

11 February 2016

General Manager
Market and Competition Policy Division
The Treasury
Langton Crescent
PARKES ACT 2600

Email: competition@treasury.gov.au

Dear Scott

Terceiro Legal Consulting Pty Ltd – Submission in response to Discussion Paper entitled “Options to Strengthen the Misuse of Market Power Law”

Terceiro Legal Consulting

Terceiro Legal Consulting (TLC) is a sole practitioner law firm which specialises in competition and consumer law (trade practices law). TLC has been operating since 2008 and has represented numerous companies and businesses in ACCC matters.

TLC's Principal, Michael Terceiro, was previously employed by the Australian Competition and Consumer Commission (ACCC) for 15 years in a number of different roles, including as:

- a Director of Enforcement and Compliance in the New South Wales Regional Office;
- the Director in charge of the Sydney Mergers and Asset Sales Branch;
- the National GST Enforcement Coordinator; and
- the Director (in charge) of the ACCC's Waterfront Team during the Waterfront Dispute.

During Michael's time at the ACCC he ran over 600 investigations, including more than 100 merger clearances, and 30 court cases.

Michael also ran numerous section 46 investigations and one section 46 case – *ACCC v Fila Oceania Pty Ltd and Ors* - <http://www.accc.gov.au/media-release/3-million-penalty-for-filas-selective-distribution-policy-for-afl-licensed-apparel>

Introduction

Section 46 is a very difficult provision to investigate and to prove in Court. The reason the provision has become so difficult to establish is due largely to the High Court's interpretation of the "taking advantage" element in section 46. However, before addressing the problems inherent in the current section 46, it is important to seek to dispel a number of common myths about the provision.

Myths about Section 46

Unfortunately, a number of myths about section 46 have been perpetuated not only by business groups, but also by the ACCC and its Chairmen, both past and present.

For example, in May 2015, ACCC Chairman Mr Rod Sims' gave a speech at the Hodgekiss Competition Law Conference in Sydney entitled "Section 46: The Great Divide".¹ In his speech, Sims sought to explore and illuminate many of the common misconceptions about section 46 of the *Competition and Consumer Act 2010* (CCA).

Sims also argued in favour of the proposed amendments to section 46 put forward by the Harper Committee which, if passed into law, would see the removal of the requirement that the ACCC prove taking advantage, as well as the introduction of both an effects tests and a substantial lessening of competition test.

A Myriad of Myths

A primary focus of Sims' speech were his attempts to dispel the myriad myths surrounding section 46.

The first myth which Sims' sought to address related to what he described as the "insider / outsider divide" as to what section 46 actually prohibits. He described this divide as follows:²

On its face the wording of the section is directed at the impact of the conduct on individual competitors rather than the impact of the conduct on the competitive process in the market.

Yet, I have also heard many times since arriving at the ACCC –well, we know the words say "substantially damage a competitor" but we all know that the law really means "do not damage the competitive process".

So there are these two very different view of s46. There is, on the one hand, an exclusive club, with members of the club knowing that section 46 means 'avoid damage to the competitive process'.

¹ Rod Sims, "Section 46: The Great Divide" at <https://www.accc.gov.au/speech/section-46-the-great-divide>

² Ibid.

On the other hand, those not in the club, the vast majority of the population, aren't privy to this insight.

Sims then goes on to make the following claim:³

Insiders may well feel special, indeed clever, but this divide between common interpretation and true meaning is bad public policy.

Unfortunately, rather than demystifying one of the myths surrounding section 46, Sims has further entrenched a common myth about section 46 – namely, that its true purpose is only to protect the competitive process and not to protect individual competitors.

As every first year law student knows the first step in statutory interpretation is to look at the words of the provision and then to work out what those words mean. You do not look behind the words of the statute unless the meaning of the words is unclear.

