Competition and Consumer Amendment (Misuse of Market Power) Bill 2016

Submission to the Senate Standing Committee on Economics

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The *Competition and Consumer Amendment (Misuse of Market Power) Bill 2016* (the Bill) would, if passed, give effect to the substance of the Harper Report's recommendation on misuse of market power. The proposed new provision is better aligned with the objectives of the law than the one it will replace. Importantly, it will address the two key deficiencies in the current law (the take advantage element and the exclusive focus on conduct having the *purpose* of harming *competitors*) which have prevented it from operating as intended.

Recommendation: the Committee should recommend passage of the *Competition and Consumer Amendment (Misuse of Market Power) Bill 2016*

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1. Overview

The existing misuse of market power provision is deficient in two key respects:

- The 'take advantage' element connecting market power and 'purpose' has failed to adequately distinguish competitive from anti-competitive conduct;
- The focus on 'purpose' of harm to *competitors* is inconsistent with the broader object of the Act and the specific object of the provision which is, or should be, to target conduct which significantly harms *competition* in the market.

The *Bill*, if passed, will address these deficiencies by removing the 'take advantage' element and will more appropriately focus attention on whether conduct has the purpose, effect or likely effect of substantially lessening competition. Concerns expressed by some commentators and interest groups that the proposed amendments will create uncertainty and/or constrain or chill vigorous competition are overstated.

The *Bill* stems from recommendations made as part of a comprehensive independent review of competition law and policy[1] (which provided multiple opportunities for comment), followed by a further Treasury review,[2] a Government commitment to enact the Harper Reforms in relation to misuse of market power[3] and a further Treasury Review of Exposure Draft Bill late last year.[4]

The current *Bill* deviates from the Exposure Draft Bill's provisions on misuse of market power in two respects; first, it limits the market in which the relevant substantial lessening of competition must occur and second, it does not incorporate the authorisation provisions for misuse of market power. The first is unfortunate; the second is presumably a result of splitting the reform legislation into stages, with the authorisation provisions expected to be incorporated in the next Harper implementation bill.

Although the changes to the *Bill* from the Exposure Draft Bill are unfortunate and should be reconsidered, the *Bill*, if passed, would nevertheless represent a significant improvement to Australia's misuse of market power laws by addressing the key deficiencies in the current provision.

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1 *Competition Policy Review* (2014-2014), reporting in March 2015: Professor Ian Harper (Chair), Peter Anderson, Su McCluskey and Michael O'Bryan QC, *Competition Policy Review: Final Report* (March 2015).

2 *Options to Strengthen the Misuse of Market Power Laws* (Treasury consultation following Harper Report recommendations, 11 December 2015).

3 'Joint Media Statement - Prime Minister, Treasurer and Assistant Treasurer - Competition Policy' (16 March 2016).

4 *Competition and Consumer Amendment (Competition Policy Review) Bill 2016* (Exposure Draft) released 5 September 2016.

2. Problems with the existing legislation

The existing misuse of market power provision is deficient in two key respects:

- the 'take advantage' element fails to distinguish competitive from anti-competitive conduct;

- the purpose element is inconsistent with a law designed to target conduct harmful to *competition* rather than individual *competitors*.

2.1. Take advantage

The requirement that a corporation 'take advantage' of its market power has been interpreted restrictively, with the result that it is not capable of appropriately distinguishing anti-competitive from normal competitive conduct. This restrictive interpretation has increased the prevalence and future risk of false negatives (or Type II errors); in other words, it has failed, and will continue to fail to capture conduct having the purpose or effect of substantially lessening competition. This is of particular concern in a relatively small and concentrated economy like Australia, in which market correction for such errors is less likely to occur in the short term, if at all.

