has been introduced since the legislative amendments were made to the TPA in 1998. The Franchising Code of Conduct effectively closed a number of gaps in relation to disclosure requirements, minimum standards for franchise agreements and dispute resolution procedures. Although there were concerns originally that the regulation would create a high amount of additional paperwork, indications from the government, franchisers and franchisees is that the Code is working well and in the broad, it has been a palatable solution to the problems that previously existed.

Further, ACCI is pleased to see that the regulatory impact on SMEs is a core consideration when deciding whether to adopt a mandatory code of conduct. The completion of Regulation Impact Statements (RISs) is a critical component of sound policy formulation, and if

completed correctly, they provide an invaluable cost/benefit analysis. ACCI encourages this continued approach.

ACCI agrees with the recommendation on mandatory codes by the Office of Regulation Review in its September 1999 *Report of the Commonwealth Interdepartmental Committee on Quasi-Regulation:*

> 'Prescription under the TPA should proceed only if all the following prerequisites have been met:
>
> - a market failure has been identified that will, in the absence of government intervention, have a significant detrimental impact on a substantial group in the community or there is a social policy objective that, if not pursued by government, will lead to a significant detrimental impact on a substantial group in the community
>
> - a systemic enforcement issue exists, for example with breaches of voluntary industry codes and lack of agreement on fair trading principles, which has led to the failure of self-regulatory or quasi-regulatory arrangements
>
> - there are significant deficiencies in any existing regulatory regime which cannot be remedied (for example, inadequate industry coverage)
>
> - a range of self-regulatory options and 'light handed' quasi-regulatory options has been examined and demonstrated to be ineffective.'[4]

Although the legislation concerning certain aspects of unconscionability and the adoption of voluntary and mandatory codes of conduct are infant in their application, all indications are that they are working well and are achieving their desired results.

Moreover, to counteract the trend of 'channelling' all contentious issues through s51AC, and thus, exposing small businesses to the considerable expense of court proceedings, codes of practice that underpin s51 and complement the ongoing application of State- and Territory-based mediation and tribunal structures (for dispute resolution), should be encouraged. Whether these codes of practice

[4] Grey Letter Law – Report of the Commonwealth Interdepartmental Committee on Quasi-regulation , Office of the regulation review, Sept 1999

should be of a voluntary or mandatory nature is the contentious issue. Invariably, there will be those that will complain that voluntary codes 'lack teeth', whilst there will be those that demand flexibility and responsiveness. The Governments position is that self-regulatory codes should be supported and mandatory codes should only be considered once the voluntary code fails. This is the stated position of ACCI also.

Recommendation

In relation to codes of practice, Government should reinforce its position that prescribed or mandatory codes, enforced by the ACCC, are not necessary when industry self-regulatory schemes are working effectively and efficiently. Furthermore, the ACCC should work with industry to develop voluntary codes where appropriate.

GOVERNANCE

The governance arrangements of the ACCC warrant the attention of the Dawson Committee. There are numerous models that abound at the federal level for various regulatory authorities. Business and the community are interested in good governance whereby there is accountability and transparency in processes. Currently the Chair and the Commissioners are ultimately accountable to the Parliament and have reasonable flexibility and independence in determining the sorts of cases the Commission will pursue. Without interfering in the day to day operations of the Commission, a Board could give strategic directions for the Commission. Restructuring the existing governance arrangements, so there is a Board that the Chair of the Commission reports to would add to the confidence of the business community.

In the Wallis Report there is a discussion of the need for review boards to maintain proper governance. These views are appropriate in the consideration of the need for adequate governance of the ACCC. In discussing the Australian Prudential Regulation Commission (APRC), the Corporations and Financial Services Commission (CFSC) and the Payments System Board (PSB), the Wallis Committee made the following relevant observations:

> 'The APRC and the CFSC should have boards of directors to determine their operational and administrative policies, to ensure that they fulfil their respective legislative mandates and to monitor their performance.
>
> 'Each of these new boards (APRC, CPSC and PSB) should be chaired by an independent member, rather than the agency's chief executive, in order to encourage a broad perspective and underline the accountability of management of the board.
>
> 'The chairpersons and other board member would need to distinguish carefully their responsibilities at policy level from the responsibility of the agencies' executives for enforcement actions and avoid adopting policies or procedures which would impede enforcement action.
>
> 'The independent members of these regulatory agency boards should have financial industry expertise or other expertise (including expertise in consumer protection) relevant to the agencies' functions. They would serve independently as individuals and not as representatives of any sectional boards.
>
> 'Conflicts of interest are an obvious potential problem for independent board members, but should not rule out the

appointment of members for whom conflicts might arise. Conflicts should be managed through some limitations in the selection of board members to avoid frequent and severe conflicts of interest and through rules of board procedure.'[5]

Proposed Board Structure

Clearly from a business perspective, amongst the key problems for business is the lack of proper governance within the administration of the ACCC. There is a concern that there are insufficient disciplines on the ACCC in interpreting its mandate. While there are a number of Commissioners appointed to the ACCC, who are to some extent intended to moderate the actions taken to regulate business, this has not proven to have been sufficiently strong in practice. Nor does the need to seek adjudication in a court of law seem to have led the ACCC to modify its stance.

Recommendation 108 of the Wallis Report stated that regulatory agencies should have boards with majorities of independent directors. In its discussion the Report discussed this proposal and included a discussion of possible compositions of such boards. :

'The regulatory agency should have a board of directors responsible for their operational and administrative policies, the fulfilment of their respective legislative mandates and their performance.

'The key principle in the composition of the new board is that there should be a majority of independent members and substantial cross-representation.

'The following board composition is illustrative and not prescriptive.

APRC – six independent members appointed on the nomination of the Treasurer, three ex officio members from the RBA including, the Governor, a deputy governor and an ex officio member of the PSB, the chief executive of the CFSC, and the chief executive of the APRC (appointed to that office on the nomination of the Treasure).'[6]

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5 Financial System Inquiry Final Report (Wallis Report). (1998) 'Coordination and Accountability, Governance.' Section 12.4, pp 535-36.

6 Financial System Inquiry Final Report (Wallis Report) 1997. 'Coordination and Accountability, Governance.' Section 12.4, p537.

There is also a concern with the economic understanding displayed by the ACCC in dealing with complex market situations. The dynamics of competitive markets, the strategies that businesses pursue, the large variety of pricing policies adopted, the need to distinguish between short- and long-term considerations are all aspects of the operation of the market that do not seem at this stage to be properly recognised by the ACCC in commencing legal proceedings and in bringing prosecutions.

The inappropriate economic framework applied by the ACCC is a problem not only because it harms the economy directly, but it needlessly discredits the processes of the market. It should be the role of the ACCC to generate a community wide understanding of the role of markets in our society, so that the community better understands how competition works in practice.

There is therefore an urgent need for a Board of Management that remains outside the ACCC but which can oversee and review its decisions. This Board would need to be made up of individuals who understand the operation of markets and who are concerned to ensure that the economy is not needlessly penalised by the heavy-handed regulation of market situations.

It is the checks and balances that such a Board would bring that would add to the clarity of the approach taken by the ACCC.

Improving Corporate Governance at the ACCC

There is the need to improve corporate governance of the ACCC to ensure that its operations remain within the limits intended by the Government. The ACCC has few disciplines on its operation at present. It is able to initiate investigations and bring court action without reference to any external body. It is able to issue media releases and has cultivated a media profile that allows it to harm business reputations before any court decisions have been made.

It is therefore imperative stronger internal checks and balances be put in place to strengthen corporate governance at the ACCC. The model of such a board would be an amalgam of the Board of Taxation and the Inspector General of Taxation. The characteristics of this Board would include the following:

- The Board would be comprised of individuals with an expertise in economics and law and would include persons drawn from the business community, including small business. It would also include individuals with an established reputation and understanding of the third strand of ACCC activity, which is consumer protection. There would be

approximately 12 members of this Board with a non-executive chairman.

- The Board would have no statutory authority but management would be expected to seek Board approval for all important matters of policy and direction. Day-to-day management of the ACCC would be the responsibility of the Chief Executive Officer.

- The Board would, like the Inspector General of Taxation, also be a forum to which complaints about the actions of the ACCC could be directed.

- Each year, the Board would provide a report to Parliament reviewing the operation of the ACCC over the previous year. The Board Report would outline where it had agreed with the management and where it had differed with it. It would put on record the major complaints that had been lodged against the ACCC.

It is imperative that the community generally maintain confidence in the actions of the ACCC, but also that the ACCC does not overstep its proper authority nor undermine the efficient operation of the economy. A properly constituted Board would be a critically important model for governance within public sector regulatory and enforcement agencies.

A Media Code of Practice

Beyond the disciplines that would be associated with a Board are additional rules for the use of the media by the ACCC.

The approach taken by the ACCC in controlling what it deems to be unacceptable behaviour goes beyond the normal actions of an enforcement agency. Its use of media has now become commonplace matter. The ACCC has, as an apparent matter of policy, chosen to hold the reputations of businesses to ransom as a means to enforce conformity with its own interpretations of trade practices law.

The unsettling matter is that this is a policy that has little power over firms that have no regard to their market reputations, and which therefore have little if any intention of being good corporate citizens. It is only against firms who have as an important corporate aim maintaining their reputations within the community that this approach works, yet it is against just such firms that such activity would be generally unnecessary. The importance of maintaining

one's name in the marketplace would be in virtually all circumstances sufficient to constrain anti-competitive behaviour.

Where this is not the case, and where the ACCC believes that the provisions of the TPA have been breached, natural justice would nevertheless require the ACCC to take a more measured approach. The powers of this regulator are enormous, and the ability to threaten and then take court action ought to be sufficient in deterring anti-competitive activity and then punishing such behaviour where it occurs.

The role of the media is part of the punishment for wrong doing, not part of the enforcement practices of a regulator. The ACCC may argue that it is doing no more than other regulators in the same circumstances. Yet it is precisely that the accusation is itself a large penalty in the market that must make the ACCC more circumspect in using its media potential. It is because it is often accusing major Australian businesses of wrong doing that such accusations draw the media attention that they do.

A code of practice that limits the ACCC's use of media to a specific and constrained set of circumstances needs to be drawn up. Such a code of practice would include the following provisions:

- Prior to any decision by a court, no media statement should be released by the ACCC that states any more than that an investigation has commenced or proceedings have been initiated in regard to some specified breach of the Trade Practices Act.

- The aim of any such media release is to provide awareness of the provisions of the Act and to explain how the ACCC is interpreting the Act in this particular circumstance. The purpose of such a release would therefore be educative rather than punitive.

- No details of the specific breach should be discussed nor should a business under investigation be named until it is formally charged with a breach of the Act.

- When a business is charged with a breach of the Act, the media statement should simply state that the ACCC has completed an investigation into the named business and that it has decided to commence court proceedings. It should not use such a release to specify the evidence that it intends to present when the case goes before a court.

- If the business wishes to put out a media statement discussing either the investigation or the subsequent charges that have been brought against it, that should be its own prerogative. The ACCC should refrain from responding to such statements.

- Upon gaining a conviction by a court of law, the ACCC may present details of its investigation and of the decision made by the court.

- Where a court decision has rejected the charges brought by the ACCC, the ACCC should refrain from commenting but it should acknowledge that the prosecution had failed. It may state in a subsequent media release that it intends to appeal the decision, but only when the formal appeal has been lodged with the courts.

The denial of natural justice is manifest in the actions taken by the ACCC to identify firms which have not even been charged never mind convicted of a breach of the Act. The role of its media statements should be to educate and instruct businesses in how the ACCC interprets the Act, not to act as a means of coercion a form of punishment in advance of decisions by the courts.

At the present, the concern is that in the manner in which the ACCC uses its media exposure in a way that is calculated to damage their commercial reputations, it is acting as the prosecutor, jury and judge in commencing an investigation, determining that the Act has been breached and in punishing firms by exposing them to negative publicity. All of this taking place prior to any evidence having been presented to a court or to a judgment having been made.

The manner in which the ACCC responds to firms which deny the charges that have been brought against them is also of concern. It is not the role of the ACCC to respond to such criticisms of its actions. If firms wish to deny in public the accusation that have been brought against them, then they ought to be free to do so without having to contend with the ACCC repeating its charges.

The aggressive and calculated manner in which the ACCC uses the media in ways that is directly intended to damage the reputation of firms must end. It causes damage to the reputation of individual firms and to the manner in which business in general is conducted. While not denying that there are breaches of the Act which occur, many of these are matters whose actual circumstances are untested through the courts and where the interpretation of the Act has not yet been clarified.

In the given circumstances, the proper approach of the ACCC must be to limit its use of media to protect the commercial reputations of those who have not had breaches of the TPA proven in a court of law.

Power to Obtain Information, Documents and Evidence

The TPA, at Part XII (in particular, s155) provides the Commission with very wide powers to obtain information, documents and evidence. The breadth of those powers is augmented by judicial decisions to the effect: common law privileges against self-incrimination do not apply for information, documentation and/or evidence provided under a s155;[7] recipients can be required to 'act as a detective', undertaking an investigation to determine matters which are properly seen as within the control of those given the notice;[8] and, the burdensomeness of compliance will not invalidate a s155 notice, nor will objective harshness, unreasonableness or oppressiveness constitute an independent ground of invalidity.[9]

Other important judicial decisions relating to the breadth and reach of s155 have dealt with: the reversal of onus of proof on the complainant that the Commission did not act in good faith/with requisite reason in the execution of a s155 notice[10]; absent evidence of invalidity, Courts on application from recipients of notices will not provide orders for discovery or allow interrogatories[11]; and orders cannot be acquired under the Administrative Decisions (Judicial Appeal) Act (1977(Cth) to obtain the reasons for the issuance of a s155 notice.[12]

The Courts have also given broad meaning and reach to the important 'reason to believe' test within s155 – that is, the Commission must believe a person is capable of providing information, documents or evidence, and there must be reasonable grounds for that belief. It is not necessary there be a belief such

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[7] *Melbourne Home of Ford Pty Ltd vs TPC (1979) 36 FLR 450; ATPR 40-107*

[8] *Dunlop Olympic Ltd vs TPC (1982) 62 FLR 145; 1 TPR 223*

[9] *Pyneboard Pty Ltd vs TPC (1982) 57 FLR 368*

[10] *Melbourne Home of Ford Pty Ltd vs TPC (1979) 36 FLR 450; ATPR 40-107*

[11] *Melbourne Home of Ford Pty Ltd vs TPC (1979) 36 FLR 450; ATPR 40-107*

[12] *Rice Growers Co-operative Mills Ltd vs Bannerman (1981) 53 FLR 408; 35 ALR 553*

material(s) would or tend to establish a contravention, 'merely that they relate to the matter.'[13]

ACCI is greatly concerned with a number of elements of s155 of the Act, generally regarding the very wide, if not sweeping, powers granted to the Commission in such matters, and the very low thresholds (and hence checks on its conduct) applied by judicial authorities.