Therefore, the first step in understanding section 46 is it to look at the actual words of the provision:

- (1) *A corporation that has a substantial degree of power in a market shall not take advantage of that power in that or any other market for the purpose of:*
- (a) *eliminating or substantially damaging a competitor of the corporation or of 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; or*
 - (c) *detrerring or preventing a person from engaging in competitive conduct in that or any other market.*

When one looks at the actual words of the first prohibition in section 46 - namely section 46(1)(a) – it is abundantly clear that the purpose of this provision is to prevent a corporation with a substantial degree of market power from using that market power for the purpose of:

...eliminating or substantially damaging a competitor of the corporation.

There are no words in section 46(1)(a) to suggest that it is concerned with the competitive process. Rather the plain and ordinary meaning of the provision is that its purpose is to prevent corporations with a substantial degree of market power from using that power to eliminate or damage their competitors.

³ Ibid

There is also no basis for seeking to impute into section 46(1)(a) some additional requirement that the provision only applies where the conduct is likely to have the effect of undermining the competitive process.

However, that is not the end of the story. It is equally apparent that the purpose of the second and third prohibitions in section 46 is to protect the competitive process. Sections 46(1)(b) and (c) show that the legislature also wanted to prevent corporations with a substantial degree of market power from using that market power for the purpose of damaging the competitive process - ie prohibits conduct which prevents new entry to markets and conduct which otherwise deters or prevents competitive conduct.

That section 46 has these dual purposes is also consistent with the broader objectives of the CCA as set out in section 5:

The object of this Act is to enhance the welfare of Australians through the promotion of competition and fair trading and provision for consumer protection.

Section 46 is directed to achieving the goals of both promoting competition (sections 46(1)(b) and (c)), as well as the promotion of fair trading (section 46(1)(a)).

Senator Murphy's Second Reading Speech also appears to provide greater support for the first of the two purposes identified above – namely to protect competitors from the use of market power by their larger competitors:⁴

The clause [46] covers various forms of conduct by a monopolist against his competitors or would-be competitors. A monopolist for this purpose is a person who substantially controls a market. The application of this provision will be a matter for the Court. An arithmetical test such as one third of the market- as in the existing legislation- is unsatisfactory. The certainty which it appears to give is illusory.

Clause 46 as now drafted makes it clear that it does not prevent normal competition by enterprises that are big by, for example, their taking advantage of economies of scale or making full use of such skills as they have; the provision will prohibit an enterprise which is in a position to control a market from taking advantage of its market power to eliminate or injure its competitors.

Unfortunately, both Sims' and other knowledgeable insiders appear to have constructed a false dichotomy in the operation of section 46. It is not an either / or scenario between the protection of competitors and the protection of the competitive process. Rather section 46 was intended to protect (and was drafted to

⁴ The Hon. Senator Murphy, *Second Reading Speech re Trade Practices Bill*, 30 July 1974 at <http://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;query=Id%3A%22hansard80%2Fhansards80%2F1974-07-30%2F0175%22>

protect) both competitors and the competitive process from the illegal conduct of corporations which possess a substantial degree of market power.

Given the apparently faulty “insider” view held by the ACCC as to the scope of section 46, one can only speculate as to whether the ACCC’s understanding may have resulted in it failing to pursue meritorious cases which fell under the terms of section 46(1)(a). It seems probable that the ACCC may have declined to take cases which involved large corporations using their market power to eliminate and damage their smaller competitors simply because there was no demonstrable harm to the competitive process.

It was refreshing to note that your Discussion Paper does not perpetuate this myth. Rather the Discussion Paper clearly recognises that the words of section 46 are, in part, aimed at providing protection to competitors from the misuse of market power by their larger competitors. As stated in the Discussion Paper:

The current provision outlines specific examples of conduct that are prohibited, including “eliminating or substantially damaging a competitor”. However, in practice the courts have interpreted the provision to protect the process of competition, and not individual competitors.

The obvious question arises as to why the Courts have taken it upon themselves to interpret section 46 in a way which appears contrary to both the wording of the provision and, arguably, to Parliament’s intentions as to the proper operation of the provision.

