Submission to the Committee reviewing the Competition Provisions of the Trade Practices Act 1974

Introduction

This submission is in relation to s46 *Trade Practices Act 1974*.

Prior to and since the announcement of this review there has been considerable discussion over the terms of and application of s46. There has been a well-publicised debate as to whether s46 should be retained in its current form or amended to incorporate an effects test.[1]

While this debate is useful, it distracts from the more pertinent question -what is the law intended to do (which reflects its economic and policy objectives), and whether s46 in its current form accurately reflects that law and by implication those objectives. As Bork said:

> "Antitrust policy cannot be made rational until we are able to give a firm answer to one question: What is the point of the law – what are its goals? Everything else follows from the answer we give….Only when the issue of goals has been settled is it possible to frame a coherent body of substantive rules."[2]

The committee's assessment of s46 should adopt a similar principled approach. It is important to understand the foundations for and the current state of the law before we are in any position to formulate an appropriate response. It should not simply translate into a choice between one or other models presented in the debate.

It has been argued that the Australian law on monopolisation should be brought into line, among other things, with the position in the United States. It is best to consider this proposition in the context of the United States law on monopolisation. This is the purpose of the submission. What emerges is that it is not at all obvious that one or other models for s46 will bring our law into line with the U.S. Such a proposition is far too simplistic.

The policy rationale for the monopolisation offence

Antitrust policy is capable of delivering a number of policy outcomes which include the promotion of competitive processes, economic performance and wealth distribution.[3] We may argue about the primary goal of competition law, however the promotion of economic efficiency and the maximisation of consumer welfare certainly feature prominently.

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1 See for example A Kohler, " A power play with only one winner", *Australian Financial Review* 11 June 2002, 71; R Steinwall "T he battle over champions" *Australian Financial Review*, 4 June 2002, 70; P Switzer "David v Goliath over Fels" *Australian*, 24 June 2002, 27; J Thompson "Fights Back" *Business Review Weekly*, 4 July 2002, 50; Editorial *Business Review Weekly*, 4 July 2002, 8; M Fenton-Jones "Independent retail grocers back ACCC" *Australian Financial Review*, 9 July 2002, 49; S Marris "More power to Fels: Small business" *Australian* 16 July 2002; 19, P Charlton "Besting the big end of town" *Courier Mail* 13 July 2002, 32; K Lahey "Effects test rather ineffective" Australian Financial Review, 10 July 2002, 55.

2 R. Bork The Antitrust paradox Basic Books, New York 1978, p50.

3 See Kaysen and Turner Antitrust Policy: An Economic and Legal Analysis, Harvard University Press, Cambridge 1965, p11.

Section 46 is modelled on s2 *Sherman Act 1890*. The history of the Sherman Act indicates a policy intention of promoting consumer welfare.[4] It has been suggested that "competition" is a short hand way of expressing a state of affairs in which consumer welfare cannot be increased by moving to an alternative state of affairs through judicial decree.

Conversely monopoly would be employed to describe a situation where consumer welfare could be improved. Under conditions of monopoly, output is reduced and prices are higher compared to a more competitive environment. The ill effects of monopoly include allocative efficiency losses and wealth distortions.[5] Therefore to monopolise (and the offence of monopolisation) is to use practices inimical to consumer welfare.[6]

The offence of monopolisation under the US law is at least intended to prohibit no more and no less than those practices that violate this policy directive. No more, because an unnecessarily restrictive application of the law will stifle innovation, investment and legitimate behaviour and contribute to the very inefficiencies it is intended to overcome. No less, because it is conducive to the policy outcome.

The monopolisation offence

Section 2 *Sherman Act 1890* provides that every person who shall monopolize or attempt to monopolize or combine or conspire with any other person to monopolise will be guilty of a violation. The section therefore establishes three separate offences – actual monopolisation, attempted monopolisation and conspiracy to monopolise. The elements of each offence are different.