It is concerned s155 provides the Commission with the quite broad powers granted to the ACCC to compel recipients of notices to provide information, even that which may incriminate themself(ves). The grounds for the issuance of a notice – 'reason to believe' – have been given a very low threshold ('merely relate to the matter') by judicial authorities.

ACCI is also concerned at the seemingly low level of transparency, and potentially arising from this situation, accountability of the ACCC for the execution of s155 notices. Judicial authorities have greatly limited the potential for aggrieved parties – usually recipients of such notices – from obtaining information on the reasons and processes behind their issuance, something which does not sit comfortably with our view of the common law and administrative law.

Against this background, it is recommended that legislative amendments to introduce more stringent thresholds on the powers of the ACCC to initiate searches for information, documents and evidence. In this regard, ACCI would propose an amendment to s155 of the Act requiring the Commission, where it has reasonable grounds to believe there is a contravention of the Act, to seek a warrant from the Federal Court of Australia.

Such a reform would introduce appropriate checks and balances into the processes by which the Commission exercising this sweeping power, and go some small way to redress what commerce and industry considers the inadequate threshold – 'reason to believe' – contained in s155 of the Act.

Breaking Up the ACCC?

> 'The objective of the Trade Practices Act as set out in the legislation, is to enhance the welfare of Australians through

[13] *WA Pines Pty Ltd vs Bannerman (1980) 30 ALR 559 at 561; 41 FLR 175*

> the promotion of competition and fair trading and provision for consumer protection.'[14]

TPA has a dual objective: to promote competition and to protect consumers, and although these two ideas are not entirely unrelated delivering on both simultaneously offers the potential for conflict. To promote competition it is necessary that the ACCC and industry specific regulators analyse any possible long-term and short-term consequences of their actions. This essential process undertaken by both will at times require trade-offs between consumers experiencing immediate price reductions and the development of stronger competition in the future.

Section 2 of the TPA sets out the role that was envisaged for Australia's competition agency. Originally, the duties of such an agency included the enforcement of the restrictive trade practices, part IV of the TPA, and consumer protection, part V, VA and VB of the TPA. The Trade Practices Commission performed these duties up to 1995 when the Competition Reform Policy Act was legislated. This piece of legislation saw the formation of the ACCC. The newly introduced legislation expanded the role of the regulator, including giving it responsibility for price surveillance, formerly undertaken by the Prices Surveillance Authority.[15]

The ACCC is responsible for economy-wide competition enforcement. Another of its roles is to administer consumer protection laws, which are primarily intended to protect the interests of consumers by prohibiting firms from misleading consumers under Part V of the TPA. The ACCC is also responsible for protecting small business through unconscionable conduct legislation under Part IVA of the TPA.

The ACCC also has regulatory duties which cover a small number of sectors where the Government believes the public interest is not being adequately advanced merely by private markets. The Government having decided to empower a regulator to directly supervise these industries, then allows the regulator to specify acceptable technologies, marketing methods and/or prices

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[14] Trade Practices Act 1974, 'PART I – *Preliminary*', s2.

[15] Standing Committee on Economics, Finance and Public Administration '*Competing Interests: is there balance? Review of the Australian Competition and Consumer Commission Annual Report 1999-2000*', Enforcement Issues, Splitting the ACCC (4.50), Pg 55.

charged.[16] Currently included in the ACCC's regulatory responsibilities are the Prices Surveillance Act (PSA), access regimes (Part IIIA) and the Telecommunications Access Regime (Part XIC).

Regulatory agencies generally have different objectives and requirements to economy-wide regulators. Listed below are some of the differences that contribute to a confusion of roles under the current ACCC structure.

Competition agencies are generally focussed on trying to reduce the effects of market power whereas specific industry or sector regulators will try to alleviate such powers. These opposing positions can deliver some differing views on the management of market power.

Regulators generally monitor and impose some behavioural conditions upon a particular sector whereas competition agencies will try to perform structural remedies. Regulation has an ex ante prescriptive approach and competition agencies have an ex post approach, with the expectation of merger provisions.

Sector-specific regulators typically intervene more frequently and require a continual flow of information from regulated entities, while competition offices rely more on complaints and gather information only when necessary in connection with possible enforcement action.

Regulators are generally set more specific and targeted roles than an economy-wide agency, whereby after a point in time the regulator has been deemed successful and regulation no longer being required, responsibility for the industry can be passed to the competition agency. These broader goals imply regulators are more adept at trading of opposing views[17]. However, it is generally accepted that small synergies may exist with economic-wide competition agencies and regulatory agencies working under the one umbrella.

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16 DAFFE/CLP(99)8, Directorate for Financial, Fiscal and Enterprise Affairs Committee on Competition Law and Policy, '*Relationship between Regulators and Competition Authorities*', 24 th June 1999, p18.

17 DAFFE/CLP(99)8, Directorate for Financial, Fiscal and Enterprise Affairs Committee on Competition Law and Policy, '*Relationship between Regulators and Competition Authorities*', 24 th June 1999, pp8-9.

If a particular sector is considered to require long-term regulation, then it may be better to allow a sector-specific regulator to control the market. Over time, the regulator will acquire all the necessary experience to enable it to effectively manage the industry compared to an economy-wide agency. The challenge for an economy-wide agency is to manage its conflicting agenda whereby it considers matters directly relating to business profitability while at the same time representing consumers whose short-term interests are often merely reflected in a desire to keep prices low.

One problem associated with industry specific regulators is 'regulatory capture'. While it is also a problem under an economy-wide agency, it is generally considered less so. In relation to an economy-wide agency, the motivation to continue in a regulatory capacity is not as strong, possibly due to fact that no loss of power or status is likely to occur upon cessation of the regulatory role. Given that the role for deciding when a particular industry is competitive enough to fall within the Restrictive TPA can be under the control of an external agency, the risk of 'regulatory capture' is not such a concern. The ACCC would then be able to relinquish its regulatory role to a sector-specific regulator, without fear of 'regulatory capture'.

The ACCC is not only a regulator in some industries and the economy-wide competition agency, but is also responsible of consumer protection. Consumer protection is used to ensure the availability of adequate information, fair treatment and avenue of redress to individuals. Given the diverse objectives and requirements of undertaking the dual roles of regulation and economy-wide competition, the question needs to be asked whether the one agency should do both jobs.

Price determination in a competitive market occurs through the interaction between firms and consumers. When the market fails to provide competition, it is the role of the government, through the ACCC's interpretation of the TPA, to create an environment conducive to fair trade. This particular role requires that the ACCC consider the welfare of Australians through the promotion of competition. The enhancement of welfare must be seen in the context of providing long-term welfare enhancing policy, not only in light of short-term price reductions.

Firms are particularly responsive to changes in market incentives. Decisions to undertake risky strategies such as investments in capital, research and development and innovation require the delivery of potential benefits in the long-run in order to establish a dynamically efficient economy.

American experience with competition policy has seen the formation of two agencies, the Federal Trade Commission (FTC) and the Anti-trust Division of the US Department of Justice (DoJ) with both responsible for the promotion of marketplace competition. The Federal Trade Commission is responsible for consumer competition through 'guarding the marketplace from unfair methods of competition and to prevent unfair or deceptive acts or business practices that harm customers.'

More specifically the FTC undertakes actions primarily under the Federal Trade Commissions Act, the Clayton Act and practices that 'violate the spirit' of the law[18]. The DoJ handles violations under the Sherman Act, usually involving criminal prosecutions, and is also responsible for special industry regulation such as airlines, railways and telecommunication matters.

In the United Kingdom, regulation is undertaken by the Office of Fair Trading whose objective is the enforcement of consumer and competition protection rules. The Competition Commission replaced the Monopolies and Mergers Commission in 1999. As such, the Competition Commission undertakes reporting duties, inquires into matters referred to it by other agencies and conducts the regulation of utility companies. The Competition Commission also hears appeals in respect of infringements of the prohibitions contained in the Act concerning anti-competitive agreements and abuse of dominant position.

The issues of whether it was preferable to have a single agency dealing with competition and consumer affairs within the same agency was dealt with by the Wallace Committee. In its Report, it made the following observations on this issue:

> 'A number of submissions to the Inquiry argued for the creation of a separate specialist consumer protection regulator because of the concern that consumer protection would otherwise become subservient to other objectives. However, this risk is more likely to arise where consumer protection is combined with the functionally different task of prudential regulation. The tasks of consumer protection, market integrity and corporations regulation are more complementary than conflicting.

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18 The Bureau of Competition Federal Trade Commission, '*Promoting Competition Protecting Consumers: A Plain English Guide to Anti-trust Law*', Preface.

> 'The Inquiry also considers that there is merit in establishing an agency which has a broader task than consumer protection in isolation to ensure that there is a balance of perspective in pursuing regulatory objectives.'[19]

The ACCC is currently a powerful organisation whose reach has managed to extend to all parts of Australia's competition policy. It is the role of the ACCC to interpret the TPA and using their understanding of competition and the Act prosecute actions believed to contravene the Act. An effective regulator is seen as independent from the government, but more so, objective on all issues. Objectivity in its decision making process will lead to a greater confidence in the regulator from both consumers and businesses.

Objectivity requires that an agency will not have to face a conflict of interest in terms of its decisions and in relation to whom it represents during those decisions. As a competition agency acquires more regulatory responsibilities, the potential for instances of conflict of interest are increased. Warren Pengilley has already provided an example in the Telecommunications Access Regime case, where the ACCC has to assess the rate of return in arbitration disputes. The ACCC is a consumer advocate and Telstra is seen as the 'enemy' so that fairness and impartially is perceived to be unattainable.

> 'Telstra would believe – and there is a lot to be said in the old adage that justice must not only be done but must appear to be done – that it could not get a fair shake out of the ACCC, because the ACCC has a consumer interest and it is going to balance it that way.'[20]

Another example of regulatory agencies working independently of the economy-wide competition agency is that of the Corporations and Financial Services Commission (CFSC). This recommendation was made during the Wallis enquiry which stated:

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19 Financial System Inquiry (Wallis Inquiry), Final Report '*Conduct and Disclosure, PART 2 Key Issues in Regulatory Reform*' Chapter 7 Summary pp 244-45.

20 Warren Pengilley, Submission 7 (supplementary), Standing Committee on Economics, Finance and Public Administration '*Competing Interests: is there balance? Review of the Australian Competition and Consumer Commission Annual Report 1999-2000*', p53.

> 'A single agency, the Corporations and Financial Services Commission (CFSC), should be established to provide Commonwealth regulation of corporations, financial market integrity and consumer protection.'[21]

This arrangement left the ACCC powers in tact, as jurisdiction over existing areas remained. The ACCC and CFSC then entered into an operating agreement to eliminate duplication of enforcement effort.

The role of consumer protection in the Wallis report stated that:

> 'The Committee accepts that the substantive consumer protection provisions of the TPA should apply to the financial system. However, it does not follow that the ACCC should administer these provisions in relation to the financial system once the CFSC is established.'[22]

The above statement is considered to strike an appropriate balance between industry specific regulation and an economy-wide regulator. Had the government taken such decisions in the past, there would not be in evidence presently such a growth in the powers of the ACCC.

Independence from government interference makes it difficult to strike a balance in terms of how accountable a competition-wide regulator should be to the public, not to business or politicians or consumers individually.

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[21] Financial System Inquiry (Wallis Inquiry), Final Report '*Conduct and Disclosure, PART 2 Key Issues in Regulatory Reform*' Chapter 7 Summary p245.

[22] Ibid p247.

ADDITIONAL POWERS SOUGHT BY THE ACCC

The current review of the TPA is the logical continuation of the Joint Select Committee's report on the Retail Sector that preceded the Inquiry into s46 and s50 of the TPA, which was undertaken by the Senate Legal and Constitutional Reference Committee.

Over this period, ACCI has followed the progress of the debate and contributed in an on-going manner. Having considered the arguments into the 'cease and desist', 'effects' test, reversal of onus of proof and divestiture, ACCI has concluded that the impact of the currently proposed changes to the TPA would be detrimental to the economy and to the business community. ACCI cannot support any of these propositions which have been put forward by the ACCC.

The role of the market is to reward those producers most capable of producing what consumers wish to buy, with businesses constantly vying for each other's consumers. Competition encourages entrepreneurial spirit, greater efficiency within the economy, greater productivity and lower prices. To obtain these goals, competition policy must have the ability to 'distinguish between desirable and undesirable activity while providing an acceptable level of business certainty.'[23] The currently proposed changes to the TPA will instead create needless uncertainty, harm business and not compensate efficiency.

In reference to 'cease and desist' and the 'effects' test, we consider the Australian Consumer and Competition Commission (ACCC) to have considerable powers already. The evolution of the ACCC has seen its responsibilities balloon from overseeing the restrictive TPA and consumer protection to wider ranging duties including: determinations under the access regime for telecommunications, arbitration of disputes of access to facilities of national interest and price surveillance and monitoring. These particular powers put the ACCC in a remarkable position with respect to consumer protection and competition enhancement.

The roles of consumer protection and competition enhancement can be viewed as a trade-off. On one hand, short-term price reductions are often mistakenly interpreted as consumer protection. However, when it comes to competition enhancement, this requires that one take a longer-term view through innovation incentives and ensuring that firms stay in the market.

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[23] Report by the Independent Committee of Inquiry (Hilmer Report) '*National Competition Policy*', August 1993, Pg 63.

The responsibilities of the ACCC also include regulation. This means Australia is not in line with international practices where regulation is generally carried out by multiple agencies. The United States for example, uses both the Department of Justice Anti-Trust Division and the Federal Trade Commission for Competition policy while in the UK the responsibility is shared between the Office of Fair Trading and the Competition Commission.