Existing myths

There are also a myriad of existing myths concerning the meaning and operation of the current section 46. Three of the most common myths are that:

1. the ACCC usually loses section 46 cases in court;
2. the ACCC usually loses section 46 cases because it fails to prove purpose; and
3. section 46 cases are hard fought by the respondents.

The attached table shows all of the section 46 cases commenced by the ACCC over the last 43 years:

Table: ACCC and TPC Section 46 cases – 1974 to 2016

	Case	Year	Sections	Result
1.	CSBP Farmers Limited	1980	ss. 45, 46	Lost
2.	Carlton United Breweries Limited	1990	s.46	Won - consent
3.	CSR Limited	1991	ss.45, 46	Won - consent
4.	Commonwealth Bureau of Meteorology	1997	s.46	Won - consent
5.	Darwin Radio Taxi Cooperative Limited	1997	s.46	Won - consent
6.	Garden City Cabs	1997	s.45, 46	Won - consent
7.	Safeway Limited	2003	ss.45, 46	Won - contested
8.	Rural Press Limited	2003	s.45, 46	Lost s.46 case but won s.45 case
9.	Boral Limited	2003	s.46	Lost - High Court
10.	Qantas Limited	2003	s.46	No result – case settled with each party bearing their own costs
11.	Universal Music and Warner Music (CD's case)	2003	s.45, 46, 47	Lost ss.45 and 46 cases but won s.47 case
12.	FILA Pty Ltd	2004	ss.46, 47	Won - uncontested
13.	Eurong Beach Resort	2005	s.45, 46, 47	Won - consent
14.	Cardiothoracic surgeons	2007	ss.45, 46	No result – s.46 claim dropped as part of the settlement
15.	Baxter Limited	2008	ss.46, 47	Won - contested
16.	Cabcharge Limited	2010	ss.46, 47	Won - consent
17.	Ticketek Pty Ltd	2011	s.46	Won – consent
18.	Cement Australia Pty Ltd	2014	ss.45, 46	Lost s.46 case, won s.45 case.
19.	Pfizer	2016	ss.46, 47	Lost – contested
20.	Visa International	2014	ss.46, 47	Won s.47 case, dropped s.46 case

The data from the above table clearly dispels the first common myth about section 46 which is that the ACCC almost always loses such cases. Of the 20 section 46 cases run by the ACCC over the last 43 years it has won eleven times. In other words, the ACCC has won eleven of the 20 cases it has pursued for a success rate of 55%.

However, if one looks at the data from the perspective of the number of section 46 cases which the ACCC has actually lost in court, the myth is entirely “busted”. Of the 20 cases taken by the ACCC, it has won eleven, dropped the section 46 allegations in three cases and lost the remaining six cases. Therefore, the ACCC has only lost 6 cases out of the 20 section 46 cases it has commenced, which represents a failure rate of only 30%.

The above table also debunks the myth that the ACCC generally loses section 46 cases because it fails to establish purpose. Prior to the Pfizer case in 2015, the ACCC had never lost a section 46 because it failed to establish purpose. Rather the ACCC most often loses section 46 cases because it fails to prove the taking advantage element.

Finally, there is no evidence to support the view that section 46 cases are generally “hard fought” by respondents. Eight of the eleven successful section 46 cases taken

by the ACCC were not contested, as the respondents in these cases either consented to a finding that they had breached section 46 or did not contest that finding. In other words, 72% of the section 46 cases won by the ACCC were not contested by the respondents.