The offence of actual monopolisation comprise two requirements:

- the possession of monopoly power in a relevant market; and
- the wilful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident.[7]

Liability for actual monopolisation requires that it be established the defendant used anticompetitive methods to achieve or maintain its position.[8]

It is said that if the evidence reveals a significant exclusionary impact in the relevant market the conduct will be labelled anticompetitive unless the defendant comes forward with specific, pro-competitive business motivations that explain the full extent of the exclusionary conduct.[9] Similarly proof that a profit maximising firm took predatory action is said to demonstrate the threat of substantial exclusionary effect.[10]

In *United States v Microsoft Corporation* Jackson J accepted the view that the defendant's conduct must be shown to be exclusionary – that is, whether it has restricted significantly, or

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4 R. Bork The Antitrust paradox Basic Books, New York 1978, p61.

5 E Gellhorn ad W Kovacic Antitrust Law and Economics in a Nutshell 4th ed 1994p 68-69.

6 R. Bork The Antitrust paradox Basic Books, New York 1978, p61.

7 *United States v Grinnell Corp* 384 U.S. 563,570-571 (1966); *Aspen Skiing Co v Aspen Highlands Skiing Corp* 472 U.S. 585,596 (1985).

8 *United States v Grinnell* 384 U.S. 563, 570-71 (1966); *Eastman Kodak Co v Image Technical Services Inc* 504 U.S. 451, 488 (1992).

9 *United States v Microsoft Corporation*, Conclusions of Law, p 7.

10 Ibid p7.

threatens to restrict significantly the ability of other firms to compete in the relevant market on the merits of what they offer customers.[11]

Many synonyms have been used to describe the wilful nature of the defendants conduct. However it begs the question whether the defendant has acted lawfully (that is aggressively or competitively) and not unlawfully, that is monopolised. Expressions such as "exclusionary", "predatory" and so on are no more that convenient shorthand means of expressing this distinction. Establishing aggressive competitive behaviour from a misuse of market power is at the heart of the dilemma.

The early United States decisions referred to intent as the basis for identifying monopolisation. In *Standard Oil*, White J said that the prima facie presumption of intent to restrain trade was evidenced by the elements of the defendants behaviour.[12] In *Griffith* the court said that:

> " It is not…. always necessary to find a specific intent to restrain trade or to build a monopoly in order to find that the anti-trust laws have been violated. It is sufficient that a restrain t of trade or monopoly results as the consequence of a defendant's conduct or business arrangements."[13]

However intention has been said to be relevant, not because it proves or disproves specific conduct, but because knowledge of intent may help the court to interpret facts and to predict consequences. [14] The best that may be said of it is that it is simply part of the evidence which the court will consider. Alone it is not a necessary or sufficient condition for liability.

Areeda and Turner have said that the benefits of conduct will not be apparent or persuasive unless the defendant identifies his purpose in acting, shows the legitimacy of that purpose in terms of antitrust objectives and suggests that the challenged action is an appropriate and perhaps the least restrictive way of achieving that legitimate purpose. [15]However as the authors point out, it is the nature and consequences of a particular practice that is the vital consideration, not the purpose or intent.[16]

The reason is that action that damages or drives out a competitor is "intended" by the company as the natural result of its efforts. It is no more useful a test for determining whether the conduct is legitimate or prohibited and is analytically limited:

> " but to so read "purpose or intent" would be to read the behaviour requirement out of the monopolisation offence altogether and make monopoly unlawful per se…The short of it is that talk of "purpose or intent" is largely diversionary or redundant."[17]

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11 *United States v Microsoft Corporation*, Conclusions of Law, p7.
12 *Standard Oil Co v United States* 221 U.S. 1, 75 (1911).
13 *United States v Griffith* 334 U.S. 100,105 (1948)
14 *Chicago Board of Trade v United States* 246 U.S. 231, 238 (1918)
15 Areeda P and Turner D, Antitrust Law, *An Analysis OF Antitrust Principles and Their Application, Volume III,* Little, Brown and Company, Boston, 1978, p 75-76.
16 Ibid p 76.
17 Ibid p 76.