Some contributors to the current debate suggested that the 'cease and desist' orders and the 'effects' test be applied only to certain parts of the TPA or after certain action has been taken by the ACCC. Both the 'cease and desist' orders and 'effects' test have irreparable flaws that no implementation of different variations can fix. The proposed changes to the TPA would only increase the amount of uncertainty faced by business while at the same time widen the basis upon which the ACCC can prosecute. The amount of extra protection afforded to small business due to these changes has been overstated and in some cases the powers sought by the ACCC are already available to them through the courts. In terms of the protections sought by small business, virtually all of these are already available within the Act as it is presently found.

The ACCC and its predecessor the Trade Practice Commission (TPC) have argued in the past for such powers to be legislated[24]. Having been rejected on five previous occasions, in the case of the 'effects' test, ACCI would like to see the issue finally resolved so no further attempts are made to resurrect this debate given that the ACCC has not addressed the short comings of the 'cease and desist' orders and 'effects' test raised by previous enquires.

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[24]House of Representatives Standing Committee on Legal and Constitutional Affairs. 1989.
Mergers, takeovers and monopolies: Profiting from competition? (Griffiths). Canberra, AGPS, pp 29-
30 and 41; Senate Standing Committee on Legal and Constitutional Affairs. 1991. *Mergers,*
monopolies and acquisitions: Adequacy of existing legislative controls. (Cooney). Canberra, AGPS,
pp 81-86 and 96; Hilmer, J. 1993. *National Competition Policy: Report by the Independent Committee*
of Inquiry. Canberra, AGPS, pp 70-71 and 74; House of Representatives Standing Committee on
Industry, Science and Technology. 1997. *Finding a balance: towards fair trading in Australia*.
(Reid). Canberra, AGPS, p 132; and Joint Select Committee on the Retailing Sector. 1999. *Fair*
market or market failure. (Baird). Canberra, Parliament, p 100.

Under the current guidelines on competition policy, businesses come under scrutiny with respect to pricing policy if all firms' prices are the same. Collusion may be alleged, if prices are too 'low' implying vigorous competition or predatory pricing. If prices are too 'high', monopoly profits are suggested. Competition policy has begun to look like a bedtime story; prices are either too high, too low or just right.

Firms that have achieved dominance through internal growth and dynamic competition are no threat to consumers. A criticism of competition policy is that higher cost companies may indeed use regulation to stop their more competitive neighbours from exploiting their efficiencies. For example, if a competitor's price is rising then a less efficient firm is able to increase its prices, leaving little reason for less efficient firms to complain. However, there are incentives to use the courts if their competitor's prices are falling or if its sales and market share are increasing. This situation then becomes consistent with the alternative notion of competition policy protecting the inefficient.

The points alluded to above are not to say competition policy is unnecessary, only to remind policy makers of the possible implications of an overly restrictive regulatory regime. Regulation may come with its own set of costs and often it introduces inefficiencies through problems of asymmetric information and uncertainty.

The ACCIs concerns with the proposed changes can be summarised as follows:

- the amount of uncertainty introduced into the market because of these new powers

- 'cease and desist' orders would be implemented by the ACCC when they thought there was breach of the Act. There is no mechanism to gain a second opinion to establish the validity of the ACCC's action

- a firm's protection under the law will be diminished given the implementation of the 'cease and desist' order

- the Trade Practices Commission previously asked for the same powers and were rejected on the basis that an administrative body cannot exercise judicial power

- in the event it is needed, an injunction (under s80 of the TPA) which the ACCC already has the ability to obtain and the

Australian Law Review (ALR) concluded this could be received in 48 hours or less.

Implementing an 'effects' test would have permanent negative repercussions such as:

- its inability to distinguish between competitive and anti-competitive behaviour

- inferring market abuse from 'effects' only will in fact capture any improvements in productivity and investment in capital and plant and equipment. Companies may no longer feel compelled to continually improve their products or services

- since a business cannot usually anticipate in any detail the effects of its actions before it has taken any action, the uncertainty this creates whereby every business must fully understand all consequences before undertaking any action would be extremely large

- at present purpose can be inferred from actions taken. This does not require a 'smoking gun' document.

Consumer Welfare

One of the objectives of the TPA is to increase the welfare of Australians through the promotion of competition. In order to enhance the welfare of consumers some of the questions that arise, although not an exhaustive list include: broadening the range of suppliers of goods and services, better information as to what choices exist in the market place, understanding that consumers' interests are not only represented by static efficiency and how best to minimise the degree of regulation.

In order to define consumer welfare it is necessary to have an understanding of the notion of a consumer. Consumers are generally considered in the simplified context, a single person whose final demand use is not that of an intermediary nature. This simplification makes competition policy unbalanced and ineffective.

Consumers are many and varied; they may include individuals and households through to small, medium and large enterprises, farms and non-government enterprises. Adding to the complexity of consumer welfare is the idea that economies are not made up of 'consumers' and 'producers' interacting separately. Trading interactions span and integrate the various stages of production, so a

firm may be a consumer and producer simultaneously. Understanding that consumers affect and interact in and with all facets of the economy means that inefficient producers and uncompetitive markets will affect all areas of the economy and the welfare of all consumers.

Viewing consumers as heterogeneous implies that not all competition policy should be centred on a short-term lowest price policy. This kind of strategy in some circumstances may be palatable for the non-business community but is not beneficial for the longer-term welfare of the business consumer where investment in infrastructure and Research and Development (R&D) will suffer under a price orientated, short-term policy outlook.

With regard to the above statements we can say consumers are the drivers of competition with the incentive to find the best quality product or service at the lowest possible price. The better or more efficiently this process works in an economy the higher the living standard and welfare within that society.

Competition

Competition is a means, not an end in itself. It should be seen as a mechanism to enhance communal wellbeing and not as the goal itself. By promoting efficient regulation, we can improve market competition in Australia. Some of the questions that must be addressed by competition policy makers when formulating or changing existing legislation include:

- whether particular regulations are restrictive in terms of competition either in the establishment of new business or in daily operation terms

- does competition policy foster the use of innovation and the adoption of new technology

- do markets that provide the inputs needed to produce goods and services operate efficiently or will operate efficiently once competition policy is introduced?

When regulation of firms becomes overly restrictive or burdensome the resultant loss of economic efficiency leads to an over investment in either labour or capital due to the lower incentive to economise. Lack of vigorous competition results in higher rents for production and/or labour leading to higher wages, profits or prices than would normally be sustained under competitive markets. More is paid per unit while supply is reduced. There is less innovation

either managerial or technological. Some changes to competition policy introduce a high degree of uncertainty for small and large firms with significant market power and therefore reduce the incentive to invest in Research and Development (R&D) and Innovation[25].

The goal for competition policy makers and legislators should be to impose the minimum amount of restrictions on business and competition with respect to the objective of 'enhance[ing] the welfare of Australians through the promotion of competition'.

Market Economies

An understanding of the impact and mechanisms of a market economy is important when developing and implementing competition policy and legislation. There are many aspects of a market economy. Two roles of the market are firstly being to determine prices and secondly, allocate scarce resources through the use of incentive based reward systems. These are some of the factors that identify a market economy. Importantly, one must consider how the market sets prices and through this process allocates those goods and services produced. In many countries where economies are centrally planned, prices are determined not by the interaction of consumers and producers in the marketplace, but by governments and bureaucracies. Key factors of this process are outlined below.

Market based economies use private enterprise for the maintenance and development of society's welfare. In order to achieve welfare improvements, it is important that economic growth be nurtured and encouraged through flexibility, practicality and adaptability. Freedom in a market economy is the ability to choose a career, a particular job, and product and to risk present resources for future benefits. When regulation places a restriction upon these choices, our very own economic and personal freedoms are reduced.

In centralised economies, planners determine prices, distribution, technology and quantity. In decentralised economies individuals make the decisions and accept the risk in deciding the number and type of products they want to consume and produce.

[25] Regulatory Reform, Volume II: *thematic studies*, OECD, Paris, 1997, p. 9

Because of scarcity, producing an item will necessarily reduce the amount produced of another product. This change in production will occur when people believe they can make more profit from their venture than the current or next best alternative.

In addition, the notion of next best alternative can be applied to the consumption of goods and services. As individuals in the society make production and consumption decisions, a variety of products and technologies are developed and compete against each other with the 'best' one eventually adopted by the consumer. In this context, the 'best' one may mean the product that uses the least resources, is of the highest quality or is simply the most affordable.

The individual is responsible, not an economic planning committee, for determining prices in a market economy. This degree of flexibility allows prices to rise and fall as seen fit by the producer, thus allowing adjustments to market conditions to take place. These changes to prices allow people to recognise that profits are either falling or increasing, and this signal transfers information to other parts of the economy about when to enter or exit a particular market. It also sends a signal to producers to either increase or reduce production.

Allowing prices to be set within the boundaries of a market gives consumers the same opportunity to buy the expensive product, as long as they are willing to pay, or substitute to a product they find more attractive, with this trade-off between products helping to determine what is produced. On the production side of the economy, companies will make profits by continuing to make products that are demanded by consumers. Firms that continue to produce unwanted items will not recover the cost of production, leaving the option to improve their efficiency, change products or exit the market. At this point, the resources previously used to produce the unwanted products will be bought by somebody else and used to produce other (demanded) goods or services.

To stay competitive a firm must become efficient. To do so, the firm must produce at least the same amount of goods or output as its competitors with either less labour or capital, thus increasing the productivity of the firm or its workers. This efficiency will then produce goods of higher quality or lower cost. In short newer, cheaper and better products.

Higher production levels justify higher wages and living standards. Higher productivity means higher output per worker, which translates into greater prosperity that can be shared through higher wages and a better standard of living. Reducing costs and working more efficiently are ways of increasing productivity. In modern

technology-based economies, research and innovation are critical to the sustained productivity and growth of economies at both the national and global level.

Market competition brings allocative efficiency where inputs or resources are used to produce goods or services that are distributed to the highest value consumer. Productive efficiency gains are derived through the convergence of price and the marginal cost of a firm, which produces goods and services required by the economies consumers at the lowest or least cost. These type of gains, however, are not just reaped in the static sense (the most productive use of today's resources at least cost in terms of both production and consumption) they are also gained from dynamic efficiencies in the economy. 'Dynamic' efficiency is broadly defined as productivity growth due to innovation, the introduction of new production methods and goods and services demanded by the consumer. All these benefits to a market economy will raise living standards.

Dynamic competition also allows new firms with differing technology from the incumbent firm to enter and compete in the market. If the technology is successful then new entrants will replace the old players. Similarly, it new entrants fail, then they will exit the market. This type of competition not only challenges for the marginal profit but the position of preexisting firms. With substantial experience may come an aversion to newer methods of production, these risky ventures are generally the upper hand new entrants require and therefore the drives of innovation.

In some industries where technological changes are rapid and competition is 'destructive', dynamic efficiencies maybe more important in terms of welfare than static efficiency. Providing the necessary incentives for competition may require that market power, in the short-term, be granted to the firm who posses the innovation, although this does not imply a lack of competition.

Competitive markets are the best way to provide an efficient allocation of resources. They ensure that firms have incentives to use their inputs to increase variety and quality as efficiently as possible. Markets that work well therefore bring benefits to society such as greater productive use of resources, increased range of products, lower prices to consumers and a better quality of goods and services. Competition that increases efficiency in the domestic market will also have spillover effects with respect to international competitiveness.

The impact of competition policy cannot generally be analysed in the light of static efficiency gains in the short-run. Changes to competition policy have long lasting effects upon the market due to

the interaction between competition policy and the incentives available to a firm to continue to produce its goods and services efficiently. These incentives should encourage innovation and choose more efficient firms over less efficient firms in the long-run.

Market economies operate most efficiently when there are a large number of firms and consumers interacting, and thereby where none of the actors have the ability to affect prices and there is a market for every commodity. A consumer will pay the same as every other consumer in the economy, and all firms pay the same price for their inputs such as labour and capital. Deregulation, privatization and the introduction of greater competition into markets has, in general, reduced entry barriers, costs and prices and improved service quality and innovation.

This is evidenced in the United States where the introduction of competition into what were regulated industries has indeed led to reduced production costs, improved productivity and innovation, increased market entry opportunities, downward pressures on prices, greater product variety and better quality of service. Tangible benefits are seen in the form of annual increases of $32-42 billion in consumer welfare and $3.2 billion in producers' profits, which amount to a 7-9 per cent improvement to that component of GNP affected by the reforms[26].

Market Failures and the TPA

For the market to produce efficient outcomes, there must be competition, and although the results of market economies are desirable, there are some problems associated with a free market. In this respect, governments have a role in helping to correct problems that private markets cannot overcome. It should be stated that market failure is considered a necessary condition for government intervention but not a sufficient condition. If intervention, by a government is necessary, then the most important and difficult issues will be what are the most appropriate form and level of regulation. Inefficiency in regulation will ultimately produce the same problems as those encountered in an inefficient market.

In some situations where perfect competition does not exist there are different market structures in place. These can include oligopolies, monopolies or monopolistic competition. The Australian economy is generally viewed as containing monopolistic

26 Clifford Winston, '*Economic deregulation: Days of reckoning for microeconomists*', Journal of Economic Literature (1993), vol. XXXI, pp. 1,263-1,289.

forms of competition in different markets. Imperfections arise in markets due to incomplete and asymmetric information and the fact that transactions and information are not costless. These problems can manifest in various ways including the formation of barriers to entry and the formation of cartels.

Monopoly power is generally seen to manifest through barriers to entry, where firms wishing to enter a market cannot, even though to enter clearly represents an attractive proposition, as evidenced through the profits of the incumbent firm. If a firm could enter the market, the incumbent firm by definition, is no longer a monopolist. There are two types of barriers. The first are structural barriers (or economic) and the second are strategic (or behavioural).

Natural monopoly barriers, a type of structural barrier in markets generally requires production of a good to exhibit decreasing marginal cost over a wide range of output levels. A monopoly of this type will produce goods at a relatively low cost over large quantities and may not necessarily be confined to large markets. For example, if a producer in a small country town exhibits declining marginal cost then he may be able to form a monopoly. The essence of a natural monopoly is that one firm will be able to produce an amount of goods cheaper than would two firms. Natural monopolies can also be identified through their market structure where large fixed costs exist in tandem with a low marginal cost of production. Industries that require large sunk costs as occurs with respect to many infrastructure projects will have the necessary qualities for a natural monopoly.