This result was not inevitable and almost certainly not anticipated by those enacting the law. The potential difficulties were, however, acknowledged during the course of the Griffiths Review in 1988, where Alan Griffiths MP observed:

> 'It puts a great limitation on the operation of section 46 by insisting that the proscribed purpose alone is not sufficient; the nature of the activity also has to fall within the terms of section 46 … a corporation which has a statutory monopoly, such as Telecom … would all be capable of characterising activities as the exercise of a right given to it by statute, rather than taking advantage of the market power which it has by virtue of its position … [130] … The real problem with the drafting … is that it enables a corporation to engage in anti-competitive conduct which breaches the proscribed purposes provision of section 46 but the conduct itself does not fall within the narrow definition of taking advantage of the market power'.[5]

These comments were made prior to the decision of the High Court *Qld Wire,*[6] which rejected the attempt to introduce a pejorative element into the 'take advantage' requirement and found that BHP had misused its market power in refusing to supply Y-Bar to Qld Wire. In its final report,[7] which post-dated this decision, the Griffith Committee considered that the *Qld Wire*

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5 Hansard Report of the House of Representatives Standing Committee on Legal and Constitutional Affairs (Reference: Mergers, takeovers and monopolies) Canberra 25 October 1988, page 129-130 (per Alan Griffiths MP (Chairman)).

6 *Queensland Wire Industries v BHP* (1989) 167 CLR 177.

7 'Mergers, Takeovers and Monopolies: Profiting from Competition?' (Report of the House of Representatives Standing Committee on Legal and Constitutional Affairs) 1989

decision had resolved the 'debate about the interpretation of the take advantage provision' and that it should 'make it easier for aggrieved parties to establish a breach of section 46.'[8]

The predictions of the Griffith Committee proved far too optimistic, with subsequent decisions, such as *Rural Press*[9] and *Cement Australia,*[10] abandoning the neutral and holistic approach to s 46 and the 'take advantage' element exemplified in *Qld Wire,* instead engaging in a 'complex, disaggregated form of analysis' which has rendered the provision of 'limited utility'.[11] Legislative intervention, of the kind proposed in the *Bill*, is needed to resolve the problem caused by the 'take advantage' requirement.

Some submissions in relation to the Harper Recommendation and subsequent Exposure Draft Bill proposed an alternative 'connector' between market power and anti-competitive purpose or effect, such as whether the conduct would be a rational business decision absent the market power. However, these proposals miss the point: conduct might be perfectly rational both when taken by a firm with or without market power and each might be equally capable of engaging in the conduct. The effect on competition, however, is dependent on the level of market power enjoyed by the firm engaging in the relevant conduct. Firms lacking market power generally lack the ability (unilaterally) to substantially lessen competition: the absence of market power means their conduct can typically be matched by efficient firms, with the result that they have no capacity to foreclose *competition*. On the other hand, a firm enjoying market power, by engaging in the *same type of conduct*, may be able to leverage that power to foreclose or limit the market to actual or potential competitors.

The result of the current interpretation of the take advantage element is that it creates an effective safe harbour for conduct by firms with market power whenever it is capable of being rationally engaged in by firms lacking market power. There is no policy or economic rationale for this, given the effects on competition do not depend only the conduct involved but also on the market conditions and, in particular, the power enjoyed by the firm engaging in the conduct.

2.2. Purpose or effect of substantially lessening competition

The *Bill* removes the existing purpose requirement (focussing predominantly on purposes of harming *competitors*) and replaces it with a test focussed on whether conduct has the purpose, effect, or likely effect of substantially lessening competition. This is appropriate and consistent with the approach adopted to both unilateral and coordinated conduct elsewhere in the Act. The Explanatory Memorandum (para 1.13) provides that the objective of section 46:

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8 'Mergers, Takeovers and Monopolies: Profiting from Competition?' (Report of the House of Representatives Standing Committee on Legal and Constitutional Affairs) 1989 paragraph 4.6.26.

9 *Rural Press Ltd v ACCC* [2003] HCA 75.

10 *ACCC v Cement Australia Pty Ltd* [2013] FCA 909.

11 ACCC Submission to the Competition Policy Review (Issues Paper), pages 79-80.

> 'is to prevent firms from engaging in unilateral conduct that harms the competitive process. This requires distinguishing between vigorous competitive activity which is desirable, and economically inefficient monopolistic practices that may exclude rivals and harm the competitive process.'