Investigating a section 46 allegation

As stated above, during my time as an ACCC Director of Enforcement and Compliance I ran a number of section 46 investigations. Therefore, based on this experience, I believe I am able to make the following general observations about the way in which section 46 investigations have generally been conducted in the past:

1. the first step we undertook when we received a section 46 allegation was to determine whether the corporation being complained about possessed a substantial degree of market power. This involved defining a relevant market and then determining whether the corporation possessed a substantial degree of market power in that market by reference to the section 50 factors ie barriers to entry, import competition and so on;
2. once we were satisfied that the corporation being complained about possessed a substantial degree of market power, we would then focus on whether we could satisfy the taking advantage test, as defined by the High Court. Unfortunately, this stage of the investigatory process often generated considerable internal debate and disagreement. We often spent interminable periods of time debating whether the test set down by the High Court required consideration of whether a company without market power “could” engage in the alleged conduct (ie was capable of engaging in such conduct) as opposed to whether they “would” engage in the alleged conduct (ie whether it would be economically rational for a corporation without market power to engage in the alleged conduct);
3. once we believed we could satisfy both the substantial market power and taking advantage elements of section 46, we would spend lengthy periods of time searching through vast amounts of internal company documents (obtained from the corporation under investigation through the use of numerous section 155 Notices) for some evidence of their purpose in engaging in the alleged conduct. In other words, we spent a great deal of time searching for the “smoking gun” document which would prove that the corporation had the purpose of misusing their market power for a proscribed purpose; and
4. the final relevant observation relates to the importance of effect when deciding whether to pursue a section 46 allegation further, say to an in-depth investigation or litigation. Even though the test in the current section 46 is a purpose test, that is not to say that the ACCC did not consider the likely effect of the alleged conduct when investigating section 46 allegations. Rather ACCC officers would always be focused on whether the alleged conduct would in fact have the effect of harming the competitive process. The reason for this approach is simple. The ACCC could not justify committing its scarce resources

to cases where corporations with a substantial degree of market power which admittedly had the purpose of damaging the competitive process also had no realistic prospect of actually achieving their desired goal of harming the competitive process.

Harper Recommendation

The Harper Committee Section 46 Recommendation has simultaneously raised the hopes of small business groups and the ire of big business groups. Many small businesses have high expectations of the proposed section 46, whilst big businesses claim that the new provision will have dire impacts on competitiveness and innovation.

The Harper Committee's proposed new section 46 is as follows:⁵

(1) A corporation that has a substantial degree of power in a market shall not engage in conduct if the conduct has the purpose, or would have or be likely to have the effect, of substantially lessening competition in that or any other market.

Harper's proposed amendment makes three main changes to section 46:

- remove the take advantage test;
- add an effects test; and
- add a substantial lessening of competition test.

The proposal to remove the taking advantage test is a crucial change.

The taking advantage test is the element of the existing section 46 which is most often misapplied by the Courts. As stated by Sims, the take advantage element:⁶

...is meant to provide the filter for distinguishing pro-competitive from anti-competitive conduct.

Sims' claim is only half correct. While it is true that the taking advantage test has been applied by the courts as a filter for distinguishing pro-competitive from anti-competitive conduct, it is not correct to suggest that Parliament ever intended the taking advantage element to act as a filter. Rather, as argued above, Parliament's intention was for section 46(1)(a) to be used to protect businesses from other businesses which possessed a substantial degree of market power, while sections 46(1)(b) and (c) were directed to protecting the competitive process.

The Courts have interpreted taking advantage as requiring a consideration of whether the corporation would be able to engage in the particular conduct under examination if they did not have market power. As stated in the Discussion Paper:

⁵ Harper Committee, *Final Report – March 2015* at http://competitionpolicyreview.gov.au/files/2015/03/Competition-policy-review-report_online.pdf

⁶ Sims, above n1.

The ‘take advantage’ test allows firms with substantial market power to engage in particular business conduct if firms without market power can also commercially engage in that conduct.

In effect, the Court has applied a counterfactual analysis. If the answer to the posited question is “yes”, then the courts have concluded that section 46 was not contravened because the taking advantage limb had not been established.

The Court’s interpretation of the taking advantage test is an inappropriate gloss on the meaning of taking advantage. Unfortunately, this interpretation has had the effect of rendering section 46 largely ineffectual, as demonstrated by the fact that the ACCC has only taken 20 such cases in 43 years.