That is not to say that benefits cannot be derived from a market economy in which there are fewer firms than previously existed. Instances where market concentration decreases competition such as mergers can still lead to greater efficiencies by allowing economies of scale or scope in production, organization or other activities. In these cases there remains the potential for such benefits to be passed on to consumers.

The significance of some barriers to entry is also debated in the economic world. George Stigler and the proponents of the Chicago school of antitrust analysis have given a narrower definition of structural barriers to entry than usually exists in some economic circles. Stigler et al suggest that barriers to entry arise only when an entrant must incur costs that incumbents do not bear. Therefore, excluded from their structural barriers definition are scale economies and advertising expenses as barriers (these costs are sustained by the incumbent and not just new entrants).

Structural economists emphasize the importance of sunk costs as a barrier to entry.

Since sunk costs must be incurred by new entrants, but have already been borne by incumbents, a barrier to entry may be inferred to exist. In addition, sunk costs reduce the ability to exit and thus impose extra risks on potential entrants. Incumbents in the market have already accepted these risks.

Legal barriers to entry in the form of patents also lead to the formation of monopoly markets for products that are generally uniquely designed by one company. This particular monopoly however, does have an advantage in the fact it encourages firms to take risks and innovate. Firms that do take such risks, invest in innovation and produce a new product can therefore expect and indeed should be entitled to, reap monopoly profits over the term of the patent. These potential monopoly profits are the incentives to develop better products and techniques. High profits from innovation may remain over time, as continual investment in research and development lead to higher returns on previous innovations and incentives to continually innovate.

A firm operating in a monopoly market may also wish to maintain its expected profit level and to do so will attempt to set up barriers to entry to its market. These barriers may be created through the purchasing of unique resources, lobbying and the maintenance of secrecy and all require the use of costly resources. A monopoly will tend to raise prices and cut output and through these decisions reduce the welfare of society.

The notion of predatory pricing has been around since Standard Oil in America began charging irrationally low (predatory) prices in the late nineteenth century. Although in this particular case, predatory pricing has been largely ruled out since it would have been rational and cheaper for Rockefeller to buy out the competition at market price rather than make losses across all output. Successful predatory pricing in the long run reduces the amount of competition in the market. Without competition, prices will increase, quality and choice are reduced and productivity remains stagnant.

The TPA is focused on many of the problems associated with market failure, monopolies and monopolistic competition. Other forms of anti-competitive behaviour include price fixing agreements, retail price maintenance (RPM), collusive tendering, customer allocation and ‘hard core’ cartels.

Price fixing agreements are designed to stop competition impacting upon firms in the same product market. They can be oral or written, formal or informal. Price fixing, anti-competitive behaviour may involve businesses in one off or isolated cases, or larger collusive agreements between enterprises entailing most activities undertaken by the members of the organisation involved.

Some examples of anti-competitive behaviour undertaken by an enterprise include collusive tendering, market allocation of customers, and sales and production quotas. Demand side collusion effects may include cartels, which enforce member's buying power.

Collusive tendering should be seen as illegal under any circumstance as it undermines the competitive nature of auctions. The purpose of inviting tenders is to attain prices for goods and services under the most favorable conditions. Collusive tendering manifests itself in many ways in the marketplace. Some of these include firms lodging identical bids, not bidding against each other, devising agreements as to who will submit the lowest bid, devising agreements on how to form prices or terms on bids, determining amongst themselves who the winners and losers will be, with the winners being allocated on a rotational basis or on a geographical or customer allocation basis. This type of horizontal cooperation (cooperation between competitors in the same market or engaged in broadly the same activities) should be considered under a general prohibition of anti-competitive behaviour.

Market or customer allocation involves the assignment to a particular company by other companies, which may be considered competitors, particular consumers of goods and services. This type of arrangement preserves the trading patterns of firms and undermines competition between different firms for markets and consumers, with such restrictions having an adverse impact upon a particular line of products, services or customers.

Restraint on production, sales and quotas are similar in principle to market and customer allocation whereby restrictions to competition are based on the quantity of a particular good produced. The object of these arrangements is generally to raise prices in markets where there is excess capacity although this is not exclusively the case. This agreement may be reached though agreeing to limit the number of sales to a proportion of the firm's previous sales.

A vertical restraint to competition is a commercial agreement between a supplier and buyer whereby the freedom of one or the other is restricted. Not all vertical restraints are considered to automatically breach the TPA, economists maintain that some agreements increase competition.

RPM occurs when a producer specifies the resale price of an item. This is generally given in the form of a minimum or maximum price. RPM also applies to businesses in different parts of the supply chain, not only the manufacturer and the retailer. The effect of fixing prices at either a minimum or a maximum is the stifling of horizontal competition between retailers of products.

Cartels have the effect of increasing prices and reducing output in a particular sector in order to lessen competition and raise profits. Consumers can either choose to pay the higher price, therefore transferring wealth to the cartel, or forgo consumption of the product. This type of market behaviour diminishes competition and thereby reduces the incentives to innovate and reduce costs.

Boycotts by companies that act as barriers to entry and disadvantage other firms already in the market or force a competitor to pay higher prices is in breach of the TPA s45. These types of boycotts should not be seen as competition in the market place and every effort to should be made to stop these practices which effect price competition, although under s45(8) and s45A, joint ventures and related parties are exempt.

The ability to gain exemptions from certain actions through the authorisation process shows a degree of flexibility required to conduct good competition policy. As economic theory and the economy changes, s88 allows the ACCC to produce the most relevant and specific policy. It also allows for a public benefit test to be applied when making decisions that may reduce competition but still enhance welfare through greater efficiency gains.

> "(1) Subject to this Part, the Commission may, upon application by or on behalf of a corporation, grant an authorization to the corporation:
>
> (a) to make a contract or arrangement, or arrive at an understanding, where a provision of the proposed contract, arrangement or understanding would be, or might be, an exclusionary provision or would have the purpose, or would have or might have the effect, of substantially lessening competition within the meaning of s45[27]

[27] Trade Practices Act 1974, 'PART VII – *Authorisations and notifications in respect of restrictive trade practices'*, s88 (1).

(b) to give effect to a provision of a contract, arrangement or understanding where the provision is, or may be, an exclusionary provision or has the purpose, or has or may have the effect, of substantially lessening competition within the meaning of s45."

Such principles of anti-competitive behaviour are not within the sprit of a fully functioning market economy. These arrangements, although not an exhaustive list, affect the entire economy, small and large business and consumers alike. As such their place within the TPA is invaluable and should remain.

Firms that have for any reason under their control the ability to influence prices or entry and exit to a market, will generally be considered to have market power and are therefore, in a position to potentially abuse that power. A firm that abuses market power does so with the intension of creating higher profits in an industry by either deterring entry or disciplining the prices of its competitors.

It is important to understand the distinction between monopoly power and market power. Monopoly power along with monopoly profits, given no barriers to entry, will encourage firms to enter a market and innovate in order to capture some or all of those profits. The use of market power for an anti-competitive purpose will reduce the number of firms entering the market and slow innovation in an industry.

It is important to note that however necessary government intervention may seem at certain points in time, there are serious risks associated with such actions. It is generally accepted that regulators work for the public good and are above reproach; however regulators do make errors and may have multiple objectives or personal agendas.

There are difficulties associated with regulation. Many of them are derived from the notion of information asymmetry where one or both parties do not have the same information on which to base an opinion or decision. For any regulatory authority therefore, it is difficult to judge whether actions by the incumbent firm were anti-competitive. Information pertaining to the cost structure of the firm will make it difficult to judge the intention of a low pricing strategy and recommend appropriate remedies. For example, predictions of future market demand will be impractical and unreliable due to the imperfect nature of information available upon which to base the decision.

A regulator must develop an understanding of the pricing structure of a firm in order to ascertain whether market power has been abused or if it is simply a case that competitive forces are responsible for reducing prices. Even where powerful enforcement legislation allows information to be gathered from a firm, regulatory uncertainty will not be entirely removed and business uncertainty will increase. Attempts that require firms to undertake account-keeping measures in order to reduce informational asymmetry do produce significant compliance costs.

Competition agencies and regulators have the potential to be 'captured' by the interests of other institutions and lobby groups. In such cases, a regulator is seen as no longer pursuing its original objective of promoting competition and consumer protection. Generally, capture of a regulator is undertaken by businesses through lobby groups applying pressure however this is not the only possibility of regulatory capture.

Many other institutions within an economy may in fact capture regulators. Governments have the ability to capture regulators, especially those that rely heavily upon government as a major source of income. Regulators may be captured by precedence where their credibility and reputation are dependent upon past decisions[28].

Independent competition agencies and regulatory authorities are a fundamental element for the effective implementation of the TPA. There must be, at least a perception of neutrality and insulation from political influence. This in turn, leads to confidence that a market will be regulated with transparency and objectivity, but this will also be dependant upon the credibility of the regulator or competition agency, which needs to demonstrate its ability to work in an impartial and professional manner[29].

The TPA is an important part of Australian legislation. Given the mechanisms of a market economy and the potential for market failure, there must exist transparent processes that allow all stakeholders to fairly and objectively scrutinise the operations of competition agencies and regulatory authorities. The current review of the TPA seeks to understand the role of competition policy within Australia and its effects on the welfare of society.

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28 Productivity Commission '*Telecommunications Competition Regulation*' Inquiry, Final Report, 21st December 2001, Chapter 2, p47.

29 Telecommunications Regulation Handbook, '*Overview of Telecommunication Regulation*', Module 1: http://www.infodev.org/projects/314regulationhandbook/ (accessed June 15th 2002)

Operations of the Market

A market regulator by nature has a very difficult job. He or she must strike a balance between determining what are anti-competitive actions undertaken by businesses on one hand, while on the other hand, not stymieing competition through the single-minded goal of deterring uncompetitive conduct. This requires lawmakers to be sure that regulation does not impose restrictions that tend to lessen competition and lead to higher prices. ACCI certainly agrees that some practices undertaken by firms with market power should be considered welfare reducing and therefore illegal. These concerns should then be viewed under the rule of reason by the ACCC, with individual cases taking precedence over the concerns of a regulatory framework that stifles competition.

Integral to the operation of the market and important to the welfare of all Australians is investment in Research and Development (R&D). R&D is considered to be a risky venture but is vital to maintaining and developing the competitiveness of a company both domestically and internationally. Any company considering whether to undertake an innovation-led strategy will either benefit from this investment or find no practical change in technology to increase either its market share or profits. A company's decision to undertake R&D in the first place is influenced by many factors such as, the ability to exploit any gains to the fullest if indeed the investment proves to be fruitful and the amount of regulatory barriers to the exploitation of R&D. Barriers to the investment in R&D should be not introduced into the TPA especially considering its importance to the nations competitiveness and welfare.

Restrictive information flows have detrimental effects on a market in the form of higher prices and lower service or product quality. Imbalances in information or asymmetric information not only occur between buyers and sellers it can also occur between businesses and regulators. Competition policy can improve the flow of information to consumers through the promotion of rights and standards. Competition policy should also reduce the amount of uncertainty faced by firms, as confusion in regulation policy will lead to the problems stated above.

Defining the Market

> *For the purposes of this Act, unless the contrary intention appears, market means a market in Australia and, when used in relation to any goods or services, includes a market for those goods or services and other goods or services that are*

> *substitutable for, or otherwise competitive with, the first-mentioned goods or services.*[30]

When interpreting the influence that changes to the TPA may have, it is important to understand the impact that different definitions of a 'market' may have and its effect upon the TPA's implementation. s46 promotes competition through the exclusion of some practices that have been deemed anti-competitive. A firm with market power shall not use that power for the purpose of:

(a) eliminating or substantially damaging a competitor of the corporation or a body corporate that is related to the corporation in that or any other market

(b) preventing the entry of a person into that or any other market

(c) deterring or preventing a person from engaging in competitive conduct in that or any other market.

The manner in which a market is defined is important to business, with respect to the implementation of regulation under s46. Defining the market therefore should be the first stage in any analysis of competition. The definition of the market a firm operates is a critical aspect of determining the boundary at which competition is considered to be taking place. It also impact upon the scope of regulation and affects the likelihood that regulation will or will not apply. The definition of a market is generally considered using two basic dimensions, product and geography. Disagreement between regulating bodies and firms usually centred around the size of a market. Firms prefer to define their market as broadly as possible thereby avoiding market power. Regulators will try to make the firms compete in a market as small as possible in order to establish market power and build a case for anti-competitive behaviour.

In relation to geographical considerations, issues that are more practical by nature emerge with respect to defining market size. These include transportation costs, perishability of goods and ease of transportability. These types of issues can lead to definitions of a market that includes small country towns, national borders to global markets.

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30 Trade Practices Act 1974, 'PART I – *Preliminary'*, s4 E.

In a recent case *Australian Consumer and Competition Commission v Universal Music Australia Pty Ltd [2001]* judge Hill stated:

> 'Market share is not irrelevant to the issue of market power, although on its own it is not determinative.'

Warner music had a market share of 15-18% and was judged to have market power. Furthermore, multiple firms may have market power. Decision in the courts, have over recent years, trended towards interpreting the existence of substantial market power as occurring when firms have had relatively low market share. The consequence of this type of action will inevitably subject more and more companies to abuse of market power legislation.

In some cases, the existence of market power has been determined by a lower court and is subsequently overturned on appeal in a higher court and visa versa as in the recent Boral case. This demonstrates the difficulties in determining which market a business in competing in. There is a range of methods to determine the market, each being used and given varied influence from one case to another. This highlights another problem that arises, particularly in relation to businesses that feel they have no market power, who will invariably be caught up in s46 proceedings without understanding their obligations.

Definition of a Market – Legal Aspects

A pivotal element of the TPA is the definition of 'a market', especially relating to conduct under Part IV of the Act (for example, 'misuse of market power': s46; 'substantial lessening of competition in a market': s50).