Although the objectives of the Australian competition law provisions are open to debate, given the ambiguous language in article 2 of the legislation, few would suggest that the objective identified in the Explanatory Memorandum is not an appropriate objective for misuse of market power laws. With this objective in mind, it is clear that the proposed test focussing on purpose or effect of harming *competition*, is more consistent with this objective than the current focus on purpose of harming *competitors*.

In relation to distinguishing vigorous competitive activity from anti-competitive conduct, it has been observed above that the 'take advantage' element is inappropriate and ineffective in making this distinction. The connection is also unnecessary. Vigorous competition which harms less efficient competitors, or innovation which is rewarded with temporary enhancement to market power or share, is not anticompetitive; it is what is expected of effective competition and should deliver efficiency gains to firms and benefits to consumers in the form of lower prices and better or more diverse products or services. This would be recognised in any appropriate assessment of the 'substantial lessening of competition' test, which is capable itself of distinguishing competition on the merits from anti-competitive exclusionary behaviour. Existing case law does not suggest that in other contexts (particularly, for example, in relation to exclusive dealing, which overlaps considerably with the misuse of market power prohibition) the courts have been quick to find a substantial lessening of competition arising from vigorous competition; in fact the reverse is true.

Despite limited justification for this concern, to avoid doubt about the meaning of substantial lessening of competition in this context, the Harper Report recommended guidance be given to the courts on the factors to be considered when making a competition assessment. This recommendation can be found in the *Bill* as a mandatory directive to the court in s 46(2) of the proposed new provision. This directive, which requires the court to consider, for example, the extent to which the conduct has the purpose or effect of increasing competition by enhancing efficiency and innovation, should mitigate concern that it will be interpreted in a narrow way which may risk 'chilling' genuine competitive activity. In particular, it should ensure that competition in this context is viewed in a broad, economic, sense and not narrowly so as to protect competitors from conduct which does not also harm *competition*.

2.3. The current provision is not effective

Some commentators have claimed that section 46 is working effectively because there have been a number of successful cases and that it is therefore not in need of change. Even if this was the case, it would not alter the fact that the 'take advantage' element, as interpreted by the courts, is inappropriate as a distinguisher between pro- and anti-competitive conduct and that the existing purpose element is not appropriately directed toward conduct which is harmful to competition.

It is, however, not the case that the provision is working effectively. Those who choose to point to ACCC successes frequently refrain from observing that the majority of those successes have involved firms admitting to conduct (with the result that litigation costs are minimised and reductions in penalty are typically achieved) and, in many of these consent cases, the relevant conduct was alleged to have contravened multiple provisions.

When consent cases are removed from the story a different picture emerges. In recent times the ACCC has almost always lost contested cases, particularly when they have proceeded to appeal. It has never won a High Court case relating to s 46 (the only High Court cases involving the ACCC were *Boral*[12] and *Rural Press* in 2003). *Baxter Healthcare* (2008)[13] is the only relatively recent contested success and also involved a contravention of the exclusive dealing prohibition. This was preceded by an earlier success in *Safeway* (2003).[14] More recently, the ACCC has experienced losses in *Pfizer*[15] and *Cement Australia.* With very few exceptions private actions have also failed. The most recent private success involved *NT Power*[16] in 2004, which involved unique facts.

This is not to suggest that all the cases that failed should have succeeded, or would have done so under the proposed provision; however, it does suggest some caution should be given to claims that the provision is working successfully in light of a number of ACCC successes.

3. The proposed new provision will not chill competition

Concerns that the provision will 'chill' competition by generating uncertainty and risking 'over-capture' are (at best) exaggerated. The provision itself provides mandatory guidance to the court to ensure that it does not apply an unduly narrow assessment the effect of conduct on the market. In addition, there is nothing in the recent history of competition law litigation in Australia to suggest that the courts have been quick to find anti-competitive conduct merely because competitors have been harmed as a result of competition on the merits.

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12 *Boral Besser Masonry Ltd v ACCC* [2003] HCA 5.
13 *ACCC v Baxter Healthcare Pty Ltd (No 2)* [2008] FCAFC 141.
14 *ACCC v Australian Safeway Stores Pty Ltd* [2003] FCAFC 149.
15 *ACCC v Pfizer* [2015] FCA 113.
16 *NT Power Generation Pty Ltd v Power & Water Authority* [2004] HCA 48.