The impact of the High Court’s interpretation of the taking advantage element in section 46 has been aptly described by Justice Kirby in his dissenting judgment in *Rural Press*, where he stated:⁷

In my view, the approach taken by the majority is insufficiently attentive to the object of the Act to protect and uphold market competition. It is unduly protective of the depredations of the corporations concerned. It is unrealistic, bordering on ethereal, when the corporate conduct is viewed in its commercial and practical setting. The outcome cripples the effectiveness of s 46 of the Act. It undermines this Court’s earlier and more realistic decision in Queensland Wire. The victims are Australian consumers and the competitors who seek to engage in competitive conduct in a naive faith in the protection of the Act. Section 46 might just as well not have been enacted for cases like these where its operation is sorely needed to achieve the purposes of the Act. Judicial lightning strikes thrice. A novel doctrine of innocent coincidence prevails. Effective anti-competitive threats can be made without the redress which s 46 appears to promise. Once again I dissent.

Historically, the ACCC’s position on “taking advantage” was that the term meant no more than “use”.⁸ In other words, the taking advantage element does no more than import a causal requirement between the substantial degree of market power of the corporation and their relevant conduct.

The second reason why it is appropriate to remove the taking advantage element from section 46 is because it is an aberration in the context of the approach taken in almost every other jurisdiction when dealing with the problem of monopolisation. As stated by Sims:⁹

⁷ *Rural Press v ACCC* (2003) 216 CLR 53, para. 139.

⁸ ACCC, “High Court Confirms and enhances current approach to ‘misuse of market power’” *ACCC Media Release*, dated 16 March 2001 – at <https://www.accc.gov.au/media-release/high-court-confirms-and-enhances-current-approach-to-misuse-of-market-power>

⁹ Sims, above n1.

Most jurisdictions do not require proof of the nexus between market power and the conduct itself (the taking advantage).

Sims specifically refers to section 2 of the US Sherman Act and Article 102 of the Treaty in the Functioning of the European Union, neither of which contain a taking advantage element.

Emerging myths

Unfortunately, one can also discern a number of newly emerging myths about the Harper Committee's proposed section 46. The main originators of these myths appear to be large business groups, particularly the Business Council of Australia.

The first of these emerging myths relates to the alleged anti-competitive impacts of the proposed effects test. Sims identifies the supermarket sector as the primary source of this emerging myth:¹⁰

The supermarket sector in particular has dominated the section 46 debate and, amazingly, the two major supermarkets have argued that, were the proposed changes implemented, they risk breaching the law if they were to open a supermarket in a market where they do not currently operate.

The large supermarket chains are claiming that the mere act of opening a new store in a market is likely to breach the new section 46 because such conduct will have the likely effect of damaging competition.

This claim would have some credibility but for the fact that the Harper Committee has also proposed the introduction of a substantially lessening competition test, which limits the application of the effects test. As explained by Sims:¹¹

I find it curious that the main opponents of the Harper s46 change are suggesting that larger companies would be stopped from opening a new store in a new market. How can such a move be said to substantially lessen competition?

Under the proposed section 46, the Court will have to be satisfied about two requirements before a corporation can be found to have breached the provision. First, the corporation will have to be shown to have a substantial degree of market power in a market. Second the corporation will have to have engaged in conduct for the purpose or with the effect or likely effect of substantially lessening competition.

It is clear that the opening of a new store in a market will not have the effect of substantially lessening competition - rather such conduct will have the opposite effect – namely, of substantially increasing competition in the market.

¹⁰ Ibid.

¹¹ Ibid.

Other emerging myths being perpetuated by opponents of the proposed change are:¹²

- because businesses cannot know the effects of their actions on markets, they cannot be held liable for the unintended consequences of their actions;
- that the introduction of an effects test will introduce major uncertainty; and
- the new provision will result in over capture ie false negatives.