The TPA at s4E provides a definition of 'a market' as being 'a market in Australia' for any goods or services 'that are substitutable for, or otherwise competitive with' other goods and services. Judicial authorities have clearly, and repeatedly, stated that identification of a market in practice is, ostensibly, a question of economics.[31] For example,

> 'A market is the area of close competition between firms or, putting it a little differently, the field of rivalry between them…. Within the bounds of a market there is substitution – substitution between one product and another, and between

[31] *Re QCMA and Defiance Holdings (1976) ATPR 40-012; Singapore Airlines Ltd vs Taprobane Tours WA Pty Ltd (1991) 33 FCR 158; TPC vs Australian Meat Holdings Pty Ltd (1988) ATPR 40-876*

> one source of supply and another, in response to changing prices. So a market is the field of actual and *potential* transactions between buyers and sellers amongst whom there can be strong substitution, *at least in the long run*, if given a sufficient price incentive.
>
> 'In the language of economics the question is this: From which products and which activities could we expect a relatively high demand or supply response to price change, ie a relatively high cross-elasticity of demand or cross-elasticity of supply?'[32] (Italics added.)

This judgement recognises implicitly the dynamic nature of markets where in terms of competition it is the potential for others to begin competing and that a longer-term perspective is required.

The Courts have identified a number of characteristics to be taken into account in determining the structure of a market, and whether corporations are in competition with each other. These include: the degree of market concentration; the height of barriers to entry; the extent of product differentiation and sales promotion; vertical integration between suppliers and vertical relationships between sellers and buyers; and, formal relationships which restrict the ability of sellers and buyers to act as independent entities.[33]

Nevertheless, the Courts still accept there can be a degree of judicial discretion, even subjectivity, in determination of a market, stating that '(it) involves value judgements, about which there is some room for legitimate differences of opinion …. The outer limits … of a particular market are likely to be blurred.'[34]

Even so, the Courts have still recognised such considerations must be framed in the light of commercial realities.[35]

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32 *Re Queensland Co-operative Milling Association Ltd; Re Defiance Holdings Ltd (1976) 35 FLR 169* at 190*;* quoted with approval in *Queensland Wire Industries Pty Ltd vs Broken Hill Proprietary Co Ltd (1989) 167 CLR 177; 63 ALJR 181*

33 *Re Queensland Co-operative Milling Association Ltd; Re Defiance Holdings Ltd (1976) 35 FLR 169;* see also *Re Tooth and Co Pty Ltd; Re Tooheys Ltd (1979) 39 FLR 1; ATPR 40-113*

34 *Queensland Wire Industries Pty Ltd vs Broken Hill Proprietary Co Ltd (1989) 167 CLR 177,* per DeaneJ at 195-196

35 *Re Queensland Independent Wholesalers Ltd (1995) ATPR 41-438; Australian Meat Holdings Pty Ltd vs TPC (1989) ATPR 4-932*

Overall, the current approach taken to the definition of 'a market' in the Act, and related judicial authorities, as sound and appropriate. As such, there appears to be no need, at this time, for any legislative amendments to s4E. What does need to occur, however, is closer recognition by the ACCC of the dynamics of 'potential' competition and that the longer-run considerations are the appropriate time dimension.

Cease and Desist

The power to enforce 'cease and desist' orders is currently being sought as an addition to existing legislation by the ACCC. The addition of 'cease and desist' orders would allow an administrative body to order companies to halt their current actions. The 'cease and desist' orders will be issued in the belief that a company is abusing its market power. 'Failure to comply with this formal administrative injunction would be punishable by the Federal Court.'[36]

The uncertainty of this proposed legislation is exacerbated in the absence of clear guidelines as to how a belief or reason to believe that a company is/has engaged in anti-competitive conduct is formed by the ACCC. For example, will an anonymous letter be enough for a 'cease and desist' order to be exploited. This type of benchmark would be far to low a hurdle for any reasoned consideration for the implementation of 'cease and desist' orders.

As a justification for acquiring 'cease and desist' orders, the ACCC puts forward the view that businesses must not be allowed to benefit from the abuse of market power from the period of implementing proceedings to the determination of wrong doings by the courts. The ACCC believes that other avenues have to be looked at so that proceeding or actions can be sped up. 'Cease and desist' powers could be used in cases where 'blatant anti-competitive conduct' is being undertaken. The problem with this argument is that the ACCC must still investigate the allegation and collect evidence to come to the belief that market power is being abused. When the ACCC has formed a belief that that a company is abusing market power only then will the 'cease and desist' order be applied.

36 Australian Law Reform Commission '*Compliance with the Trade Practices Act, 1974',* Administrative Powers, 'Cease and Desist' orders Sydney, ALRC 68.

> 'Cease and desist orders would provide a means of stopping anti-competitive conduct quickly and avoiding irreversible damage to markets while matters are fully investigated and pursued through the judicial process.'[37]

The benefits to the community and to competition in general of legislating 'cease and desist' order should not be overstated, given that time and other ACCC resources would still be required in order to gather evidence against a company. After satisfying themselves there is a case to pursue, natural justice would still need to prevail whereby a company could defend itself against such accusations. After having seen the accusations, companies will require time to digest the charges to be brought against them and state their case. This process of natural justice may in fact increase the length of time in which 'cease and desist' orders can be implemented in comparison with the time required to obtain a Federal court injunction.

> 'The allegations raised highly complex issues of trade practices law. In December the Federal Court determined that Safeway had not breached the Act. In this decision, Goldberg J. found that, although Safeway held a substantial degree of market power, it did not take advantage of such power for a purpose proscribed by s.46. Broadly, he regarded Safeway's behaviour as pro-competitive'[38].

With respect to 'cease and desist' orders the ACCC states that its ability to enforce the TPA would be enhanced, as companies could not gain benefit from reduced competition during the period before the court hearing. 'Cease and desist' orders have been sought previously by the Trade Practices Commission and rejected. The Hilmer Inquiry also rejected this proposal in 1993.

> 'In instances where there is an urgent need to prevent particular conduct, the competition authority may seek interim injunctions to preserve the status quo pending a full hearing. Overall, the Committee is not satisfied of the need for such additional remedies.'[39]

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37 Speech by Allen Fels to Food and Grocery Council '*Retail Groceries and Food: A perspective of the Australian Consumer and Competition Commission*', Sanctuary Cove, 11 May 2002.

38 Speech to Food and Grocery Council '*Retail Groceries and Food: A perspective of the Australian Consumer and Competition Commission*', Sanctuary Cove, 11 May 2002.

39 Report by the Independent Committee of Inquiry (Hilmer Report) '*National Competition Policy*', August 1993, Pg 168.

The Australian Law Reform Commission (ARLC) found that enforcement tools, such as urgent judicial injunctions and enforceable undertakings under s80 of the TPA from the Federal Court, already allowed the ACCC to respond quickly and effectively to contraventions of the TPA. The ALRC reported that the ACCC could obtain an interim injunction in less than 48 hours and recommended against the granting cease and desist powers.

> 'The availability of judicial injunctions on short notice and the existence of s87B undertakings make a cease and desist power unnecessary'.' The Commission considers that cease and desist orders are not as quick and efficient an enforcement mechanism as their supporters argue.'[40]

The Hilmer Inquiry reached the same conclusion with respect to 'cease and desist' orders. It also described such orders as being particularly harsh where complex economic matters are involved.

> 'Cease and desist orders effectively reverse the onus of proof, which could be particularly harsh where complex economic matters are involved, as is often the case in competition cases.'[41]

If complex matters are involved it would be difficult for the ACCC to have the appropriate information with which to form a belief let alone make a decision. This problem is due to information asymmetry, where a firm has all the necessary information to make its decision but the ACCC does not have enough information to analyse the firm's decision. Information asymmetry will generally lead to incorrect conclusions on the part of the ACCC. The burden of excessive compliance costs and uncertainty leads to substantial welfare losses in the economy for firms and consumers alike.

Interpretation of the TPA by the ACCC makes it difficult for business to be certain when and where its actions may be understood by the ACCC to be in contravention of the Act. Businesses invest time and money in making strategic decisions with the intent of receiving rewards in the form of higher profits or greater market share. Consequences from such decisions are difficult to judge. A rival going out of business may or may not

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[40] Australian Law Reform Commission '*Compliance with the Trade Practices Act, 1974',* Administrative Powers, 'Cease and Desist' orders Sydney, ALRC 68.

[41] Report by the Independent Committee of Inquiry (Hilmer Report) '*National Competition Policy*', August 1993, Pg 168.

have been a result of the first firm's action. Nobody doubts that the economy is a place of complex interactions between an almost limitless numbers of players but this market structure makes causality and correlation difficult to distinguish. Although it is the goal of business to take customers from competitors, the difficulty is determining just who is responsible for the actions that send a firm out of business and whether such actions were premeditated. A firm with market power making a vigorous strategic decision is not necessarily responsible for the downfall of a competitor, to the extent a firm may be responsible for its own downfall. Causality must be decided in a manner that gives full consideration to the complexities of the issue at hand.

With the increasing breadth of powers available to the ACCC the power to order 'cease and desist' notices will give an unelected public department, that has as it purpose administrative duties and judicial powers. The circumventing of the judicial process cannot be allowed to take place when dealing with an institution that has at its purpose public service. This power, through a court injunction under s87(B), already exists as a matter of course and is readily within the reach of the competition regulator. Gaining 'cease and desist' orders may have the effect, through the expectation of natural justice, of slowing down legal proceedings, a result not in the interest of consumers, small, medium and large enterprises or indeed the ACCC.

The idea of natural justice when dealing with matters such as 'cease and desist' effectively reverses the onus of proof. This leaves the ACCC in a position of unprecedented power held by a non-elected administrative body. After the ACCC forms the belief that an abuse of market power has occurred, it will be necessary for a company to prove otherwise. The role of the ACCC with respect to 'cease and desist' orders will become one of accusing the company and then standing in judgment of it own decision, under the notion of natural justice prevailing. Effectively the ACCC will be asked to change its own mind with respect to its earlier decision and accept that it was wrong to believe an abuse of market power was occurring.

Competition is vigorous. Small firms and large are constantly removed from the marketplace due to both their own actions and those of their competitors. A large proportion of failures take place because one firm is just not as efficient as another. Costs begin to rise relative to newer competitors that have entered the market or old competitors have made better strategic decisions. This is how an economy should work. Investment will also suffer under a regulatory regime that uses reversal of onus of proof by stealth, as companies will constantly be subjected to the inquiries of the ACCC.

This depth of involvement in the economy will deter companies from undertaking an aggressive marketing campaign or from introducing a range of new and better products. The threat of 'cease and desist' orders will influence a company's decision as to how vigorously to compete. In essence, a company will not only have to predict the future success of any strategic decision but also predict the logic and reaction of the ACCC to these new competitive conditions. This again leads to the problem of asymmetric information, whereby the ACCC has information on what it considers legitimate behaviour but the company does not. Commercial decisions will become based not only on commercial uncertainties but also on regulatory uncertainties. Regulation now becomes a source of market inefficiency.

The ability to order 'cease and desist' action gives the impression to the community, through possible statements to the media, that the company is guilty long before a court of law has been able to assess the guilt or innocence of the firm. This type of cost, in the form of damaged reputation, cannot be recouped through financial means alone, due in part to the difficulty in estimating such costs. Businesses put time and money into developing brand images and that for the few misschosen words can be tarnished.

If 'cease and desist' orders are considered to be valid at the moment of issue, a company may, if it decides to contest the order, go to court and seek a review. If the court upholds that the company did not act in any way to abuse its market power, then compensation would be sought from the ACCC. Due to the connected nature of a market economy whereby large companies are customers to small suppliers, this litigation may filter down through the supply chain. The consequences for smaller market players are potentially dire. The ACCC may also be adversely affected due to the potentially high costs of litigation.

With respect to the above point, consumers may also wish to state their case if actions proscribed by the ACCC result in price increases. This situation would lead to large compliance costs for the government, which increase in proportion to the length of the court case.

Giving the ACCC the ability to issue 'cease and desist' orders does not respect the fundamental distinction between adjudicator and investigator. This is also inconsistent with the fundamental laws of justice, and ensuring the impartially of the decision-maker. Giving the ACCC powers to issue 'cease and desist' orders may very well rest with one person, the head of the ACCC, and this should be considered as giving one person too much power. A similar point, giving an administrative body judicial powers, was made by the

Attorney General's Department in the Senate Standing Committee on Legal and Constitutional Affairs (1991) and it advised against such measures.

Many issues as yet unanswered would need to be clarified before 'cease and desist' orders are legislated. Will the ACCC dictate the new action to be undertaken by the firm? Is the ACCC responsible for the new pricing policy if market power abuse takes the form of predatory pricing contraventions of the TPA? After the alleged incident has taken place and deemed by the administrator to be a misuse of market power will the firm be expected to act in a manner consistent with that of the market conditions prevailing before the suspected action? How far back will the company be expected to go when implementing business changes and will dynamic changes to the economy be taken into account when referring to amendments to a firm's strategic policy?

Cease and Desist – Legal Aspects

The ACCC has called for 'cease and desist' powers to be included in the Act. In effect, the Commission is proposing it be granted a quasi-judicial power to issue injunctions. The clear implication of this argument is the current arrangements under s80 of the Act, where injunctions must be sought from the Federal Court of Australia, are inadequate, and/or the Court is deficient in the exercise of its powers.

In this context, it is useful to review the existing legislative arrangements and judicial authorities for the issuance of injunctions. Section 80 of the Act states the Federal Court of Australia may issue an injunction in such terms as it determines appropriate where it is satisfied a person is engaged, or is proposing to engage, in conduct which would breach a provision of (*inter alia*) Parts IV or V.

Such conduct could also involve: attempting; aiding, abetting, counselling or procuring a person; inducing or attempting to induce a person; being in any way, directly or indirectly, knowingly concerned in or party; or conspiring with others, to contravene such a provision (s80 (1)(b) to (f)).

Importantly, the applicant for an injunction may be the Commission 'or any other person' (s80(1), excepting for injunctions under ss50 and 50A, relating to mergers, where only the ACCC can seek

injunctions). The Courts have afforded very broad definition of 'any person' (and hence standing to seek injunctions).[42]

The Court can also grant an interim injunction pending the determination of an application under s80(2). The Court in granting an interim injunction does not need to be satisfied the person intends to engage or continue to engage in the conduct of that kind, or there is imminent prospect of substantial damage to the complainant (s80(4)).