It has therefore been said that the emphasis should be on conduct not intent:

> " …in defining the behavioural component of the monopolisation offence, one must concentrate on conduct and define the characteristics of conduct that are undesirable. Despite loose language, this is in fact what the courts have attempted to do. They have focussed on conduct while talking about intent."[18]

The distinction is important because documentary evidence that a company is proposing to take action to drive out a competitor or to seize market share does not of itself establish the economic evidence necessary to establish the offence. In *Ball Memorial Hospital v Mutual Hospital Insurance Inc,* Easterbrook J said that intent to harm rivals without more offers too vague a standard because vigorous competitors intend to harm rivals.[19]

A point of distinction between the U.S and Australian law is the use in the U.S of juries. The consequence is that intent, and proof of intent through various "smoking gun" documents takes on a far greater significance. This is not because the offence requires it, but rather because it may be crucial in influencing the jury's perception of the defendant and tip the balance in favour of the prosecution:

> " Lawyers rummage through business records seeking to discover tidbits that will sound impressive (or aggressive) when read to a jury. Traipsing through the warehouses of business in search of misleading evidence both increases the costs of litigation and reduces the accuracy of decisions."[20]

Therefore in the case of actual monopolisation, if a company has exploited its market position there is arguably no separate need to establish intent as this may be assumed from its behaviour. [21]

In the United States monopolisation may also require the demonstration of some reprehensible behaviour against a competitor. [22] Conversely evidence by the defendant of valid business reasons for the conduct is a defence.[23]

Actual monopolisation also requires behaviour that not only impairs the opportunities of rivals but also does not further competition on the merits or does so in an unnecessarily restrictive way. [24] That is, the monopolisation offence also requires evidence that the defendant's action does not promote competition. It for this reason that some have suggested that to accurately replicate the U.S law requires an amendment to s46 to

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18 Areeda and Turner p 77.

19 784 F 2d 1325 at 1337-9 (7th Cir 1986)

20 Easterbrook J in *A.A. Poultry Farms Inc v Rose Acre Farms Inc* 57 A.T.R.R. 260 (1989), 263.

21 Neale A and Goyder D, *The Antitrust Laws of the United States of America: A Study of Competition Enforced by Law,* 3rd edition, Cambridge University Press, Cambridge 1980, p 93.

22 See the comments of Pincus J in *General Newspapers Pty Limited v Telstra Corporation* (1993) ATPR 41-274 at 48,819.

23 See the comments of Pincus J in *General Newspapers Pty Limited v Telstra Corporation* (1993) ATPR 41-274 at 48,819.

24 *United States v Microsoft Corporation*, Conclusions of Law p 78.

emphasise the effect of the conduct on *competition* rather than the purpose or intent of the defendant to harm or injure a particular competitor.[25]

However, though intent may not be at the heart of the offence it similarly does not follow that the test merely focuses on the *effect* of the conduct. The behaviour of the defendant and the effect of the conduct are indeed relevant considerations but do not of themselves fully articulate the offence. As indicated, it is the nature and consequences of a particular practice that is the vital consideration which include the components of the offence described above. As indicated it is also necessary that the conduct satisfy the economic basis for liability.

A further caveat in the suggestion that the Australian law be brought into line with the U.S position on monopolisation stems from the use in the U.S of objective tests that have no equivalent in Australia. Take for example predatory pricing. The difficulty is to distinguish pricing which is predatory and that which is competitive. In the U.S cost based tests have been employed to introduce an economic measure of cost, below which pricing is regarded as predatory or raises a presumption to that effect.[26]

Areeda and Turner postulate a test where predation is assumed where pricing is below marginal cost or average variable cost. This approach does not merely raise a presumption of predation but rather conclusively establishes the offence, regardless of any explanations that may be raised by the respondent. Posner on the other hand has suggested that long run marginal cost raises a presumption of predatory pricing which permits other credible explanations to be put forward by the respondent.[27]

In William *Inglis and Sons Baking Co v ITT Continental Baking Co* the court proposed a two stage test involving a shifting in the evidential burden:

> "If the defendant's prices were below average total cost but above average variable cost, the plaintiff bears the burden of showing defendant's pricing was predatory. If, however, the plaintiff proves that the defendants prices were below average variable costs, the plaintiff has established a prima facie case of predatory pricing and the burden shifts to the defendant to prove that the prices were justified without regard to any anticipated destructive effect they might have on competitors".[28]

Recoupment is another test employed in the U.S. It recognises that short term losses sustained during the period of predation will be recouped by monopoly profits in the future[29] Under the recoupment approach, it is only if market structure makes recoupment possible that a Court needs to consider the relation between price and cost.