It is quite surprising that business groups are arguing that they should not be liable under the proposed section 46 effects test because they cannot know the likely consequences of their actions on markets. Businesses are effectively claiming that their knowledge and understanding of the markets in which they operate is so deficient that they cannot predict with any certainty the consequences of their actions. If this were truly the case, it is difficult to see how these businesses would be capable of making even rudimentary pricing and output decisions.

In reality businesses are the entities in our economies which possess the best knowledge and understanding of the markets in which they operate. Businesses also have the best knowledge and understanding of how their business decisions will impact on both the market and the participants within those markets.

One should also note that corporations are already liable for the effects of their conduct under section 45, 47 and 50 of the CCA. Despite this fact, businesses have not been calling for the repeal of these other provisions or at the very least the removal of the effects tests from these sections.

The claim that the new provisions will introduce major uncertainty is misplaced. Rather, the new provision is likely to reduce uncertainty because it will remove the major source of uncertainty in relation to section 46, namely the taking advantage element.

The new provision will no doubt capture more conduct than its predecessor, but there is no reason for believing that the provision will result in over capture. Rather, the new provision will reverse the under-capture which has characterised the enforcement of the existing section 46 over the last 43 years.

It is unfortunate that a number of the emerging myths being propounded by business groups appear to have gained some traction at the political level. That these concerns are myths is beyond serious debate. The more puzzling question is why a major political party, which should be able to understand the legal and

¹² Business Council of Australia, Submission to the Department of Treasury on the Final Report of the Competition Policy Review", May 2015 2014 – at [file:///C:/Documents%20and%20Settings/Michael/My%20Documents/Downloads/BCA_Submission_o_n_the_Final_Report_of_the_Competition_Policy_Review_FINAL%20\(1\).pdf](file:///C:/Documents%20and%20Settings/Michael/My%20Documents/Downloads/BCA_Submission_o_n_the_Final_Report_of_the_Competition_Policy_Review_FINAL%20(1).pdf)

economic logic underpinning Harper's recommendation, appear to be supporting the status quo on the basis of these demonstrably false myths.

Conclusions

Sims' speech "Section 46: The great divide" is a valuable contribution to the perennial debate about the scope and utility of section 46. While Sims comprehensively "busts" a number of the emerging myths concerning Harper's proposed section 46, unfortunately he also perpetuates an existing and longstanding myth about the provision.

While we may agree as a matter of policy that section 46 **should** be directed exclusively to protecting the competitive process, that is not to say that it is currently drafted to achieve that outcome alone.

Furthermore, there is no evidence to suggest that section 46 was ever intended by Parliament (or The Hon Lionel Murphy for that matter) to achieve the narrow goal of protecting the competitive process, to the exclusion of an equally important goal – namely to protect small businesses from bigger businesses which are abusing their substantial degree of market power

Harper's proposed section 46 should be embraced by everybody:

- Who values competition in markets
- Who accepts that there is a clear need for governments to curb the conduct of corporations which possess a substantial degree of market power
- Who recognises that the existing section 46 is all but unworkable and has resulted in significant under-capture over the last 43 years and
- Who recognises that corporations in Australia with a substantial degree of market power should be held liable for the effects of their unilateral conduct, as they are in almost every other leading other anti-trust and competition law regime around the world.

Now that the myths about section 46, both existing and emerging, have been "busted", there can be no legitimate basis for standing in the way of this essential and long overdue change to Australian competition laws.

It is also time to end the great Australia/international divide between our unique and largely ineffective monopolisation prohibition and the economically sound and largely effective monopolisation provisions which exist in almost every other anti-trust and competition law regime.

If you have any questions about this submission, please contact me (02) 8086 2005.

Yours sincerely

A handwritten signature in black ink that reads "M Terceiro". The signature is written in a cursive style with a large, stylized initial "M".

Michael Terceiro
Competition and Consumer Lawyer
Terceiro Legal Consulting