The essential 'cease and desist' nature of injunctions in trade practices matters has been recognised by the Courts: 'A statutory provision that enables an injunction to be granted to *prevent* the commission of conduct that has never been done before and is not likely to be done is a statutory enlargement of traditional equitable principles.'[43] (emphasis added)

Furthermore, the Courts have indicated a willingness to embrace 'public interest' as grounds for granting injunctions: where 'in an application under Section 80 a breach of Parts IV or V is shown, it will often be in the public interest that an injunction under s80 be granted whatever the interest of the applicant in bringing the suit'.[44]

Also: 'an applicant for an injunction under s80 need not show that a proprietary interest of his is affected, or that he has suffered special damage or, indeed, that he has suffered any damage at all.'[45]

The powers of the Courts under Section 80 of the Act, and associated judicial authorities, to vest real and effective 'cease and desist' powers in the Federal Court of Australia, are appropriate and should not be changed. As the Act states, 'any person' can seek an interim injunction for a broad range of conduct, actual or potential,

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[42] *R vs Judges of the Federal Court of Australia; Ex Parte Pilkington ACI (Operations) Pty Ltd (1978) 142 CLR 113* per Murphy J

[43] *ICI Australia Operations vs TPC (1992) 38 FCR 248,* Lockett J at 256-257.

[44] *Phelps vs Western Mining Corporation Ltd (1978) 33 FLR 327,* Bowen CJ at 332; see also *Glev Pty Ltd vs Kentucky Fried Chicken Pty Ltd (1994) ATPR 41-299;* see also *Insurance Commissioner vs Australian Associated Motor Insurers Ltd (1982) ATPR 40-299* per Northrop J; *Glev Pty Ltd vs Kentucky Fried Chicken Pty Ltd (1994) ATPR 41-299*

[45] *World Series Cricket Pty Ltd vs Parish (1977) 16 ALR 181; ATPR 40-040* per Bowen CJ; *Phelps vs Western Mining Corporation Ltd (1978) 33 FLR 327; Morey vs Transurban City Link Ltd (1996) ATPR 41-492; Truth About Motorways Pty Ltd vs Macquarie Infrastructure Investment Management Ltd (2000) 169 ALR 616; (2000) HCA 11*

direct or indirect, which could be in breach of Parts IV (restrictive trade practices) or Part V (consumer protection) of the Act; standing is also allowed to a person expressing a 'public interest'.

Against this background, and consistent with our strong opposition-in-principle to the ACCC being 'policeman, prosecutor and judge', the Australian Chamber of Commerce and Industry strongly opposes vesting the ACCC with 'cease and desist' powers.

There is no coherent, let alone sufficient or persuasive, evidence the existing legal processes relating to the granting of injunctions is inadequate. That is, that the Federal Court of Australia has not been proven deficient in performing this vital function.

Effects Test

The ACCC as a matter of consideration wishes to enhance its regulatory power through an 'effects' test applicable to s46 of the TPA due to problems with proving purpose even when 'the conduct appeared to have anti-competitive effects'.[46] These statements by the ACCC in their submission to the inquiry into the TPA do not appear to be in line with the facts, as recent success in prosecuting companies by the ACCC shows.

Any unilateral breach under an 'effects' test will be considered illegal if actions taken by a firm with market power have the effect of significantly lessening competition. The application of an 'effects' test will broaden and significantly strengthen s46 of the TPA. This will lead to increased intervention in the marketplace and thereby increase the risk of capturing legitimate business transactions through the prosecution of more cases. An 'effects' test will also change the strategic behaviour of firms by making it more difficult to avoid confrontation with the ACCC, reducing a firm's incentives to compete through price changes so not to be seen as affecting their competitors or the marketplace. These are a few problems with expanding s46 beyond its reasonable limit of defining what is and what isn't competition.

The ACCC and its predecessor the Trade Practices Commission (TPC) have sought these powers numerous times in the past without success. Previous reviews considered the argument for the 'effects' test but remained unconvinced with the major reason being its inability to distinguish between competitive and anti-competitive behaviour.

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[46] Ibid

> 'Such a test in the committees view, constitute an improvement on the current test. It does not address the central issue of how to distinguish between socially detrimental and socially beneficial conduct'.[47]
>
> 'The Committee accepts that in a provision directed explicitly at misuse of market power it is appropriate that a distinction between purpose and consequence be retained.'[48]

An 'effects' test by its nature looks into the cause of events, it sees an effect on the market and then attributes a cause to that effect. Interaction within the economy is extremely complex. Deciding what is a causal effect and what is simply a correlation can be a difficult task even in small isolated markets. A firm's decision to cut prices or enter into a vertical agreement with a supplier, or the fact a competitor goes bankrupt or leaves the market, does not imply one caused the other. If indeed some amount of causality were proved, what would be a sufficient amount to consider a firm responsible for the effects upon a competitor and the market? How much responsibility will be placed on the decisions taken by a competitor? More importantly, causality does not mean nor can it determine that was the intension of the larger firm and intent is a defining characteristic between competitive and anti-competitive behaviour. Businesses with market power might have no comprehension of the effects their decisions have on smaller companies in a competitive environment, nor should they be required to take these factors into account during the strategic decision-making process.

The concept of causality is important to this debate. With an 'effects' test in place competition policy is asking businesses to undertake predictions about the effect their actions have on their competitors and potential competitors. Indeed a company is uncertain, to varying degrees, of the effects their own actions have upon themselves. To consider other players in the market is asking business to make judgements they are often incapable of making. Forecasting a competitor's next move and the effect it will have to your business is a monumental task in itself. Add to this, changes to your business plan and its interaction with a competitor, judging the effects makes for an informational impossibility. To judge anti-competitive behaviour under such circumstances makes the chances

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47 Report by the Independent Committee of Inquiry (Hilmer Report) '*National Competition Policy*', August 1993, p168.

48 *Mergers, monopolies and acquisitions: Adequacy of existing legislative controls.* (Cooney). Canberra, AGPS, p66.

of reaching a spurious conclusion inevitable, thus making such an idea utterly impractical.

The notion of causality and correlation presents a major hurdle when using the 'effects' test to impose notions of what is competitive or anti-competitive behaviour. When combined with uncertainty in the business sector about the possible outcomes of strategic decisions upon their own welfare and others, the potential for regulatory error becomes a significant factor in limiting economic efficiency and welfare. With such a broad and imprecise test, the chances of making a mistake in the form of prosecuting an innocent business increase. Under an 'effects' test suspicion will fall on a great number of firms and it will be more difficult to prove that anti-competitive effects were not the result of an abuse of market power. The 'effects' test then loses the power to discriminate between competitive and anti-competitive actions.

The question then becomes one regarding the costs to making these types of judgements. In one case it is not prosecuting a firm that is abusing its market power. The costs of punishing competitive behaviour however, have a far greater reach in terms of static and dynamic efficiencies. The likely economic effects are evaporating the incentives firms have to compete, the burden of excessive compliance costs and uncertainty leads to a less competitive environment for firms and consumers alike. There are always trade-offs when making new legislation. This particular change to the TPA however, will have the opposite effect on competition throughout Australian industries and this will reduce the welfare of all Australian's.

Section 46 is and should remain about the exploitation of market power, which is damaging to competition. It should not concentrate on the damaging effects of competition itself. Where strong and aggressive competition does exist this will have an effect on marginal competitors, but so long as market power is not abused, through specifically identified forms or action, we can consider this normal robust competition. An 'effects' test does not have the power or ability to distinguish between these fundamentally different forms of competition. Competition in economics is developed and strengthened through incentives to firms to do better than their competitors and reap the rewards of higher profits and/or greater market share. However, any policy that reduces these incentives to outperform their competitor will reduce competition itself. ACCI believes this is the inevitable consequence of an 'effects' test upon competition in the Australian economy.

As it currently stands, under s46, the purpose test is unlikely to result in the prosecution of a company through the unintended

consequences of its actions. The use of purpose therefore adds a degree of certainty to business decisions. On the other hand, introducing the 'effects' test makes it more likely that unintended consequences will be punishable and that firms will be caught up in unnecessary, costly and time consuming legal deliberations. This will only increase the amount of uncertainty and does not give firms an incentive to compete vigoursly.

Recent court decisions have lowered the hurdle for prosecution under s46.[49] Determining the purpose of a company's action no longer requires the 'smoking gun' documents suggested by the ACCC. Purpose in the cases recently prosecuted by the ACCC has not been an issue.

> 'The High Court adopted a more expansive view of Section 46 than in the past. The hurdles that have to be got over have been lowered significantly by the High Court.'[50]

The issue of purpose was addressed in the Cooney Committee report where it was acknowledged that proof of purpose does pose difficulties to both the ACCC and private litigants, although it considered these issues to have been address in 1986 with the addition to the TPA of s46 (7) and 84(1). These alterations allow purpose to be inferred from the actions of corporations meaning that purpose may be established through the effect of actions, although purpose would still need to exist.

Purpose can be inferred if a corporation does not offer a 'legitimate reason'. This interpretation negates, to some extent, the ACCC's burden of finding and the need for a 'smoking gun' document. These changes have also made proving predatory pricing easier, particularly for private litigants but also for the ACCC.

In the *Melway Publishing Pty Ltd v Robert Hicks Pty Ltd* [2001] case, a firm may have abused its market power if it can be shown to have done something that is materially facilitated by the existence of power, even though that conduct may not have been absolutely impossible without power.

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49 (a) Melway Publishing Pty Ltd v Robert Hicks Pty Ltd (2001) 178 ALR 253; (b) ACCC v Boral Ltd (2001) 106 FCR 328; (c) ACCC v Rural Press Ltd (2001) ATPR 41-804; and (d) ACCC v Universal Music Australia Pty Ltd (No 2) [2002] FCA 192.

50 Standing Committee on Economics, Finance and Public Administration '*Competing Interests: is there balance? Review of the Australian Competition and Consumer Commission Annual Report 1999-2000*', Enforcement Issues, Effects Test (4.29), Pg 50.

The ACCC's apparent lack of success being due to the absence of a 'smoking gun' document does not tell the whole story. The ACCC under Sections 155 and 156 of the TPA have very powerful, effective and unique weapons to maximise its chances of obtaining a 'smoking gun' document. The Act gives the administration body the power to require a person that is believed capable of giving information, documents or evidence that relate to contraventions of the TPA to come before them. It also allows officers of the ACCC to enter the premises of a company and inspect any document under the control of a person that may have contravened the TPA. s156 allows for the extraction or copy of such documents related to the 155 notice. This power is available only to the ACCC and gives them a decided advantage over private litigants.

This particular power was upheld and strengthened in ACCC v Daniels (16 March 2001). Where the Federal Court held a person cannot refuse a request for documents made by the ACCC pursuant to s155 of the TPA, on the grounds that the requested documents are subject to common law legal professional privilege.

When undertaking an analysis of economic efficiency, in light of market intervention, it is important for the regulator to consider both types of efficiency promoted by competition. Firstly, static efficiency is considered to be the optimal use of current resources at least cost. Secondly, dynamic efficiency refers to the optimal introduction of new products, more efficient production processes and better organisational structures over time. Dynamic competition is probably the most important and beneficial effect of competition. However, some of the trade-offs to reach better dynamic efficiencies may be greater than those of static efficiency. Policies by regulators aimed at creating greater dynamic competition are generally more complex to introduce and also require there is no reduction in market incentives.

Profits are likely to be reinvested in innovation efforts. There may also be a trade-off between static and dynamic efficiency, and between short-term and long-term consumer welfare. Companies need profits over the traditional marginal cost to reimburse the costs of past R&D ventures and to fund future research endeavors. New product markets must be vigorously defended so money can be recouped from often large and risky investments in R&D. The development of a new product market through R&D automatically guarantees market power. Combined with the use of patents, a firm has the ability to control and set prices. Improvements in a product will have an effect on competition when to people substitute away from the older product and into the newer improved one offered by a competitor. An 'effects' test will not have the power to discriminate and compensate firms for pursuing an R&D agenda.

The Blunt Committee also concluded that an 'effects' test would stifle competition that lead to improvements in efficiency and products and therefore would not enhance Australia's welfare. They also acknowledged this new and improved product or technological market would cause some competitors to fail.

There also exists the possibility competition policy with an 'effects' test will be used by litigants who are unable to compete in the market, as protection from a stronger competitor. This type of outcome should never be possible using the very legislation designed to protect competition not competitors. The benefit of current s46 legislation where purpose is the primary determinant of guilt is the ability to prevent the marginal competitor from using anti-competitive laws to compete.

The Chamber views the 'effects' tests inability to distinguish between anti-competitive effects and competitive effects and the degree of uncertainty it introduces into the market as unacceptable and does not wish to see the 'effects' test introduced.

An Earlier ACCC View on the Effects Test

Allan Fels, Head of the ACCC, delivered this address when he appeared before the Joint Committee on the Retailing Sector on the 13th July 1999. It is interesting to note some comments he made about the effects test at that time.

> 'Some points against an effects tests are that it is a considerable strengthening of section 46 and it would be too intrusive and too interventionist for many tastes. Over the years there is no doubt that parliament and governments of all persuasions have not wanted to take that step of putting an effects test into the act, because they have just felt it would go too far. The purpose test, with all of its imperfections, is a way of making sure that section 46 is not carried too far. There are dangers in taking section 46 too far, because one always has the problem that it can deter genuinely pro-competitive behaviour. Just take the famous price cutting matter. There is always an issue as to whether price cutting is good for consumers. On the face of it, one would think so. But an effects test could take the edge off the incentive for firms to compete keenly on price and other dimensions.
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> 'It is also likely to create greater uncertainty for business. That is compounded by the fact that section 46 in its present form, because it has a purpose test, is far less likely to catch unintended behaviour. In other words, a firm may innocently

> be competing and unknowingly breaching a section 46 effects test. So firms may unintendedly do anti-competitive things – the big fish wags its tail and, without knowing it, wipes a small player and, in doing so, breaches the law. So there is that kind of consideration.
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> 'Another matter is that under section 46 there is the right of private action. So, every time section 46 is strengthened you get a double effect. You get more vigorous enforcement action, because if the commission did not act – and there a number of reasons why we do not act – then you may get more private actions. If you are, so to speak, a hawk on this matter, you will be delighted at the prospect that there would be a lot of private action under section 46. But it is also possible that actions under section 46 can be used for tactical and anti-competitive reasons to stop competition. So there are some concerns about the private uses that can be made of section 46 if taken too far.'[51]

Through his address, Professor Fels illustrates some of the intrinsic problems associated with the introduction of an 'effects' test. Indeed, the business community has understood many of the problems since the Griffith's committee held the first enquiry into the TPA in 1989. The first and most important point made by Fels is that an 'effects' test can deter perfectly legitimate, pro-competitive behaviour. The ACCC holds responsibility for the protection of competition, yet ironically it is the initiatives of the ACCC that pose the greatest threat to such activity.