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25 See the submission to this review by Professor Stephen Corones, 18 June 2002, p1.

26 See K McMahon "Predatory Pricing under Section 46 of the Trade Practices Act and the decision in Eastern Express v General Newspapers - Part II (1993) 1 *Trade Practices Law Journal* 130; R Steinwall "The Use of cost Based Tests and the Tests of Recruitment by Australian Courts in Predatory Pricing Cases: Some Further Insights from the Recent Federal Court Decision in Boral Limited (1999) 7(2) *Competition and Consumer Law Journal* 140;V Nagarajan, "The Regulation of Predatory Pricing within s46 of the Trade Practices Act 1974" (1990) 18 *Australian Business Law Review* 293 at 308-312.

27 R Posner *Antitrust Law: An Economic Perspective*, University of Chicago Press, Chicago, 1976, p190.

28 688 F 2d 1014 (9th Cir) (1981) at p1035 - 1036.

29 R Bork, *The Anti Trust Paradox: A Policy at War with I*tself, Basic Books, New York 1978 at p 145,approved in *Matsushita Electric Co v Zenith Radio Corp* 106 S Ct 1348 (1986) at 1357.

In *Boral* Beaumont J expressly rejected the United States approach to recoupment.[30] Merkel J expressly rejected both recoupment and the cost based tests.[31] The reason appears to be that these tests are not relevant to the clear words of s46. Finkelstein J also rejected recoupment and the cost based tests for a number of reasons including because it is said that intent rather than recoupment is at the heart of s46.[32]

The reluctance of Australian courts to employ these tests represents a significant discontinuity in the approaches of the two jurisdictions and makes it even more precarious to make simple pronouncements about bringing Australian law into line with the U.S.

The position in the U.S. in relation to attempted monopolisation is quite different to actual monopolisation. The offence of attempted monopolisation requires that the plaintiff establish a specific intent to monopolise and demonstrate that there is a dangerous probability that it will achieve monopoly power. [33]As the defendant does not possess sufficient power at the time of the attempt, specific intent to achieve the result is an essential ingredient.[34] It is conceivable that the distinction between actual and attempted monopolisation has been partly responsible for the inaccurate representation of the United States law in Australia.

Conclusion and recommendation

This is merely a brief review of some of the facets of the United States position on monopolisation. However it suggests that it is far too simplistic and indeed incorrect to assert that the United States law reflects an effects test or indeed a purpose test that focuses simply on the intent of the conduct. The United States law incorporates features of both elements. The reason is that otherwise the law would not reflect the identified policy need to balance the existence of monopoly lawfully attained (and the intent to use that monopoly position) with the unlawful attainment or use of monopoly power having an anti-competitive effect, including an effect on individual competitors.

Whether s46 should be retained or amended is a decision that should be made only after considering its policy intent. There is certainly value in examining the U.S position, as its jurisprudence has been influential in shaping the Australian law. However in doing so it is best to follow the principled approach alluded to in the introduction.

It is recommended that the committee not simply accept the proposition (without first putting it to the test) that bringing the Australian law into line with the U.S can simply be achieved by adopting one or other model or that one or other model is an accurate embodiment of the U.S position.

Ray Steinwall
Visiting Fellow, Faculty of Law, University of NSW

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30 See [2001] FCA 30 at para 154,234.
31 [2001] FCA 30 at para 197.
32 [2000] FCA 30 at para 262.
33 *United States v Microsoft Corporation*, Conclusions of Law, p21-2
34 Ibid p 93.