There will, of course, always be a period of adjustment to new law, but natural levels of uncertainty associated with new law is no justification for retaining bad law. In any event, the concept of substantially lessening competition is not new to Australian competition law jurisprudence.

To some extent the approach adopted must reflect a policy decision about whether to be more concerned about false positives (Type I errors) or false negatives (Type II errors). This is a balance that must be struck in relation to all laws. For criminal laws, where the consequence of false positives can include deprivation of liberty, there is and should be a natural tendency to favour false negatives. For civil laws, such as the misuse of market power provisions, the consequence to the market and, by extension, the Australian public (and consumers in particular) of false negatives can be severe. It is suggested that the scales are currently tipped too heavily in favour of avoiding false positives, with the result that anti-competitive conduct is too frequently allowed to continue unabated. The proposed *Bill* would go some way toward re-balancing the scales toward an equilibrium which neither risks being too permissive of anti-competitive conduct, nor involves a significant risk of prohibiting competitive conduct which incidentally causes harm to one or more individual *competitors* without also harming *competition*.

4. The relevant market

The core prohibition in the *Bill* (s 46(1)) is significantly more convoluted than that proposed in the Harper Report and which featured in the Exposure Draft Bill. This has arisen from attempts to define the market or markets in which the substantial lessening of competition must occur. In particular, it specifies, in substance, that the substantial lessening of competition must occur in the market in which substantial market power is held, or any other market in which it or a related body corporate supplies or acquires goods or services.

This change is not necessary and, despite two pages in the Explanatory Memorandum devoted to the change, no satisfactory explanation for it has been provided. The only explanation that is provided is that some 'stakeholders' expressed concern that the proposed law (which simply referenced a purpose or effect of harming competition in 'any market') may be too broad.

The Explanatory Memorandum correctly notes that, in practice, it is unlikely conduct will have the purpose or effect of harming competition in markets in which the firm with substantial market power (or related entities) does not compete or supply or acquire goods or services. As a result, the capture of the provision remains broad and in line with the substance of the Harper recommendations. However, it is not obvious that the more restrictive definition is needed or that conduct by a company enjoying substantial market power, and which has the purpose or effect of harming competition in any market, should not be prohibited.

It is suggested that it would be preferable to retain the wording which appeared in the Exposure Draft Bill and which was recommended by the Harper Panel.

5. Authorisation

The Harper Report recommended authorisation be made available for misuse of market power. This makes sense. Currently, the conduct prohibited is that which has the purpose of harming competitors; for such a purpose focussed prohibition authorisation seems inappropriate. However, where the prohibition includes conduct which may have the *effect* of harming *competition* then it is appropriate to treat misuse of market power in the same way as other prohibitions against conduct having this effect (such as exclusive dealing). This requires providing for authorisation on public benefit grounds, even if such grounds are likely to arise only very infrequently.

This recommendation was accepted by the Government and appeared in the Exposure Draft Bill. It does not, however, appear in the current *Bill.* It is presumed that this results from the fact that the changes to the authorisation regime in the Exposure Draft Bill are more extensive than merely adding misuse of market power to a list and that all of these changes will be introduced collectively in the next Harper implementation bill. However, it is suggested that, given that the timeline for introduction and passage of the remaining Harper reforms is unknown, some transitional provision should be made for authorisation of misuse of market power which could operate between the passage of the current *Bill* and the second suite of reforms.

6. Other amendments

The *Bill* sensibly implements the Harper Report's recommendations to repeal post-2007 amendments to the provision. These include the *Birdsville Amendment*, which proved an ineffective mechanism for addressing the broader defects in the provision, and interpretative provisions relating to 'take advantage' which will cease to be relevant when that requirement is removed.

7. Recommendation

The Committee should recommend passage of the *Bill*. Consideration should be given to retaining reference to 'any market' as appeared in the Exposure Draft Bill to avoid unnecessary complexity in s 46(1) and to adding a transitional authorisation provision for section 46. However, neither of these considerations should delay the passage of the *Bill;* its passage will implement a long-overdue improvement to a core element of Australia's competition law.

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