In his 1999 address, Professor Fels alludes to another important point, that businesses will be under a cloud of uncertainty if an 'effects' test is ever introduced through its capture of unintended behaviour. However, the fact that small businesses are sometimes removed from the marketplace does not mean that 'big' business or the 'big end of town' is out to eliminate all opposition through illegal means, as he seems to be implying at present. The 'unintended behaviour' to which Fels refers in his address, is less likely to be prosecuted under a purpose test. Moreover, the effects test will lead to competitive and successful businesses being wrongly convicted for anti-competitive behaviour. This in turn would reduce the incentives that firms have to lower prices for consumers. This is the objective of competition and competition policy.

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51 Speech by Allan Fels, on the 'Effects' Test for s.46 Appearing before the Joint Committee on the Retailing Sector, Canberra, 13 July 1999, Hansard, RS 1162

The business sector acknowledges that some businesses do act in an anti-competitive manner and when caught, should be prosecuted to the fullest extent of the powers vested in the ACCC. However, another less obvious form of anti-competitive behaviour mentioned by Professor Fels occurs when a company uses the existing competition laws for protection. The TPA was never intended to provide protection for competitors, only competition. This again emphasizes the large potential for damage of introducing an 'effects' upon competition.

Criminal Sanctions

The ACCC has called for criminal sanctions to be introduced into the TPA for 'the most serious' breaches of Part IV of the Act, and specifically section 45A (contracts, arrangements or understandings relating to prices) and section 4D (exclusionary provisions). [52]

From the ACCC's public statements on the matter[53] the Commission would see such penalties applying to 'the most serious and profitable acts of collusion such as price-fixing, bid-rigging and market-sharing'; 'major businesses', 'large profitable multinational companies' but not small businesses or trade unions; 'extreme collusive behaviour'.

The Commission argues expanded criminal powers are necessary to deal with what it regards as 'troubling signs of an increase in hard core collusive activity internationally (and locally) which will not be deterred by anything other than true criminal sanctions, including imprisonment.'[54] It also points out other western industrialised nations, such as Canada, Japan, South Korea and the United States, have such provisions within their domestic competition laws.

Building on its call for criminal powers for 'hard core cartel' activity, the Commission goes on to argue 'its existing investigative powers will not be sufficient to successfully detect and prosecute modern, international cartels. There is a need to expand these powers to include the investigation tools usually available in

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[52] Untitled Address by Prof Allan Fels to 'Policy, Principles and Practice in Government Regulation' Conference, Sydney, 9 June 2001; see also, ACCC Media Release, 'ACCC Calls for Stronger Criminal Sanctions Including Jail Sentences for Price-Fixing Offences Under Trade Practices Act', 8 June 2001. These arguments were repeated by the ACCC in its submission to this Inquiry.

[53] ibid

[54] ibid

criminal matters, such as the ability to seize records and the power to intercept electronic communications.'[55]

Importantly, the ACCC's concept of 'hard core cartels' and their (mis)behaviour is narrower than that enunciated by the Organisation for Economic Co-operation and Development (OECD), which defines/states:

> 'A "hard core cartel" is an anti-competitive agreement, anti-competitive concerted practice, or anti-competitive arrangement by competitors to fix prices, make rigged bids (collusive tenders), establish output restrictions or quotas, or share or divide markets by allocating customers, suppliers, territories or lines of commerce.'[56]

ACCI is strongly opposed to the expansion of the TPA to include criminal penalties for so-called 'hard core cartels'. The ACCC has failed to demonstrate a proven need for such dramatically enhanced investigation and prosecutorial powers. Claims regarding overseas practices are not, of themselves, sufficient.

Proven cases of cartel behaviour in this country are rare and exceptional, reflecting the similar incidence of such conduct. Existing substantial financial penalties under the Act appear more than adequate to punish and deter such activities.

At the same time, criminal powers would also be inconsistent with the authorisation powers of the TPA; a regulatory agency cannot condone criminal activity. Such powers would have to be substantially wound back, and eliminated in certain areas, if the ACCC were given powers of criminal investigation and prosecution.

Where the ACCC identifies particularly egregious incidences of cartel activity, the existing criminal law, particularly concerning conspiracy[57], is available and more than adequate to punish and deter such conduct.

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[55] ibid

[56] OECD, '1998 Recommendation of the Council Concerning Effective Action Against Hard Core Cartels', Para 1 (A) (a)

[57] Crimes Act (Cth), s 86 (4) (b); there is also a substantial body of common law on the matter

The issue of whether criminal penalties should be introduced into the Trade Practices Act is really a question of which forms of penalties are more effective in preventing certain breaches. Price fixing, bid rigging and market sharing agreements are rightly illegal and are not defended by business. Indeed, it is other businesses which are often the entities harmed by such behaviours. At the present time, there are fines of $10 million for such breaches of the Act. The issue that has been raised is whether criminal sanctions are also needed to limit this form of illegal conduct.

There is little evidence that such problems exist in great numbers in Australia and the present penalty structure appears to provide sufficient protection against such practices. There are already great difficulties and risks in managing businesses in Australia without also adding the threats of jail for those who are accused of behaviours which contravene the Trade Practices Act.

Against this background, it is recommended that the Dawson Review clearly and decisively reject calls for the inclusion of criminal investigation powers and penalties into Part VI for breaches of the restrictive trade practices elements of the Trade Practices Act. In its Report, the Review Committee should state that there is no proven need for such expanded powers on the part of the Commission, and/or that existing legal avenues are inadequate to deter and punish such conduct.

Predatory Pricing

There are a number of issues associated with predatory pricing that need consideration, but most importantly is the question of what role regulators and governments have in determining the pricing policies of firms. Since the visible actions that are taken to court are decisions by firms to lower prices, which is obviously of benefit to consumers, the matter at issue is whether the price will be raised at a later date to make up for the earlier losses when the prices were reduced. There is thus good reason for concern if regulators are to see their role being to second guess businesses over their pricing decisions.

The ACCC wishes to deal with the problem of predatory pricing undertaken by large companies who intend to drive out competition. Predatory pricing places a serious restriction on competition in a market and acts as a barrier to entry. As such, predatory pricing under the TPA is and should be considered illegal, for the protection of both competition and small business. It is not a question of whether predatory pricing should be illegal but one of whether the ACCC currently has the powers to deal with the problem. The question then arises as to whether the ACCC has an

advantage in prosecuting predatory pricing when compared to overseas competition agencies. What is of upmost concern is the manner in which the ACCC proposes to resolve problems of this nature. The 'effects' test carries its own set of potential barriers to competition, all of which must be considered when looking at the possible implications of introducing such a radical change in legislation.

> 'The defendant may have been innovative in developing product attributes, distribution channels, marketing strategies, or backward integration into the supply of requisite inputs. If such strategies allowed it to price its products or services below those of its rivals or to otherwise offer a more attractive package to its customers, such a strategy could hardly be considered predatory'[58].

Predatory pricing is not an easy economic concept to define. Traditional predatory pricing would require a firm with market power to set its price low for a sufficient period of time to encourage firms to exit the market and discourage others from entering. Under the assumption that all firms are equally efficient losses by both the 'predatory' firm and 'prey' firms are incurred if the 'prey' firm attempts to match their competitors prices. This then requires that the predatory firm can increase prices after the other firms have left the market in order to recoup losses. Theoretically the predator firm can outlast its competition through cross-subsidisation, deeper pockets or better financing. In the short-run consumers will benefit from lower prices, although, in the long-run, consumers will face higher prices, reduced services and lower quality.

For a firm to undertake predatory pricing it must necessarily weigh up the costs and benefits of such actions. For large firms, the costs of predation are impacted by market share- costs increase as a proportion of market share; with respect to competitors' cost structure- again costs rise in (inverse) proportion to a competitors' cost structure, and with increases in the amount of time it takes for a successful outcome i.e. for competitors to leave the market. These costs must outweigh the discounted or present value profits, which are then discounted again to reflect the firm's subjective probability of success.

US authority Justice Heerey stated that the essential elements of predatory pricing, in order for it to occur, include pricing below

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58 Robert W. Crandall '*The Failure of Structural Remedies in Sherman Act Monopolization Cases*', Working Paper, March 2001, Pg 3.

cost and the *existence of a reasonable likelihood of recouping losses*. The last point in Australian law has been lost, economic forces appear to have been disregarded by judges and courts whereby the need to prove recoupment of losses is not applied in Australian courts.
In relation to Boral and s46, the Act:

> 'does not have these theoretical economic doctrines written into it and, if the purpose is to drive someone out of business and it is connected with the misuse of market power, then it is a breach of the law'[59].

The court also rejected rational business behaviour by Boral and found it guilty of predatory pricing in a highly price competitive environment. American courts also require that below cost pricing be established in order for predatory pricing to be established.

In a recent US case *United States of America v AMR Corporation, American Airlines Inc. and AMR Eagle Holding Company* this decision continued the predatory test found in *Brook Group Ltd v Brown Williamson Tobacco Group.* What is essential to predatory pricing is objective evidence of pricing below average variable cost and realistic prospects of recouping losses,[60] no longer necessary under Australian law. The requirement under US law to prove predatory pricing is more stringent than the requirements that currently exist in Australia. This lesser requirement in Australia has helped the ACCC to prosecute and protect small business.

> 'For example, Justice Merkel explained the differing approach in Australia as resulting from amendments to the Trade Practices Act in 1986 which, he said: "lowered the section 46 threshold to 'ensure that small businesses are given a measure of protection from the predatory actions of powerful competitors' who include 'major participants in a oligopolistic market and in some cases …a leading firm in a less concentrated market."'[61]

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59 Standing Committee on Economics, Finance and Public Administration '*Competing Interests: is there balance? Review of the Australian Competition and Consumer Commission Annual Report 1999-2000*', Chapter 4 Enforcement Issues, Effects Test (4.29), Pg 51.

60 Serje, Ron. '*Predatory Pricing*' Competition Law Issues, Clayton Utz, August 2001.

61 ACCC Media Release 28th February 2001.

Indeed the ACCC has stated that the Boral decision

> 'It assists new entry into markets and protects efficient small businesses from abuses of well-financed larger players. This ruling will enhance the ability of small businesses to enter and compete in markets with big businesses'.[62]

ACCI acknowledges that an appeal by Boral is underway.

Of particular concern is another form of predatory behaviour called non-price predation. This type of strategy tends to raise costs rather than reduce income. Actions undertaken by a company that apply this form of behaviour may include 'the abuse of judicial and administrative procedures to impede domestic and foreign competitors. Because the rules' against predatory pricing are natural weapons for the non-price predator, it is important that these rules be no broader than necessary; rules which are overbroad or imprecise invite their abuse for anti-competitive purposes.'[63]

This type of predation requires no information about the firm including its cost structure. Sham litigation is one instrument in the non-price predator's armory. Therefore, increased attention by competition authorities to allegations of non-price predation may deter pro-competitive activity. Indeed, *determining those rare instances when such normally productive practices are inefficient may be beyond the scope of the legal process*. These concerns do not apply, however, when a firm engages in non-price predation by abusing judicial or administrative procedures to impede competitors.'[64] 'Finally, note that a firm may engage in non-price predation against a rival by accusing the rival of engaging in predatory pricing. Misuse of the legal process can be minimised by assuring that any rule against predatory pricing is narrowly drawn.'[65]

Given the difficulty in recouping losses from a strategy that involves predatory pricing, in light of the potential Boral case, in which prices are lower than cost and the increased incentive to use non-pricing predatory behaviour with broader market power laws, ACCI would argue against the use of an 'effects' test to capture

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62 Ibid

63 OECD '*Predatory Pricing*' 05/31/89, Pg 8.

64 OECD '*Predatory Pricing*' 05/31/89, Pg 12-13.

65 Ibid Pg 13.

predatory pricing behaviour. Any rule against predatory pricing will condemn some and deter others engaged in legitimate competition. This will outweigh any benefits from catching or deterring what is true predatory pricing. Extending the scope of regulatory error must be kept to a minimum if we wish to promote a competitive national economy with rising living standards and faster growth.

Divestiture

> 'In some cases of flagrant or repeated anti-competitive conduct in contexts beyond the merger context, a divestiture power would provide a further alternative for the Court to consider in ordering appropriate remedies.'[66]

> '[ACCC] reiterates its previous position of support for a limited extension of the existing power by providing the Court with the option to order divestiture where there is a contravention of Section 46 of the Trade Practices Act.'[67]

Some have argued that the ACCC should have the power to divest a company 'to ensure that, where markets are highly concentrated (regardless of the way in which such concentration was achieved) no public detriment results.'[68] Such an application for divestiture powers would extend the ACCC's reach into that of section IV of the TPA as an additional remedy. ACCI's view is that this is an extreme and unacceptable remedy for concentrated markets and moreover, economically controversial. In the context of a dynamic economy, this remedy would require predicting the future structure of a particular market. This task is difficult enough when looking at contemporary issues: it becomes exponentially more difficult and inaccurate when considering ex-post markets.

In its submission to the Senate Legal and Constitutional Reference Committee, the ACCC argued that:

> 'It is likely that the courts would not be willing to order divestiture other than in extraordinary situations and this is a position strongly endorsed by the ACCC.'[69]

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66 *Submission 21,* Australian Consumer and Competition Commission, pp 12-13.

67 Ibid p 2.

68 The Australian Parliament of the Commonwealth of Australia, Senate Legal and Constitutional Reference Committee, '*Inquiry into s.46 and s.50 of the Trade Practices Act 1974*', May 2002, p 26.

69 *Submission 21,* Australian Consumer and Competition Commission, p 13.

The ACCC has stated that out of 500 merger proposals that have come before it, it has opposed only 25 (or five percent). Given this figure, divestiture orders would only place unnecessary and superfluous legislation into the TPA. Divestiture legislation, if included in the TPA, would lead to considerable uncertainty within the business community. The uncertainty would also spread beyond Australia's shores and into the boardrooms of foreign companies considering Australian investments.

Consider the following example: suppose a business through no intervention of its own, found itself with one less competitor and a large market share. The inclusion of divestiture powers, regardless of the way such concentration was achieved would be a critical deterrent to any business wishing to expand or invest in Australia. It would then be incumbent upon such a business to divest itself of assets legally gained through the process of competition. Will the loss of efficiency through vertical integration and economies of scale and scope be sacrificed under the guise of competition law? This example highlights the potential for competition law to deem that a business, which did not act illegally nor abuse its market power to become a target for divestiture.

Those who believe that more regulation is the way to improve the efficiency of the economy and increase Australia's welfare will no doubt cover the potential benefits of divesture powers. It is worth noting that any battle between firms and the ACCC that involves divestiture will require the expenditure of real economic resources, lengthy legal proceedings with both parties being tied up in court for years, lost output in the short-run and the loss of synergies due to scale and scope. Any gains from restructuring the market will have to be large in order for Australia's welfare to increase.

If a firm, through superior foresight, skill and innovation obtains market power, is that to be considered enough to invoke divestiture orders? At the very least it must be incumbent upon the ACCC to prove, through careful consideration, that market power was not achieved through progressiveness and efficiency but by actions designed to exclude competitors from the market. Any decision about divestiture of a company's assets would require determination of how market power was achieved.

If no consideration were given to the above issues, a firm would have little incentive to gain market share through the implementation of research and development, competitive pricing and superior customer service. These issues become more important when considering the dynamic efficiency of the market, whereby

these benefits are perhaps not seen in immediate price reductions but in longer-term improvements to the market and consumer welfare.

Any form of divestiture has the potential to affect smaller shareholders in the companies also which presents an externality problem, whereby an agreement undertaken by two parties affects a third party, which has not taken part in the original agreement. Divestiture as a measure supposedly introduced to increase welfare, must include these real costs. This level of micro management will be prohibitively expensive, leaving the issue of externalities unresolved and will lead to enormously unproductive outcomes, exacerbating and contributing to the problem of inefficient resource allocation.

This type of problem would, with certainty, lead to court battles with minority shareholders feeling that actions taken by the ACCC and the courts gave little regard to consideration of their position. This situation once again gives rise to inefficiencies in the expenditure of real resources and therefore any gains to the economy from divestiture would have to be substantial.

Divesting a company may well be ineffective due to the ACCC and the courts unsuccessfully predicting changes in technology and consumer demand. This is especially true in industries characterised by rapid change in product and service delivery.

> 'Divestiture would provide an appropriate structural remedy to overcome anti-competitive structural issues in the economy.'[70]

The ACCC appears to want divestiture powers in order to put in place structural remedies within a firm or industry market. Structural remedies may involve horizontal divestiture where two or more companies are created from the one firm or vertical divestiture where separate companies are created at different points in the production process. Vertical divestiture will reduce the efficiency a firm commands through the integration of its production and distribution processes. The net effect in this instance may be to increase consumer price and reduce consumer welfare.

The introduction of divestiture powers has the capacity to create a situation where the court is forced to monitor divestiture decisions over an extended period of time, with the cost of enforcement of such decrees potentially significant. Additional costs can also be incurred when supervision of divestiture orders by a lower court

[70] Ibid p13.

leads to appeals in higher courts, thereby serving to use up court and company resources in a manner which was not envisaged by competition law. The difficulty of enforcement also increases in a more dynamic market, such as, for example, the telecommunications market where monitoring changes within the constantly shifting industry landscape requires constant attention. At the level of the firm an additional difficulty, say, in relation to a vertical integration, relates to the difficulty of ascertaining where the production processes of each provider along the value chain begin and end.

Another limiting factor highlighted by previous cases is the ability to find a buyer willing to take components of a business that has been dismantled through the divestiture process. As a relatively small market, this situation is likely to have a greater impact in Australia than upon countries with larger markets such as Europe and the United States. In the event that no buyer can be found, divestiture proceedings would be stopped with the company able to continue as before – a costly exercise in market intervention indeed.

The proposed divestiture powers outlined in the draft if widened to include s46 would be undesirable in principle and likely to prove unworkable in practice. As such, divestiture under s46 should be abandoned.

Reversal of Onus of Proof

> 'The ACCC takes the view that the reversal of onus of proof proposal would be preferable to the way in which Section 46 actions taken by the ACCC are currently proved before the courts.'[71]

The ACCC also wishes to introduce the reversal of onus of proof. This requires that a company would bear the responsibility of proving its actions were not intended in the manner of one of the proscribed 'purposes' with respect to s46 (1)(a), (b) or (c)[72]. If the regulator has reason to believe that a company has abused or taken advantage of its market power, it is the company's responsibility to prove its intended purpose was not detrimental to competition. The burden of proof will rest on a party other than the party that bore the evidential burden.

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71 Ibid p2.

72 Ibid p5.

Under the current s46 (7) legislation purpose can be inferred when a company does not give a legitimate reason for business actions. Currently a company must give a reason, if the case against it is strong enough, as to why such conduct was undertaken. This interpretation of 47(7) in effect can act as a reversal to the onus of proof.

> 'The ACCC's experience has been that in the absence of "smoking gun" documents, proving a relevant purpose under Section 46 to the satisfaction of a Court is an onerous forensic process.'[73]

As outlined above, the ACCC currently has powers under Sections 155 and 156 to require a person that is believed capable of giving information, documents or evidence that relate to contraventions of the TPA to come before them. Allowing the onus of proof to be reversed under s46 would only give the ACCC another advantage over business and private litigants. This power is sought because of the perceived difficulty in obtaining favourable outcomes under s46. Although as stated in earlier submissions, recent court successes by the ACCC have not escaped the attention of both small and large businesses in the Australian business community.

The courts would still need to decide in cases where explanations of actions are required, if the evidence or lack thereof establishes an abuse of market power. The ability of the ACCC to prove cases would be greatly enhanced by its additional powers. For one, it would face a lower burden of proof in order to obtain prosecutions. The only result from granting the reversal of onus of proof legislation would be to shift the costs of litigation from the government to business.

Reversal of onus of proof would also place successful businesses in a position whereby they would have to justify their actions against all components of s46 (1). This justification would require proof that actions where taken to increase general competition and not targeted towards an individual company.

As in the case of 'cease and desist' orders, reversing the onus of proof implies an amount of guilt or prejudgement. This again would cost businesses in terms of reputation, while not improving competition in the market.

As with private litigants, when the bar is lowered in terms of the ability to gain convictions or use regulation as a barrier to

[73] Ibid p5.

competition, the amount of litigation increases. This type of behaviour could also pertain to the ACCC. Where a lower standard of proof or a reversal of proof applies, the ACCC may give less consideration as to the guilt of the company when seeking a conviction or legal hearing. This in turn, may also serve to increase the amount of litigation undertaken by the ACCC.

The ACCC has enough power and advantage over private litigants not to require this new benefit. The balance between a strong competition policy and an overly restrictive and financially burdensome policy will have been crossed with the introduction of the reversal of onus of proof.

Mergers and Acquisitions

In an economy, there are no permanent monopolies and if the market is defined properly, few if any firms are ever without genuine competition of some kind. Markets are dynamic, and successful firms relentlessly attract competition to take away excess profits. And importantly, excess means profits higher than would be necessary to attract industry into satisfying consumer demands in a particular market. Both the level and rate of profits will be different in different industries depending on the risks as well as other circumstances particular to the industry.

What business seeks is a market structure that encourages firms to provide existing products at the lowest prices and highest quality consistent with profitable outcomes. It also seeks a market structure in which businesses are encouraged to innovate so that existing products are improved and new products developed. This is the kind of environment which will lead to the greatest benefit to consumers overall.

Where firms seek to earn a positive return on their outlays in an open market situation in which a competitive environment exists, they will act in ways that lead to the greatest net benefit to consumers. The pressure on businesses to earn higher profits, combined with the need to at least match the ongoing improvements offered by competitors, are the best guarantors that consumers' welfare will increase on an ongoing basis.

Within this overall framework there is no single textbook form of market structure that is best. No market will ever conform to the textbook version of a perfectly competitive market as there are virtually no markets in which sellers do not have at least some market power. Firms have discretion over their pricing policy and they typically sell differentiated products. It is not possible to use a

perfectly competitive model as the ideal of market based competition as it is an unrealistic aim either to achieve or to imitate.

Instead, markets will be shaped by the circumstances in which firms attempt to compete. Australia will develop its own structures because of the nature of the economic conditions businesses must contend with. Firms and market structures have developed to meet local conditions. In this regard it is important to recognise that the market structures of North America, Europe and Asia cannot provide appropriate models for Australia since the surrounding conditions, in terms of income, density of population, level of income and other factors, are so entirely different.

Because of this different economic structure, the regulatory requirements to meet market conditions in Australia are different from those found overseas. Firms in Australia will tend, on average, to be smaller and market concentration will equally tend, on average, to be greater. Competition policy objectives should promote and facilitate competition both domestically and internationally as the best means to promote allocative, productive and dynamic efficiencies in free market economies.

In practice, economic efficiencies should be relevant in merger analysis only when there is concern that the transaction is anti-competitive. Competition agencies should typically conduct analysis of the competitive effects of a merger, and if anti-competitive effects are judged to be non-existent or small, there should be no need to go further; approval for the merger to proceed should be granted. The process through which mergers are granted should be conducted as quickly and transparently as possible in order to reduce expense and uncertainty.

In some cases, mergers have a role in producing welfare enhancing outcomes and as such should be settled quickly. Mergers achieve improvements in society's welfare through economies of scale and scope. They act as a source of risk diversification, reduce transportation costs, produce savings in non-manufacturing activities such as distribution and research costs and allow corporate governance mechanisms to use resources efficiently.

Regulators must consider dynamic efficiencies of mergers and acquisitions although they are generally more difficult to quantify than production efficiencies. Such efficiencies may include product quality, product mix and service quality.

There is also the issue of 'national champions' which is a way of referring to firms that are able to engage at the top level in international markets. But to be able to engage at that level may

require firms to have reached an appropriate critical mass so that there are efficiencies that accrue by being recognised on international markets. It should be one consideration of the ACCC in adjudicating mergers that Australia may need to cultivate internationally well-known businesses which through their reputations attract foreign firms to the Australian economy.

Under s50 of the TPA, Mergers and Acquisitions, any acquisition that would result in a substantial lessening of competition[74] is not permitted. Merger and Acquisition legislation allows for consideration of matters that must be taken into account in deliberations[75]. Although this list is not exhaustive and other matters may be taken into consideration, those matters appearing in s50(3) must be taken into account.

In 1992 s50 was amended to prohibit any mergers or acquisitions which have, or are likely to have, the effect of substantially lessening competition. Under s50, the substantial lessening of competition test for mergers is not opposed by the ACCI.

The matters that must presently be taken into account are accurate indications of important issues for merger considerations and ACCI would recommend that none of the matters be removed from the section.

Mergers by their very nature reduce competition. This does not, however, mean that prices will necessarily rise. Horizontal mergers combine firms from the same product and geographic market, which in turn reduces competition. The integration of production, marketing and distribution and other processes create economies of scale or scope, which may affect both firms' costs of production. A lower variable cost may result in lower prices and therefore increase society's welfare.

Vertical mergers involve firms along the supply chain joining together to manufacture a product. This product can then be on-sold as either an input to another product or as a consumer item. This type of merger helps to reduce transaction and distribution costs, which may be significant in some industries. Through these cost savings it is possible that prices are keener with consumers the beneficiaries of integration.

It is therefore possible that some mergers and acquisitions may provide a benefit to the public. A merger that substantially lessens

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74 Trade Practices Act 1974, 'PART IV – *Restrictive Trade Practices*', s50.

75 Trade Practices Act 1974, 'PART IV – *Restrictive Trade Practices*', s50 (3).

competition can still be allowed to continue under authorisation. This is considered under s88(9), and if public benefits are deemed to outweigh the negative effects of reduced competition, then authorisation, with or without remedies, can be granted by the ACCC and the merger will still proceed.

Furthermore, s90(9A) includes a list of items that must be considered in order to ascertain whether a merger contributes to public the benefit.

> 'In determining what amounts to a benefit to the public for the purposes of subsection (9):
>
> (a) the Commission must regard the following as benefits to the public (in addition to any other benefits to the public that may exist apart from this paragraph)
>
> (i) a significant increase in the real value of exports
> (ii) a significant substitution of domestic products for imported goods
>
> (b) without limiting the matters that may be taken into account, the Commission must take into account all other relevant matters that relate to the international competitiveness of any Australian industry.'

This process of public benefit consideration should take place, not after other matters have been considered, but included in s50(3).

In terms of globalisation, the ACCC allows mergers to proceed when a firm faces competition from imports of greater than 10% for a period of three years. In dynamic markets where a product can change dramatically over a short period, this timeframe may disadvantage Australian business. Imports that make up a small proportion of market in dynamics sectors should be considered more weightily than in less dynamic sectors.

The issue of mergers and acquisitions is an important aspect of the TPA and the assessment of applications is a major part of the work of the ACCC. The Review will need to examine whether the public interest test in s88 is robust enough given the needs of the Australian economy.

At this stage ACCI does not advocate change from the present structure of the Act or from the manner in which applications are assessed but does note that these are major issues that do require serious consideration.

Survey Material on New Powers Sought by the ACCC

There have been a number of surveys conducted on the ACCC which have focused on the new powers sought to regulate business, and in particular the commercial relationships between large business and small. There is no doubt that many small businesses feel aggrieved about the actions taken by larger firms with greater market power. This sense of grievance is demonstrated in the results to a number of surveys.

ACCI had considered conducting a survey of its own but having looked closely at the problems involved came to the conclusion that it would be almost impossible to elicit sensible results in this way. The issues are far too complex to be part of a survey of businesses who could not be expected to understand all of the intricacies of the issues involved.

Consideration of the knowledge required to answer questions on the consequences and desirability of the introduction of cease and desist powers or an effects test would make it clear how inadequate any response to such questions would be. Business people might be able to identify the existence of practices that have placed pressures on their firms, but they would be generally unable to judge whether the actions taken had been a mis-use of market power rather than just the normal competitive pressures that larger firms often place on smaller competitors.

Further, the owners of such businesses would be less able to recognise the damage to competition of granting such enormous powers to regulators since these are economic questions which cannot be understood without specialist in-depth study.

In consequence, the results of surveys in this area would indicate a desire to limit the market pressures placed on firms in competitive industries but would not provide sound guidance on public policy in such a difficult area requiring fine judgements on economic and legal matters. The respondents to such surveys are unlikely to have the expertise required to make informed judgements and little reliance should be placed on such results.